ORDER GRANTING PETITION FOR DECLARATORY ORDER

(Issued April 16, 2004)

1. In this order, the Commission grants a petition for declaratory order (Petition) filed by ALLETE, Inc. (ALLETE) seeking a Commission ruling that its proposed distribution of all the common stock in ALLETE’s indirect wholly-owned subsidiary, the ADESA Corporation (ADESA), is not prohibited by section 305(a) of the Federal Power Act (FPA)\(^1\) and that ALLETE’s proposed accounting for the distribution is in accordance with the Commission’s accounting requirements.\(^2\) This order is beneficial because it allows ALLETE to make maximum use of its jurisdictional assets to the benefit of both ALLETE’s ratepayers and shareholders.

I. Participants

2. ALLETE is an electric utility engaged in the generation, transmission and sale of electricity in the upper Midwest. Minnesota Power, an electric utility operating division of ALLETE, is an integrated public utility that is engaged in the generation, transmission and distribution of electricity to customers throughout northeastern Minnesota.\(^3\) Superior Water, Light and Power Company (SWL&P), an electric utility subsidiary of ALLETE,

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\(^1\) 16 U.S.C. § 825d (2000). Section 305(a) of the FPA states that “it shall be unlawful for any officer or director of any public utility… to participate in the making or paying of any dividends of such public utility from any funds properly included in capital account.”


\(^3\) Minnesota Power’s operations are subject to regulation by the Minnesota Public Utilities Commission as well as by this Commission.
is engaged in the retail sale of electricity, natural gas and water service to customers in adjacent areas of northwestern Wisconsin.\(^4\) ALLETE also has investments in certain independent power generation facilities and power marketers in the region.

3. In 1995, ALLETE acquired ADESA, a full service automotive vehicle remarketing company. ADESA owns and operates the second largest wholesale automobile auction network in North America. Through its wholly-owned subsidiaries and other related entities, ADESA owns (or leases) and operates 53 wholesale automobile auction facilities in the United States and Canada. For the twelve-month period ending December 31, 2003, the revenues of ADESA represented approximately 57 percent of the consolidated revenues of ALLETE and its subsidiaries, and for the same period, the net income of ADESA represented approximately 80 percent of the consolidated net income from continuing operations of ALLETE and its subsidiaries.

II. ALLETE’s Petition and the Proposed Transaction

4. On February 9, 2004, ALLETE filed a petition for declaratory order seeking a Commission ruling that its proposed distribution of common stock of ADESA to ALLETE’s shareholders is not prohibited by section 305(a) of the FPA and that the manner in which it is proposing to account for the distribution is permissible under the Uniform System of Accounts. ALLETE states that it hopes to begin the first phase of transactions related to the distribution of the common stock of ADESA in early April, 2004. In its Petition, ALLETE proposes to separate the automotive re-marketing and financing activities of ADESA from its regulated utility operations through a distribution of the common stock that ALLETE holds in ADESA. This distribution will be accomplished as a tax-free stock dividend to ALLETE’s shareholders, who will receive a proportionate share of the common stock of ADESA based on their relative ownership of ALLETE stock. Immediately following the distribution, ALLETE states that the interests of its stockholders in ADESA and in ALLETE’s other businesses will be the same as they were immediately prior to the distribution. However, those interests will be represented by stock holdings in two separate publicly traded companies instead of one. ADESA common stock will be listed on the New York Stock Exchange and will be publicly traded independently of the stock of ALLETE.

5. ALLETE states that its board of directors and management recognize the importance of structuring the separation in a manner that protects the financial well-being of ALLETE so that there will be no impairment of its ability to deliver utility services. Therefore, prior to the separation ALLETE and ADESA will enter into recapitalization and debt reallocation transactions that are expected to establish a post-spin capital structure for ALLETE of roughly 50 percent or higher equity. ALLETE asserts that the

\(^4\) SWL&P’s retail operations are subject to regulation by the Public Service Commission of Wisconsin.
board and management have established a goal of maintaining or improving ALLETE’s current investment grade credit rating.

6. ALLETE explains that it would be beneficial for its electric utility operations and its automotive re-marketing and financing businesses to be independent of each other. ALLETE states that its regulated electric utility business has growth characteristics, capital requirements, risk profiles, regulatory burdens and workforce characteristics that are very different from those associated with the automotive re-marketing and financing businesses in which ADESA participates. ALLETE states that, as a stand-alone company free of the constraints associated with its continued affiliation with ALLETE, ADESA will be better positioned to pursue growth opportunities and develop a capital structure better suited to its business. For the utility and other remaining operations of ALLETE, it states that the separation of ADESA from ALLETE will create a simplified regulatory and risk profile and a more stable credit rating, which will enhance its ability to pursue its own strategic growth initiatives. Conversely, ALLETE states that as long as ADESA remains a subsidiary of ALLETE, the substantially different risks and potential rewards of each of these two lines of business hinder their ability to pursue strategies that will enable them to maximize their long-term value. The separation will also enable each business to raise both debt and equity capital in the future more efficiently.

7. ALLETE argues that its proposed corporate separation is similar to the restructuring that the Commission found permissible under section 305(a) of the FPA in Citizens Utilities Company. ALLETE explains that in its case, as in Citizens, a public utility that owns a non-utility subsidiary proposed to distribute the stock in the subsidiary to its stockholders and the goal of the distribution was to enhance the treatment of the company as a public utility company in capital markets. ALLETE also asserts that none of the potential abuses identified by the Commission in Citizens, under section 305(a) of the FPA, exist in ALLETE’s case. ALLETE explains that: (1) the source of the distribution of stock in ADESA has been clearly identified and the distribution itself is not excessive, but simply represents the value of ALLETE’s investment in ADESA; (2) the proposed separation of ADESA from ALLETE will have no adverse effect on the value of shareholders’ interests; and (3) shareholders will have the same ownership interests in the utility and non-utility businesses of ALLETE after the distribution as

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5 ALLETE asserts that the Commission has endorsed the clear separation of utility businesses from non-utility businesses. ALLETE points to Westar Energy, Inc., 102 FERC ¶ 61,186 (2003), where the Commission announced its intention to impose certain restrictions on all future public utility issuances of debt authorized by the Commission in order to prevent public utilities from borrowing substantial amounts of monies and using the proceeds to finance non-utility businesses. ALLETE Petition at 8.

6 84 FERC ¶ 61,158 at 61,865 (1998) (Citizens).
before; it simply will be ownership of stock in two companies rather than one.\(^7\) As a result, ALLETE states that the Commission should find that the distribution of stock in ADESA is permissible under the FPA.

8. Notice of ALLETE’s filing was published in the Federal Register, 69 Fed. Reg. 8399 (2004), with comments, protests, or interventions due on or before March 1, 2004. None was filed.

III. Discussion

9. We will grant ALLETE’s Petition because the concerns underlying section 305(a) of the FPA are not present in the circumstances of this transaction. Section 305(a) of the FPA reads:

   It shall be unlawful for any officer or director of any public utility to receive for his own benefit, directly or indirectly, any money or thing of value in respect of the negotiation, hypothecation, or sale by such public utility of any security issued or to be issued by such public utility, or to share in any of the proceeds thereof, or to participate in the making or paying of any dividends of such public utility from any funds properly included in capital account.\(^8\)

10. The concerns underlying the enactment of section 305(a) of the FPA included “that sources from which cash dividends were paid were not clearly identified and that holding companies had been paying out excessive dividends on the securities of their operating companies.”\(^9\) A central concern thus “was corporate officials raiding corporate coffers for their personal financial benefit.”\(^10\) The record in this case justifies no such concerns.

11. The Commission finds that the source of ALLETE’s proposed distribution has been clearly identified and nothing indicates that the distribution will be excessive or preferential, but simply represents the value of ALLETE’s investment in ADESA. This

\(^7\) ALLETE Petition at 6-7.


\(^10\) Id.
value is based on the amount originally invested by ALLETE in the common stock of ADESA and the unappropriated undistributed earnings of ADESA. Moreover, the proposed separation of ADESA from ALLETE will have no adverse effect on the value of shareholders’ interests. Shareholders will have the same ownership interests in the utility and non-utility businesses of ALLETE after the distribution as before; “it will simply be ownership of stock in two companies rather than one.” Further, the separation of ADESA is less like a payment of dividends than it is a corporate restructuring with a one-time distribution of property, involving a transfer of stock in a non-utility company, rather than a payment of cash. For these reasons, and under the circumstances of this case, we grant the Petition and find that section 305(a) is not a bar to ALLETE’s capital structure realignment and the proposed distribution of ADESA’s common stock to its parents’ common stock shareholders. However, the Commission expects, as ALLETE states in its Petition, that ALLETE will establish a post-spin capital structure of 50 percent or higher equity in order to maintain or improve ALLETE’s current investment grade credit rating.

12. We also approve the proposed accounting related to the distribution of ADESA common stock. In implementing the spin-off of ADESA, ALLETE will assume that its entire capital contribution to acquire ADESA was funded with the proceeds of common stock that had been issued by ALLETE. Accordingly, the spin-off of ADESA will be accomplished in part through a distribution to shareholders of amounts recorded in Account 201 - Common Stock Issued, while the remainder will represent a distribution to common shareholders of ALLETE of the net undistributed earnings of ADESA. Consequently, ALLETE proposes to record its spin-off of ADESA by: (1) debiting Account 216.1 for the amount of its equity in the undistributed earnings of ADESA ($424.8 million); (2) crediting Account 123.1 for the value of its investment in ADESA ($950.1 million); and (3) debiting Account 201 for the remaining equity investment of ALLETE in ADESA ($525.3 million).

11 Citizens, 84 FERC at 61,865.
The Commission orders:

(A) The petition for declaratory order is hereby granted, as discussed in the body of the order.

(B) ALLETE’s proposed accounting is hereby approved, as discussed in the body of this order.

By the Commission.

(SEAL)

Magalie R. Salas, Secretary.