Alliant™ Corporation

ALLIANT™

What can we do for you?

Analyst inquiries

Inquiries from the financial community may be directed to: Robert Rusch, Investor Relations, P.O. Box 192, Madison, Wisconsin 53701-0192, Telephone: 608.252.3470.

Duplicate mailings

Annual Reports are mailed to all shareowners. You will receive duplicate mailings if your shares are registered in different names, but using the same address. To eliminate duplicate annual reports, call or send your request to Shareowner Services.

If you receive duplicate mailings of proxies and dividend checks because of slight differences in the registration of your accounts, please call Shareowner Services for instructions on combining your accounts.

Shareowner Direct Plan

The Plan is available to all shareowners of record, first-time investors, customers, vendors and employees. The Plan enables shareowners to buy common stock directly through the company without paying any brokerage commissions, fees or service charges. You may obtain a copy of the Plan Prospectus by contacting Shareowner Services.

Highlights of the plan include:

- Optional cash investments by check or electronic transfer
- Dividends can be reinvested or received in cash
- Stock certificate safekeeping
- Sale of shares
- Electronic deposit of dividends

Direct Deposit

Shareowners who are not reinvesting their dividends through the Plan may choose to have their quarterly dividend checks electronically deposited in their checking or savings accounts through this service.

Shareowner Information

The company keeps its shareowners informed regularly through the *Annual Report*, the *Quarterly Report* and other communications. We encourage shareowners with questions or concerns to contact Shareowner Services.

Stock transfer agent and registrar

For Alliant Corporation (Interstate Energy Corporation) common stock and all preferred stock of Wisconsin Power and Light Company, IES Utilities Inc. and Interstate Power Company, contact:

Alliant Corporation (Interstate Energy Corporation)
Attn: Shareowner Services
P.O. Box 2568
Madison, Wisconsin 53701-2568

Shareowner Services

The company's Shareowner Services representatives are available to assist you from 8:30 a.m. to 4:30 p.m. (Central Standard Time) each business day.

Madison, Wisconsin Area	**608.252.3110**
Toll-free	**800.356.5343**

Please direct written inquiries to Shareowner Services at the address above.

Internet Address: **www.alliant-energy.com**

1998 record and dividend payment dates

Anticipated record and dividend payment dates are as follows:

Common Stock

Record Dates	Payment Dates
Jan. 26	Feb. 14
Apr. 30	May 15
July 31	Aug. 15
Oct. 30	Nov. 14

Shareowner information

Interstate Energy Corporation (doing business as Alliant Corporation) has an estimated 87,000 shareowners, following completion of the merger. Shareowner records are maintained in the corporate general office in Madison, Wisconsin. (As of December 31, 1997, there were 35,789, 15,886 and 35,677 shareowners of IES Industries Inc., Interstate Power Company and WPL Holdings, Inc., respectively.)

Market information

Exchange Listings

	Stock Exchange	Stock Exchange	Newspaper Abbreviation
Alliant Corporation (Interstate Energy Corporation) Commen	New York Stock Exchange	LNT	IntstEngy
Wisconsin Power & Light Co. 4.50% Preferred	American Stock Exchange	Wis Pr	WI P&L pf

All other Wisconsin Power and Light Company preferred series and all preferred issues from IES Utilities Inc. and Interstate Power Company are traded on the over-the-counter market.

Common Stock quarterly price ranges and dividends (WPL Holdings, Inc. only)

	1997			1996		
Quarter	**High**	**Low**	**Dividend**	**High**	**Low**	**Dividend**
First	$28 7/8	$27 3/8	$0.50	$32	$29 7/8	$0.4925
Second	28 1/4	26 3/4	0.50	32 7/8	28 5/8	0.4925
Third	29	27	0.50	32 7/8	28 7/8	0.4925
Fourth	34 7/16	28 3/8	0.50	29 5/8	27 1/2	0.4925
Year	**$34 7/16**	**$26 3/4**	**$2.00**	**$32 7/8**	**$27 1/2**	**$1.97**

WPL Holdings, Inc. year-end 1997 common stock price: $33 1/8

Street-name accounts

Shareowners whose stock is held by banks or brokerage firms and who wish to receive quarterly reports directly from the company should contact Shareowner Services to be placed on the mailing list.

Form 10-K information

Upon request, the company will provide, without charge, copies of the Annual Report on Form 10-K for the year ended December 31,1997, as filed with the Securities and Exchange Commission. Requests should be directed to Shareowner Services. *All reports filed with the SEC are also available on the internet at www.alliant-energy.com.*

To our fellow shareowners:

March 30, 1998

Welcome to the world of Alliant™. Built on the rich traditions and proud heritage of three companies – IES Industries Inc., Interstate Power Company and WPL Holdings, Inc. – Alliant is the name of a new company with a new face, heart and soul. (Although we are doing business as Alliant Corporation, the legal name of the corporation remains Interstate Energy Corporation. The proxy materials for the 1998 annual meeting include a proposal asking you to approve a change in the legal name of the corporation from Interstate Energy Corporation to Alliant Corporation.)

When we officially completed our three-way merger in early 1998, it, in one sense, marked the end of a journey spanning 27 months and 11 approvals. In truth, however, we have only just begun.

Unlike many of our competitors who have resisted the inevitability of a competitive energy-services marketplace, Alliant has aggressively built itself for the day when customers will decide for themselves which provider offers the greatest value. By completing this historic three-way merger, we are far better positioned to offer our customers around the world an array of comfort, security and productivity solutions that can enhance their lives.

Only by wooing, wowing and winning over our customers each and every day can Alliant deliver for you, our shareowners, a return on your investment that stacks up favorably against the competition. Clearly, our merger will contribute to the bottom line by allowing us to operate more cost-effectively. Over the long term, however, Alliant cannot cost-cut its way to success in a competitive marketplace; it must grow and do so profitably. Under the banner of Alliant, our growth prospects clearly exceed those of our three predecessor companies.

As you will see in the new Alliant corporate brochure, which is included in this *Annual Report*, we are not focused solely on energy anymore. This is because our customers – whether here in the heartland or halfway around the world – don't really want just electricity or natural gas. They want the comfort and security in their home and the productivity of their business provided by our energy services.

On behalf of more than 6,000 employees who are working every day to enhance the value of your investment, thank you very much for your confidence and support. We look forward to rewarding the trust you have placed in us.

Sincerely,

Lee Liu
Chairman of the Board

Wayne H. Stoppelmoor
Vice Chairman of the Board

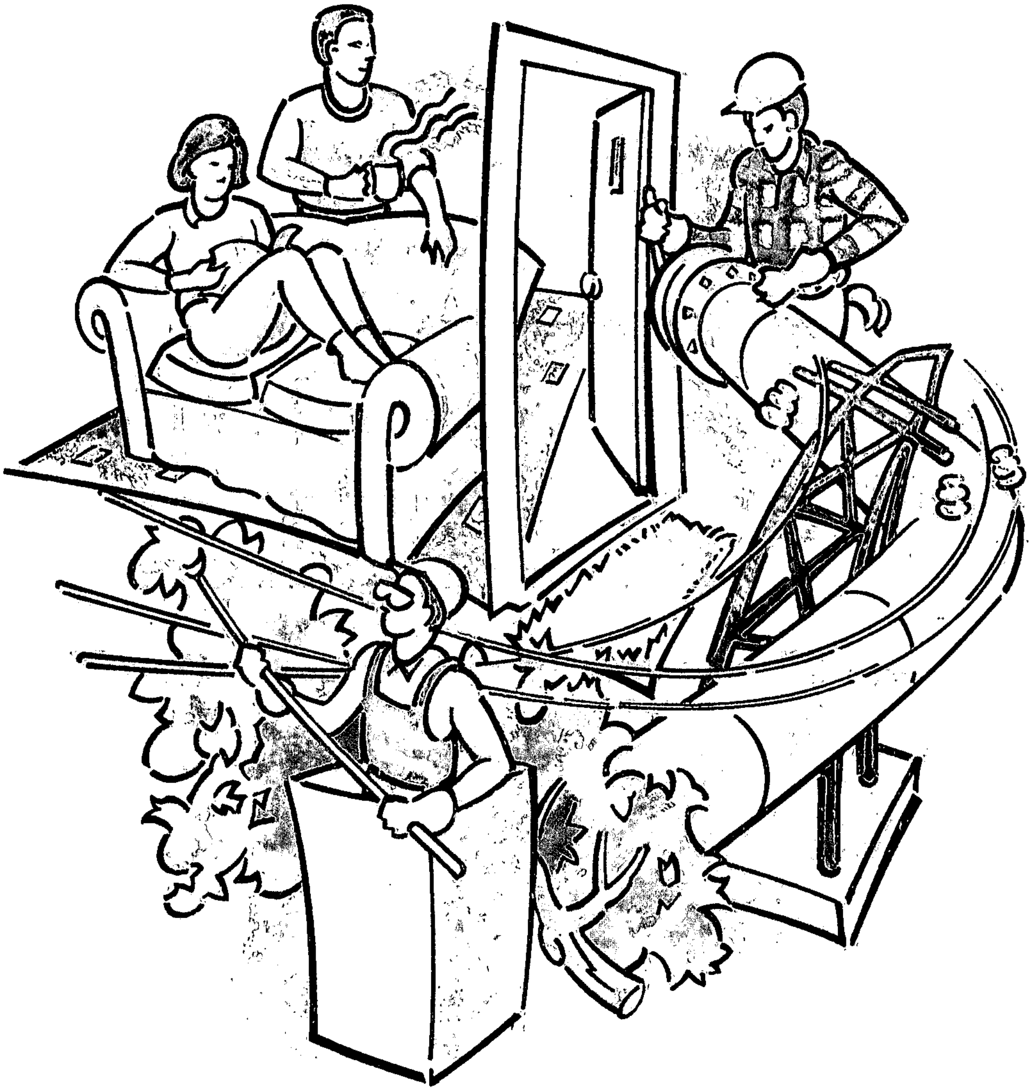
Erroll B. Davis Jr.
President and Chief Executive Officer

Lee Liu

Wayne H. Stoppelmoor

Erroll B. Davis Jr.

Welcome to the world of Alliant™

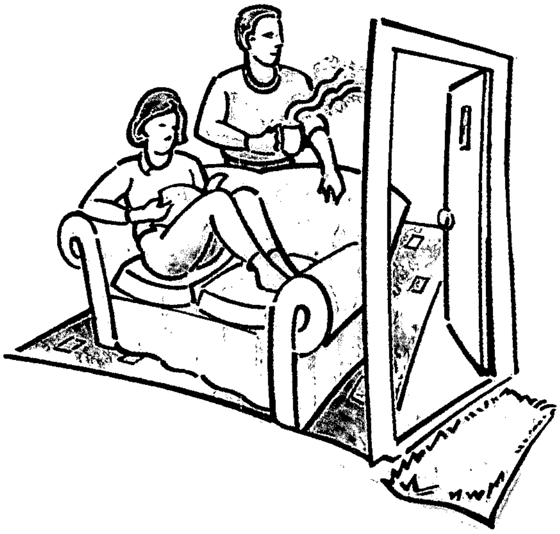


ALLIANT™

What can we do for you?

ALLIANT™

What can we do for you?



More than you might think. Alliant™ offers customers an ever-expanding array of products and services designed to enhance the comfort and security of their homes and the productivity of their businesses.

More than one million residential and business customers throughout Iowa, Wisconsin, Minnesota and Illinois count on us for:

- Reliable, competitively priced electric and natural-gas energy that allows for easier living at home and a more productive environment at work.

And business customers, both within and outside of our utility service territory, turn to us for total energy solutions such as:

- Comprehensive business-process improvements designed to drive down production costs while driving up product quality; and
- Backup energy supplies to ensure uninterrupted production for their businesses or their manufacturing plants.

Key Facts About Alliant:

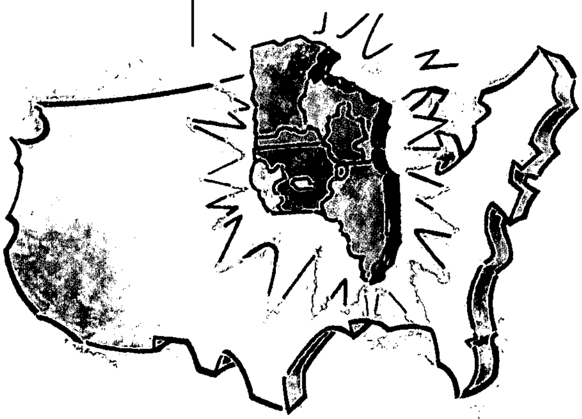
- Electric customers: 897,000
- Natural-gas customers: 382,000
- Water customers: 32,000
- Total assets (year-end 1997): $5.0 billion
- Operating revenues (1997): $2.3 billion
- Employees: Approximately 6,000

We're Alliant, a new company born from the proud traditions of three outstanding energy-services providers – IES Industries Inc., Interstate Power Company and WPL Holdings, Inc.

For more than a century, we've kept homes warm, lights burning and factories running in more than 1,000 communities across Iowa, Wisconsin, Minnesota and Illinois.

We know that customers want reliable service, personal attention and an energy partner that will anticipate their needs. With strong Midwestern values and a reputation for service excellence, we have promised our customers that they can rely on us – and we've kept that promise.

Now, under the banner of Alliant, we will work to create partnerships and solutions that increase the comfort, security and productivity of customers around the world.

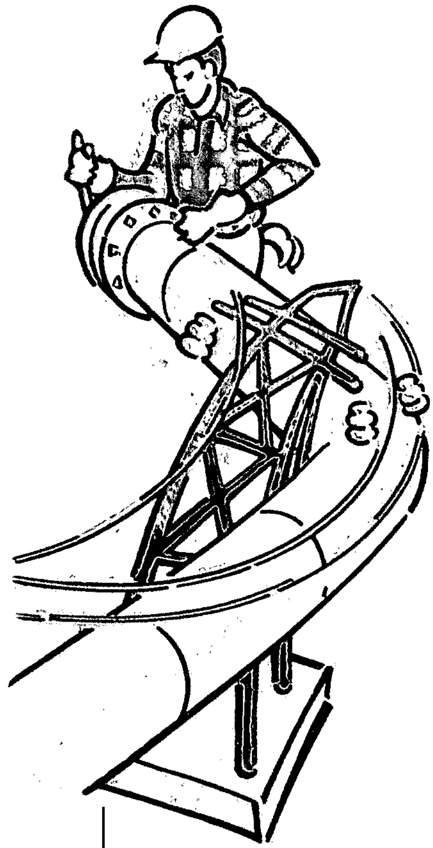


The Alliant Family: Focused on customers in a world of choice

The Alliant family of companies is poised to compete in the rapidly changing energy-services marketplace. Backed by $5 billion in assets, an energized workforce, a commitment to the future, and a promise to solve customer problems, Alliant is positioned to meet the ever-changing needs of customers here in America's heartland and around the world.

In a world where all customers soon will have a choice of energy suppliers, we are finding better, more responsive ways to deliver services traditionally provided by electric and natural-gas utilities. And, we are finding new ways to meet customer needs by developing an array of products and services that no other provider can match.

To become the partner of choice for a variety of energy-services customers with vastly different needs, Alliant is organized into strategic business units – Alliant Utilities, Alliant Power and Alliant Industries. Internal support comes from a separate centralized Alliant Corporate Services unit. Together, these four business units help us keep our promise to all customers today, tomorrow and well into the future.



Alliant
Worldwide Headquarters: Madison, Wisconsin

A parent-company staff provides overall strategic guidance and also ensures proper coordination among Alliant's business units.

ALLIANT™

Alliant Corporate Services
Headquarters: Dubuque, Iowa

Alliant Corporate Services provides value-added services to our *internal* customers to help us better meet the needs of our *external* customers.

ALLIANT™
CORPORATE
SERVICES

ALLIANT™

ALLIANT™ UTILITIES | ALLIANT™ POWER | ALLIANT™ INDUSTRIES | ALLIANT™ CORPORATE SERVICES

Alliant Utilities
Headquarters: Cedar Rapids, Iowa

The tradition of operational excellence is being carried on at Alliant under three familiar names: IES Utilities, Interstate Power Company, and Wisconsin Power and Light. Under one banner, these three utility companies help our customers live more comfortably and work more productively by offering them a reliable, competitively priced supply of electricity, natural gas, water or steam. More than one million customers count on Alliant not only for their energy supply, but also for responsive, round-the-clock service.

ALLIANT™ UTILITIES

Alliant Power
Headquarters: Madison, Wisconsin

Alliant Power manufactures and markets electric energy from 18 generating facilities with a total output of nearly 5,000 megawatts – enough to light 1.5 million homes. One of the lowest-cost electricity manufacturers in the nation, Alliant Power provides affordable and reliable electric energy to customers within Alliant's service territory. As the electric-utility industry opens up to competition, Alliant Power is well-positioned to serve customers throughout the nation who have a choice of supplier.

ALLIANT™ POWER

Alliant Industries
Headquarters: Cedar Rapids, Iowa

Alliant Industries is the umbrella under which we: (1) market competitively priced energy and other products and services to industrial, commercial and residential customers; and (2) pursue energy-related partnerships in attractive marketplaces around the globe.

Alliant Industries will serve customers through the following subsidiaries:

- **Alliant Industrial Services** offers large energy users an array of services to maximize productivity and energy efficiency. Also available are solutions for waste remediation and other environmental needs.
- **Alliant At Home** markets new products and services to enhance the security and comfort of residential and small-commercial customers.
- **Alliant Internatienal** seeks opportunities to increase the efficiency of energy operations in markets throughout the world. Current operations are in China and New Zealand.
- **Cargill/Alliant** is a joint venture combining the world-class commodity and risk-management experience of Cargill with Alliant's energy-trading expertise. Cargill/Alliant buys, sells and trades electricity for those customers who already have access to the increasingly robust electric-power marketplace.

ALLIANT™
INDUSTRIES

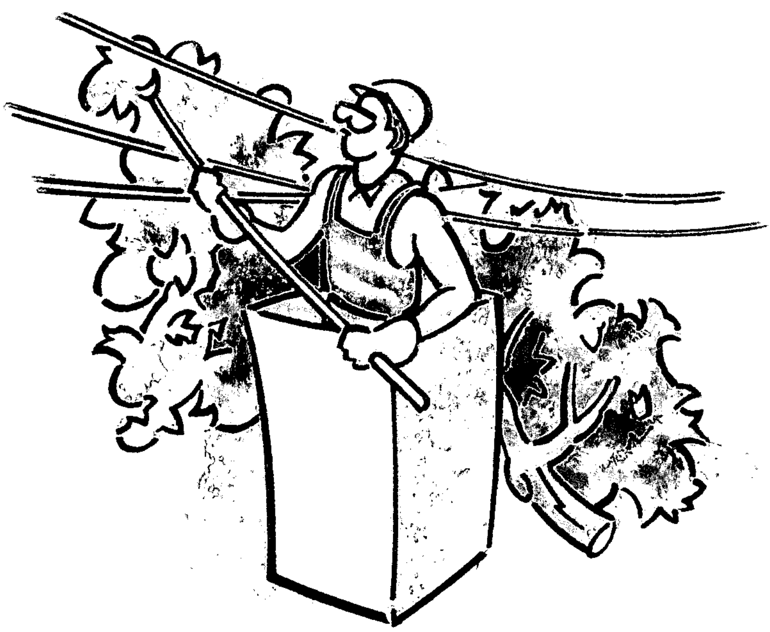
Our new name, Alliant, conveys a commitment to our customers. We are an **ally** for our customers, communities, investors and employees. We are **reliable**. And we will be **all** we can be for those who work with us and for us.

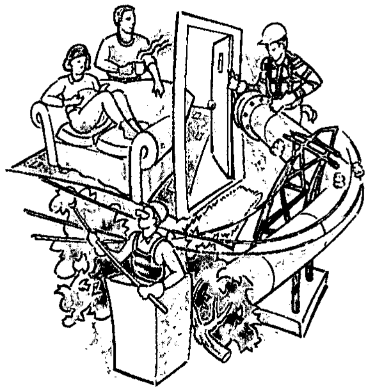
Promising Solutions to people around the world

Only by striving to upbold our values can we deliver all that wo promiso:

Alliant will . . .

- Become a partner with our customers, anticipating their needs and seeking creative solutions to their home and business problems.
- Strive for excellence in service, responsiveness and operational performance.
- Protect the safety of our employees and the public at large.
- Communicate openly and honestly, and uphold the highest standards of ethical behavior throughout the organization.
- Increase the value of investments made in the company by our shareowners.
- Be a responsible corporate citizen, caring for the environment and the communities where we do business, and encouraging diversity in our employee and supplier ranks.





We are your partners, bringing a range of resources and technical skills to help you be more productive and profitable.

Interstate Energy Corporation, doing business as Alliant Corporation, is a major energy-services provider with growing national and international diversified operations. Headquartered in Madison, Wisconsin, Alliant and its subsidiaries provide electric, natural gas, water or steam energy to more than one million customers in four Midwestern states. Alliant also has diversified interests throughout the United States and in China and New Zealand.

Alliant

- **Worldwide Headquarters**
  222 West Washington Avenue
  P.O. Box 192
  Madison, Wisconsin 53701-0192 U.S.A.

  Corporate Office: 608.252.3311
  Internet: www.alliant-energy.com

Alliant Business Unit Operating Headquarters

- **Alliant Utilities**
  200 First Street SE
  Cedar Rapids, Iowa 52401
- **Alliant Power**
  222 West Washington Avenue
  P.O. Box 192
  Madison, Wisconsin 53701-0192
- **Alliant Industries**
  200 First Street SE
  Cedar Rapids, Iowa 52401
- **Alliant Corporate Services**
  1000 Main Street
  Dubuque, Iowa 52001

ALLIANT™

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ALLIANT™

Alliant
Worldwide Headquarters
222 West Washington Avenue
P.O. Box 192
Madison, WI 53701-0192

www.alliant-energy.com

News Release

INTERSTATE ENERGY CORPORATION BOARD OF DIRECTORS ELECTS OFFICERS

MADISON, Wis. — April 21, 1998 — The Board of Directors of Interstate Energy Corporation (NYSE: LNT) announced the election of officers. The company — which is doing business as Alliant Corporation — will be led by Lee Liu, who was elected chairman of the board; Wayne H. Stoppelmoor, who was elected vice chairman of the board; and Erroll B. Davis Jr., who was elected president and chief executive officer.

Liu, 65, was formerly chairman of the board and chief executive officer of IES Industries Inc. and its utility subsidiary, IES Utilities Inc. He has held various management positions with IES and one of its predecessor companies, Iowa Electric Light and Power Co., since joining the company in 1957. He was first elected to the board of directors in 1981. Liu is a graduate of Iowa State University.

Stoppelmoor, 64, was formerly chairman of the board of Interstate Power Co. He retired as president and chief executive officer of the company in 1997. He joined IPC in 1960 and was elected president and chief executive officer in 1987. He was first elected to the board of directors in 1986. Stoppelmoor is a graduate of the University of Iowa.

Davis, 53, was formerly president and chief executive officer of WPL Holdings, Inc. and its principal subsidiary, Wisconsin Power and Light Co. He joined WP&L in 1978 and was first elected to the WP&L board of directors in 1982. Davis is a graduate of Carnegie-Mellon University and has a M.B.A. degree from the University of Chicago.

The list of the corporate board of directors in the company's 1997 annual report inaccurately indicates that Liu had retired as president and chief executive officer of IES Industries Inc.

Interstate Energy Corporation, doing business as Alliant, is headquartered in Madison, Wis. Formed as a result of the merger of IES Industries Inc., Interstate Power Co. and WPL Holdings, Inc., Alliant is a major energy-services corporation with growing national and international diversified operations. Through its regulated utility businesses, Alliant provides electric, natural-gas, water and steam energy to more than one million customers in four Midwestern states. Alliant also has diversified interests throughout the United States and in China and New Zealand.

Jack R. Newman, 64 [1994] □ ◆*
Partner
Morgan, Lewis & Bockius
Washington, D.C.

Milton E. Neshek, 67 [1984] ● ▲
General Counsel and Secretary
Kikkoman Foods, Inc.
Walworth, Wisconsin

Judith D. Pyle, 54 [1992] □ ◆
Vice Chair
The Pyle Group
Madison, Wisconsin

Robert D. Ray, 69 [1987] ◆ ▼
Retired President and Chief Executive Officer
IASD Health Services Inc.
Des Moines, Iowa

David Q. Reed, 66 [1967] ●
Independent Practitioner of Law
Kansas City, Missouri

Robert W. Schlutz, 62 [1989] ● ▲
President
Schlutz Enterprises
Columbus Junction, Iowa

Anthony R. Weiler, 61 [1979] □ ◆
Senior Vice President, Merchandising
Heilig-Meyers Co.
Richmond, Virginia

Key to committee membership

● = Audit Committee
□ = Compensation and Personnel Committee
▲ = Environmental/Safety Committee
◆ = Nominating & Governance Committee
▼ = Executive Committee
* = Committee Chair
† = Committee Vice Chair

Ages are as of December 31, 1997. Bracketed information represents first year of board affiliation with a company that ultimately became part of the Alliant family.

Edward M. Gleason, 57 [1977]
Vice President, Treasurer and Corporate Secretary
Dale R. Sharp, 57 [1964]
Vice President-Engineering and Standards
Donald D. Jannette, 55 [1966]
Assistant Corporate Secretary
Steven F. Price, 45 [1984]
Assistant Treasurer
Kent M. Ragsdale, 48 [1985]
Assistant Secretary
Robert A. Rusch, 35 [1989]
Assistant Treasurer

WISCONSIN PDWER AND LIGHT COMPANY CORPORATE OFFICERS

Errcll B. Davis Jr., 53 [1978]
Chief Executive Officer
William D. Harvey, 48 [1986]
President
Daniel A. Doyle, 39 [1992]
Vice President-Fossil Plants
John E. Ehright, 54 [1996]
Vice President-Controller
Dean E. Ekstrom, 50 [1985]
Vice President-Sales and Service
John F. Franz Jr., 58 [1992]
Vice President-Nuclear Operations
Edward M. Gleason, 57 [1977]
Vice President, Treasurer and Corporate Secretary
Daniel L. Mineck, 49 [1970]
Vice President-Performance Engineering and Environmental
Kim K. Zuhlke, 44 [1978]
Vice President-Customer Operations
David L. Wilson, 51 [1966]
Assistant Vice President-Nuclear Operations

Donald D. Jannette, 55 [1966]
Assistant Corporate Secretary
Steven F. Price, 45 [1984]
Assistant Treasurer
Robert A. Rusch, 35 [1989]
Assistant Treasurer

ALLIANT INDUSTRIES CORPORATE OFFICERS

Erroll B. Davis Jr., 53 [1978]
Chief Executive Officer
James E. Hoffman, 44 [1995]
President
Thomas L. Aller, 48 [1993]
Vice President-Investments
John E. Ebright, 54 [1996]
Vice President-Controller
Edward M. Gleason, 57 [1977]
Vice President, Treasurer and Corporate Secretary
Claire K. Fnlenwider, 55 [1993]
Vice President-Business Development
Cynthia P. Kellogg, 43 [1992]
Vice President-Finance
Donald D. Jannette, 55 [1966]
Assistant Corporate Secretary
Steven F. Price, 45 [1984]
Assistant Treasurer
Robert A. Rusch, 35 [1989]
Assistant Treasurer
Daniel Siegfriod, 38 [1992]
Assistant Secretary

Ages are as of December 31, 1997. Dates in brackets represent the year each person joined a company that ultimately became part of the Alliant family.

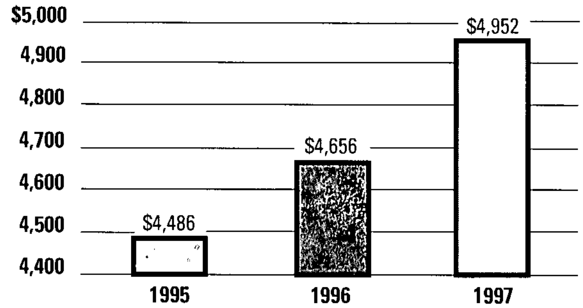
Financial highlights

	1997 PRO FORMA	1996 PRO FORMA	PERCENT CHANGE
	(Dollars are in millions except for per-share data)		
Operating Results:			
Operating revenues	$2,301	$2,233	3%
Operating income	$350	$370	(5%)
Income from continuing operations	$154	$160	(4%)
Net income	$154	$159	(3%)
Return on average common equity	9.98%	11.14%	(10%)
Utility electric sales from ultimate customers (thousands of MWH)	24,015	23,212	3%
Total utility electric sales (thousands of MWH)	30,944	30,832	—
Utility gas sold and transported (thousands of dekatherms)	117,972	121,874	(3%)
Construction and acquisition expenditures	$330	$414	(20%)
Total assets at year-end	$4,952	$4,656	6%
Per Share Data:			
Earnings per average common share from continuing operations (basic and diluted)	$2.02	$2.12	(5%)
Earnings per average common share (basic and diluted)	$2.02	$2.10	(4%)
Boek value at year-end	$21.52	$19.06	13%

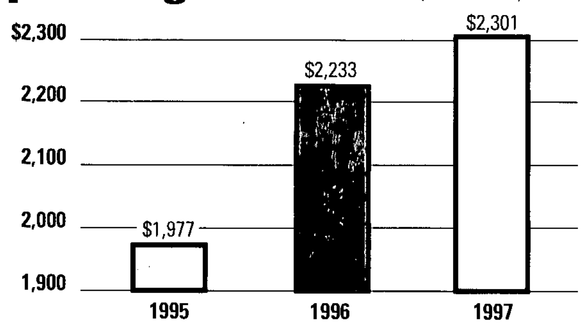
Due to the closing of the merger following year-end 1997, this summary information sets forth selected unaudited pro forma financial data for Interstate Energy Corporation. The information combines the historical consolidated balance sheets, statements of income, and utility sales of IES Industries Inc. (IES), Interstate Power Company (IPC) and WPL Holdings, Inc. (WPLH), including certain pro forma adjustments, after giving effect to the merger as if it was in place for the entire reporting periods shown. The adjustments do not include any merger-related transaction costs that will be recorded upon consummation of the merger.

The financial data are prepared on the basis of accounting for the merger as a pooling of interests. The data are not necessarily indicative of the financial position or operating results that would have occurred had the merger been consummated for the entire reporting period. Accordingly, the data do not give effect to the expected synergies or the costs to be incurred to achieve such synergies. The data also are not necessarily indicative of future operating results or financial position. The financial data should be read in conjunction with the historical financial data of IES, IPC and WPLH, as well as the unaudited pro forma combined financial statements and related notes of Interstate Energy Corporation, which are all included elsewhere in this annual report to shareowners.

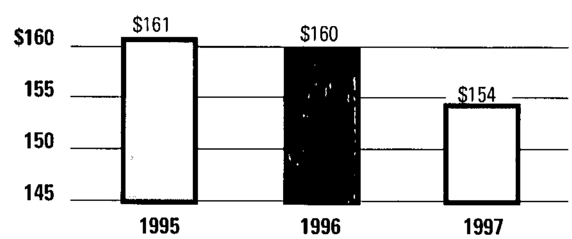
Total Assets (in millions)



Operating Revenues (in millions)



Income From Continuing Operations (in millions)



INTERSTATE ENERGY CORPORATION

(doing business as Alliant Corporation)

UNAUDITED PRO FORMA COMBINED FINANCIAL STATEMENTS

The unaudited pro forma combined financial statements for Interstate Energy Corporation (Merged Company) combine the historical consolidated balance sheets and statements of income of IES Industries Inc. (IES), Interstate Power Company (IPC) and WPL Holdings, Inc. (WPLH) as adjusted by various pro forma adjustments identified in Note 1. All material adjustments known at this time which impact the reporting periods shown have been included. The combination of WPLH, IES and IPC is referred to herein as the "Merger."

These pro forma combined financial statements set forth the restated combined financial data that will be presented for future comparative financial data for the Merged Company. The pro forma balance sheet that will be filed with the Securities and Exchange Commission following consummation of the Merger will also include an additional pro forma adjustment for certain merger-related costs to be recorded upon completion of the Merger.

These statements are prepared on the basis of accounting for the Merger as a pooling of interests and are based on the assumptions set forth in the notes thereto. The historical data for WPLH have been adjusted to reflect the restatement of such data to account for certain discontinued operations as discussed in Note 6.

The following information is not necessarily indicative of the financial position or operating resnlts that wonld have occnrred bad the Merger been consummated on the date, or at the beginning of tbe periods, for wbicb tbe Merger is being given effect nor is it necessarily indicative of future operating resnlts or financial position.

INTERSTATE ENERGY CORPORATION
UNAUDITED PRO FORMA COMBINED BALANCE SHEET
December 31, 1997
(In thousands)

	WPLH (As Reported)	IES (As Reported)	IPC (As Reported)	Pro Forma Adjustments (See Note 1)	Pro Forma Combined
ASSETS					
UTILITY PLANT					
Electric	$1,790,641	$2,072,866	$869,715	$ —	$4,733,222
Gas	237,856	187,098	70,201	—	495,155
Other	220,679	145,716	—	—	366,395
Total	2,249,176	2,405,680	939,916	—	5,594,772
Less: Accumulated provision for depreciation	1,065,726	1,115,261	450,595	—	2,631,582
Construction work in progress	42,312	38,923	5,276	—	86,511
Nuclear fuel — net	19,046	36,731	—	—	55,777
Net utility plant	1,244,808	1,366,073	494,597	—	3,105,478
OTHER PROPERTY, PLANT AND EQUIPMENT — NET AND OTHER INVESTMENTS	139,548	319,657	4,746	(125)	463,826
CURRENT ASSETS					
Cash and cash equivalents	13,987	10,143	2,897	302	27,329
Accounts receivable — net	78,082	52,295	27,061	12,489	169,927
Fossil fuel inventories, at average cost	18,857	10,579	11,220	—	40,656
Materials and supplies, at average cost	19,274	24,274	6,297	—	49,845
Prepayments and other	42,808	69,920	15,035	(3,278)	124,485
Total current assets	173,008	167,211	62,510	9,513	412,242
EXTERNAL DECOMMISSIONING FUND	112,356	77,882	—	—	190,238
INVESTMENT IN MCLEODUSA INC.	—	326,582	1,440	—	328,022
DEFERRED CHARGES AND OTHER	192,087	199,814	75,456	(15,442)	451,915
TOTAL ASSETS	$1,861,807	$2,457,219	$638,749	$ (6,054)	$4,951,721
CAPITALIZATION AND LIABILITIES					
CAPITALIZATION					
Common Stock Equity:					
Common stock	$ 308	$ —	$ 34,163	$ (33,706)	$ 765
Other stockholders' equity	607,275	818,133	181,457	38,404	1,645,269
Total common stock equity	607,583	818,133	215,620	4,698	1,646,034
Preferred stock not mandatorily redeemable	59,963	18,320	10,819	—	89,102
Preferred stock mandatory sinking fund	—	—	24,267	—	24,267
Long-term debt — net	457,520	845,189	165,194	—	1,467,903
Total capitalization	1,125,066	1,681,642	415,900	4,698	3,227,306
CURRENT LIABILITIES					
Current maturities, sinking funds, and capital lease obligations	11,528	13,684	6,314	—	31,526
Commercial paper, notes payable and other	123,095	—	33,500	—	156,595
Variable rate demand bonds	56,975	—	—	—	56,975
Accounts payable and accruals	91,175	78,702	13,208	9,549	192,634
Taxes accrued	412	62,432	16,014	65	78,923
Other accrued liabilities	55,987	67,174	12,445	(2,468)	133,138
Total current liabilities	339,172	221,992	81,481	7,146	649,791
OTHER LIABILITIES					
Deferred income taxes	253,519	372,837	104,670	—	731,026
Deferred investment tax credits	35,039	31,838	15,985	—	82,862
Accrued environmental remediation costs	9,238	46,989	5,794	—	62,021
Capital lease obligations	—	23,548	86	—	23,634
Other liabilities and deferred credits	99,773	78,373	14,833	(17,898)	175,081
Total other liabilities	397,569	553,585	141,368	(17,898)	1,074,624
TOTAL CAPITALIZATION AND LIABILITIES	$1,861,807	$2,457,219	$638,749	$ (6,054)	$4,951,721

See accompanying Notes to Unaudited Pro Forma Combined Financial Statements.

INTERSTATE ENERGY CORPORATION
UNAUDITED PRO FORMA COMBINED STATEMENTS OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 1997
(In thousands, except per share amounts)

	WPLH (As Reported)	IES (As Reported)	IPC (As Reported)	Pro Forma Adjustments (See Note 1)	Pro Forma Combined
Operating Revenues					
Electric utility	$634,143	$604,270	$277,340	$ —	$1,515,753
Gas utility	155,883	183,517	54,507	—	393,907
Other	129,229	142,912	—	118,826	390,967
Total operating revenues	919,255	930,699	331,847	118,826	2,300,627
Operating Expenses					
Electric and steam production fuels	116,812	108,344	55,402	—	280,558
Purchased power	125,438	74,098	56,770	—	256,306
Cost of gas sold	99,267	126,631	33,324	—	259,222
Other operation	254,796	231,481	64,685	119,306	670,268
Maintenance	48,058	57,185	17,782	96	123,121
Depreciation and amortization	111,289	114,122	31,676	245	257,332
Taxes other than income taxes	34,988	51,701	16,708	—	103,397
Total operating expenses	790,648	763,562	276,347	119,647	1,950,204
Operating Income	128,607	167,137	55,500	(821)	350,423
Other Income (Expense)					
Allowance for funds used during construction	2,775	2,309	190	—	5,274
Other income and deductions, net	4,432	1,850	6,772	856	13,910
Total other income (expense)	7,207	4,159	6,962	856	19,184
Interest Charges	42,535	64,383	15,610	35	122,563
Income from Continuing Operations before Income Taxes and Preferred Dividends	93,279	106,913	46,852	—	247,044
Income Taxes	28,715	39,662	17,684	—	86,061
Preferred Dividends of Subsidiaries (Note 2)	3,310	914	2,469	—	6,693
Income from Continuing Operations	$ 61,254	$ 66,337	$ 26,699	$ —	$ 154,290
Average Common Shares Outstanding	30,782	30,380	9,725	5,323	76,210
Earnings per Share of Common Stock from Continuing Operations (Basic and diluted)	$ 1.99	$ 2.18	$ 2.74	N/A	$ 2.02

See accompanying Notes to Unaudited Pro Forma Combined Financial Statements.

INTERSTATE ENERGY CORPORATION
UNAUDITED PRO FORMA COMBINED STATEMENTS OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 1996
(In thousands, except per share amounts)

	WPLH (As Reported)	IES (As Reported)	IPC (As Reported)	Pro Forma Adjustments (See Note 1)	Pro Forma Combined
Operating Revenues					
Electric utility	$589,482	$574,273	$276,620	$ —	$1,440,375
Gas utility	165,627	273,979	49,464	(113,115)	375,955
Other	177,735	125,660	—	113,115	416,510
Total operating revenues	932,844	973,912	326,084	—	2,232,840
Operating Expenses					
Electric and steam production fuels	114,470	84,579	57,560	—	256,609
Purchased power	81,108	88,350	61,556	—	231,014
Cost of gas sold	104,830	217,351	31,617	(113,474)	240,324
Other operation	317,608	212,501	51,707	113,474	695,290
Maintenance	46,492	49,001	16,164	—	111,657
Depreciation and amortization	90,683	107,393	31,087	—	229,163
Taxes other than income taxes	34,603	48,171	16,064	—	98,838
Total operating expenses	789,794	807,346	265,755	—	1,862,895
Operating Income	143,050	166,566	60,329	—	369,945
Other Income (Expense)					
Allowance for funds used during construction	3,208	2,103	263	—	5,574
Other income and deductions, net	14,098	(4,591)	2,336	—	11,843
Total other income (expense)	17,306	(2,488)	2,599	—	17,417
Interest Charges	42,027	54,822	16,472	—	113,321
Income from Continuing Operations before Income Taxes and Preferred Dividends	118,329	109,256	46,456	—	274,041
Income Taxes	41,814	47,435	18,133	—	107,382
Preferred Dividends of Subsidiaries (Note 2)	3,310	914	2,463	—	6,687
Income from Continuing Operations (Notes 3 and 6)	$ 73,205	$ 60,907	$ 25,860	$ —	$ 159,972
Average Common Shares Outstanding	30,790	29,861	9,594	5,236	75,481
Earnings per Share of Common Stock from Continuing Operations (Basic and diluted)	$ 2.38	$ 2.04	$ 2.69	N/A	$ 2.12

See accompanying Notes to Unaudited Pro Forma Combined Financial Statements.

(a) Consolidation of IEA-HES L.L.C.

In January 1997, IES and WPLH formed a gas marketing joint venture named IEA-HES L.L.C. Pursuant to the applicable accounting rules, IES and WPLH each accounted for this joint venture in 1997 under the equity method of accounting with their investment recorded on the balance sheet in "Other Property, Plant and Equipment — Net and Other Investments" and their allocated portion of earnings on the income statement in "Other Income and Deductions, Net". This pro forma adjustment reflects the financial results of IEA-HES L.L.C. as a consolidated subsidiary.

(b) Eliminations for IEA-HES L.L.C.

This pro forma adjustment reflects the elimination of intercompany balances of IEA-HES L.L.C. and also eliminates the equity investments of IES and WPLH and their allocated portion of revenues and expenses.

(c) Merged Company Common Stock Adjustment

The pro forma combined financial statements reflect the conversion of each share of IES Common Stock (no par value) outstanding into 1.14 shares of Merged Company Common Stock ($.01 par value) and the conversion of each share of IPC Common Stock ($3.50 par value) into 1.11 shares of Merged Company Common Stock ($.01 par value), and the continuation of each share of WPLH Common Stock ($.01 par value) outstanding as one share of Merged Company Common Stock, as provided in the Merger Agreement. The pro forma adjustment to common stock equity restates the common stock account to equal par value for all shares to be issued ($.01 par value per share of Merged Company Common Stock) and reclassifies the excess to other stockholders' equity. The average number of shares of common stock used for calculating per share amounts is based on the exchange ratios shown below.

	Exchange Ratio	As reported 12/31/97	Pro forma 12/31/97	As reported 12/31/96	Pro forma 12/31/96	As reported 12/31/95	Pro forma 12/31/95
WPLH	N/A	30,782	30,782	30,790	30,790	30,774	30,774
IES	1.14	30,380	34,633	29,861	34,042	29,202	33,290
IPC	1.11	9,725	10,795	9,594	10,649	9,564	10,616

The number of shares of common stock at December 31, 1997 used for calculating the par value of common stock is based on the exchange ratios shown below.

	Exchange Ratio	As reported 12/31/97	Pro forma 12/31/97
WPLH	N/A	30,789	30,789
IES	1.14	30,577	34,858
IPC	1.11	9,761	10,835

(d) IPC Unbilled Revenues

The financial results of IPC do not include accrued revenues for services rendered but unbilled at month-end. The pro forma adjustment reflects the impact of adopting unbilled revenues, including the tax impact of the adoption. The change is being implemented to conform to the method currently utilized by WPLH and IES.

(e) IES Pension Liability

The accrued pension liability (and offsetting regulatory asset), included in the financial results of IES, was calculated using a five-year smoothed method of recognizing deferred asset gains. The pro forma adjustment reflects a change to the straight market value method which recognizes deferred asset gains sooner. The change is being implemented to conform to the method currently utilized by WPLH and IPC.

1997 INCOME STATEMENT

	Consolidation of IEA-HES LLC (Note 1(a))	Eliminations for IEA-HES LLC (Note 1(b))	Merged Company Common Stock Adjustment (Note 1(c))	Total Pro Forma Adjustments
OPERATING REVENUES:				
Gas utility	$ —	$ —	$ —	$ —
Other	118,826	—	—	118,826
Total operating revenues	118,826	—	—	118,826
OPERATING EXPENSES:				
Cost of gas sold	—	—	—	—
Other operation	119,306	—	—	119,306
Maintenance	96	—	—	96
Depreciation and amortization	245	—	—	245
Total operating expenses	119,647	—	—	119,647
OPERATING INCOME	(821)	—	—	(821)
OTHER INCOME (EXPENSE)				
Other income and deductions, net	61	795	—	856
Total other income (expense)	61	795	—	856
INTEREST CHARGES	35	—	—	35
INCOME FROM CONTINUING OPERATIONS	$ (795)	$795	$ —	$ —
AVERAGE COMMON SHARES	—	—	5,323	5,323

1996 INCOME STATEMENT

	Merged Company Common Stock Adjnstment (Note 1(c))	IEA Gas Activity (Note 1(f))	Total Pro Forma Adjustments
OPERATING REVENUES:			
Gas utility	$ —	$(113,115)	$(113,115)
Other	—	113,115	113,115
Total operating revenues	—	—	—
OPERATING EXPENSES:			
Cost of gas sold	—	(113,474)	(113,474)
Other operation	—	113,474	113,474
Total operating expenses	—	—	—
INCOME FROM CONTINUING OPERATIONS	$ —	$ —	$ —
AVERAGE COMMON SHARES	5,236	—	5,236

1995 INCOME STATEMENT

	Merged Company Common Stock Adjustment (Note 1(c))	IEA Gas Activity (Note 1(f))	Total Pro Forma Adjnstments
OPERATING REVENUES:			
Gas utility	$ —	$(53,047)	$(53,047)
Other	—	53,047	53,047
Total operating revenues	—	—	—
OPERATING EXPENSES:			
Cost of gas sold	—	(50,519)	(50,519)
Other operation	—	50,519	50,519
Total operating expenses	—	—	—
INCOME FROM CONTINUING OPERATIONS	$ —	$ —	$ —
AVERAGE COMMON SHARES	5,140	—	5,140

INTERSTATE ENERGY CORPORATION

NOTES TO UNAUDITED PRO FORMA COMBINED FINANCIAL STATEMENTS

I. Pro Forma Adjustments

December 31, 1997 BALANCE SHEET

	Consolidation of IEA-HES LLC (Note 1(a))	Eliminations for IEA-HES LLC (Note 1(b))	Merged Company Common Stock Adjnstment (Note 1(c))	IPC Unbilled Revennes (Note 1(d))	IES Pension Liability (Note 1(e))	Total Pro Forma Adjustments
ASSETS						
OTHER PROPERTY, PLANT AND EQUIPMENT — NET AND OTHER INVESTMENTS	$ 3,458	$(3,583)	$ —	$ —	$ —	$ (125)
CURRENT ASSETS						
Cash and cash equivalents	3,308	(3,006)	—	—	—	302
Accounts receivable — net	8,932	(1,965)	—	5,522	—	12,489
Prepayments and other	2	—	—	(3,280)	—	(3,278)
Total current assets	12,242	(4,971)	—	2,242	—	9,513
DEFERRED CHARGES AND OTHER	—	—	—	2,456	(17,898)	(15,442)
TOTAL ASSETS	$15,700	$(8,554)	$ —	$ 4,698	$(17,898)	$ (6,054)
CAPITALIZATION AND LIABILITIES						
CAPITALIZATION						
Common Stock Equity:						
Common stock	$ —	$ —	$ (33,706)	$ —	$ —	$ (33,706)
Other stockholders' equity	3,583	(3,583)	33,706	4,698	—	38,404
Total common stock equity	3,583	(3,583)	—	4,698	—	4,698
CURRENT LIABILITIES						
Accounts payable and accruals	11,514	(1,965)	—	—	—	9,549
Taxes accrued	65	—	—	—	—	65
Other accrued liabilities	538	(3,006)	—	—	—	(2,468)
Total current liabilities	12,117	(4,971)	—	—	—	7,146
OTHER LIABILITIES						
Other liabilities and deferred credits	—	—	—	—	(17,898)	(17,898)
Total other liabilities	—	—	—	—	(17,898)	(17,898)
TOTAL CAPITALIZATION AND LIABILITIES	$15,700	$(8,554)	$ —	$ 4,698	$(17,898)	$ (6,054)

INTERSTATE ENERGY CORPORATION
UNAUDITED PRO FORMA COMBINED STATEMENTS OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 1995
(In thousands, except per share amounts)

	WPLH (As Reported)	IES (As Reported)	IPC (As Reported)	Pro Forma Adjustments (See Note 1)	Pro Forma Combined
Operating Revenues					
Electric utility	$546,324	$560,471	$274,873	$ —	$1,381,668
Gas utility	139,165	190,339	43,669	(53,047)	320,126
Other	121,766	100,200	—	53,047	275,013
Total operating revenues	807,255	851,010	318,542	—	1,976,807
Operating Expenses					
Electric and steam production fuels	116,488	96,256	62,164	—	274,908
Purchased power	44,940	66,874	57,566	—	169,380
Cost of gas sold	84,002	141,716	25,888	(50,519)	201,087
Other operation	252,722	199,768	44,581	50,519	547,590
Maintenance	42,043	46,093	14,881	—	103,017
Depreciation and amortization	86,319	97,958	29,560	—	213,837
Taxes other than income taxes	34,188	49,011	15,990	—	99,189
Total operating expenses	660,702	697,676	250,630	—	1,609,008
Operating Income	146,553	153,334	67,912	—	367,799
Other Income (Expense)					
Allowance for funds used during construction	2,088	3,424	341	—	5,853
Other income and deductions, net	5,954	1,548	(4,008)	—	3,494
Total other income (expense)	8,042	4,972	(3,667)	—	9,347
Interest Charges	43,559	50,727	17,136	—	111,422
Income from Continuing Operations before Income Taxes and Preferred Dividends	111,036	107,579	47,109	—	265,724
Income Taxes	36,108	42,489	19,453	—	98,050
Preferred Dividends of Subsidiaries (Note 2)	3,310	914	2,458	—	6,682
Income from Continuing Operations (Note 6)	$ 71,618	$ 64,176	$ 25,198	$ —	$ 160,992
Average Common Shares Outstanding	30,774	29,202	9,564	5,140	74,680
Earnings per Share of Common Stock from Continuing Operations (Basic and diluted)	$ 2.33	$ 2.20	$ 2.63	N/A	$ 2.16

See accompanying Notes to Unaudited Pro Forma Combined Financial Statements

(f) IEA Gas Activity

The gas revenues and cost of gas sold of Industrial Energy Applications, Inc. (IEA), a subsidiary of IES, for 1996 and 1995 have been reclassified into "Other" operating revenues and "Other operation" expenses, respectively consistent with the 1997 presentation.

2. Preferred Stock Dividends of IPC

The Preferred Stock Dividends of IPC have been reclassified in the unaudited pro forma combined statements as "Preferred Dividends of Subsidiaries" and deducted in the determination of income from continuing operations which reflects the holding company structure of the Merged Company.

3. Nonrecurring Material Items Included in Historical Financial Results

IES's income from continuing operations for the year ended December 31, 1996 included costs incurred relating to its successful defense of a hostile takeover attempt mounted by MidAmerican Energy Company. The after-tax impact on income from continuing operations was a decrease of $4.6 million.

Nonrecurring items affecting WPLH's performance for the year ended December 31, 1996 included the impact of the sale of a combustion turbine and the sale of WPLH's assisted-living real estate investments. The after-tax impact of these items on continuing operations was an increase of $5.9 million.

4. Estimated Costs and Cost Savings of Proposed Merger

The allocation between WPLH, IES and IPC and their customers of the estimated cost savings of approximately $749 million over ten years resulting from the merger, net of the costs incurred to achieve such savings, will be subject to regulatory review and approval. Costs arising from the Merger are currently estimated to be approximately $78 million. Approximately $22 million of these costs had been incurred through December 31, 1997 and are reflected in results of operations. The estimate of potential cost savings constitutes a forward-looking statement and actual results may differ materially from this estimate. The estimate is necessarily based upon various assumptions that involve judgments with respect to, among other things, future national and regional economic and competitive conditions, technological developments, inflation rates, regulatory treatment, weather conditions, financial market conditions, future business decisions and other uncertainties. No assurance can be given that the estimated cost savings will actually be realized. None of the estimated cost savings, or costs to be incurred subsequent to December 31, 1997 to achieve such savings, have been reflected in the unaudited pro forma combined financial statements.

5. Intercompany Transactions

Intercompany transactions (including purchased and exchange power transactions) between WPLH, IES and IPC during the periods presented were included in the determination of regulated rates and/or were not material. Accordingly, no pro forma adjustments were made to eliminate such transactions.

6. Discontinued Operations

The financial statements of WPLH reflect the discontinuance of operations of its utility energy and marketing consulting business in 1995. The discontinuance of this business resulted in a pre-tax loss in the fourth quarter of 1995 of $7.7 million. The after-tax loss on disposition was $11.0 million reflecting the associated tax expense on disposition due to the non-deductibility of the carrying value of goodwill at sale. During 1996, WPLH recognized an additional loss of $1.3 million, net of applicable income tax benefit, associated with the final disposition of the business. Operating revenues, operating expenses, other income and expense and income taxes for the discontinued operations for the time periods presented have been excluded from income from continuing operations. Interest expense has been adjusted for the amounts associated with direct obligations of the discontinued operations.

WPL HOLDINGS, INC.

IES INDUSTRIES INC.

INTERSTATE POWER COMPANY

(Merged as Interstate Energy Corporation,
doing business as Alliant Corporation)

1997 FINANCIAL INFORMATION

The following items are included in this financial insert:

1. **Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A)** — the discussion of historical results of operations focuses primarily on WPL Holdings, Inc. (WPLH). This presentation is in accordance with the rules of the Securities and Exchange Commission (SEC) since WPLH (now Interstate Energy Corporation) was the surviving holding company in the merger involving WPLH, IES Industries Inc. (IES) and Interstate Power Company (IPC). The portions of MD&A which are prospective in nature generally reflect a discussion of Interstate Energy Corporation's operations on a post-merger basis.

2. **Selected Consolidated Quarterly Financial Data (Unaudited)** — in accordance with SEC rules, reflects WPLH results on a stand-alone basis.

3. **Consolidated Financial Statements and Related Notes** — in accordance with SEC rules, reflects WPLH results on a stand-alone basis.

4. **WPL Holdings, Inc. Selected Financial and Operating Statistics** — includes statistics for the last five years for WPLH on a stand-alone basis.

5. **IES Industries Inc. Selected Financial and Operating Statistics** — includes statistics for the last five years for IES Industries Inc. on a stand-alone basis.

6. **Interstate Power Company Selected Financial and Operating Statistics** — includes statistics for the last five years for Interstate Power Company on a stand-alone basis.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (MD&A)

MERGER

In April 1998, WPL Holdings, Inc. (WPLH), IES Industries Inc. (IES) and Interstate Power Company (IPC) completed the three-way merger (Merger) forming Interstate Energy Corporation (Merged Company). In connection with the Merger, IES was merged with and into WPLH forming the Merged Company and IPC became a subsidiary of the Merged Company. In addition, following the Merger, the holding companies for the nonregulated businesses of the former WPLH and IES (Heartland Development Corporation (HDC) and IES Diversified Inc. (Diversified), respectively) were merged. The resulting company from this merger is referred to as New Diversified. As a result of the Merger, the first tier subsidiaries of the Merged Company include: Wisconsin Power & Light Company (WP&L), IES Utilities Inc. (IESU), IPC, New Diversified and Alliant Services Company (the subsidiary formed to provide administrative services as required under the Public Utility Holding Company Act of 1935). Among various other regulatory constraints, the Merged Company will operate as a registered public utility holding company subject to the limitations imposed by the Public Utility Holding Company Act of 1935. For additional information regarding the terms of the Merger, see Notes 2 and 15 of the "Notes to Consolidated Financial Statements" of WPLH included elsewhere in this Annual Report.

The Merged Company currently anticipates cost savings resulting from the Merger of approximately $749 million over a ten-year period, net of transaction costs and costs to achieve the savings of approximately $78 million. Approximately $22 million of these costs had been incurred through December 31, 1997. Upon consummation of the Merger, the Merged Company estimates it will expense approximately $40 million of additional merger-related costs (e.g., required payments to or for financial advisors, employee retirements and separations, attorneys, accountants, etc.). The estimate of potential cost savings constitutes a forward-looking statement and actual results may differ materially from this estimate. The estimate is necessarily based upon various assumptions that involve judgments with respect to, among other things, future national and regional economic and competitive conditions, technological developments, inflation rates, regulatory treatments, weather conditions, financial market conditions, future business decisions and other uncertainties. No assurance can be given that the entire amount of estimated cost savings will actually be realized. In addition, the allocation between WPLH, IES and IPC and their customers of the estimated cost savings of approximately $749 million over ten years resulting from the Merger, net of costs incurred to achieve such savings, will be subject to regulatory review and approval.

As part of the approval process for the Merger, the Merged Company has agreed to various rate freezes and rate caps to be implemented in certain jurisdictions for periods not to exceed four years commencing on the effective date of the Merger (see "Liquidity and Capital Resources — Rates and Regulatory Matters" for a further discussion).

Assuming capture of the anticipated merger-related synergies and no significant legislative or regulatory changes affecting the Merged Company, the Merged Company does not expect the merger-related electric and natural gas price freezes to have a material adverse effect on its financial position or results of operations.

FORWARD-LOOKING STATEMENTS

Statements contained in this Annual Report (including MD&A) that are not of historical fact are forward-looking statements intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. From time to time, the Merged Company may make other forward-looking statements within the meaning of the federal securities laws that involve judgments, assumptions and other uncertainties beyond the control of the Merged Company. These forward-looking statements may include, among others, statements concerning revenue and cost trends, cost recovery, cost reduction strategies and anticipated outcomes, pricing strategies, changes in the utility industry, planned capital expenditures, financing needs and availability, statements of the Merged Company's expectations, beliefs, future plans and strategies, anticipated events or trends and similar comments concerning matters that are not historical facts. Investors and other users of the forward-looking statements are cautioned that such statements are not a guarantee of future performance of the

Merged Company and that such forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in, or implied by, such statements. Some, but not all, of the risks and uncertainties include weather effects on sales and revenues, competitive factors, general economic conditions in the Merged Company's service territory, federal and state regulatory or government actions, the operations of the Merged Company's nuclear facilities, the ability of the Merged Company to successfully integrate the operations of WPLH, IES and IPC and changes in the rate of inflation.

UTILITY INDUSTRY OUTLOOK

The Merged Company competes in an ever-changing utility industry. Set forth below is an overview of this evolving marketplace.

Electric energy generation, transmission, and distribution are in a period of fundamental change in the manner in which customers obtain, and energy suppliers provide, energy services. As legislative, regulatory, economic and technological changes occur, electric utilities are faced with increasing pressure to become more competitive. Such competitive pressures could result in loss of customers and an incurrence of stranded costs (i.e., assets and other costs rendered unrecoverable as the result of competitive pricing). To the extent stranded costs cannot be recovered from customers, they would be borne by security holders.

The Merged Company realized 54%, 41%, 3% and 2% of its electric utility revenues in 1997 in Iowa, Wisconsin, Minnesota and Illinois, respectively. Approximately 87% of the electric revenues were regulated by the respective state commissions while the other 13% were regulated by the Federal Energy Regulatory Commission (FERC). The Merged Company realized 56%, 38%, 3% and 3% of its gas utility revenues in Iowa, Wisconsin, Minnesota and Illinois, respectively.

Federal Regulation

IESU, IPC and WP&L are all subject to regulation by the FERC. The National Energy Policy Act of 1992 addresses several matters designed to promote competition in the electric wholesale power generation market. In 1996, the FERC issued final rules (FERC Orders 888 and 889) requiring electric utilities to open their transmission lines to other wholesale buyers and sellers of electricity. In March 1997, FERC issued orders on rehearing for Orders 888 and 889 (Orders 888-A and 889-A). In response to FERC Orders 888 and 888-A, IESU, WP&L and IPC have on file with the FERC pro forma open access transmission tariffs. In response to FERC Orders 889 and 889-A, each of the three utility subsidiaries is participating in a regional Open Access Same-Time Information System. The utility subsidiaries cannot predict the long-term consequences of these rules on their results of operations or financial condition.

FERC Order 888 permits utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and transmission services. FERC does not have jurisdiction over retail distribution and, consequently, the final FERC rules do not provide for the recovery of stranded costs resulting from retail competition. The various states retain jurisdiction over the question of whether to permit retail competition, the terms of such retail competition, and the recovery of any portion of stranded costs that are ultimately determined to have resulted from retail competition.

State Regulation

Iowa

IESU and IPC are subject to regulation by the Iowa Utilities Board (IUB). The IUB initiated a Notice of Inquiry (Docket No. NOI-95-1) in early 1995 on the subject of "Emerging Competition in the Electric Utility Industry" to address all forms of competition in the electric utility industry and to gather information and perspectives on electric competition from all persons or entities with an interest or stake in the issues. The IUB staff's report in this docket was accepted by the IUB, finding, in part, that there is no compelling reason to move quickly into restructuring the electric utility industry in Iowa, based upon the existing level of relative prices. However, the IUB is continuing the analysis and debate on restructuring and retail competition in Iowa.

On August 18, 1997, the IUB issued an order that promulgated draft principles for an Independent System Operator (ISO) and invited public comment. On September 10, 1997, the IUB issued an order adopting an "Action Plan to Develop a Competitive Model for the Electric Industry in Iowa." The IUB states in this action plan that while "the IUB has not determined retail competition in the electric industry is in the best interests of Iowa's consumers...", the State of Iowa is likely to be affected by federal or neighboring states' actions so there is a need for the IUB to design a model that suits Iowa's needs. The priority concerns in the plan are public interest issues (an Iowa-specific pilot project, customer information and assessment, environmental impacts, public benefits and transition costs/benefits) and transmission-related issues (transmission and distribution system reliability and transmission system operations). There is no timetable in the action plan. On October 2, 1997, the IUB staff sent to the advisory group (of which IESU and IPC are members) for written comment a set of proposed guidelines for an Iowa-specific electric pilot project that would allow retail access to a "subset of all customer classes." IESU has indicated to the IUB its interest in pursuing such a pilot program. The IUB has also issued an order covering unbundling of natural gas rates for all Iowa customers to be effective in 1999.

Wisconsin

WP&L is subject to regulation by the Public Service Commission of Wisconsin (PSCW). The PSCW's inquiries into the future structure of the natural gas and electric utility industries are ongoing. The stated goal of the PSCW in the natural gas docket is "to accommodate competition but not create it." The PSCW has followed a measured approach to restructuring the natural gas industry in Wisconsin. The PSCW has determined that customer classes will be deregulated (i.e., the gas utility would no longer have an obligation to procure gas commodity for customers, but would still have a delivery obligation) in a step-wise manner, after each class has been demonstrated to have a sufficient number of gas suppliers available. In 1997, a number of working groups were established by the PSCW and these working groups are addressing numerous subjects which need to be resolved before deregulation may proceed.

The short-term goals of the electric restructuring process are to ensure reliability of the state's electric system and development of a robust wholesale electric market. The longer-term goal is to establish prerequisite safeguards to protect customers prior to allowing retail customer choice. The PSCW is following a timetable to make this latter determination on allowing customer choice in 1999-2000.

On September 26, 1996, the PSCW issued an order which establishes the minimum standards for a Wisconsin ISO. The standards will be applied by the PSCW in Advance Plan proceedings, merger review cases, transmission construction cases and other proceedings as appropriate. The order provides that the standards will be reviewed and revised as necessary in light of ongoing regional and national events, such as FERC requirements or policy, regional institutions, or relevant actions of neighboring states. In approving the Merger, the PSCW gave the merger partners a choice of either filing their own ISO proposal, giving notice of their intent to join a regional ISO or spinning off existing transmission assets and operations into a separate independent transmission company. IESU, IPC and WP&L developed an ISO proposal of their own. However, the PSCW did not believe it met the PSCW's ISO guidelines. IESU, IPC and WP&L subsequently asked the PSCW to permit them to join the Midwest ISO, a regional ISO that has been filed with FERC. The member companies of the ISO would retain ownership of the facilities, but the ISO would assume control of the facilities, set rates for access and assure fair treatment for all companies seeking access. Various other proposals for ISOs, which are being monitored by the Merged Company, have been proposed by other entities.

In addition to the ISO proceedings, the PSCW has issued an order outlining its policies and principles for Public Benefits (low-income assistance, energy efficiency, renewable generation and environmental research and development) including funding levels, administration of the funds and how funds should be collected from customers. The PSCW has proposed increasing funding levels through utility rates by $50 to $75 million statewide. Legislation to implement this proposal is being developed and likely will be introduced in 1998.

The PSCW has also initiated a Service Quality administrative rulemaking process to establish measurement and reporting requirements for reliability of service, call center answering times, safety, tree trimming, generation, transmission and distribution inspection and maintenance plans, etc. A hearing was held on these issues in March 1998.

Minnesota

IPC is subject to regulation by the Minnesota Public Utilities Commission (MPUC). The MPUC established an Electric Competition Working Group in April 1995. On October 28, 1997, the Working Group issued a report and recommendations on retail competition. The MPUC reviewed the report and directed its staff to develop an electric utility restructuring plan and timeline. The Minnesota legislature had established a joint legislative task force on electric utility restructuring in 1995. This joint task force has generally been inactive the past year. It appears the earliest restructuring legislation could be introduced is in 1999.

Illinois

IPC and WP&L are subject to regulation by the Illinois Commerce Commission. The State of Illinois has passed electric deregulation legislation requiring customer choice of electric supplier for all customers by May 1, 2002.

Summary

Each of the utilities complies with the provisions of Statement of Financial Accounting Standards No. 71 (SFAS 71) "Accounting for the Effects of Certain Types of Regulation." SFAS 71 provides that rate-regulated public utilities record certain costs and credits allowed in the ratemaking process in different periods than for nonregulated entities. These are deferred as regulatory assets or regulatory liabilities and are recognized in the consolidated statements of income at the time they are reflected in rates. If a portion of the utility subsidiaries' operations becomes no longer subject to the provisions of SFAS 71 as a result of competitive restructurings or otherwise, a write-down of related regulatory assets and possibly other charges would be required, unless some form of transition cost recovery is established by the appropriate regulatory body that would meet the requirements under generally accepted accounting principles for continued accounting as regulatory assets during such recovery period. In addition, each utility subsidiary would be required to determine any impairment of other assets and write-down any impaired assets to their fair value. The utility subsidiaries believe they meet the requirements of SFAS 71.

IESU, IPC and WP&L cannot currently predict the long-term consequences of the competitive and restructuring issues described above on their results of operations or financial condition. The major objective is to allow the utilities to better prepare for a competitive, deregulated utility industry. The strategy for dealing with these emerging issues includes seeking growth opportunities, continuing to offer quality customer service, ongoing cost reductions and productivity enhancements.

WPLH RESULTS OF OPERATIONS — 1997 COMPARED WITH 1996

Pursuant to the rules of the Securities and Exchange Commission, the "Results of Operations" discussion set forth below covers only the results of WPLH since the Merger was consummated after December 31, 1997, and WPLH (renamed Interstate Energy Corporation) was the surviving holding company resulting from the Merger. Certain information regarding the operations of IES and IPC are set forth below under the heading "Pro Forma Earnings Per Share Information and Historical IES and IPC Data." For additional information regarding the pro forma results of the combined companies, see "Interstate Energy Corporation Unaudited Pro Forma Combined Financial Statements." All references to earnings per share throughout MD&A refer to both basic and diluted earnings per share.

Overview

WPLH reported consolidated net income from continuing operations of $61.3 million or $1.99 per share for 1997, as compared to $73.2 million or $2.38 per share for 1996. Earnings per share for 1997 and 1996 were $1.99 and $2.34, respectively, reflecting the impact of discontinued operations.

The decrease in 1997 earnings versus 1996 was primarily the result of lower operating income at WP&L and the impact of non-recurring gains which contributed 5 cents per share to earnings in 1997 compared to 19 cents in 1996.

Gas and electric margins were down $4.2 and $2.0 million, respectively, in 1997 as compared to 1996. The decrease in gas margin was primarily due to lower weather-driven sales to residential customers as well as a 2.2% average retail gas rate decrease which went into effect on April 29, 1997. The lower electric margin was the result of a 2.4% average retail electric rate decrease effective April 29, 1997, as well as higher purchased power expense due to an extended outage at the Kewaunee Nuclear Power Plant (Kewaunee). Sales to other utilities and continued economic strength in WP&L's service territory partially offset the impact of the decline in margin. In addition, income in 1997 was also lower than 1996 due to increased expenses for plant maintenance, depreciation and interest.

HDC, parent company of WPLH's nonregulated operations, reported a loss from continuing operations of $2.8 million for 1997 compared with a loss from continuing operations of $3.5 million for 1996. HDC's 1997 results reflect improved performance of the energy marketing business. In 1997, HDC recognized an after-tax loss of $1.1 million as a result of a write-off of nonproductive assets in its environmental and engineering services business. In 1996, HDC recognized an after-tax gain of $2.5 million related to the sale of HDC's investment in assisted living properties.

WPLH also recognized a 1996 after-tax loss of $1.3 million resulting from additional fees and expenses related to discontinued operations which is discussed in Note 12 of "Notes to Consolidated Financial Statements."

WPLH Electric Operations

	Reveuues aud Costs (In Thousauds)			kWhs Sold (In Thonsands)			Customers at Year End		
	1997	1996	Change	**1997**	1996	Change	**1997**	1996	Chauge
Residential	**$199,633**	$201,690	(1%)	**2,973,932**	2,979,826	—	**343,637**	336,933	2%
Commercial	**107,132**	105,319	2%	**1,877,640**	1,814,324	3%	**46,823**	45,669	3%
Industrial	**152,073**	143,734	6%	**4,255,637**	3,985,672	7%	**855**	815	5%
Sales for resale	**160,917**	131,836	22%	**5,823,521**	5,245,812	11%	**122**	90	36%
Other	**14,388**	6,903	108%	**61,330**	57,757	6%	**1,753**	1,730	1%
Total	**634,143**	589,482	8%	**14,992,060**	14,083,391	6%	**393,190**	385,237	2%
Electric									
Production Fuels	**116,812**	114,470	2%						
Purchased Power	**125,438**	81,108	55%						
Margin	**$391,893**	$393,904	(1%)						

Electric revenues increased $44.7 million, or 8%, in 1997 as compared with 1996. Continued customer growth, economic strength in the service area and increased sales to other utilities offset the impact of cooler summer weather and warmer weather during the winter months of 1997. Revenues were also affected by an average retail rate decrease of 2.4% effective April 29, 1997. Other revenues increased in 1997 compared with 1996 due to increases in conservation services. Refer to the "Liquidity and Capital Resources — Rates and Regulatory Matters" section below for further discussion of these rate modifications.

Despite higher electric revenues, electric margin decreased $2.0 million, or 1%, as compared with 1996. The decline in margin reflects the impact of the shutdown at Kewaunee throughout most of the first half of 1997 for steam generator tube repairs as well as several temporary, routine outages at WP&L's coal-fired plants through the first five months of 1997. These outages caused a greater reliance on more costly purchased power to meet customer requirements. The PSCW ordered a temporary customer surcharge effective April 29, 1997 through July 1, 1997, to allow WP&L to recover a portion of the higher purchased power costs associated with the Kewaunee outage. Refer to the "Liquidity and Capital Resources — Capital Requirements" section below for further discussion of the Kewaunee plant outage. The Kewaunee outage and increased sales to other utilities resulted in a 55% increase in the cost of purchased power.

For a discussion of electric capacity and reliability refer to "Other Matters — Power Supply" section below.

WPLH Gas Operations

	Reveuues and Costs (In Thousands)			Therms Sold (In Tbousands)			Customers at Year End		
	1997	1996	Change	1997	1996	Change	1997	1996	Change
Residential	**$ 84,513**	$ 90,382	(6%)	**127,704**	142,974	(11%)	**137,827**	133,580	3%
Commercial	**45,456**	46,703	(3%)	**85,917**	91,665	(6%)	**16,653**	16,083	4%
Industrial	**8,378**	11,410	(27%)	**17,144**	19,974	(14%)	**488**	529	(8%)
Transportation and other	**17,536**	17,132	2%	**175,943**	185,671	(5%)	**358**	252	42%
Total	**155,883**	165,627	(6%)	**406,708**	440,284	(8%)	**155,326**	150,444	3%
Purchased Gas	**99,267**	104,830	(5%)						
Margin	**$ 56,616**	$ 60,797	(7%)						

Gas revenues decreased $9.7 million, or 6%, in 1997 as compared with 1996. The decline in revenues and margin reflected an average retail rate decrease of 2.2%, effective April 29, 1997, and lower sales. Therm sales declined by 8% due to warmer weather in the winter months of 1997. This decrease was directly reflected in the decline in revenues and corresponding $4.2 million, or 7%, decrease in margin. WP&L realized favorable contributions to gas margin of $0.6 million and $1.1 million for 1997 and 1996, respectively, through its gas incentive program. Refer to the "Liquidity and Capital Resources — Rates and Regulatory Matters" section below for further discussion of this adjustment mechanism.

Fees, Rents, Non-Utility Energy Sales and Other Revenues

Fees, rents, non-utility energy sales and other revenues primarily reflect sales and revenues of WPLH's nonregulated subsidiaries, consolidated under HDC. Revenues of the principal businesses of HDC were as follows:

	1997	1996
Environmental and engineering services	**$ 78.1**	$ 84.8
Energy marketing	**30.8**	73.8
Other	**15.6**	14.9
	$124.5	$173.5

Contributing to the decrease in these revenues for 1997 was the formation of a joint venture, effective January 1, 1997, between the gas marketing business of the energy marketing subsidiary and Industrial Energy Applications, Inc. (IEA), the energy marketing subsidiary of IES. HDC owns 50% of this joint venture and for the year ended December 31, 1997, accounted for the investment under the equity method. Therefore, HDC's share of revenues and expenses related to this joint venture have been included with "Interest Expense and Other." Revenues for 1996 included $26.4 million related to gas marketing sales now associated with the joint venture. In addition, the softening market for the environmental and engineering services business and the transfer of the power marketing business to a joint venture formed with Cargill Incorporated contributed to the decline in revenues for 1997. See Note 14 of "Notes to Consolidated Financial Statements" for a further discussion of this joint venture.

In addition to the revenues of the nonregulated businesses, other revenues also include the water operations of WP&L. These revenues were $4.7 million in 1997 and $4.2 million in 1996.

Other Operation and Cost of Non-Utility Energy

Other operation and cost of non-utility energy expense includes expenses related to WP&L, WPLH and the nonregulated businesses of HDC. The distribution of other operations expense was as follows:

	1997	1996
WP&L	**$131.4**	$140.3
Nonregulated businesses and parent company operations	**123.4**	177.3
	$254.8	$317.6

Contributing to the decrease in other operation and cost of non-utility energy was the recording of HDC's share of the expenses associated with the gas marketing joint venture under "Interest Expense and Other," as discussed above. Operating expenses at the nonregulated businesses for the year ended December 31, 1996, included $30.8 million related to gas marketing sales now associated with the joint venture. In 1997, these expenses were included with "Interest Expense and Other", as previously discussed under "Fees, Rents, Non-Utility Energy Sales and Other Revenues." In addition, the softening market for the environmental and engineering services business and the reduced activity in the electric power area of the energy marketing subsidiary also contributed to the decline in other operations expense for 1997.

Conservation expense at WP&L was reduced significantly under the retail rate order, effective April 29, 1997. This reduction decreased WP&L's operating expenses by $8.8 million in 1997 compared with the same period in 1996. Partially offsetting this decrease was an additional $3.0 million of operating expense in the fourth quarter of 1997, associated with an early retirement program for eligible bargaining unit employees.

Maintenance Expense

Maintenance expense increased as a result of higher plant maintenance expenses at Kewaunee and several of WP&L's coal-fired plants, as discussed above under "WPLH Electric Operations."

Depreciation and Amortization

Depreciation expense increased due to higher depreciation rates at WP&L approved by the PSCW, effective January 1, 1997, and property additions. The increases approved by the PSCW included higher depreciation expense for Kewaunee, based on the use of an accelerated plant end-of-life, increased contributions to the nuclear decommissioning trust fund and other items. (See "Liquidity and Capital Resources — Capital Requirements" for additional information). In 1997, HDC recognized an after-tax loss of $1.1 million as a result of a write-off of nonproductive assets in its environmental and engineering services business.

Interest Expense and Other

The increase in interest expense and other is primarily the result of non-recurring gains which contributed 5 cents per share in 1997 and 19 cents per share in 1996.

Income Taxes

The decrease in income taxes between periods reflects lower taxable income, an adjustment of prior period taxes and increased affordable housing and historical tax credits.

WPLH RESULTS OF OPERATIONS — 1996 COMPARED WITH 1995

Overview

WPLH reported consolidated net income from continuing operations of $73.2 million or $2.38 per share for 1996, as compared to $71.6 million or $2.33 per share for 1995. Earnings per share for 1996 and 1995 were $2.34 and $1.90, respectively, reflecting the impact of the discontinued operations.

The increase in earnings in 1996 primarily reflects the operations of WPLH's utility subsidiary, WP&L. Continued customer growth in the service territory and increased power marketing activity contributed to a $9 million increase in electric margin in 1996 as compared with 1995. The 1996 gas margin also increased due primarily to higher weather-driven sales. (See "WPLH Electric Operations" and "WPLH Gas Operations" below). In addition, a $3.4 million after-tax gain on the sale of a combustion turbine was recognized during 1996. These events were partially offset by higher plant maintenance and depreciation expenses in 1996.

HDC, parent company of WPLH's nonregulated operations, rcported a loss from continuing operations of $3.5 million for 1996 compared with a loss from continuing operations of $1.5 million for 1995. HDC's 1996 results were adversely impacted by contract losses early in 1996 associated with the start-up of the energy marketing business as well as a softening market for the environmental and engineering services business. Partially offsetting these losses was an after-tax gain of $2.5 million in 1996, related to the sale of HDC's investment in assisted living properties.

WPLH also recognized a 1996 after-tax loss of $1.3 million resulting from additional fees and expenses related to the discontinued operations which is discussed in Note 12 of "Notes to Consolidated Financial Statements."

WPLH Electric Operations

	Revenues and Costs (In Thousands)			kWhs Sold (In Thousands)			Customers at Year End		
	1996	1995	Change	1996	1995	Change	1996	1995	Change
Residential	**$201,690**	$199,850	1%	**2,979,826**	2,937,825	1%	**336,933**	329,643	2%
Commercial	**105,319**	102,129	3%	**1,814,324**	1,773,406	2%	**45,669**	44,730	2%
Industrial	**143,734**	140,562	2%	**3,985,672**	3,872,520	3%	**815**	795	3%
Sales for resale	**131,836**	97,350	35%	**5,245,812**	3,109,385	69%	**90**	48	88%
Other	**6,903**	6,433	7%	**57,757**	54,042	7%	**1,730**	1,294	34%
Total	**589,482**	546,324	8%	**14,083,391**	11,747,178	20%	**385,237**	376,510	2%
Electric Production Fuels	**114,470**	116,488	(2%)						
Purchased Power	**81,108**	44,940	80%						
Margin	**$393,904**	$384,896	2%						

Electric margin increased $9.0 million, or 2%, during 1996 compared with 1995 primarily due to higher sales to commercial and industrial customers as well as other utilities combined with reduced costs per kWh for electric production fuels and purchased power. Although fuel and purchased power costs declined on a per kWh basis, purchased power expense increased by 80%. This increase was due to WP&L's higher level of sales to other utilities as well as a $5.0 million increase in purchased power related to the purchase of replacement power during the extended 1996 refueling outage at Kewaunee. Partially offsetting increased purchased power costs were slightly lower delivered coal and nuclear fuel costs per kWh.

WPLH Gas Operations

	Revenues and Costs (In Thousands) 1996	1995	Change	Therms Sold (In Thousands) 1996	1995	Change	Customers at Year End 1996	1995	Change
Residential	**$ 90,382**	$ 70,382	28%	**142,974**	126,903	13%	**133,580**	129,576	3%
Commercial	**46,703**	35,411	32%	**91,665**	82,448	11%	**16,083**	15,724	2%
Industrial	**11,410**	17,984	(37%)	**19,974**	21,435	(7%)	**529**	566	(7%)
Transportation and other	**17,132**	15,388	11%	**185,671**	168,702	10%	**252**	227	11%
Total	**165,627**	139,165	19%	**440,284**	399,488	10%	**150,444**	146,093	3%
Purchased Gas	**104,830**	84,002	25%						
Margin	**$ 60,797**	$ 55,163	10%						

Gas margins increased $5.6 million, or 10%, during 1996 compared with 1995 primarily as a result of higher sales. Therm sales increased 10% due to a combination of colder weather during the first five months of 1996 as compared to 1995, and customer growth of 3%. The 19% increase in gas revenues reflects not only the higher therm sales but also the pass through of higher natural gas costs to WP&L's customers. WP&L realized favorable contributions to gas margins of $1.1 million and $0.8 million for 1996 and 1995, respectively, due to favorable gas procurement activities. Refer to the "Liquidity and Capital Resources — Rates and Regulatory Matters" section below for further discussion of this adjustment mechanism.

Fees, Rents, Non-Utility Energy Sales and Other Revenues

Fees, rents, non-utility energy sales and other revenues primarily reflect sales and revenues of WPLH's nonregulated subsidiaries, consolidated under HDC, as adjusted for discontinued operations. Revenues of the principal businesses of HDC were as follows:

	1996	1995
Environmental and engineering services	**$ 84.8**	$ 88.6
Energy marketing	**73.8**	12.6
Other	**14.9**	16.4
	$173.5	$117.6

Energy marketing revenues were higher due to an increase in the volume of electric power and natural gas sales by the energy marketing subsidiary. The subsidiary meets these sales commitments through spot market purchases and short-term purchase contracts. (See "Other Operation and Cost of Non-Utility Energy"). Revenues at the environmental and engineering services business were lower in 1996 due to a softening market for environmental services.

In addition to the revenues of the nonregulated businesses, other revenues also include the water operations of WP&L. These revenues were $4.2 million in both 1996 and 1995.

Other Operation and Cost of Non-Utility Energy

Other operation and cost of non-utility energy expense includes expenses related to WP&L, the parent company and the nonregulated businesses of HDC. The distribution of other operations expense was as follows:

	1996	1995
WP&L	$140.3	$139.3
Nonregulated businesses and parent company operations	177.3	113.4
	$317.6	$252.7

The increase in operations expense associated with the nonregulated businesses is primarily a result of increased volume at the energy marketing subsidiary. Several commitments made in early 1996 resulted in substantial losses. On a comparative basis, the non-utility energy marketing business incurred net losses of 17 cents per share in 1996 and 3 cents per share in 1995.

The environmental and engineering services business also incurred higher contract related costs which were partially offset by labor and benefit savings. The environmental and engineering services business lost 4 cents per share in 1996 as compared to a 7 cent per share contribution in 1995.

Operating expenses in the affordable housing business were significantly reduced in 1996 as operations support was outsourced and development activity was curtailed. After adjusting for the tax benefits and credits associated with this business, the affordable housing business contributed approximately 8 cents per share in 1996 including 2 cents per share related to the sale of two properties. In 1995, the affordable housing business contributed 4 cents per share.

Maintenance

Maintenance expense increased due to higher plant maintenance and the extended 1996 refueling outage at Kewaunee (See "Liquidity and Capital Resources — Capital Requirements" below).

Depreciation and Amortization

Depreciation and amortization expense increased $4.4 million as a result of property additions and greater amortization of contributions in aid of construction (a reduction of expense) in 1995.

Interest Expense and Other

The $9.1 million increase in other income is the result of two significant gains recognized in 1996. The sale of a combustion turbine by WP&L resulted in other income of $5.7 million. In addition, HDC recognized a gain of $4.2 million on the sale of its investment in assisted living properties. Interest expense was lower in 1996 as compared to 1995 as a result of less short-term debt outstanding and a slight decrease in interest rates.

Income Taxes

Income taxes increased for 1996 as a result of higher taxable income. The effective tax rate on continuing operations was 35.4% and 32.5% for 1996 and 1995, respectively. The lower rate in 1995 was the result of prior years' tax contingencies resolved favorably in 1995 and increased non-deductible Merger expenses in 1996.

PRO FORMA EARNINGS PER SHARE INFORMATION AND HISTORICAL IES AND IPC DATA

Set forth below is information regarding pro forma earnings per share (basic and diluted) of the Merged Company and certain historical financial information regarding IES and IPC for the years ended December 31, 1997, 1996 and 1995.

1997 versus 1996

The earnings per average common share for the Merged Company on a pro forma basis and for each of WPLH, IES and IPC for the years ended December 31, 1997 and 1996 were as follows:

	1997	1996
Merged Company pro forma combined*	**$2.02**	$2.10
WPLH	**1.99**	2.34
IES	**2.18**	2.04
IPC	**2.74**	2.69

The growth in IES's earnings per share in 1997 as compared with 1996 was primarily the result of: a 3.8% increase in electric sales (excluding off-system sales), a lower effective income tax rate, and increased operating income from IES's non-utility operations. The increased earnings were partially offset by higher interest expense, higher utility operating expenses, and start-up expenses in international and domestic growth areas. Expenses incurred defending an unsuccessful hostile takeover bid for IES reduced 1996 earnings per share by 15 cents.

The growth in IPC's earnings per share in 1997 as compared with 1996 was primarily the result of: electric and gas rate increases, a favorable court ruling regarding the recovery of manufactured gas plant costs (see "Liquidity and Capital Resources — Rates and Regulatory Matters"), and the continued control of operation and maintenance costs. Partially offsetting the increase in earnings were slightly depressed sales due to milder weather and the loss of eight municipal customers to other energy suppliers.

1996 versus 1995

The earnings per average common share for the Merged Company on a pro forma basis and for each of WPLH, IES and IPC for the years ended December 31, 1996 and 1995 were as follows:

	1996	1995
Merged Company pro forma combined*	$2.10	$1.98
WPLH	2.34	1.90
IES	2.04	2.20
IPC	2.69	2.63

The decrease in IES's earnings was primarily due to costs incurred in 1996 defending an unsuccessful takeover bid for IES which decreased earnings per share by 15 cents. Increased sales, electric and gas ratc increases, and continuing efforts to control costs contributed to the increased earnings for IPC.

* The pro forma earnings per share reflect the impact of the discontinued operations recorded by WPLH in 1996 and 1995. For additional information regarding the derivation of the pro forma earnings per share data, see "Interstate Energy Corporation Unaudited Pro Forma Combined Financial Statements" included elsewhere in this Annual Report.

LIQUIDITY AND CAPITAL RESOURCES

Historical WPLH Analysis

Cash flows from operating activities at WPLH decreased to $151 million in 1997 compared with $191 million in 1996 primarily due to a reduction in net income and working capital. Cash flows used for financing were $2.2 million in 1997 as compared to $72.4 million in 1996 resulting from a net increase in the amount of debt outstanding. Cash flows used for financing activities increased to $72.4 million in 1996 from $31.0 million in 1995 due to the net change in short-term debt. Cash flows used for investing activities were significantly lower in 1996 as compared with 1997 and 1995 due to the proceeds received in 1996 from both the sale of other property and equipment and the sale of a subsidiary and investments. Times interest earned before income taxes for WPLH for 1997, 1996 and 1995 was 3.19, 3.82 and 3.55, respectively.

Prospective Considerations

The capital requirements of the Merged Company will be primarily attributable to its utility subsidiaries' construction and acquisition programs, its debt maturities and business opportunities of New Diversified. The Merged Company anticipates that future capital requirements will be met by cash generated from operations and external financing. The level of cash generated from operations is partially dependent upon economic conditions, legislative activities, environmental matters and timely regulatory recovery of utility costs. The Merged Company's liquidity and capital resources will be affected by costs associated with cnvironmental and regulatory issues. Emerging competition in the utility industry could also impact the Merged Company's liquidity and capital resources, as discussed previously in the "Utility Industry Outlook" section.

The Merged Company has interests in the international arena. At December 31, 1997, IES had approximately $57 million of investments in foreign entities. At December 31, 1997, WPLH and IPC did not have material foreign investments. The Merged Company continues to explore additional international investment opportunities. Such investments may carry a higher level of risk than the Merged Company's traditional domestic utility investments or New Diversified's domestic investments. Such risks could include foreign government actions, foreign economic and currency risks and others.

The Merged Company is engaged in pursuing various potential business development opportunities, including international as well as domestic investments, and is devoting resources to such efforts. The Merged Company is striving to select investments where the international and other risks are both understood and manageable.

At December 31, 1997, IES and IPC had investments in the stock of McLeodUSA Inc. (McLeod), a telecommunications company, valued at $327 million and $1.4 million (as compared to a cost basis of $29 million and $0.1 million), respectively. Pursuant to the applicable accounting rules, the carrying value of the investments are adjusted to the estimated fair value each quarter based on the closing price at the end of the quarter. The adjustments do not impact earnings as the unrealized gains or losses, net of taxes, are recorded directly to the common equity section of the balance sheet. In addition, any such gains or losses are reflected in current earnings only at the time they are realized through a sale. IES and IPC have entered into agreements with McLeod which restricts the sale or disposal of its shares without the consent of the McLeod Board of Directors until September and June 1998, respectively.

The Merged Company had certain financial guarantees and commitments outstanding at December 31, 1997 which are not reflected in the pro forma consolidated financial statements. They generally consist of third-party borrowing arrangements and lending commitments as well as guarantees of financial performance of syndicated affordable housing properties. Management believes the possibility of the Merged Company having to make any material cash paymcnts under these agreements is remote.

Financing and Capital Structure

Access to the long-term and short-term capital and credit markets, and costs of external financing, are dependent on creditworthiness. The debt ratings of the Merged Company and certain subsidiaries are as follows:

		Moody's (As of 3/26/98)	Standard & Poor's (As of 3/2/98)
IESU	• Secured long-term debt	A2	A+
	• Corporate credit rating (a)	N/A	A+
	• Unsecured long-term debt	A3	A
WP&L	• Secured long-term debt	Aa2	AA
	• Corporate credit rating (a)	N/A	AA-
	• Unsecured long-term debt	Aa3	A+
IPC	• Secured long-term debt	A1	A+
	• Corporate credit rating	N/A	A+
	• Unsecured long-term debt	A2	A
New Diversified	• Commercial paper	P2	A1
Merged Company	• Corporate credit rating (a)	N/A	A+
	• Commercial paper (b)	P1	A1

(a) The "Corporate credit rating" is the overall rating of the parent company and is used by Standard & Poor's but not by Moody's.

(b) Upon consummation of the Merger, IESU, WP&L and IPC will participate in a utility money pool which will be funded, as needed, by the Merged Company through the issuance of commercial paper. This utility money pool replaces the commercial paper programs previously held at IESU, WP&L and IPC.

The following material long-term debt financing activities involving subsidiaries of the Merged Company took place in 1997 —

- On April 28, 1997, WP&L entered into an interest rate forward contract to hedge interest rate risk related to the anticipated issuance of $105 million of long-term debt securities. The securities were issued on June 30, 1997 (7.00% interest rate, maturing in 2007) and the forward contract was settled which resulted in a cash payment of $3.8 million by WP&L. This payment is being recognized as an adjustment to interest expense over the life of the new debt securities to approximate the interest rate implicit in the forward contract.

- WP&L utilized the net proceeds from the issuance of the $105 million of debt securities described above to repay maturing short-term debt, finance utility construction expenditures and to repay at maturity $55 million of WP&L's First Mortgage Bonds, Series Z, 6.125%.

- In October 1997, Diversified entered into a 3-Year Credit Agreement with various banking institutions which replaced its variable rate credit facility. The agreement extends through October 2000, with one-year extensions available upon agreement by the parties. Unused borrowing availability under this agreement is also used to support Diversified's commercial paper program. A combined maximum of $450 million of borrowings under this agreement and the commercial paper program may be outstanding at any one time. Interest rates and maturities are set at the time of borrowing. The rates are based upon quoted market prices and the maturities are less than one year. At December 31, 1997, Diversified had $182 million of borrowings outstanding under this facility with interest rates ranging from 6.05%-7.30%. New Diversified intends to continue borrowing under the renewal options of this facility and no conditions exist at December 31, 1997 that would prevent such borrowings. Accordingly, this debt is classified as long-term. In addition, Diversified also entered into a $150 million 364-Day Credit Agreement as discussed later.

- In August 1997, IESU issued $135 million of 6.625% Senior Debentures, due 2009. The proceeds from these debentures were used to reduce IESU's short-term borrowings.

- IESU repaid at maturity $8 million of 6.125% First Mortgage Bonds during the second quarter of 1997.

- Also in the second quarter of 1997, IESU issued $55 million of Collateral Trust Bonds, 6.875%, due 2007. Holders thereof may elect to have their Collateral Trust Bonds redeemed, in whole but not in part, on May 1, 2002, at 100% of the principal amount thereof, plus accrued interest. The proceeds from the Collateral Trust Bonds were used to refinance $15 million of Series L, 7.875% First Mortgage Bonds, $30 million of Series M, 7.625% First Mortgage Bonds and $10 million of 7.375% First Mortgage Bonds.

- IPC repaid at maturity $17 million of 6.125% First Mortgage Bonds in May 1997.

Other than the Merged Company's periodic sinking fund requirements, which will not require additional cash expenditures, the following long-term debt (in millions) will mature prior to December 31, 2002:

IESU	$185.1
IPC	8.1
WP&L	10.8
New Diversified	207.6
Merged Company	$411.6

Depending upon market conditions, it is currently anticipated that a majority of the maturing debt will be refinanced with the issuance of long-term securities.

IESU, IPC and WP&L currently have no authority from their applicable federal/state regulatory commissions or the Securities and Exchange Commission (SEC) to issue additional long-term debt. The companies are evaluating their future financing needs and will make the necessary regulatory filings as needed.

Under the most restrictive terms of their respective indentures, WP&L, IESU and IPC could have issued at least $276 million, $234 million and $200 million of long-term debt at December 31, 1997, respectively.

The various charter provisions of the subsidiaries of the Merged Company authorize and limit the aggregate amount of additional shares of Cumulative Preferred Stock and Cumulative Preference Stock that may be issued. At December 31, 1997, the companies could have issued the following additional shares of Cumulative Preferred or Preference Stock:

	IESU	IPC	WP&L	IES
Cumulative Preferred	—	1,238,619	2,700,775	5,000,000
Cumulative Preference	700,000	2,000,000	—	—

The capitalization ratios of WPLH, IES and IPC at year-end were as follows:

	Pro Forma Combined	WPLH		IES		IPC	
	1997	1997	1996	1997	1996	1997	1996
Common equity	**51%**	**54%**	59%	**49%**	47%	**52%**	50%
Preferred stock	**3**	**5**	6	**1**	1	**8**	8
Long-term debt	**46**	**41**	35	**50**	52	**40**	42
	100%	**100%**	100%	**100%**	100%	**100%**	100%

For interim financing, WP&L, IESU and IPC are authorized by the applicable federal or state regulatory agency to issue short-term debt as follows (in millions) at December 31, 1997:

	WP&L	IESU	IPC
Regulatory authorization	$138	$200	$75
Short-term debt outstanding	$ 81	—	$34

WPLH also had $42 million of short-term debt outstanding at December 31, 1997. In addition to providing for ongoing working capital needs, this availability of short-term financing provides the companies flexibility in the issuance of long-term securities. The level of short-term borrowing fluctuates based on seasonal corporate needs, the timing of long-term financing, and capital market conditions. To maintain flexibility in its capital structure and to take advantage of favorable short-term rates, WP&L and IESU also use proceeds from the sale of accounts receivable and unbilled revenues to finance a portion of their long-term cash needs. The Merged Company anticipates that short-term debt will continue to be available at reasonable costs due to current ratings by independent utility analysts and rating services.

WPLH, IES and IPC had the following bank lines of credit (in millions) at December 31, 1997 available to support its borrowings:

	WPLH	IES	IPC
Bank lines of credit	$170	$ 45	$53
Amount utilized	—	$ 11	$34

Commitment fees are paid to maintain these lines and there are no conditions which restrict the unused lines of credit. From time to time, the Merged Company may borrow from banks and other financial institutions in lieu of commercial paper, and has agreements with several financial institutions for such borrowings. There are no commitment fees associated with these agreements and there were no borrowings outstanding under these agreements at December 31, 1997.

In October 1997, Diversified entered into a 364-Day Credit Agreement with various banking institutions. The agreement extends through October 20, 1998, with 364 day extensions available upon agreement by the parties. The unborrowed portion of this agreement is also used to support Diversified's commercial paper program. A combined maximum of $150 million of borrowings under this agreement and the commercial paper program may be outstanding at any one time. Interest rates and maturities are set at the time of borrowing. The rates are based upon quoted market prices and the maturities are less than one year. There were no borrowings under this facility at December 31, 1997.

Given the above financing flexibility available to the Merged Company, management believes it has the necessary financing capabilities in place to adequately finance its capital requirements for the foreseeable future.

Capital Requirements

General

Capital expenditure and investment and financing plans are subject to continual review and change. The capital expenditure and investment programs may be revised significantly as a result of many considerations, including changes in economic conditions, variations in actual sales and load growth compared to forecasts, requirements of environmental, nuclear and other regulatory authorities, acquisition and business combination opportunities, the availability of alternate energy and purchased power sources, the ability to obtain adequate and timely rate relief, escalations in construction costs and conservation and energy efficiency programs.

The Merged Company's anticipated construction and acquisition expenditures for 1998 are estimated to be approximately $630 million, consisting of approximately $277 million in its utility operations, $190 million for energy-related international investments and $163 million for new business development initiatives at New Diversified. The level of 1998 domestic and international investments could vary significantly from the estimates noted here dependent on actual investment opportunities as well as the timing of the opportunities. The Merged Company estimates it will spend approximately $1.2 billion on utility construction and acquisition expenditures during 1999-2002. The strategy related to the construction and acquisition program for New Diversified during 1999-2002 is currently being finalized. New Diversified expects to invest in energy products and services in domestic and international markets, industrial services initiatives and other strategic initiatives.

One of the Merged Company's objectives is to finance utility construction expenditures through internally generated funds supplemented, when required, by outside financing. The Merged Company anticipates funding the large majority of its utility construction expenditures during 1998-2002 through internally generated funds, supplemented by external financings as needed. Funding of a majority of the New Diversified construction and acquisition expenditures is expected to be completed with external financings.

Nuclear Facilities

The Merged Company owns interests in two nuclear facilities, Kewaunee and the Duane Arnold Energy Center (DAEC). Set forth below is a discussion of certain matters impacting these facilities.

Kewaunee, a 535-megawatt (nameplate capacity) pressurized water reactor plant, is operated by Wisconsin Public Service Corporation (WPSC) and is jointly owned by WPSC (41.2%), WP&L (41.0%), and Madison Gas & Electric Company (MG&E) (17.8%). The Kewaunee operating license expires in 2013.

Kewaunee returned to service on June 12, 1997 after having been out of service since September 21, 1996 for refueling, routine maintenance, and repair of the two steam generators. The original Kewaunee steam generator tubes are susceptible to corrosion. Tubes are repaired by inserting sleeves (tubes within tubes) in the original steam generator tubes. The most recent repair was undertaken when previously repaired tubes failed. The repair consisted of removing old sleeves and inserting new slightly longer sleeves which cover the areas of concern in the original steam generator tubes. The new sleeves will be inspected during the next refueling and maintenance outage which is scheduled for the Fall of 1998. As of this filing, Kewaunee had remained in continuous operation since the plant was returned to service with the exception of a one-week outage for replacement of a reactor coolant pump seal. Kewaunee is operating at 97% of rated capacity because certain steam generator tubes have been removed from service rather than repaired.

In accordance with the PSCW authorization, WP&L had deferred $3.1 million at December 31, 1997, associated with Kewaunee steam generator repair costs. In March 1998, the PSCW approved recovery of these costs through a customer surcharge effective April 1, 1998 through May 31, 1998.

The total cost of replacing the two steam generators would be approximately $89.0 million of which WP&L's share would be $36.5 million. Because of work already completed, the elapsed time from placing a firm order for steam generators to receiving delivery has been shortened to approximately 22 months.

The owners of Kewaunee have differing views on the desirability of proceeding with the steam generator replacement project. Although the new resleeving repair technology may allow the plant to remain in service for an extended period of time, WPSC favors replacement at the earliest possible date because of reliability and cost concerns related to steam generator repairs. WP&L and MG&E have been unwilling to support replacement. In March 1996, WPSC filed an application with the PSCW for permission to replace the Kewaunee steam generators. This application was approved in April 1998. The issues related to the continued operation and future ownership still need to be resolved before steam generator replacement can proceed. The joint owners continue to analyze and discuss other options related to the future of Kewaunee including various ownership transfer alternatives. If it should become necessary to retire Kewaunee permanently, WP&L would replace the Kewaunee generation through a combination of purchased power, increased generation at existing WP&L generating units and new generating unit additions, if necessary.

The PSCW has directed the owners of Kewaunee to develop depreciation and decommissioning cost levels based on an expected plant end-of-life of 2002 versus a license end-of-life of 2013. This was prompted by the uncertainty regarding the expected useful life of the plant without steam generator replacement. At December 31, 1997, the net carrying amount of WP&L's investment in Kewaunee was approximately $45.7 million. The current cost of WP&L's share of the estimated costs to decommission Kewaunee is $181.3 million and exceeds the trust assets at December 31, 1997 by $68.9 million. The costs of decommissioning are assumed to escalate at an annual rate of 5.83%. WP&L's retail customers in the Wisconsin jurisdiction are responsible for approximately 80% of WP&L's share of Kewaunee costs.

As a result of accelerating the recovery of WP&L's share of Kewaunee related costs, depreciation expense and decommissioning funding will increase approximately $3.0 million (from $4.8 million to $7.8 million) and $5.4 million (from $10.7 million to $16.1 million), respectively, on an annualized basis. During 1997, $6.5 million of depreciation expense related to unrecovered plant investment was recognized compared to $4.8 million which was recognized in 1996. During 1997, decommissioning expensc associated with funding increased to $14.3 million from $10.7 million in 1996. The $14.3 million represents a combination of the annual funding levels in accordance with UR-109 through April 29, 1997 and UR-110 post-April 29, 1997. Customer rates, which became effective in Wisconsin on April 29, 1997, are designed to recover the accelerated Kewaunee depreciation and decommissioning costs.

DAEC, a 520-megawatt boiling water reactor plant, is operated by IESU and IESU has a 70% ownership interest in the plant. The DAEC operating license expires in 2014. Pursuant to the most recent electric rate case order, the IUB allows IESU to recover $6.0 million annually for the cost to decommission the DAEC. The current recovery figures are based on an assumed cost to decommission the DAEC of $252.8 million, which is IESU's 70% portion in 1993 dollars, based on the Nuclear Regulatory Commission (NRC) minimum formula (which exceeds the amount in the current site-specific study completed in 1994). At December 31, 1997, IESU had $77.9 million invested in external decommissioning trust funds and also had an internal decommissioning reserve of $21.7 million recorded as accumulated depreciation.

Refer to the "Other Matters — Environmental" section for a discussion of various issues impacting the Merged Company's future capital requirements.

Rates and Regulatory Matters

In November 1997, as part of its merger approval, FERC accepted a proposal by IESU, WP&L, and IPC, which provides for a four-year freeze on wholesale electric prices beginning with the effective date of the Merger.

WP&L

In connection with its approval of the Merger, the PSCW accepted a WP&L proposal to freeze rates for four years following the date of the Merger. A re-opening of an investigation into WP&L's rates during the rate freeze period, for both cost increases and decreases, may occur only for single events that are not Merger-related and have a revenue requirement impact of $4.5 million or more.

In rate order UR-110, the PSCW approved new rates effective April 29, 1997 through 1998. On average, WP&L's retail electric rates declined by 2.4% and retail gas rates declined by 2.2%. Other items included in the rate order were: authorization of a surcharge to collect replacement power costs while Kewaunee remained out of service for the period effective April 29, 1997 through July 1, 1997; authorization of an increase in the return on equity to 11.7% from 11.5%; reinstatement of the electric fuel adjustment clause; continuation of a modified gas performance based ratemaking incentive mechanism; and a modified SO2 incentive. In addition, the PSCW ordered that it must approve the payment of dividends by WP&L to its parent company that are in excess of the level forecasted in the rate order ($58.3 million), if such dividends would reduce WP&L's average common equity ratio below 52.00% of total capitalization. Based on a 13-month average for 1997, WP&L's common equity ratio was 52.56%.

The retail electric rates are based in part on forecasted fuel and purchase power costs. Under PSCW rules, Wisconsin utilities can seek emergency rate increases if these costs are more than three percent higher than the estimated costs used to establish rates. In WP&L's case, actual fuel costs since May 1997 have been higher than estimated and are expected to remain well above the estimated levels in 1998. As a result, WP&L has asked the PSCW to approve a rate increase. It is expected that the PSCW will issue a decision in the second quarter of 1998. Any increase approved by the PSCW will be implemented on a prospective basis.

The gas performance incentive was modified to eliminate the maximum gain or loss to be recognized by WP&L. Previously, this incentive was limited to $1.1 million to WP&L. The incentive includes a sharing mechanism, whereby 40% of all gains and losses relative to current commodity prices as well as other benchmarks are recognized by WP&L rather than refunded to or recovered from customers.

IESU

In September 1997, IESU agreed with the IUB to provide Iowa customers a four-year retail electric and gas price freeze commencing on the effective date of the Merger. The agreement excluded price changes due to government-mandated programs, such as energy efficiency cost recovery or unforeseen dramatic changes in operations. In addition, the price freeze does not preclude a review by either the IUB or Office of Consumer Advocate (OCA) into whether IESU is exceeding a reasonable return on common equity.

Under provisions of the IUB rules, IESU is currently recovering the costs it has incurred for its energy efficiency programs. There have been several cost recovery filings made and approved by the IUB over the course of the last few years. Generally, the costs incurred through July 1997 are being recovered over various four-year periods. The IUB commenced a rulemaking in January 1997 to implement statutory changes allowing concurrent recovery and a final order in this proceeding was issued in April 1997. The new rules allowed IESU to begin concurrent recovery of its prospective expenditures on August 1, 1997. The implementation of these changes will gradually eliminate the regulatory asset that was created under the prior rate making mechanism as these costs are recovered.

IESU has the following amounts of energy efficiency costs included in regulatory assets on its Consolidated Balance Sheets (in thousands):

	Four-Year Recovery Begiuuiug	December 31, 1997	December 31, 1996
Costs incurred through 1993	6/95	**$ 7,779**	$12,834
Costs incurred in 1994-1995	8/97	**30,924**	33,161
Costs incurred from 1/96-7/97	8/97	**19,847**	15,087
Under collection of concurrent recovery	N/A	**850**	—
		$59,400	$61,082

IPC

In September 1997, IPC agreed with the IUB to provide Iowa customers a four-year retail electric and gas price freeze commencing on the effective date of the Merger. The agreement excluded price changes due to government-mandated programs, such as energy efficiency cost recovery, or unforeseen dramatic changes in operations. In addition, the price freeze does not preclude a review by either the IUB or OCA into whcther IPC is exceeding a reasonable return on common equity. IPC also agreed with the MPUC and Illinois Commerce Commission to four-year and three-year rate freezes, respectively, commencing on the effective date of the Merger.

On September 30, 1997, the IUB approved a settlement between IPC and the OCA which provided for an electric rate reduction of approximately $3.2 million annually. The reduction applied to all bills rendered on and after October 7, 1997.

In May 1995, IPC filed an application with the MPUC for an increase in gas rates in an annual amount of $2.4 million. Incrcased interim rates in an annual amount of $1.5 million were placed in effect in June 1995. On February 29, 1996, MPUC issued an order allowing an increase in gas rates of $2.1 million. Rates reflecting the increase were implemented in September 1996. The Department of Public Service and the Office of Attorney General appealed the MPUC's decision. The appeal was denied by the Minnesota Court of Appeals on February 18, 1997. On March 21, 1997, the Department of Public Service and the Office of Attorney General appealed the decision of the Court of Appeals (and the MPUC) to the Minnesota Supreme Court. On January 8, 1998, the

Minnesota Supreme Court upheld the MPUC's initial decision allowing IPC to recover $4.9 million of manufactured gas plant clean-up expenses over a 10 year period.

IPC is also recovering its energy efficiency costs in Iowa in a similar manner as IESU and began its concurrent cost recovery in October 1997. IPC has the following amounts of energy efficiency costs to be recovered in Iowa included in regulatory assets on its Balance Sheets (in thousands):

	Four-Year Recovery Beginning	December 31, 1997	December 31, 1996
Costs incurred through 1992	10/94	**$ 912**	$ 2,128
Costs incurred in 1993-1995	5/97	**16,576**	19,193
Costs incurred from 1/96-9/97	10/97	**9,796**	6,042
		$27,284	$27,363

In addition, IPC had $2.7 million and $2.5 million at December 31, 1997 and December 31, 1996, respectively, included in regulatory assets for energy efficiency recoveries in Minnesota.

Assuming capture of the Merger-related synergies described under the caption "Merger" above and no significant legislative or regulatory changes affecting its utility subsidiaries, the Merged Company does not expect the Merger-related electric and gas price freezes to have a material adverse effect on its financial position or results of operations.

OTHER MATTERS

Year 2000

The Merged Company utilizes software, embedded systems and related technologies throughout its businesses that will be affected by the date change in the Year 2000. An internal task force has been assembled to review and develop the full scope, work plan and cost estimates to ensure that the Merged Company's systems continue to meet its internal and customer needs.

Phase I of the project, which encompassed a review of the necessary software modifications that will need to be made to the Merged Company's financial and customer systems, has been completed. The Merged Company currently estimates that the remaining costs to be incurred on this phase of the project will be approximately $4 million to $8 million in the aggregate.

The task force has also begun Phase II of the project which is an extensive review of the Merged Company's embedded systems for Year 2000 conversion issues. The task force has inventoried critical embedded operating systems and is working with the system vendors to ascertain Year 2000 compliance of these systems. The task force is also developing detailed plans for testing and remediating critical systems (i.e., systems whose failure could affect employee safety or business operations).

As part of an awareness effort, the Merged Company has also notified its utility customers of its Year 2000 project efforts. Key suppliers are also being contacted to confirm their Year 2000 readiness plans. Efforts are also underway to develop contingency plans for critical embedded operating systems. The Merged Company is currently unable to estimate the costs to be incurred on this phase of the project but does believe that the costs will be significant. An estimate of the expenses to be incurred on this phase of the project is expected to be available by the third quarter of 1998.

The goal of the Merged Company is to have all the material Year 2000 conversions made sufficiently in advance of December 31, 1999 to allow for unanticipated issues. At this time, management is unable to determine if the Year 2000 issue will have a material adverse effect on the Merged Company's financial position or results of operations.

In April 1998, WP&L filed a request with the PSCW requesting deferral treatment of Year 2000 costs in excess of $4.5 million. Currently, management cannot predict the action the PSCW may take regarding this request.

Labor Issues

The status of the collective bargaining agreements at each of the utilities is as follows:

	IESU	WP&L	IPC
Number of collective bargaining agreements	6	1	3
Percentage of workforce covered by agreements	53	69	64

There are two agreements at IESU expiring in 1998 and the number of employees covered under these agreements is relatively small.

Financial Instruments

WPLH has historically had only limited involvement with derivative financial instruments and has not used them for trading purposes. They have been used to manage well-defined interest rate and commodity price risks. WP&L historically has entered into interest rate swap agreements to reduce the impact of changes in interest rates on its floating-rate long-term debt, short-term debt and the sales of its accounts receivable. The total notional amount of interest rate swaps outstanding was $40 million at December 31, 1997. WPLH has used swaps, futures and options to hedge the price risks associated with the purchase and sale of stored gas at WP&L and with the purchases and sales of gas and electric power at the energy marketing subsidiary. On April 28, 1997, WP&L entered into an interest rate forward contract to hedge interest rate risk related to the anticipated issuance of $105 million of long-term debt securities. See Note 8 of the "Notes to Consolidated Financial Statements" for additional information.

IES historically had a policy that derivative financial instruments were to be used only to mitigate business risks and not for speculative purposes. Derivatives were used on a very limited basis. At December 31, 1997, IES did not have any material derivatives outstanding. IPC had no derivatives outstanding at December 31, 1997. The Merged Company is in the process of developing its policy for the use of derivative financial instruments.

Accounting Pronouncements

Statement of Financial Accounting Standards No. 130 (SFAS 130), Reporting Comprehensive Income, was issued by the Financial Accounting Standards Board (FASB) in the second quarter of 1997. SFAS 130 establishes standards for reporting of comprehensive income and its components in a full set of general purpose financial statements. SFAS 130 will require reporting a total for comprehensive income which includes: (a) unrealized holding gains/losses on securities classified as available-for-sale under SFAS 115, (b) foreign currency translation adjustments accounted for under SFAS 52, and (c) minimum pension liability adjustments made pursuant to SFAS 87. SFAS 130 is effective for periods beginning after December 15, 1997.

Statement of Financial Accounting Standards No. 131 (SFAS 131), Disclosures About Segments of an Enterprise and Related Information, was issued by the FASB in the second quarter of 1997. SFAS 131 requires disclosures for each business segment in a manner consistent with how management disaggregates and evaluates the company, with the addition of quarterly disclosure requirements and a finer partitioning of geographic disclosures. SFAS 131 is effective for periods beginning after December 15, 1997.

Accounting for Obligatious Associated witb tbe Retirement of Long-Lived Assets

The staff of the Securities and Exchange Commission has questioned certain of the current accounting practices of the electric utility industry, including IESU and WP&L, regarding the recognition, measurement and classification of decommissioning costs for nuclear generating stations in financial statements of electric utilities. In response to these questions, the FASB is reviewing the accounting for closure and removal costs, including decommissioning of nuclear power plants. If current electric utility industry accounting practices for nuclear power plant decommissioning are changed, the annual provision for decommissioning could increase relative to 1997, and the estimated cost for decommissioning could be recorded as a liability (rather than as accumulated depreciation), with recognition of an increase in the cost of the related nuclear power plant. Assuming no significant regulatory shift, IESU and WP&L do not believe that such changes, if required, would have an adverse effect on its financial position or results of operations due to its ability to recover decommissioning costs through rates.

Inflation

The Merged Company does not expect the effects of inflation at current levels to have a significant effect on its financial position or results of operations.

Environmental

The pollution abatement programs of IESU, IPC, WP&L and New Diversified are subject to continuing review and are revised from time to time due to changes in environmental regulations, changes in construction plans and escalation of construetion costs. While the Merged Company cannot precisely forecast the effect of future environmental regulations on its operations, it has taken steps to anticipate the future while also meeting the requirements of current environmental regulations.

IESU, IPC and WP&L all have current or previous ownership interests in properties previously associated with the production of gas at manufactured gas plants (MGP) for which they may be liable for investigation, remediation and monitoring costs relating to the sites. A summary of information relating to the sites is as follows:

	IESU	IPC	WP&L
Number of known sites for which liability may exist	34	9	14
Liability rccorded at December 31, 1997 (millions)	$33.2	$5.8	$ 9.2
Regulatory asset recorded at December 31, 1997 (millions)	$33.2	$6.2	$16.3

The companies are working pursuant to the requirements of various federal and state agencies to investigate, mitigate, prevent and remediate, where necessary, the environmental impacts to property, including natural resources, at and around the sites in order to protect public health and the environment. The companies each believe that they have completed the remediation at various sites, although they are still in the process of obtaining final approval from the applicable environmental agencies for some of these sites.

Each company has recorded environmental liabilities related to the MGP sites; such amounts are based on the best current estimate of the amount to be incurred for investigation, remediation and monitoring costs for those sites where the investigation process has been or is substantially completed, and the minimum of the estimated cost range for those sites where the investigation is in its earlier stages. The Merged Company currently estimates the range of costs to be incurred for the investigation, remediation and monitoring of the sites to be approximately $36 million to $83 million. It is possible that future cost estimates will be greater than the current estimates as the investigation process proceeds and as additional facts become known.

WP&L completed a comprehensive review of its MGP liability in the third quarter of 1997. This review resulted in a $65 million reduction in the recorded MGP liability, largely due to the approval by the Wisconsin Department of Natural Resources (WDNR) of less costly containment and control strategies as an alternative to excavation processes at various sites. See Note 11 c. of the "Notes to Consolidated Financial Statements" for additional information.

Under the current rate making treatment approved by the PSCW, the MGP expenditures, net of any insurance proceeds, are deferred and collected from gas customers over a five-year period after new rates are implemented. The MPUC also allows the deferral of MGP-related costs applicable to the Minnesota sites and IPC has been successful in obtaining approval to recover such costs in rates in Minnesota. While the IUB does not allow for the deferral of MGP-related costs, it has permitted utilities to recover its prudently incurred costs. As a result, regulatory assets have been recorded by each company which reflect the probable future rate recovery, where applicable. Considering the current rate treatment, and assuming no material change therein, each of IESU, IPC and WP&L believes that the clean-up costs incurred for these MGP sites will not have a material adverse effect on their respective financial positions or results of operations.

In April 1996, IESU filed a lawsuit against certain of its insurance carriers seeking reimbursement for its MGP-related costs. Settlement discussions are proceeding with its insurance carriers regarding the recovery of these costs. Settlement has been reached with sixteen carriers. In 1994, IPC filed a lawsuit against certain of its insurance carriers to recover its MGP-related costs. Settlements have been reached with eight carriers. Both companies are continuing their pursuit of additional recoveries. Amounts received from insurance carriers are being deferred by IESU and IPC pending a determination of the regulatory treatment of such recoveries. WP&L has settled with twelve carriers and is also continuing to pursue additional recoveries from other carriers. The three companies are unable to predict the amount of any additional insurance recoveries they may realize.

The Clean Air Act Amendments of 1990 (Act) require emission reductions of sulfur dioxide (SO2), nitrogen oxides (NOx) and other air pollutants to achieve reductions of atmospheric chemicals believed to cause acid rain. IESU, IPC and WP&L have met the provisions of Phase I of the Act and are in the process of meeting the requirements of Phase II of the Act (effective in the year 2000). The Act also governs SO2 allowances, which are defined as an authorization for an owner to emit one ton of SO2 into the atmosphere. The companies are reviewing their options to ensure they will have sufficient allowances to offset their emissions in the future. The companies believe that the potential costs of complying with these provisions of Title IV of the Act will not have a material adverse impact on their financial position or results of operations.

The Act and other federal laws also require the United States Environmental Protection Agency (EPA) to study and regulate, if necessary, additional issues that potentially affect the electric utility industry, including emissions relating to ozone transport, mercury and particulate control as well as modifications to the Polychlorinated Biphenyl (PCB) rules. In July 1997, the EPA issued final rules that would tighten the National Ambient Air Quality Standards (NAAQS) for ozone and particulate matter emissions. IESU, IPC and WP&L are currently reviewing the rules to determine what impact they may have on their operations.

In October 1997, the EPA issued a proposed rule to require 22 states, including Wisconsin, to modify their State Implementation Plans (SIPs) to address the ozone transport issue. The proposed rule would require WP&L to reduce its NOx emissions at all of its plants to .15 lbs/mmbtu. WP&L cannot presently predict the final outcome of this proposal but believes that, under the terms of the proposed rule, it would be required to install controls at its plants and that the cost related thereto would be significant.

In 1995, the EPA published the Sulfur Dioxide Network Design Review for Cedar Rapids, Iowa, which, based on the EPA's assumptions and worst-case modeling method suggested that the Cedar Rapids area could be classified as "nonattainment" for the NAAQS standards established for SO2. The worst-case modeling suggested that two of IESU's generating facilities contributed to the modeled exceedences. As a result of exceedences at a monitor near one of IESU's generating facilities, the EPA issued a letter to the Iowa Governor's office directing the state to develop a plan of action. In this regard, IESU entered into a consent order with the Iowa Department of Natural Resources (IDNR) in the third quarter of 1997 on this issue. IESU agreed to limit the SO2 emissions from the two noted generating facilities and to install a new stack (potential aggregate capital cost of up to $2.5 million over the next two years) at one of the facilities. The IDNR approved the consent order in the fourth quarter of 1997 and it is expected to be approved by the EPA in the second quarter of 1998.

Pursuant to a routine internal review of documents, IESU determined that certain changes undertaken during previous years at one of its generating facilities may have required a federal Prevention of Significant Deterioration (PSD) permit. IESU initiated discussions with its regulators on the matter, resulting in the submittal of a PSD permit application in February 1997. IESU expects to receive the permit in the second quarter of 1998. IESU may be subject to a penalty for not having obtained the permit previously; howcver, IESU believes that any likely actions resulting from this matter will not have a material adverse effect on its financial position or results of operation..

Pursuant to a separate routine internal review of plant operations, IESU determined that certain permit limits were exceeded in 1997 at one of its generating facilities in Cedar Rapids. IESU has initiated discussions with its regulators on the matter and has proposed a compliance plan which contemplates operational changes. In addition, IESU will be submitting a PSD permit application in the second quarter of 1998. IESU may be subject to a penalty for exceeding permit limits established for this facility; however, management believes that any likely actions resulting from this matter will not have a material adverse effect on IESU's financial position or results of operations.

A global treaty has been negotiated that could require reductions of greenhouse gas emissions from utility plants. Negotiators left significant implementation and compliance questions open to resolution at meetings to be held starting in November 1998. At this time, the Merged Company is unable to predict whether Congress will ratify the treaty. Given the uncertainty of the treaty ratification and the ultimate terms of the final regulations, the Merged Company cannot currently estimate the impact the implementation of the treaty would have on its operations.

The Nuclear Waste Policy Act of 1982 (NWPA) assigned responsibility to the U.S. Department of Energy (DOE) to establish a facility for the ultimate disposition of high level waste and spent nuclear fuel and authorized the DOE to enter into contracts with parties for the disposal of such material beginning in January 1998. IESU and WP&L entered into such contracts and have made the agreed payments to the Nuclear Waste Fund (NWF) held by the U.S. Treasury. The companies were subsequently notified by the DOE that it was not able to begin acceptance of spent nuclear fuel by January 31, 1998. Furthermore, DOE has experienced significant delays in its efforts and material acceptance is now expected to occur no earlier than 2010 with the possibility of further delay being likely. IESU and WP&L are evaluating and pursuing multiple options, including litigation and legislation to protect its customers and its contractual and statutory rights that are diminished by delays in the DOE program.

The NWPA assigns responsibility for interim storage of spent nuclear fuel to generators of such spent nuclear fuel, such as IESU and WP&L. In accordance with this responsibility, IESU and WP&L have been storing spent nuclear fuel on site at DAEC and Kewaunee, respectively, since plant operations began. DAEC has current on-site capability to store spent fuel until 2001. IESU is currently reviewing its options to expand on-site storage capability. To provide assurance that both the operating and post-shutdown storage needs are satisfied, a combination of expanding the capacity of the existing fuel pool and construction of a dry cask modular facility are being contemplated. With minor modifications, Kewaunec would have sufficient fuel storage capacity to the end of the license life in 2013. Legislation is being considered on the federal level to provide for the establishment of an interim storage facility as early as 2002.

The Low-Level Radioactive Waste Policy Amendments Act of 1985 mandates that each state must take responsibility for the storage of low-level radioactive waste produced within its borders. The States of Iowa and Wisconsin are members of the six-state Midwest Interstate Low-Level Radioactive Waste Compact (Compact) which is responsible for development of any new disposal capability within the Compact member states. In June 1997, the Compact commissioners voted to discontinue work on a proposed waste disposal facility in the State of Ohio because the expected cost of such a facility was comparably higher than other options currently available. Dwindling waste volumes and continued access to existing disposal facilities were also reasons cited for the decision. A disposal facility located near Barnwell, South Carolina continues to accept the low-level waste and IESU and WP&L currently ship the waste each produces to such site, thereby minimizing the amount of low-level waste stored on-site. In addition, given technological advances, waste compaction and the reduction in the amount of waste generated, DAEC and Kewaunee each have on-site storage capability sufficient to store low-level waste expected to be generated over at least the next ten years, with continuing access to the Barnwell disposal facility extending that on-site storage capability indefinitely.

The National Energy Policy Act of 1992 requires owners of nuclear power plants to pay a special assessment into a "Uranium Enrichment Decontamination and Decommissioning Fund." The assessment is based upon prior nuclear fuel purchases. IESU is recovering the costs associated with this assessment through its electric fuel adjustment clauses over the period the costs are assessed. IESU's 70% share of the future assessment at December 31, 1997 was $8.9 million and has been recorded as a liability with a related regulatory asset for the unrecovered amount. WP&L is also recovering these costs from its customers and at December 31, 1997 had a regulatory asset and a liability of $5.9 million and $5.1 million recorded, respectively.

Whiting Petroleum Corporation (Whiting), a wholly-owned subsidiary of New Diversified, is responsible for certain dismantlement and abandonment costs related to various off-shore oil and gas platforms (and related on-shore plants and equipment), the most significant of which is located off the coast of California. Whiting estimates the total costs for these properties to be approximately $14 million and the expenditures are not expected to be incurred for approximately five years. Whiting accrues these costs as reserves are extracted, resulting in a recorded liability of $8.6 million at December 31, 1997.

Power Supply

The power supply concerns of 1997 have raised awareness of the electric system reliability challenges facing Wisconsin and the Midwest region. WP&L was among an 11-member group of Wisconsin energy suppliers that, on October 1, 1997, recommended to the Governor of Wisconsin a series of recommendations to improve electric reliability in the state. The recommendations included additional transmission system capacity to substantially increase Wisconsin's ability to import electricity from other states in the region and additional power plant capacity in eastern Wisconsin. As a result, WP&L and other Wisconsin-based utilities are advocating faster PSCW approval of needed transmission projects.

On September 24, 1997, the PSCW ordered WP&L and two other Wisconsin utilities to arrange for additional electric capacity to help maintain reliable service for their customers. In response to this order, WP&L has issued a Request for Proposal (RFP) for contracts to provide WP&L with an additional 150 megawatts of electric capacity beginning as early as June 1, 1999. WP&L anticipates its RFP will result in a purchased power arrangement with a contract period of three to eight years and contract extension or "rollover" options. WP&L expects to award the contract at the end of the second quarter of 1998.

Utility officials noted that it will take time to get new transmission and power plant projects approved and built. While utility officials fully expect to meet customer demands in 1998 and 1999, problems still could arise if there are unexpected power plant outages, transmission system outages or extended periods of extremely hot weather.

WPLH SELECTED CONSOLIDATED QUARTERLY FINANCIAL DATA (Unaudited)

The following unaudited consolidated quarterly data of WPLH, in the opinion of management, include adjustments which are normal and recurring in nature necessary for the fair presentation of the results of operations and financial position. WP&L's results of operations are a significant portion of the consolidated results. The quarterly amounts were affected by, among other items, WP&L's rate activities, seasonal weather conditions and changes in sales and operating expenses. Refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations" for a discussion of these items. Net income in both the first and second quarter of 1997 was lower than the first and second quarter of 1996 primarily due to lower electric and gas margins. The lower margins resulted from warmer weather and several temporary plant outages during the first five months of 1997. In addition, a $3.4 million after-tax gain was recognized on the sale of a combustion turbine in the second quarter of 1996.

	Operating Revenues	Operating Income	Net Income	Earnings per Share (basic and diluted)
	(in thousands except per share data)			
Quarter Ended				
1997:				
March 31	$261,688	$40,637	$21,827	$0.71
June 30	206,681	19,900	9,007	0.29
September 30	214,412	31,877	13,953	0.45
December 31	236,474	36,193	16,467	0.54
1996:				
March 31	$260,877	$54,012	$31,680	$1.03
June 30	208,293	30,361	16,539	0.54
September 30	212,263	28,417	12,596	0.41
December 31	251,411	30,260	11,093	0.36

WPLH REPORT ON THE FINANCIAL INFORMATION

WPL Holdings, Inc. management is responsible for the information and representations contained in the financial statements and in certain other sections of this Annual Report. The consolidated financial statements that follow have been prepared in accordance with generally accepted accounting principles. In addition to selecting appropriate accounting principles, management is responsible for the manner of presentation and for the reliability of the financial information. In fulfilling that responsibility, it is necessary for management to make estimates based on currently available information and judgments of current conditions and circumstances.

Through a well-developed system of internal controls, management seeks to ensure the integrity and objectivity of the financial information presented in this report. This system of internal control is designed to provide reasonable assurance that the assets of the company are safeguarded and that the transactions are executed according to management's authorizations and are recorded in accordance with the appropriate accounting principles.

The Board of Directors participates in the financial information reporting process through its Audit Committee.

Erroll B. Davis Jr.
President and Chief Executive Officer
WPL Holdings, Inc.

Edward M. Gleason
Vice President, Treasurer and Corporate Secretary
Principal Financial Officer
WPL Holdings, Inc.

January 30, 1998

WPL HOLDINGS, INC.

CONSOLIDATED STATEMENTS OF INCOME

	Year Ended December 31,		
	1997	1996	1995
	(in tbousands except for per share data)		
Operating revennes:			
Electric	**$634,143**	$589,482	$546,324
Gas	**155,883**	165,627	139,165
Fees, rents, non-utility energy sales and other	**129,229**	177,735	121,766
	919,255	932,844	807,255
Operating expenses:			
Electric production fuels	**116,812**	114,470	116,488
Purchased power	**125,438**	81,108	44,940
Purchased gas	**99,267**	104,830	84,002
Other operation and cost of non-utility energy	**254,796**	317,608	252,722
Maintenance	**48,058**	46,492	42,043
Depreciation and amortization	**111,289**	90,683	86,319
Taxes other than income	**34,988**	34,603	34,188
	790,648	789,794	660,702
Operating income	**128,607**	143,050	146,553
Interest expense and other:			
Interest expense	**42,535**	42,027	43,559
Allowance for funds used during construction	**(2,775)**	(3,208)	(2,088)
Miscellaneous, net	**(4,432)**	(14,098)	(5,954)
	35,328	24,721	35,517
Income before income taxes and preferred dividend requirement of subsidiary	**93,279**	118,329	111,036
Income taxes	**28,715**	41,814	36,108
Preferred dividend reqnirement of subsidiary	**3,310**	3,310	3,310
Income from continuing operations	**61,254**	73,205	71,618
Discontinued operations:			
Loss from operation of discontinued subsidiary, net of applicable tax benefits of $1,451	—	—	2,212
Loss on disposal of subsidiary, net of applicable tax benefit of $575 and tax expense of $3,271	—	1,297	10,974
	—	1,297	13,186
Net income	**$ 61,254**	$ 71,908	$ 58,432
Earnings per common sbare (basic and diluted):			
Income from continuing operations	**$ 1.99**	$ 2.38	$ 2.33
Discontinued operations	—	(0.04)	(0.43)
Net income	**$ 1.99**	$ 2.34	$ 1.90
Weigbted average number of shares of common stock outstanding	**30,782**	30,790	30,774
Cash dividends paid per common share	**$ 2.00**	$ 1.97	$ 1.94

The accompanying notes are an integral part of the consolidated financial statements.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareowners of WPL Holdings, Inc.:

We have audited the accompanying consolidated balance sheets and statements of capitalization of WPL Holdings, Inc. (a Wisconsin corporation) and subsidiaries as of December 31, 1997 and 1996, and the related consolidated statements of income, cash flows and common shareowners' investment for each of the three years in the period ended December 31, 1997. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of WPL Holdings, Inc. and subsidiaries as of December 31, 1997 and 1996, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1997, in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Milwaukee, Wisconsin,
January 30, 1998

WPL HOLDINGS, INC.

CONSOLIDATED BALANCE SHEETS

ASSETS	December 31, 1997	December 31, 1996
	(in thousands)	
Utility plant:		
Plant in service —		
Electric	$1,790,641	$1,729,311
Gas	237,856	227,809
Water	24,864	23,905
Common	195,815	152,093
	2,249,176	2,133,118
Less — accumulated provision for depreciation	1,065,726	967,436
	1,183,450	1,165,682
Construction work in progress	42,312	55,519
Nuclear fuel, net	19,046	19,368
	1,244,808	1,240,569
Other property and equipment:		
Rental, net	101,835	112,913
Other, net	9,424	16,350
	111,259	129,263
Investments:		
Nuclear decommissioning trust funds	112,356	90,671
Other investments	28,289	15,408
	140,645	106,079
Current assets:		
Cash and equivalents	13,987	11,070
Net accounts receivable and unbilled revenue, less allowance for doubtful accounts of $1,104 and $1,524, respectively	78,082	88,798
Coal, at average cost	18,857	15,841
Materials and supplies, at average cost	19,274	19,915
Gas in storage, at average cost	12,504	9,992
Prepaid gross receipts tax	22,153	19,389
Prepayments and other	8,151	7,397
	173,008	172,402
Restricted cash	8,146	6,848
Deferred charges:		
Regulatory assets	91,314	160,877
Other	92,627	84,493
	183,941	245,370
TOTAL ASSETS	$1,861,807	$1,900,531
CAPITALIZATION AND LIABILITIES		
Capitalization (See Consolidated Statements of Capitalization):		
Common shareowners' investment	$ 607,583	$ 607,355
Subsidiary preferred stock not mandatorily redeemable	59,963	59,963
Long-term debt, net	457,520	362,564
	1,125,066	1,029,882
Current liabilities:		
Current maturities of long-term debt	11,528	67,626
Variable rate demand bonds	56,975	56,975
Short-term debt	123,095	102,779
Accounts payable and accruals	91,175	106,486
Accrued payroll and vacation	16,030	14,500
Accrued income taxes	412	4,669
Accrued interest	8,229	9,085
Other	31,728	45,218
	339,172	407,338
Other credits:		
Accumulated deferred income taxes	253,519	245,686
Accumulated deferred investment tax credits	35,039	36,931
Accrued environmental remediation costs	9,238	74,075
Deferred credits and other	99,773	106,619
	397,569	463,311
Commitments and contingencies (Note 11)		
TOTAL CAPITALIZATION AND LIABILITIES	$1,861,807	$1,900,531

The accompanying notes are an integral part of the consolidated financial statements.

WPL HOLDINGS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31, 1997	1996	1995
		(in thousands)	
Cash flows generated from (used for) operating activities:			
Net income	**$ 61,254**	$ 71,908	$ 58,432
Adjustments to reconcile net income to net cash generated from operating activities:			
Depreciation and amortization	**111,289**	90,683	86,319
Deferred income taxes	**4,957**	7,078	9,908
Investment tax credit restored	**(1,892)**	(1,911)	(1,916)
Amortization of nuclear fuel	**4,444**	6,057	7,787
Allowance for equity funds used during construction	**(2,033)**	(2,270)	(1,425)
(Gain) loss on sale of subsidiary and investment	**—**	(4,149)	10,974
(Gain) loss on disposition of other property and equipment	**710**	(5,676)	—
Changes in assets and liabilities:			
Restricted cash	**(1,298)**	(3,582)	(49)
Net accounts receivable and unbilled revenue	**10,716**	5,850	(23,183)
Inventories	**(4,887)**	(4,081)	3,750
Prepayments and other	**(3,518)**	1,201	2,292
Accounts payable and accruals	**(14,637)**	11,661	19,966
Accrued taxes	**(4,257)**	(1,814)	88
Other, net	**(9,625)**	19,764	12,974
Net cash from (used for) operating activities	**151,223**	190,719	185,917
Cash flows generated from (used for) financing activities:			
Common stock cash dividends	**(61,562)**	(60,656)	(59,701)
Proceeds from issuance of long-term debt	**105,000**	1,370	756
Reduction of long-term debt	**(65,921)**	(5,000)	(18,000)
Net change in short-term debt	**20,316**	(6,746)	45,024
Other, net	**—**	(1,367)	941
Net cash from (used for) financing activities	**(2,167)**	(72,399)	(30,980)
Cash flows generated from (used for) investing activities:			
Proceeds from sale of other property and equipment	**9,700**	36,264	—
Additions to utility plant, excluding AFUDC	**(116,457)**	(120,732)	(99,746)
Additions to nuclear fuel	**(4,123)**	(6,558)	(7,258)
Allowance for borrowed funds used during construction	**(742)**	(938)	(663)
Dedicated nuclear decommissioning trust funds	**(21,685)**	(17,314)	(21,566)
Proceeds from sale of subsidiary and investments	**—**	24,930	—
Purchase of other property and equipment	**(2,855)**	(20,824)	(26,696)
Contribution to nonutility joint venture	**(5,000)**	—	—
Other, net	**(4,977)**	(13,464)	5,105
Net cash from (used for) investing activities	**(146,139)**	(118,636)	(150,824)
Net increase (decrease) in cash and equivalents	**2,917**	(316)	4,113
Cash and equivalents at beginning of year	**11,070**	11,386	7,273
Cash and eqnivalents at end of year	**$ 13,987**	$ 11,070	$ 11,386
Supplemental disclosures of cash flow information:			
Cash paid during the year:			
Interest on debt	**$ 42,706**	$ 35,855	$ 39,984
Preferred stock dividends of subsidiary	**$ 3,310**	$ 3,310	$ 3,310
Income taxes	**$ 23,662**	$ 39,795	$ 29,499

The accompanying notes are an integral part of the consolidated financial statements.

WPL HOLDINGS, INC.

CONSOLIDATED STATEMENTS OF CAPITALIZATION

	December 31, 1997	December 31, 1996
	(in thousands except for share data)	
Common shareowners' investment:		
Common stock $.01 par value, authorized 100,000,000 shares, issued and outstanding — 30,788,593 and 30,773,735 shares, respectively	$ 308	$ 308
Additional paid-in capital	304,392	303,856
Reinvested earnings	302,883	303,191
	607,583	607,355
Preferred stock:		
Wisconsin Power and Light Company —		
Cumulative, without par value, authorized 3,750,000 shares, maximum aggregate stated value $150,000,000:		
Preferred stock without mandatory redemption, $100 stated value —		
4.50% series, 99,970 shares outstanding	9,997	9,997
4.80% series, 74,912 shares outstanding	7,491	7,491
4.96% series, 64,979 shares outstanding	6,498	6,498
4.40% series, 29,957 shares outstanding	2,996	2,996
4.76% series, 29,947 shares outstanding	2,995	2,995
6.20% series, 150,000 shares outstanding	15,000	15,000
Cumulative, without par value, $25 stated value — 6.50% series, 599,460 shares outstanding	14,986	14,986
	59,963	59,963
Long-term debt:		
Wisconsin Power and Light Company —		
First mortgage bonds:		
Series L, 6.25%, due 1998	8,899	8,899
1984 Series A, variable rate, due 2014 (3.80% at 12/31/97)	8,500	8,500
1988 Series A, variable rate, due 2015 (3.80% at 12/31/97)	14,600	14,600
1990 Series V, 9.3%, due 2025	27,000	27,000
1991 Series A, variable rate, due 2015 (5.05% at 12/31/97)	16,000	16,000
1991 Series B, variable rate, due 2005 (5.05% at 12/31/97)	16,000	16,000
1991 Series C, variable rate, due 2000 (5.05% at 12/31/97)	1,000	1,000
1991 Series D, variable rate, due 2000 (5.05% at 12/31/97)	875	875
1992 Series W, 8.6%, due 2027	90,000	90,000
1992 Series X, 7.75%, due 2004	62,000	62,000
1992 Series Y, 7.6%, due 2005	72,000	72,000
1992 Series Z, 6.125%, repaid 1997	—	55,000
Debentures, 7%, due 2007	105,000	—
	421,874	371,874
Heartland Development Corporation —		
Multifamily Housing Revenue Bonds issued by various housing and community development authorities, due 2004-2024, 2.00% – 7.55%	36,503	37,445
Other mortgage notes payable, due 1998-2042, 0% – 10.75%	45,106	45,086
	81,609	82,531
WPL Holdings, Inc. —		
8.96% Senior notes, repaid 1997	—	10,000
8.59% Senior notes, due 2004	24,000	24,000
	24,000	34,000
Less —		
Current maturities	(11,528)	(67,626)
Variable rate demand bonds	(56,975)	(56,975)
Unamortized discount and premium, net	(1,460)	(1,240)
	457,520	362,564
TOTAL CAPITALIZATION	$1,125,066	$1,029,882

The accompanying notes are an integral part of the consolidated financial statements.

WPL HOLDINGS, INC.

CONSOLIDATED STATEMENTS OF COMMON SHAREOWNERS' INVESTMENT

	Year Ended December 31,		
	1997	1996	1995
	(in thousands except for per share data)		
Common stock:			
Balance at beginning of year	$ 308	$ 308	$ 308
Balance at end of year	308	308	308
Additional paid-in capital:			
Balance at beginning of year	303,856	305,223	304,442
Other	536	(1,367)	781
Balance at end of year	304,392	303,856	305,223
Reinvested earnings:			
Balance at beginning of year	303,191	291,939	293,048
Net income	61,254	71,908	58,432
Cash dividends ($2.00 per share, $1.97 per share and $1.94 per share, respectively)	(61,562)	(60,656)	(59,701)
Expense of issuing stock and other	—	—	160
Balance at end of year	302,883	303,191	291,939
TOTAL COMMON SHAREOWNERS' INVESTMENT	$607,583	$607,355	$597,470

The accompanying notes are an integral part of the consolidated financial statements.

Normal repairs, maintenance and minor items of utility plant and other property and equipment are expensed. Ordinary utility plant retirements, including removal costs less salvage value, are charged to accumulated depreciation upon removal from utility plant accounts, and no gain or loss is recognized. Upon retirement or sale of other property and equipment, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is included in other income and deductions.

f. Depreciation

The Company uses the straight-line method of depreciation. For utility plant, straight-linc depreciation is computed on the average balance of depreciable property at individual straight-line regulatory-approved rates that consider the estimated useful life and removal cost or salvage value as follows:

	1997	1996	1995
Electric	**3.6%**	3.3%	3.3%
Gas	**3.8%**	3.7%	3.7%
Water	**2.7%**	2.6%	2.5%
Common	**11.9%**	8.1%	7.9%

Depreciation expense related to WP&L's share of the decommissioning of the Kewaunee Nuclear Power Plant (Kewaunee) is discussed in Note 11 "Commitments and Contingencies." WP&L implemented higher depreciation rates effective January 1, 1997.

Estimated useful lives related to other property and equipment are from 4 to 12 years for equipment and 31.5 to 40 years for buildings.

g. Nuclear Fuel

Nuclear fuel is recorded at its original cost and is amortized to expense based upon the quantity of heat produced for the generation of electricity. This accumulated amortization assumes spent nuclear fuel will have no residual value. Estimated future disposal costs of such fuel are expensed based on kilowatthours generated.

b. Regulatory Assets and Liabilities

Statement of Financial Accounting Standards No. 71 (SFAS 71), "Accounting for the Effects of Certain Types of Regulation," provides that rate-regulated public utilities, such as WP&L, record certain costs and credits allowed in the ratemaking process in different periods than for unregulated entities. These are deferred as regulatory assets or regulatory liabilities and are recognized in the consolidated statements of income at the time they are reflected in rates. If a portion of WP&L's operations becomes no longer subject to the provisions of SFAS 71 as a result of competitive restructuring or otherwise, a write-down of related regulatory assets would be required, unless some form of transition cost recovery is established by the appropriate regulatory body that would meet the requirements under generally accepted accounting principles for continued accounting as regulatory assets during such recovery period. In addition, WP&L would be required to determine any impairment to other assets and write-down such assets to their fair value. As of December 31, 1997 and 1996, regulatory-created assets included the following:

	1997	1996
Environmental remediation costs (Note 11)	**$16.3**	$ 81.4
Tax related	**52.2**	57.2
Jurisdictional plant differences	**7.9**	7.6
Decontamination and decommissioning costs of federal enrichment facilities	**5.9**	6.1
Other	**9.0**	8.6
	$91.3	$160.9

WPL HOLDINGS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in millions except as otherwise indicated)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. General

The consolidated financial statements include the accounts of WPL Holdings, Inc. (WPLH) and its consolidated subsidiaries (collectively, the Company). WPLH is an investor-owned holding company whose primary operating company, Wisconsin Power & Light Company (WP&L), is engaged principally in the generation, transmission, distribution and sale of electric energy and the purchase, distribution, transportation and sale of natural gas primarily in the state of Wisconsin. WP&L's principal consolidated subsidiary is South Beloit Water, Gas and Electric Co. The Company also has various non-utility subsidiaries which are primarily engaged in the environmental and engineering service, affordable housing and energy marketing businesses.

All subsidiaries for which the Company owns directly or indirectly more than 50% of the voting stock are included as consolidated subsidiaries. All significant intercompany balances and transactions have been eliminated from the consolidated financial statements.

Unconsolidated investments for which the Company has at least a 20% interest are generally accounted for under the equity method of accounting. These investments are stated at acquisition cost, increased or decreased for the Company's equity in net income or loss, which is included in "Miscellaneous, net" in the consolidated statements of income and decreased for any dividends received. Investments that do not meet the criteria for consolidation or the equity method of accounting are accounted for under the cost method.

Certain reclassifications have been made to the prior years financial statements to conform with the current year presentation.

b. Regulation

WP&L's financial records are maintained in accordance with the uniform system of accounts prescribed by its regulators. The Public Service Commission of Wisconsin (PSCW) and the Illinois Commerce Commission (ICC) have jurisdiction over retail electric and gas revenues. The Federal Energy Regulatory Commission (FERC) has jurisdiction over wholesale electric revenues.

c. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

d. Cash and Eqnivalents

The Company considers all short-term liquid investments with a maturity of three months or less to be cash equivalents.

e. Utility Plant and Other Property and Equipment

Utility plant and other property and equipment are recorded at original cost. Utility plant costs include financing costs that are capitalized using the FERC method for allowance for funds used during construction (AFUDC). The AFUDC capitalization rates for 1997, 1996 and 1995 were 6.22%, 10.23% and 6.68%, respectively. These capitalized costs are recovered in rates as the cost of the utility plant is depreciated.

As of December 31, 1997 and 1996, WP&L had recorded regulatory-related liabilities of $39.6 and $33.9, respectively. These liabilities are primarily tax related.

i. Revenue

The Company accrues revenues for services provided but not yet billed at month-end.

j. Income Taxes

The Company follows the liability method of accounting for deferred income taxes, which requires the establishment of deferred tax assets and liabilities, as appropriate, for all temporary differences between the tax basis of assets and liabilities and the amounts reported in the financial statements using currently enacted tax rates as shown in Note 6.

Investment tax credits are accounted for on a deferred basis and reflected in income ratably over the life of the related utility plant. As part of the affordable housing business, the Company is eligible to claim affordable housing and historic rehabilitation credits. These tax credits reduce current federal taxes to the extent the Company has consolidated taxes payable.

k. Common Sbares Outstanding

The weighted average common shares outstanding used in the calculation of basic earnings per share were 30,781,998; 30,789,813 and 30,773,588 for 1997, 1996 and 1995, respectively. The common stock shares used for calculating diluted earnings per share were 30,784,136; 30,793,555 and 30,775,965 for 1997, 1996 and 1995, respectively.

NOTE 2. PROPOSED MERGER OF THE COMPANY

On November 10, 1995, WPLH, IES Industries Inc. (IES), and Interstate Power Company (IPC) entered into an Agreement and Plan of Merger, as amended (Merger Agreement), providing for: a) IPC becoming a subsidiary of WPLH, and b) the merger of IES with and into WPLH, which merger will result in the combination of IES and WPLH as a single holding company (collectively, the Proposed Merger). The new holding company will be named Interstate Energy Corporation (Merged Company). The Proposed Merger, which will be accounted for as a pooling of interests and is intended to be tax-free for federal income tax purposes, has been approved by the respective Boards of Directors, shareowners, state regulatory agencies and most of the federal agencies. It is still subject to approval by the Securities and Exchange Commission (SEC). The companies expect to receive SEC approval in the second quarter of 1998.

The summary below contains selected unaudited pro forma financial data for the year ended December 31, 1997. The financial data should be read in conjunction with the historical consolidated financial statements and related notes thereto of WPLH and in conjunction with the unaudited pro forma combined financial statements and related notes of the Merged Company included elsewhere in this Annual Report. The pro forma combined earnings per share reflect the issuance of shares associated with the exchange ratios discussed below.

	WPLH (As Reported)	IES (As Reported)	IPC (As Reported)	Pro Forma Adjustments	Pro Forma Combined (Unaudited)
Operating revenues	$ 919.3	$ 930.7	$331.8	$118.8	$2,300.6
Income from continuing operations	$ 61.3	$ 66.3	$ 26.7	$ —	$ 154.3
Earnings per share from continuing operations (basic and diluted)	$ 1.99	$ 2.18	$ 2.74	$ —	$ 2.02
Assets at December 31, 1997	$1,861.8	$2,457.2	$638.7	$ (6.0)	$4,951.7
Long-term obligations, net at December 31, 1997	$ 526.0	$ 882.4	$195.9	$ —	$1,604.3

Under the terms of the Merger Agreement, the outstanding shares of WPLH's common stock will remain unchanged and outstanding as shares of the Merged Company's common stock, each outstanding share of IES common stock will be converted to 1.14 shares of the Merged Company's common stock and each share of IPC common stock will be converted to 1.11 shares of the Merged Company's common stock. It is anticipated that the Merged Company will retain WPLH's common share dividend payment level as of the effective time of the Proposed Merger. On January 16, 1998, the Board of Directors of WPLH declared a quarterly dividend of $0.50 per share. This represents an annual rate of $2.00 per share.

IES is a holding company headquartered in Cedar Rapids, Iowa, and is the parent company of IES Utilities Inc. (IESU) and IES Diversified Inc. (Diversified). IESU supplies electric and gas service to approximately 339,000 and 178,000 customers, respectively, in Iowa. Diversified and its principal subsidiaries are primarily engaged in the energy-related, transportation and real estate development businesses. IPC, an operating public utility headquartered in Dubuque, Iowa, supplies electric and gas service to approximately 166,000 and 50,000 customers, respectively, in northeast Iowa, northwest Illinois and southern Minnesota.

The Merged Company will be the parent company of WP&L, IESU and IPC and will be registered under the Public Utility Holding Company Act of 1935, as amended (1935 Act). The Merger Agreement provides that these operating utility companies will continue to operate as separate entities for a minimum of three years after the effective date of the Proposed Merger. In addition, the non-utility operations of WPLH and IES will be combined shortly after the effective date of the Proposed Merger under one entity to manage the diversified operations of the Merged Company. The corporate headquarters of the Merged Company will be in Madison, Wisconsin.

NOTE 3. JOINTLY-OWNED UTILITY PLANTS

WP&L participates with other Wisconsin utilities in the construction and operation of several jointly-owned utility generating plants. Each of the respective owners is responsible for the financing of its portion of the construction costs. Kilowatthour generation and operating expenses are divided on the same basis of ownership with each owner reflecting its respective costs in its consolidated statements of income. The chart below represents WP&L's proportionate share of such plants as reflected in the consolidated balance sheets at December 31, 1997 and 1996.

				1997			1996		
	Ownership Interest %	Inservice Date	Plant MW Capacity	Plant in Service	Accumulated Provision for Depreciation	CWIP	Plant in Service	Accumulated Provision for Depreciation	CWIP
Coal:									
Columbia Energy Center	46.2	1975 & 1978	1,023	$161.4	$ 89.2	$ 0.8	$161.8	$ 86.4	$1.6
Edgewater Unit 4	68.2	1969	330	51.5	29.5	1.0	50.8	28.0	0.7
Edgewater Unit 5	75.0	1985	380	229.4	79.8	0.1	228.8	73.7	0.0
Nuclear:									
Kewaunee Nuclear Power Plant	41.0	1974	535	132.0	86.6	0.3	131.2	80.6	0.8
Total				$574.3	$285.1	$ 2.2	$572.6	$268.7	$3.1

NOTE 4. UTILITY ACCOUNTS RECEIVABLE

WP&L has a contract with a financial organization to sell, with limited recourse, certain accounts receivable and unbilled revenues. These receivables include customer receivables, sales to other public utilities and billings to the co-owners of the jointly-owned electric generating plants that WP&L operates. The contract allows WP&L to sell up to $150.0 of receivables at any time. Expenses related to the sale of receivables are paid to the financial organization under this contract, and include, along with various other fees, a monthly discount charge on the outstanding balance of receivables sold that approximated a 5.83% annual rate during 1997. These costs are recovered in retail utility rates as an operating expense. All billing and collection functions remain the responsibility of WP&L. The contract expires August 16, 1998, unless extended by mutual agreement.

As of December 31, 1997 and 1996, the balance of sold accounts receivable that had not been collected totaled $91.0 and $86.5, respectively. During 1997, the monthly proceeds from the sale of accounts receivable averaged $92.1, compared with $86.6 in 1996. As of December 31, 1997, the amount of sold receivables subject to recourse was $8.2.

The Company does not have any significant concentrations of credit risk in the December 31, 1997 and 1996 utility accounts receivable balances.

In June 1996, the Financial Accounting Standards Board (FASB) issued SFAS No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," which establishes standards for asset and liability recognition when transfers occur. This statement, effective January 1, 1997, specifies conditions when control has been surrendered which determines if sale treatment of the receivables would be allowed. This standard has not had any impact on the Company's financial position or results of operations.

NOTE 5. EMPLOYEE BENEFIT PLANS

a. Pension Plans

WP&L has noncontributory, defined benefit retirement plans covering substantially all employees. The benefits are based upon years of service and levels of compensation. The projected unit credit actuarial cost method was used to compute net pension costs and the accumulated and projected benefit obligations. WP&L's policy is to fund the pension cost in an amount that is at least equal to the minimum funding requirements mandated by the Employee Retirement Income Security Act of 1974, as amended (ERISA), and that does not exceed the maximum tax deductible amount for the year.

The following table sets forth the funded status of the plans and amounts recognized in the Company's consolidated balance sheets at December 31, 1997 and 1996:

	1997	1996
Accumulated benefit obligation		
Vested benefits	**$(173.4)**	$(161.0)
Non-vested benefits	**(6.1)**	(3.3)
Total	**(179.5)**	(164.3)
Projected benefit obligation	**(205.1)**	(189.6)
Plan assets at fair value	**244.4**	218.9
Plan assets in excess of projected benefit obligation	**39.3**	29.3
Unrecognized net transition asset	**(12.0)**	(14.5)
Unrecognized prior service cost	**7.8**	3.7
Unrecognized net loss	**0.8**	15.0
Prepaid pension costs	**$ 35.9**	$ 33.5
Assumed rate of return on plan assets	**9.00%**	9.00%
Discount rate of projected benefit obligation	**7.25%**	7.50%
Range of assumed rate increases for future compensation levels	**3.50-4.50%**	3.50-4.50%

The net pension cost (benefit) recognized in the consolidated statements of income for 1997, 1996 and 1995 included the following components:

	1997	1996	1995
Service cost	$ **4.8**	$ 5.1	$ 3.9
Interest cost on projected benefit obligation	**13.8**	13.6	12.9
Actual return on assets	**(36.2)**	(25.0)	(31.6)
Amortization and deferrals	**15.1**	5.5	15.1
Net pension cost (benefit)	**$ (2.5)**	$ (0.8)	$ 0.3

During 1997, WP&L expensed $1.3 for an early retirement program for eligible bargaining unit employees.

b. Other Postretirement Benefits

WP&L accrues for the expected cost of postretirement health-care and life insurance benefits during the employees' years of service based on actuarial methodologies that closely parallel pension accounting requirements. WP&L elected delayed recognition of the transition obligation in accordance with current accounting principles and is amortizing the discounted present value of the transition obligation to expense over 20 years. For WP&L, the cost of providing postretirement benefits, including the transition obligation, is being recovered in retail rates under current regulatory practices. WP&L's policy is to fund the postretirement cost in an amount that is at least equal to the minimum funding requirements mandated by ERISA and that does not exceed the maximum tax deductible amount for the year.

The following table sets forth the funded status of the plans and amounts recognized in the Company's consolidated balance sheets at December 31, 1997 and 1996:

	1997	1996
Accumulated benefit obligation		
Retirees	**$(31.4)**	$(32.2)
Fully eligible active plan participants	**(4.4)**	(5.0)
Other active plan participants	**(11.3)**	(9.4)
Total	**(47.1)**	(46.6)
Plan assets at fair value	**16.1**	13.8
Accumulated benefit obligation in excess of plan assets	**(31.0)**	(32.8)
Unrecognized transition obligation	**21.0**	23.5
Unrecognized prior service cost	**(0.3)**	(0.3)
Unrecognized net gain	**(8.3)**	(5.0)
Accrued postretirement benefits liability	**$(18.6)**	$(14.6)
Assumed rate of return on plan assets	**9.00%**	9.00%
Discount rate of projected benefit obligation	**7.25%**	7.50%
Medical cost trend on paid charges:		
Initial trend rate	**8.00%**	9.00%
Ultimate trend rate	**5.00%**	5.00%

The net postretirement benefits cost recognized in the consolidated statements of income for 1997, 1996 and 1995 included the following components:

	1997	1996	1995
Service cost	**$ 1.8**	$ 1.8	$ 1.5
Interest cost on projected benefit obligation	**3.3**	3.4	3.6
Actual return on assets	**(1.9)**	(1.3)	(2.1)
Amortization of transition obligation	**1.5**	1.5	1.5
Amortization and deferrals	**0.5**	0.3	1.3
Net postretirement benefits cost	**$ 5.2**	$ 5.7	$ 5.8

Increasing the assumed health-care cost trend rate by one percentage point in each year would increase the accumulated postretirement benefit obligation as of December 31, 1997 by $2.7 and the aggregate of the service and interest cost components of the net periodic postretirement benefit cost for the year by $0.4.

During 1997, WP&L expensed $1.7 for an early retirement program for eligible bargaining unit employees.

c. Long-Term Equity Incentive Plan

WPLH has a long-term equity incentive plan which permits the grant of non-qualified stock options, incentive stock options, restricted stock, performance shares and performance units to key employees. As of December 31, 1997, only non-qualified stock options and equivalent performance units had been granted to key employees. The maximum number of shares of common stock that may be issued under the plan may not exceed one million. Options granted to date become exercisable after three years. Options outstanding will expire no later than 10 years after the grant date. The first options were granted in 1995 and will become exercisable in January 1998. No options have been canceled or exercised to date. The options granted and the value of those options using the Black-Scholes model is as follows:

	1997	1996	1995
Options granted	**77,650**	72,250	41,900
Weighted average Black-Scholes value of options	**$2.15**	$2.23	$2.71
Volatility	**0.15**	0.16	0.16
Risk free interest rate	**6.13%**	5.26%	7.84%
Expected life	**3 years**	3 years	3 years
Annual dividend rate	**7.0%**	7.0%	7.0%

WPLH follows APB Opinion 25, "Accounting for Stock Issued to Employees," to account for stock options. No compensation cost is recognized because the option exercise price is equal to the market price of the underlying stock on the date of grant. Had compensation cost for the plan been determined based on the Black-Scholes value at the grant dates for awards as prescribed by SFAS No. 123 "Accounting for Stock-Based Compensation," pro forma net income and earnings per share would have been:

	1997	1996	1995
Pro forma net income	**$61.1**	$71.7	$58.3
Pro forma earnings per share (basic and diluted)	**$1.98**	$2.33	$1.90

The performance units granted under the plan to date are expensed over the three-year vesting period based on the current dividend rate. In 1997, 1996 and 1995, WPLH recognized expense of $0.4, $0.2 and $0.1, respectively.

NOTE 6. INCOME TAXES

The following table reconciles the statutory federal income tax rate to the effective income tax rate on continuing operations:

	1997	1996	1995
Statutory federal income tax rate	**35.0%**	35.0%	35.0%
State income taxes, net of federal benefit	**7.0**	6.8	6.0
Investment tax credits restored	**(2.0)**	(1.6)	(1.7)
Amortization of excess deferred taxes	**(1.6)**	(1.4)	(1.5)
Affordable housing and historical tax credits	**(6.7)**	(5.0)	(4.5)
Adjustment of prior period taxes	**(2.6)**	—	—
Other differences, net	**1.7**	1.6	(0.8)
Effective income tax	**30.8%**	35.4%	32.5%

The breakdown of income tax expense as reflected in the consolidated statements of income is as follows:

	1997	1996	1995
Current federal	**$25.2**	$32.8	$25.9
Current state	**6.6**	9.7	7.2
Deferred	**5.0**	7.1	9.9
Investment tax credit restored	**(1.9)**	(1.9)	(1.9)
Affordable housing and historical tax credits	**(6.2)**	(5.9)	(5.0)
	$28.7	$41.8	$36.1

The temporary differences that resulted in accumulated deferred income tax (assets) and liabilities as of December 31, 1997 and 1996, are as follows:

	1997	1996
Property related	$295.4	$282.0
Investment tax credit related	(23.5)	(19.9)
Decommissioning related	(16.0)	(14.5)
Other	(2.4)	(1.9)
	$253.5	$245.7

NOTE 7. SHORT-TERM DEBT AND LINES OF CREDIT

WPLH and its subsidiaries maintain committed bank lines of credit, most of which are at the bank prime rates, to obtain short-term borrowing flexibility, including pledging lines of credit as security for any commercial paper outstanding. Amounts available under these lines of credit totaled $170.0 as of December 31, 1997. Information regarding short-term debt and lines of credit is as follows:

	1997	1996	1995
As of year end —			
Lines of credit borrowings	—	—	—
Commercial paper outstanding	$ 81.0	$ 59.5	$ 56.5
Notes payable outstanding	$ 42.1	$ 43.3	$ 53.0
Discount rates on commercial paper	5.48-5.90%	5.35-5.65%	5.73-5.77%
Interest rates on notes payable	5.00-5.90%	5.28-6.31%	5.80-6.42%
For the year ended —			
Maximum month-end amount of short-term debt	$140.0	$103.5	$117.0
Average amount of short-term debt (based on daily outstanding balances)	$ 94.5	$ 60.8	$ 68.7
Average interest rate on short-term debt	5.65%	5.72%	5.95%

NOTE 8. DERIVATIVE FINANCIAL INSTRUMENTS

The Company has only limited involvement with derivative financial instruments and does not use them for trading purposes. They arc used to manage well-defined interest rate and commodity price risks.

Interest rate swaps and forward contracts: WP&L enters into interest rate swap agreements to reduce the impact of changes in interest rates on its floating-rate debt and fees associated with the sale of its accounts receivable. The notional principal amount of interest rate swaps outstanding as of December 31, 1997, was $40.0. Average variable rates are based on rates implied in the forward yield curve at the reporting date. The average pay and receive rates associated with these agreements are 4.11% and 3.61%, respectively. The swap agreements have contract maturities from three months to two years. It is not WP&L's intent to terminate these contracts; however, the total cost to WP&L if it had terminated all of the agreements existing at December 31, 1997 would have been $0.2.

In 1995, WP&L entered into an interest rate forward contract related to the anticipated issuance of $60.0 of long-term debt securities. The securities were not issued in 1996 and the forward contract was closed which resulted in a gain of $0.8 to WP&L. The gain was deferred and was recognized as an adjustment to interest expense over the life of the debt securities issued during 1997 as discussed in Note 10(b).

On April 28, 1997, WP&L entered into an interest rate forward contract to hedge interest rate risk related to the anticipated issuance of $105.0 of long-term debt securities. The securities were issued in June 1997 and the forward contract was settled which resulted in a cash payment of $3.8 by WP&L. This payment was recognized as an adjustment to interest expense over the life of the new debt securities to approximate the interest rate implicit in the forward contract.

Gas Swaps: WP&L uses gas commodity swaps to reduce the impact of price fluctuations on gas purchased and injected into storage during the summer months and withdrawn and sold at current market prices during the winter months. The notional amount of gas commodity swaps outstanding as of December 31, 1997 was 4.8 million dekatherms. Variances between underlying commodity prices and financial contracts on these agreements are deferred and recognized as increases or decreases in the cost of gas at the time the storage gas is sold. It is not WP&L's intent to terminate these contracts; however, the total cost to WP&L if it had terminated all of the agreements existing at December 31, 1997 would have been a gain of $1.0.

Other: The Company's non-utility energy marketing business periodically uses commodity futures contracts, options and swaps to hedge the impact of natural gas and electric power price fluctuations on its purchase and sale commitments. Gains and losses on these instruments are deferred and recognized in income as adjustments to the costs of energy when the related transaction being hedged is finalized. At December 31, 1997 and 1996, the instruments outstanding were immaterial.

NOTE 9. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Current Assets and Current Liabilities — The carrying amount approximates fair value due to the short maturities of these financial instruments.

Nuclear Decommissioning Trust Funds — As of December 31, 1997 and 1996, the investments in the nuclear decommissioning trust fund are carried at fair value, as reported by the trustee. The balance as shown on the consolidated halance sheets included a net unrealized gain of $16.4 and $9.4 as of December 31, 1997 and 1996, respectively.

Preferred Stock of WP&L — Based on quoted market prices for the same or similar issues.

Long-Term Deht — Based upon the market yield of similar securities and quoted market prices on the current rates for debt of the same remaining maturities.

The estimated fair values of financial instruments at December 31, 1997 and 1996:

	1997		1996	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Nuclear decommissioning trust funds	**$112.4**	**$112.4**	$ 90.7	$ 90.7
Preferred stock	**60.0**	**51.7**	60.0	47.7
Long-term debt, including current portion	**526.0**	**555.7**	487.2	503.5

Since WP&L is subject to regulation, any gains or losses related to the difference between the carrying amount and the fair value of WP&L's nuclear decommissioning trust funds and long-term debt may not be realized by the Company's shareowners.

NOTE 10. CAPITALIZATION

a. Common Shareowners' Investment

During 1997, 1996 and 1995, the Company did not issue any new shares of common stock through either its Shareowner Direct Plan or 401(k) Savings Plan.

In February 1989, the Board of Directors of the Company declared a dividend distribution of one common stock purchase right (right) on each outstanding share of the Company's common stock. Each right would initially entitle shareowners to buy one-half of one share of the Company's common stock at an exercise price of $60.00 per share, subject to adjustment. The rights are not currently exercisable, but would become exercisable if certain events occurred related to a person or group acquiring or attempting to acquire 20% or more of the outstanding shares of common stock. The rights expire on February 22, 1999, unless redeemed or exchanged earlier by the Company.

A retail rate order effective April 29, 1997 requires WP&L to maintain a utility common equity level of 52.00% of total utility capitalization. In addition, the PSCW ordered that it must approve the payment of dividends by WP&L to the Company that are in excess of the level forecasted in the rate order ($58.3), if such dividends would reduce WP&L's average common equity ratio below 52.00% of total capitalization. Based on a 13-month average for 1997, WP&L's common equity ratio was 52.56%.

h. Long-Term Debt

Substantially all of WP&L's utility plant is secured by its first mortgage bonds. In addition, the Company's long-term debt includes unsecured debentures, notes payable and revenue bonds related to its affordable housing properties. Current maturities of long-term debt of the Company are as follows: $11.5 in 1998, $4.5 in 1999, $4.1 in 2000, $2.6 in 2001 and $2.7 in 2002.

In June 1997, WP&L issued $105.0 of 7% Debentures due June 15, 2007. Approximately $50.0 of the net proceeds was used to repay maturing short-term debt and finance utility construction expenditures. The balance of the proceeds was used to retire the $55.0 of WP&L's First Mortgage Bonds, Series Z, 6.125%, due July 15, 1997.

NOTE 11. COMMITMENTS AND CONTINGENCIES

a. Coal Contract Commitments

To ensure an adequate supply of coal, WP&L has entered into certain long-term coal contracts. These contracts include a demand or take-or-pay clause under which payments are required if contracted quantities are not purchased. Purchase obligations on these coal and related rail contracts total approximately 12.5 million tons through December 31, 2002. WP&L's management believes it will meet minimum coal and rail purchase obligations under the contracts. Minimum purchase obligations on these contracts over the next five years are estimated to be $36.0 in 1998, $29.0 in 1999, $9.0 in 2000, $9.0 in 2001 and $4.0 in 2002.

b. Purchased Power and Gas

Under firm purchased power and gas contracts, the Company is obligated as follows:

	Power	Gas
1998	$72.0	$37.0
1999	76.3	32.7
2000	86.5	27.1
2001	38.1	22.4
2002	28.0	18.0
Thereafter	58.0	29.6

c. Manufactured Gas Plant Sites

WP&L has a current or previous ownership interest in 11 properties, consisting of 14 individual sites, associated in the past with the production of manufactured gas. Some of these sites contain coal tar waste products which may present an environmental hazard. WP&L owns six of these sites, three are currently owned by municipalities and the remaining five are all or partially owned by private companies.

WP&L conducted a comprehensive review in the third quarter of 1997 of its liability at each of the 14 sites. This comprehensive review considered several recent significant developments and resulted in a reduction in the estimate of the probable liability for cleanup. At December 31, 1997, the liability is $9.2. In addition, management believes it is possible, but not likely, that an additional $3.2 of remediation costs may be incurred. In 1996, the Wisconsin Department of Natural Resources (DNR) approved less costly containment and control strategies as an alternative to excavation processes at two sites. The decline in the liability of approximately $65.0 from December 31, 1996 to December 31, 1997, is due to the successful implementation of these strategies at those two sites and several additional sites. Further reductions in the liability resulted from WP&L receiving an additional close out letter from the DNR, bringing the total number of sites with close out letters to four.

The cleanup estimate discussed above includes the costs of feasibility studies, data collection, soil and groundwater remediation activities, and ongoing monitoring activities through 2027. The estimate is based on a number of factors including the estimated extent and volume of contaminated soil and/or groundwater. Changes in the estimate are reasonably possible in the near term.

Changes in the liability do not immediately impact the earnings of WP&L. Under the current rate making treatment approved by the PSCW, the costs expended in the environmental remediation of these sites, net of any insurance proceeds, are deferred and collected from gas customers over a five-year period after new rates are implemented. Although no assurance can be given, management currently believes future costs will also be recovered in rates. The associated regulatory asset is $16.3 as of December 31, 1997.

d. Spent Nuclear Fuel and Decommissioning Costs

The current cost of WP&L's share of the estimated costs to decommission Kewaunee ($181.3), assuming early retirement, exceeds the trust assets at December 31, 1997 ($112.4) by $68.9. The costs of decommissioning are assumed to escalate at an annual rate of 5.83%.

As required by the PSCW and FERC, WP&L makes annual contributions to qualified and nonqualified external trust funds to provide for decommissioning of Kewaunee. The Company's annual contribution was $14.3 for 1997 and $10.7 for 1996 and 1995. These amounts are fully recovered in rates. The after-tax income of the external trust funds was $3.2 , $2.7 and $2.8 for 1997, 1996 and 1995, respectively.

Decommissioning costs, which include the annual contribution to external trust funds and earnings on the assets of these trusts, are recorded as depreciation expense in the consolidated statements of income with the cumulative amount included in the accumulated provision for depreciation on the consolidated balance sheets. As of December 31, 1997, the total decommissioning costs included in the accumulated provision for depreciation were $112.4.

Under the Nuclear Waste Policy Act of 1982, the U.S. Department of Energy (DOE) is responsible for the ultimate storage and disposal of spent nuclear fuel removed from nuclear reactors. Interim storage space for spent nuclear fuel is currently provided at Kewaunee. Currently, there is on-site storage capacity for spent fuel through the year 2001. An investment of approximately $2.5 could provide additional storage sufficient to meet spent fuel storage needs until the expiration of the current operating license.

The following summarizes the Company's investment in nuclear fuel at December 31, 1997 and 1996:

	1997	1996
Original cost of nuclear fuel	**$169.6**	$166.4
Less — Accumulated amortization	**150.5**	147.0
Nuclear fuel, net	**$ 19.1**	$ 19.4

e. Nuclear Performance

WP&L has a 41% ownership interest in Kewaunee. Kewaunee resumed operations on June 12, 1997 after being out of service since September 21, 1996 for refueling and repairs to the steam generator tubes. The joint owners continue to analyze and discuss other options related to the future of Kewaunee, including various ownership transfer alternatives.

f. Nuclear Insurance

The Price Anderson Act provides for the payment of funds for public liability claims arising from a nuclear incident. Accordingly, in the event of a nuclear incident, WP&L, as a 41% owner of Kewaunee, is subject to an overall assessment of approximately $32.5 per incident, not to exceed $4.1 payable in any given year.

Through its membership in Nuclear Mutual Limited and Nuclear Electric Insurance Limited, WP&L has obtained property damage and decontamination insurance totaling $1.8 billion for loss from damage at Kewaunee. In addition, WP&L maintains outage and replacement power insurance coverage totaling $101.4 in the event an outage exceeds 21 weeks.

g. Planned Capital Expenditures

Plans for the construction and financing of future additions to utility plant can be found elsewhere in this report under "Management's Discussion and Analysis of Financial Condition and Results of Operations."

h. Loan Commitments

As of December 31, 1997, HDC had extended commitments to provide $15.7 in nonrecourse, fixed rate, permanent financing to developers which are secured by affordable housing properties. The Company anticipates other lenders will ultimately finance these properties.

NOTE 12. DISCONTINUED OPERATIONS

The Company's financial statements reflect the discontinuance of operations of its utility energy and marketing consulting business in 1995. The discontinuance of this business resulted in a pre-tax loss in the fourth quarter of 1995 of $7.7. The after tax loss on disposition was $11.0 reflecting the associated tax expense on disposition due to the non-deductibility of the carrying value of goodwill at sale. During 1996, the Company recognized an additional loss of $1.3, net of applicable income tax benefit, associated with the final disposition of the business. Operating revenues, operating expenses, other income and expense and income taxes for the discontinued operations for the time periods presented have been excluded from income from continuing operations. Interest expense has been adjusted for the amounts associated with direct obligations of the discontinued operations.

NOTE 13. SEGMENT INFORMATION

The following table sets forth certain information relating to the Company's consolidated continuing operations:

	1997	1996	1995
Operation information:			
Customer revenues —			
Electric — utility	**$ 634.1**	$ 589.5	$ 546.3
Gas — utility	**155.9**	165.6	139.2
Environmental and engineering services	**78.1**	84.8	88.6
Other	**51.1**	92.9	33.2
Operating income (loss) —			
Electric — utility	**$ 125.9**	$ 136.3	$ 134.2
Gas — utility	**13.7**	18.9	17.0
Environmental and engineering services	**(2.0)**	0.1	3.7
Other(a)	**(9.0)**	(12.2)	(8.3)
Investment information:			
Identifiable assets, including allocated common plant at December 31 —			
Electric — utility	**$1,245.2**	$1,225.3	$1,226.8
Gas — utility	**193.6**	262.1	250.6
Environmental and engineering services	**26.6**	33.5	38.1
Other	**396.4**	379.6	356.9
Other information:			
Construction, decommissioning and nuclear fuel —			
Electric — utility	**$ 123.8**	$ 125.9	$ 122.3
Gas — utility	**15.3**	18.0	16.9
Other	**14.2**	22.5	14.6
Depreciation and amortization expense —			
Electric — utility	**$ 91.2**	$ 74.5	$ 71.4
Gas — utility	**12.3**	9.8	9.6
Other	**7.8**	6.4	5.3

(a) Excludes the effects of affordable housing and historical tax credits of $6.2, $5.9 and $5.0 in 1997, 1996 and 1995, respectively.

NOTE 14. CARGILL JOINT VENTURE

In July 1997, the Company announced a joint venture with Cargill Incorporated to market electricity and risk management services to wholesale buyers. This joint venture, in which the Company has a 50% interest, is named Cargill-Alliant. The joint venture is accounted for using the equity method. As of December 31, 1997, the carrying amount of the investment was $4.7.

NOTE 15. SUBSEQUENT EVENT (Unaudited)

In April 1998, the Proposed Merger involving WPLH, IES and IPC was consummated and the Company was renamed Interstate Energy Corporation. For information regarding the terms of the Proposed Merger and selected unaudited pro forma financial data of Interstate Energy Corporation, see Note 2. The authorized common stock of Interstate Energy Corporation was increased from 100 million to 200 million shares at the effective date of the merger.

WPL HOLDINGS, INC.

IES INDUSTRIES INC.

INTERSTATE POWER COMPANY

(Merged as Interstate Energy Corporation, doing business as Alliant Corporation)

1997 SELECTED FINANCIAL AND OPERATING STATISTICS

Note: Certain reclassifications have been made to the 1993-1996 figures to conform with the 1997 presentation. In addition, other reclassifications have been made for consisteney purposes across the three companies.

WPL HOLDINGS, INC.

SELECTED FINANCIAL AND OPERATING STATISTICS

Financial Information

	1997	1996	1995	1994	1993
		(Dollars in thousands except for per share data)			
Income Statement Data:					
Operating revenues	**$ 919,255**	$ 932,844	$ 807,255	$ 795,717	$ 738,604
Operating expenses	**790,648**	789,794	660,702	666,537	610,660
Operating income	**128,607**	143,050	146,553	129,180	127,944
Income from continuing operations	**61,254**	73,205	71,618	66,424	63,685
Discontinued operations	**—**	(1,297)	(13,186)	(1,174)	(1,162)
Net income	**61,254**	71,908	58,432	65,250	62,523
Common Stock Data:					
Weighted average common shares outstanding ('000s)	**30,782**	30,790	30,774	30,671	29,681
Return on average common equity	**10.1%**	11.9%	9.8%	11.1%	11.7%
Per Share Data:					
Income from continuing operations	**$ 1.99**	$ 2.38	$ 2.33	$ 2.17	$ 2.15
Discontinued operations	**—**	$ (0.04)	$ (0.43)	$ (0.04)	$ (0.04)
Earnings per average common share (basic and diluted)	**$ 1.99**	$ 2.34	$ 1.90	$ 2.13	$ 2.11
Dividends declared per common share	**$ 2.00**	$ 1.97	$ 1.94	$ 1.92	$ 1.90
Book value at year-end	**$ 19.73**	$ 19.73	$ 19.41	$ 19.43	$ 19.15
Market value at year-end	**$ 33.13**	$ 28.13	$ 30.63	$ 27.38	$ 32.88
Other Selected Financial Data:					
Construction and acquisition expenditures	**$ 129,833**	$ 144,205	$ 129,698	$ 144,072	$ 171,134
Total assets at year-end	**$1,861,807**	$1,900,531	$1,872,414	$1,805,901	$1,761,899
Long-term obligations, net	**$ 526,023**	$ 487,165	$ 490,734	$ 507,917	$ 482,862
Times interest earned before income taxes	**3.19X**	3.82X	3.55X	3.81X	3.45X
Capitalization Ratios:					
Common stock	**54%**	59%	55%	54%	54%
Preferred and preference stock	**5%**	6%	5%	5%	6%
Long-term debt	**41%**	35%	40%	41%	40%
Total	**100%**	100%	100%	100%	100%

IES INDUSTRIES INC.

SELECTED FINANCIAL AND OPERATING STATISTICS

Electric Operating Information (Utility Only)

	1997	1996	1995	1994	1993
Operating Revenues ('000s):					
Residential	**$227,496**	$213,838	$217,351	$200,686	$206,562
Commercial	**162,626**	153,163	150,722	146,119	145,898
Industrial	**177,890**	160,477	148,529	143,965	137,595
Total from ultimate customers	**568,012**	527,478	516,602	490,770	490,055
Sales for resale	**25,719**	37,384	35,356	37,271	49,654
Other	**10,539**	9,411	8,513	9,286	10,812
Total	**$604,270**	$574,273	$560,471	$537,327	$550,521
Electric Sales ('000s MWH):					
Residential	**2,682**	2,642	2,690	2,494	2,528
Commercial	**2,378**	2,315	2,296	2,148	2,079
Industrial	**4,743**	4,436	4,248	4,015	3,674
Total from ultimate customers	**9,803**	9,393	9,234	8,657	8,281
Sales for resale	**794**	1,746	1,586	1,705	2,629
Other	**43**	46	50	67	64
Total	**10,640**	11,185	10,870	10,429	10,974
Customers (End of Period):					
Residential	**288,387**	286,315	284,154	281,653	279,187
Commercial	**48,962**	48,593	48,196	47,595	46,957
Industrial	**711**	703	695	706	677
Other	**442**	437	444	451	444
Total	**338,502**	336,048	333,489	330,405	327,265
Other Selected Electric Data:					
System capacity at time of peak demand (MW):					
Company-owned	**1,892**	1,864	1,873	1,741	1,734
Firm purchases and sales (net)	**232**	232	207	280	248
Total	**2,124**	2,096	2,080	2,021	1,982
Maximum peak hour demand (MW)	**1,854**	1,833	1,824	1,780	1,716
Sources of electric energy ('000s MWH):					
Steam	**5,499**	4,936	5,759	5,509	5,349
Nuclear	**2,904**	2,753	2,611	2,876	2,265
Hydroelectric	**8**	7	8	8	7
Purchases	**2,789**	4,177	3,013	2,647	3,949
Other	**156**	37	16	14	8
Total	**11,356**	11,910	11,407	11,054	11,578
Cooling degree days	**858**	766	1,093	846	765
Revenue per KWH from ultimate customers (in cents)	**5.79**	5.62	5.59	5.67	5.92

IES INDUSTRIES INC.

SELECTED FINANCIAL AND OPERATING STATISTICS

Financial Information

	1997	1996	1995	1994	1993
	(Dollars in thousands except for per share data)				
Income Statement Data:					
Operating revenues	**$ 930,699**	$ 973,912	$ 851,010	$ 785,864	$ 801,266
Operating expenses	**763,562**	807,346	697,676	637,931	649,997
Operating income	**167,137**	166,566	153,334	147,933	151,269
Net income	**66,337**	60,907	64,176	66,818	67,938
Common Stock Data:					
Weighted average common shares outstanding ('000s)	**30,380**	29,861	29,202	28,560	27,764
Return on average common equity(1)	**9.2%**	9.8%	10.7%	11.5%	12.9%
Per Share Data:					
Earnings per average common share (basic and diluted)	**$2.18**	$2.04	$2.20	$2.34	$2.45
Dividends declared per common share	**$2.10**	$2.10	$2.10	$2.10	$2.10
Book value at year-end(1)	**$26.76**	$20.84	$20.75	$20.56	$20.21
Market value at year-end	**$36.81**	$29.88	$26.50	$25.25	$31.25
Other Selected Financial Data:					
Construction and acquisition expenditures	**$ 171,125**	$ 238,378	$ 218,099	$ 206,548	$ 169,017
Total assets at year-end(1)	**$2,457,219**	$2,125,562	$1,985,591	$1,849,093	$1,699,819
Long-term obligations, net	**$ 882,421**	$ 744,298	$ 654,090	$ 623,359	$ 574,488
Times interest earned before income taxes	**2.66X**	2.99X	3.12X	3.38X	3.38X
Capitalization Ratios:					
Common stock(1)	**49%**	47%	49%	50%	51%
Preferred and preference stock	**1%**	1%	2%	2%	2%
Long-term debt	**50%**	52%	49%	48%	47%
Total	**100%**	100%	100%	100%	100%

(1) In the third quarter of 1997, IES Industries Inc. began adjusting the carrying value of its investment in McLeodUSA Inc. to its estimated fair value, pursuant to the applicable accounting rules. At December 31, 1997, the adjustment reflected an unrealized gain of approximately $298 million with a net of tax increase to other common equity of $174 million.

WPL HOLDINGS, INC.

SELECTED FINANCIAL AND OPERATING STATISTICS

Gas Operating Information (Utility Only)

	1997	1996	1995	1994	1993
Operating Revenues ('000s):					
Residential	**$ 84,513**	$ 90,382	$ 70,382	$ 71,555	$ 71,632
Commercial	**45,456**	46,703	35,411	38,516	37,993
Industrial	**8,378**	11,410	17,984	22,629	23,196
Transportation and other	**17,536**	17,132	15,388	6,946	4,449
Total	**$155,883**	$165,627	$139,165	$139,646	$137,270
Gas Sales ('000s Dekatherms):					
Residential	**12,770**	14,297	12,690	11,956	12,001
Commercial	**8,592**	9,167	8,245	8,128	7,994
Industrial	**1,714**	1,997	2,144	3,113	3,497
Transportation and other	**17,595**	18,567	16,870	9,279	8,487
Total	**40,671**	44,028	39,949	32,476	31,979
Customers at End of Period (Excludiug Transportation and Other):					
Residential	**137,827**	133,580	129,576	124,938	120,829
Commercial	**16,653**	16,083	15,724	15,270	14,826
Industrial	**488**	529	566	561	549
Total	**154,968**	150,192	145,866	140,769	136,204
Other Selected Gas Data:					
Heating degree days	**7,350**	8,124	7,431	7,170	7,351
Revenue per dekatherm sold (excluding transportation and other)	**$ 6.00**	$ 5.83	$ 5.36	$ 5.72	$ 5.65
Purchased gas costs per dekatherm sold (excluding transportation and other)	**$ 4.30**	$ 4.12	$ 3.64	$ 3.82	$ 3.85

WPL HOLDINGS, INC.

SELECTED FINANCIAL AND OPERATING STATISTICS

Electric Operating Information (Utility Only)

	1997	1996	1995	1994	1993
Operating Revenues ('000s):					
Residential	**$199,633**	$201,690	$199,850	$194,242	$184,176
Commercial	**107,132**	105,319	102,129	101,382	95,977
Industrial	**152,073**	143,734	140,562	140,487	132,903
Total from ultimate customers	**458,838**	450,743	442,541	436,111	413,056
Sales for resale	**160,917**	131,836	97,350	86,400	78,955
Other	**14,388**	6,903	6,433	9,236	11,176
Total	**$634,143**	$589,482	$546,324	$531,747	$503,187
Electric Sales ('000s MWH):					
Residential	**2,974**	2,980	2,938	2,777	2,751
Commercial	**1,878**	1,814	1,773	1,688	1,630
Industrial	**4,256**	3,986	3,873	3,765	3,540
Total from ultimate customers	**9,108**	8,780	8,584	8,230	7,921
Sales for resale	**5,824**	5,246	3,109	2,574	2,388
Other	**60**	57	54	55	52
Total	**14,992**	14,083	11,747	10,859	10,361
Customers (End of Period):					
Residential	**343,637**	336,933	329,643	322,924	316,870
Commercial	**46,823**	45,669	44,730	43,793	42,884
Industrial	**855**	815	795	776	714
Other	**1,875**	1,820	1,342	1,298	1,275
Total	**393,190**	385,237	376,510	368,791	361,743
Other Selected Electric Data:					
System capacity at time of peak demand (MW):					
Company-owned	**2,337**	2,300	2,176	2,193	2,019
Firm purchases and sales (net)	**145**	68	57	40	83
Total	**2,482**	2,368	2,233	2,233	2,102
Maximum peak hour demand (MW)	**2,253**	2,124	2,197	2,002	1,971
Sources of electric energy ('000s MWH):					
Steam	**8,587**	8,687	8,323	7,821	7,616
Nuclear	**970**	1,301	1,555	1,625	1,565
Hydroelectric	**234**	244	222	228	276
Purchases	**5,744**	4,494	2,227	1,786	1,488
Other	**121**	59	86	24	6
Total	**15,656**	14,785	12,413	11,484	10,951
Cooling degree days	**369**	408	982	637	630
Revenue per KWH from ultimate customers (in cents)	**5.04**	5.13	5.16	5.30	5.21

IES INDUSTRIES INC.

SELECTED FINANCIAL AND OPERATING STATISTICS

Gas Operating Iuformation (Utility Only)

	1997	1996	1995	1994	1993
Operating Revennes ('000s):					
Residential	**$110,663**	$ 97,708	$ 84,562	$ 82,795	$ 90,462
Commercial	**54,383**	46,966	40,390	40,912	45,528
Industrial	**13,961**	12,256	8,790	12,515	15,593
Transportation and other	**4,510**	3,934	3,550	2,811	2,735
Total	**$183,517**	$160,864	$137,292	$139,033	$154,318
Gas Sales ('000s Dekatherms):					
Residential	**16,317**	17,680	16,302	15,766	16,971
Commercial	**9,602**	10,323	9,534	9,298	10,133
Industrial	**3,318**	3,796	3,098	4,010	4,618
Transportation and other	**10,321**	10,341	10,871	8,901	7,284
Total	**39,558**	42,140	39,805	37,975	39,006
Customers at End of Period (Excluding Transportation and Other):					
Residential	**155,859**	154,457	152,873	151,367	152,472
Commercial	**21,431**	21,364	21,193	21,053	17,757
Industrial	**399**	417	404	409	490
Total	**177,689**	176,238	174,470	172,829	170,719
Other Selected Gas Data:					
Heating degree days	**6,685**	7,204	6,686	6,380	6,816
Revenue per dekatherm sold (excluding transportation and other)	**$ 6.12**	$ 4.94	$ 4.62	$ 4.69	$ 4.78
Purchased gas cost per dekatherm sold (excluding transportation and other)	**$ 4.33**	$ 3.27	$ 3.15	$ 3.28	$ 3.44

INTERSTATE POWER COMPANY

SELECTED FINANCIAL AND OPERATING STATISTICS

Financial Information

	1997	1996	1995	1994	1993
	(Dollars in thousands except for per share data)				
Income Statement Data:					
Operating revenues	**$331,847**	$326,084	$318,542	$307,650	$309,468
Operating expenses	**276,347**	265,755	250,630	264,215	265,677
Operating income	**55,500**	60,329	67,912	43,435	43,791
Net income	**26,699**	25,860	25,198	18,213	16,126
Common Stock Data:					
Weighted average common shares outstanding ('000s)	**9,725**	9,594	9,564	9,479	9,316
Return on average common equity	**12.7%**	12.8%	12.9%	9.5%	8.5%
Per Share Data:					
Earnings per average common share (basic and diluted)	**$2.74**	$2.69	$2.63	$1.92	$1.73
Dividends declared per common share	**$2.08**	$2.08	$2.08	$2.08	$2.08
Book value at year-end	**$22.09**	$21.31	$20.68	$20.13	$20.21
Market value at year-end	**$37.44**	$29.00	$33.13	$23.75	$30.13
Other Selected Financial Data:					
Construction and acquisition expenditures	**$ 28,888**	$ 30,997	$ 28,579	$ 41,098	$ 34,117
Total assets at year-end	**$638,749**	$639,200	$634,316	$628,845	$604,361
Long-term obligations, net	**$195,861**	$212,892	$212,931	$226,982	$227,024
Times interest earned before income taxes	**4.00X**	3.82X	3.75X	2.74X	2.70X
Capitalization Ratios:					
Common stock	**52%**	50%	47%	46%	44%
Preferred and preference stock	**8%**	8%	8%	8%	8%
Long-term debt	**40%**	42%	45%	46%	48%
Total	**100%**	100%	100%	100%	100%

INTERSTATE POWER COMPANY

SELECTED FINANCIAL AND OPERATING STATISTICS

Electric Operating Information

	1997	1996	1995	1994	1993
Operatiug Revenues ('000s):					
Residential	**$ 82,078**	$ 79,121	$ 80,870	$ 74,289	$ 72,432
Commercial	**50,550**	49,998	50,038	48,828	51,101
Industrial	**125,949**	124,515	123,620	116,645	111,540
Total from ultimate customers	**258,577**	253,634	254,528	239,762	235,073
Sales for resale	**5,710**	12,145	11,020	13,168	10,381
Other	**13,053**	10,841	9,325	8,800	10,305
Total	**$277,340**	$276,620	$274,873	$261,730	$255,759
Electric Sales ('000s MWH):					
Residential	**1,043**	1,046	1,077	1,005	1,000
Commercial	**740**	749	747	742	782
Industrial	**3,321**	3,244	3,239	3,090	2,927
Total from ultimate customers	**5,104**	5,039	5,063	4,837	4,709
Sales for resale	**150**	467	306	478	311
Other	**58**	58	59	60	62
Total	**5,312**	5,564	5,428	5,375	5,082
Cnstomers (End of Period):					
Residential	**132,580**	131,837	130,643	129,289	128,388
Commercial	**31,174**	31,164	30,860	30,829	30,650
Industrial	**989**	954	928	880	795
Other	**964**	950	963	985	937
Total	**165,707**	164,905	163,394	161,983	160,770
Other Selected Electric Data:					
System capacity at time of peak demand (MW):					
Company-owned	**1,028**	1,028	1,028	1,026	1,023
Firm purchases and sales (net)	**283**	283	283	283	273
Total	**1,311**	1,311	1,311	1,309	1,296
Maximum peak hour demand (MW)	**938**	996	1,011	932	927
Sources of electric energy ('000s MWH):					
Steam	**3,337**	3,391	3,524	3,409	3,282
Purchases	**2,127**	2,224	2,176	2,021	1,944
Other	**46**	45	17	15	16
Total	**5,510**	5,660	5,717	5,445	5,242
Cooling degree days	**926**	757	1,065	826	701
Revenue per KWH from ultimate customers (in cents)	**5.07**	5.03	5.03	4.96	4.99

INTERSTATE POWER COMPANY

SELECTED FINANCIAL AND OPERATING STATISTICS

Gas Operating Information

	1997	1996	1995	1994	1993
Operating Revenues ('000s):					
Residential	**$30,366**	$28,178	$24,817	$25,344	$28,791
Commercial	**16,019**	14,518	12,150	12,654	14,429
Industrial	**5,054**	3,903	3,688	5,283	6,235
Transportation and other	**3,068**	2,865	3,014	2,639	4,254
Total	**$54,507**	$49,464	$43,669	$45,920	$53,709
Gas Sales ('000s Dekatherms):					
Residential	**4,807**	5,188	4,835	4,725	4,957
Commercial	**2,948**	3,123	2,820	2,793	2,911
Industrial	**1,185**	1,063	1,139	1,586	1,557
Transportation and other	**28,803**	26,332	26,526	24,550	24,584
Total	**37,743**	35,706	35,320	33,654	34,009
Customers at End of Period (Excluding Transportation and Other):					
Residential	**44,270**	43,882	43,556	43,323	42,915
Commercial	**5,232**	5,211	5,178	5,173	5,088
Industrial	**76**	76	89	88	92
Total	**49,578**	49,169	48,823	48,584	48,095
Other Selected Gas Data:					
Heating degree days	**7,097**	8,083	7,452	7,115	7,466
Revenue per dekatherm sold (excluding transportation and other)	**$5.75**	$4.97	$4.62	$4.75	$5.25
Purchased gas costs per dekatherm sold (excluding transportation and other)	**$3.73**	$3.37	$2.94	$3.39	$4.06

Corporate Board of Directors

Lee Liu, 64 [1981] ▽*
Chairman of the Board
Retired President and Chief Executive Officer
IES Industries Inc.

Wayne H. Stoppelmoor, 63 [1986] ▽†
Vice Chairman of the Board
Retired President and Chief Executive Officer
Interstate Power Company

Erroll B. Davis Jr., 53 [1982]
President and Chief Executive Officer
Alliant Corporation
Madison, Wisconsin

Alan B. Arends, 64 [1993] □ ◆
President
Allied Benefit Group Financial Services, Corp.
Albert Lea, Minnesota

Rockne G. Flowers, 66 [1979] ◆* ▼
President and CEO
Nelson Industries, Inc.
Stoughton, Wisconsin

Joyce L. Hanes, 65 [1982] ●* ▲
Chairman of the Board
Midwest Wholesale, Inc.
Mason City, Iowa

Katharine C. Lyall, 56 [1986] ● ▲
President
University of Wisconsin System
Madison, Wisconsin

Arnold M. Nemirow, 54 [1991] □* ▼
Chairman, President and CEO
Bowater, Inc.
Greenville, South Carolina

Executive Group of the Alliant Family of Companies

ALLIANT CORPORATE OFFICERS

Erroll B. Davis Jr., 53 [1978]
President and Chief Executive Officer
Michaol R. Chase, 59 [1962]
Executive Vice President-Corporate Services
William D. Harvey, 48 [1986]
Executive Vice President-Generation
James E. Hoffman, 44 [1995]
Executive Vice President-Business Development
Eliot G. Protsch, 44 [1978]
Executive Vice President-Energy Delivery
Thomas M. Walker, 50 [1996]
Executive Vice President and Chief Financial Officer
John E. Ehright, 54 [1996]
Vice President-Controller
Edward M. Gleason, 57 [1977]
Vice President, Treasurer and Corporate Secretary
Donald D. Jannette, 55 [1966]
Assistant Corporate Secretary
Susan J. Kosmo, 51 [1986]
Assistant Controller
John E. Kratchmer, 35 [1985]
Assistant Controller

Richard R. Ewers,* 53 [1967]
Vice President-Sourcing and Support Services
Barbara J. Swan,* 46 [1987]
Vice President and General Counsel
Pamela J. Wegner,* 50 [1993]
Vice President-External Affairs and Administration
Joseph E. Shefchek,* 41 [1984]
Assistant Vice President-Environmental Affairs

* Those with an asterisk are not corporate officers; they are officers of Alliant Services, Inc., the company that provides internal services to the business units.

IES UTILITIES CORPORATE OFFICERS

Erroll B. Davis Jr., 53 [1978]
Chief Executive Officer
Eliot G. Protsch, 44 [1978]
President
John E. Ehright, 54 [1996]
Vice President-Controller
Dean E. Ekstrom, 50 [1985]
Vice President-Sales and Service
John F. Franz Jr., 58 [1992]
Vice President-Nuclear Operations
Edward M. Gleason, 57 [1977]
Vice President, Treasurer and Corporate Secretary
Dundeana K. Langer, 39 [1984]
Vice President-Customer Operations
David L. Wilson, 51 [1966]
Assistant Vice President-Nuclear Operations
Donald D. Jannette, 55 [1966]
Assistant Corporate Secretary
Steven F. Price, 45 [1984]
Assistant Treasurer
Robert A. Rusch, 35 [1989]
Assistant Treasurer
Daniel Siegfriod, 38 [1992]
Assistant Secretary

INTERSTATE POWER COMPANY CORPORATE OFFICERS

Erroll B. Davis Jr., 53 [1978]
Chief Executive Officer
Michaol R. Chase, 59 [1962]
President
John E. Ebright, 54 [1996]
Vice President-Controller
Dean E. Ekstrom, 50 [1985]
Vice President-Sales and Service

ALLIANT™

Interstate Energy Corporation doing business as Alliant Corporation

Alliant is a major energy-services corporation with growing national and international diversified operations. Headquartered in Madison, Wisconsin, Alliant and its subsidiaries provide electric, natural gas, water or steam energy to more than one million customers in four Midwestern states. Alliant also has diversified interests throughout the United States and in China and New Zealand.

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