

ALLETE INC  
Form 10-Q  
August 05, 2009

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

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the quarterly period ended June 30, 2009

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-3548

ALLETE, Inc.  
(Exact name of registrant as specified in its charter)

Minnesota 41-0418150  
(State or other jurisdiction of incorporation or (IRS Employer Identification No.)  
organization)

30 West Superior Street  
Duluth, Minnesota 55802-2093  
(Address of principal executive offices)  
(Zip Code)

(218) 279-5000  
(Registrant's telephone number, including area code)

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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  No

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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. (Check one):

Large Accelerated Filer   
Non-Accelerated Filer

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

Common Stock, no par value,  
34,100,096 shares outstanding  
as of June 30, 2009

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## Definitions

The following abbreviations or acronyms are used in the text. References in this report to “we,” “us” and “our” are to ALLETE, Inc. and its subsidiaries, collectively.

Abbreviation or Acronym	Term
AFUDC	Allowance for Funds Used During Construction – consisting of the cost of both the debt and equity funds used to finance utility plant additions during construction periods
ALLETE	ALLETE, Inc.
ALLETE Properties	ALLETE Properties, LLC and its subsidiaries
APB	Accounting Principles Board
AREA	Arrowhead Regional Emission Abatement
ARS	Auction Rate Securities
ATC	American Transmission Company LLC
BNI Coal	BNI Coal, Ltd.
BNSF	BNSF Railway Company
Boswell	Boswell Energy Center
Company	ALLETE, Inc. and its subsidiaries
DC	Direct Current
EITF	Emerging Issues Task Force
EPA	Environmental Protection Agency
ESOP	Employee Stock Ownership Plan
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
Form 10-K	ALLETE Annual Report on Form 10-K
Form 10-Q	ALLETE Quarterly Report on Form 10-Q
FSP	FASB Staff Position
FTR	Financial Transmission Rights
GAAP	United States Generally Accepted Accounting Principles
GHG	Greenhouse Gases
IBEW Local 31	International Brotherhood of Electrical Workers Local 31
Invest Direct	ALLETE’s Direct Stock Purchase and Dividend Reinvestment Plan
kV	Kilovolt(s)
Laskin	Laskin Energy Center
Minnesota Power	An operating division of ALLETE, Inc.
Minnkota Power	Minnkota Power Cooperative, Inc.
MISO	Midwest Independent Transmission System Operator, Inc.
MPCA	Minnesota Pollution Control Agency
MPUC	Minnesota Public Utilities Commission
MW / MWh	Megawatt(s) / Megawatt-hour(s)
Non-residential	Retail commercial, non-retail commercial, office, industrial, warehouse, storage and institutional
NOX	Nitrogen Oxide
Note ____	Note ____ to the consolidated financial statements in this Form 10-Q
OES	Minnesota Office of Energy
Oliver Wind I	Oliver Wind I Energy Center
Oliver Wind II	Oliver Wind II Energy Center



Definitions (Continued)

Abbreviation or Acronym	Term
Palm Coast Park	Palm Coast Park development project in Florida
Palm Coast Park District	Palm Coast Park Community Development District
PSCW	Public Service Commission of Wisconsin
Rainy River Energy	Rainy River Energy Corporation - Wisconsin
SEC	Securities and Exchange Commission
SFAS	Statement of Financial Accounting Standards No.
SO <sub>2</sub>	Sulfur Dioxide
Square Butte	Square Butte Electric Cooperative
SWL&P	Superior Water, Light and Power Company
Taconite Harbor	Taconite Harbor Energy Center
Town Center	Town Center at Palm Coast development project in Florida
Town Center District	Town Center at Palm Coast Community Development District
WDNR	Wisconsin Department of Natural Resources

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Safe Harbor Statement  
Under the Private Securities Litigation Reform Act of 1995

Statements in this report that are not statements of historical facts may be considered “forward-looking” and, accordingly, involve risks and uncertainties that could cause actual results to differ materially from those discussed. Although such forward-looking statements have been made in good faith and are based on reasonable assumptions, there is no assurance that the expected results will be achieved. Any statements that express, or involve discussions as to, future expectations, risks, beliefs, plans, objectives, assumptions, events, uncertainties, financial performance, or growth strategies (often, but not always, through the use of words or phrases such as “anticipates,” “believes,” “estimates,” “expects,” “intends,” “plans,” “projects,” “will likely result,” “will continue,” “could,” “may,” “potential,” “target,” “outlook” or similar meaning) are not statements of historical facts and may be forward-looking.

In connection with the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, we are hereby filing cautionary statements identifying important factors that could cause our actual results to differ materially from those projected, or expectations suggested, in forward-looking statements made by or on behalf of ALLETE in this Quarterly Report on Form 10-Q, in presentations, on our website, in response to questions or otherwise. These statements are qualified in their entirety by reference to, and are accompanied by, the following important factors, in addition to any assumptions and other factors referred to specifically in connection with such forward-looking statements:

- our ability to successfully implement our strategic objectives;
- our ability to manage expansion and integrate acquisitions;
- prevailing governmental policies, regulatory actions, and legislation including those of the United States Congress, state legislatures, the FERC, the MPUC, the PSCW, and various local and county regulators, and city administrators, about allowed rates of return, financings, industry and rate structure, acquisition and disposal of assets and facilities, real estate development, operation and construction of plant facilities, recovery of purchased power, capital investments and other expenses, present or prospective wholesale and retail competition (including but not limited to transmission costs), zoning and permitting of land held for resale and environmental matters;
- the potential impacts of climate change and future regulation to restrict the emissions of GHG on our Regulated Operations;
- effects of restructuring initiatives in the electric industry;
- economic and geographic factors, including political and economic risks;
- changes in and compliance with laws and regulations;
- weather conditions;
- natural disasters and pandemic diseases;
- war and acts of terrorism;
- wholesale power market conditions;
- population growth rates and demographic patterns;
- effects of competition, including competition for retail and wholesale customers;
- changes in the real estate market;
- pricing and transportation of commodities;
- changes in tax rates or policies or in rates of inflation;
- project delays or changes in project costs;
- availability and management of construction materials and skilled construction labor for capital projects;
- changes in operating expenses, capital and land development expenditures;
- global and domestic economic conditions affecting us or our customers;



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- our ability to access capital markets and bank financing;
- changes in interest rates and the performance of the financial markets;
- our ability to replace a mature workforce and retain qualified, skilled and experienced personnel; and
- the outcome of legal and administrative proceedings (whether civil or criminal) and settlements that affect the business and profitability of ALLETE.

Additional disclosures regarding factors that could cause our results and performance to differ from results or performance anticipated by this report are discussed in Item 1A under the heading “Risk Factors” beginning on page 20 of our 2008 Form 10-K. Any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which that statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for management to predict all of these factors, nor can it assess the impact of each of these factors on the businesses of ALLETE or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statement. Readers are urged to carefully review and consider the various disclosures made by us in this Form 10-Q and in our other reports filed with the SEC that attempt to advise interested parties of the factors that may affect our business.

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PART I. FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS

ALLETE  
CONSOLIDATED BALANCE SHEET  
Millions – Unaudited

	June 30, 2009	December 31, 2008
<b>Assets</b>		
<b>Current Assets</b>		
Cash and Cash Equivalents	\$72.4	\$102.0
Accounts Receivable (Less Allowance of \$0.7 at June 30, 2009 and \$0.7 at December 31, 2008)	80.7	76.3
Inventories	53.6	49.7
Prepayments and Other	25.7	24.3
Total Current Assets	232.4	252.3
Property, Plant and Equipment - Net	1,481.7	1,387.3
Investment in ATC	82.1	76.9
Other Investments	135.6	136.9
Other Assets	285.8	281.4
<b>Total Assets</b>	<b>\$2,217.6</b>	<b>\$2,134.8</b>
<b>Liabilities and Equity</b>		
<b>Liabilities</b>		
<b>Current Liabilities</b>		
Accounts Payable	\$59.0	\$75.7
Accrued Taxes	15.8	12.9
Accrued Interest	12.0	8.9
Long-Term Debt Due Within One Year	13.0	10.4
Notes Payable	6.0	6.0
Other	40.1	36.8
Total Current Liabilities	145.9	150.7
Long-Term Debt	627.2	588.3
Deferred Income Taxes	199.3	169.6
Other Liabilities	360.4	389.3
Total Liabilities	1,332.8	1,297.9
<b>Commitments and Contingencies (Note 14)</b>		
<b>Equity</b>		
<b>ALLETE's Equity</b>		
<b>Common Stock Without Par Value, 80.0 Shares Authorized, 34.1 and 32.6 Shares Outstanding</b>		
	575.1	534.1
Unearned ESOP Shares	(48.3)	(54.9)
Accumulated Other Comprehensive Loss	(31.6)	(33.0)
Retained Earnings	380.0	380.9
Total ALLETE's Equity	875.2	827.1

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Non-Controlling Interest in Subsidiaries	9.6	9.8
Total Equity	884.8	836.9
Total Liabilities and Equity	\$2,217.6	\$2,134.8

The accompanying notes are an integral part of these statements.

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ALLETE  
CONSOLIDATED STATEMENT OF INCOME  
Millions Except Per Share Amounts – Unaudited

	Quarter Ended		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
<b>Operating Revenue</b>				
Operating Revenue	\$167.0	\$189.8	\$371.9	\$403.2
Prior Year Rate Refunds	(2.3)	–	(7.6)	–
Total Operating Revenue	164.7	189.8	364.3	403.2
<b>Operating Expenses</b>				
Fuel and Purchased Power	56.8	75.0	129.6	161.3
Operating and Maintenance	76.7	84.4	157.2	167.5
Depreciation	15.5	12.9	30.7	25.6
Total Operating Expenses	149.0	172.3	317.5	354.4
<b>Operating Income</b>	15.7	17.5	46.8	48.8
<b>Other Income (Expense)</b>				
Interest Expense	(8.4)	(6.6)	(17.1)	(12.6)
Equity Earnings in ATC	4.3	3.6	8.5	7.0
Other	1.9	2.5	3.0	11.1
Total Other Income (Expense)	(2.2)	(0.5)	(5.6)	5.5
<b>Income Before Non-Controlling Interest and Income Taxes</b>	13.5	17.0	41.2	54.3
<b>Income Tax Expense</b>	4.2	6.2	15.0	19.9
<b>Net Income</b>	9.3	10.8	26.2	34.4
Less: Non-Controlling Interest in Subsidiaries	(0.1)	0.1	(0.1)	0.1
<b>Net Income Attributable to ALLETE</b>	\$9.4	\$10.7	\$26.3	\$34.3
<b>Average Shares of Common Stock</b>				
Basic	31.8	28.8	31.3	28.7
Diluted	31.8	28.9	31.4	28.8
<b>Basic and Diluted Earnings Per Share of Common Stock</b>	\$0.29	\$0.37	\$0.84	\$1.19
<b>Dividends Per Share of Common Stock</b>	\$0.44	\$0.43	\$0.88	\$0.86

The accompanying notes are an integral part of these statements.



ALLETE  
CONSOLIDATED STATEMENT OF CASH FLOWS  
Millions - Unaudited

	Six Months Ended	
	June 30,	
	2009	2008
<b>Operating Activities</b>		
Net Income	\$26.2	\$34.4
Allowance for Funds Used During Construction	(2.9)	(2.0)
Income from Equity Investments, Net of Dividends	(0.5)	(1.0)
Gain on Sale of Assets	–	(4.6)
Gain on Sale of Available-for-Sale Securities	–	(6.5)
Depreciation Expense	30.7	25.6
Amortization of Debt Issuance Costs	0.4	0.4
Deferred Income Tax Expense	24.0	9.1
Stock Compensation Expense	1.1	0.8
Bad Debt Expense	0.6	0.5
Changes in Operating Assets and Liabilities		
Accounts Receivable	(5.0)	19.7
Inventories	(3.9)	(4.2)
Prepayments and Other	(1.5)	11.1
Accounts Payable	(3.5)	(15.5)
Other Current Liabilities	9.4	(0.6)
Other Assets	(4.3)	(4.9)
Other Liabilities	(7.1)	(7.6)
Cash from Operating Activities	63.7	54.7
<b>Investing Activities</b>		
Proceeds from Sale of Available-for-Sale Securities	0.9	52.3
Payments for Purchase of Available-for-Sale Securities	(0.9)	(39.3)
Investment in ATC	(3.5)	(2.8)
Changes to Other Investments	5.2	6.5
Additions to Property, Plant and Equipment	(133.3)	(130.5)
Proceeds from Sale of Assets	–	20.2
Other	(3.4)	(3.0)
Cash for Investing Activities	(135.0)	(96.6)
<b>Financing Activities</b>		
Proceeds from Issuance of Common Stock	27.9	7.9
Proceeds from Issuance of Long-Term Debt	43.3	138.7
Reductions of Long-Term Debt	(1.8)	(8.2)
Debt Issuance Costs	(0.5)	(1.1)
Dividends on Common Stock	(27.2)	(25.6)
Changes in Notes Payable	–	6.0
Cash from Financing Activities	41.7	117.7
Change in Cash and Cash Equivalents	(29.6)	75.8
Cash and Cash Equivalents at Beginning of Period	102.0	23.3

Cash and Cash Equivalents at End of Period	\$72.4	\$99.1
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The accompanying notes are an integral part of these statements.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X and do not include all of the information and notes required by GAAP for complete financial statements. Similarly, the December 31, 2008 consolidated balance sheet was derived from audited financial statements but does not include all disclosures required by GAAP. All adjustments are of a normal, recurring nature, except as otherwise disclosed. Certain prior year amounts within operating activities in our consolidated statement of cash flows have been reclassified between line items for comparative purposes. The reclassifications did not affect our net income or cash flows from operating activities. In the opinion of management, the accompanying unaudited consolidated financial statements contain all normal and recurring adjustments necessary to make a fair statement of the consolidated financial position, results of operations and cash flows of ALLETE for the interim periods presented. Operating results for the period ended June 30, 2009, are not necessarily indicative of results that may be expected for any other interim period or for the year ending December 31, 2009. For further information, refer to the consolidated financial statements and notes included in our 2008 Form 10-K and Form 10-K/A.

Subsequent Events. The Company performed an evaluation of subsequent events for potential recognition and disclosure through the time of issuing the financial statements on August 5, 2009.

## NOTE 1. OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Inventories. Inventories are stated at the lower of cost or market. Amounts removed from inventory are recorded on an average cost basis.

	June 30, December 31,	
	2009	2008
Inventories		
Millions		
Fuel	\$21.7	\$16.6
Materials and Supplies	31.9	33.1
Total Inventories	\$53.6	\$49.7

Other Assets and Other Liabilities.

	June 30, December 31,	
	2009	2008
Other Assets		
Millions		
Deferred Regulatory Assets	\$253.2	\$249.3
Other	32.6	32.1
Total Other Assets	\$285.8	\$281.4

Other Liabilities

Millions

Future Benefit Obligation Under Defined Benefit Pension and Other Postretirement Plans	\$221.8	\$251.8
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Deferred Regulatory Liabilities	60.6	50.0
Asset Retirement Obligation	43.3	39.5
Other	34.7	48.0
Total Other Liabilities	\$360.4	\$389.3

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## NOTE 1. OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

## Supplemental Statement of Cash Flows Information.

For the Six Months Ended June 30,	2009	2008
Millions		
Cash Paid During the Period for		
Interest – Net of Amounts Capitalized	\$13.6	\$11.8
Income Taxes	\$0.8	\$4.2
Noncash Investing and Financing Activities		
Change in Accounts Payable for Capital Additions to Property Plant and Equipment	\$(13.2)	\$12.0
ALLETE Common Stock contributed to the Pension Plan	\$(12.0)	–

New Accounting Standards. FSP FAS 157-2. In February 2008, the FASB issued FSP FAS 157-2, "Effective Date of FASB Statement 157," which delayed the effective date of SFAS 157 for all nonrecurring fair value measurements of nonfinancial assets and liabilities until fiscal years beginning after November 15, 2008. The implementation of FSP FAS 157-2 did not have a material impact on our consolidated financial position, results of operations or cash flows. (See Note 5. Fair Value.)

SFAS 160. In December 2007, the FASB issued SFAS 160, "Non-controlling Interests in Consolidated Financial Statements – an amendment of Accounting Research Bulletin (ARB) 51," to improve the relevance, comparability, and transparency of the financial information a reporting entity provides in its consolidated financial statements. SFAS 160 amends ARB 51 to establish accounting and reporting standards for non-controlling interests in subsidiaries and to make certain consolidation procedures consistent with the requirements of SFAS 141R. SFAS 160 defines a non-controlling interest in a subsidiary as an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. SFAS 160 changes the presentation of the consolidated income statement by requiring consolidated net income to include amounts attributable to the parent and the non-controlling interest. SFAS 160 establishes a single method of accounting for changes in a parent's ownership interest in a subsidiary which do not result in deconsolidation. SFAS 160 also requires expanded disclosures that clearly identify and distinguish between the interests of the parent and the interests of the non-controlling owners of a subsidiary. SFAS 160 is effective for financial statements issued for fiscal years beginning on or after December 15, 2008, and interim periods within those fiscal years. SFAS 160 shall be applied prospectively, with the exception of the presentation and disclosure requirements, which shall be applied retrospectively for all periods presented. SFAS 160 was adopted on January 1, 2009. ALLETE Properties does have certain non-controlling interests in consolidated subsidiaries. SFAS 160 impacted the presentation, but did not have a material impact on our consolidated financial position, results of operations or cash flows.

SFAS 161. In March 2008, the FASB issued SFAS 161, "Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement 133." SFAS 161 amends and expands the disclosure requirements of SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," by requiring enhanced disclosures about how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. SFAS 161 was adopted on January 1, 2009. As SFAS 161 provides only disclosure

requirements, the adoption of this standard did not have an impact on our consolidated financial position, results of operations or cash flows. (See Note 4. Derivatives.)

FSP FAS 132(R)-1. In December 2008, the FASB issued FSP FAS 132(R)-1. This FSP amends SFAS 132(R), "Employers' Disclosures about Pensions and Other Postretirement Benefits," to provide guidance on an employer's disclosures about plan assets, including employers' investment strategies, major categories of plan assets, concentrations of risk within plan assets, and valuation techniques used to measure the fair value of plan assets. This FSP is effective for fiscal years ending after December 15, 2009. Upon initial adoption, the provisions of this FSP are not required for earlier periods that are presented for comparative purposes. As FSP FAS 132(R)-1 provides only disclosure requirements, the adoption of this standard will not have an impact on our consolidated financial position, results of operations or cash flows.

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NOTE 1. OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

FSP FAS 107-1 and APB 28-1. In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1, "Interim Disclosures about Fair Value of Financial Instruments," which amends SFAS 107, "Disclosures about Fair Value of Financial Instruments" and APB Opinion 28, "Interim Financial Reporting," respectively, to require disclosure about fair value of financial instruments for interim reporting periods of publicly traded companies in addition to annual financial statements. FSP FAS 107-1 and APB 28-1 was adopted on June 30, 2009. As FSP FAS 107-1 and APB 28-1 provide only disclosure requirements, the adoption of this standard did not have a material impact on our consolidated financial position, results of operations or cash flows. (See Note 5. Fair Value.)

FSP FAS 157-4. In April 2009, the FASB issued FSP FAS 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly," which provides additional guidance for applying the provisions of SFAS 157. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants under current market conditions. This FSP requires an evaluation of whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. If there has, transactions or quoted prices may not be indicative of fair value and a significant adjustment may need to be made to those prices to estimate fair value. Additionally, an entity must consider whether the observed transaction was orderly (that is, not distressed or forced). If the transaction was orderly, the obtained price can be considered a relevant observable input for determining fair value. If the transaction is not orderly, other valuation techniques must be used when estimating fair value. FSP FAS 157-4 was adopted on June 30, 2009, and did not have a material impact on our consolidated financial position, results of operations or cash flows.

FSP FAS 115-2 and FAS 124-2. In April 2009, the FASB issued FSP FAS 115-2 and FAS 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments," which amends SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities" and SFAS 124, "Accounting for Certain Investments Held by Not-for-Profit Organizations." This standard establishes a different other-than-temporary impairment indicator for debt securities than previously prescribed. If it is more likely than not that an impaired security will be sold before the recovery of its cost basis, either due to the investor's intent to sell or because it will be required to sell the security, the entire impairment is recognized in earnings. Otherwise, only the portion of the impaired debt security related to estimated credit losses is recognized in earnings, while the remainder of the impairment is recorded in other comprehensive income and recognized over the remaining life of the debt security. In addition, the standard expands the presentation and disclosure requirements for other-than-temporary impairments for both debt and equity securities. FSP FAS 115-2 and FAS 124-2 was adopted on June 30, 2009, and did not have an impact on our consolidated financial position, results of operations or cash flows.

SFAS 165. In May 2009, the FASB issued SFAS 165, "Subsequent Events," to provide guidance on accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Entities are required to disclose the date through which subsequent events have been evaluated and the basis for that date. SFAS 165 was adopted on June 30, 2009, and did not have a material impact on our consolidated financial position, results of operations, or cash flows.

SFAS 166. In June 2009, the FASB issued SFAS 166 "Accounting for Transfers of Financial Assets, an amendment of SFAS 140." SFAS 166 amends current guidance for accounting for the transfers of financial assets, and was issued with the objective of improving the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. Key provisions of SFAS 166 include (1) the removal of the concept of qualifying special purpose entities, (2) the introduction of the concept of a participating interest, in circumstances in which a portion of a

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financial asset has been transferred, and (3) the requirement that to qualify for sale accounting, the transferor must evaluate whether it maintains effective control over transferred financial assets either directly or indirectly. Further, SFAS 166 requires enhanced disclosures about transfers of financial assets and a transferor's continuing involvement. SFAS 166 is effective January 1, 2010, and is required to be applied prospectively. We are currently assessing the impact of SFAS 166 on our consolidated financial position, results of operations and cash flows, but we do not believe it will have a material impact on the Company.

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## NOTE 1. OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

SFAS 167. In June 2009, the FASB issued SFAS 167 “Amendments to FASB Interpretation No. 46(R).” SFAS 167 amends the manner in which entities evaluate whether consolidation is required for variable interest entities (VIEs). A company must first perform a qualitative analysis in determining whether it must consolidate a VIE, and if the qualitative analysis is not determinative, must perform a quantitative analysis. Further, SFAS 167 requires that companies continually evaluate VIEs for consolidation, rather than assessing based upon the occurrence of triggering events. SFAS 167 also requires enhanced disclosures about how an entity’s involvement with a VIE affects its financial statements and exposure to risks. SFAS 167 is effective January 1, 2010. We are currently assessing the impact of SFAS 167 on our consolidated financial position, results of operations and cash flows, but we do not believe it will have a material impact on the Company.

SFAS 168. In June 2009, the FASB approved the FASB Accounting Standards Codification (Codification) as the single source of authoritative nongovernmental GAAP. The Codification is an online research system that reorganizes the thousands of GAAP pronouncements into a topical structure. The Codification was launched on July 1, 2009; at which time all existing accounting standard documents were superseded and all accounting literature not included in the Codification were considered non-authoritative, except for guidance issued by the SEC. The Codification is effective for interim and annual periods ending after September 15, 2009.

## NOTE 2. BUSINESS SEGMENTS

Regulated Operations includes our regulated utilities, Minnesota Power and SWL&P, as well as our investment in ATC, a Wisconsin-based utility that owns and maintains electric transmission assets in parts of Wisconsin, Michigan, Minnesota and Illinois. Investments and Other is comprised primarily of BNI Coal, our coal mining operations in North Dakota, and ALLETE Properties, our Florida real estate business. This segment also includes Emerging Technology Investments, a small amount of non-rate base generation, approximately 7,000 acres of land for sale in Minnesota, and earnings on cash and short-term investments.

	Consolidated	Regulated Operations	Investments and Other
Millions			
For the Quarter Ended June 30, 2009			
Operating Revenue	\$167.0	\$147.4	\$19.6
Prior Year Rate Refunds	(2.3)	(2.3)	–
Total Operating Revenue	164.7	145.1	19.6
Fuel and Purchased Power	56.8	56.8	–
Operating and Maintenance	76.7	56.9	19.8
Depreciation Expense	15.5	14.3	1.2
Operating Income (Loss)	15.7	17.1	(1.4)
Interest Expense	(8.4)	(6.6)	(1.8)
Equity Earnings in ATC	4.3	4.3	–
Other Income	1.9	1.7	0.2
Income (Loss) Before Non-Controlling Interest and Income Taxes	13.5	16.5	(3.0)
Income Tax Expense (Benefit)	4.2	5.8	(1.6)
Net Income (Loss)	9.3	10.7	(1.4)
Less: Non-Controlling Interest in Subsidiaries	(0.1)	–	(0.1)
Net Income (Loss) Attributable to ALLETE	\$9.4	\$10.7	\$(1.3)



## NOTE 2. BUSINESS SEGMENTS (Continued)

	Consolidated	Regulated Operations	Investments and Other
Millions			
For the Quarter Ended June 30, 2008			
Operating Revenue	\$189.8	\$163.5	\$26.3
Fuel and Purchased Power	75.0	75.0	—
Operating and Maintenance	84.4	63.5	20.9
Depreciation Expense	12.9	11.7	1.2
Operating Income	17.5	13.3	4.2
Interest Expense	(6.6)	(5.6)	(1.0)
Equity Earnings in ATC	3.6	3.6	—
Other Income	2.5	1.1	1.4
Income Before Non-Controlling Interest and Income Taxes	17.0	12.4	4.6
Income Tax Expense	6.2	5.2	1.0
Net Income	10.8	7.2	3.6
Less: Non-Controlling Interest in Subsidiaries	0.1	—	0.1
Net Income Attributable to ALLETE	\$10.7	\$7.2	\$3.5

	Consolidated	Regulated Operations	Investments and Other
Millions			