MADISON GAS & ELECTRIC CO
Form 10-Q
August 07, 2012

United States

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended:

June 30, 2012

[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _______________ to _______________

Commission File No.	**Name of Registrant, State of Incorporation, Address of Principal Executive Offices, and Telephone No.**	**IRS Employer Identification No.**
000-49965	**MGE Energy, Inc.** (a Wisconsin Corporation) 133 South Blair Street Madison, Wisconsin 53703 (608) 252-7000 www.mgeenergy.com	39-2040501
000-1125	**Madison Gas and Electric Company** (a Wisconsin Corporation)	39-0444025

133 South Blair Street

Madison, Wisconsin 53703

(608) 252-7000

www.mge.com

Indicate by check mark whether the registrants (1) have 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) have been subject to such filing requirements for the past 90 days: Yes [X] No [ ]

Indicate by check mark whether the registrants have submitted electronically and posted on their corporate Web sites, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrants were required to submit and post such files):

Yes [X] No [ ]

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	**Accelerated Filer**	**Non-accelerated Filer**	**Smaller Reporting Company**
MGE Energy, Inc.	X			
Madison Gas and Electric Company			X	

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

MGE Energy, Inc. and Madison Gas and Electric Company: Yes [ ] No [X]

Number of Shares Outstanding of Each Class of Common Stock as of July 31, 2012

MGE Energy, Inc.	Common stock, $1.00 par value, 23,113,638 shares outstanding.
Madison Gas and Electric Company	Common stock, $1.00 par value, 17,347,894 shares outstanding (all of which are owned beneficially and of record by MGE Energy, Inc.).

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PART I. FINANCIAL INFORMATION.

Filing Format

This combined Form 10-Q is being filed separately by MGE Energy, Inc. (MGE Energy) and Madison Gas and Electric Company (MGE). MGE is a wholly owned subsidiary of MGE Energy and represents a majority of its assets, liabilities, revenues, expenses, and operations. Thus, all information contained in this report relates to, and is filed by, MGE Energy. Information that is specifically identified in this report as relating solely to MGE Energy, such as its financial statements and information relating to its nonregulated business, does not relate to, and is not filed by, MGE. MGE makes no representation as to that information. The terms "we" and "our," as used in this report, refer to MGE Energy and its consolidated subsidiaries, unless otherwise indicated.

Forward-Looking Statements

This report, and other documents filed by MGE Energy and MGE with the Securities and Exchange Commission (SEC) from time to time, contain forward-looking statements that reflect management's current assumptions and estimates regarding future performance and economic conditions especially as they relate to future load growth, revenues, expenses, capital expenditures, financial resources, regulatory matters, and the scope and expense associated with future environmental regulation. These forward-looking statements are made pursuant to the provisions of the Private Securities Litigation Reform Act of 1995. Words such as "believe," "expect," "anticipate," "estimate," "could," "should," "intend," and other similar words generally identify forward-looking statements. Both MGE Energy and MGE caution investors that these forward-looking statements are subject to known and unknown risks and uncertainties that may cause actual results to differ materially from those projected, expressed, or implied.

The factors that could cause actual results to differ materially from the forward-looking statements made by a registrant (a) include those factors discussed in the Registrants' 2011 Annual Report on Form 10-K: Item 1A. Risk Factors, as updated by Part II. Item 1A. Risk Factors in this Report, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations, as updated by Part I, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations in this report, and Item 8. Financial Statements and Supplementary Data Note 18, as updated by Part I, Item 1. Financial Statements Note 8 in this report, and (b) other factors discussed herein and in other filings made by that registrant with the SEC.

Readers are cautioned not to place undue reliance on these forward-looking statements, which apply only as of the date of this report. MGE Energy and MGE undertake no obligation to publicly release any revision to these forward-looking statements to reflect events or circumstances after the date of this report.

Where to Find More Information

The public may read and copy any reports or other information that MGE Energy and MGE file with the SEC at the SEC's public reference room at 100 F Street, NE, Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. These documents also are available to the public from commercial document retrieval services, the website maintained by the SEC at http://www.sec.gov, MGE Energy's website at http://www.mgeenergy.com, and MGE's website at http://www.mge.com. Copies may be obtained from our websites free of charge. Information contained on MGE Energy's and MGE's websites shall not be deemed incorporated into, or to be a part of, this report.

Definitions, Abbreviations, and Acronyms Used in the Text and Notes of this Report

Abbreviations, acronyms, and definitions used in the text and notes of this report are defined below.

<u>MGE Energy and Subsidiaries</u>:

MAGAEL	MAGAEL, LLC
MGE	Madison Gas and Electric Company
MGE Construct	MGE Construct, LLC
MGE Energy	MGE Energy, Inc.
MGE Power	MGE Power, LLC
MGE Power Elm Road	MGE Power Elm Road, LLC
MGE Power West Campus	MGE Power West Campus, LLC
MGE Transco	MGE Transco Investment, LLC

<u>Other Defined Terms</u>:

AFUDC	Allowance for Funds Used During Construction
ATC	American Transmission Company LLC
BART	Best Available Retrofit Technology
Blount	Blount Station
CAA	Clean Air Act
CAIR	Clean Air Interstate Rule
CAVR	Clean Air Visibility Rule
Codification	Financial Accounting Standards Board Accounting Standards Codification
Columbia	Columbia Energy Center
cooling degree days	Measure of the extent to which the average daily temperature is above 65 degrees Fahrenheit, which is considered an indicator of possible increased demand for energy to provide cooling
CSAPR	Cross-State Air Pollution Rule
CWA	Clean Water Act
CWDC	Central Wisconsin Development Corporation
DOE	U.S. Department of Energy
Dth	Dekatherms, a quantity measure used in respect of natural gas
Elm Road Units	Elm Road Generating Station
EPA	United States Environmental Protection Agency
ERISA	Employee Retirement Income Security Act
EGU	Electric Generating Unit
FASB	Financial Accounting Standards Board
FTR	Financial Transmission Rights
GHG	Greenhouse Gas
HAPs	Hazardous Air Pollutants
heating degree days (HDD)	Measure of the extent to which the average daily temperature is below 65 degrees Fahrenheit, which is considered an indicator of possible increased demand for energy to provide heating
IRS	Internal Revenue Service
kWh	Kilowatt-hour, a measure of electric energy produced
MACT	Maximum Achievable Control Technology
MAP-21	Moving Ahead for Progress in the 21st Century Act

MATS	Mercury and Air Toxics Standards
MISO	Midwest Independent System Operator (a regional transmission organization)
MW	Megawatt, a measure of electric energy generating capacity
MWh	Megawatt-hour, a measure of electric energy produced
NAAQS	National Ambient Air Quality Standards
NGCC	Natural Gas Combined Cycle
NO2	Nitrogen Dioxide
NOV	Notice of Violation
NOx	Nitrogen Oxides
NSPS	New Source Performance Standards
OPRB	Other Postretirement Benefits
PGA	Purchased Gas Adjustment clause, a regulatory mechanism used to reconcile natural gas costs recovered in rates to actual costs
PJM	PJM Interconnection, LLC (a regional transmission organization)
PM	Particulate Matter
PPA	Purchased power agreement
PSCW	Public Service Commission of Wisconsin
PSD	Prevention of Significant Deterioration
RICE	Reciprocating Internal Combustion Engine
SEC	Securities and Exchange Commission
SIP	State Implementation Plan
SO2	Sulfur Dioxide
Stock Plan	Direct Stock Purchase and Dividend Reinvestment Plan of MGE Energy
UW	University of Wisconsin at Madison
VIE	Variable Interest Entity
WCCF	West Campus Cogeneration Facility
WDNR	Wisconsin Department of Natural Resources
Working capital	Current assets less current liabilities
WPDES	Wisconsin Pollutant Discharge Elimination System
WPL	Wisconsin Power and Light Company
WPSC	Wisconsin Public Service Corporation

Item 1. Financial Statements.

MGE Energy, Inc.

Consolidated Statements of Income (unaudited)

(In thousands, except per-share amounts)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating Revenues:				
Regulated electric revenues	$ 96,339	$ 90,834	$ 186,275	$ 176,841
Regulated gas revenues	18,629	25,062	75,648	102,499
Nonregulated revenues	2,253	1,363	4,557	2,524
Total Operating Revenues	117,221	117,259	266,480	281,864
Operating Expenses:				
Fuel for electric generation	11,481	11,599	20,332	22,648
Purchased power	17,314	14,392	36,860	31,973
Cost of gas sold	7,801	13,052	42,646	63,999
Other operations and maintenance	41,278	40,657	84,227	80,070
Depreciation and amortization	9,712	10,357	19,336	20,373
Other general taxes	4,554	4,005	9,554	8,706
Total Operating Expenses	92,140	94,062	212,955	227,769
Operating Income	25,081	23,197	53,525	54,095
Other income, net	2,549	2,153	5,119	4,539
Interest expense, net	(4,764)	(5,055)	(9,868)	(9,905)
Income before income taxes	22,866	20,295	48,776	48,729
Income tax provision	(8,596)	(7,572)	(18,458)	(18,223)
Net Income	$ 14,270	$ 12,723	$ 30,318	$ 30,506
Earnings Per Share of Common Stock (basic and diluted)	$ 0.62	$ 0.55	$ 1.31	$ 1.32
Dividends per share of common stock	$ 0.383	$ 0.375	$ 0.766	$ 0.750
Average Shares Outstanding (basic and diluted)	23,114	23,114	23,114	23,114

MGE Energy, Inc.

Consolidated Statements of Comprehensive Income (unaudited)

(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	**2011**	**2012**	**2011**
Net Income	$ 14,270	$ 12,723	$ 30,318	$ 30,506
Other comprehensive income, net of tax:				
Unrealized gain on available-for-sale securities, net of tax ($24 and $6, and $29 and $54)	36	9	43	81
Reclassification of realized gain on available-for-sale securities, net of tax ($- and $10, and $-and $10)	-	(15)	-	(15)
Comprehensive Income	$ 14,306	$ 12,717	$ 30,361	$ 30,572

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

MGE Energy, Inc.

Consolidated Statements of Cash Flows (unaudited)

(In thousands)

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating Activities:		
Net income	$ 30,318	$ 30,506
Items not affecting cash:		
Depreciation and amortization	19,336	20,373
Deferred income taxes	14,657	9,263
Provision for doubtful receivables	1,207	1,013
Employee benefit plan expenses	9,222	6,818
Equity earnings in ATC	(4,484)	(4,267)
Other items	1,102	725
Changes in working capital items:		
Decrease in current assets	15,323	29,171
Decrease in current liabilities	(10,948)	(8,629)
Dividend income from ATC	3,494	3,327
Cash contributions to pension and other postretirement plans	(21,593)	(19,932)
Other noncurrent items, net	3,152	(945)
Cash Provided by Operating Activities	60,786	67,423
Investing Activities:		
Capital expenditures	(39,553)	(28,591)
Capital contributions to investments	(938)	(691)
Purchase of investment - land	(2)	(1,801)
Other	(338)	(90)
Cash Used for Investing Activities	(40,831)	(31,173)
Financing Activities:		
Cash dividends paid on common stock	(17,687)	(17,340)
Repayment of long-term debt	(29,334)	(1,167)
Issuance of long-term debt	28,000	30,000
Decrease in short-term debt	-	(22,500)
Other	(815)	(299)
Cash Used for Financing Activities	(19,836)	(11,306)
Change in Cash and Cash Equivalents:	119	24,944
Cash and cash equivalents at beginning of period	41,169	7,110
Cash and cash equivalents at end of period	$ 41,288	$ 32,054

Supplemental disclosures of cash flow information:

Significant noncash investing activities:		
Accrued capital expenditures	$ 4,779	$ 963

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

MGE Energy, Inc.

Consolidated Balance Sheets (unaudited)

(In thousands)

		June 30, 2012		December 31, 2011
ASSETS				
Current Assets:				
Cash and cash equivalents	$	41,288	$	41,169
Receivable - margin account		2,695		2,477
Accounts receivable, less reserves of $3,727 and $3,662, respectively		30,551		36,744
Other accounts receivable, less reserves of $616 and $439, respectively		5,381		5,318
Unbilled revenues		22,311		25,754
Materials and supplies, at average cost		16,875		14,758
Fossil fuel		8,928		5,468
Stored natural gas, at average cost		12,716		19,575
Prepaid taxes		21,242		22,251
Regulatory assets - current		9,643		7,347
Other current assets		7,056		8,270
Total Current Assets		178,686		189,131
Regulatory assets		235,570		205,835
Other deferred assets and other		6,830		8,018
Property, Plant, and Equipment:				
Property, plant, and equipment, net		969,707		961,511
Construction work in progress		53,434		34,055
Total Property, Plant, and Equipment		1,023,141		995,566
Investments		62,323		60,332
Total Assets	$	1,506,550	$	1,458,882
LIABILITIES AND CAPITALIZATION				
Current Liabilities:				
Long-term debt due within one year	$	2,667	$	2,667
Accounts payable		28,238		34,532
Accrued interest and taxes		4,131		4,085
Accrued payroll related items		7,789		9,987
Deferred income taxes		2,791		3,020
Derivative liabilities		10,180		4,568
Other current liabilities		6,324		4,215
Total Current Liabilities		62,120		63,074
Other Credits:				
Deferred income taxes		215,151		199,850
Investment tax credit - deferred		1,650		1,780
Regulatory liabilities		21,170		20,463
Accrued pension and other postretirement benefits		167,028		183,622
Derivative liabilities		69,570		34,908

Other deferred liabilities and other		46,076	43,330
Total Other Credits		520,645	483,953
Capitalization:			
Common shareholders' equity		563,626	550,952
Long-term debt		360,159	360,903
Total Capitalization		923,785	911,855
Commitments and contingencies (see Footnote 8)		-	-
Total Liabilities and Capitalization	$	1,506,550$	1,458,882

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

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MGE Energy, Inc.

Consolidated Statements of Common Equity (unaudited)

(In thousands, except per-share amounts)

	Common Stock		Additional Paid-in	Retained	Accumulated Other Comprehensive	
	Shares	Value	Capital	Earnings	(Loss)/Income	Total
2011						
Beginning balance - December 31, 2010	23,114	$ 23,114	$ 316,268	$ 185,556	$ 142	$ 525,080
Net income				30,506		30,506
Other comprehensive income					66	66
Common stock dividends declared ($0.750 per share)				(17,340)		(17,340)
Ending balance - June 30, 2011	23,114	$ 23,114	$ 316,268	$ 198,722	$ 208	$ 538,312
2012						
Beginning balance - December 31, 2011	23,114	$ 23,114	$ 316,268	$ 211,458	$ 112	$ 550,952
Net income				30,318		30,318
Other comprehensive income					43	43
Common stock dividends declared ($0.766 per share)				(17,687)		(17,687)
Ending balance - June 30, 2012	23,114	$ 23,114	$ 316,268	$ 224,089	$ 155	$ 563,626

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

Madison Gas and Electric Company

Consolidated Statements of Income (unaudited)

(In thousands)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating Revenues:				
Regulated electric revenues	$ 96,339	$ 90,834	$ 186,275	$ 176,841
Regulated gas revenues	18,629	25,062	75,648	102,499
Nonregulated revenues	2,253	1,363	4,557	2,524
Total Operating Revenues	117,221	117,259	266,480	281,864
Operating Expenses:				
Fuel for electric generation	11,481	11,599	20,332	22,648
Purchased power	17,314	14,392	36,860	31,973
Cost of gas sold	7,801	13,052	42,646	63,999
Other operations and maintenance	41,026	40,369	83,554	79,604
Depreciation and amortization	9,712	10,357	19,336	20,373
Other general taxes	4,554	4,005	9,554	8,706
Income tax provision	7,635	6,666	16,604	16,557
Total Operating Expenses	99,523	100,440	228,886	243,860
Operating Income	17,698	16,819	37,594	38,004
Other Income and Deductions:				
AFUDC - equity funds	310	116	464	203
Equity in earnings in ATC	2,242	2,170	4,484	4,267
Income tax provision	(975)	(950)	(1,968)	(1,756)
Other income, net	(186)	(274)	(130)	(161)
Total Other Income and Deductions	1,391	1,062	2,850	2,553
Income before interest expense	19,089	17,881	40,444	40,557
Interest Expense:				
Interest on long-term debt	5,073	5,223	10,270	10,214
Other interest, net	(148)	(105)	(141)	(252)
AFUDC - borrowed funds	(126)	(48)	(189)	(83)
Net Interest Expense	4,799	5,070	9,940	9,879
Net Income	$ 14,290	$ 12,811	$ 30,504	$ 30,678
Less Net Income Attributable to Noncontrolling Interest, net of tax	(6,080)	(5,992)	(12,152)	(11,925)
Net Income Attributable to MGE	$ 8,210	$ 6,819	$ 18,352	$ 18,753

Madison Gas and Electric Company

Consolidated Statements of Comprehensive Income (unaudited)

(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	**2011**	**2012**	**2011**
Net Income	$ 14,290	$ 12,811	$ 30,504	$ 30,678
Other comprehensive income (loss), net of tax:				
Unrealized gain (loss) on available-for-sale securities, net of tax ($5 and $2, and $15 and $21)	(7)	(3)	(23)	32
Reclassification of realized gain on available-for-sale securities, net of tax ($- and $10, and $- and $10)	-	(15)	-	(15)
Comprehensive Income	$ 14,283	$ 12,793	$ 30,481	$ 30,695
Less: Comprehensive income attributable to Noncontrolling Interest, net of tax	(6,080)	(5,992)	(12,152)	(11,925)
Comprehensive Income attributable to MGE	$ 8,203	$ 6,801	$ 18,329	$ 18,770

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

Madison Gas and Electric Company

Consolidated Statements of Cash Flows (unaudited)

(In thousands)

	Six Months Ended June 30, 2012	2011
Operating Activities:		
Net income	$ 30,504	$ 30,678
Items not affecting cash:		
Depreciation and amortization	19,336	20,373
Deferred income taxes	14,444	8,827
Provision for doubtful receivables	1,207	1,013
Employee benefit plan expenses	9,222	6,818
Equity earnings in ATC	(4,484)	(4,267)
Other items	1,367	1,017
Changes in working capital items:		
Decrease in current assets	13,822	28,916
Decrease in current liabilities	(11,589)	(9,687)
Dividend income from ATC	3,494	3,327
Cash contributions to pension and other postretirement plans	(21,593)	(19,932)
Other noncurrent items, net	2,961	(989)
Cash Provided by Operating Activities	58,691	66,094
Investing Activities:		
Capital expenditures	(39,553)	(28,591)
Capital contributions to investments	(888)	(621)
Other	(286)	406
Cash Used for Investing Activities	(40,727)	(28,806)
Financing Activities:		
Cash dividends paid to parent by MGE	(13,456)	(13,192)
Distributions to parent from noncontrolling interest	(8,500)	(37,000)
Equity contribution received by noncontrolling interest	888	622
Repayment of long-term debt	(29,334)	(1,167)
Issuance of long-term debt	28,000	30,000
Decrease in short-term debt	-	(3,500)
Other	(795)	(297)
Cash Used for Financing Activities	(23,197)	(24,534)
Change in Cash and Cash Equivalents:	(5,233)	12,754
Cash and cash equivalents at beginning of period	13,898	4,494
Cash and cash equivalents at end of period	$ 8,665	$ 17,248

Supplemental disclosures of cash flow information:			
Significant noncash investing activities:			
Accrued capital expenditures	$	4,779$	963

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

Madison Gas and Electric Company

Consolidated Balance Sheets (unaudited)

(In thousands)

		June 30, 2012	December 31, 2011
ASSETS			
Current Assets:			
Cash and cash equivalents	$	8,665	$ 13,898
Receivable - margin account		2,695	2,477
Accounts receivable, less reserves of $3,727 and $3,662, respectively		29,873	35,765
Affiliate receivables		670	605
Other accounts receivable, less reserves of $616 and $439, respectively		5,370	5,301
Unbilled revenues		22,311	25,754
Materials and supplies, at average cost		16,875	14,758
Fossil fuel		8,928	5,468
Stored natural gas, at average cost		12,716	19,575
Prepaid taxes		22,082	21,977
Regulatory assets - current		9,643	7,347
Other current assets		7,046	8,245
Total Current Assets		146,874	161,170
Affiliate receivable long-term		6,619	6,884
Regulatory assets		235,570	205,835
Other deferred assets and other		6,208	7,286
Property, Plant, and Equipment:			
Property, plant, and equipment, net		969,203	961,007
Construction work in progress		53,434	34,055
Total Property, Plant, and Equipment		1,022,637	995,062
Investments		59,395	57,556
Total Assets	$	1,477,303	$ 1,433,793
LIABILITIES AND CAPITALIZATION			
Current Liabilities:			
Long-term debt due within one year	$	2,667	$ 2,667
Accounts payable		28,238	34,532
Affiliate payables		1,491	2,152
Accrued interest and taxes		4,083	4,037
Accrued payroll related items		7,789	9,987
Deferred income taxes		2,856	3,020
Derivative liabilities		10,180	4,568
Other current liabilities		6,126	3,997
Total Current Liabilities		63,430	64,960
Other Credits:			
Deferred income taxes		211,529	196,550
Investment tax credit - deferred		1,650	1,780

Regulatory liabilities	21,170	20,463
Accrued pension and other postretirement benefits	167,028	183,622
Derivative liabilities	69,570	34,908
Other deferred liabilities and other	46,077	43,330
Total Other Credits	517,024	480,653
Capitalization:		
Common shareholder's equity	417,799	412,926
Noncontrolling interest	118,891	114,351
Total Equity	536,690	527,277
Long-term debt	360,159	360,903
Total Capitalization	896,849	888,180
Commitments and contingencies (see Footnote 8)	-	-
Total Liabilities and Capitalization	$ 1,477,303	$ 1,433,793

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

Madison Gas and Electric Company

Consolidated Statements of Common Equity (unaudited)

(In thousands)

	Common Stock		Additional		Accumulated Other	Non-	
			Paid-in	Retained	Comprehensive	Controlling	
	Shares	Value	Capital	Earnings	(Loss)/Income	Interest	Total
2011							
Beginning balance - Dec. 31, 2010	17,348	$ 17,348	$ 192,417	$ 192,480	$ 71	$ 141,993	$ 544,309
Net income				18,753		11,925	30,678
Other comprehensive income					17		17
Cash dividends paid to parent by MGE				(13,192)			(13,192)
Equity contribution received by noncontrolling interest						622	622
Distributions to parent from noncontrolling interest						(37,000)	(37,000)
Ending balance - June 30, 2011	17,348	$ 17,348	$ 192,417	$ 198,041	$ 88	$ 117,540	$ 525,434
2012							
Beginning balance - Dec. 31, 2011	17,348	$ 17,348	$ 192,417	$ 203,114	$ 47	$ 114,351	$ 527,277
Net income				18,352		12,152	30,504
Other comprehensive loss					(23)		(23)
Cash dividends paid to parent by MGE				(13,456)			(13,456)
Equity contribution received by noncontrolling interest						888	888
Distributions to parent from noncontrolling interest						(8,500)	(8,500)
	17,348	$ 17,348	$ 192,417	$ 208,010	$ 24	$ 118,891	$ 536,690

Ending balance -
June 30, 2012

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

MGE Energy, Inc., and Madison Gas and Electric Company

Notes to Consolidated Financial Statements (unaudited)

June 30, 2012

1.

Basis of Presentation - MGE Energy and MGE.

This report is a combined report of MGE Energy and MGE. References in this report to "MGE Energy" are to MGE Energy, Inc., and its subsidiaries. References in this report to "MGE" are to Madison Gas and Electric Company.

MGE Power Elm Road and MGE Power West Campus own electric generating assets and lease those assets to MGE. Both entities are variable interest entities under applicable authoritative guidance. MGE is considered the primary beneficiary of these entities as a result of contractual agreements. As a result, MGE has consolidated MGE Power Elm Road and MGE Power West Campus.

The accompanying consolidated financial statements as of June 30, 2012, and for the three and six months ended, are unaudited, but include all adjustments that MGE Energy and MGE management consider necessary for a fair statement of their respective financial statements. All adjustments are of a normal, recurring nature except as otherwise disclosed. The year-end consolidated balance sheet information was derived from the audited balance sheet appearing in MGE Energy's and MGE's 2011 Annual Report on Form 10-K, but does not include all disclosures required by accounting principles in the United States of America. These notes should be read in conjunction with the financial statements and the notes on pages 54 through 107 of the 2011 Annual Report on Form 10-K.

2.

Equity and Financing Arrangements.

a.

Common Stock - MGE Energy.

MGE Energy purchases stock in the open market for issuance pursuant to its Stock Plan. All MGE Energy common stock issued under the Stock Plan is sold pursuant to a registration statement that has been filed with the SEC and is currently effective.

MGE Energy can issue new shares of its common stock through the Stock Plan. For both the six months ended June 30, 2012 and 2011, MGE Energy did not issue any new shares of common stock under the Stock Plan.

b.

Dilutive Shares Calculation - MGE Energy.

MGE Energy does not hold any dilutive securities.

c.

Long-term Debt - MGE Energy and MGE.

On April 2, 2012, MGE issued $28 million in principal amount of its 4.38% senior notes, due April 1, 2042. The Notes were issued pursuant to a Note Purchase Agreement. The Notes are unsecured and are not issued under, or governed by, MGE's Indenture dated as of September 1, 1998, which governs MGE's Medium-Term Notes. MGE used the net proceeds from the sale of the Notes, together with other available corporate funds, to repay and retire on April 3, 2012, its obligations under a Loan Agreement dated as of April 1, 2002 with the City of Madison, Wisconsin, under which MGE received the net proceeds from the issuance of $28 million aggregate principal amount of 5.875% Series 2002A, Industrial Development Revenue Bonds that were issued by the City of Madison for MGE's benefit. The 5.875% Series 2002A Bonds were redeemed and retired on April 3, 2012, at 100% of their principal amount plus accrued interest with the proceeds of that loan repayment. Any interest savings in 2012 will be deferred.

d.

Remarketing of 4.875% Series 2002B, Industrial Development Revenue Bonds - MGE Energy and MGE.

On April 2, 2012, $19.3 million of 4.875% Series 2002B, Industrial Development Revenue Bonds were remarketed at an interest rate of 3.45%. The net proceeds of the 4.875% Series 2002B Bonds were originally loaned to MGE pursuant to a Loan Agreement dated as of April 1, 2002 with the City of Madison, which issued the Series 2002B Bonds in 2002. MGE is responsible for the payment of principal, premium, if any, and interest on the Bonds. The 4.875% Series 2002B Bonds were originally issued bearing an interest rate of 4.875% per annum for a period that ended April 1, 2012, at which point the Bonds were subject to mandatory tender by their holders and remarketing. The Series 2002B Bonds were remarketed and carry an interest rate of 3.45% per annum, which is payable semi-annually on April 1 and October 1, until their maturity on October 1, 2027. The Series 2002B Bonds are redeemable on or after April 1, 2017, at a redemption price equal to 100% of the principal amount of the Bonds to be redeemed, plus accrued interest to the redemption date.

3.

Investment in ATC - MGE Energy and MGE.

ATC owns and operates electric transmission facilities primarily in Wisconsin. MGE received an interest in ATC when it, like other Wisconsin electric utilities, contributed its electric transmission facilities to ATC. That interest is presently held by MGE Transco, which is jointly owned by MGE Energy and MGE.

MGE Transco has accounted for its investment in ATC under the equity method of accounting. For the six months ended June 30, 2012 and 2011, MGE Transco recorded equity earnings from the investment in ATC of $4.5 million and $4.3 million, respectively. Dividend income received from ATC was $3.5 million and $3.3 million for the six months ended June 30, 2012 and 2011, respectively. In addition, during the six months ended June 30, 2012 and 2011, MGE Transco made $0.9 million and $0.6 million in capital contributions to ATC, respectively.

MGE Energy and MGE's investment in ATC as of June 30, 2012, and December 31, 2011, was $58.9 million and $57.0 million, respectively.

At June 30, 2012, MGE is the majority owner, and MGE Energy, the holding company, is the minority owner of MGE Transco. MGE Energy's proportionate share of the equity and net income of MGE Transco is classified within the MGE financial statements as noncontrolling interest.

ATC's summarized financial data for the three and six months ended June 30, 2012 and 2011, is as follows:

(In thousands)	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating revenues	$ 152,171	$ 138,203	$ 299,833	$ 277,820
Operating expenses	(71,760)	(62,951)	(141,326)	(126,077)
Other expense, net	(327)	(134)	(827)	(492)
Interest expense, net	(20,776)	(19,479)	(40,277)	(41,376)
Earnings before members' income taxes	$ 59,308	$ 55,639	$ 117,403	$ 109,875

4.

Columbia Environmental Project Construction - MGE Energy and MGE.

MGE and two other utilities jointly own Columbia, a coal-fired generating facility. WPL is the plant operator and permit holder, and owns 46.2% of Columbia. WPSC owns a 31.8% interest, and MGE owns a 22% interest in Columbia. In early 2011, the PSCW issued a *Certificate and Order* authorizing the construction of scrubbers and bag houses and associated equipment on Columbia Units 1 and 2 to reduce SO_2 and mercury emissions. The scrubbers and bag houses are expected to support compliance obligations for current and anticipated air quality regulations, including CAIR or CSAPR, the Utility MACT Rule and the Wisconsin Mercury Rule. The operator's current estimate shows that MGE's share of the capital expenditures required for this project will be approximately $140 million. As of June 30, 2012, MGE had accumulated $25.1 million (excluding carrying costs) related to its share of the project, which is reflected in the Construction Work in Progress balance on MGE Energy's and MGE's consolidated balance sheets. MGE expects to incur capital expenditures as follows: $33 million for the remainder of 2012, $68 million in 2013, and $14 million in 2014. These amounts may change as a result of modifications to the project estimate or timing difference.

MGE expects that the costs pertaining to this project will be fully recoverable through rates. Additionally, MGE is entitled to a carrying cost on the related construction costs at 100% of the determined AFUDC rate.

5.

Taxes - MGE Energy and MGE.

a.

Accounting for Uncertainty in Income Taxes.

MGE Energy and MGE account for the difference between the tax benefit amount taken on prior year tax returns, or expected to be taken on a current year tax return, and the tax benefit amount recognized in the financial statements as an unrecognized tax benefit.

MGE Energy has adopted a tax method of accounting to accelerate tax deductions for repairs in accordance with Treasury Regulations and case law, as compared to the prior method of claiming tax depreciation on project costs. The method change for electric generation and transmission and distribution repairs was included on the 2009 tax return while the change for gas distribution repairs was included on the 2010 return. During 2011, the IRS issued guidance on the treatment of electric transmission and distribution repairs. This guidance prompted the reversal of a portion of the unrecognized tax benefits for these repairs during 2011. MGE Energy and MGE have an unrecognized tax benefit at June 30, 2012, and December 31, 2011, in the amount of $2.5 million and $2.4 million, respectively, for the tax uncertainty primarily related to the change in tax method of accounting for electric generation and gas distribution repairs.

b.

Effective Tax Rate.

MGE Energy's and MGE's effective income tax rate for the three and six months ended June 30, 2012, are 37.6% and 37.8%, respectively, compared to 37.3% and 37.4% for the same period in 2011. The higher effective tax rate is, in part, attributable to a lower estimated domestic manufacturing deduction.

6.

Pension and Other Postretirement Plans - MGE Energy and MGE.

MGE maintains qualified and nonqualified pension plans, health care, and life insurance benefits. Additionally, MGE has defined contribution 401(k) benefit plans.

The following table presents the components of MGE Energy's and MGE's net periodic benefit costs recognized for the three and six months ended June 30, 2012 and 2011. A portion of the net periodic benefit cost is capitalized within the consolidated balance sheets.

(In thousands)	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Pension Benefits				
Components of net periodic benefit cost:				
Service cost	$ 1,920	$ 1,514	$ 3,743	$ 3,054
Interest cost	3,321	3,030	6,475	6,110
Expected return on assets	(4,021)	(3,473)	(7,839)	(7,004)
Amortization of:				
Prior service cost	114	107	222	216
Actuarial loss	2,112	931	4,118	1,877
Net periodic benefit cost	$ 3,446	$ 2,109	$ 6,719	$ 4,253
Postretirement Benefits				
Components of net periodic benefit cost:				
Service cost	$ 606	$ 514	$ 1,253	$ 1,001
Interest cost	1,053	1,036	2,178	2,018
Expected return on assets	(407)	(418)	(842)	(814)
Amortization of:				
Transition obligation	99	113	206	219
Prior service cost	26	29	54	57
Actuarial loss	581	117	1,201	228
Net periodic benefit cost	$ 1,958	$ 1,391	$ 4,050	$ 2,709

The PSCW allowed MGE to defer the 2009 incremental pension and OPRB costs above the amounts recovered in rates. During the three months ended June 30, 2012 and 2011, $0.3 million and $0.7 million, respectively, has been recovered in rates. During the six months ended June 30, 2012 and 2011, $0.6 million and $1.3 million, respectively, has been recovered in rates. These costs are not reflected in the table above.

7.

Share-Based Compensation - MGE Energy and MGE.

Under MGE Energy's Performance Unit Plan, eligible participants may receive performance units that entitle the holder to receive a cash payment equal to the value of a designated number of shares of MGE Energy's common stock, plus dividend equivalent payments thereon, at the end of the set performance period.

In addition to units granted in 2008 through 2011, on February 17, 2012, 16,693 units were granted based on the MGE Energy closing stock price as of that date. These units are subject to a five-year graded vesting schedule. On the grant date, MGE Energy and MGE measure the cost of the employee services received in exchange for the award based on the current market value of MGE Energy common stock. The fair value of the awards has been subsequently re-measured at June 30, 2012, as required by applicable accounting standards. Changes in fair value have been recognized as compensation cost. Since this amount is re-measured quarterly throughout the vesting period, the compensation cost is subject to variability.

For nonretirement eligible employees, stock based compensation costs are accrued and recognized using the graded vesting method. Compensation cost for retirement eligible employees or employees that will become retirement eligible during the vesting schedule are recognized on an abridged horizon.

In April 2011, the MGE Energy Board approved an amendment to the outstanding awards under the Performance Unit Plan to provide for the continued vesting of those awards in the event of a bona fide retirement, provided the retired individual does not provide services to a competitor. The amendment did not change the number of performance units covered by any outstanding awards currently held by any of the participants.

As a result of the changes made by the amendment, the Company accelerated the recognition of costs associated with the outstanding awards resulting in a compensation-related charge of $0.5 million in the second quarter of 2011.

During both the six months ended June 30, 2012 and 2011, MGE recorded $0.8 million in compensation expense as a result of the Performance Unit Plan. In January 2012, cash payments of $0.6 million were distributed relating to awards that were granted in 2007 and became payable under the Performance Unit Plan. No forfeitures occurred during the six months ended June 30, 2012 or 2011. At June 30, 2012, $2.8 million of outstanding awards are vested.

8.

Commitments and Contingencies.

a.

Environmental - MGE Energy and MGE.

Water quality

Water quality regulations promulgated by the EPA and WDNR in accordance with the Federal Water Pollution Control Act, or more commonly known as the Clean Water Act (CWA), impose restrictions on emissions of various pollutants into surface waters. The CWA also regulates surface water quality issues that affect aquatic life, such as water temperatures, intake structures, and wetlands filling. The CWA regulates discharges from "point sources" such as power plants by establishing discharge limits in water discharge permits. MGE's power plants operate under Wisconsin Pollution Discharge Elimination System (WPDES) permits to ensure compliance with these discharge limits.

EPA Cooling Water Intake Rules (Section 316(b))

In April 2011, the EPA proposed and asked for public comment on standards to reduce entrainment (drawing aquatic life into a plant's cooling system) and impingement (trapping aquatic life on screens) from existing structures designed to take in cooling water for plants such as power plants. This rule is commonly referred to as Phase II of Section 316(b) of the CWA. Both our Blount and Columbia generating plants are subject to the impingement and entrainment aspects of the current proposed rule. Our WCCF plant is subject to the impingement aspect only. Under the current proposed rule, equipment would need to be installed at Blount, WCCF and Columbia to meet these new standards. The EPA has until June 27, 2013 to issue the final rule, pursuant to a recently announced settlement agreement. It is not presently possible to estimate the potential costs associated with the implementation of any of these initiatives because the rule has not been finalized.

WPDES Thermal Discharge Rule

WDNR rules to regulate thermal effluent discharges from point sources in Wisconsin became effective on October 1, 2010. We will need to meet the revised rule requirement as MGE's WPDES permits are issued or renewed. If we, in the cases of Blount and WCCF, or the plant operator, in the cases of Columbia and Elm Road, are unable to demonstrate that any of these permitted plants are able to comply with its associated WPDES permit requirements, then we may face operational controls and/or incur capital costs associated with plant modifications to meet discharge requirements. Those expenditures could be material, but would be anticipated to be recoverable in rates.

WPDES Phosphorus Nutrient Standards

In December 2010, the WDNR established water quality standards for phosphorus and effluent limitations for permitted discharges into specific waterbodies. Phosphorus limitations will be added to water effluent discharge permits as they are issued or renewed. The WDNR will be developing site-specific phosphorus limits. MGE's facilities subject to these standards include Blount, Columbia, Elm Road and WCCF. MGE may incur additional capital or operational expenditures and/or need to install additional pollution controls to meet the new phosphorus limits. MGE has, however, identified potential compliance options and believes compliance can be managed without significant capital investments.

Air quality

Air quality regulations promulgated by the EPA and the WDNR in accordance with the Federal Clean Air Act and the Clean Air Act Amendments of 1990 impose restrictions on emission of particulates, sulfur dioxide (SO_2), nitrogen oxides (NO_x), and other pollutants and require permits for operation of emission sources. These permits have been obtained by MGE and must be renewed periodically.

Various initiatives, including the EPA's recently finalized Cross-State Air Pollution Rule (CSAPR), maximum achievable control technology (MACT) standards, new source performance standards (NSPS) and the Clean Air Visibility Rule (also known as the Regional Haze Rule), as well as state mercury emissions limits, are expected to result in additional operating and capital expenditure costs for electric generating units.

Maximum Achievable Control Technology (MACT) for Utility Boilers (Also Referred to as the Mercury and Air Toxics Standards or MATS)

In December 2011, the EPA finalized its Mercury and Air Toxics Standards for coal and oil-burning electric generating unit (EGU) boilers. MATS will require emissions standards for mercury, non-mercury HAPs metals, and acid gases. MGE's Columbia and Elm Road Units are subject to MATS. The Elm Road Unit's current pollution controls and Columbia's planned mercury pollution controls are expected to allow both facilities to comply with the MATS rule (see the discussion regarding Columbia below).

Reciprocating Internal Combustion Engine (RICE) MACT

In December 2011, the EPA finalized its RICE MACT standard. RICE MACT applies to combustion turbines that contain a reciprocating internal combustion engine. Under the current RICE MACT, MGE may have to adjust its dispatching of several small generation units used for emergency and backup generation or install pollution controls. In June 2012, the EPA introduced a proposed rule that revised RICE MACT and introduced a New Source Performance Standard for RICE based on a settlement agreement with several power companies. MGE is currently reviewing the proposed rule and evaluating potential impacts associated with complying with the proposed RICE MACT.

Stay of EPA's Cross State Air Pollution Rule (CSAPR) and Reinstatement of the Clean Air Interstate Rule (CAIR)

The CAIR, which became effective in 2009, generally requires NO_x and SO_2 emission reductions from fossil fuel-fired electric generating units (25 MW or greater) (EGUs) in the eastern half of the United States in two phases and includes a regional cap-and-trade system. The first phase (currently in place) requires annual regional emission reductions from 2003 levels of 55% for NO_x and 40% for SO_2. The second phase (beginning in 2015) reduces regional NO_x and SO_2 emissions further from 2003 levels to 65% and 70%, respectively. MGE owns or has partial ownership in several generation units currently subject to the CAIR: Blount, Columbia, Elm Road, and its combustion turbines located in West Marinette and Fitchburg.

In December 2008, the U.S. Court of Appeals for the D.C. Circuit remanded the CAIR to the EPA for further review. In August 2011, the EPA published the Cross-State Air Pollution Rule (CSAPR) to replace the CAIR. Similar to the CAIR, CSAPR requires NO_x and/or SO_2 air emissions reductions by fossil fuel-fired EGUs (25 MW or greater) in 28 states in the eastern half of the U.S. CSAPR established state emission restrictions, referred to as budgets, for SO_2 and NO_x beginning in 2012 (Phase I). Under CSAPR, SO_2 emission budgets in certain states, including Wisconsin, will be lowered further in 2014 (Phase II). CSAPR affects the same electric generation units at MGE as CAIR: Blount, Columbia, Elm Road, and the combustion turbines at West Marinette and Fitchburg. Plants in Wisconsin that are subject to CSAPR have been allocated CSAPR emission allowances and will need to hold sufficient allowances to cover emissions on an annual basis. If CSAPR allowances are not adequate for a given plant, emissions will need to be reduced at the plant level by fuel-switching, installation of controls, curtailment of operations or a combination thereof. MGE's Columbia plant, which is operated by WPL (MGE has a 22% ownership interest), has significantly fewer SO_2 allocations under CSAPR in 2012 and 2013 than recent actual emissions.

In December 2011, the U.S. Court of Appeals for the D.C. Circuit stayed the implementation of CSAPR pending judicial review. The ruling leaves the CAIR in place while the court considers the merits and challenges to CSAPR. MGE expects to hold sufficient emissions allowances under the CAIR for 2012.

If CSAPR is reinstated in 2012 or 2013, the Columbia co-owners will need to evaluate and implement interim strategies to address anticipated SO_2 allowance deficiencies under CSAPR. Current analysis shows that, if reinstated in 2013, additional allowances (if available) may need to be purchased, Columbia generation may need to be reduced to comply with CSAPR limits, or a combination of these two strategies may be employed. These interim measures may increase MGE's costs. MGE expects that the costs of meeting CSAPR requirements will be fully recoverable through rates. Planned new SO_2 controls at Columbia are expected to be completed by mid 2014 (see the discussion regarding the Columbia Environmental Project below). Once the new environmental control project is completed at Columbia, it is expected that the plant will emit below anticipated CSAPR allocation levels.

Clean Air Visibility Rule (CAVR)

Air modeling indicates that SO_2 and NO_x emissions (and to a lesser extent particulate matter, or PM) from Columbia may impair visibility at certain Class I Scenic Areas and may therefore be subject to the best available retrofit technology (BART) regulations, a subsection of the EPA's Clean Air Visibility Rule (CAVR), which requires pollution retrofits. The EPA has proposed that compliance with CAIR and with CSAPR emissions limitations could also serve as compliance with BART for SO_2 and NO_x emissions. However, with the uncertainty regarding the future of CAIR and CSAPR, the future of BART regulation and compliance strategies and costs are also uncertain.

Wisconsin State Mercury Rule

Beginning January 1, 2015, phase two of the Wisconsin mercury rule will require large coal-fired electric generating units (larger than 150 MW) to reduce mercury emissions by 90%, or choose a multi-pollutant reduction approach, which allows a stepped approach to mercury reduction while reducing NO_x and SO_2 emissions at prescribed rates. Elm Road currently meets this requirement. The Columbia co-owners plan to meet the 90% reduction option by installing pollution controls needed to meet this and other rules (see the discussion regarding the Columbia Environmental Project below).

National Ambient Air Quality Standards (NAAQS)

The EPA has developed National Ambient Air Quality Standards (NAAQS) for six compounds currently identified as criteria pollutants: nitrogen dioxide (NO_2), particulate matter (PM), ozone, SO_2, lead and carbon monoxide. The NAAQS for criteria pollutants establish acceptable ambient air levels based on effects to human health and the environment, and changes to those NAAQS can affect compliance requirements and associated capital and operating costs. The EPA is required to review NAAQS every five years. MGE is currently tracking two NAAQS developments: (1) EPA's proposed changes to the PM2.5 NAAQS announced in June 2012, which would lower the primary annual limit and add a secondary PM2.5 standard pertaining to a measure of visibility, and (2) the WDNR attainment/nonattainment designations associated with the EPA's June 2010 final revisions to its SO_2 NAAQS. These two NAAQS developments could have a potential material effect on capital and maintenance costs at our generating facilities. However, the potential impact will not be known until implementation of the rules are finalized.

EPA's Prevention of Significant Deterioration and Title V Greenhouse Gas Tailoring Rule

The EPA's Greenhouse Gas "Tailoring Rule" regulates stationary sources for GHG emissions by "phasing in" over time different types of facilities subject to Prevention of Significant Deterioration (PSD) pre-construction program or Title V permitting (i.e. new facilities and existing facilities with certain qualifying modifications). MGE facilities may become subject to this rule if modifications at any facilities trigger PSD or if MGE invests in new facilities that trigger PSD.

GHG New Source Performance Standards for Electric Generating Units (EGU GHG NSPS)

On March 27, 2012, the EPA proposed greenhouse gas (GHG) New Source Performance Standards (NSPS) for coal fired and natural gas combined cycle (NGCC) electric generation units (EGUs). The proposal applies to new EGUs only; the EPA has stated that it does not intend for these rules to apply to modified or existing units at this time. The proposed NSPS may be finalized within 2012 and is not anticipated to significantly affect MGE's existing generation units.

Columbia

MGE and two other utilities jointly own Columbia, a coal-fired generating facility, which accounts for 225 MW (29%) of MGE's net summer generating capability. WPL is the plant operator and permit holder, and owns 46.2% of Columbia. Wisconsin Public Service Corporation (WPSC) owns a 31.8% interest, and MGE owns a 22% interest in Columbia. Based upon current available information, compliance with various environmental requirements and initiatives is expected to result in significant additional operating and capital expenditures at Columbia.

Columbia Environmental Project

In early 2011, the PSCW issued a *Certificate and Order* authorizing the construction of scrubbers and bag houses and associated equipment on Columbia Units 1 and 2 to reduce SO_2 and mercury emissions. The scrubbers and bag houses are expected to support compliance obligations for current and anticipated air quality regulations, including CAIR or CSAPR, the Utility MACT Rule and the Wisconsin Mercury Rule. The operator's current estimate shows that MGE's share of the capital expenditures required for this project will be approximately $140 million.

As of June 30, 2012, Columbia has entered into various contractual commitments with vendors for a portion of the $140 million project. MGE is indirectly a party to these agreements as a result of its joint ownership of Columbia and is also contractually obligated, under the applicable ownership and operating agreements. MGE's share of these commitments is $99.9 million. These costs are expected to be capitalized and included in the consolidated balance sheets of MGE Energy and MGE. See Footnote 4 for further information regarding the Columbia environmental construction project.

Title V Operating Permit Petition

In September 2008, the WDNR issued a Title V renewal operating permit to WPL for Columbia. A citizen group petitioned the EPA to object to the issuance of the permit renewal. In October 2009, the EPA issued an order granting in part and denying in part the petition and sent the operating permit back to the WDNR for further review based on the EPA order. The WDNR took various preliminary actions but has not yet fully responded to the EPA's order. In February 2011, the citizen group involved filed an action against the EPA in the U.S. District Court for the Western District of Wisconsin seeking to have the EPA take over the permit process. In June 2012, the EPA notified the plant operator of its intent to assume responsibility for issuing the renewed operating permit for Columbia, but agreed to provide the plant operator with more time to potentially resolve the issues raised in the EPA's order. MGE believes the permits currently in effect for Columbia remain in place at this time. MGE continues to follow these developments and is unable to predict the outcome of this matter and its impact on its operations or financial condition.

Columbia Clean Air Act Litigation

In December 2009, the EPA sent a Notice of Violation (NOV) to MGE as one of the co-owners of Columbia. The NOV alleges that WPL, as operator, and the Columbia co-owners failed to comply with appropriate pre-construction review and permitting requirements and as a result violated the PSD program requirements, Title V Operating Permit requirements of the CAA and the Wisconsin SIP.

In September 2010, Sierra Club filed a civil lawsuit against WPL alleging violations of the CAA at Columbia and other Wisconsin facilities operated by WPL. WPL has informed MGE that WPL believes the projects at Columbia were routine or not projected to increase emissions and therefore did not violate the permitting requirements of the CAA. MGE and the other co-owners of Columbia are defending against these allegations while actively pursuing settlement options with the EPA and Sierra Club.

MGE believes that the parties have reached a tentative agreement on the general terms of a settlement with the EPA and Sierra Club regarding various facilities, including Columbia. The Sierra Club has stipulated to dismissal of its lawsuit, without prejudice, while the parties attempt to reach a final settlement. The parties are currently negotiating a consent decree based upon those general terms, which may change during the negotiations. Based on a review of existing EPA consent decrees, the final consent decree could include the installation of emission control technology, changed operating conditions (including use of fuels other than coal and retirement of units), limitations on emissions, beneficial environmental mitigation projects, and a civil penalty.

Once the parties agree to the final terms, the Court must approve the settlement agreement. MGE cannot predict the outcome of these claims, but believes the outcome could be significant if the parties are unable to reach final agreement, or reach final agreement on different terms than currently anticipated, or if the Court does not approve the final settlement agreement and should there ultimately be an adverse outcome.

b.

Chattel Paper Agreement and Other Guarantees - MGE Energy and MGE.

MGE makes available to qualifying customers a financing program for the purchase and installation of energy-related equipment that will provide more efficient use of utility service at the customer's property. MGE is party to a chattel paper purchase agreement with a financial institution under which it can sell or finance an undivided interest with recourse, in up to $10.0 million of the financing program receivables, until July 31, 2013. At June 30, 2012, MGE has outstanding a $4.5 million interest in these receivables. MGE retains the servicing responsibility for these receivables. As of June 30, 2012, the servicing asset recognized by MGE is $0.2 million.

MGE accounts for servicing rights under the amortization method. Initial determination of the servicing asset fair value is based on the present value of the estimated future cash flows. The discount rate is based on the PSCW authorized weighted cost of capital.

MGE would be required to perform under its guarantee if a customer defaulted on its loan. The energy-related equipment installed at the customer sites is used to secure the customer loans. The loan balances outstanding at June 30, 2012, approximate the fair value of the energy-related equipment acting as collateral. The length of the MGE guarantee to the financial institution varies from one to ten years depending on the term of the underlying customer loan. Principal payments for the remainder of 2012 and the next four years on the loans are:

(In thousands)	**2012**	**2013**	**2014**	**2015**	**2016**
Chattel Paper	$ 284	$ 679	$ 494	$ 807	$ 732

c.

Purchase Power Agreement Contract Dispute - MGE Energy and MGE.

MGE is seeking resolution to a contract dispute regarding its Purchase Power Agreement with Riverside Energy Center LLC, a Calpine subsidiary, for capacity and energy from the Riverside Energy Center located in Beloit, Wisconsin. MGE declared the PPA terminated. Any savings in capacity costs that ultimately result from the termination of the Riverside PPA will flow through to the Company's customers. MGE is currently deferring amounts equal to the capacity payments MGE would be making under the terms of the Riverside PPA if it were still in effect. This deferral will create a liability to MGE's customers for a future credit, assuming MGE's right to terminate the PPA is ultimately upheld. If MGE does not prevail in the dispute, the capacity payment deferred will be paid to Riverside Energy Center, LLC.

d.

Other Legal Matters - MGE Energy and MGE.

MGE is involved in various other legal matters that are being defended and handled in the normal course of business. MGE maintains accruals for such costs that are probable of being incurred and subject to reasonable estimation. MGE has accrued for such matters in the financial statements. The ultimate outcomes of such matters are uncertain and may have an adverse effect on MGE Energy's and MGE's results of operations, financial position, or cash flows.

e.

Purchase Contracts - MGE Energy and MGE.

MGE Energy and MGE have entered into various commodity supply, transportation and storage contracts to meet their obligations to deliver electricity and natural gas to customers. As of June 30, 2012, the future commitments related to these purchase contracts were as follows:

(In thousands)		**2012**	**2013**	**2014**	**2015**	**2016**
Natural gas supply*(a)*	$	10,830$	12,266$	-$	-$	-
Purchase power*(b)*		39,266	51,455	49,372	47,523	48,491
	$	50,096$	63,721$	49,372$	47,523$	48,491

(a)

These commitments include market-based pricing. Management expects to recover these costs in future customer rates.

(b)

MGE has several purchase power agreements to help meet future electric supply requirements. Management expects to recover these costs in future customer rates.

f.

Smart Grid Investment Grant - MGE Energy and MGE.

MGE was approved in 2010 by the U.S. Department of Energy (DOE) under the federal stimulus program for a $5.5 million grant for smart grid projects. The DOE grant requires MGE to match the grant funding, bringing the total cost of the projects to more than $11 million. The projects involve the installation of technologies to boost efficiency, enhance service and improve reliability for customers. The stimulus grant is being used to fund the following projects: advanced metering infrastructure, plug-in hybrid electric vehicles support, and distribution management. As of June 30, 2012, MGE has spent $7.6 million related to these projects and has outstanding agreements to purchase $0.5 million in smart grid related products for the remainder of 2012.

g.

Other Commitments - MGE Energy.

On January 31, 2012, MGE Energy entered a subscription agreement to invest in a nonpublic venture capital fund. From time to time, this entity will require capital infusions from its investors. MGE Energy has committed to contribute $2.0 million in capital for such infusions. The timing of these infusions is dependent on the needs of the investee and is therefore uncertain at this time.

9.

Derivative and Hedging Instruments - MGE Energy and MGE.

a.

Purpose.

As part of its regular operations, MGE enters into contracts, including options, swaps, futures, forwards, and other contractual commitments, to manage its exposure to commodity prices and gas revenues. To the extent that these contracts are derivatives, MGE assesses whether or not the normal purchases or normal sales exclusion applies. For contracts to which this exclusion cannot be applied, MGE Energy and MGE recognize such derivatives in the consolidated balance sheets at fair value. The majority of MGE's derivative activities are conducted in accordance with its electric and gas risk management program, which is approved by the PSCW and limits the volume MGE can hedge with specific risk management strategies. The maximum length of time over which cash flows related to energy commodities can be hedged is four years. If the derivative qualifies for regulatory deferral, the derivatives are marked to fair value and are offset with a corresponding regulatory asset or liability. The deferred gain or loss is recognized in earnings in the delivery month applicable to the instrument. Gains and losses related to hedges qualifying for regulatory treatment are recoverable in gas rates through the PGA or in electric rates as a component of the fuel rules mechanism.

b.

Notional Amounts.

The gross notional volume of open derivatives is as follows:

	June 30, 2012	December 31, 2011
Commodity derivative contracts	460,825 MWh	482,545 MWh
Commodity derivative contracts	3,550,000 Dth	4,030,000 Dth
FTRs	5,587 MW	2,382 MW

c.

Financial Statement Presentation.

MGE Energy and MGE offset fair value amounts recognized for the right to reclaim collateral (a receivable) or the obligation to return collateral (a payable) against fair value amounts recognized for derivative instruments executed with the same counterparty under a master netting agreement. At June 30, 2012, and December 31, 2011, MGE Energy and MGE had $0.7 million and $3.0 million, respectively, in collateral that was netted against the net derivative positions with counterparties.

MGE purchases and sells exchange-traded and over-the-counter options, swaps, and future contracts. These arrangements are primarily entered into to help stabilize the price risk associated with gas or power purchases. These transactions are employed by both MGE's gas and electric segments. Additionally, as a result of the firm transmission agreements that MGE holds on transmission paths in the MISO and PJM markets, MGE holds FTRs. An FTR is a financial instrument that entitles the holder to a stream of revenues or charges based on the differences in hourly day-ahead energy prices between two points on the transmission grid. The fair values of these instruments are reflected as a regulatory asset/liability depending on whether they are in a net loss/gain position. Depending on the nature of the instrument, the gain or loss associated with these transactions will be reflected as cost of gas sold, fuel for electric generation, or purchased power expense in the delivery month applicable to the instrument. At June 30, 2012, the fair value of exchange traded derivatives and FTRs exceeded their cost basis by $0.4 million. At December 31, 2011, the cost basis of exchange traded derivatives and FTRs exceeded their fair value by $2.8 million.

MGE has also entered into a ten-year purchased power agreement that provides MGE with firm capacity and energy during a base term from June 1, 2012, through May 31, 2022. The agreement also allows MGE an option to extend the contract after the base term. The agreement is accounted for as a derivative contract and is recognized at its fair value on the balance sheet. However, the derivative qualifies for regulatory deferral and is recognized with a corresponding regulatory asset or liability depending on whether the fair value is in a loss or gain position. The fair value of the contract at June 30, 2012, and December 31, 2011, reflects a loss position of $79.8 million and $39.5 million, respectively. The actual fuel cost will be recognized in purchased power expense in the month of purchase.

The following table summarizes the fair value of the derivative instruments on the balance sheet. All derivative instruments in this table are presented on a gross basis and are calculated prior to the netting of instruments with the same counterparty under a master netting agreement as well as the netting of collateral. For financial statement purposes, MGE Energy and MGE have netted instruments with the same counterparty under a master netting agreement as well as the netting of collateral.

	Asset Derivatives			Liability Derivatives		
(In thousands)	Balance Sheet Location		Fair Value	Balance Sheet Location		Fair Value
June 30, 2012						
	Other current assets	$	727		$	1,151

Commodity derivative contracts				Derivative liability (current)		
Commodity derivative contracts	Other deferred charges		65	Derivative liability (long-term)		239
FTRs	Other current assets		986	Derivative liability (current)		-
Ten-year PPA	N/A		N/A	Derivative liability (current)		10,180
Ten-year PPA	N/A		N/A	Derivative liability (long-term)		69,570
December 31, 2011						
Commodity derivative contracts	Other current assets	$	177	Derivative liability (current)	$	3,060
Commodity derivative contracts	Other deferred charges		92	Derivative liability (long-term)		231
FTRs	Other current assets		186	Derivative liability (current)		-
Ten-year PPA	N/A		N/A	Derivative liability (current)		4,600
Ten-year PPA	N/A		N/A	Derivative liability (long-term)		34,920

The following tables summarize the unrealized and realized gains (losses) related to the derivative instruments on the balance sheet at June 30, 2012 and 2011, and the income statement for the three and six months ended June 30, 2012 and 2011.

	2012		2011	
(In thousands)	Current and long-term regulatory asset	Other current assets	Current and long-term regulatory asset	Other current assets
Three Months Ended June 30:				
Balance at April 1,	$ 71,514	$ 672	$ 21,677	$ 505
Change in unrealized loss	9,791	-	888	-
Realized loss reclassified to a deferred account	(222)	222	(610)	610
Realized gain (loss) reclassified to income statement	(1,721)	(176)	649	(114)
Balance at June 30,	$ 79,362	$ 718	$ 22,604	$ 1,001
Six Months Ended June 30:				
Balance at January 1,	$ 42,356	$ 1,604	$ 19,230	$ 1,411
Change in unrealized loss	43,101	-	3,936	-
Realized loss reclassified to a deferred account	(2,880)	2,880	(1,274)	1,274
Realized gain (loss) reclassified to income statement	(3,215)	(3,766)	712	(1,684)
Balance at June 30,	$ 79,362	$ 718	$ 22,604	$ 1,001

		Realized losses (gains)	
(In thousands)	Regulated gas revenues	Fuel for electric generation/ purchased power	Cost of gas sold
Three Months Ended June 30, 2012:			
Commodity derivative contracts	$ -	$ 582	$ -
FTRs	-	96	-
Ten-year PPA	-	1,219	-
Three Months Ended June 30, 2011:			
Commodity derivative contracts	$ -	$ 90	$ -
FTRs	-	(625)	-
Ten-year PPA	-	-	-
Six Months Ended June 30, 2012:			
Commodity derivative contracts	$ -	$ 2,510	$ 3,090
FTRs	-	162	-
Ten-year PPA	-	1,219	-

Six Months Ended June 30, 2011:			
Commodity derivative contracts	$ -	$ 28	$ 1,315
FTRs	-	(371)	-
Ten-year PPA	-	-	-

MGE's commodity derivative contracts, FTRs, and ten-year PPA are subject to regulatory deferral. These derivatives are marked to fair value and are offset with a corresponding regulatory asset or liability. Realized gains and losses are deferred on the balance sheet and are recognized in earnings in the delivery month applicable to the instrument. As a result of the above described treatment, there are no unrealized gains or losses that flow through earnings.

The ten-year PPA has a provision that may require MGE to post collateral if MGE's debt rating falls below investment grade (i.e., below BBB-). The amount of collateral that it may be required to post varies from $20.0 million to $40.0 million, depending on MGE's nominated capacity amount. As of June 30, 2012, no collateral has been posted. Certain counterparties extend MGE a credit limit. If MGE exceeds these limits, the counterparties may require collateral to be posted. As of June 30, 2012, and December 31, 2011, no counterparties were in a net liability position.

Nonperformance of counterparties to the non-exchange traded derivatives could expose MGE to credit loss. However, MGE enters into transactions only with companies that meet or exceed strict credit guidelines, and it monitors these counterparties on an ongoing basis to mitigate nonperformance risk in its portfolio. As of June 30, 2012, no counterparties have defaulted.

10.

Rate Matters - MGE Energy and MGE.

a.

Rate Proceedings.

On March 23, 2012, MGE filed an application with the PSCW requesting a 5.8% increase to electric rates and a 2.6% increase to gas rates. The proposed electric increase will cover costs for new environmental equipment at Columbia, final construction costs for the Elm Road Units (including the prudence of construction costs incurred above a previously approved cap), transmission reliability enhancements, and purchased power costs. MGE has requested that these rates become effective January 1, 2013.

On December 15, 2011, under a limited reopener of MGE's last rate order, the PSCW authorized MGE to increase 2012 rates for retail electric customers by 4.3% or $15.7 million and to increase gas rates by 0.3% or $0.6 million. The change in retail electric rates was driven by MGE's electric fuel and purchased power costs, increased transmission costs, an update to the Elm Road Units' costs, and an increase for energy efficiency programs. The PSCW also approved deferral of CSAPR costs.

On January 12, 2011, the PSCW authorized MGE to increase 2011 rates for retail electric customers by 2.3% or $8.0 million and to increase gas rates by 1.0% or $1.9 million. The increase in retail electric rates is driven by costs for MGE's share of the Elm Road Units. Pursuant to the provisions of this rate order, the fuel rules bandwidth effective January 1, 2011, will be plus or minus 2%. See below for further description of fuel rules. Authorized return on common stock equity was set at 10.3% based on a 58.1% utility common equity.

b.

Fuel Rules.

The PSCW approved new fuel rules that became effective January 1, 2011. The new rules require the PSCW and Wisconsin utilities to automatically defer electric fuel-related costs that fall outside a symmetrical cost tolerance band.

Any over/under recovery of the deferred costs is determined on an annual basis and will be adjusted in future billings to electric retail customers. Under fuel rules, MGE would defer costs, less any excess revenues, if its actual electric fuel costs exceeded 102% of the electric fuel costs allowed in its latest rate order. Excess revenues are defined as revenues in the year in question that provide MGE with a greater return on common equity than authorized by the PSCW in MGE's latest rate order. Conversely, MGE is required to defer the benefit of lower costs if actual electric fuel costs were less than 98% of the electric fuel costs allowed in that order. As of June 30, 2012, MGE has deferred $2.7 million (for credit back to customers) of electric fuel-related savings that are outside the 98% range authorized by the PSCW in the most recent rate order.

c.

Purchased Gas Adjustment Clause.

MGE's natural gas rates are subject to a fuel adjustment clause designed to recover or refund the difference between the actual cost of purchased gas and the amount included in rates. Differences between the amounts billed to customers and the actual costs recoverable are deferred and recovered or refunded in future periods by means of prospective monthly adjustments to rates. At June 30, 2012, and December 31, 2011, MGE had over collected $1.9 million and $0.9 million, respectively. These amounts were recorded in other current liabilities on the consolidated balance sheet.

11.

Fair Value of Financial Instruments - MGE Energy and MGE.

a.

Fair Value of Financial Assets and Liabilities Recorded at the Carrying Amount.

At June 30, 2012, and December 31, 2011, the carrying amount of cash, cash equivalents, and outstanding commercial paper approximates fair market value due to the short maturity of those investments and obligations. The estimated fair market value of MGE Energy's and MGE's long-term debt is based on quoted market prices for similar financial instruments at June 30, 2012, and December 31, 2011. Since the long-term debt is not traded in an active market, it is classified as Level 2 (see discussion regarding the fair value level hierarchy below in section b).

The estimated fair market value of MGE Energy's and MGE's financial instruments are as follows:

	June 30, 2012		December 31, 2011	
(In thousands)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
MGE Energy				
Assets:				
Cash and cash equivalents	$ 41,288	$ 41,288	$ 41,169	$ 41,169
Liabilities:				
Long-term debt*	363,139	429,115	364,473	432,515
MGE				
Assets:				
Cash and cash equivalents	8,665	8,665	13,898	13,898
Liabilities:				
Long-term debt*	363,139	429,115	364,473	432,515

**Includes long-term debt due within one year.*

b.

Recurring Fair Value Measurements.

Fair value is defined as the price that would be received to sell an asset or would be paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. The standard clarifies that fair value should be based on the assumptions market participants would use when pricing the asset or liability including assumptions about risk. The standard also establishes a three level fair value hierarchy based upon the observability of the assumptions used and requires the use of observable market data when available. The levels are:

Level 1 - Pricing inputs are quoted prices within active markets for identical assets or liabilities.

Level 2 - Pricing inputs are quoted prices within active markets for similar assets or liabilities; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations that are correlated with or otherwise verifiable by observable market data.

Level 3 - Pricing inputs are unobservable and reflect management's best estimate of what market participants would use in pricing the asset or liability.

The following table presents the balances of assets and liabilities measured at fair value on a recurring basis for MGE Energy and MGE.

	Fair Value as of June 30, 2012			
(In thousands)	Total	Level 1	Level 2	Level 3
MGE Energy				
Assets:				
Exchange-traded investments	$ 422	$ 422	$ -	$ -
Total Assets	$ 422	$ 422	$ -	$ -
Liabilities:				
Derivatives, net[(a)]	$ 79,362	$ (218)	$ -	$ 79,580
Deferred compensation	1,856	-	1,856	-
Total Liabilities	$ 81,218	$ (218)	$ 1,856	$ 79,580
MGE				
Assets:				
Exchange-traded investments	$ 150	$ 150	$ -	$ -
Total Assets	$ 150	$ 150	$ -	$ -
Liabilities:				
Derivatives, net[(a)]	$ 79,362	$ (218)	$ -	$ 79,580
Deferred compensation	1,856	-	1,856	-
Total Liabilities	$ 81,218	$ (218)	$ 1,856	$ 79,580

(a)

These amounts are shown gross and exclude $0.7 million of collateral that was posted against derivative positions with counterparties.

No transfers were made in or out of Level 1 or Level 2 for the six months ended June 30, 2012.

		Fair Value as of December 31, 2011			
(In thousands)		Total	Level 1	Level 2	Level 3
MGE Energy					
Assets:					
Exchange-traded investments	$	350$	350$	-$	-
Total Assets	$	350$	350$	-$	-
Liabilities:					
Derivatives, net(b)	$	42,356$	1,695$	-$	40,661
Deferred compensation(c)		1,725	-	1,725	-
Total Liabilities	$	44,081$	1,695$	1,725$	40,661
MGE					
Assets:					
Exchange-traded investments	$	188$	188$	-$	-
Total Assets	$	188$	188$	-$	-
Liabilities:					
Derivatives, net(b)	$	42,356$	1,695$	-$	40,661
Deferred compensation(c)		1,725	-	1,725	-
Total Liabilities	$	44,081$	1,695$	1,725$	40,661

(b)

These amounts are shown gross and exclude $3.0 million of collateral that was posted against derivative positions with counterparties.

(c)

The deferred compensation liability at December 31, 2011, was transferred from Level 1 to Level 2.

Investments include exchange-traded investment securities valued using quoted prices on active exchanges and are therefore classified as Level 1.

Derivatives include exchange-traded derivative contracts, over-the-counter party transactions, a ten-year purchased power agreement, and FTRs. Most exchange-traded derivative contracts are valued based on unadjusted quoted prices in active markets and are therefore classified as Level 1. A small number of exchange-traded derivative contracts are valued using quoted market pricing in markets with insufficient volumes and are therefore classified as Level 3. Transactions done with an over-the-counter party are on inactive markets and are therefore classified as Level 3. These transactions are valued based on quoted prices with markets with similar exchange traded transactions. FTRs are priced based upon monthly auction results for identical or similar instruments in a closed market with limited data available and are therefore classified as Level 3.

The ten-year purchased power agreement (see Footnote 9) was valued using an internally-developed pricing model and therefore is classified as Level 3. The model projects future market energy prices and compares those prices to the projected power costs to be incurred under the contract. Inputs to the model require significant management judgment and estimation. Future energy prices are based on a forward power pricing curve using exchange-traded contracts in the electric futures market, where such exchange-traded contracts exist, and upon calculations based on forward gas prices, where such exchange-traded contracts do not exist. A basis adjustment is applied to the market energy price to reflect the price differential between the market price delivery point and the counterparty delivery point. The historical relationship between the delivery points is reviewed and a discount (below 100%) or premium (above 100%) is derived. This comparison is done for both peak times when demand is high and off peak times when demand is low. If the basis adjustment is lowered, the fair value measurement will decrease and if the basis adjustment is increased, the fair value measurement will increase.

The projected power costs anticipated to be incurred under the purchased power agreement are determined using many factors, including historical generating costs, future prices, and expected fuel mix of the counterparty. An increase in the projected fuel costs would result in a decrease in the fair value measurement of the purchased power agreement. A significant input that MGE estimates is the counterparty's fuel mix in determining the projected power cost. MGE also considers the assumptions that market participants would use in valuing the asset or liability. This consideration includes assumptions about market risk such as liquidity, volatility and contract duration. The fair value model uses a discount rate that incorporates discounting, credit, and model risks.

This model is prepared by members of the Energy Supply group. It is reviewed on a quarterly basis by management in Energy Supply and Finance to review the assumptions, inputs and fair value measurements.

The following table presents the significant unobservable inputs used in the pricing model.

Significant Unobservable Inputs	Model Input
Basis adjustment	
On peak	95.5 %
Off peak	94.1 %
Counterparty fuel mix:	
Internal generation	49 % - 65 %
Purchased power	51 % - 35 %

The deferred compensation plan allows participants to defer certain cash compensation into a notional investment account. These amounts are included within other deferred liabilities in the balance sheets of MGE Energy and MGE. The notional investments earn interest based upon the semiannual rate of U.S. Treasury Bills having a 26 week maturity increased by 1% compounded monthly with a minimum annual rate of 7%, compounded monthly. The notional investments are based upon observable market data, however, since the deferred compensation obligations themselves are not exchanged in an active market, they are classified as Level 2.

The following table summarizes the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for both MGE Energy and MGE.

	Three Months Ended		Six Months Ended	
(In thousands)	June 30,		June 30,	
	2012	2011	2012	2011
Beginning balance,	$ (71,188)	$ (22,148)	$ (40,661)	$ (19,216)
Realized and unrealized gains (losses):				
Included in regulatory liabilities (assets)	(8,392)	(835)	(38,919)	(3,767)
Included in other comprehensive income	-	-	-	-
Included in earnings	(1,726)	579	(3,228)	564
Included in current assets	(94)	(229)	(145)	(229)
Purchases	1,917	334	1,967	334
Sales	32	-	64	71
Issuances	-	-	-	-
Settlements	(129)	(684)	1,342	(740)
Transfers in and/or out of Level 3	-	-	-	-
Balance as of June 30,	$ (79,580)	$ (22,983)	$ (79,580)	$ (22,983)
Total gains (losses) included in earnings attributed to				

the change in unrealized gains (losses) related to assets and liabilities held at June 30,(d)	$ -	$ -	$ -	$ -

The following table presents total realized and unrealized gains (losses) included in income for Level 3 assets and liabilities measured at fair value on a recurring basis for both MGE Energy and MGE *(d)*.

	Three Months Ended		Six Months Ended	
(In thousands)	June 30,		June 30,	
	2012	2011	2012	2011
Purchased Power Expense	$ (1,726)	$ 579	$ (3,228)	$ 564
Cost of Gas Sold Expense	-	-	-	-
Regulated Gas Revenues	-	-	-	-
Total	$ (1,726)	$ 579	$ (3,228)	$ 564

(d)

MGE's exchange-traded derivative contracts, over-the-counter party transactions, ten-year purchased power agreement, and FTRs are subject to regulatory deferral. These derivatives are therefore marked to fair value and are offset with a corresponding regulatory asset or liability.

12.

New Accounting Pronouncements - MGE Energy and MGE.

a.

Fair Value Measurements and Disclosures.

In May 2011, the FASB issued authoritative guidance within the Codification's Fair Value Measurements and Disclosures topic that provides guidance on additional disclosures about fair value measurements, specifically related to Level 3 assets and liabilities. This authoritative guidance became effective January 1, 2012. The authoritative guidance did not have any financial impact, but required additional disclosures. See Footnote 11 for additional information.

b.

Presentation of Comprehensive Income.

In June 2011, the FASB issued authoritative guidance within the Codification's Comprehensive Income topic that provides guidance on presentation of comprehensive income. Comprehensive income will be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. This authoritative guidance became effective January 1, 2012. The authoritative guidance had an effect on our financial statement presentation of comprehensive income. See the Statement of Comprehensive Income for additional information.

c.

Disclosures about Offsetting Assets and Liabilities.

In December 2011, the FASB issued authoritative guidance within the Codification's Balance Sheet topic that provides guidance on disclosures about offsetting assets and liabilities. The new disclosure requirements mandate that entities disclose both gross and net information for instruments and transactions eligible for offset in the balance sheet as well as instruments and transactions subject to a master netting arrangement. In addition, the standard requires disclosure of collateral received and posted in connections with a master netting arrangement. This authoritative guidance will become effective January 1, 2013. The authoritative guidance will not have a financial impact, but will require additional disclosures.

13.

Segment Information - MGE Energy and MGE.

MGE Energy operates in the following business segments: electric utility, gas utility, nonregulated energy, transmission investment, and all other. See MGE Energy's and MGE's 2011 Annual Report on Form 10-K for additional discussion of each of these segments.

The following tables show segment information for MGE Energy's operations for the indicated periods:

(In thousands) **MGE Energy**	Electric	Gas	Non-Regulated Energy	Transmission Investment	All Others	Consolidation/ Elimination Entries	Consolidated Total
Three Months Ended June 30, 2012							
Operating revenues	$ 96,339	$ 18,629	$ 2,253	$ -	$ -	$ -	$ 117,221
Interdepartmental revenues	119	3,077	8,677	-	-	(11,873)	-
Total operating revenues	96,458	21,706	10,930	-	-	(11,873)	117,221
Depreciation and amortization	(6,546)	(1,389)	(1,777)	-	-	-	(9,712)
Other operating expenses	(72,265)	(21,746)	(37)	-	(253)	11,873	(82,428)
Operating income (loss)	17,647	(1,429)	9,116	-	(253)	-	25,081
Other income, net	96	27	-	2,242	184	-	2,549
Interest (expense) income, net	(2,465)	(695)	(1,639)	-	35	-	(4,764)
Income (loss) before taxes	15,278	(2,097)	7,477	2,242	(34)	-	22,866
Income tax (provision) benefit	(5,642)	933	(3,001)	(900)	14	-	(8,596)
Net income (loss)	$ 9,636	$ (1,164)	$ 4,476	$ 1,342	$ (20)	$ -	$ 14,270
Three Months Ended June 30, 2011							
Operating revenues	$ 90,834	$ 25,062	$ 1,363	$ -	$ -	$ -	$ 117,259
Interdepartmental revenues	121	2,173	9,581	-	-	(11,875)	-
Total operating revenues	90,955	27,235	10,944	-	-	(11,875)	117,259
Depreciation and amortization	(7,052)	(1,532)	(1,773)	-	-	-	(10,357)
Other operating expenses	(69,522)	(25,717)	(55)	-	(286)	11,875	(83,705)
Operating income (loss)	14,381	(14)	9,116	-	(286)	-	23,197
Other (deductions) income, net	(124)	(35)	-	2,170	142	-	2,153
Interest (expense) income, net	(2,653)	(748)	(1,669)	-	15	-	(5,055)
Income (loss) before taxes	11,604	(797)	7,447	2,170	(129)	-	20,295
	(4,121)	366	(2,990)	(870)	43	-	(7,572)

Income tax (provision) benefit								
Net income (loss)	$	7,483$	(431)$	4,457$	1,300$	(86)$	-$	12,723
Six Months Ended June 30, 2012								
Operating revenues	$	186,275$	75,648$	4,557$	-$	-$	-$	266,480
Interdepartmental revenues		228	6,063	17,353	-	-	(23,644)	-
Total operating revenues		186,503	81,711	21,910	-	-	(23,644)	266,480
Depreciation and amortization		(13,024)	(2,759)	(3,553)	-	-	-	(19,336)
Other operating expenses		(145,053)	(71,487)	(49)	-	(674)	23,644	(193,619)
Operating income (loss)		28,426	7,465	18,308	-	(674)	-	53,525
Other income, net		260	73	-	4,484	302	-	5,119
Interest (expense) income, net		(5,192)	(1,464)	(3,284)	-	72	-	(9,868)
Income (loss) before taxes		23,494	6,074	15,024	4,484	(300)	-	48,776
Income tax (provision) benefit		(8,427)	(2,305)	(6,030)	(1,810)	114	-	(18,458)
Net income (loss)	$	15,067$	3,769$	8,994$	2,674$	(186)$	-$	30,318
Six Months Ended June 30, 2011								
Operating revenues	$	176,841$	102,499$	2,524$	-$	-$	-$	281,864
Interdepartmental revenues		228	3,164	18,977	-	-	(22,369)	-
Total operating revenues		177,069	105,663	21,501	-	-	(22,369)	281,864
Depreciation and amortization		(14,029)	(2,869)	(3,475)	-	-	-	(20,373)
Other operating expenses		(140,438)	(88,770)	(94)	-	(463)	22,369	(207,396)
Operating income (loss)		22,602	14,024	17,932	-	(463)	-	54,095
Other income, net		33	9	-	4,267	230	-	4,539
Interest expense, net		(5,353)	(1,509)	(3,017)	-	(26)	-	(9,905)
Income (loss) before taxes		17,282	12,524	14,915	4,267	(259)	-	48,729
Income tax (provision) benefit		(5,722)	(4,882)	(5,987)	(1,722)	90	-	(18,223)
Net income (loss)	$	11,560$	7,642$	8,928$	2,545$	(169)$	-$	30,506

The following tables show segment information for MGE's operations for the indicated periods:

(In thousands) **MGE**	Electric	Gas	Non-Regulated Energy	Transmission Investment	Consolidation/ Elimination Entries	Consolidated Total
Three Months Ended June 30, 2012						
Operating revenues	$ 96,339	$ 18,629	$ 2,253	$ -	$ -	$ 117,221
Interdepartmental revenues	119	3,077	8,677	-	(11,873)	-
Total operating revenues	96,458	21,706	10,930	-	(11,873)	117,221
Depreciation and amortization	(6,546)	(1,389)	(1,777)	-	-	(9,712)
Other operating expenses*	(77,849)	(20,797)	(3,038)	-	11,873	(89,811)
Operating income (loss)*	12,063	(480)	6,115	-	-	17,698
Other income, net*	38	11	-	1,342	-	1,391
Interest expense, net	(2,465)	(695)	(1,639)	-	-	(4,799)
Net income (loss)	9,636	(1,164)	4,476	1,342	-	14,290
Less: Net income attributable to noncontrolling interest, net of tax	-	-	-	-	(6,080)	(6,080)
Net income (loss) attributable to MGE	$ 9,636	$ (1,164)	$ 4,476	$ 1,342	$ (6,080)	$ 8,210
Three Months Ended June 30, 2011						
Operating revenues	$ 90,834	$ 25,062	$ 1,363	$ -	$ -	$ 117,259
Interdepartmental revenues	121	2,173	9,581	-	(11,875)	-
Total operating revenues	90,955	27,235	10,944	-	(11,875)	117,259
Depreciation and amortization	(7,052)	(1,532)	(1,773)	-	-	(10,357)
Other operating expenses*	(73,581)	(25,333)	(3,044)	-	11,875	(90,083)
Operating income*	10,322	370	6,127	-	-	16,819
Other (deductions) income, net*	(185)	(52)	-	1,299	-	1,062
Interest expense, net	(2,653)	(748)	(1,669)	-	-	(5,070)
Net income (loss)	7,484	(430)	4,458	1,299	-	12,811
Less: net income attributable to	-	-	-	-	(5,992)	(5,992)

noncontrolling interest, net of tax							
Net income (loss) attributable to MGE	$	7,484$	(430)$	4,458$	1,299$	(5,992)$	6,819
Six Months Ended June 30, 2012							
Operating revenues	$	186,275$	75,648$	4,557$	-$	-$	266,480
Interdepartmental revenues		228	6,063	17,353	-	(23,644)	-
Total operating revenues		186,503	81,711	21,910	-	(23,644)	266,480
Depreciation and amortization		(13,024)	(2,759)	(3,553)	-	-	(19,336)
Other operating expenses*		(153,357)	(73,758)	(6,079)	-	23,644	(209,550)
Operating income*		20,122	5,194	12,278	-	-	37,594
Other income, net*		137	39	-	2,674	-	2,850
Interest expense, net		(5,192)	(1,464)	(3,284)	-	-	(9,940)
Net income		15,067	3,769	8,994	2,674	-	30,504
Less: Net income attributable to noncontrolling interest, net of tax		-	-	-	-	(12,152)	(12,152)
Net income attributable to MGE	$	15,067$	3,769$	8,994$	2,674$	(12,152)$	18,352
Six Months Ended June 30, 2011							
Operating revenues	$	176,841$	102,499$	2,524$	-$	-$	281,864
Interdepartmental revenues		228	3,164	18,977	-	(22,369)	-
Total operating revenues		177,069	105,663	21,501	-	(22,369)	281,864
Depreciation and amortization		(14,029)	(2,869)	(3,475)	-	-	(20,373)
Other operating expenses*		(146,132)	(93,644)	(6,080)	-	22,369	(223,487)
Operating income*		16,908	9,150	11,946	-	-	38,004
Other income, net*		6	2	-	2,545	-	2,553
Interest expense, net		(5,353)	(1,509)	(3,017)	-	-	(9,879)
Net income		11,561	7,643	8,929	2,545	-	30,678
Less: net income attributable to noncontrolling interest, net of tax		-	-	-	-	(11,925)	(11,925)
Net income attributable to MGE	$	11,561$	7,643$	8,929$	2,545$	(11,925)$	18,753

**Amounts are shown net of the related tax expense, consistent with the presentation on the consolidated MGE Income Statement.*

The following table shows segment information for MGE Energy's and MGE's assets and capital expenditures:

(In thousands)	Utility			Consolidated				
MGE Energy			Assets not	Nonregulated	Transmission	All	Consolidation/ Elimination	
	Electric	Gas	Allocated	Energy	Investment	Others	Entries	Total
Assets:								
June 30, 2012	$ 868,718	$ 258,569	$ 24,595					