

WEC ENERGY GROUP, INC.
Form 10-Q
August 05, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended June 30, 2016

Commission File Number	Registrant; State of Incorporation; Address; and Telephone Number	IRS Employer Identification No.
001-09057	WEC ENERGY GROUP, INC. (A Wisconsin Corporation) 231 West Michigan Street P.O. Box 1331 Milwaukee, WI 53201 (414) 221-2345	39-1391525

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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 registrant was required to submit and post such files).

Yes 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 the 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

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

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, \$.01 Par Value,
315,619,968 shares outstanding at
June 30, 2016

Table of Contents

WEC ENERGY GROUP, INC.
 QUARTERLY REPORT ON FORM 10-Q
 For the Quarter Ended June 30, 2016
 TABLE OF CONTENTS

	Page
<u>CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION</u>	<u>1</u>
<u>PART I. FINANCIAL INFORMATION</u>	<u>3</u>
<u>ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)</u>	<u>3</u>
<u>Condensed Consolidated Income Statements</u>	<u>3</u>
<u>Condensed Consolidated Statements of Comprehensive Income</u>	<u>4</u>
<u>Condensed Consolidated Balance Sheets</u>	<u>5</u>
<u>Condensed Consolidated Statements of Cash Flows</u>	<u>6</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>7</u>
	Page
<u>Note 1 General Information</u>	<u>7</u>
<u>Note 2 Acquisition</u>	<u>7</u>
<u>Note 3 Dispositions</u>	<u>9</u>
<u>Note 4 Common Equity</u>	<u>10</u>
<u>Note 5 Short-Term Debt and Lines of Credit</u>	<u>10</u>
<u>Note 6 Long-Term Debt</u>	<u>11</u>
<u>Note 7 Materials, Supplies, and Inventories</u>	<u>11</u>
<u>Note 8 Fair Value Measurements</u>	<u>11</u>
<u>Note 9 Derivative Instruments</u>	<u>13</u>
<u>Note 10 Guarantees</u>	<u>15</u>
<u>Note 11 Employee Benefits</u>	<u>15</u>
<u>Note 12 Goodwill</u>	<u>16</u>
<u>Note 13 Investment in American Transmission Company</u>	<u>16</u>
<u>Note 14 Segment Information</u>	<u>17</u>
<u>Note 15 Variable Interest Entities</u>	<u>19</u>
<u>Note 16 Commitments and Contingencies</u>	<u>20</u>
<u>Note 17 Supplemental Cash Flow Information</u>	<u>25</u>
<u>Note 18 Regulatory Environment</u>	<u>25</u>
<u>Note 19 New Accounting Pronouncements</u>	<u>27</u>
<u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF</u>	
<u>ITEM 2. FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	<u>28</u>
<u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	<u>47</u>
<u>ITEM 4. CONTROLS AND PROCEDURES</u>	<u>48</u>
<u>PART II. OTHER INFORMATION</u>	<u>49</u>
<u>ITEM 1. LEGAL PROCEEDINGS</u>	<u>49</u>
<u>ITEM 1A. RISK FACTORS</u>	<u>49</u>
<u>ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	<u>49</u>
<u>ITEM 6. EXHIBITS</u>	<u>50</u>
<u>SIGNATURE</u>	<u>51</u>

Table of Contents

GLOSSARY OF TERMS AND ABBREVIATIONS

The abbreviations and terms set forth below are used throughout this report and have the meanings assigned to them below:

Subsidiaries and Affiliates

ATC	American Transmission Company LLC
IntegrYS	IntegrYS Holding, Inc. (previously known as IntegrYS Energy Group, Inc.)
ITF	IntegrYS Transportation Fuels, LLC
MERC	Minnesota Energy Resources Corporation
MGU	Michigan Gas Utilities Corporation
NSG	North Shore Gas Company
PDL	WPS Power Development, LLC
PGL	The Peoples Gas Light and Coke Company
WBS	WEC Business Services LLC
WE	Wisconsin Electric Power Company
We Power	W.E. Power, LLC
WG	Wisconsin Gas LLC
Wisvest	Wisvest LLC
WPS	Wisconsin Public Service Corporation

Federal and State Regulatory Agencies

EPA	United States Environmental Protection Agency
FERC	Federal Energy Regulatory Commission
ICC	Illinois Commerce Commission
MDEQ	Michigan Department of Environmental Quality
MPSC	Michigan Public Service Commission
MPUC	Minnesota Public Utilities Commission
PSCW	Public Service Commission of Wisconsin
SEC	United States Securities and Exchange Commission
WDNR	Wisconsin Department of Natural Resources

Accounting Terms

AFUDC	Allowance for Funds Used During Construction
ASC	Accounting Standards Codification
ASU	Accounting Standards Update
FASB	Financial Accounting Standards Board
GAAP	United States Generally Accepted Accounting Principles
LIFO	Last-In, First-Out
OPEB	Other Postretirement Employee Benefits

Environmental Terms

CAA	Clean Air Act
CAIR	Clean Air Interstate Rule
CSAPR	Cross-State Air Pollution Rule
GHG	Greenhouse Gas
MATS	Mercury and Air Toxics Standards
NAAQS	National Ambient Air Quality Standards
NOV	Notice of Violation
NOx	Nitrogen Oxide

SO₂ Sulfur Dioxide

Measurements

Btu British Thermal Units

Dth Dekatherm (One Dth equals one million Btu)

MW Megawatt (One MW equals one million Watts)

MWh Megawatt-hour

06/30/2016 Form 10-Q ii WEC Energy Group, Inc.

Table of Contents

Other Terms and Abbreviations

6.11% Junior Notes	Integrus's 2006 6.11% Junior Subordinated Notes Due 2066
ALJ	Administrative Law Judge
AMRP	Accelerated Natural Gas Main Replacement Program
CNG	Compressed Natural Gas
D.C. Circuit Court of Appeals	United States Court of Appeals for the District of Columbia Circuit
Exchange Act	Securities Exchange Act of 1934, as amended
FTRs	Financial Transmission Rights
MCCP	Milwaukee County Power Plant
MISO	Midcontinent Independent System Operator, Inc.
MISO Energy Markets	MISO Energy and Operating Reserves Markets
N/A	Not Applicable
PIPP	Presque Isle Power Plant
ROE	Return on Equity
SSR	System Support Resource
Supreme Court	United States Supreme Court
VAPP	Valley Power Plant

Table of Contents

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

In this report, we make statements concerning our expectations, beliefs, plans, objectives, goals, strategies, and future events or performance. These statements are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act. Readers are cautioned not to place undue reliance on these forward-looking statements. Forward-looking statements may be identified by reference to a future period or periods or by the use of terms such as "anticipates," "believes," "could," "estimates," "expects," "forecasts," "goals," "guidance," "intends," "may," "objectives," "plans," "possible," "potential," "projects," "seeks," "should," "targets," "will," or variations of these terms.

Forward-looking statements include, among other things, statements concerning management's expectations and projections regarding earnings, completion of capital projects, sales and customer growth, rate actions and related filings with regulatory authorities, environmental and other regulations and associated compliance costs, legal proceedings, dividend payout ratios, effective tax rate, pension and OPEB plans, fuel costs, sources of electric energy supply, coal and natural gas deliveries, remediation costs, liquidity and capital resources, and other matters.

Forward-looking statements are subject to a number of risks and uncertainties that could cause our actual results to differ materially from those expressed or implied in the statements. These risks and uncertainties include those described in risk factors as set forth in this report and our Annual Report on Form 10-K for the year ended December 31, 2015, and those identified below:

• Factors affecting utility operations such as catastrophic weather-related damage, environmental incidents, unplanned facility outages and repairs and maintenance, and electric transmission or natural gas pipeline system constraints;

• Factors affecting the demand for electricity and natural gas, including political developments, unusual weather, changes in economic conditions, customer growth and declines, commodity prices, energy conservation efforts, and continued adoption of distributed generation by customers;

• The timing, resolution, and impact of rate cases and negotiations, including recovery of deferred and current costs and adjustments to the ROE at any of our utilities and/or ATC, and other regulatory decisions impacting our regulated operations;

• The ability to obtain and retain customers, including wholesale customers, due to increased competition in our electric and natural gas markets from retail choice and alternative electric suppliers, and continued industry consolidation;

• The timely completion of capital projects within budgets, as well as the recovery of the related costs through rates;

• The impact of federal, state, and local legislative and regulatory changes, including changes in rate-setting policies or procedures, tax law changes, deregulation and restructuring of the electric and/or natural gas utility industries, transmission or distribution system operation, the approval process for new construction, reliability standards, pipeline integrity and safety standards, allocation of energy assistance, and energy efficiency mandates;

• Federal and state legislative and regulatory changes relating to the environment, including climate change and other environmental regulations impacting generation facilities and renewable energy standards, the enforcement of these laws and regulations, changes in the interpretation of permit conditions by regulatory agencies, and the recovery of associated remediation and compliance costs;

• The risks associated with changing commodity prices, particularly natural gas and electricity, and the availability of sources of fossil fuel, natural gas, purchased power, materials needed to operate environmental controls at our electric

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generating facilities, or water supply due to high demand, shortages, transportation problems, nonperformance by electric energy or natural gas suppliers under existing power purchase or natural gas supply contracts, or other developments;

Changes in credit ratings, interest rates, and our ability to access the capital markets, caused by volatility in the global credit markets, our capitalization structure, and market perceptions of the utility industry, us, or any of our subsidiaries;

Costs and effects of litigation, administrative proceedings, investigations, settlements, claims, and inquiries;

Restrictions imposed by various financing arrangements and regulatory requirements on the ability of our subsidiaries to transfer funds to us in the form of cash dividends, loans or advances;

06/30/2016 Form 10-Q 1 WEC Energy Group, Inc.

Table of Contents

• The risk of financial loss, including increases in bad debt expense, associated with the inability of our customers, counterparties, and affiliates to meet their obligations;

• Changes in the creditworthiness of the counterparties with whom we have contractual arrangements, including participants in the energy trading markets and fuel suppliers and transporters;

• The direct or indirect effect on our business resulting from terrorist incidents, the threat of terrorist incidents, and cyber intrusion, including the failure to maintain the security of personally identifiable information, the associated costs to protect our assets and personal information, and the costs to notify affected persons to mitigate their information security concerns;

• The financial performance of ATC and its corresponding contribution to our earnings, as well as the ability of ATC and Duke-American Transmission Company to obtain the required approvals for their transmission projects;

• The investment performance of our employee benefit plan assets, as well as unanticipated changes in related actuarial assumptions, which could impact future funding requirements;

• Factors affecting the employee workforce, including loss of key personnel, internal restructuring, work stoppages, and collective bargaining agreements and negotiations with union employees;

• Advances in technology that result in competitive disadvantages and create the potential for impairment of existing assets;

• The terms and conditions of the governmental and regulatory approvals of the acquisition of Integrys that could reduce anticipated benefits and our ability to successfully integrate the operations of the combined company;

• The risk associated with the values of goodwill and other intangible assets and their possible impairment;

• Potential business strategies to acquire and dispose of assets or businesses, which cannot be assured to be completed timely or within budgets, and legislative or regulatory restrictions or caps on non-utility acquisitions, investments, or projects, including the state of Wisconsin's public utility holding company law;

• The timing and outcome of any audits, disputes, and other proceedings related to taxes;

• The effect of accounting pronouncements issued periodically by standard-setting bodies; and

• Other considerations disclosed elsewhere herein and in other reports we file with the SEC or in other publicly disseminated written documents.

We expressly disclaim any obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

WEC ENERGY GROUP, INC.

CONDENSED CONSOLIDATED INCOME STATEMENTS
(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30		June 30	
(in millions, except per share amounts)	2016	2015	2016	2015
Operating revenues	\$1,602.0	\$991.2	\$3,796.8	\$2,379.1
Operating expenses				
Cost of sales	508.3	353.0	1,347.2	966.9
Other operation and maintenance	522.0	337.0	1,053.5	617.7
Depreciation and amortization	190.0	103.5	377.9	206.1
Property and revenue taxes	49.6	31.9	96.8	63.8
Total operating expenses	1,269.9	825.4	2,875.4	1,854.5
Operating income	332.1	165.8	921.4	524.6
Equity in earnings of transmission affiliate	30.9	14.3	69.4	30.4
Other income, net	32.4	26.1	65.1	29.1
Interest expense	100.1	61.8	201.0	121.2
Other expense	(36.8)	(21.4)	(66.5)	(61.7)
Income before income taxes	295.3	144.4	854.9	462.9
Income tax expense	113.6	63.2	326.7	185.6
Net income	181.7	81.2	528.2	277.3
Preferred stock dividends of subsidiary	0.3	0.3	0.6	0.6
Net income attributed to common shareholders	\$181.4	\$80.9	\$527.6	\$276.7
Earnings per share				
Basic	\$0.57	\$0.36	\$1.67	\$1.22
Diluted	\$0.57	\$0.35	\$1.66	\$1.21
Weighted average common shares outstanding				
Basic	315.6	227.5	315.6	226.5
Diluted	317.0	229.1	317.0	228.2
Dividends per share of common stock	\$0.4950	\$0.8629	\$0.9900	\$1.2854

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

Table of Contents

WEC ENERGY GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)	Three Months		Six Months	
	Ended		Ended	
(in millions)	June 30		June 30	
	2016	2015	2016	2015
Net income	\$181.7	\$81.2	\$528.2	\$277.3
Other comprehensive income (loss), net of tax				
Derivatives accounted for as cash flow hedges				
Gains on settlement, net of tax of \$7.6	—	11.4	—	11.4
Reclassification of gains to net income, net of tax	(0.3)	(0.1)	(0.6)	(0.1)
Cash flow hedges, net	(0.3)	11.3	(0.6)	11.3
Defined benefit plans				
Amortization of pension and OPEB costs included in net periodic benefit cost, net of tax	0.4	—	0.4	—
Other comprehensive income (loss), net of tax	0.1	11.3	(0.2)	11.3
Comprehensive income	181.8	92.5	528.0	288.6
Preferred stock dividends of subsidiary	0.3	0.3	0.6	0.6
Comprehensive income attributed to common shareholders	\$181.5	\$92.2	\$527.4	\$288.0

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

06/30/2016 Form 10-Q 4 WEC Energy Group, Inc.

Table of Contents

WEC ENERGY GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

(in millions, except share and per share amounts)

	June 30, 2016	December 31, 2015
Assets		
Property, plant, and equipment		
In service	\$26,690.7	\$ 26,249.5
Accumulated depreciation	(8,049.1)	(7,919.1)
	18,641.6	18,330.4
Construction work in progress	723.7	822.9
Leased facilities, net	33.6	36.4
Net property, plant, and equipment	19,398.9	19,189.7
Investments		
Equity investment in transmission affiliate	1,425.0	1,380.9
Other	88.0	85.8
Total investments	1,513.0	1,466.7
Current assets		
Cash and cash equivalents	32.1	49.8
Accounts receivable and unbilled revenues, net of reserves of \$109.4 and \$113.3, respectively	914.9	1,028.6
Materials, supplies, and inventories	494.5	687.0
Assets held for sale	—	96.8
Prepayments	235.3	285.8
Other	89.1	58.8
Total current assets	1,765.9	2,206.8
Deferred charges and other assets		
Regulatory assets	3,031.4	3,064.6
Goodwill	3,046.2	3,023.5
Other	419.9	403.9
Total deferred charges and other assets	6,497.5	6,492.0
Total assets	\$29,175.3	\$ 29,355.2
Capitalization and liabilities		
Capitalization		
Common stock – \$.01 par value; 325,000,000 shares authorized; 315,619,968 and 315,683,496 shares outstanding, respectively	\$3.2	\$ 3.2
Additional paid in capital	4,310.9	4,347.2
Retained earnings	4,515.0	4,299.8
Accumulated other comprehensive income	4.4	4.6
Preferred stock of subsidiary	30.4	30.4
Long-term debt	8,902.1	9,124.1
Total capitalization	17,766.0	17,809.3
Current liabilities		
Current portion of long-term debt	95.8	157.7
Short-term debt	927.8	1,095.0
Accounts payable	620.5	815.4
Accrued payroll and benefits	134.5	169.7
Other	358.5	471.2
Total current liabilities	2,137.1	2,709.0
Deferred credits and other liabilities		

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Regulatory liabilities	1,469.7	1,392.2
Deferred income taxes	4,938.3	4,622.3
Deferred revenue, net	572.3	579.4
Pension and OPEB obligations	541.9	543.1
Environmental remediation	617.9	628.2
Other	1,132.1	1,071.7
Total deferred credits and other liabilities	9,272.2	8,836.9
Commitments and contingencies (Note 16)		
Total capitalization and liabilities	\$29,175.3	\$ 29,355.2

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

06/30/2016 Form 10-Q 5 WEC Energy Group, Inc.

Table of Contents

WEC ENERGY GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)	Six Months Ended June 30	
(in millions)	2016	2015
Operating Activities		
Net income	\$528.2	\$277.3
Reconciliation to cash provided by operating activities		
Depreciation and amortization	386.0	215.1
Deferred income taxes and investment tax credits, net	307.1	121.7
Contributions and payments related to pension and OPEB plans	(19.5)	(106.1)
Equity income in transmission affiliate, net of distributions	(22.7)	(9.2)
Change in –		
Accounts receivable and unbilled revenues	130.1	134.5
Materials, supplies, and inventories	193.5	72.2
Other current assets	66.7	16.7
Accounts payable	(112.4)	27.4
Accrued taxes, net	(51.3)	10.5
Other current liabilities	(87.7)	(1.2)
Other, net	(93.9)	(42.4)
Net cash provided by operating activities	1,224.1	716.5
Investing Activities		
Capital expenditures	(618.7)	(368.0)
Business acquisition, net of cash acquired of \$156.3	—	(1,329.4)
Investment in transmission affiliate	(12.1)	(2.6)
Proceeds from the sale of assets and businesses	161.0	21.2
Withdrawal of restricted cash from Rabbi trust for qualifying payments	22.5	—
Other, net	(1.8)	(0.4)
Net cash used in investing activities	(449.1)	(1,679.2)
Financing Activities		
Exercise of stock options	35.0	12.2
Purchase of common stock	(94.2)	(32.0)
Dividends paid on common stock	(312.4)	(190.5)
Issuance of long-term debt	—	1,450.0
Retirement of long-term debt	(241.8)	(11.6)
Change in short-term debt	(167.2)	(105.7)
Other, net	(12.1)	(7.2)
Net cash (used in) provided by financing activities	(792.7)	1,115.2
Net change in cash and cash equivalents	(17.7)	152.5
Cash and cash equivalents at beginning of period	49.8	61.9
Cash and cash equivalents at end of period	\$32.1	\$214.4

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

06/30/2016 Form 10-Q 6 WEC Energy Group, Inc.

Table of Contents

WEC ENERGY GROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

June 30, 2016

NOTE 1—GENERAL INFORMATION

On June 29, 2015, Wisconsin Energy Corporation acquired Integrys and changed its name to WEC Energy Group, Inc. WEC Energy Group serves approximately 1.6 million electric customers and 2.8 million natural gas customers, and it owns approximately 60% of ATC. See Note 2, Acquisition, for more information.

As used in these notes, the term "financial statements" refers to the condensed consolidated financial statements. This includes the income statements, statements of comprehensive income, balance sheets, and statements of cash flows, unless otherwise noted. In this report, when we refer to "the Company," "us," "we," "our," or "ours," we are referring to WEC Energy Group and all of its subsidiaries.

We have prepared the unaudited interim financial statements presented in this Form 10-Q pursuant to the rules and regulations of the SEC and GAAP. Accordingly, these financial statements do not include all of the information and footnotes required by GAAP for annual financial statements. These financial statements should be read in conjunction with the consolidated financial statements and footnotes in our Annual Report on Form 10-K for the year ended December 31, 2015. Financial results for an interim period may not give a true indication of results for the year. In particular, the results of operations for the three and six months ended June 30, 2016, are not necessarily indicative of expected results for 2016 due to seasonal variations and other factors.

In management's opinion, we have included all adjustments, normal and recurring in nature, necessary for a fair presentation of our financial results.

Reclassifications

On the income statements for the three and six months ended June 30, 2015, we reclassified \$2.2 million and \$4.7 million, respectively, from treasury grant to depreciation and amortization. We also reclassified an insignificant amount from interest expense to preferred stock dividends of subsidiary on the income statements for the three and six months ended June 30, 2015. These reclassifications were made to be consistent with the current period presentation.

On the statement of cash flows for the six months ended June 30, 2015, we reclassified \$1.7 million from depreciation and amortization to other operating activities. In addition, we reclassified \$6.1 million of non-qualified pension and OPEB contributions from other operating activities to contributions and payments related to pension and OPEB plans. We also reclassified \$11.5 million from other investing activities to capital expenditures on the statement of cash flows for the six months ended June 30, 2015. An insignificant amount of preferred stock dividends of subsidiary was also reclassified from other financing activities to net income. These reclassifications were made to be consistent with the current period presentation.

During the third quarter of 2015, following the acquisition of Integrys, we reorganized our business segments. All prior period amounts impacted by this change were reclassified to conform to the new presentation. See Note 14, Segment Information, for more information on our business segments.

NOTE 2—ACQUISITION

On June 29, 2015, Wisconsin Energy Corporation acquired 100% of the outstanding common shares of Integrys and changed its name to WEC Energy Group, Inc.

Allocation of Purchase Price

The Integrys assets acquired and liabilities assumed were measured at estimated fair value in accordance with the accounting guidance under the Business Combinations Topic in the FASB ASC. Substantially all of Integrys's operations are subject to the rate-setting authority of federal and state regulatory commissions. These operations are accounted for following the accounting guidance under the Regulated Operations Topic of the FASB ASC. The underlying assets and liabilities of ATC are also regulated by the FERC. The fair values of Integrys's assets and liabilities subject to rate-setting provisions provide revenues derived from costs, including a return on investment of assets and liabilities included in rate base. As such, the fair values of these assets and liabilities equal their

06/30/2016 Form 10-Q 7 WEC Energy Group, Inc.

Table of Contents

carrying values. Accordingly, neither the assets and liabilities acquired, nor the pro forma financial information, reflect any adjustments related to these amounts.

The excess of the purchase price over the estimated fair values of the assets acquired and liabilities assumed was recognized as goodwill. The goodwill reflects the value paid for the increased scale and efficiencies as a result of the combination. The goodwill recognized is not deductible for income tax purposes, and as such, no deferred taxes have been recorded related to goodwill. See Note 12, Goodwill, for the allocation of goodwill to our reportable segments.

The table below shows the allocation of the purchase price to the assets acquired and liabilities assumed at the date of the acquisition. In 2016, adjustments were made to the estimated fair values of the assets acquired and liabilities assumed, primarily in connection with the sale of ITF and reserves recorded for likely settlements of certain legal and regulatory matters.

(in millions)

Current assets	\$1,060.1
Net property, plant, and equipment	7,107.4
Investments *	1,072.0
Goodwill	2,604.3
Deferred charges and other assets, excluding goodwill	1,758.5
Current liabilities, including current maturities of long-term debt	(1,320.7)
Deferred credits and other liabilities	(3,703.8)
Long-term debt	(2,943.6)
Preferred stock of subsidiary	(51.1)
Total purchase price	\$5,583.1

*Includes equity method goodwill related to Integrys's investment in ATC.

Pro Forma Information

The following unaudited pro forma financial information reflects the consolidated results and amortization of purchase price adjustments as if the acquisition had taken place on January 1, 2014. The unaudited pro forma financial information is presented for illustrative purposes only and is not necessarily indicative of the consolidated results of operations that would have been achieved or our future consolidated results.

The pro forma financial information does not reflect any potential cost savings from operating efficiencies resulting from the acquisition and does not include certain acquisition-related costs.

(in millions, except per share amounts)	Three	Six
	Months	Months
	Ended	Ended
	June 30,	June 30,
	2015	2015
Unaudited Pro Forma Financial Information		
Operating revenues	\$1,629.2	\$4,180.1
Net income	\$159.1	\$488.7
Earnings per share (Basic)	\$0.50	\$1.55
Earnings per share (Diluted)	\$0.50	\$1.54

Impact of Acquisition

In connection with the acquisition, WEC Energy Group and its subsidiaries recorded pre-tax acquisition costs of \$65.0 million and \$73.7 million during the three and six months ended June 30, 2015, respectively. These costs consisted of employee-related expenses, professional fees, and other miscellaneous costs. They were recorded in other operation and maintenance on our income statements. Acquisition costs incurred during the three and six months ended June 30, 2016 were not significant.

Our revenues for the three and six months ended June 30, 2015 did not include any revenues attributable to Integrys. Included in our net income for the three and six months ended June 30, 2015, is a net loss attributable to Integrys of \$26.6 million related to acquisition costs that were incurred post-acquisition.

06/30/2016 Form 10-Q 8 WEC Energy Group, Inc.

Table of Contents

NOTE 3—DISPOSITIONS

Wisconsin Segment – Sale of Milwaukee County Power Plant

In April 2016, we sold the MCPP steam generation and distribution assets, located in Wauwatosa, Wisconsin. MCPP primarily provides steam to the Milwaukee Regional Medical Center hospitals and other campus buildings. During the second quarter of 2016, we recorded a pre-tax gain on the sale of \$10.9 million (\$6.5 million&#