INTEGRYS ENERGY GROUP, INC.
Form 10-K
February 26, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-K

(Mark One)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2008

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ________________ to ___________________

Commission File Number	Registrant; State of Incorporation; Address; and Telephone Number	IRS Employer Identification No.
1-11337	INTEGRYS ENERGY GROUP, INC. (A Wisconsin Corporation) 130 East Randolph Drive Chicago, IL 60601 800-699-1269	39-1775292

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $1 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes [X] No [ ]

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes [ ] No [X]

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer [X]	Accelerated filer [ ]
Non-accelerated filer [ ]	Smaller reporting company [ ]

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

State the aggregate market value of the voting and
non-voting common equity held by non-affiliates of the Registrant.

$3,884,606,353 as of June 30, 2008

Number of shares outstanding of each class
of common stock, as of February 25, 2009

Common Stock, $1 par value, 76,425,737 shares

DOCUMENT INCORPORATED BY REFERENCE

Definitive proxy statement for the Integrys Energy Group, Inc. Annual Meeting of Shareholders to be held on May 13, 2009 is incorporated by reference into Part III.

INTEGRYS ENERGY GROUP, INC.

ANNUAL REPORT ON FORM 10-K
For the Year Ended December 31, 2008

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Acronyms Used in this Annual Report on Form 10-K

AFUDC	Allowance for Funds Used During Construction
ATC	American Transmission Company LLC
EPA	United States Environmental Protection Agency
ESOP	Employee Stock Ownership Plan
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
GAAP	United States Generally Accepted Accounting Principles
IBS	Integrys Business Support, LLC
ICC	Illinois Commerce Commission
IRS	United States Internal Revenue Service
LIFO	Last-in, first-out
MERC	Minnesota Energy Resources Corporation
MGU	Michigan Gas Utilities Corporation
MISO	Midwest Independent Transmission System Operator, Inc.
MPSC	Michigan Public Service Commission
MPUC	Minnesota Public Utility Commission
N/A	Not Applicable
NSG	North Shore Gas Company
NYMEX	New York Mercantile Exchange
PEC	Peoples Energy Corporation
PEP	Peoples Energy Production Company
PGL	The Peoples Gas Light and Coke Company
PSCW	Public Service Commission of Wisconsin
SEC	United States Securities and Exchange Commission
SFAS	Statement of Financial Accounting Standards
UPPCO	Upper Peninsula Power Company
VBA	Volume Balancing Adjustment
WDNR	Wisconsin Department of Natural Resources
WPS	Wisconsin Public Service Corporation
WRPC	Wisconsin River Power Company

Forward-Looking Statements

In this report, Integrys Energy Group and its subsidiaries make statements concerning expectations, beliefs, plans, objectives, goals, strategies, and future events or performance. Such statements are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements are subject to assumptions and uncertainties; therefore, actual results may differ materially from those expressed or implied by such forward-looking statements. Although Integrys Energy Group and its subsidiaries believe that these forward-looking statements and the underlying assumptions are reasonable, they cannot provide assurance that such statements will prove correct.

Forward-looking statements include, among other things, statements concerning management's expectations and projections regarding earnings, regulatory matters, fuel costs, sources of electric energy supply, coal and natural gas deliveries, remediation costs, environmental and other capital expenditures, liquidity and capital resources, trends, estimates, completion of construction projects, and other matters.

Forward-looking statements involve a number of risks and uncertainties. Some risk factors that could cause results to differ from any forward-looking statement include those described in Item 1A of this Annual Report on Form 10-K for the year ended December 31, 2008. Other factors include:

- Resolution of pending and future rate cases and negotiations (including the recovery of deferred costs) and other regulatory decisions impacting Integrys Energy Group's regulated businesses;
- The impact of recent and future federal and state regulatory changes, including legislative and regulatory initiatives regarding deregulation and restructuring of the electric and natural gas utility industries and possible future initiatives to address concerns about global climate change, changes in environmental, tax, and other laws and regulations to which Integrys Energy Group and its subsidiaries are subject, as well as changes in the application of existing laws and regulations;
- Current and future litigation, regulatory investigations, proceedings, or inquiries, including but not limited to, manufactured gas plant site cleanup, reconciliation of revenues from the Gas Charge and related natural gas costs, and the contested case proceeding regarding the Weston 4 air permit;
- The impacts of changing financial market conditions, credit ratings, and interest rates on the liquidity and financing efforts of Integrys Energy Group and its subsidiaries;
- The risks associated with executing Integrys Energy Group's plan to significantly reduce the scope and scale of, or divest in its entirety, the nonregulated energy services business;
- The risks associated with changing commodity prices (particularly natural gas and electricity) and the available sources of fuel and purchased power, including their impact on margins;
- Resolution of audits or other tax disputes with the IRS and various state, local, and Canadian revenue agencies;
- The effects, extent, and timing of additional competition or regulation in the markets in which Integrys Energy Group's subsidiaries operate;
- The retention of market-based rate authority;
- The risk associated with the value of goodwill or other intangibles and their possible impairment;
- Investment performance of employee benefit plan assets;
- Advances in technology;

Effects of and changes in political and legal developments, as well as economic conditions and the related impact on customer demand;
Potential business strategies, including mergers, acquisitions, and construction or disposition of assets or businesses, which cannot be assured to be completed timely or within budgets;
The direct or indirect effects of terrorist incidents, natural disasters, or responses to such events;
The effectiveness of risk management strategies and the use of financial and derivative instruments;
The risks associated with the inability of Integrys Energy Group's and its subsidiaries' counterparties, affiliates, and customers to meet their obligations;
Weather and other natural phenomena, in particular the effect of weather on natural gas and electricity sales;

- The utilization of tax credit carryforwards;
- The effect of accounting pronouncements issued periodically by standard-setting bodies; and
- Other factors discussed elsewhere herein and in other reports filed by Integrys Energy Group from time to time with the SEC.

Except to the extent required by the federal securities laws, Integrys Energy Group and its subsidiaries undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

PART I

ITEM 1. BUSINESS

A. GENERAL

For purposes of this Annual Report on Form 10-K, unless the context otherwise indicates, when referring to "us," "we," "our" or "ours," we are referring to Integrys Energy Group, Inc. References to "Notes" are to the Notes to the Consolidated Financial Statements included in this Annual Report on Form 10-K.

Integrys Energy Group, Inc.

Integrys Energy Group is domiciled in the United States and was incorporated in Wisconsin in 1993. Integrys Energy Group is a holding company for its regulated utility and nonregulated business units.

Natural Gas Utility Segment

The natural gas utility segment includes the regulated natural gas utility operations of WPS, MGU, MER, PGL, and NSG. MGU and MER, both Delaware corporations, are domiciled in the United States and began operations upon acquisition of their natural gas distribution operations in Michigan and Minnesota, respectively, from Aquila, Inc. in April 2006 and July 2006, respectively. PGL and NSG, both Illinois corporations, are domiciled in the United States and began operations in 1855 and 1900, respectively. Integrys Energy Group acquired PGL and NSG in February 2007 in the PEC merger.

Electric Utility Segment

The electric utility segment includes the regulated electric utility operations of WPS and UPPCO. WPS, a Wisconsin corporation, is domiciled in the United States and began operations in 1883. UPPCO, a Michigan corporation, is domiciled in the United States and began operations in 1884. For the last three years, all of the electric utility segment's revenues were earned within the United States and all assets were located within the United States.

Integrys Energy Services

Integrys Energy Services, a Wisconsin corporation, is domiciled in the United States and was established in 1994. Integrys Energy Services is a diversified nonregulated natural gas and electric power supply and services company serving residential, commercial, industrial, and wholesale customers in certain developed competitive markets in the United States and Canada. Integrys Energy Services provides energy supply solutions, products, and strategies that enable customers to manage energy needs while capitalizing on opportunities resulting from deregulated markets.

See Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction,” for a discussion of the revised strategy for Integrys Energy Services going forward.

Holding Company and Other Segment

The Holding Company and Other segment includes the operations of the Integrys Energy Group holding company and the PEC holding company, along with any nonutility activities at WPS, MGU, MER, UPPCO, PGL, and NSG. Also included in the Holding Company and Other segment is WPS Investments, LLC, a nonutility company which holds an approximate 34% ownership interest in ATC. On December 31, 2008, WPS Investments was owned 82.9% by

Integrys Energy Group, 14.1% by WPS, and 3.0% by UPPCO. Equity earnings from our investments in ATC, WRPC, and Guardian Pipeline, LLC (prior to its sale in 2006) are included in the Holding Company and Other segment.

See Note 24, "Segments of Business," for information on Integrys Energy Group's foreign and domestic revenues, foreign and domestic long-lived assets, revenues from external customers, income (loss) available for common shareholders, and total assets by reportable segment.

B. REGULATED NATURAL GAS UTILITY OPERATIONS

Integrys Energy Group provides regulated natural gas utility service to Chicago and northern suburbs of Chicago, northeastern Wisconsin, adjacent portions of Michigan's Upper Peninsula, various cities and communities throughout Minnesota, and in the southern portion of lower Michigan.

Regulated Natural Gas Utility Segment Operating Statistics

	2008	2007	2006
Operating Revenues (Millions)			
Residential	$ 2,128.3	$ 1,441.7	$ 401.4
Commercial and industrial	668.0	481.2	218.3
Transportation	185.4	130.3	22.1
Other	44.2	50.5	35.1
Total	$ 3,025.9	$ 2,103.7	$ 676.9
Therms Delivered (Millions)			
Residential	1,708.9	1,251.8	351.5
Commercial and industrial	610.9	498.6	230.7
Other	28.6	47.1	27.6
Total therm sales	2,348.4	1,797.5	609.8
Transportation	1,834.0	1,505.6	657.5
Total	4,182.4	3,303.1	1,267.3
Customers Served (Approximate, end of period)			
Residential	1,489,800	1,497,000	620,500
Commercial and industrial	111,900	111,100	62,600
Transportation customers	68,200	64,100	900
Total	1,669,900	1,672,200	684,000
Average therm price (Cents)			
Residential	124.54	115.17	114.20
Commercial and industrial	109.35	96.51	94.63

Facilities

For information regarding our regulated natural gas facilities, see Item 2, "Properties," in this Annual Report on Form 10-K. For Integrys Energy Group's natural gas utility plant asset book value, see Note 4, "Property, Plant, and Equipment."

Natural Gas Supply

Integrys Energy Group's natural gas utilities manage portfolios of natural gas supply contracts, storage services, and pipeline transportation services designed to meet their varying load patterns at the lowest reasonable cost.

Integrys Energy Group's regulated natural gas subsidiaries contract for fixed-term firm natural gas supplies with various natural gas suppliers each year to meet the November through March winter period demand of firm system sales customers. Integrys Energy Group's regulated natural gas supply requirements are met through a combination of physical fixed price purchases, storage (contracted and

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owned), natural gas call options and physical index price purchases, and through the purchase of additional natural gas supplies on the monthly spot market through fixed-term firm contracts to supplement natural gas supplies and minimize risk. During periods of colder than normal weather, purchasing natural gas in the daily spot market may be necessary.

Integrys Energy Group's natural gas utilities contract with various underground storage facilities for underground natural gas storage capacity and have company-owned storage. Besides providing the ability to manage significant changes in daily natural gas demand, storage also provides Integrys Energy Group with the ability to purchase steady levels of natural gas on a year-round basis, thus lowering supply cost volatility.

For further information on Integrys Energy Group's regulated natural gas utility supply and transportation contracts, see Note 15, "Commitments and Contingencies."

The following table shows the expected design peak-day availability of natural gas in thousands of dekatherms (MDth) during the 2008 through 2009 heating season for Integrys Energy Group's natural gas utilities:

Source (MDth)	Design Peak-Day Availability	Year of Contract Expiration
Firm pipeline capacity	897	2009-2027
Firm city-gate supply	142	2009
Liquefied petroleum gas	40	N/A
Natural gas in storage:		
Contracted	1,136	2010-2028
Company-owned	1,150	N/A
Customer-owned	333	N/A
Total expected design peak-day availability	3,698	

Integrys Energy Group's natural gas utilities forecast design peak-day demand of 3,622 MDth for the 2008 through 2009 heating season. Design peak-day demand for WPS and MERC is associated with firm system sales customers only. Design peak-day demand for WPS includes 732 dekatherms per day of peak-day back-up service.

Regulatory Matters

Legislation and Regulation at State Level

The natural gas retail rates of Integrys Energy Group are regulated by the ICC, PSCW, MPSC, and MPUC. Under current regulatory practice, the ICC, PSCW, MPUC, and MPSC allow Integrys Energy Group's regulated natural gas utilities to pass the prudently incurred cost of natural gas on to customers on a one-for-one basis through purchased gas adjustment clauses. Changes in the cost of natural gas are reflected in both natural gas revenues and natural gas purchases, thus having little or no impact on net income.

Effective March 1, 2008, PGL and NSG received approval from the ICC for a four-year pilot program of a VBA decoupling mechanism that mitigates the impact of variations in weather from normal conditions and mitigates the impact of customer conservation. The VBA decoupling mechanism allows PGL and NSG to adjust rates going forward to recover or refund the difference between the actual and authorized margin impact of variations in volumes. (See Note 23, "Regulatory Environment," for further discussion of the PGL and NSG 2008 rate case and VBA decoupling mechanism.)

Effective January 1, 2009, WPS received approval from the PSCW for a four-year pilot program of a decoupling mechanism, which will allow WPS to adjust rates to recover or refund the difference between the actual and authorized margin impacts of variations in volumes. The PSCW approved this decoupling mechanism, with certain conditions, in the 2009 WPS rate case order. (See Note 23, "Regulatory Environment," for further discussion of the WPS 2009 rate case and the decoupling mechanism.)

All of Integrys Energy Group's utility subsidiaries are required to provide service and grant credit to customers within their service territories. The utilities are generally precluded from discontinuing service to residential customers during winter moratorium months.

Legislation and Regulation at Federal Level

Most of the natural gas distributed by Integrys Energy Group is transported to its distribution systems by interstate pipelines. The pipelines' services (transportation and storage) are regulated by the FERC under the Natural Gas Act and the Natural Gas Policy Act of 1978 (see "Natural Gas Supply" section above).

Under United States Department of Transportation regulations, the state commissions are responsible for monitoring the regulated natural gas utilities' safety compliance program for its pipelines under 49 Code of Federal Regulations (CFR) Part 192 (Transportation of Natural and Other Gas by Pipeline: Minimum Federal Safety Standards) and 49 CFR Part 195 (Transportation of Hazardous Liquids by Pipeline).

PGL utilizes its storage and transmission assets as a natural gas hub. This activity is regulated by the FERC and consists of providing wholesale transportation and storage services in interstate commerce.

For additional information, see Note 23, "Regulatory Environment."

Other Matters

Seasonality

The natural gas throughput of Integrys Energy Group's regulated natural gas utilities follows a seasonal pattern because the heating requirements of customers are temperature driven. Specifically, customers typically use more natural gas during the winter months. During 2008, the regulated natural gas utility segment recorded approximately 68% of its revenues from January through March and November through December.

Competition

Integrys Energy Group's regulated natural gas utility operations face competition with other entities and forms of energy in varying degrees, particularly for large commercial and industrial customers who have the ability to switch between natural gas and alternate fuels. Due to the volatility of natural gas prices, Integrys Energy Group has seen customers with dual fuel capability switch to alternate fuels for short periods of time, then switch back to natural gas as market rates change. Interruptible natural gas sales and natural gas transportation service is offered for customers to enable them to reduce their energy costs. Transportation customers purchase their natural gas directly from third-party natural gas suppliers and contract with one of Integrys Energy Group's natural gas utility entities to transport the natural gas from pipelines to their facilities. These purchases have little effect on net income because these transportation services provide margins similar to those applicable to conventional natural gas sales. Additionally, some customers still purchase their natural gas commodity directly from one of Integrys Energy Group's natural gas utility entities but have elected to do so on an interruptible basis, as a means to reduce their costs. Customers continue to switch between firm system supply, interruptible system supply, and transportation service each year as the economics and service options change.

Working Capital Requirements

The seasonality of natural gas revenues causes the timing of cash collections to be concentrated from January through June. A portion of the winter natural gas supply needs is typically purchased and stored from April through November. In addition, planned capital spending on the natural gas distribution facilities is concentrated in April through November. Because of these timing differences, the cash flow from customers is typically supplemented with temporary increases in short-term borrowings during the late summer and fall. Short-term debt is typically reduced over the January through June period.

C. REGULATED ELECTRIC UTILITY OPERATIONS

Integrys Energy Group's regulated electric utility operations are provided through WPS and UPPCO. WPS's regulated electric operations generate and distribute electric energy mainly to northeastern Wisconsin and a small portion of Michigan's Upper Peninsula. UPPCO provides electric energy in Michigan's Upper Peninsula. Wholesale electric service is provided to various customers, including municipal utilities, electric cooperatives, energy marketers, other investor-owned utilities, and municipal joint action agencies.

Both WPS and UPPCO are members of MISO, a FERC-approved, independent, non-profit organization, which operates a financial and physical electric wholesale market in the Midwest. WPS and UPPCO offer their generation and bid their customer load into the MISO market. MISO evaluates WPS's, UPPCO's, and other market participants' energy injections into, and withdrawals from, the system to economically dispatch the MISO system. MISO settles the participants' offers and bids based on locational marginal prices, which are market-driven values based on the specific time and location of the purchase and/or sale of energy.

Regulated Electric Utility Segment Operating Statistics

	2008	2007	2006
Operating revenues (Millions)			
Residential	$ 391.7	$ 381.8	$ 353.0
Commercial and industrial	649.6	607.0	548.8
Wholesale and other	287.6	257.3	197.6
Total	$ 1,328.9	$ 1,246.1	$ 1,099.4
Kilowatt-hour sales (Millions)			
Residential	3,064.5	3,173.6	3,144.8
Commercial and industrial	8,632.8	8,750.9	8,645.2
Wholesale and other	4,807.2	4,067.3	4,135.3
Total	16,504.5	15,991.8	15,925.3
Customers served (Approximate, end of period)			
Residential	426,500	424,400	421,000
Commercial and industrial	60,200	59,600	59,100
Wholesale and other	800	1,000	900
Total	487,500	485,000	481,000

In 2008, WPS reached a firm net design peak of 2,171 megawatts on July 15. As a result of continually reaching demand peaks in the summer months, primarily due to air conditioning load, the summer period is the most relevant for WPS's regulated electric utility capacity. WPS expects future supply reserves to meet the minimum planning reserve margin criteria through 2009 as required by the PSCW. The PSCW requires WPS to maintain a planning reserve margin above its projected annual peak demand forecast to help ensure reliability of electric service to its customers. In October 2008, the PSCW issued a written order to lower the reserve margin requirement from 18.0% to 14.5% for long-term planning (planning years two through ten). The PSCW also determined that the short-term planning (planning year one) reserve margin for Wisconsin utilities will follow the planning reserve margin established by MISO under Module E of its Open Access Transmission and Energy Markets Tariff. In 2008, UPPCO reached a firm net design peak of 174 megawatts on December 16. The MPSC has not established minimum guidelines for future supply reserves.

WPS and UPPCO had adequate capacity to meet all firm electric load obligations during 2008 and expect to have adequate capacity to meet all obligations during 2009.

Facilities

For a complete listing of Integrys Energy Group's regulated electric facilities, see Item 2, "Properties," in this Annual Report on Form 10-K. For Integrys Energy Group's electric utility plant asset book value, see Note 4, "Property, Plant, and Equipment."

Electric Supply

Electric Supply Mix

The sources of Integrys Energy Group's regulated electric supply were as follows:

Energy Source	2008		2007	
Company-owned generating plants				
Coal	59.6%		52.4%	
Hydroelectric	1.6%		1.3%	
Natural gas and fuel oil	1.2%		2.2%	
Wind	0.1%		0.1%	
Total company-owned generating plants		62.5%		56.0%
Purchased power				
Nuclear (Kewaunee Power Station)	16.5%		19.3%	
Natural gas (Fox Energy Center, LLC and Combined Locks Energy Center, LLC)	4.4%		3.4%	
Hydroelectric	2.3%		2.4%	
Other (including MISO)	14.3%		18.9%	
Total purchased power		37.5%		44.0%

Fuel Costs

The cost of fuel per generation of one million British thermal units (Btus) was as follows:

Fuel Type	2008	2007
Coal	$ 1.78	$ 1.47
Natural gas	9.74	7.36
Fuel oil	19.07	13.95

Coal Supply

Coal is the primary fuel source for WPS's regulated electric generation facilities, the majority of which is purchased from the Powder River Basin mines located in Wyoming. This low sulfur coal has been WPS's lowest cost coal source from any of the subbituminous coal-producing regions in the United States. WPS's regulated electric fuel portfolio strategy is to maintain a 25- to 40-day supply of coal at each plant site.

Historically, WPS has purchased coal directly from the producer for its wholly owned plants. Wisconsin Power and Light purchases coal for the jointly owned Edgewater and Columbia plants and is reimbursed by WPS for its share of the coal costs. At December 31, 2008, WPS had coal transportation contracts in place for 90% of its 2009 coal transportation requirements. For more information on coal purchases and coal deliveries under contract, see Note 15, "Commitments and Contingencies."

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Natural Gas Supply – Generation

WPS supplies natural gas through its natural gas distribution system to its approximately 437 megawatts of natural gas-fired combustion turbine generation facilities. In addition, WPS is committed through a power purchase agreement to provide fuel for 500 megawatts of the Fox Energy Center, a natural gas-fired combined cycle generation facility owned by a third party with a total combined electric capacity of approximately 600 megawatts. For more information on natural gas supply under contract, see Note 15, "Commitments and Contingencies."

In December 2008, WPS received approval from the PSCW to continue its Energy Market Risk Management Plan to govern its activities in the energy markets. The order extends WPS's authority to engage in activities to limit exposure to the volatility of natural gas prices affecting its electric generation, as well as to use financial transmission rights to manage energy congestion costs. The plan provides for the use of financial futures contracts for natural gas and the use of financial options that cap the price of natural gas for a portion of WPS's forecasted natural gas fuel generation requirements and natural gas price sensitive purchased power contracts.

Power Purchase Agreements

Integrys Energy Group's regulated electric facilities enter into short-term and long-term power purchase agreements to meet a portion of electric energy supply needs. The most significant of these is an agreement through 2013 with Dominion Energy Kewaunee, LLC to purchase energy and capacity from the Kewaunee Power Station consistent with volumes available when WPS owned the facility. For more information on power purchase obligations, see Note 15, "Commitments and Contingencies."

Regulatory Matters

Integrys Energy Group's electric utility operations are regulated by the PSCW, MPSC, and FERC. WPS's retail electric rates are regulated by the PSCW and MPSC, and UPPCO's retail electric rates are regulated by the MPSC. The FERC regulates wholesale electric rates for WPS and UPPCO. In 2008, retail electric revenues accounted for 79.5% of total electric revenues, while wholesale electric revenues accounted for 20.5% of total electric revenues.

The PSCW sets rates through its ratemaking process, which is based upon recovery of operating costs and a return on invested capital. One of the cost recovery components is fuel and purchased power, which is governed by a fuel window mechanism. Under the fuel window, if actual fuel and purchased power costs deviate by more than 2% from costs included in the rates charged to customers, a rate review can be triggered. Once a rate review is triggered, rates may be reset (subject to PSCW approval) for the remainder of the year to recover or refund, on an annualized basis, the projected increase or decrease in the cost of fuel and purchased power. The MPSC and FERC ratemaking processes are similar to those of the PSCW, with the exception of fuel and purchased power, which are recovered on a one-for-one basis.

Effective January 1, 2009, WPS received approval from the PSCW for a four-year pilot program of a decoupling mechanism, which will allow WPS to adjust rates to recover or refund the difference between the actual and authorized margin impacts of variations in volumes. The PSCW approved this decoupling mechanism, with certain conditions, in the 2009 WPS rate case order. (See Note 23, "Regulatory Environment," for further discussion of the WPS 2009 rate case and the decoupling mechanism.)

For additional information, see Note 23, "Regulatory Environment."

Hydroelectric Licenses

WPS, UPPCO, and WRPC (a company in which WPS has 50% ownership), have long-term licenses from FERC for all of their hydroelectric facilities.

In 2007, UPPCO decided to restore Silver Lake as a reservoir to support power generation, pending approval of an economically feasible design by the FERC. In November 2008, the construction phase at Silver Lake was completed and approved by the FERC. The project will be completed after the FERC approves the refill plan and the reservoir regains historical water levels.

For more information on Silver Lake, see Note 15, "Commitments and Contingencies."

Other Matters

Seasonality

Integrys Energy Group's regulated electric utility sales in Wisconsin generally follow a seasonal pattern due to the air conditioning requirements of customers that are primarily impacted by the variability of summer temperatures. Regulated electric utility sales in Michigan follow no significant seasonal trend due to cooler climate conditions in the Upper Peninsula of Michigan.

Generally, during the winter months, the purchase price of fuel (natural gas and fuel oil) for generation is heavily influenced by weather and the availability of baseload generation units within the MISO energy market. Sustained colder than normal weather and unexpected extended generation outages can influence fuel supply and demand, impacting the production costs at Integrys Energy Group's natural gas and oil-fired facilities, as well as natural gas supply commitments under power purchase agreements. For Integrys Energy Group's regulated electric utility segment, the impact on utility production costs is managed through WPS's Energy Market Risk Management Plan.

Competition

The retail electric utility market in Wisconsin is regulated by the PSCW. Retail electric customers currently do not have the ability to choose their electric supplier. However, in order to increase sales, utilities work to attract new commercial and industrial customers into their service territory. As a result, there is competition among utilities to keep energy rates low. Wisconsin utilities have continued to refine regulated tariffs in order to provide the true cost of electric energy to each class of customer by reducing or eliminating rate subsidies among different ratepayer classes. Although Wisconsin electric energy markets are regulated, utilities still face competition from other energy sources, such as self-generation by large industrial customers and alternative energy sources.

Michigan electric energy markets are open to competition; however, an active competitive market has not yet developed in the Upper Peninsula of Michigan, primarily due to a lack of excess generation and transmission system capacity.

D. INTEGRYS ENERGY SERVICES

Integrys Energy Services is a diversified nonregulated natural gas and electric power supply and services company serving residential, commercial, industrial, and wholesale customers in certain developed competitive markets in the United States and Canada. Integrys Energy Services provides energy supply solutions, products, and strategies that enable customers to manage energy needs while capitalizing on opportunities resulting from deregulated markets.

Integrys Energy Services and its subsidiaries market energy products in the retail market serving commercial and industrial customers, direct and "aggregated" small commercial and residential customers, as well as provide standard offer service. Aggregated customers are associations or groups of customers, which have joined together to negotiate purchases of electric or natural gas energy as a larger group.

In the wholesale market, Integrys Energy Services focuses on the execution and optimization of structured transactions with large end-users, regulated local distribution companies, generators, pipelines, storage companies, and other nonregulated energy marketing and trading companies.

Integrys Energy Services currently owns and operates electric generation facilities in the United States and Canada.

Integrys Energy Services is investing in and promoting renewable energy, which it believes is key to the future of the energy industry. Clean, renewable, and efficient energy sources are developed, acquired, owned, and operated by Integrys Energy Services. Integrys Energy Services assists customers with selecting an energy solution that is economically optimal and collaborates with energy developers of wholesale energy projects to overcome challenges with integrating the technical, regulatory, and financial aspects of their projects.

Integrys Energy Services utilizes derivative instruments, including forwards, futures, options and swaps, to manage its exposure to market risks and to extract additional value from its generation and energy contract portfolios in accordance with limits and approvals established in its risk management and credit policies. A diverse mix of products and markets, combined with disciplined execution and exit strategies, generally allows Integrys Energy Services to generate economic value and earnings from these activities while staying within the value-at-risk (VaR) limits authorized by Integrys Energy Group's Board of Directors. The Market Risk Oversight Committee, comprised of cross-functional members of management and senior leadership of Integrys Energy Services and its parent company, Integrys Energy Group, monitors compliance with these policies.

For more information on the trading and risk management activities of Integrys Energy Services, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Market Price Risk Management Activities."

See Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction,” for a discussion of the revised strategy for Integrys Energy Services going forward.

Recent Developments

As part of Integrys Energy Group's asset management strategy, Integrys Energy Services continually assesses its portfolio by reviewing opportunities regarding existing assets, the acquisition of assets, and contractual commitments to obtain resources that complement its existing business and strategy while maintaining an acceptable risk profile. This strategy calls for a focus on the disposition of assets, including plants and entire business units, which are either no longer strategic to ongoing operations, are not performing as needed, or have an unacceptable risk profile. Integrys Energy Services believes the following developments in the past five years have helped, or will help, manage assets and risk:

Acquisitions

- In 2008, Integrys Energy Services continued its development of renewable energy products by investing in 14 solar projects located throughout the United States and construction of a pipeline that will transport methane gas produced at a landfill for use at a chemical plant as a replacement for natural gas, scheduled to be in-service in 2009.
- In 2007, the merger with PEC combined the nonregulated energy marketing businesses of both companies. The combination created a stronger, more competitive, and better-balanced market position in the Illinois retail electric market and expanded its originated wholesale natural gas business.
- In 2007, Integrys Energy Services opened an office in Denver, Colorado, to expand its operation into the Western Systems Coordinating Council markets.
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In 2007, Integrys Energy Services initiated its renewable energy program by developing the Winnebago Energy Center, a landfill gas-to-electricity plant in Rockford, Illinois.

- In 2006, Integrys Energy Services developed a retail electric product offering in the Mid-Atlantic market (Pennsylvania, Delaware, Washington, D.C., Maryland, and New Jersey) as well as the Texas market.
- In 2004, Integrys Energy Services completed the acquisition of Advantage Energy, a privately held nonregulated electric power marketer based in Buffalo, New York. This acquisition provided enhanced opportunities to participate in the New York market and sell new products.

Dispositions

- In 2008, Integrys Energy Services sold its subsidiary Mid-American Power, LLC for approximately $5 million, which resulted in a pre-tax gain of $1.5 million. Mid-American Power, LLC owned the 44.5-megawatt Stoneman generation facility. In the fourth quarter of 2008, Integrys Energy Services recognized an additional pre-tax gain of $6.3 million on the sale of this facility as a component of discontinued operations when a previous contingent payment was earned and paid by the buyer. This contingent payment resulted from legislation that passed in the fourth quarter of 2008, which extended the production tax credits available for certain biomass facilities.
- In 2007, Integrys Energy Services sold WPS Niagara Generation, LLC for approximately $31 million. WPS Niagara Generation, LLC owned the 50.1-megawatt Niagara Falls generation facility located in Niagara Falls, New York. The pre-tax gain on the sale was approximately $25 million.
- In 2006, Integrys Energy Services completed the sale of Sunbury Generation, LLC for approximately $34 million. Sunbury Generation's primary asset was the Sunbury generation facility located in Pennsylvania. The pre-tax gain on the sale was approximately $20 million.
    - In 2006, Integrys Energy Services sold WPS ESI Gas Storage, LLC, which owned a natural gas storage field located in Michigan, for approximately $20 million. This facility was used for structured wholesale natural gas transactions as natural gas storage spreads arbitrage opportunities. The pre-tax gain on the sale was approximately $9 million.

See Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction,” for a discussion of the revised strategy for Integrys Energy Services going forward.

Integrys Energy Services' revenues, margin, operating income, volumes, and long-lived assets include the operations of Integrys Energy Services' Canadian subsidiaries and are reported as follows:

	2008	2007	2006
Revenues (Millions)			
United States	$ 7,326.7	$ 5,031.1	$ 3,177.0
Canada	2,408.5	1,948.6	1,982.1
Total	$ 9,735.2	$ 6,979.7	$ 5,159.1
Margin (Millions)			
United States	$ 64.9	$ 275.3	$ 148.3
Canada	20.8	28.8	32.8
Total	$ 85.7	$ 304.1	$ 181.1
Operating Income (Millions)			
United States	$ (131.8)	$ 100.9	$ 55.7
Canada	13.5	22.3	27.3
Total	$ (118.3)	$ 123.2	$ 83.0
Physical Electric Volumes (Million Kilowatt-Hours)			
United States	21,038.6	18,143.2	5,502.2
Canada	156.8	40.9	31.6
Total	21,195.4	18,184.1	5,533.8
Physical Natural Gas Volumes (Billion Cubic Feet)			
United States	655.8	522.7	408.2
Canada	275.1	242.3	229.3
Total	930.9	765.0	637.5
Long-Lived Assets (Millions)			
United States	$ 210.7	$ 168.3	
Canada	20.0	20.6	
Total	$ 230.7	$ 188.9	

Facilities

Generation

At December 31, 2008, Integrys Energy Services owned and operated electric generation facilities in the Midwest and Northeast regions of the United States with a total rated capacity of approximately 329 megawatts. In July 2008, Integrys Energy Services sold its subsidiary Mid-American Power, LLC, which owned the 44.5 megawatt Stoneman coal-fired, electric generating facility.

Integrys Energy Services' direct ownership of generation facilities allows for more efficient management of the market risk associated with its generation capabilities and related contracts to provide electric energy. Integrys Energy Services focuses on effective economic dispatch and risk management strategies in order to enhance the returns of its generation facilities.

A possible disposition of these assets is under consideration based on Integrys Energy Group implementing its strategic decision to either divest of this business segment or significantly reduce its size. See Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction,” for a discussion of the revised strategy for Integrys Energy Services going forward.

Renewable Energy

In response to customers' growing interest in sustainability and Integrys Energy Group's own concern for the environment, Integrys Energy Services is now focusing on delivering value-added energy services and renewable commodities to its wholesale and retail customers. New product offerings include Renewable

Energy Certificates, energy-efficiency programs that promote conservation, and development of green power generation projects.

Integrys Energy Services initially showed its commitment to a greener environment by developing the Winnebago Energy Center in 2007. The 6.4-megawatt plant captures methane gas produced by decomposing trash at a landfill, and the gas powers generators producing enough electricity to power about 5,000 homes while offering the potential to save nearly 590,000 barrels of oil a year.

In 2008, Integrys Energy Services continued its development of renewable energy products and focus on conservation by investing approximately $46 million in 14 solar projects located throughout the United States for a total capacity of 6.2 megawatts. Integrys Energy Services' business model offers clients solar-generated electric power without the need for any customer capital investment. Customers agree to purchase all the solar power produced at a price generally less than their current retail rate. These solar investments receive substantial tax benefits, including the Investment Tax Credit and accelerated tax depreciation. These projects may also benefit from attractive state incentive programs including rebates or Solar Renewable Energy Certificates.

In 2009, Integrys Energy Services, through its partially owned subsidiary, LGS Renewables I, LC, expects to complete construction of a pipeline, which will transport methane gas produced at a landfill for use at a chemical plant as a replacement for natural gas. As of December 31, 2008, Integrys Energy Services' investment in construction was approximately $17 million. For a complete listing of energy-producing facilities of Integrys Energy Services, see Item 2, "Properties."

Fuel Supply for Generation Facilities

Integrys Energy Services' fuel inventory policy varies for each generation facility depending on the type of fuel used and available natural gas storage facilities. In 2008, Integrys Energy Services' merchant coal-fired generation facilities consisted of its Westwood and Stoneman facilities until the Stoneman facility was sold in July 2008. Actual fuel needs in 2009 will depend on market conditions and operational capability of the Westwood facility. Integrys Energy Services' Westwood facility burns waste coal left behind by mining operations and has several year's supply on site. All fuel is located within a seven-mile radius of the plant.

Energy Supply

Physical supply obligations are created when Integrys Energy Services' wholesale and retail marketing groups execute forward sales contracts which may have fixed or variable volumes, or a combination thereof. Additionally, contracts may have fixed or variable pricing components. Whenever possible, any price risk is mitigated at the time the commitment is executed with the customer. Smaller contracts may remain open for short periods of time until a hedgeable volume has been sold.

Integrys Energy Services' electricity and natural gas supply requirements are primarily met through the procurement of natural gas and electricity in the wholesale markets. Only a small portion of its electricity supply requirements are met through owned generation. Integrys Energy Services does not own any reserves, so all natural gas supply is procured from producers and other suppliers in the wholesale markets.

Retail Electricity

The majority of Integrys Energy Services' obligations to provide physical electricity results from retail sales to commercial and industrial customers, many of which are full-requirements in nature. Integrys Energy Services uses a combination of bilateral electricity purchase agreements from generation companies and other marketers as well as regional power pools to meet those obligations. Integrys Energy Services employs load forecasting models populated with historical usage data and current weather and production assumptions to estimate the amount of electric supply to be acquired. Day-to-day shortfalls or overages are balanced out in the day ahead and real-time markets.

Wholesale Electricity

Wholesale supply obligations primarily result from the activities of Integrys Energy Services' electric origination operation. Sales to energy intermediaries such as local distribution companies (LDCs), municipalities, aggregators, and marketers require Integrys Energy Services to procure electric supply for fixed and variable volume contracts. Supply is acquired directly from merchant generation companies, electric utilities, marketers, and regional power pools. Some of Integrys Energy Services' supply contracts are unit contingent, which means that electricity is only provided to the extent that a specific generator is operational. Integrys Energy Services attempts to match unit contingent sales and supply contracts in order to reduce the risk of supply disruptions.

Retail Natural Gas

Physical natural gas supply obligations are created by the execution of forward sales contracts by Integrys Energy Services' retail marketing operation. Commercial and industrial customers, as well as some residential customers, make up the majority of its load requirements. Natural gas is sourced in the wholesale markets at the load zone, or in some cases is transported to the load zone using natural gas transportation contracts. Floating volume contracts are aggregated and modeled in order to estimate the load requirements taking into consideration the potential impact of weather and operational variability of the customer. Integrys Energy Services balances the differences between the actual sales demand or usage of customers and its block purchases by buying and selling any shortfall or excess in the spot market. Many of Integrys Energy Services' customers are also allotted storage capacity from their LDCs which Integrys Energy Services utilizes to manage daily load variability.

Wholesale Natural Gas

Integrys Energy Services' wholesale natural gas operation acquires physical supply as part of its asset optimization and trading program. When Integrys Energy Services signs sales contracts with wholesale origination customers such as utilities and other marketing companies, it hedges the majority of the price risk using financial contracts such as NYMEX futures and over-the-counter NYMEX swaps. The physical supply is acquired from producers or other suppliers at the load zone or is transported into the load zone using natural gas transportation contracts. Integrys Energy Services also contracts to store the natural gas it purchases in lower priced periods for sale in higher priced future periods. The usage and optimization of transportation and storage contracts ultimately results in more reliable and lower cost supply.

Regulatory Matters

Integrys Energy Services is a FERC-authorized power marketer and has received import/export authorization from the United States Department of Energy (DOE) and the Canadian National Energy Board (NEB). Integrys Energy Services on its own, or through certain of its subsidiaries, is registered to sell retail electric service in Connecticut, Delaware, District of Columbia, Illinois, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Texas, and Virginia in the United States, and in the provinces of Ontario and Alberta in Canada.

Integrys Energy Services, on its own, or through certain of its subsidiaries, is registered to sell natural gas in the states of Illinois, Iowa, Michigan, Ohio, Pennsylvania, New York and Alberta, Canada. Integrys Energy Services also sells natural gas in Wisconsin where no license is required. Integrys Energy Services' subsidiary, Integrys Energy Services of Canada Corp., is registered to do business in the Canadian provinces of Alberta, British Columbia, Manitoba, Nova Scotia, Ontario, Quebec, and Saskatchewan. Integrys Energy Services and Integrys Energy Services of Canada Corp. have a natural gas import/export permit through the DOE and the NEB.

Integrys Energy Services, or certain of its subsidiaries, are also members of the following regional transmission operators and North American Electric Reliability Council reliability regions:

- Alberta Electric System Operator;
- California Independent System Operator;
- Independent Electricity System Operator (located in Ontario);
- Electric Reliability Council of Texas;
- ISO New England;
- MISO;
- New Brunswick System Operator;
- New York Independent System Operator;
- Northeast Power Coordinating Council;
- Northern Maine Independent System Administrator;
- PJM Interconnection;
- ReliabilityFirst Corporation;
- SERC Reliability Corporation;
- Texas Regional Entity; and
- Western Systems Coordinating Council.

All the FERC hydroelectric facility licenses held by Integrys Energy Services' subsidiaries are current.

Other Matters

Customer Segmentation

As of December 31, 2008, Integrys Energy Services was delivering electricity and natural gas supply to customers in 20 states in the United States and 6 provinces in Canada. Integrys Energy Services periodically reviews and evaluates the profitability of its operations in each of these markets. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction," for a discussion of the revised strategy for Integrys Energy Services going forward.

As of December 31, 2008, Integrys Energy Services served electricity customers within 18 states in the United States and 2 Canadian provinces, including its largest markets in Illinois, Texas, and the northeastern United States. Integrys Energy Services served natural gas customers within 10 states in the United States and 6 Canadian provinces, including its largest markets in Illinois, Wisconsin, Michigan, Ohio, and Canada.

Although Integrys Energy Services is not dependent on any one customer, a significant percentage of its retail sales volume is derived from industries related to:

- Paper and allied products;
- Food and kindred products;
- Chemicals and paint;
- Steel and foundries; and
- Ethanol production facilities.

Seasonality

Integrys Energy Services believes that its business, in the aggregate, is not seasonal, even though certain products sell more heavily in some seasons than in others. Sales of natural gas generally peak in the winter months, while sales of electricity generally peak in the summer months. Generally in the summer months, the demand for electricity is high, which increases the price at which electricity can be sold. In

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periods of high residential fuel consumption (generally the winter months), the purchase price of oil and natural gas increases, which increases the production costs at Integrys Energy Services' natural gas- and oil-fired generation facilities. Integrys Energy Services' business can be volatile as a result of market conditions and the related market opportunities available to its customers.

Competition

Integrys Energy Services is a nonregulated energy marketer that competes against regulated utilities, energy marketers, and energy trading companies. Integrys Energy Services competes with other energy providers on the basis of price, reliability, customer service, product offerings, financial strength, consumer convenience, performance, and reputation.

The competitive landscape differs in each service area and within each targeted customer segment. For residential and small commercial customers, the primary competitive challenges come from the incumbent utility and affiliated utility marketing companies. The large commercial, institutional and industrial segments are very competitive in most markets with nearly all natural gas customers having already switched away from utilities to an alternative provider. National affiliated marketers, energy producers and other independent retail energy companies compete for customers in this segment.

The incumbent regulated utilities and the nationally-branded utility affiliates typically benefit from the economies of scale derived from the strength of substantial asset-based balance sheets, and vertically integrated business models that combine production, transmission, and distribution assets. These advantages are offset by the lack of flexibility to offer multiple product choices to their customers, while the nationally-branded utility affiliates struggle with long-term focus and cultural adaptation to a nonregulated market environment.

The local utilities have the advantage of long-standing relationships with their customers, and they have longer operating histories, greater financial and other resources, and greater name recognition in their markets than Integrys Energy Services does. In addition, local utilities have been subject to many years of regulatory oversight and thus have a significant amount of experience regarding the policy preferences of their regulators. Local utilities may seek to decrease their tariff retail rates to limit or preclude the opportunities for competitive energy suppliers and may seek to establish rates, terms, and conditions to the disadvantage of competitive energy suppliers.

Working Capital

The working capital needs of Integrys Energy Services vary significantly over time due to volatility in commodity prices, and related margin calls, levels of natural gas inventories, the structure of wholesale transactions, and the price of energy for natural gas and electricity. Integrys Energy Services' working capital needs are met by cash generated from operations, equity infusions, and debt (both long-term and short-term). Integrys Energy Services has access to its own credit line (up to $175 million) from independent financial institutions, and has the ability to borrow up to $400 million through an intercompany loan agreement with Integrys Energy Group. At December 31, 2008, Integrys Energy Group was authorized to provide aggregate guarantees for Integrys Energy Services' commodity and financial transactions up to $2.95 billion (which includes guarantees on the $175 million credit line). These guarantees provide the credit support needed to participate in the nonregulated energy market.

The capital and credit markets experienced extreme volatility, uncertainty, and disruption in 2008, which has continued into 2009. The strength and depth of competition in the nonregulated energy markets depends heavily on active participation by multiple trading parties, which could be adversely affected by disruptions in the capital and credit markets. Reduced capital and liquidity and failures of significant institutions that participate in the nonregulated energy markets could diminish the liquidity and competitiveness of those markets, which are important to the business of Integrys Energy Services.

See Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction,” for a discussion of the revised strategy for Integrys Energy Services going forward.

E. ENVIRONMENTAL MATTERS

For information on environmental matters related to Integrys Energy Group and any of its subsidiaries, see Note 15, "Commitments and Contingencies."

F. CAPITAL REQUIREMENTS

For information on capital requirements related to Integrys Energy Group, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources."

G. EMPLOYEES

Integrys Energy Group and its subsidiaries had 5,191 employees at December 31, 2008, of which approximately 44% were union employees. The reduction in the number of employees at Integrys Energy Group's subsidiaries listed below at December 31, 2008, compared with December 31, 2007, was primarily due to the 2008 formation of IBS, a wholly owned subsidiary of Integrys Energy Group. A significant portion of Integrys Energy Group's administrative employees were transferred to IBS on January 1, 2008. At December 31, 2008, IBS had 1,296 employees.

At December 31, 2008, WPS had 1,543 employees, of which approximately 64% were union employees represented by Local 310 of the International Union of Operating Electricians. The current Local 310 collective bargaining agreement expires on October 17, 2009.

At December 31, 2008, PGL had 1,085 employees, of which approximately 83% were union employees represented by Local 18007 of the Utility Workers Union of America. The current collective bargaining agreement with PGL union employees expires on April 30, 2013.

At December 31, 2008, MERC had 224 employees, of which approximately 19% were union employees represented by Local 31 of the International Brotherhood of Electrical Workers, AFL CIO. The current collective bargaining agreement expires on May 31, 2011.

At December 31, 2008, NSG had 168 employees, of which approximately 81% were union employees represented by Local 2285 of the International Brotherhood of Electrical Workers. The current collective bargaining agreement with NSG union employees expires on June 30, 2013.

At December 31, 2008, MGU had 167 employees, of which approximately 69% were union employees represented by Local 12295 of the United Steelworkers of America, AFL CIO CLC, and Local 417 of the Utility Workers Union of America, AFL CIO. The Local 12295 of the United Steelworkers of America, AFL CIO CLC, contract expires on January 15, 2010. The Local 417 of the Utility Workers Union of America, AFL CIO, collective bargaining agreement expires on February 15, 2012.

At December 31, 2008, UPPCO had 153 employees, of which approximately 78% were union employees represented by Local 510 of the International Brotherhood of Electrical Workers, AFL CIO. The current collective bargaining agreement expires on April 18, 2009. A new collective bargaining agreement has been reached and is effective April 19, 2009. The new agreement expires on April 12, 2014.

H. AVAILABLE INFORMATION

Integrys Energy Group files with the SEC its:

- Annual Report on Form 10-K;
- Quarterly Reports on Form 10-Q;
- Proxy statement;
- Registration statements, including prospectuses;
- Current Reports on Form 8-K; and
- Any amendments to these documents.

Integrys Energy Group makes these reports available, free of charge, on Integrys Energy Group's Internet website, www.integrysgroup.com, as soon as reasonably practicable after they are filed with the SEC. Integrys Energy Group's Code of Conduct may also be accessed on Integrys Energy Group's website, and any amendments to, or waivers from the Code of Conduct will be timely disclosed on Integrys Energy Group's website. Statements and amendments posted on Integrys Energy Group's website do not include access to exhibits and supplemental schedules electronically filed with the reports or amendments. Integrys Energy Group is not including the information contained on or available through its website as a part of, or incorporating such information by reference into, this Annual Report on Form 10-K.

You may also obtain materials filed with the SEC by Integrys Energy Group at the SEC Public Reference Room at 100 F Street, N.E., Washington, DC 20549. To obtain information on the operation of the Public Reference Room, you may call 1-800-SEC-0330. You may also view reports, proxy statements and other information regarding Integrys Energy Group (including exhibits), filed with the SEC, at the SEC's website at www.sec.gov.

ITEM 1A. RISK FACTORS

You should carefully consider the following risk factors, as well as the other information included or incorporated by reference in this Annual Report on Form 10-K, when making an investment decision. The risks and uncertainties described below are not the only ones Integrys Energy Group faces. Additional risks and uncertainties not presently known or that Integrys Energy Group currently believes to be immaterial may also adversely affect Integrys Energy Group.

Adverse capital and credit market conditions could negatively affect Integrys Energy Group's ability to meet liquidity needs, access capital, and/or grow or sustain its current businesses. Cost of capital and disruptions, uncertainty, and/or volatility in the financial markets could also adversely impact the results of operations and financial condition of Integrys Energy Group, as well as exert downward pressure on its stock price.

The capital and credit markets experienced extreme volatility, uncertainty, and disruption in 2008, which has continued into 2009. Having access to the credit and capital markets, at a reasonable cost, is necessary for Integrys Energy Group to fund its operations, including capital requirements. The capital and credit markets provide Integrys Energy Group with liquidity to operate and grow its businesses that is not otherwise provided from operating cash flows. The credit and capital markets also support the ability of Integrys Energy Group to provide credit support for the nonregulated operations of Integrys Energy Services. Disruptions, uncertainty, and/or volatility in those markets could increase Integrys Energy Group's cost of capital. If Integrys Energy Group or its subsidiaries are unable to access the credit and capital markets on terms that are reasonable, they may have to delay raising capital, issue shorter-term securities, and/or bear an increased cost of capital. This, in turn, could impact Integrys Energy Group's ability to grow or sustain its current businesses including its ability to provide adequate credit support for Integrys Energy Services, cause a reduction in earnings, and/or limit Integrys Energy Group's ability to sustain its current common stock dividend level.

The strength and depth of competition in the nonregulated energy markets depends heavily on active participation by multiple trading parties, which was adversely affected by disruptions in the capital and credit markets in 2008 and could continue to be affected in 2009. Reduced capital and liquidity and failures of significant institutions that participate in the nonregulated energy markets have diminished the liquidity and competitiveness of those markets and could continue to do so into 2009, which could negatively impact the business of Integrys Energy Services. These diminished markets have also increased counterparty credit risk.

A reduction in Integrys Energy Group's or its subsidiaries' credit ratings could materially and adversely affect their business, financial position, results of operations, and liquidity.

Integrys Energy Group cannot be sure that any of Integrys Energy Group's or its subsidiaries' credit ratings will remain in effect for any given period of time or that a credit rating will not be lowered by a rating agency if, in the rating agency’s judgment, circumstances in the future so warrant. Any downgrade could:

- Require the payment of higher interest rates in future financings and possibly reduce the potential pool of creditors;
- Increase borrowing costs under certain existing credit facilities;
- Limit access to the commercial paper market;
- Limit the availability of adequate credit support for Integrys Energy Services' operations; and
- Require provision of additional credit assurance, including cash margin calls, to contract counterparties.

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The failure to effectively execute Integrys Energy Group’s plan to significantly reduce the scope and scale, partially divest of, or fully divest of the nonregulated energy services business segment, Integrys Energy Services, could negatively impact the future results of operations and financial condition of Integrys Energy Group.

We cannot be certain that we will be able to execute our strategic decision for our nonregulated business segment in a timely manner. The process of selling assets or the full business segment, exiting markets, reducing operating costs, and managing exposures can result in increased risks, including but not limited to:

- A reduction in operating efficiencies, as operating margins may decline at a faster rate than the associated operating expenses;
- Potential loss of key employees during periods of increased employment uncertainty;
- A reduction in the value of the nonregulated business segment, including a potential corresponding negative impact on Integrys Energy Group;
- Lower customer retention rates at Integrys Energy Services due to short-term uncertainty about the ultimate outcome of the strategic decision;
- Losses on the disposition of specific assets, components of the business segment, or the entire business segment during this period of economic turmoil;
- Lower earnings capacity from this business segment going forward, which Integrys Energy Group may not be able to replace.

Refer to Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations – Introduction,” for a further discussion of the revised strategy for Integrys Energy Services.

Counterparties and customers may not meet their obligations.

Integrys Energy Group is exposed to the risk that counterparties to various arrangements who owe Integrys Energy Group money, energy, natural gas, coal or other commodities or services will not be able to perform their obligations. Should the counterparties to these arrangements fail to perform, Integrys Energy Group might be forced to replace or to sell the underlying commitment at then-current market prices. In such event, Integrys Energy Group might incur losses, or its results of operations, financial position, or liquidity could otherwise be adversely affected.

Some of Integrys Energy Group's customers are experiencing, or may experience, financial problems that could have a significant impact on their creditworthiness. Integrys Energy Group cannot provide assurance that its financially distressed customers will not default on their obligations to Integrys Energy Group and that such a default will not have a material adverse effect on Integrys Energy Group's business, financial position, results of operations, or cash flows. Furthermore, the bankruptcy of one or more of its customers, or some other similar proceeding or liquidity constraint, might make it unlikely that Integrys Energy Group would be able to collect all or a significant portion of amounts owed by distressed entities or residential customers. Such events could adversely impact Integrys Energy Group's receivable collections and additional allowances may be required, which could adversely affect its operating results. In addition, such events might force customers to reduce or curtail their future use of Integrys Energy Group's products and services, which could have a material adverse effect on Integrys Energy Group’s results of operations and financial condition.

The use of derivative instruments could result in financial losses and liquidity constraints.

Integrys Energy Group uses derivative instruments, including futures, forwards, options and swaps, to manage its commodity and financial market risks. Integrys Energy Group also purchases and sells commodity-based contracts in the natural gas and electric energy markets for trading purposes. Integrys Energy Group has in the past, and could in the future, recognize financial losses (on both an economic and GAAP basis) on these contracts as a result of volatility in the market values of the underlying commodities or if a counterparty fails to perform under a contract. Additionally, significant volatility in energy prices could adversely impact Integrys Energy Group's cash collateral requirements due to counterparty margin calls.

In the absence of actively quoted market prices and pricing information from external sources, the valuation of derivative contracts involves management's judgment or use of estimates. As a result, changes in the underlying assumptions or use of alternative valuation methods could affect the reported fair value of these contracts. Furthermore, realized values could differ from values determined by management.

For additional information concerning derivatives and commodity-based trading contracts, see Note 2, "Risk Management Activities."

Integrys Energy Group has recorded goodwill that could become impaired and adversely affect financial results.

The merger with PEC and the acquisition of natural gas distribution operations in Minnesota and Michigan are accounted for as purchases by Integrys Energy Group in accordance with GAAP. Under the purchase method of accounting, the assets and liabilities acquired were recorded at their respective fair values at the date of acquisition and added to those of Integrys Energy Group. As a result of the application of purchase accounting, these transactions resulted in a significant amount of goodwill. To the extent the value of goodwill or intangibles becomes impaired, Integrys Energy Group may be required to incur material charges relating to such impairment. Such an impairment charge could have a material impact on the financial results of Integrys Energy Group.

Integrys Energy Group is subject to changes in government regulation, which may have a negative impact on its businesses, financial position, and results of operations.

The rates that Integrys Energy Group's regulated utilities are allowed to charge for their retail and wholesale services are some of the most important items influencing its business, financial position, results of operations, and liquidity.

Integrys Energy Group is subject to comprehensive regulation by several federal and state regulatory agencies, which significantly influences its operating environment and may affect Integrys Energy Group's ability to recover costs from utility customers. In particular, the PSCW, ICC, MPSC, MPUC, FERC, SEC, EPA, Minnesota Office of Pipeline Safety, United States Department of Transportation, WDNR, and Illinois Environmental Protection Agency regulate many aspects of Integrys Energy Group's utility operations, including, but not limited to, construction of facilities, conditions of service, the issuance of securities, and the rates that it can charge customers. Integrys Energy Group is required to have numerous permits, approvals, and certificates from these agencies to operate its business.

Existing statutes and regulations may be revised or reinterpreted by these agencies or these agencies may adopt new laws and regulations that apply to Integrys Energy Group. Integrys Energy Group is unable to predict the impact on its businesses and operating results of any such actions by these agencies. However, changes in regulations or the imposition of additional regulations may require Integrys Energy Group to incur additional expenses or change business operations, which may have an adverse impact on results of operations. In addition, federal regulatory reforms may produce unexpected changes and costs in the public utility industry.

Any change in Integrys Energy Group's ability to sell electricity generated from its facilities at market based rates may impact earnings.

The FERC has authorized Integrys Energy Group to sell generation from certain of its facilities at market prices. The FERC retains the authority to modify or withdraw Integrys Energy Group's market based rate authority. If the FERC determines that the market is not workably competitive, that Integrys Energy Group possesses market power, or that it is not charging just and reasonable rates, it may require its subsidiaries to sell power at a price based upon the costs incurred in producing the power. Integrys Energy Group's revenues and profit margins may be negatively affected by any reduction by the FERC of the rates it may receive.

Integrys Energy Group may face significant costs to comply with the regulation of greenhouse gas emissions.

Climate change and the effect of greenhouse gas emissions, most notably carbon dioxide, are increasingly becoming a concern for the energy industry. While there is currently no federal regulation in the United States that mandates the reduction of greenhouse gas emissions, it is possible that such legislation may be enacted in the future. To that end, federal and state legislative proposals have been introduced to regulate the emission of greenhouse gases. Until legislation is passed at the federal or state level, it remains unclear as to (1) which industry sectors will be impacted, (2) when compliance will be required, (3) the magnitude of the greenhouse gas emissions reductions that will be required, and (4) the costs and opportunities associated with compliance. Integrys Energy Group is evaluating both the technical and cost implications which may result from future state, regional, or federal greenhouse gas regulatory programs, but at this time, it is uncertain as to the effect climate change regulation may have on Integrys Energy Group's future operations, capital expenditures, and financial results.

Based on the complexity and uncertainty of these issues, it is possible that future carbon regulation will increase the cost of electricity produced at coal-fired generation units and may affect the capital expenditures Integrys Energy Group would make at its generation units. At this time, there is no commercially available technology for removing carbon dioxide from a pulverized coal-fired plant. In addition, future legislation designed to reduce greenhouse gas emissions could make some of the generating units uneconomic to maintain or operate and could affect future results of operations, cash flows, and financial condition if such costs are not recoverable through regulated rates.

Integrys Energy Group's natural gas delivery systems may also generate fugitive gas as a result of normal operations and as a result of excavation, construction, and repair of natural gas delivery systems. Fugitive gas typically vents to the atmosphere and consists primarily of methane, a greenhouse gas.

Costs of environmental compliance, liabilities, fines, penalties, and litigation could exceed Integrys Energy Group's estimates.

Compliance with current and future federal and state environmental laws and regulations may result in increased capital, operating and other costs, including remediation and containment expenses and monitoring obligations. Integrys Energy Group cannot predict with certainty the amount and timing of all future expenditures (including the potential or magnitude of fines or penalties) related to environmental matters because of the difficulty of estimating clean-up and compliance costs and the possibility that changes will be made to the current environmental laws and regulations.

Integrys Energy Group's natural gas utility subsidiaries are accruing liabilities and deferring costs (recorded as regulatory assets) incurred in connection with their former manufactured gas plant sites, including related legal expenses, pending recovery through rates or from other entities. Regulatory assets reflect the net amount of (1) costs incurred to date, (2) carrying costs (excluding those for WPS), (3) amounts recovered from insurance companies, other entities and customers, and (4) management's best estimates of the costs Integrys Energy Group will spend in the future for investigating and remediating the manufactured gas plant sites. Integrys Energy Group believes that any of these costs that are not recoverable from other entities or from insurance carriers are recoverable through rates for utility services under approved mechanisms for the recovery of prudently incurred costs. A change in these rate recovery mechanisms, however, or a decision by the applicable state commission that some or all of these costs were not prudently incurred, could result in the present recognition as expense of some or all of these costs. For more information, see Note 15, "Commitments and Contingencies."

In addition, impacts resulting from future federal or state regulation regarding mercury, sulfur dioxide, and nitrogen oxide emissions are uncertain. There is also uncertainty in quantifying liabilities under environmental laws that impose joint and several liability on all potentially responsible parties.

Citizen groups that feel there are compliance issues not sufficiently enforced by environmental regulatory agencies may also bring citizen enforcement actions against Integrys Energy Group. Such actions could seek penalties, injunctive relief, and costs of litigation.

Poor investment performance of retirement plan investments and other factors impacting retirement plan costs could unfavorably impact Integrys Energy Group's liquidity and results of operations.

Integrys Energy Group has employee benefit plans that cover substantially all of its employees and retirees. Integrys Energy Group's cost of providing these benefit plans is dependent upon actual plan experience and assumptions concerning the future, such as earnings on and/or valuations of plan assets, discount rates, the level of interest rates used to measure the required minimum funding levels of the plans, future government regulation and required or voluntary contributions to the plans. Depending upon the investment performance over time and other factors impacting its costs (as listed above), Integrys Energy Group could be required to make larger contributions in the future to fund these plans. These additional funding obligations could have a material adverse impact on Integrys Energy Group's cash flows, financial condition, and/or results of operations. Changes made to the plans may also impact current and future pension and other postretirement benefit costs.

Fluctuating commodity prices may reduce energy margins.

Integrys Energy Group's regulated natural gas margins are sensitive to changes in natural gas commodity prices. Any changes could affect the prices the regulated natural gas utilities charge, their operating costs, and the competitive position of their products and services. Prudently incurred costs for purchased natural gas and pipeline transportation and storage services are fully recoverable through the annual reconciliation of revenues from the natural gas charge. However, increases in natural gas costs affect total retail prices and, therefore, the competitive position of Integrys Energy Group's natural gas business relative to other forms of energy. In addition, the timing and extent of high natural gas prices can adversely affect accounts receivable, bad debts, fuel cost, and interest expense. Integrys Energy Group is also subject to margin requirements in connection with its use of forward contracts and these requirements could escalate if prices move adversely relative to these positions.

Integrys Energy Group's regulated electric utility margins are directly affected by commodity costs related to coal, natural gas, and other fuels used in the electric generation process. Integrys Energy Group may experience increased expenses, including interest costs and bad debts, higher working capital requirements, and possibly reduction in demand as a result of any increase in the cost of fuel or purchased power.

Higher commodity prices result in increased energy prices that may impact customer demand for energy in the nonregulated market and increase counterparty and bad debt risk. This may stress margins at Integrys Energy Group's nonregulated subsidiaries. If market prices for electric energy decline below the cost of production at Integrys Energy Group's nonregulated facilities, these units may be temporarily shut down.

Integrys Energy Group's operations are subject to risks beyond our control, including but not limited to weather, terrorist attacks, or acts of war.

Integrys Energy Group's revenues are affected by the demand for electricity and natural gas. That demand can vary greatly based upon:

- Weather conditions, seasonality, and temperature extremes;
- Fluctuations in economic activity and growth in Integrys Energy Group's regulated service areas, as well as areas in which its nonregulated subsidiaries operate; and
- The amount of additional energy available from current or new competitors.

Weather conditions directly influence the demand for electricity and natural gas and affect the price of energy commodities.

In addition, the cost of repairing damage to Integrys Energy Group's facilities due to storms, natural disasters, wars, terrorist acts and other catastrophic events, that is in excess of insurance limits established for such repairs or excluded by insurance policies, may adversely impact Integrys Energy Group's results of operations, financial condition, and cash flows. The occurrence or risk of occurrence of future terrorist activity and the high cost or potential unavailability of insurance to cover such terrorist activity may impact Integrys Energy Group's results of operations and financial condition in unpredictable ways. These actions could also result in disruptions of power and fuel markets. In addition, Integrys Energy Group's natural gas distribution system and pipelines could be directly or indirectly harmed by future terrorist activity.

Actual results could differ from estimates used to prepare Integrys Energy Group's financial statements.

In preparing the financial statements in accordance with GAAP, management must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures at the date of the financial statements and during the reporting period. Some of those judgments can be subjective and complex and actual results could differ from those estimates. For more information about significant estimates and assumptions, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies."

Integrys Energy Group may not be able to utilize tax credit carryforwards.

Integrys Energy Group has significantly reduced its consolidated federal and state income tax liability in the past through tax credits and tax losses available under the applicable tax codes. Integrys Energy Group has not fully utilized these tax credits and tax losses in its previous tax filings, but expects to prior to their expiration in future filings. However, Integrys Energy Group may not be able to fully utilize the tax credits and tax losses available as carryforwards if its future federal and state taxable income and related income tax liability is insufficient to permit the use of such credits and losses.

In addition, any future disallowance of some or all of those tax credits or tax losses as a result of legislative change or adverse determination by one of the applicable taxing jurisdictions could materially affect Integrys Energy Group's tax obligations.

Integrys Energy Group is subject to provisions that can limit merger and acquisition opportunities for its shareholders.

The Wisconsin Public Utility Holding Company Law precludes the acquisition of 10% or more of the voting shares of a holding company of a Wisconsin public utility unless the PSCW has first determined that the acquisition is in the best interests of utility consumers, investors and the public. Those interests may, to some extent, be mutually exclusive. This provision and other requirements of the Wisconsin Public Utility Holding Company Law may delay, or reduce the likelihood of, a sale or change of control thus reducing the likelihood that shareholders will receive a takeover premium for their shares.

Provisions of Integrys Energy Group's articles of incorporation and by-laws may delay or frustrate the removal of incumbent directors and may prevent or delay a merger, tender offer or proxy contest involving Integrys Energy Group that is not approved by its board of directors, even if the shareholders believe that such events may be beneficial to Integrys Energy Group's interests. In addition, the Wisconsin Business Corporation Law contains provisions that may have the effect of delaying or making more difficult attempts by others to obtain control of Integrys Energy Group without the approval of its board of directors.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

A. REGULATED

Electric Facilities

The following table summarizes information on the electric generation facilities of Integrys Energy Group, including owned and jointly owned facilities as of December 31, 2008:

Type	Name	Location	Fuel	Rated Capacity (Megawatts)	(a)
Steam	Columbia Units 1 and 2	Portage, WI	Coal	355.6	(b)
	Edgewater Unit 4	Sheboygan, WI	Coal	101.9	(b)
	Pulliam (4 units)	Green Bay, WI	Coal	326.8	
	Weston Units 1, 2, and 3	Wausau, WI	Coal	471.2	
	Weston Unit 4	Wausau, WI	Coal	374.8	(b)
Total Steam				1,630.3	
Combustion	De Pere Energy Center	De Pere, WI	Natural Gas	170.4	
Turbine and	Eagle River	Eagle River, WI	Distillate Fuel Oil	4.2	
Diesel	Gladstone	Gladstone, MI	Oil	18.7	
	Juneau #31	Adams County, WI	Distillate Fuel Oil	6.3	(b)
	Oneida Casino	Green Bay, WI	Distillate Fuel Oil	3.5	
	Portage	Houghton, MI	Oil	17.6	
	Pulliam #31	Green Bay, WI	Natural Gas	81.2	
	West Marinette #31	Marinette, WI	Natural Gas	36.0	
	West Marinette #32	Marinette, WI	Natural Gas	34.2	
	West Marinette #33	Marinette, WI	Natural Gas	51.7	(b)
	Weston #31	Marathon County, WI	Natural Gas	16.9	
	Weston #32	Marathon County, WI	Natural Gas	46.8	
Total Combustion Turbine and Diesel				487.5	
Hydroelectric	Alexander	Lincoln County, WI			