SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)
/X/ Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the Fiscal Year Ended DECEMBER 31, 1997

/ / 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. 1-3548

MINNESOTA POWER & LIGHT COMPANY
(Exact name of registrant as specified in its charter)

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

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

Registrant's telephone number, including area code (218) 722-2641

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

Title of Each Class	Name of Each Stock Exchange on Which Registered
Common Stock, without par value	New York Stock Exchange
5% Cumulative Preferred Stock, par value $100 per share	American Stock Exchange
8.05% Cumulative Quarterly Income Preferred Securities of MP&L Capital I, a subsidiary of Minnesota Power & Light Company	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
Preferred Stock, without par value

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

Yes /X/ No / /

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

The aggregate market value of voting stock held by nonaffiliates on March 2, 1998 was $1,370,119,250.

As of March 2, 1998 there were 33,699,517 shares of Minnesota Power & Light Company Common Stock, without par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Minnesota Power 1997 Annual Report are incorporated by reference in Part II, Items 7 and 8, and portions of the Proxy Statement for the 1998 Annual Meeting of Shareholders are incorporated by reference in Part III.

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DEFINITIONS

The following abbreviations or acronyms are used in the text.

ABBREVIATION OR ACRONYMS	TERM
ADESA	ADESA Corporation
AFC	Automotive Finance Corporation
Americas' Water	Americas' Water Services Corporation
BNI Coal	BNI Coal, Ltd.
Boswell	Boswell Energy Center
Capital Re	Capital Re Corporation
CIP	Conservation Improvement Program(s)
Company	Minnesota Power & Light Company and its Subsidiaries
Duluth	City of Duluth, Minnesota
EPA	Environmental Protection Agency
FERC	Federal Energy Regulatory Commission
Florida Water	Florida Water Services Corporation
FPSC	Florida Public Service Commission
Great Rigs	Great Rigs Incorporated
Heater	Heater Utilities, Inc.
Hibbard	M.L. Hibbard Station
ISI	Instrumentation Services, Inc.
Laskin	Laskin Energy Center
Lehigh	Lehigh Acquisition Corporation
MAPP	Mid-Continent Area Power Pool
MBtu	Million British thermal units
Minnesota Power	Minnesota Power & Light Company and its Subsidiaries
Minnkota Power	Minnkota Power Cooperative, Inc.
MP Telecom	Minnesota Power Telecom, Inc.
MPCA	Minnesota Pollution Control Agency
MPUC	Minnesota Public Utilities Commission
MW	Megawatt(s)
MWh	Megawatthour
NCUC	North Carolina Utilities Commission
Note_	Note __ to the consolidated financial statements in the Minnesota Power 1997 Annual Report
NPDES	National Pollutant Discharge Elimination System
PSCW	Public Service Commission of Wisconsin
Square Butte	Square Butte Electric Cooperative
SWL&P	Superior Water, Light and Power Company
U.S. Maintenance and Management	U.S. Maintenance and Management Services Corporation
WPPI	Wisconsin Public Power, Inc.

SAFE HARBOR STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

In connection with the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 (Reform Act), the Company is hereby filing cautionary statements identifying important factors that could cause the Company's actual results to differ materially from those projected in forward-looking statements (as such term is defined in the Reform Act) made by or on behalf of the Company in this annual report on Form 10-K, in presentations, in response to questions or otherwise. Any statements that express, or involve discussions as to expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, through the use of words or phrases such as "anticipates", "believes", "estimates", "expects", "intends", "plans", "predicts", "projects", "will likely result", "will continue", or similar expressions) are not statements of historical facts and may be forward-looking.

Forward-looking statements involve estimates, assumptions, and uncertainties and are qualified in their entirety by reference to, and are accompanied by, the following important factors, which are difficult to predict, contain uncertainties, are beyond the control of the Company and may cause actual results to differ materially from those contained in forward-looking statements:

- prevailing governmental policies and regulatory actions, including those of the FERC, the MPUC, the FPSC, the NCUC and the PSCW, with respect to allowed rates of return, industry and rate structure, acquisition and disposal of assets and facilities, operation and construction of plant facilities, recovery of purchased power, and present or prospective wholesale and retail competition (including but not limited to retail wheeling and transmission costs);
- economic and geographic factors including political and economic risks;
- changes in and compliance with environmental and safety laws and policies;
- weather conditions;
- population growth rates and demographic patterns;
- competition for retail and wholesale customers;
- pricing and transportation of commodities;
- market demand, including structural market changes;
- changes in tax rates or policies or in rates of inflation;
- changes in project costs;
- unanticipated changes in operating expenses and capital expenditures;
- capital market conditions;
- competition for new energy development opportunities; and
- legal and administrative proceedings (whether civil or criminal) and settlements that influence the business and profitability of the Company.

Any forward-looking statement speaks only as of the date on which such statement is made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such 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 such factors, nor can it assess the impact of any such factor on the business or the extent to which any factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement.

PART I

ITEM 1. BUSINESS.

Minnesota Power, a broadly diversified service company incorporated under the laws of the State of Minnesota in 1906, has operations in four business segments: (1) Electric Operations, which include electric and gas services, and coal mining; (2) Water Services, which include water and wastewater services; (3) Automotive Services, which include a network of vehicle auctions, a finance company and an auto transport company; and (4) Investments, which include a securities portfolio, a 21 percent equity investment in a financial guaranty reinsurance and insurance company and real estate operations. Corporate Charges represent general corporate expenses, including interest, not specifically related to any one business segment. As of December 31, 1997 the Company and its subsidiaries had approximately 6,800 employees.

	1997	1996	1995
		Millions	
Operating Revenue and Income			
Electric Operations	$ 541.9	$ 529.2	$ 503.5
Water Services	95.5	85.2	66.1
Automotive Services (a)	255.5	183.9	61.6
Investments	60.9	49.9	43.7
Corporate Charges	(0.2)	(1.3)	(2.0)
	$ 953.6	$ 846.9	$ 672.9
Net Income			
Electric Operations	$ 43.1	$ 39.4	$ 41.0
Water Services	8.2	5.4	(1.0)
Automotive Services (a)	14.0	3.7	-
Investments	32.1	38.1	41.3
Corporate Charges	(19.8)	(17.4)	(19.4)
	77.6	69.2	61.9
Discontinued Operations (b)	-	-	2.8
	$ 77.6	$ 69.2	$ 64.7
Basic and Diluted Earnings Per Share of Common Stock	$2.47	$2.28	$2.16
Average Shares of Common Stock - Millions	30.6	29.3	28.5

(a) The Company purchased 80 percent of ADESA, including AFC and Great Rigs, on July 1, 1995, another 3 percent in January 1996 and the remaining 17 percent in August 1996.

(b) On June 30, 1995 the Company sold its interest in the paper and pulp business to Consolidated Papers, Inc.

Since 1983 Minnesota Power has been diversifying to reduce its reliance on electricity sales to Minnesota's taconite industry and to gain additional earnings growth potential. Acquisitions have been a primary means of diversification. During 1997 the Company continued its corporate strategy of expanding existing business segments. Electric Operations created a telecommunications subsidiary, while Water Services acquired a water subsidiary and established two non-regulated subsidiaries. Automotive Services added two auction facilities and 25 loan production offices. The Company plans to consider other acquisitions that would complement its businesses, expand its services and contribute to earnings growth.

For a detailed discussion of results of operations and trends, see Management's Discussion and Analysis of Financial Condition and Results of Operations in the Minnesota Power 1997 Annual Report. For business segment information, see Note 1.

ELECTRIC OPERATIONS

Electric Operations generate, transmit, distribute and market electricity. In addition Electric Operations include coal mining, telecommunications and economic development projects within the Company's service area. Electric Operations intend to seek cost saving alternatives and efficiencies, and expand non-regulated services.

- MINNESOTA POWER provides electricity in a 26,000 square mile electric service territory located in northeastern Minnesota. As of December 31, 1997 Minnesota Power was supplying retail electric service to 122,000 customers in 153 cities, towns and communities, and outlying rural areas. The largest city served is Duluth with a population of 85,000 based on the 1990 census. Wholesale electric service for resale is supplied to 15 municipal distribution systems, one private utility and SWL&P.

  MPEX, a division of Minnesota Power, is an expansion of the Company's inter-utility marketing group which has been a buyer and seller of capacity and energy for over 25 years in the wholesale power market. The customers of MPEX are other power suppliers in the Midwest and Canada. MPEX also contracts with its customers to provide hourly energy scheduling and power trading services.

- SUPERIOR WATER, LIGHT AND POWER COMPANY sells electricity and natural gas, and provides water service in northwestern Wisconsin. As of December 31, 1997 SWL&P served 14,000 electric customers, 11,000 natural gas customers and 10,000 water customers.

- BNI COAL owns and operates a lignite mine in North Dakota. Two electric generating cooperatives, Minnkota Power and Square Butte, presently consume virtually all of BNI Coal's production of lignite coal under coal supply agreements extending to 2027. Under an agreement with Square Butte, Minnesota Power purchases about 71 percent of the output from the Square Butte unit which is capable of generating up to 455 MW. Minnkota Power has an option to extend its coal supply agreement to 2042. (See - Fuel and Note 5.)

- ELECTRIC OUTLET, INC. is a retail store that sells life-style changing electric products and also researches new products to be offered for sale and distribution.

- MINNESOTA POWER TELECOM, INC., formed in 1997, will provide high volume fiber optic and microwave communications to businesses across the Company's service territory.

- UPPER MINNESOTA PROPERTIES, INC. has invested in affordable housing projects located in Electric Operations' service territory. The Company is also an active participant in a variety of economic development projects throughout Electric Operations' service territory providing resources and expertise.

ELECTRIC SALES

The two major industries in Minnesota Power's service territory are taconite production, and paper and pulp mills. Taconite customers accounted for 31 percent of the Company's electric operating revenue and income in 1997 (32 percent in 1996; 35 percent in 1995). Paper and pulp customers accounted for 12 percent of electric operating revenue and income in 1997 (11 percent in 1996; 12 percent in 1995). Sales to other power suppliers accounted for 12 percent of electric operating revenue and income in 1997 (13 percent in 1996; 9 percent in 1995). As deregulation of the electric utility industry approaches, the Company believes the percentage of electric revenue from sales to other power suppliers will continue to increase. The percentage of electric revenue from taconite customers is expected to decrease as other strategic initiatives, including MPEX and MP Telecom, add to electric operating revenue and income.

Over the last five years, 80 percent of the domestic ore consumed by iron and steel plants in the United States has originated from plants within the Company's electric service territory. Taconite, an iron-bearing rock of relatively low iron content which is abundantly available in Minnesota, is an important domestic source of raw material for the steel industry. Taconite processing plants use large quantities of electric power to grind the ore-bearing rock, and agglomerate and pelletize the iron particles into taconite pellets. Annual taconite production in Minnesota was 47 million tons in 1997 (46 million tons in 1996;

47 million tons in 1995). Based on the Company's research of the taconite industry, 1998 Minnesota taconite production is anticipated to remain at or near the 1997 level. While taconite production is expected to continue at annual levels over 40 million tons, the long-term future of this cyclical industry is less certain. Production may decline gradually some time after the year 2008.

	Year Ended December 31,		
	1997	1996	1995
Total Electric Operating Revenue and Income - Millions	$541.9	$529.2	$503.5
Percentage of Total Electric Operating Revenue and Income			
Retail			
Industrial			
Taconite Producers	31%	32%	35%
Paper and Pulp Mills	12	11	12
Other Industrial	6	6	7
Total Industrial	49	49	54
Residential	12	12	11
Commercial	11	11	12
Other Retail	1	1	1
Sales to Other Power Suppliers	12	13	9
Other Revenue and Income	15	14	13
	100%	100%	100%

The Company's two largest customers represented 10 percent and 8 percent, respectively, of total electric operating revenue and income in 1997 (11 percent and 8 percent in 1996; 12 percent and 9 percent in 1995).

LARGE POWER CUSTOMER CONTRACTS

The Company has Large Power Customer contracts with five taconite producers, four paper and pulp mills, and two pipeline companies (Large Power Customers), each of which requires 10 MW or more of generating capacity. Large Power Customer contracts require the Company to have a certain amount of generating capacity available at all times. In turn each Large Power Customer is required to pay a minimum monthly demand charge that covers the fixed costs associated with having capacity available to serve the customer, including a return on common equity. Most contracts allow customers to establish the level of MW subject to a demand charge on a periodic (pool season) basis and require that a portion of their MW needs be committed on a take-or-pay basis for the entire term of the agreement. In addition to the demand charge, each Large Power Customer is billed an energy charge for each kilowatthour used that recovers the variable costs incurred in generating electricity. Six of the Large Power Customers have interruptible service for a portion of their needs which includes a discounted demand rate and energy priced at the Company's incremental cost after serving all firm power obligations. The Company also provides incremental production service for customer demand levels above the contract take-or-pay levels. There is no demand charge for this service and energy is priced at an increment above the Company's cost. Incremental production service is interruptible.

Each contract continues after the contract termination date, unless the required four-year advance notice of cancellation has been given. Such contracts minimize the impact on earnings that otherwise would result from significant reductions in kilowatthour sales to such customers. Large Power Customers are required to purchase their entire electric service requirements from the Company for the duration of their contracts. The rates and corresponding revenue associated with capacity and energy provided under these contracts are subject to change through the same regulatory process governing all retail electric rates. Minnesota Power has implemented a key account management process to heighten its focus on large commercial and industrial customers' needs, and anticipates continuing negotiations with these customers to explore options to respond to those needs. (See Regulatory Issues - Electric Rates.)

As of March 15, 1998 the minimum annual revenue the Company would collect under contracts with these Large Power Customers, assuming no electric energy use by these customers, is estimated to be $101.8, $78.3, $69.2, $66.5 and $47.3 million during the years 1998, 1999, 2000, 2001 and 2002, respectively. Based on past experiences and projected operating levels, the Company believes revenue from these Large Power Customers will be substantially in excess of the minimum contract amounts.

CONTRACT STATUS FOR MINNESOTA POWER LARGE POWER CUSTOMERS
AS OF MARCH 15, 1998

Customer	Location	Ownership	Earliest Termination Date
Eveleth Mines LLC	Eveleth, MN	45% Rouge Steel Co. 40% AK Steel Co. 15% Stelco Inc.	October 31, 1999
Hibbing Taconite Co.	Hibbing, MN	70.3% Bethlehem Steel Corp. 15% Cleveland-Cliffs Inc 14.7% Stelco Inc.	December 31, 2001
Inland Steel Mining Co.	Virginia, MN	Inland Steel Co.	December 31, 2007
U.S. Steel - Minntac	Mt. Iron, MN	USX Corporation	December 31, 2007
National Steel Pellet Co.	Keewatin, MN	National Steel Corp.	October 31, 2004
Blandin Paper Co.	Grand Rapids, MN	UPM-Kymmene Corporation	April 30, 2004
Boise Cascade Corp.	International Falls, MN	Boise Cascade Corp.	December 31, 2002
Lake Superior Paper Industries and Superior Recycled Fiber Industries	Duluth, MN	Consolidated Papers, Inc.	July 31, 2008
Potlatch Corp.	Cloquet, MN and Brainerd, MN	Potlatch Corp.	December 31, 2002
Lakehead Pipe Line Co. L.P.	Deer River, MN Floodwood, MN	Lakehead Pipe Line Partners, L.P.	April 30, 2001
Minnesota Pipeline Company	Staples, MN Little Falls, MN Park Rapids, MN	60% Koch Pipeline Co LP 40% Marathon Ashland Petroleum LLC	September 30, 2002

A contract amendment, which provides for the Company to continue to meet all of Eveleth Mines LLC's electric requirements through October 2008, has been filed for MPUC approval.

A contract amendment, which provides for the Company to continue to meet all of Hibbing Taconite Co.'s electric requirements through December 2008, has been filed for MPUC approval.

PURCHASED POWER

Minnesota Power has contracts to purchase capacity and energy from various entities. In addition to the contracts listed below, the Company has entered into various smaller purchased power contracts for the purposes of meeting its capacity needs or brokering power.

STATUS OF MINNESOTA POWER PURCHASED POWER CONTRACTS

Entity	Contract MW	Contract Period
Participation Power Purchases (a)		
Square Butte (b)	322	May 6, 1977 through December 31, 2007
LTV Steel	210	May 1, 1995 though April 30, 2000
Silver Bay Power	78	November 1, 1995 through October 31, 2000

(a) Participation power purchase contracts require the Company to pay the demand charges for generating capacity under contract and an energy charge for each MWh purchased. The selling entity is obligated to provide energy as scheduled by the Company from the generating unit specified in the contract as energy is available from that unit.

(b) Under an agreement extending through 2007 with Square Butte, Minnesota Power purchases about 71 percent of the output of a mine-mouth generating unit capable of generating up to 455 MW. The Square Butte generating unit is located near Center, North Dakota and is one of two lignite-fired units at Minnkota Power's Milton R. Young Generating Station. Reductions to about 49 percent of the output are provided for in the contract and, at the option of Square Butte, could begin after a five-year advance notice to the Company. The cost of the power and energy purchased is a proportionate share of Square Butte's fixed and variable costs. The Company is responsible for paying all costs and expenses of Square Butte (including leasing, operating and any debt service costs) if not paid by Square Butte when due. These obligations of the Company are absolute and unconditional, whether or not any power is actually delivered to the Company. (See Note 5.)

CAPACITY SALES

Minnesota Power has contracts to sell capacity to nonaffiliated utility companies. In addition to the contracts listed below, the Company has entered into various smaller capacity sales contracts for the purposes of selling surplus capacity or brokering power.

STATUS OF MINNESOTA POWER CAPACITY SALES CONTRACTS

Utility	Contract MW	Contract Period
Participation Power Sales (a)		
Interstate Power Company	55	May 1 through October 31 of each year from 1994 through 2000
	20	November 1, 1997 through April 30, 1998
	35	November 1, 1998 through April 30, 1999
	50	November 1, 1999 through April 30, 2000
Firm Power Sales (b)		
Wisconsin Power & Light Company	75	January 1, 1998 through December 31, 2007
Northern States Power Company	150	May 1 through October 31 of each year from 1997 through 2000

(a) Participation power sales contracts require the purchasing utility to pay the demand charges for MW under contract and an energy charge for each MWh purchased. The Company is obligated to provide energy as scheduled by the purchasing utility from the generating unit specified in the contract as energy is available from that unit.
(b) Firm power sales contracts require the purchasing utility to pay the demand charges for MW under contract and an energy charge for each MWh purchased. The Company is obligated to provide energy as scheduled by the purchasing utility.

FUEL

The Company purchases low-sulfur, sub-bituminous coal from the Powder River Basin coal field located in Montana and Wyoming. Coal consumption for electric generation at the Company's Minnesota coal-fired generating stations in 1997 was about 4.1 million tons. As of December 31, 1997 the Company had a coal inventory of about 497,000 tons. The Company has three coal supply agreements in place with Montana suppliers. Two terminate in December 1999 and the other terminates in December 2000. Under these agreements the Company has the tonnage flexibility to procure 70 percent to 100 percent of its total coal requirements. The Company will obtain coal in 1998 under these agreements and the spot market. This mix of coal supply options allows the Company to reduce market risk and to take advantage of favorable spot market prices. The Company is exploring future coal supply options and believes that adequate supplies of low-sulfur, sub-bituminous coal will continue to be available.

Burlington Northern Santa Fe Railroad transports the coal by unit train from Montana or Wyoming to the Company's generating stations. The Company and Burlington Northern Santa Fe Railroad have two long-term coal freight-rate contracts that provide for coal deliveries through 2002 to Laskin and through 2003 to Boswell. The Company also has a contract with the Duluth Missabe & Iron Range Railway which is the final destination short-hauler to Laskin. This contract provides for deliveries through 2002. The delivered price of coal is subject to periodic adjustments in freight rates.

	Year Ended December 31,		
COAL DELIVERED TO MINNESOTA POWER	1997	1996	1995
Average Price Per Ton	$20.26	$19.30	$19.19
Average Price Per MBtu	$1.11	$1.06	$1.07

The generating unit operated by Square Butte burns North Dakota lignite supplied by BNI Coal, a wholly owned subsidiary of the Company, pursuant to the terms of a contract expiring in 2027. Square Butte's cost of lignite burned in 1997 was approximately 64 cents per MBtu. The lignite acreage that has been dedicated to Square Butte by BNI Coal is located on lands essentially all of which are under private control and presently leased by BNI Coal. This lignite supply is sufficient to provide the fuel for the anticipated useful life of the generating unit. Under the various agreements with Square Butte, the Company is unconditionally obligated to pay all costs not paid by Square Butte when due. These costs include the price of lignite purchased under a cost-plus contract from BNI Coal. (See Item 2. Properties and Note 5.) BNI Coal has experienced no difficulty in supplying all of Square Butte's lignite requirements.

REGULATORY ISSUES

The Company and its subsidiaries are exempt from regulation under the Public Utility Holding Company Act of 1935, except as to Section 9(a)(2) which relates to acquisition of securities of public utility operations.

The Company and its subsidiaries are subject to the jurisdiction of various regulatory authorities. The MPUC has regulatory authority over Electric Operations' service area in Minnesota, retail rates, retail services, issuance of securities and other matters. The FERC has jurisdiction over the licensing of hydroelectric projects, the establishment of rates and charges for the sale of electricity for resale and transmission of electricity in interstate commerce, and certain accounting and record keeping practices. The PSCW has regulatory authority over the retail sales of electricity, water and gas by SWL&P. The MPUC, FERC and PSCW had regulatory authority over 68 percent, 12 percent, and 8 percent, respectively, of the Company's 1997 electric operating revenue and income.

ELECTRIC RATES

The Company has historically designed its electric service rates based on cost of service studies under which allocations are made to the various classes of customers. Nearly all retail sales include billing adjustment clauses which adjust electric service rates for changes in the cost of fuel and purchased energy, and recovery of current and deferred CIP expenditures.

The demand charge component of the Company's large power rate schedules are designed to recover the fixed costs of providing capacity to Large Power Customers, including a return on common equity. A Large Power Customer's monthly demand charge obligation in any particular month is determined based upon the firm demand amount. The rates and corresponding revenue associated with capacity and energy provided under these contracts are subject to change through the regulatory process governing all retail electric rates. Contracts with ten of the eleven Large Power Customers provide for deferral without interest or diminishment of one-half of demand charge obligations incurred during the first three months of a strike or illegal walkout at a customer's facilities, with repayment required over the 12-month period following resolution of the work stoppage. (See Electric Sales - Large Power Customer Contracts.)

The Company also has contracts with large industrial and commercial customers who have monthly demands of more than 2 MW but less than 10 MW of capacity (Large Light and Power Customers). The terms of these contracts vary depending upon the customers' demand for power and the cost of extending the Company's facilities to provide electric service. Generally, the contracts for less than 3 MW have one-year terms and the contracts ranging from 3 to 10 MW have initial five-year terms. The Company's rate schedule for Large Light and Power Customers is designed to minimize fluctuations in revenue and to recover a significant portion of the fixed costs of providing service to such customers.

The Company requires that all large industrial and commercial customers under contract specify the date when power is first required, and thereafter the customer is billed for at least the minimum power for which they contracted. These conditions are part of all contracts covering power to be supplied to new large industrial and commercial customers and to current customers as their contracts expire or are amended. All contracts provide that new rates which have been approved by appropriate regulatory authorities will be substituted immediately for obsolete rates, without regard to any unexpired term of the existing contract. All rate schedules are subject to approval by appropriate regulatory authorities.

FEDERAL ENERGY REGULATORY COMMISSION

The FERC has jurisdiction over the Company's wholesale electric service resale customers and transmission service (wheeling) customers.

The Company has long-term contracts with 15 Minnesota municipalities receiving resale service. Two contracts are for service through 2002 and 2004, while the other 13 are for service through at least 2007. The contracts limit rate increases (including fuel costs) to about 2 percent per year on a cumulative basis. In 1997 the 15 municipal customers purchased 615,422 MWh from the Company.

A contract between Minnesota Power and SWL&P provides for SWL&P to purchase its power from the Company through at least 2010 and limits rate increases (including fuel costs) to about 2 percent per year on a cumulative basis. SWL&P purchased 564,200 MWh from the Company in 1997.

The Company also has a contract through 2004 to supply electricity to Dahlberg Light and Power Company (Dahlberg), a private utility. Dahlberg purchased 86,434 MWh from the Company in 1997.

The Company's hydroelectric facilities, which are located in Minnesota, are licensed by the FERC. In 1995 the FERC issued to the Company a 30-year license for the St. Louis River hydroelectric project (87.6 MW generating capability). In 1996 the FERC extended the license term from 30 to 40 years because of certain mandates to mitigate environmental consequences of the project. In May 1997 the FERC issued an annual license for the Pillager hydroelectric project (1.5 MW generating capability) under the existing license terms and conditions. This annual license is effective until the new license is issued. (See Environmental Matters - Water.)

MINNESOTA PUBLIC UTILITIES COMMISSION

The Company's retail rates are based on a 1994 MPUC retail rate order which allows for an 11.6 percent return on common equity devoted to utility plant.

Minnesota requires investor owned electric utilities to spend a minimum of 1.5 percent of gross annual retail electric revenue on conservation improvement programs (CIP) each year. The MPUC approved a minimum statutory spending requirement of $5.1 million for 1997 ($5.1 million for 1996; $5.3 million for 1995). In 1997 the Company spent $5.8 million on CIP ($14.4 million in 1996; $14.2 million in 1995) and expects to spend a total of $11.9 million during 1998. The MPUC allows such conservation expenditures in excess of amounts recovered through current rates to be accumulated in a deferred account for future recovery. Through a billing adjustment and retail base rates approved by the MPUC, the Company is allowed to recover current and deferred CIP expenditures, a carrying charge on unrecovered expenditures and the lost margins associated with power saved as a result of these programs. The Company collected CIP related revenue of $13.7 million in 1997 ($10.8 million in 1996 and 1995).

CAPITAL EXPENDITURE PROGRAM

Capital expenditures for Electric Operations totaled $35 million during 1997. Internally generated funds and long-term financing were used to fund these capital expenditures. Electric Operations capital expenditures are expected to be $44 million in 1998 and total approximately $144 million during the period 1999 through 2002. The 1998 amount is for electric system component replacement and upgrades, telecommunication fiber and coal handling equipment. The Company's estimates of such capital expenditures and the sources of financing are subject to continuing review and adjustment.

COMPETITION

The electric utility industry continues to become more competitive at both the wholesale and retail levels. This is particularly the case in the wholesale markets. Retail deregulation of the industry is being considered at both the federal and state level, and effects the way the Company strategically views the future. With electric rates among the lowest in the United States and with long-term wholesale and Large Power Customer retail contracts in place, Minnesota Power believes Electric Operations are well positioned to address and benefit from competitive pressures.

WHOLESALE

Minnesota Power's MPEX division conducts an active wholesale power marketing and trading business, including participation in the new power and energy markets within the Mid-Continent Area Power Pool and other regional reliability councils. In 1997 Manitoba Hydro and Minnesota Power signed a three-year agreement whereby MPEX will provide Manitoba Hydro with exclusive hourly power trading and energy scheduling services in the United States. This agreement became effective January 1, 1998. Also in 1997 Manitoba Hydro and Minnesota Power signed a memorandum of understanding that establishes an alliance whereby the two utilities are and will market electric energy in the Midwest, including but not limited to Wisconsin, Michigan and Illinois. This memorandum strengthens the international relationship beyond the wholesale power trading agreement. Manitoba Hydro is the fourth largest electric utility in Canada. More than a third of Manitoba Hydro's electric sales represent exports of renewable hydroelectricity to the United States and neighboring provinces in Canada. MPEX is reviewing new strategic opportunities for its wholesale marketing operations in light of the new Open Access Transmission Rules enacted by the FERC in 1996. The Company also has wholesale contracts with a number of municipal customers. (See Regulatory Issues - Federal Energy Regulatory Commission.)

In 1996 the Company completed functional unbundling of its operations under FERC Order No. 888, "Open Access Transmission Rules." This order requires public utilities to take transmission service for their own wholesale transactions under the same terms and conditions on which transmission service is provided to third parties. Also in 1996 the Company filed its "Code of Conduct" under FERC Order No. 889, "Open Access Same Time Information System and Standards of Conduct," which formalized the functional separation of generation from transmission within the organization. The transmission component of Electric Operations is organized for and conducting business under these new federal regulatory requirements. (See Item 2. Properties - Electric Operations.)

RETAIL

In 1995 the MPUC initiated an investigation into structural and regulatory issues in the electric utility industry. To make certain that delivery of electric service continues to be efficient following any restructuring, the MPUC adopted 15 principles to guide a deliberate and orderly approach to developing reasonable restructuring alternatives that ensure the fairness of a competitive market and protect the public interest. In January 1996 the MPUC established a competition working group in which company representatives have participated in addressing issues related to wholesale and retail competition. The working group issued a Wholesale Competition Report in October 1996 and a Retail Competition Report in November 1997. The MPUC is expected to begin identifying the steps necessary to successfully implement restructuring upon receipt of a legislative mandate.

LEGISLATION

During 1998 Congress is expected to continue to debate proposed legislation which, if enacted, would promote customer choice and a more competitive electric market. The Company is actively participating in the dialogue and debate on these issues in various forums, principally to advocate fairness and parity for all power and energy competitors in any deregulated markets that may be created by new legislation. While Congress is not expected to pass legislation in 1998, the Company cannot predict the timing or substance of any future legislation which might ultimately be enacted. However, the Company will take the necessary steps to maintain its competitive position as a low-cost and long-term supplier to large industrial customers.

Legislative activity is evolving both in Minnesota and Wisconsin. An electric Energy Task Force comprised of representatives of both houses of the Minnesota legislature continues to study a variety of issues related to industry restructuring. In Minnesota legislation has been introduced, but the Governor and legislative leadership have indicated that no action to restructure the industry will be taken in 1998. The Company is also promoting property tax reform before the Minnesota legislature in order to eliminate the taxation of personal property that results in an inequitable tax burden among current and potential competitors in local markets. The Wisconsin legislature is pursuing electric utility industry restructuring, including the possible formation of an independent transmission system operator within the state.

FRANCHISES

Minnesota Power holds franchises to construct and maintain an electric distribution and transmission system in 85 cities and towns located within its electric service territory. SWL&P holds franchises in 15 cities and towns within its service territory. The remaining cities and towns served do not require a franchise to operate within their boundaries.

ENVIRONMENTAL MATTERS

Certain businesses included in the Company's Electric Operations segment are subject to regulation by various federal, state and local authorities with respect to air quality, water quality, solid wastes and other environmental matters. The Company considers these businesses to be in substantial compliance with those environmental regulations currently applicable to its operations and believes all necessary permits to conduct such operations have been obtained. The Company does not currently anticipate that potential capital expenditures for environmental matters will be material. However, because environmental laws and regulations are constantly evolving, the character, scope and ultimate costs of environmental compliance cannot be estimated.

AIR

CLEAN AIR ACT. The federal Clean Air Act Amendments of 1990 (Clean Air Act) require that specified fossil-fueled generating plants obtain air emission permits from the EPA (or, when delegated, from individual state and pollution control agencies), and meet new sulfur dioxide and nitrogen oxide emission standards beginning January 1, 1995 (Phase I) and that virtually all generating plants meet more strict emission standards beginning January 1, 2000 (Phase II). None of Minnesota Power's generating facilities are covered by the Phase I requirements of the Clean Air Act for sulfur dioxide. However, Phase II requirements apply to the Company's Boswell, Laskin and Hibbard plants, as well as Square Butte.

The Clean Air Act creates emission allowances for sulfur dioxide based on formulas relating to the permitted 1985 emissions rate and a baseline of average fossil fuel consumed in the years 1985, 1986 and 1987. Each allowance is an authorization to emit one ton of sulfur dioxide, and each utility must have sufficient allowances to cover its annual emissions. Minnesota Power's generating facilities in Minnesota burn mainly low-sulfur western coal and Square Butte, located in North Dakota, burns lignite coal. All of these facilities are equipped with pollution control equipment such as scrubbers, baghouses or electrostatic precipitators. Phase II sulfur dioxide emission requirements are currently being met by Boswell Unit 4. Some moderate reductions in emissions may be necessary for Boswell Units 1, 2 and 3, Laskin Units 1 and 2, and Square Butte to meet the Phase II sulfur dioxide emission requirements. The Company believes it is in a good position to comply with the sulfur dioxide standards without extensive modifications. Any required reductions at the Minnesota generating facilities are expected to be achieved through the use of lower sulfur coal. Square Butte anticipates meeting its sulfur dioxide requirements through increased use of existing scrubbers or by purchasing additional allowances. The estimated cost to meet sulfur dioxide requirements at Square Butte is $500,000 to $600,000 per year.

Pursuant to the Clean Air Act, the EPA has established nitrogen oxide limitations for Phase II generating units. To meet Phase II nitrogen oxide limitations, the Company has spent $4.2 million and will spend an additional $1.8 million in 1998 on advanced low emission burner technology and associated control equipment to operate the Boswell and Laskin facilities at or below the compliance standards. Options for complying with the nitrogen oxide limitations at Square Butte are being studied at this time and include operational changes, capital expenditures and seeking regulatory relief. The EPA decided not to promulgate nitrogen oxide limitations for the type of boilers at Hibbard.

The Company has obtained all necessary Title V air operating permits from the MPCA for applicable facilities to conduct its electric operations.

AIR QUALITY EMISSION PERMITS

Facility	Effective Date	Expiration Date
Boswell	March 24, 1997	March 24, 2002
Laskin	May 12, 1997	May 12, 2002
Hibbard	July 14, 1997	July 14, 2002

CLIMATE CHALLENGE. The Company is participating in a voluntary program (Climate Challenge) with the United States Department of Energy to identify activities that the Company has taken and additional measures that the Company may undertake on a voluntary basis that will result in limitations, reductions or sequestrations of greenhouse gas emissions by the year 2000. The Company has agreed to participate in this voluntary program provided that such participation is consistent with the Company's integrated resource planning process, does not have a material adverse effect on the Company's competitive position with respect to rates and costs, and continues to be acceptable to the Company's regulators. The costs to Minnesota Power associated with Climate Challenge participation are minor, reflecting program facilitation and voluntary reporting costs.

KYOTO PROTOCOL. On December 11, 1997 the United Nations Framework Convention on Climate Change agreed upon a draft international treaty, the Kyoto Protocol (Protocol), which, if ratified, would call for reductions in greenhouse gas emissions. The United States' target is to achieve a 7 percent reduction below 1990 emission levels by the period 2008-2012. The Protocol must be ratified by the United States Senate by March 15, 1999; however, the Protocol does not currently satisfy the guidance provided in a 1997 Senate resolution. The Company currently cannot predict when or if the Protocol will be ratified nor can it determine the impact such ratification would have on the Company.

WATER

The Federal Water Pollution Control Act of 1972 (FWPCA), as amended by the Clean Water Act of 1977 and the Water Quality Act of 1987, established the National Pollutant Discharge Elimination System (NPDES) permit program. The FWPCA requires that NPDES permits be obtained from the EPA (or, when delegated, from individual state pollution control agencies) for any wastewater discharged into navigable waters. The Company has obtained all necessary NPDES permits, including NPDES storm water permits for applicable facilities, to conduct its electric operations.

NATIONAL POLLUTANT DISCHARGE ELIMINATION SYSTEM PERMITS

Facility	Effective Date	Expiration Date
Boswell	February 4, 1993	December 31, 1997 (a)
Laskin	December 22, 1993	October 31, 1998 (b)
Hibbard	September 29, 1994	June 30, 1999
Arrowhead DC Terminal	June 17, 1996	March 31, 2001
General Office Building/ Lake Superior Plaza	January 6, 1998	December 31, 2002
Square Butte	July 1, 1995	June 30, 2000

(a) On June 27, 1997 a renewal application for this permit was submitted to the MPCA. A new permit is expected to be issued in the second quarter of 1998. Permits are extended by the timely filing of a renewal application which stays the expiration of the previously issued permit.
(b) A renewal application for this permit is due April 30, 1998. The renewal application is expected to be filed on or before March 30, 1998.

The Company holds FERC licenses authorizing the ownership and operation of seven hydroelectric generating projects with a total generating capacity of about 118 MW.

FERC LICENSES FOR HYDROELECTRIC PROJECTS

Facility	Name Plate Rating	Effective Date	Expiration Date
	MW		
Pillager	1.5	May 12, 1997	May 11, 1998 (a)
Blanchard	18.0	December 1, 1987	August 24, 2003 (b)
Winton	4.0	March 1, 1981	October 31, 2003 (b)
Little Falls	4.7	January 1, 1994	December 31, 2023
Prairie River	1.1	January 1, 1994	December 31, 2023
Sylvan	1.8	January 1, 1994	December 31, 2023
St. Louis River	87.6	July 1, 1995	June 30, 2035 (c)

(a) The FERC issued an annual license to the Company under the existing license terms and conditions. This annual license is effective until the new license is issued. An application to relicense this facility was filed with the FERC on May 11, 1995. The FERC will perform an engineering, environmental and economic analysis of that application in order to determine whether to issue a new license for the project. FERC scoping meetings to discuss any environmental and operational issues related to this project were held in October 1996 with the resource agencies and the public. The FERC staff sought input related to any water quality, fishery, terrestrial, cultural and recreation issues that the agencies and public have prior to preparing the environmental assessment for this project. To date, no substantive issues have been raised by the resource agencies or the public in the license process.
(b) The Company is currently in the planning stages for the relicensing of this facility.
(c) The Company filed a request for rehearing of the FERC's order for the purpose of challenging certain terms and conditions of the license which, if accepted by the Company, would alter the Company's operation of the project. In 1996 the FERC issued an order on rehearing in response to the rehearing request and extended the license term from 30 to 40 years because of the anticipated impact of the FERC's mandates to mitigate environmental consequences of the project. The FERC also directed the Company to negotiate with the Fond du Lac Band of Lake Superior Chippewa (Fond du Lac Band) a reasonable annual charge for the use of tribal lands within the project. In June 1996 the Company filed in the U.S. Court of Appeals for the District of Columbia Circuit a petition for review of the license as issued by the FERC. Separate petitions for review were also filed in June 1996 in the same court by the U.S. Department of the Interior and the Fond du Lac Band, two intervenors in the licensing proceedings. The issues to be resolved concern the terms and conditions of the license which will govern the Company's operation and maintenance of the project. In July 1996 the court consolidated the three petitions for review. In October 1996 the Company filed with the court an unopposed motion for a procedural schedule pursuant to which the briefing of the issues would be completed in May 1997. The motion was granted by the court; however, the briefing schedule has been suspended while the Company and the Fond du Lac Band negotiate the reasonable fee for use of tribal lands as mandated by the new license. Both parties have informed the court that these negotiations may resolve other disputed issues, and they are obligated to report to the court periodically the status of these discussions. Beginning in 1996, and most recently in February 1998, the Company filed requests with the FERC for extensions of time to comply with certain plans and studies required by the license which might conflict with the settlement discussions. The FERC granted an extension until August 1, 1998 to comply with those requirements.

SOLID AND HAZARDOUS WASTE

The Resource Conservation and Recovery Act of 1976 regulates the management and disposal of solid wastes. As a result of this legislation, the EPA has promulgated various hazardous waste rules. The Company is required to notify the EPA of hazardous waste activity and routinely submits the necessary annual reports to the EPA.

In response to EPA Region V's request for utilities to participate in their Great Lakes Initiative by voluntarily removing remaining polychlorinated biphenyl (PCB) inventories, the Company has scheduled replacement of PCB-contaminated oil from substation equipment by 2000 and the removal of PCB capacitors by 2006. The total cost is expected to be between $1.5 million and $2 million of which $400,000 was expended through December 31, 1997. The Company expects to spend about $110,000 in 1998.

MINING CONTROL AND RECLAMATION

BNI Coal's mining operations are governed by the Federal Surface Mining Control and Reclamation Act of 1977. This Act, together with the rules and regulations adopted thereunder by the Department of the Interior, Office of Surface Mining Reclamation and Enforcement (OSM), governs the approval or disapproval of all mining permits on federally owned land and the actions of the OSM in approving or disapproving state regulatory programs regulating mining activities. The North Dakota Reclamation of Strip Mined Lands Act and rules and regulations enacted thereunder in 1969, as subsequently amended by the North Dakota Mining and Reclamation Act and rules and regulations enacted thereunder in 1977, govern the reclamation of surface mined lands and are generally as stringent or more stringent than the federal rules and regulations. Compliance is monitored by the North Dakota Public Service Commission. The federal and state laws and regulations require a wide range of procedures including water management, topsoil and subsoil segregation, stockpiling and revegetation, and the posting of performance bonds to assure compliance. In general these laws and regulations require the reclaiming of mined lands to a level of usefulness equal to or greater than that available before active mining. The Company considers BNI Coal to be in substantial compliance with those environmental regulations currently applicable to its operations and believes all necessary permits to conduct such operations have been obtained.

WATER SERVICES

Water Services are comprised of regulated and non-regulated wholly owned subsidiaries of the Company. Water Services have been laying the groundwork for future growth in several new areas of the water business. Non-regulated subsidiaries have initiated marketing the Company's water expertise outside traditional utility boundaries.

REGULATED SUBSIDIARIES

- FLORIDA WATER, the largest investor owned water supplier in Florida, owns and operates water and wastewater treatment facilities within that state. As of December 31, 1997 Florida Water served 119,000 water customers and 52,000 wastewater treatment customers.

  In 1997 Florida Water sold certain water and wastewater assets to Orange County in Florida for $13.1 million. These assets served about 4,000 customers. The transaction resulted in a $4.7 million after-tax gain.

- HEATER owns and operates four companies which provide water and wastewater treatment services primarily in North Carolina. As of December 31, 1997 these companies served 28,000 water customers and 2,000 wastewater treatment customers.

  In 1997 the NCUC approved the transfer of LaGrange Waterworks Corporation (LaGrange) to Heater. The Company exchanged 96,000 shares of common stock, with a market value of approximately $3.4 million, for the outstanding shares of LaGrange. The transaction was accounted for as a pooling of interest. LaGrange provides water services to approximately 5,300 customers near Fayetteville, North Carolina.

NON-REGULATED SUBSIDIARIES

- INSTRUMENTATION SERVICES, INC. provides predictive maintenance and instrumentation consulting services to water and wastewater utilities, and other industrial operations throughout the southeastern part of the United States as well as Texas and Minnesota.

- U.S. MAINTENANCE AND MANAGEMENT SERVICES CORPORATION was incorporated in 1997 to complement ISI's operations. U.S. Maintenance and Management provides maintenance services to water and wastewater utilities and other industrial operations primarily in Florida.

- AMERICAS' WATER SERVICES CORPORATION was incorporated in 1997. Headquartered near Chicago, Illinois, Americas' Water offers contract management, operations and maintenance services to governments and industries throughout the Americas.

REGULATORY ISSUES

FLORIDA PUBLIC SERVICE COMMISSION

- 1991 RATE CASE REFUNDS. In 1995 the Florida First District Court of Appeals (Court of Appeals) reversed a 1993 FPSC order establishing uniform rates for most of Florida Water's service areas. With "uniform rates," all customers in each uniform rate area pay the same rates for water and wastewater services. In response to the Court of Appeals' order, in August 1996 the FPSC ordered Florida Water to issue refunds to those customers who paid more since October 1993 under uniform rates than they would have paid under stand-alone rates. This order did not permit a balancing surcharge to customers who paid less under uniform rates. Florida Water appealed, and the Court of Appeals ruled in June 1997 that the FPSC could not order refunds without balancing surcharges. In response to the Court of Appeals' ruling, the FPSC issued an order on January 26, 1998 that would not require Florida Water to refund about $12.5 million, which included interest, to customers who paid more under uniform rates.

  In the same January 26, 1998 order, the FPSC required Florida Water to refund $2.5 million, the amount paid by customers in the Spring Hill service area from January 1996 through June 1997 under uniform rates which exceeded the amount these customers would have paid under a modified stand-alone rate structure. No balancing surcharge was permitted. The FPSC ordered this refund because Spring Hill customers continued to pay uniform rates after other customers began paying modified stand-alone rates effective January 1996 pursuant to the FPSC's interim rate order in Florida Water's 1995 Rate Case. The FPSC did not include Spring Hill in this interim rate order because Hernando County had assumed jurisdiction over Spring Hill's rates. In June 1997 Florida Water reached an agreement with Hernando County to revert to stand-alone rates for Spring Hill customers.

  Customer groups which paid more under uniform rates have appealed the FPSC's January 26, 1998 order. The Company has also appealed the $2.5 million refund order. No provision for refund has been recorded.

- 1995 RATE CASE. Florida Water requested an $18.1 million rate increase in June 1995 for all water and wastewater customers of Florida Water regulated by the FPSC. In October 1996 the FPSC issued its final order approving an $11.1 million annual increase. In November 1996 Florida Water filed with the Court of Appeals an appeal of the FPSC's final order seeking judicial review of issues relating to the amount of investment in utility facilities recoverable in rates from current customers. Other parties to the rate case also filed appeals. In June 1997, as part of the review process, the FPSC allowed Florida Water to resume collecting approximately $1 million, on an annual basis, in new customer connection fees. Oral argument on the appeal was heard by the Court of Appeals on February 10, 1998. The Company is unable to predict the timing or outcome of the appeals process.

- HILLSBOROUGH COUNTY RATES. On July 2, 1997 Florida Water filed for a rate change with the Hillsborough County Utilities Department. Florida Water filed for an annual interim rate increase of $848,845 (43.1 percent) and a final rate increase of $877,607 (44.6 percent). Interim rates became effective on August 18, 1997. Hearings are scheduled for April, May and June 1998. It is anticipated that final rates will be implemented in July 1998. The Company is unable to predict the outcome of this case.

NORTH CAROLINA UTILITIES COMMISSION

On September 30, 1997 Heater filed with the NCUC for a $1.1 million annual increase for its water and wastewater customers. The hearing was held on March 10, 1998. The annual increase in operating revenue is expected to be $343,000. The test year was adjusted for customer growth and consumption which substantially decreased the annual rate increase required. A final order from the NCUC is expected in May 1998.

CAPITAL EXPENDITURE PROGRAM

Capital expenditures for Water Services totaled $22 million during 1997. Expenditures were funded with internally generated funds. Capital expenditures for the Company's Water Services are expected to be $22 million in 1998 to meet environmental standards, expand water and wastewater treatment facilities to accommodate customer growth, and for water conservation initiatives. Capital expenditures are expected to total approximately $110 million during the period 1999 through 2002.

COMPETITION

Water Services provide water and wastewater services at regulated rates within exclusive service territories granted by regulators.

With respect to non-regulated businesses within Water Services, significant competition exists for the provision of the types of services provided by Americas' Water. Although a few private contractors control a large percentage of the market for contract management, operations and maintenance services, the Company believes that the current and anticipated growth in that market will allow for emerging companies like Americas' Water to succeed.

FRANCHISES

Florida Water provides water and wastewater treatment services in 21 counties regulated by the FPSC and holds franchises in three counties which have retained authority to regulate such operations. (See Regulatory Issues - - - - Florida Public Service Commission.)

Water and wastewater services provided by Heater are under the jurisdiction of the NCUC. The commission grants franchises for Heater's service territory when the rates are authorized.

ENVIRONMENTAL MATTERS

The Company's Water Services are subject to regulation by various federal, state and local authorities with respect to water quality, solid wastes and other environmental matters. The Company considers these businesses to generally be in compliance with those environmental regulations currently applicable to its operations and have the permits necessary to conduct such operations. The Company does not currently anticipate that potential capital expenditures for environmental matters will be material. However, because environmental laws and regulations are constantly evolving, the character, scope and ultimate costs of environmental compliance cannot be estimated.

UNIVERSITY SHORES AND SEABOARD FACILITIES

In 1993 the EPA notified Florida Water of alleged exceedences of effluent limitations in its NPDES permit for Florida Water's University Shores wastewater facility in Orange County, Florida. During 1993 and 1994, Florida Water periodically corresponded and met with the EPA concerning the alleged exceedences of the permit. The matters at issue were resolved in February 1994 when the University Shores facility was modified such that effluent was no longer discharged to surface waters. In 1992 the EPA notified Florida Water of alleged exceedences of effluent limitations in the NPDES permit for Florida Water's Seaboard wastewater treatment facility in Hillsborough County, Florida. Between 1992 and 1994, Florida Water periodically corresponded and met with the EPA concerning alleged exceedences of the permit. In March 1994 the matters at issue were resolved when the facility was taken out of service and the collection system was interconnected with the City of Tampa utilities. In 1997 the United States Department of Justice (DOJ), on behalf of the EPA, served Florida Water with a complaint in a civil action in the U.S. District Court for the Middle District of Florida (District Court). The suit sought civil penalties not to exceed $25,000 per day for each alleged violation of effluent limitations in the NPDES permits occurring at the University Shores and Seaboard wastewater facilities from February 1992 through March 1994. In 1998 Florida Water, the DOJ and the EPA executed a Consent Decree as a settlement of the complaint filed in 1997. The Consent Decree requires Florida Water to pay a $250,000 civil penalty; complete a Supplemental Environmental Project totaling $200,000; and complete an additional environmental project totaling $450,000. After a 30 day period for notice and public comment, the Consent Decree will be filed with the District Court for approval.

AUTOMOTIVE SERVICES

Automotive Services include wholly owned subsidiaries operating as integral parts of the vehicle auction business: ADESA, a network of vehicle auctions; AFC, a finance company; and Great Rigs, an auto transport company. The Company acquired 80 percent of ADESA, including AFC and Great Rigs, on July 1, 1995. The Company increased its ownership interest to 83 percent in January 1996 and acquired the remaining 17 percent interest in August 1996. Automotive Services plans on growth through selective acquisitions and expanding services.

- ADESA is the third largest vehicle auction network in the United States. Headquartered in Indianapolis, Indiana, ADESA owns and operates 25 vehicle auction facilities in the United States and Canada through which used cars and other vehicles are sold to franchised automobile dealers and licensed used car dealers. Sellers at ADESA's auctions include domestic and foreign auto manufacturers, car dealers, automotive fleet/lease companies, banks and finance companies. During 1997 ADESA sold one of its auction facilities in Florida, acquired a new auction facility in Sacramento, California and 80 percent of another auction facility in Columbus, Indiana.

  PROFESSIONAL AUTO REMARKETING (PAR), a division of ADESA, provides customized remarketing services to various businesses with fleet operations.

- AUTOMOTIVE FINANCE CORPORATION provides inventory financing for wholesale and retail automobile dealers who purchase vehicles from ADESA auctions, independent auctions and other auction chains. AFC is headquartered in Indianapolis, Indiana, and has 57 loan production offices which are located at most ADESA auctions, as well as at or near independently owned auto auctions. From these offices car dealers obtain credit to purchase vehicles at any of the over 300 auctions approved by AFC. During 1997 AFC added 25 loan production offices. In early 1998 three more loan production offices were added.

- GREAT RIGS is one of the nation's largest independent used automobile transport carriers with 110 leased automotive carriers operating as an integral part of the vehicle auction business. Headquartered in Moody, Alabama, Great Rigs offers customers pick up and delivery through 11 strategically located transportation hubs. Customers of Great Rigs include ADESA auctions, car dealerships, vehicle manufacturers, leasing companies, finance companies and other auctions. Major customers include GE Capital, Nissan, Ford Motor Credit and General Motors Acceptance Corp. By the end of second quarter 1998, Great Rigs expects to expand its fleet to 150 automobile carriers.

CAPITAL EXPENDITURE PROGRAM

Capital expenditures for automobile auction site relocation, development and facility improvements were $11 million during 1997. Capital expenditures for Automotive Services are expected to be $24 million in 1998 and to total approximately $47 million during the period 1999 through 2002. Capital expenditures in 1998 are for on-going improvements and relocation of existing vehicle auction facilities, and associated information systems.

COMPETITION

Within the automobile auction industry, ADESA's competition includes independently owned auctions as well as major chains and associations with auctions in geographic proximity. ADESA competes with other auctions for a supply of vehicles to be sold on consignment for automobile dealers, financial institutions and other sellers. ADESA also competes for a supply of rental repurchase vehicles from automobile manufacturers for auction at factory sales. Automobile manufacturers often choose between auctions across multi-state areas in distributing rental repurchase vehicles. ADESA competes for these customers by attempting to attract a large number of dealers to purchase vehicles, which ensures competitive prices and supports the volume of vehicles auctioned. ADESA also competes by providing a full range of services including dealer inventory financing, reconditioning services which prepare vehicles for auction, transporting vehicles and the prompt processing of sale transactions. Another factor affecting the industry, the impact of which is yet to be determined, is the entrance of large used car dealerships called "superstores" that have emerged in densely populated markets.

AFC is well positioned as a provider of floorplan financing services to the used vehicle industry. AFC's competition includes other specialty lenders, as well as banks and other financial institutions. AFC competes with other floorplan providers and strives to distinguish itself based upon convenience and quality of service. A key component of AFC's program is conveniently located loan production offices with personnel available to assist automobile dealers with their financing needs. As part of AFC's continued effort to focus on providing other financing services to dealers, in 1997 AFC entered into an agreement with ACC Consumer Finance Corp. (ACC). ACC has subsequently been acquired by Household International. Together these two companies will test a program designed to promote ACC's retail financing of used vehicles floorplanned by AFC.

ENVIRONMENTAL MATTERS

Certain businesses in the Company's Automotive Services segment are subject to regulation by various federal, state and local authorities with respect to air quality, water quality, solid wastes and other environmental matters. The Company considers these businesses to be in substantial compliance with those environmental regulations currently applicable to its operations and believes all necessary permits to conduct such operations have been obtained. The Company does not currently anticipate that potential capital expenditures for environmental matters will be material. However, because environmental laws and regulations are constantly evolving, the character, scope and ultimate costs of environmental compliance cannot be estimated.

INVESTMENTS

The Investments segment is comprised of a securities portfolio, an investment in a financial guaranty reinsurance and insurance company, and real estate operations.

PORTFOLIO AND REINSURANCE

- SECURITIES PORTFOLIO. The Company's securities portfolio is managed by selected outside managers as well as internal managers. It is intended to provide stable earnings and liquidity, and is available for investment in existing businesses, acquisitions and other corporate purposes. The Company's objective is to maintain corporate liquidity between 7 percent and 10 percent of total assets ($150 million to $200 million). The Company plans to continue to concentrate in market-neutral investment strategies designed to provide stable and acceptable returns without sacrificing needed liquidity. The securities portfolio is hedged against market downturns and aimed at an after-tax return between 7 percent and 9 percent. While these returns may seem modest compared to broader market indices over the past three years, the Company believes its hedge strategy is a wise course in a volatile economic

environment. Returns will continue to be partially dependent on general market conditions. The Company's investment in the securities portfolio at December 31, 1997 was $184 million ($155 million at December 31, 1996).

- REINSURANCE. Minnesota Power owns 3.3 million shares of Capital Re, a specialty insurance and reinsurance business. Capital Re's product lines currently include financial guaranty, mortgage, title, financial, credit and specialty reinsurance, and specialty insurance through its participation in Lloyds of London. Capital Re trades on the New York Stock Exchange under the symbol KRE. Minnesota Power's ownership represents 21 percent of the 16 million total outstanding shares of Capital Re. The market value of the Company's investment in Capital Re was $203 million at December 31, 1997 ($152 million at December 31, 1996) based on a Capital Re share price of $62 5/16 ($46 5/8 at December 31, 1996). The Company accounts for its investment in Capital Re under the equity method and the carrying value was $119 million at December 31, 1997. Capital Re will continue to be a core component of the Company's Investment segment.

- OTHER. Since 1985 the Company has invested about $8 million as a shareholder in Utech Venture Capital Corporation (Utech). Utech manages a group of venture capital funds that seek long-term capital appreciation by making investments in companies developing advanced technologies to be used by the utility industry. The

Company is committed to invest an additional $14 million over the next five years. Minnesota Power has recognized dividends and return of capital from the funds in the year they are paid. As successful companies "go public" or are sold, investors, like Minnesota Power, may realize income as the stock is sold and the cash distributed.

In 1997 Minnesota Power loaned $4 million to Car Canada Corporation, a start-up retail car "superstore" business with stores in Ottawa and Toronto. The Company holds a 10 percent note due 2002 for the principal amount of the loan. The note has five equal payments due at the end of years one through five. The Company also holds detachable warrants that can be exercised for 25 percent of the outstanding shares of Car Canada in exchange for approximately $18,000. The warrants are exercisable automatically in an initial public offering, or sale, or merger of the firm and any other time at the sole option of Minnesota Power.

REAL ESTATE OPERATIONS

The Company owns 80 percent of Lehigh, a Florida real estate company which owns property in three different locations. The real estate strategy is to continue to acquire large community properties at low cost, add value and sell them at going market prices.

- LEHIGH ACRES properties include 2,500 acres of land and approximately 4,000 home sites near Fort Myers, Florida.

- SUGARMILL WOODS properties include 1,000 home sites in Citrus County, Florida.

- PALM COAST properties include 2,700 home sites and 12,000 acres of residential, commercial and industrial land at Palm Coast, Florida. Palm Coast is a planned community between St. Augustine and Daytona Beach.

ENVIRONMENTAL MATTERS

Certain businesses included in the Company's Investments segment are subject to regulation by various federal, state and local authorities with respect to air quality, water quality, solid wastes and other environmental matters. The Company considers these businesses to be in substantial compliance with those environmental regulations currently applicable to its operations and believes all necessary permits to conduct such operations have been obtained. The Company does not currently anticipate that potential capital expenditures for environmental matters will be material. However, because environmental laws and regulations are constantly evolving, the character, scope and ultimate costs of environmental compliance cannot be estimated.

EXECUTIVE OFFICERS OF THE REGISTRANT

Executive Officers	Initial Effective Date
John A. Cirello, Age 54	
Executive Vice President and President and Chief Executive Officer - MP Water Resources Group Inc.	July 24, 1995
Donnie R. Crandell, Age 54	
Senior Vice President and President - MP Real Estate Holdings, Inc.	January 1, 1996
Senior Vice President - Corporate Development	December 1, 1994
Retired	February 28, 1994
Vice President - Corporate Development	March 1, 1993
Robert D. Edwards, Age 53	
Executive Vice President and President - MP Electric	July 26, 1995
Executive Vice President and Chief Operating Officer	March 1, 1993
Group Vice President - Corporate Services and Chief Financial Officer	January 1, 1991
John E. Fuller, Age 54	
Senior Vice President and President and Chief Executive Officer - AFC	April 23, 1997
President and Chief Executive Officer - AFC	January 1, 1994
Laurence H. Fuller, Age 49	
Vice President - Corporate Development	February 10, 1997
David G. Gartzke, Age 54	
Senior Vice President - Finance and Chief Financial Officer	December 1, 1994
Vice President - Finance and Chief Financial Officer	March 1, 1993
Vice President - Finance and Treasurer	January 1, 1991
James P. Hallett, Age 44	
Executive Vice President and President and Chief Executive Officer - ADESA	April 23, 1997
President and Chief Executive Officer - ADESA	August 21, 1996
Philip R. Halverson, Age 50	
Vice President, General Counsel and Secretary	January 1, 1996
General Counsel and Corporate Secretary	March 1, 1993
General Counsel and Assistant Secretary	January 23, 1991
James A. Roberts, Age 47	
Vice President - Corporate Relations	January 1, 1996
Edwin L. Russell, Age 53	
Chairman, President and Chief Executive Officer	May 14, 1996
President and Chief Executive Officer	January 22, 1996
President	May 9, 1995
Mark A. Schober, Age 42	
Controller	March 1, 1993
James K. Vizanko, Age 44	
Treasurer	March 1, 1993

All of the executive officers above, except Mr. Cirello, Mr. Crandell, Mr. John Fuller, Mr. Laurence Fuller, Mr. Hallet and Mr. Russell, have been employed by the Company for more than five years in executive or management positions.

- Mr. Cirello was president of Metcalf & Eddy Services, Inc. from 1992 to 1995, responsible for $64 million in water/wastewater operation services.

- Mr. Crandell was director of business development of the Company, vice president of Topeka Group Incorporated and vice president of business development for Topeka Group Incorporated prior to March 1, 1993.

- Mr. John Fuller was previously president and 50 percent owner of CITA, Inc., which he founded in 1987 (CITA was renamed Automotive Finance Corporation in December 1993 and sold to ADESA in January 1994).

- Mr. Laurence Fuller was previously senior vice president, new business development and strategic planning, for Diners Club International, a subsidiary of Citicorp, Inc.

- Mr. Hallet was previously executive vice president of ADESA and president of ADESA's Canadian operations.

- Mr. Russell was previously group vice president of J. M. Huber Corporation, a $1.5 billion diversified manufacturing and natural resources company.

Prior to election to the positions shown above, Mr. Roberts, Mr. Schober and Mr. Vizanko held other positions with the Company after January 1, 1993.

- Mr. Roberts was director of corporate relations.

- Mr. Schober was director of internal audit.

- Mr. Vizanko was director of investments and analysis.

There are no family relationships between any executive officers of the Company. All officers and directors are elected or appointed annually.

The present term of office of the above executive officers extends to the first meeting of the Company's Board of Directors after the next annual meeting of shareholders. Both meetings are scheduled for May 12, 1998.

ITEM 2. PROPERTIES.

ELECTRIC OPERATIONS

The Company had an annual and all-time record net peak load of 1,476 MW on February 10, 1997. Information with respect to existing power supply sources is shown below.

Power Supply	Unit No.	Year Installed	Net Winter Capability	Net Electric Requirements	
			MW	MWh	%
Steam					
Coal-Fired					
Boswell Energy Center					
near Grand Rapids, MN	1	1958	69		
	2	1960	69		
	3	1973	350		
	4	1980	428		
			916	5,618,246	43.7%
Laskin Energy Center					
Hoyt Lakes, MN	1	1953	55		
	2	1953	55		
			110	537,875	4.2
Purchased Steam					
M. L. Hibbard					
Duluth, MN	3	1949	33	814	-
Total Steam			1,059	6,156,935	47.9
Hydro					
Group consisting of ten stations in MN		Various	118	578,020	4.5
Purchased Power					
Square Butte burns lignite in Center, ND			322	2,307,308	18.0
All other - net			-	3,802,005	29.6
Total Purchased Power			322	6,109,313	47.6
For the Year Ended December 31, 1997			1,499	12,844,268	100.0%

The Company has electric transmission and distribution lines of 500 kilovolts (kV) (8 miles), 230 kV (606 miles), 161 kV (43 miles), 138 kV (6 miles), 115 kV (1,260 miles) and less than 115 kV (6,176 miles). The Company owns and operates 176 substations with a total capacity of 8,533 megavoltamperes. Some of the transmission and distribution lines interconnect with other utilities.

The Company owns and has a substantial investment in offices and service buildings, area headquarters, an energy control center, repair shops, motor vehicles, construction equipment and tools, office furniture and equipment, and leases offices and storerooms in various localities within the Company's service territory. It also owns miscellaneous parcels of real estate not presently used in Electric Operations.

Substantially all of the electric plant of the Company is subject to the lien of its Mortgage and Deed of Trust which secures first mortgage bonds issued by the Company. The Company's properties are held by it in fee and are free from other encumbrances, subject to minor exceptions, none of which are of such a nature as to substantially impair the usefulness to the Company of such properties. Other property, including certain offices and equipment, is utilized under leases. In general, some of the electric lines are located on land not owned in fee, but are covered by necessary consents of various governmental authorities or by appropriate rights obtained from owners of private property. These consents and rights are deemed adequate for the purposes for which the properties are being used. In September 1990 the Company sold a portion of Boswell Unit 4 to WPPI. WPPI has the right to use the Company's transmission line facilities to transport its share of generation.

Substantially all of the plant of SWL&P is subject to the lien of its Mortgage and Deed of Trust which secures first mortgage bonds issued by SWL&P.

A large dragline, shop complex, and certain other less significant property and equipment items at BNI Coal are leased under a leveraged lease agreement that expires in 2002. Certain computer and other equipment are leased under operating lease agreements that expire in 2000 and 2007, respectively. All other property and equipment is owned by BNI Coal.

The Company is a member of the Mid-Continent Area Power Pool (MAPP). The MAPP enhances electric service reliability, and provides the opportunity for members to enter into various wholesale power transactions and coordinate planning, installation and operation of new generation and transmission facilities. The MAPP membership consists of various electric power suppliers located in North Dakota, South Dakota, eastern Montana, Nebraska, Iowa, Minnesota, Wisconsin, upper Michigan, Kansas, Manitoba and Saskatchewan, and marketers and brokers located throughout North America. The electric power suppliers are investor-owned utilities including the Company, rural electric generation and transmission cooperatives, public power districts, municipal electric systems, municipal organizations, and the Western Area Power Administration - Billings, Montana. MAPP operates pursuant to an agreement that was approved by MAPP members on March 15, 1996, accepted by the FERC and became effective on November 1, 1996.

WATER SERVICES

Florida Water is the largest investor owned provider of water and wastewater services in Florida, serving more than 170,000 customers in 145 service areas. Florida Water maintains 149 water and wastewater facilities throughout the state with plants ranging in size from 6 connections to greater than 25,000 connections. Florida Water provides its customers with 14 billion gallons of water per year primarily from Florida's underground aquifer. Substantially all of Florida Water's properties used in its water and wastewater operations are encumbered by a mortgage.

Heater has water and wastewater systems located in subdivisions surrounding Raleigh, North Carolina and Fayetteville, North Carolina. Water supply is primarily from ground water deep wells. Community ground water systems vary in size from 25 connections to 6,000 connections. Some systems are supplied by purchased water. Heater has approximately 223 systems and 436 wells serving 28,000 customers. Heater also has 8 wastewater treatment plants, ranging in size from 35,000 gallons per day (gpd) to 250,000 gpd, and 19 lift stations located in its wastewater collection systems. These systems serve approximately 2,000 customers. Substantially all of Heater's properties used in its water and wastewater operations are encumbered by a mortgage.

INVESTMENTS

Property within the Company's real estate operations consists of 2,500 acres of land and approximately 4,000 home sites near Fort Myers, Florida; 1,000 home sites in Citrus County, Florida; and 2,700 home sites and 12,000 acres of residential, industrial and commercial land at Palm Coast, Florida.

AUTOMOTIVE SERVICES

The following table sets forth the vehicle auctions currently owned or leased by ADESA. Each auction has a multi-lane, drive-through auction facility, as well as additional buildings for reconditioning, registration, maintenance, body work, and other ancillary and administrative services. Each auction also has secure parking areas in which it stores vehicles for auction. All vehicle auction property owned by ADESA is subject to liens securing various notes payable.

ADESA Auctions	Location	Year Operations Commenced	No. Auction Lanes
United States			
ADESA Birmingham	Moody, Alabama	1987	10
ADESA Sacramento	Sacramento, California	1997	5
ADESA Jacksonville	Jacksonville, Florida	1996	6
ADESA South Florida	Opa-Locka, Florida (near Miami)	1994	7
ADESA Southern Indiana	Columbus, Indiana	1997	3
ADESA Indianapolis	Plainfield, Indiana	1983	10
ADESA Lexington	Lexington, Kentucky	1982	6
ADESA Boston	Framingham, Massachusetts	1995	11
ADESA New Jersey	Manville, New Jersey	1996	8
ADESA Buffalo	Akron, New York	1992	10
ADESA Charlotte	Charlotte, North Carolina	1994	8
ADESA Cincinnati/Dayton	Franklin, Ohio	1986	8
ADESA Cleveland	Northfield, Ohio	1994	8
ADESA Pittsburgh	Mercer, Pennsylvania	1971	7
ADESA Knoxville	Lenoir City, Tennessee	1984	6
ADESA Memphis	Memphis, Tennessee	1990	6
ADESA Austin	Austin, Texas	1990	6
ADESA Dallas	Mesquite, Texas	1990	6
ADESA Houston	Houston, Texas	1995	3
ADESA San Antonio	San Antonio, Texas	1989	5
ADESA Wisconsin	Portage, Wisconsin	1984	5
Canada			
ADESA Moncton	Moncton, New Brunswick	1996	2
ADESA Halifax	Lr. Sackville, Nova Scotia	1993	2
ADESA Ottawa	Vars, Ontario	1990	5
ADESA Montreal	St. Eustache, Quebec	1974	8

Leased auction facilities. (See Note 14.)
ADESA owns 51 percent of this auction business.
ADESA owns 80 percent of this auction business.

AFC has loan production offices in 57 locations across North America. Many offices are within auction facilities operated by ADESA and independent auctions.

Great Rigs leases its fleet of 110 automobile carriers under operating leases.

ITEM 3. LEGAL PROCEEDINGS.

Material legal and regulatory proceedings are included in the discussion of the Company's business in Item 1 and are incorporated by reference herein.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

No matters were submitted to a vote of security holders during the fourth quarter of 1997.

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

The Company has paid dividends without interruption on its common stock since 1948. A quarterly dividend of $.51 per share on the common stock was paid on March 2, 1998 to the holders of record on February 16, 1998. The Company's common stock is listed on the New York Stock Exchange. Dividends paid per share, and the high and low prices for the Company's common stock for the periods indicated as reported by The Wall Street Journal, Midwest Edition, were as follows:

Quarter			Price Range High	Low	Dividends Paid Per Share Quarterly	Annual
1997	-	First	$ 29	$ 27 1/4	$ .51	
	-	Second	30 5/8	27	.51	
	-	Third	36 5/16	30 1/4	.51	
	-	Fourth	44	35 3/16	.51	$2.04
1996	-	First	$ 29 3/4	$ 26 1/8	$ .51	
	-	Second	29	26	.51	
	-	Third	28 3/4	26	.51	
	-	Fourth	28 7/8	26 3/8	.51	$2.04

The amount and timing of dividends payable on the Company's common stock are within the sole discretion of the Company's Board of Directors. In 1997 the Company paid out 82 percent of its per share earnings in dividends. Through increased earnings, the Company's goal is to reduce dividend payout to between 75 percent and 80 percent of per share earnings.

The Company's Articles of Incorporation, and Mortgage and Deed of Trust contain provisions which under certain circumstances would restrict the payment of common stock dividends. As of December 31, 1997 no retained earnings were restricted as a result of these provisions. At March 2, 1998 there were approximately 37,000 common stock shareholders of record.

ITEM 6. SELECTED FINANCIAL DATA.

Financial information presented in the table below may not be comparable between periods due to: (1) the Company's purchase of 80 percent of ADESA, including AFC and Great Rigs, on July 1, 1995, another 3 percent in January 1996 and the remaining 17 percent in August 1996; and (2) and the Company's sale of its interest in the paper and pulp business to Consolidated Papers, Inc. on June 30, 1995.

	1997	1996	1995	1994	1993
			Millions except per share amounts		
Operating Revenue and Income	$953.6	$846.9	$672.9	$582.2	$582.5
Income (Loss)					
Continuing Operations	$77.6	$69.2	$61.9	$59.5	$64.4
Discontinued Operations	-	-	2.8	1.8	(1.8)
Net Income	$77.6	$69.2	$64.7	$61.3	$62.6
Basic and Diluted Earnings Per Share					
Continuing Operations	$ 2.47	$ 2.28	$ 2.06	$1.99	$2.27
Discontinued Operations	-	-	.10	.07	(.07)
Total	$ 2.47	$ 2.28	$ 2.16	$2.06	$2.20
Dividends Per Share	$2.04	$2.04	$2.04	$2.02	$1.98
Total Assets	$2,172.3	$2,146.0	$1,947.6	$1,807.8	$1,760.5
Long-Term Debt	$685.4	$694.4	$639.5	$601.3	$611.0
Redeemable Preferred Stock	$20.0	$20.0	$20.0	$20.0	$20.0
Cumulative Quarterly Income Preferred Securities	$75.0	$75.0	-	-	-

Included $14.7 million from the recognition of tax benefits associated with real estate operations and a $3.8 million reduction associated with exiting the equipment manufacturing business.

Included $11.8 million from the sale of certain water plant assets, $3.6 million from the recognition of escrow funds associated with real estate operations, a $5.9 million decrease from the write-off of an investment and a $3 million loss from the equipment manufacturing business.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The management's discussion and analysis of financial condition and results of operations appearing on pages 18 through 31 of the Minnesota Power 1997 Annual Report are incorporated by reference in this Form 10-K Annual Report.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

The financial statements, together with the report thereon of Price Waterhouse LLP dated January 26, 1998 appearing on pages 32 through 50 of the Minnesota Power 1997 Annual Report, are incorporated by reference in this Form 10-K Annual Report.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.

The information required for this Item is incorporated by reference herein from the "Election of Directors" section in the Company's Proxy Statement for the 1998 Annual Meeting of Shareholders, except for information with respect to executive officers which is set forth in Part I hereof.

ITEM 11. EXECUTIVE COMPENSATION.

The information required for this Item is incorporated by reference herein from the "Compensation of Executive Officers" section in the Company's Proxy Statement for the 1998 Annual Meeting of Shareholders.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

The information required for this Item is incorporated by reference herein from the "Security Ownership of Certain Beneficial Owners and Management" section in the Company's Proxy Statement for the 1998 Annual Meeting of Shareholders.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

The information required for this Item is incorporated by reference herein from the "Compensation Committee Interlocks and Insider Participation" section in the Company's Proxy Statement for the 1998 Annual Meeting of Shareholders.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K.

(a) Certain Documents Filed as Part of Form 10-K.

(1) Financial Statements

	Pages in Annual Report*
Minnesota Power	
Report of Independent Accountants	31
Consolidated Balance Sheet at December 31, 1997 and 1996	32
For the three years ended December 31, 1997	
Consolidated Statement of Income	34
Consolidated Statement of Retained Earnings	34
Consolidated Statement of Cash Flows	35
Notes to Consolidated Financial Statements	36-50

- - - ---------------
* Incorporated by reference herein from the Minnesota Power 1997 Annual Report.

	Page
(2) Financial Statement Schedules	
Report of Independent Accountants on Financial Statement Schedule	32
Minnesota Power and Subsidiaries Schedule:	
II-Valuation and Qualifying Accounts and Reserves	33

All other schedules have been omitted either because the information is not required to be reported by the Company or because the information is included in the consolidated financial statements or the notes thereto.

(3) Exhibits including those incorporated by reference

Exhibit Number		
*2	-	Agreement and Plan of Merger by and among Minnesota Power & Light Company, AC Acquisition Sub, Inc., ADESA Corporation and Certain ADESA Management Shareholders dated February 23, 1995 (filed as Exhibit 2 to Form 8-K dated March 3, 1995, File No. 1-3548).
*3(a)1	-	Articles of Incorporation, restated as of July 27, 1988 (filed as Exhibit 3(a), File No. 33-24936).
*3(a)2	-	Certificate Fixing Terms of Serial Preferred Stock A, $7.125 Series (filed as Exhibit 3(a)2, File No. 33-50143).
*3(a)3	-	Certificate Fixing Terms of Serial Preferred Stock A, $6.70 Series (filed as Exhibit 3(a)3, File No. 33-50143).
*3(b)	-	Bylaws as amended January 23, 1991 (filed as Exhibit 3(b), File No. 33-45549).

Exhibit
Number

*4(a)1 - Mortgage and Deed of Trust, dated as of September 1, 1945, between the Company and Irving Trust Company (now The Bank of New York)and Richard H. West (W.T. Cunningham, successor), Trustees (filed as Exhibit 7(c), File No. 2-5865).

*4(a)2 - Supplemental Indentures to Mortgage and Deed of Trust:

Number	Dated as of	Reference File	Exhibit
First	March 1, 1949	2-7826	7(b)
Second	July 1, 1951	2-9036	7(c)
Third	March 1, 1957	2-13075	2(c)
Fourth	January 1, 1968	2-27794	2(c)
Fifth	April 1, 1971	2-39537	2(c)
Sixth	August 1, 1975	2-54116	2(c)
Seventh	September 1, 1976	2-57014	2(c)
Eighth	September 1, 1977	2-59690	2(c)
Ninth	April 1, 1978	2-60866	2(c)
Tenth	August 1, 1978	2-62852	2(d)2
Eleventh	December 1, 1982	2-56649	4(a)3
Twelfth	April 1, 1987	33-30224	4(a)3
Thirteenth	March 1, 1992	33-47438	4(b)
Fourteenth	June 1, 1992	33-55240	4(b)
Fifteenth	July 1, 1992	33-55240	4(c)
Sixteenth	July 1, 1992	33-55240	4(d)
Seventeenth	February 1, 1993	33-50143	4(b)
Eighteenth	July 1, 1993	33-50143	4(c)
Nineteenth	February 1, 1997	1-3548 (1996 Form 10-K)	4(c)

4(a)3 - Twentieth Supplemental Indenture, dated as of November 1, 1997, between the Company and The Bank of New York (formerly Irving Trust Company) and W.T. Cunningham (successor to Richard H. West), Trustees.

*4(b) - Mortgage and Deed of Trust, dated as of March 1, 1943, between Superior Water, Light and Power Company and Chemical Bank & Trust Company and Howard B. Smith, as Trustees, both succeeded by First Bank N.A., as Trustee (filed as Exhibit 7(c), File No. 2-8668), as supplemented and modified by First Supplemental Indenture thereto dated as of March 1, 1951 (filed as Exhibit 2(d)(1), File No. 2-59690), Second Supplemental Indenture thereto dated as of March 1, 1962 (filed as Exhibit 2(d)1, File No. 2-27794), Third Supplemental Indenture thereto dated July 1, 1976 (filed as Exhibit 2(e)1, File No. 2-57478), Fourth Supplemental Indenture thereto dated as of March 1, 1985 (filed as Exhibit 4(b), File No. 2-78641), Fifth Supplemental Indenture thereto dated as of December 1, 1992 (filed as Exhibit 4(b)1 to Form 10-K for the year ended December 31, 1992, File No. 1-3548), Sixth Supplemental Indenture, dated as of March 24, 1994 (filed as Exhibit 4(b)1 to Form 10-K for the year ended December 31, 1996, File No. 1-3548), Seventh Supplemental Indenture, dated as of November 1, 1994 (filed as Exhibit 4(b)2 to Form 10-K for the year ended December 31, 1996, File No. 1-3548) and Eighth Supplemental Indenture, dated as of January 1, 1997 (filed as Exhibit 4(b)3 to Form 10-K for the year ended December 31, 1996, File No. 1-3548).

Exhibit
Number
- - - -------

*4(c) - Indenture, dated as of March 1, 1993, between Southern States Utilities, Inc. (now Florida Water Services Corporation) and Nationsbank of Georgia, National Association (now SunTrust Bank, Central Florida, N.A.), as Trustee (filed as Exhibit 4(d) to Form 10-K for the year ended December 31, 1992, File No. 1-3548), as supplemented and modified by First Supplemental Indenture, dated as of March 1, 1993 (filed as Exhibit 4(c)1 to Form 10-K for the year ended December 31, 1996, File No. 1-3548), Second Supplemental Indenture, dated as of March 31, 1997 (filed as Exhibit 4 to Form 10-Q for the quarter ended March 31, 1997, File No. 1-3548) and Third Supplemental Indenture, dated as of May 28, 1997 (filed as Exhibit 4 to Form 10-Q for the quarter ended June 30, 1997, File No. 1-3548).

*4(d) - Amended and Restated Trust Agreement, dated as of March 1, 1996, relating to MP&L Capital I's 8.05% Cumulative Quarterly Income Preferred Securities, between the Company, as Depositor, and The Bank of New York, The Bank of New York (Delaware), Philip R. Halverson, David G. Gartzke and James K. Vizanko, as Trustees (filed as Exhibit 4(a) to Form 10-Q for the quarter ended March 31, 1996, File No. 1-3548).

*4(e) - Amendment No. 1, dated April 11, 1996, to Amended and Restated Trust Agreement, dated as of March 1, 1996, relating to MP&L Capital I's 8.05% Cumulative Quarterly Income Preferred Securities (filed as Exhibit 4(b) to Form 10-Q for the quarter ended March 31, 1996, File No. 1-3548).

*4(f) - Indenture, dated as of March 1, 1996, relating to the Company's 8.05% Junior Subordinated Debentures, Series A, Due 2015, between the Company and The Bank of New York, as Trustee (filed as Exhibit 4(c) to Form 10-Q for the quarter ended March 31, 1996, File No. 1-3548).

*4(g) - Guarantee Agreement, dated as of March 1, 1996, relating to MP&L Capital I's 8.05% Cumulative Quarterly Income Preferred Securities, between the Company, as Guarantor, and The Bank of New York, as Trustee (filed as Exhibit 4(d) to Form 10-Q for the quarter ended March 31, 1996, File No. 1-3548).

*4(h) - Agreement as to Expenses and Liabilities, dated as of March 20, 1996, relating to MP&L Capital I's 8.05% Cumulative Quarterly Income Preferred Securities, between the Company and MP&L Capital I (filed as Exhibit 4(e) to Form 10-Q for the quarter ended March 31, 1996, File No. 1-3548).

*4(i) - Officer's Certificate, dated March 20, 1996, establishing the terms of the 8.05% Junior Subordinated Debentures, Series A, Due 2015 issued in connection with the 8.05% Cumulative Quarterly Income Preferred Securities of MP&L Capital I.

*4(j) - Rights Agreement dated as of July 24, 1996, between Minnesota Power & Light Company and the Corporate Secretary of Minnesota Power & Light Company, as Rights Agent (filed as Exhibit 4 to Form 8-K dated August 2, 1996, File No. 1-3548).

*4(k) - Indenture, dated as of May 15, 1996, relating to the ADESA Corporation's 7.70% Senior Notes, Series A, Due 2006, between ADESA Corporation and The Bank of New York, as Trustee (filed as Exhibit 4(k) to Form 10-K for the year ended December 31, 1996, File No. 1-3548).

*4(l) - Guarantee of Minnesota Power & Light Company, dated as of May 30, 1996, relating to the ADESA Corporation's 7.70% Senior Notes, Series A, Due 2006 (filed as Exhibit 4(l) to Form 10-K for the year ended December 31, 1996, File No. 1-3548).

Exhibit Number		
*4(m)	-	ADESA Corporation Officer's Certificate 1-D-1, dated May 30, 1996, relating to the ADESA Corporation's 7.70% Senior Notes, Series A, Due 2006 (filed as Exhibit 4(m) to Form 10-K for the year ended December 31, 1996, File No. 1-3548).
*10(a)	-	Asset Holdings III, L.P. Note Purchase Agreement, dated as of November 22, 1994 (filed as Exhibit 10(i) to Form 10-K for the year ended December 31, 1995, File No. 1-3548).
*10(b)	-	Lease and Development Agreement, dated as of November 28, 1994 between Asset Holdings III, L.P., as Lessor and A.D.E. of Knoxville, Inc., as Lessee (filed as Exhibit 10(j) to Form 10-K for the year ended December 31, 1995, File No. 1-3548).
*10(c)	-	Lease and Development Agreement, dated as of November 28, 1994 between Asset Holdings III, L.P., as Lessor and ADESA-Charlotte, Inc., as Lessee (filed as Exhibit 10(k) to Form 10-K for the year ended December 31, 1995, File No. 1-3548).
*10(d)	-	Lease and Development Agreement, dated as of December 21, 1994 between Asset Holdings III, L.P., as Lessor and Auto Dealers Exchange of Concord, Inc., as Lessee (filed as Exhibit 10(l) to Form 10-K for the year ended December 31, 1995, File No. 1-3548).
*10(e)	-	Guaranty and Purchase Option Agreement between Asset Holdings III, L.P. and ADESA Corporation, dated as of November 28, 1994 (filed as Exhibit 10(m) to Form 10-K for the year ended December 31, 1995, File No. 1-3548).
*10(f)	-	Receivables Purchase Agreement dated as of December 31, 1996, among AFC Funding Corporation, as Seller, Automotive Finance Corporation, as Servicer, Pooled Accounts Receivable Capital Corporation, as Purchaser, and Nesbitt Burns Securities Inc., as Agent (filed as Exhibit 10(f) to Form 10-K for the year ended December 31, 1996, File No. 1-3548).
*10(g)	-	First Amendment to Receivables Purchase Agreement, dated as of February 28, 1997, among AFC Funding Corporation, as Seller, Automotive Finance Corporation, as Servicer, Pooled Accounts Receivable Capital Corporation, as Purchaser, and Nesbitt Burns Securities Inc., as Agent (filed as Exhibit 10(g) to Form 10-K for the year ended December 31, 1996, File No. 1-3548).
*10(h)	-	Second Amendment to Receivables Purchase Agreement, dated as of August 15, 1997, among AFC Funding Corporation, as Seller, Automotive Finance Corporation, as Servicer, Pooled Accounts Receivable Capital Corporation, as Purchaser, and Nesbitt Burns Securities Inc., as Agent (filed as Exhibit 10 to Form 10-Q for the quarter ended September 30, 1997, File No. 1-3548).
*10(i)	-	Purchase and Sale Agreement dated as of December 31, 1996, between AFC Funding Corporation and Automotive Finance Corporation (filed as Exhibit 10(h) to Form 10-K for the year ended December 31, 1996, File No. 1-3548).
+*10(j)	-	Minnesota Power Executive Annual Incentive Plan, effective January 1, 1996 (filed as Exhibit 10(a) to Form 10-K for the year ended December 31, 1995, File No. 1-3548).
+*10(k)	-	Minnesota Power and Affiliated Companies Supplemental Executive Retirement Plan, as amended and restated, effective August 1, 1994 (filed as Exhibit 10(b) to Form 10-K for the year ended December 31, 1995, File No. 1-3548).
+*10(l)	-	Executive Investment Plan-I, as amended and restated, effective November 1, 1988 (filed as Exhibit 10(c) to Form 10-K for the year ended December 31, 1988, File No. 1-3548).

Exhibit
Number
- - - -------

+*10(m)	-	Executive Investment Plan-II, as amended and restated, effective November 1, 1988 (filed as Exhibit 10(d) to Form 10-K for the year ended December 31, 1988, File No. 1-3548).
+*10(n)	-	Deferred Compensation Trust Agreement, as amended and restated, effective January 1, 1989 (filed as Exhibit 10(f) to Form 10-K for the year ended December 31, 1988, File No. 1-3548).
+*10(o)	-	Executive Long-Term Incentive Plan, as amended and restated, effective January 1, 1994 (filed as Exhibit 10(e) to Form 10-K for the year ended December 31, 1994, File No. 1-3548).
+*10(p)	-	Minnesota Power Executive Long-Term Incentive Compensation Plan, effective January 1, 1996 (filed as Exhibit 10(a) to Form 10-Q for the quarter ended June 30, 1996, File No. 1-3548).
+*10(q)	-	Directors' Long-Term Incentive Plan, as amended and restated, effective January 1, 1994 (filed as Exhibit 10(f) to Form 10-K for the year ended December 31, 1994, File No. 1-3548).
+*10(r)	-	Minnesota Power Director Stock Plan, effective January 1, 1995 (filed as Exhibit 10 to Form 10-Q for the quarter ended March 31, 1995, File No. 1-3548).
+*10(s)	-	Minnesota Power Director Long-Term Stock Incentive Plan, effective January 1, 1996 (filed as Exhibit 10(b) to Form 10-Q for the quarter ended June 30, 1996, File No. 1-3548).
12	-	Computation of Ratios of Earnings to Fixed Charges and Supplemental Ratios of Earnings to Fixed Charges.
13	-	Minnesota Power 1997 Annual Report - Management's Discussion and Analysis of Financial Condition and Results of Operations, and the Company's financial statements listed in Item 14 (a)(1) of this report.
*21	-	Subsidiaries of the Registrant (reference is made to the Company's Form U-3A-2 for the year ended December 31, 1997, File No. 69-78).
23(a)	-	Consent of Independent Accountants.
23(b)	-	Consent of General Counsel.
27	-	Financial Data Schedule.

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* Incorporated herein by reference as indicated.
\+ Management contract or compensatory plan or arrangement required to be filed as an exhibit to this report pursuant to Item 14(c) of Form 10-K.

(b) Reports on Form 8-K.

Report on Form 8-K dated and filed on February 20, 1998 with respect to Item 7. Financial Statements and Exhibits.

REPORT OF INDEPENDENT ACCOUNTANTS
ON FINANCIAL STATEMENT SCHEDULE

To the Board of Directors
of Minnesota Power

Our audits of the consolidated financial statements referred to in our report dated January 26, 1998 appearing on page 32 of the 1997 Annual Report to Shareholders of Minnesota Power (which report and consolidated financial statements are incorporated by reference in this Annual Report on Form 10-K) also included an audit of the Financial Statement Schedule listed in Item 14(a) of this Form 10-K. In our opinion, the Financial Statement Schedule presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

Price Waterhouse LLP

PRICE WATERHOUSE LLP
Minneapolis, Minnesota
January 26, 1998

MINNESOTA POWER AND SUBSIDIARIES

VALUATION AND QUALIFYING ACCOUNTS AND RESERVES
FOR THE YEARS ENDED DECEMBER 31, 1997, 1996 AND 1995
Millions

	Balance at Beginning of Year	Additions Charged to Income	Additions Other Changes	Deductions from Reserves	Balance at End of Period
Reserve deducted from related assets					
Provision for uncollectible accounts					
1997 Trade accounts receivable	$ 6.6	$ 14.4	$ 0.2	$ 8.6	$12.6
Other accounts receivable	1.5	0.4	-	0.2	1.7
1996 Trade accounts receivable	3.3	4.7	1.4	2.8	6.6
Other accounts receivable	1.2	0.2	0.2	0.1	1.5
1995 Trade accounts receivable	1.0	3.0	1.5	2.2	3.3
Other accounts receivable	2.8	0.2	-	1.8	1.2
Deferred asset valuation allowance					
1997 Deferred tax assets	0.7	(0.4)	-	-	0.3
1996 Deferred tax assets	8.9	(8.2)	-	-	0.7
1995 Deferred tax assets	26.8	(17.9)	-	-	8.9

Provision for uncollectible accounts includes bad debts written off.
The deferred tax asset valuation allowance was reduced by $8.2 million in 1996 ($18.4 million in 1995) based on a detailed analysis of projected cash flow as a result of a new business strategy for real estate operations. (See Note 15.)

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

MINNESOTA POWER & LIGHT COMPANY
(Registrant)

Dated: March 25, 1998

By EDWIN L. RUSSELL

Edwin L. Russell
Chairman, President and
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
EDWIN L. RUSSELL ------------------------------ Edwin L. Russell	Chairman, President, Chief Executive Officer and Director	March 25, 1998
D.G. GARTZKE ------------------------------ D.G. Gartzke	Senior Vice President - Finance and Chief Financial Officer	March 25, 1998
MARK A. SCHOBER ------------------------------ Mark A. Schober	Controller	March 25, 1998

Signature	Title	Date
KATHLEEN BREKKEN - - - ----------------------------- Kathleen Brekken	Director	March 25, 1998
MERRILL K. CRAGUN - - - ----------------------------- Merrill K. Cragun	Director	March 25, 1998
DENNIS E. EVANS - - - ----------------------------- Dennis E. Evans	Director	March 25, 1998
PETER J. JOHNSON - - - ----------------------------- Peter J. Johnson	Director	March 25, 1998
GEORGE L. MAYER - - - ----------------------------- George L. Mayer	Director	March 25, 1998
PAULA F. MCQUEEN - - - ----------------------------- Paula F. McQueen	Director	March 25, 1998
ROBERT S. NICKOLOFF - - - ----------------------------- Robert S. Nickoloff	Director	March 25, 1998
JACK I. RAJALA - - - ----------------------------- Jack I. Rajala	Director	March 25, 1998
EDWIN L. RUSSELL - - - ----------------------------- Edwin L. Russell	Director	March 25, 1998
AREND J. SANDBULTE - - - ----------------------------- Arend J. Sandbulte	Director	March 25, 1998
NICK SMITH - - - ----------------------------- Nick Smith	Director	March 25, 1998
BRUCE W. STENDER - - - ----------------------------- Bruce W. Stender	Director	March 25, 1998
DONALD C. WEGMILLER - - - ----------------------------- Donald C. Wegmiller	Director	March 25, 1998

MINNESOTA POWER & LIGHT COMPANY

TO

THE BANK OF NEW YORK
(FORMERLY IRVING TRUST COMPANY)

AND

W.T. CUNNINGHAM

(SUCCESSOR TO RICHARD H. WEST, J.A. AUSTIN,
E.J. MCCABE, D.W. MAY AND J.A. VAUGHAN)

AS TRUSTEES UNDER MINNESOTA POWER &
LIGHT COMPANY'S MORTGAGE AND DEED OF
TRUST DATED AS OF SEPTEMBER 1, 1945

TWENTIETH SUPPLEMENTAL INDENTURE

PROVIDING AMONG OTHER THINGS FOR

FIRST MORTGAGE BONDS, 6.68% SERIES DUE NOVEMBER 15, 2007

(TWENTY-SIXTH SERIES)

DATED AS OF NOVEMBER 1, 1997

TWENTIETH SUPPLEMENTAL INDENTURE

THIS INDENTURE, dated as of November 1, 1997, by and between MINNESOTA POWER & LIGHT COMPANY, a corporation of the State of Minnesota, whose post office address is 30 West Superior Street, Duluth, Minnesota 55802 (hereinafter sometimes called the "Company"), and THE BANK OF NEW YORK (formerly Irving Trust Company), a corporation of the State of New York, whose post office address is 101 Barclay Street, New York, New York 10286 (hereinafter sometimes called the "Corporate Trustee"), and W. T. CUNNINGHAM (successor to Richard H. West, J. A. Austin, E. J. McCabe, D. W. May and J. A. Vaughan), whose post office address is 3 Arlington Drive, Denville, New Jersey 07834 (said W. T. Cunningham being hereinafter sometimes called the "Co-Trustee" and the Corporate Trustee and the Co-Trustee being hereinafter together sometimes called the "Trustees"), as Trustees under the Mortgage and Deed of Trust, dated as of September 1, 1945, between the Company and Irving Trust Company and Richard H. West, as Trustees, securing bonds issued and to be issued as provided therein (hereinafter sometimes called the "Mortgage"), reference to which mortgage is hereby made, this indenture (hereinafter sometimes called the "Twentieth Supplemental Indenture") being supplemental thereto:

WHEREAS, the Mortgage was filed and recorded in various official records in the State of Minnesota; and

WHEREAS, an instrument, dated as of October 16, 1957, was executed and delivered under which J.A. Austin succeeded Richard H. West as Co-Trustee under the Mortgage, and such instrument was filed and recorded in various official records in the State of Minnesota; and

WHEREAS, an instrument, dated as of April 4, 1967, was executed and delivered under which E. J. McCabe in turn succeeded J.A. Austin as Co-Trustee under the Mortgage, and such instrument was filed and recorded in various official records in the State of Minnesota; and

WHEREAS, under the Sixth Supplemental Indenture, dated as of August 1, 1975, to which reference is hereinafter made, D.W. May in turn succeeded E. J. McCabe as Co-Trustee under the Mortgage; and

WHEREAS, an instrument, dated as of June 25, 1984, was executed and delivered under which J. A. Vaughan in turn succeeded D.W. May as Co-Trustee under the Mortgage, and such instrument was filed and recorded in various official records in the State of Minnesota; and

WHEREAS, an instrument, dated as of July 27, 1988, was executed and delivered under which W. T. Cunningham in turn succeeded J.A. Vaughan as Co-Trustee under the Mortgage, and such instrument was filed and recorded in various official records in the State of Minnesota; and

WHEREAS, by the Mortgage the Company covenanted, among other things, that it would execute and deliver such supplemental indenture or indentures and such further instruments and do such further acts as might be necessary or proper to carry out more effectually the purposes of the Mortgage and to make subject to the lien of the Mortgage any property thereafter acquired and intended to be subject to the lien thereof; and

WHEREAS, for said purposes, among others, the Company executed and delivered the following indentures supplemental to the Mortgage:

DESIGNATION	DATED AS OF
First Supplemental Indenture	March 1, 1949
Second Supplemental Indenture...............	July 1, 1951
Third Supplemental Indenture	March 1, 1957
Fourth Supplemental Indenture	January 1, 1968
Fifth Supplemental Indenture................	April 1, 1971
Sixth Supplemental Indenture	August 1, 1975
Seventh Supplemental Indenture	September 1, 1976
Eighth Supplemental Indenture...............	September 1, 1977
Ninth Supplemental Indenture	April 1, 1978
Tenth Supplemental Indenture................	August 1, 1978
Eleventh Supplemental Indenture.............	December 1, 1982
Twelfth Supplemental Indenture..............	April 1, 1987
Thirteenth Supplemental Indenture...........	March 1, 1992
Fourteenth Supplemental Indenture...........	June 1, 1992
Fifteenth Supplemental Indenture............	July 1, 1992
Sixteenth Supplemental Indenture............	July 1, 1992
Seventeenth Supplemental Indenture..........	February 1, 1993
Eighteenth Supplemental Indenture...........	July 1, 1993

which supplemental indentures were filed and recorded in various official records in the State of Minnesota; and

WHEREAS, for said purposes, among others, the Company also executed and delivered a Nineteenth Supplemental Indenture, dated as of February 1, 1997, which was filed and recorded in various official records in the State of Minnesota for which recording information is not yet available.

WHEREAS, the Company has heretofore issued, in accordance with the provisions of the Mortgage, as heretofore supplemented, the following series of First Mortgage Bonds:

SERIES	PRINCIPAL AMOUNT ISSUED	PRINCIPAL AMOUNT OUTSTANDING
3-1/8% Series due 1975....................	$26,000,000	None
3-1/8% Series due 1979....................	4,000,000	None
3-5/8% Series due 1981....................	10,000,000	None
4-3/4% Series due 1987....................	12,000,000	None
6-1/2% Series due 1998....................	18,000,000	$18,000,000
8-1/8% Series due 2001....................	23,000,000	None
10-1/2% Series due 2005...................	35,000,000	None
8.70% Series due 2006.....................	35,000,000	None
8.35% Series due 2007.....................	50,000,000	None
9-1/4% Series due 2008....................	50,000,000	None
Pollution Control Series A................	111,000,000	None
Industrial Development Series A...........	$2,500,000	None
Industrial Development Series B...........	1,800,000	None
Industrial Development Series C...........	1,150,000	None
Pollution Control Series B................	13,500,000	None
Pollution Control Series C................	2,000,000	None
Pollution Control Series D................	3,600,000	3,600,000
7-3/4% Series due 1994....................	55,000,000	None
7-3/8% Series due March 1, 1997...........	60,000,000	None
7-3/4% Series due June 1, 2007............	55,000,000	55,000,000
7-1/2% Series due August 1, 2007..........	35,000,000	35,000,000
Pollution Control Series E................	111,000,000	111,000,000
7% Series due March 1, 2008...............	50,000,000	50,000,000
6-1/4% Series due July 1, 2003............	25,000,000	25,000,000
7% Series due February 15, 2007...........	60,000,000	60,000,000

which bonds are also hereinafter sometimes called bonds of the First through Twenty-fifth Series, respectively; and

WHEREAS, Section 8 of the Mortgage provides that the form of each series of bonds (other than the First Series) issued thereunder and of coupons to be attached to coupon bonds of such series shall be established by Resolution of the Board of Directors of the Company and that the form of such series, as established by said Board of Directors, shall specify the descriptive title of the bonds and various other terms thereof, and may also contain such provisions not inconsistent with the provisions of the Mortgage as the Board of Directors may, in its discretion, cause to be inserted therein expressing or referring to the terms and conditions upon which such bonds are to be issued and/or secured under the Mortgage; and

WHEREAS, Section 120 of the Mortgage provides, among other things, that any power, privilege or right expressly or impliedly reserved to or in any way conferred upon the Company by any provision of the Mortgage, whether such power, privilege or right is in any way restricted or is unrestricted, may (to the extent permitted by law) be in whole or in part waived or surrendered or subjected to any restriction if at the time unrestricted or to additional restriction if already restricted, and the Company may enter into any further covenants, limitations or restrictions for the benefit of any one or more series of bonds issued thereunder, or the Company may cure any ambiguity contained therein, or in any supplemental indenture, or may establish the terms and provisions of any series of bonds (other than said First Series) by an instrument in writing executed and acknowledged by the Company in such manner as would be necessary to entitle a conveyance of real estate to record in all of the states in which any property at the time subject to the lien of the Mortgage shall be situated; and

WHEREAS, the Company now desires to create a new series of bonds and (pursuant to the provisions of Section 120 of the Mortgage) to add to its covenants and agreements contained in the Mortgage, as heretofore supplemented, certain other covenants and agreements to be observed by it and to alter and amend in certain respects the covenants and provisions contained in the Mortgage, as heretofore supplemented; and

WHEREAS, the execution and delivery by the Company of this Twentieth Supplemental Indenture, and the terms of the bonds of the Twenty-sixth Series, hereinafter referred to, have been duly authorized by the Board of Directors of the Company by appropriate resolutions of said Board of Directors;

NOW, THEREFORE, THIS INDENTURE WITNESSETH:

That the Company, in consideration of the premises and of One Dollar to it duly paid by the Trustees at or before the ensealing and delivery of these presents, the receipt whereof is hereby acknowledged, and in further evidence of assurance of the estate, title and rights of the Trustees and in order further to secure the payment of both the principal of and interest and premium, if any, on the bonds from time to time issued under the Mortgage, as heretofore supplemented, according to their tenor and effect and the performance of all the provisions of the Mortgage (including any instruments supplemental thereto and any modification made as in the Mortgage provided) and of said bonds, hereby grants, bargains, sells, releases, conveys, assigns, transfers, mortgages, pledges, sets over and confirms (subject, however, to Excepted Encumbrances) unto THE BANK OF NEW YORK and W. T. CUNNINGHAM, as Trustees under the

Mortgage, and to their successor or successors in said trust, and to said Trustees and their successors and assigns forever, all property, real, personal and mixed, of the kind or nature specifically mentioned in the Mortgage, as heretofore supplemented, or of any other kind or nature acquired by the Company after the date of the execution and delivery of the Mortgage, as heretofore supplemented (except any herein or in the Mortgage, as heretofore supplemented, expressly excepted), now owned or, subject to the provisions of subsection (I) of Section 87 of the Mortgage, hereafter acquired by the Company (by purchase, consolidation, merger, donation, construction, erection or in any other way) and wheresoever situated, including (without in anywise limiting or impairing by the enumeration of the same the scope and intent of the foregoing or of any general description contained in this Twentieth Supplemental Indenture) all lands, power sites, flowage rights, water rights, water locations, water appropriations, ditches, flumes, reservoirs, reservoir sites, canals, raceways, dams, dam sites, aqueducts, and all other rights or means for appropriating, conveying, storing and supplying water; all rights of way and roads; all plants for the generation of electricity by steam, water and/or other power; all power houses, gas plants, street lighting systems, standards and other equipment incidental thereto, telephone, radio and television systems, air-conditioning systems and equipment incidental thereto, water works, water systems, steam heat and hot water plants, substations, lines, service and supply systems, bridges, culverts, tracks, ice or refrigeration plants and equipment, offices, buildings and other structures and the equipment thereof; all machinery, engines, boilers, dynamos, electric, gas and other machines, regulators, meters, transformers, generators, motors, electrical, gas and mechanical appliances, conduits, cables, water, steam heat, gas or other pipes, gas mains and pipes, service pipes, fittings, valves and connections, pole and transmission lines, wires, cables, tools, implements, apparatus, furniture and chattels; all municipal and other franchises, consents or permits; all lines for the transmission and distribution of electric current, gas, steam heat or water for any purpose including towers, poles, wires, cables, pipes, conduits, ducts and all apparatus for use in connection therewith; all real estate, lands, easements, servitudes, licenses, permits, franchises, privileges, rights of way and other rights in or relating to real estate or the occupancy of the same and (except as herein or in the Mortgage, as heretofore supplemented, expressly excepted) all the right, title and interest of the Company in and to all other property of any kind or nature appertaining to and/or used and/or occupied and/or enjoyed in connection with any property hereinbefore or in the Mortgage, as heretofore supplemented, described.

TOGETHER WITH all and singular the tenements, hereditaments, prescriptions, servitudes and appurtenances belonging or in anywise appertaining to the aforesaid property or any part thereof, with the reversion and reversions, remainder and remainders and (subject to the provisions of Section 57 of the Mortgage) the tolls, rents, revenues, issues, earnings, income, product and profits thereof, and all the estate, right, title and interest and claim whatsoever, at law as well as in equity, which the Company now has or may hereafter acquire in and to the aforesaid property and franchises and every part and parcel thereof.

IT IS HEREBY AGREED by the Company that, subject to the provisions of subsection (I) of Section 87 of the Mortgage, all the property, rights, and franchises acquired by the Company (by purchase, consolidation, merger, donation, construction, erection or in any other way) after the date hereof, except any herein or in the Mortgage, as heretofore supplemented, expressly excepted, shall be and are as fully granted and conveyed hereby and by the Mortgage and as fully embraced within the lien hereof and the lien of the Mortgage as if such property, rights and franchises were now owned by the Company and were specifically described herein or in the Mortgage and conveyed hereby or thereby.

PROVIDED that the following are not and are not intended to be now or hereafter granted, bargained, sold, released, conveyed, assigned, transferred, mortgaged, hypothecated, affected, pledged, set over or confirmed hereunder and are hereby expressly excepted from the lien and operation of this Twentieth Supplemental Indenture and from the lien and operation of the Mortgage, namely: (1) cash, shares of stock, bonds, notes and other obligations and other securities not hereafter specifically pledged, paid, deposited, delivered or held under the Mortgage or covenanted so to be; (2) merchandise, equipment, apparatus, materials or supplies held for the purpose of sale or other disposition in the usual course of business; fuel, oil and similar materials and supplies consumable in the operation of any of the properties of the Company; all aircraft, rolling stock, trolley coaches, buses, motor coaches, automobiles and other vehicles and materials and supplies held for the purpose of repairing or replacing (in whole or part) any of the same; all timber, minerals, mineral rights and royalties; (3) bills, notes and accounts receivable, judgments, demands and choses in action, and all contracts, leases and operating agreements not specifically pledged under the Mortgage or covenanted so to be; the Company's contractual rights or other interest in or with respect to tires not owned by the Company; (4) the last day of the term of any lease or leasehold which may hereafter become subject to the lien of the Mortgage; (5) electric energy, gas, steam, ice, and other materials or products generated, manufactured, produced or purchased by the Company for sale, distribution or use in the ordinary course of its business; and (6) the Company's franchise to be a corporation; provided, however, that the property and rights expressly excepted from the lien and operation of this Twentieth Supplemental Indenture and from the lien and operation of the Mortgage in the above subdivisions (2) and (3) shall (to the extent permitted by law) cease to be so excepted in the event and as of the date that either or both of the Trustees or a receiver or trustee shall enter upon and take possession of the Mortgaged and Pledged Property in the manner provided in Article XIII of the Mortgage by reason of the occurrence of a Default as defined in Section 65 thereof.

TO HAVE AND TO HOLD all such properties, real, personal and mixed, granted, bargained, sold, released, conveyed, assigned, transferred, mortgaged, pledged, set over or confirmed by the Company as aforesaid, or intended so to be, unto the Trustees and their successors and assigns forever.

IN TRUST NEVERTHELESS, for the same purposes and upon the same terms, trusts and conditions and subject to and with the same provisos and covenants as are set forth in the Mortgage, as supplemented, this Twentieth Supplemental Indenture being supplemental thereto.

AND IT IS HEREBY COVENANTED by the Company that all the terms, conditions, provisos, covenants and provisions contained in the Mortgage, as heretofore supplemented, shall affect and apply to the property hereinbefore described and conveyed and to the estate, rights, obligations and duties of the Company and Trustees and the beneficiaries of the trust with respect to said property, and to the Trustees and their successors in the trust in the same manner and with the same effect as if said property had been owned by the Company at the time of the execution of the Mortgage, and had been specifically and at length described in and conveyed to said Trustees by the Mortgage as a part of the property therein stated to be conveyed.

The Company further covenants and agrees to and with the Trustees and their successors in said trust under the Mortgage as follows:

ARTICLE I
TWENTY-SIXTH SERIES OF BONDS

SECTION 1. There shall be a series of bonds designated "6.68% Series due November 15, 2007" (herein sometimes referred to as the "Twenty-sixth Series"), each of which shall also bear the descriptive title "First Mortgage Bond", and the form thereof, which shall be established by Resolution of the Board of Directors of the Company, shall contain suitable provisions with respect to the matters hereinafter in this Section specified. Bonds of the Twenty- sixth Series shall be dated as in Section 10 of the Mortgage provided, mature on November 15, 2007, be issued as fully registered bonds in denominations of One Thousand Dollars and, at the option of the Company, in any multiple or multiples of One Thousand Dollars (the exercise of such option to be evidenced by the execution and delivery thereof) and bear interest at the rate of 6.68% per annum, payable semi-annually on November 15 and May 15 of each year, commencing May 15, 1998, the principal of and interest on each said bond to be payable at the office or agency of the Company in the Borough of Manhattan, The City of New York, in such coin or currency of the United States of America as at the time of payment is legal tender for public and private debts.

(I) Bonds of the Twenty-sixth Series shall not be redeemable prior to maturity.

(II) At the option of the registered owner, any bonds of the Twenty-sixth Series, upon surrender thereof for cancellation at the office or agency of the Company in the Borough of Manhattan, The City of New York, together with a written instrument of transfer wherever required by the Company duly executed by the registered owner or by his duly authorized attorney, shall (subject to the provisions of Section 12 of the Mortgage) be exchangeable for a like aggregate principal amount of bonds of the same series of other authorized denominations.

Bonds of the Twenty-sixth Series shall be transferable (subject to the provisions of Section 12 of the Mortgage) at the office or agency of the Company in the Borough of Manhattan, The City of New York.

Upon any exchange or transfer of bonds of the Twenty-sixth Series, the Company may make a charge therefor sufficient to reimburse it for any tax or taxes or other governmental charge, as provided in Section 12 of the Mortgage, but the Company hereby waives any right to make a charge in addition thereto for any exchange or transfer of bonds of the Twenty-sixth Series.

Upon the delivery of this Twentieth Supplemental Indenture and upon compliance with the applicable provisions of the Mortgage, there shall be an initial issue of bonds of the Twenty- sixth Series for the aggregate principal amount of $20,000,000.

ARTICLE II

DIVIDEND COVENANT

SECTION 2. The Company covenants and agrees that the provisions of subdivision (III) of Section 39 of the Mortgage, which are to remain in effect so long as any of the bonds of the First Series shall remain Outstanding, shall remain in full force and effect so long as any bonds of the First through Twenty-sixth Series shall remain Outstanding.

ARTICLE III

MISCELLANEOUS PROVISIONS

SECTION 3. Section 126 of the Mortgage, as heretofore amended, is hereby further amended by adding the words "and November 15, 2007" after the words "February 15, 2007".

SECTION 4. Subject to the amendments provided for in this Twentieth Supplemental Indenture, the terms defined in the Mortgage, as heretofore supplemented, shall, for all purposes of this Twentieth Supplemental Indenture, have the meanings specified in the Mortgage, as heretofore supplemented.

SECTION 5. The holders of bonds of the Twenty-sixth Series consent that the Company may, but shall not be obligated to, fix a record date for the purpose of determining the holders of bonds of the Twenty-sixth Series entitled to consent to any amendment, supplement or waiver. If a record date is fixed, those persons who were holders at such record date (or their duly designated proxies), and only those persons, shall be entitled to consent to such amendment, supplement or waiver or to revoke any consent previously given, whether or not such persons continue to be holders after such record date. No such consent shall be valid or effective for more than 90 days after such record date.

SECTION 6. The Trustees hereby accept the trusts herein declared, provided, created or supplemented and agree to perform the same upon the terms and conditions herein and in the Mortgage set forth and upon the following terms and conditions:

The Trustees shall not be responsible in any manner whatsoever for or in respect of the validity or sufficiency of this Twentieth Supplemental Indenture or for or in respect of the recitals contained herein, all of which recitals are made by the Company solely. In general, each and every term and condition contained in Article XVII of the Mortgage shall apply to and form part of this Twentieth Supplemental Indenture with the same force and effect as if the same were herein set forth in full with such omissions, variations and insertions, if any, as may be appropriate to make the same conform to the provisions of this Twentieth Supplemental Indenture.

SECTION 7. Whenever in this Twentieth Supplemental Indenture any party hereto is named or referred to, this shall, subject to the provisions of Articles XVI and XVII of the Mortgage, as heretofore supplemented, be deemed to include the successors or assigns of such party, and all the covenants and agreements in this Twentieth Supplemental Indenture contained by or on behalf of the Company, or by or on behalf of the Trustees shall, subject as aforesaid, bind and inure to the benefit of the respective successors and assigns of such party whether so expressed or not.

SECTION 8. Nothing in this Twentieth Supplemental Indenture, expressed or implied, is intended, or shall be construed, to confer upon, or give to, any person, firm or corporation, other than the parties hereto and the holders of the bonds and coupons Outstanding under the Mortgage, any right, remedy, or claim under or by reason of this Twentieth Supplemental Indenture or any covenant, condition, stipulation, promise or agreement hereof, and all the covenants, conditions, stipulations, promises and agreements in this Twentieth Supplemental Indenture contained by and on behalf of the Company shall be for the sole and exclusive benefit of the parties hereto, and of the holders of the bonds and of the coupons Outstanding under the Mortgage.

SECTION 9. This Twentieth Supplemental Indenture shall be executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument.

SECTION 10. The Company, the mortgagor named herein, by its execution hereof acknowledges receipt of a full, true and complete copy of this Twentieth Supplemental Indenture.

IN WITNESS WHEREOF, Minnesota Power & Light Company has caused its corporate name to be hereunto affixed, and this instrument to be signed and sealed by its President or one of its Vice Presidents, and its corporate seal to be attested by its Secretary or one of its Assistant Secretaries for and in its behalf, and The Bank of New York has caused its corporate name to be hereunto affixed, and this instrument to be signed and sealed by one of its Vice Presidents or one of its Assistant Vice Presidents and its corporate seal to be attested by one of its Assistant Treasurers or one of its Assistant Vice Presidents, and W. T. Cunningham has hereunto set his hand and affixed his seal, all in The City of New York, as of the day and year first above written.

MINNESOTA POWER & LIGHT COMPANY

[MINNESOTA POWER & LIGHT COMPANY
CORPORATE SEAL
MINESOTA]

By David G. Gartzke

David G. Gartzke
Senior Vice President - Finance
and Chief Financial Officer

Attest:

Philip R. Halverson
- - - ------------------------
Philip R. Halverson
Vice President, Counsel
and Secretary

Executed, sealed and delivered by
MINNESOTA POWER & LIGHT COMPANY
in the presence of:

Lorie Skudstad
- - - -------------------------

Geraldine Peterson
- - - -------------------------

THE BANK OF NEW YORK
as Trustee

By Thomas B. Zakrzewski

Thomas B. Zakrzewski
Assistant Vice President

Attest:

Remo J. Reale
- - - -------------------------
Remo J. Reale
Assistant Vice President

W. T. Cunningham (L.S.)

W.T. Cunningham

Executed, sealed and delivered by
THE BANK OF NEW YORK AND W. T. CUNNINGHAM
in the presence of:

Michele L. Russo
- - - -------------------------

Essie Elcock
- - - -------------------------

STATE OF MINNESOTA)
) SS.:
COUNTY OF ST. LOUIS)

On this 20th day of November, 1997, before me, a Notary Public within and for said County, personally appeared DAVID G. GARTZKE and PHILIP R. HALVERSON, to me personally known, who, being each by me duly sworn, did say that they are respectively the Senior Vice President - Finance and Chief Financial Officer and the Vice President, General Counsel and Secretary of MINNESOTA POWER & LIGHT COMPANY of the State of Minnesota, the corporation named in the foregoing instrument; that the seal affixed to the foregoing instrument is the corporate seal of said corporation; that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors; and said DAVID G. GARTZKE and PHILIP R. HALVERSON acknowledged said instrument to be the free act and deed of said corporation.

Personally came before me on this 20th day of November, 1997, DAVID G. GARTZKE to me known to be the Senior Vice President - Finance and Chief Financial Officer and PHILIP R. HALVERSON, to me known to be the Vice President, General Counsel and Secretary, of the above named MINNESOTA POWER & LIGHT COMPANY, the corporation described in and which executed the foregoing instrument, and to me personally known to be the persons who as such officers executed the foregoing instrument in the name and behalf of said corporation, who, being by me duly sworn did depose and say and acknowledge that they are respectively the Senior Vice President - Finance and Chief Financial Officer and the Vice President, General Counsel and Secretary of said corporation; that the seal affixed to said instrument is the corporate seal of said corporation; and that they signed, sealed and delivered said instrument in the name and on behalf of said corporation by authority of its Board of Directors and stockholders, and said DAVID G. GARTZKE and PHILIP R. HALVERSON then and there acknowledged said instrument to be the free act and deed of said corporation and that such corporation executed the same.

On the 20th day of November, 1997, before me personally came DAVID G. GARTZKE and PHILIP R. HALVERSON, to me known, who, being by me duly sworn, did depose and say that they respectively reside at 2609 East 5th Street, Duluth, Minnesota 55812, and 3364 West Tischer Road, Duluth, Minnesota 55803; that they are respectively the Senior Vice President - Finance and Chief Financial Officer and the Vice President, General Counsel and Secretary of MINNESOTA POWER & LIGHT COMPANY, one of the corporations described in and which executed the above instrument; that they know the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of Directors of said corporation, and that they signed their names thereto by like order.

GIVEN under my hand and notarial seal this 20th day of November, 1997.

Jeannette A. Atkinson

JEANNETTE A. ATKINSON
[SEAL] NOTARY PUBLIC-MINNESOTA
ST. LOUIS COUNTY
My Commission Expires Jan. 31, 2000

STATE OF NEW YORK)
) SS:
COUNTY OF NEW YORK)

On this 20th day of November, 1997, before me, a Notary Public within and for said County, personally appeared THOMAS B. ZAKRZEWSKI and REMO J. REALE, to me personally known, who, being each by me duly sworn, did say that they are respectively an Assistant Vice President and an Assistant Vice President of THE BANK OF NEW YORK of the State of New York, the corporation named in the foregoing instrument; that the seal affixed to the foregoing instrument is the corporate seal of said corporation; that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors; and said THOMAS B. ZAKRZEWSKI and REMO J. REALE acknowledged said instrument to be the free act and deed of said corporation.

Personally came before me on this 20th day of November, 1997, THOMAS B. ZAKRZEWSKI, to me known to be an Assistant Vice President, and REMO J. REALE, known to me to be an Assistant Vice President, of the above named THE BANK OF NEW YORK, the corporation described in and which executed the foregoing instrument, and to me personally known to be the persons who as such officers executed the foregoing instrument in the name and behalf of said corporation, who, being by me duly sworn did depose and say and acknowledge that they are respectively an Assistant Vice President and an Assistant Vice President of said corporation; that the seal affixed to said instrument is the corporate seal of said corporation; and that they signed, sealed and delivered said instrument in the name and on behalf of said corporation by authority of its Board of Directors, and said THOMAS B. ZAKRZEWSKI and REMO J. REALE then and there acknowledged said instrument to be the free act and deed of said corporation and that such corporation executed the same.

On the 20th day of November, 1997, before me personally came THOMAS B. ZAKRZEWSKI and REMO J. REALE, to me known, who, being by me duly sworn, did depose and say that they respectively reside at 63 Sargent Road, Freehold, New Jersey 07728 and 111 Jackson Street, Garden City, New York; that they are respectively an Assistant Vice President and an Assistant Vice President of THE BANK OF NEW YORK, one of the corporations described in and which executed the above instrument; that they know the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of Directors of said corporation, and that they signed their names thereto by like order.

GIVEN under my hand and notarial seal this 20th day of November, 1997.

[SEAL
William J. Cassels
Notary
Public
State of New York]

William J. Cassels

William J. Cassels
Notary Public, State of New York
No. 01CA5027729
Qualified in Bronx County
Certificate Filed in New York County
Commission Expires May 16, 1998

STATE OF NEW YORK)
) SS:
COUNTY OF NEW YORK)

On this 20th day of November, 1997 before me personally appeared W. T. CUNNINGHAM, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

Personally came before me this 20th day of November, 1997, the above named W. T. CUNNINGHAM, to me known to be the person who executed the foregoing instrument, and acknowledged the same.

On the 20th day of November, 1997, before me personally came W. T. CUNNINGHAM, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same.

GIVEN under my hand and notarial seal this 20th day of November, 1997.

[SEAL
William J. Cassels
Notary
Public
State of New York]

William J. Cassels

William J. Cassels
Notary Public, State of New York
No. 01CA5027729
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Exhibit 12

Minnesota Power & Light Company
Computation of Ratios of Earnings to Fixed Charges and
Supplemental Ratios of Earnings to Fixed Charges

	For the Year Ended December 31,				
	1993	1994	1995	1996	1997
	Millions except ratios				
Income from continuing operations per consolidated statement of income	$ 64.4	$ 59.5	$ 61.9	$ 69.2	$ 77.6
Add (deduct)					
Current income tax expense	29.3	24.1	13.4	31.4	44.6
Deferred income tax expense (benefit)	1.1	(1.0)	(11.3)	(9.8)	3.3
Deferred investment tax credits	(2.0)	(2.5)	(0.9)	(2.0)	(1.3)
Undistributed income from less than 50% owned equity investments	(6.0)	(7.5)	(9.1)	(11.0)	(13.9)
Minority interest	(0.2)	(0.9)	0.2	3.3	2.3
	86.6	71.7	54.2	81.1	112.6
Fixed charges					
Interest on long-term debt	44.6	48.1	45.7	52.4	50.4
Capitalized interest	3.0	-	1.4	1.5	1.5
Other interest charges - net	1.5	7.4	7.9	10.2	14.3
Interest component of all rentals	5.8	5.8	3.7	2.5	3.7
Distributions on redeemable preferred securities of subsidiary	-	-	-	4.7	6.0
Total fixed charges	54.9	61.3	58.7	71.3	75.9
Earnings before income taxes and fixed charges (excluding capitalized interest)	$138.5	$133.0	$111.5	$150.9	$187.0
Ratio of earnings to fixed charges	2.52	2.17	1.90	2.12	2.46
Earnings before income taxes and fixed charges (excluding capitalized interest)	$138.5	$133.0	$111.5	$150.9	$187.0
Supplemental charges	15.1	14.4	13.5	14.4	12.0
Earnings before income taxes and fixed and supplemental charges (excluding capitalized interest)	$153.6	$147.4	$125.0	$165.3	$199.0
Total fixed charges	$ 54.9	$ 61.3	$ 58.7	$ 71.3	$ 75.9
Supplemental charges	15.1	14.4	13.5	14.4	12.0
Fixed and supplemental charges	$ 70.0	$ 75.7	$ 72.2	$ 85.7	$ 87.9
Supplemental ratio of earnings to fixed charges	2.19	1.95	1.73	1.93	2.26

- - - -------------

The supplemental ratio of earnings to fixed charges includes the Company's obligation under a contract with Square Butte Electric Cooperative (Square Butte) which extends through 2007, pursuant to which the Company is purchasing 71 percent of the output of a generating unit capable of generating up to 455 megawatts. The Company is obligated to pay Square Butte all of Square Butte's leasing, operating and debt service costs, less any amount collected from the sale of power or energy to others, which shall not have been paid by Square Butte when due. (See Note 5.)

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
[MP LOGO]

MINNESOTA POWER is a broadly diversified service company with operations in four business segments: (1) Electric Operations, which include electric and gas services, and coal mining; (2) Water Services, which include water and wastewater services; (3) Automotive Services, which include a vehicle auction business, a finance company and an auto transport company; and (4) Investments, which include a securities portfolio, a 21% equity investment in a financial guaranty reinsurance and insurance company, and real estate operations.

CONSOLIDATED OVERVIEW

The Company demonstrated strong operating performance in 1997 earning $2.47 per share of common stock ($2.28 in 1996; $2.16 in 1995). Since 1995 operating income has more than doubled and net income has increased 20%.

	1997	1996	1995
	Millions		
Operating Revenue and Income			
Electric Operations	$541.9	$529.2	$503.5
Water Services	95.5	85.2	66.1
Automotive Services	255.5	183.9	61.6
Investments	60.9	49.9	43.7
Corporate Charges	(0.2)	(1.3)	(2.0)
	$953.6	$846.9	$672.9
Operating Income			
Electric Operations	$71.7	$63.6	$67.1
Water Services	12.7	8.1	(2.3)
Automotive Services	28.4	7.7	1.2
Investments	50.8	40.5	29.7
Corporate Charges	(33.4)	(26.4)	(32.7)
	$130.2	$93.5	$63.0
Net Income			
Electric Operations	$43.1	$39.4	$41.0
Water Services	8.2	5.4	(1.0)
Automotive Services	14.0	3.7	-
Investments	32.1	38.1	41.3
Corporate Charges	(19.8)	(17.4)	(19.4)
	77.6	69.2	61.9
Discontinued Operations	-	-	2.8
	$77.6	$69.2	$64.7
Earnings Per Share of Common Stock	$2.47	$2.28	$2.16
Average Shares of Common Stock - Millions	30.6	29.3	28.5
Return on Average Common Equity	12.1%	11.3%	10.7%

All of the Company's business segments reflected ongoing operational improvements in 1997, stemming from sales growth and continued implementation of the Company's corporate strategy. Most significant growth came from Automotive Services where net income increased nearly four times. Expansion projects were a success as were improvements from operations due to cost controls and increased sales volume.

The Company measures profitability of its operations through careful budgeting and monitoring of contributions by business segment to corporate net income. Corporate Charges represent general corporate expenses, including interest, not specifically related to any one business segment.

The following summarizes significant events which impacted the Company's earnings for the past three years. Detailed discussions for each business segment follow. Abbreviations and acronyms are defined on page 50.

1997. Electric Operations reflected continued strong demand for electricity from industrial customers and higher profit margins on sales to other power suppliers. Gains from the sale of certain land and other property were balanced by start-up costs associated with strategic initiatives and incentive compensation awards related to total shareholder return performance. Water Services showed improved operating efficiencies, a full year of higher rates and a gain from the sale of certain water and wastewater assets. One-time charges and start-up costs associated with strategic non-regulated initiatives were also reflected in Water Services. Automotive Services reported increased vehicle sales and services at auctions, and the addition of 25 new loan production offices by the financing business. A more conservative allowance for bad debts offset a gain from the sale of excess land. Investments recorded increased sales from real estate operations. Corporate Charges reflected increased debt service costs to finance investments in non-regulated operations and various strategic initiatives.

1996. Electric Operations exceeded the record-setting kilowatthour sales of 1995 and established MPEX, the Company's power marketing division. Water Services reflected increased rates and gains from the strategic sale of water assets. Automotive Services included a full twelve months of operations. The auction business added eight auction facilities, while the financing business added 13 loan production offices. Investments included the recognition of tax benefits and the sale of a joint venture from real estate operations. Corporate Charges included nine months of distributions with respect to Cumulative Quarterly Income Preferred Securities issued in March 1996.

1995. Electric Operations reached record-setting kilowatthour sales. Water Services reflected lower consumption due to abnormally high rainfall and less customers because of the sale of assets in December 1994. Automotive Services reported six months of operations and significant start-up costs following the July 1995 purchase of ADESA. Investments included the recognition of tax benefits from real estate operations. Corporate Charges included the write-off of the Company's investment in Reach All Partnership. Discontinued Operations represented results from the paper and pulp business which was sold in June 1995.

ELECTRIC OPERATIONS

Electric Operations generate, transmit, distribute, and market electricity. Minnesota Power provides electricity to 122,000 customers in northeastern Minnesota, while the Company's wholly owned subsidiary, Superior Water, Light and Power Company, sells electricity to 14,000 customers and natural gas to 11,000 customers, and provides water to 10,000 customers, all in northwestern Wisconsin. Another wholly owned subsidiary, BNI Coal, owns and operates a lignite coal mine in North Dakota. Two electric generating cooperatives, Minnkota Power Cooperative, Inc. and Square Butte, consume virtually all of BNI Coal's production of lignite coal under contracts extending to 2027.

Electric Operations contributed net income of $43.1 million in 1997 ($39.4 million in 1996; $41.0 million in 1995). Financial performance for 1997 reflected solid operating results, which included higher profit margins from sales to other power suppliers and gains from the sale of certain land and other property.

Changes in Electric Operating Revenue and Income	1997	1996
	(Change from previous year in millions)	
Retail electric sales	$ 1.1	$(2.7)
Sales to other power suppliers	(3.0)	22.4
Transmission revenue	2.9	-
Conservation improvement programs	2.9	-
Fuel clause adjustments	2.9	-
Coal revenue	0.5	1.1
Other	5.4	4.9
	$12.7	$25.7

ELECTRIC SALES. Total kWh sales were 12.4 billion in 1997 (13.2 billion in 1996, the record high; 11.5 billion in 1995). The 6% decline in 1997 was attributable to restricted market opportunities for MPEX sales. Less power was available for sale because of higher prices for purchased power, reduction in transmission capability damaged by severe spring storms in the Midwest, various generating unit outages at Company and other plants in the Midwest, and less hydro generation in Canada. MPEX is an expansion of the Company's inter-utility marketing group which has been a buyer and seller of capacity and energy for over 25 years in the wholesale power market. The customers of MPEX are other power suppliers in the Midwest and Canada. MPEX also contracts with its customers to provide hourly energy scheduling and power trading services.

The two major industries in Minnesota Power's service territory are taconite production, and paper and pulp mills. Taconite mining customers accounted for 31% of electric operating revenue in 1997 (32% in 1996; 35% in 1995). Paper and pulp customers accounted for 12% of electric operating revenue in 1997 (11% in 1996; 12% in 1995). In addition to these industries, sales to otherpower suppliers accounted for 12% of electric operating revenue in 1997 (13% in 1996; 9% in 1995).

Taconite is an important raw material for the steel industry and is made from low iron content ore mined in northern Minnesota. Taconite processing plants use large quantities of electric power to grind the ore and concentrate the iron particles into taconite pellets. Annual taconite production in Minnesota was 47 million tons in 1997 (46 million tons in 1996; 47 million tons in 1995). Minnesota Power expects taconite production in 1998 to remain at or near the 1997 level.

While taconite production is expected to continue at annual levels over 40 million tons, the long-term future of this cyclical industry is less certain. Production may decline gradually some time after the year 2008.

LARGE POWER CUSTOMER CONTRACTS. The Company has electric service contracts with 11 large power industrial customers that require 10 MW or more of power (five taconite producers, four paper and pulp mills, and two pipeline companies). Each contract requires payment of a minimum monthly demand charge that covers a portion of the fixed costs associated with having capacity available to serve them, including a return on common equity. The demand charge is paid by these customers even if no electrical energy is taken. An energy charge is also paid to cover the variable cost of energy actually used. The rates and corresponding revenue associated with capacity and energy provided under these contracts are subject to change through the regulatory process governing all retail electric rates.

Minimum Revenue and Demand
Under Contract as of February 1, 1998

	Minimum Annual Revenue	Monthly Megawatts
1998	$92.1 million	586
1999	$78.3 million	512
2000	$69.2 million	465
2001	$66.5 million	448
2002	$47.3 million	319

Based on past experience and projected operating levels, the Company believes revenue from large power customers will be substantially in excess of the minimum contract amounts.

In addition to the minimum demand provisions, contracts with taconite producers and pipeline companies require these customers to purchase their entire electric service requirements from the Company for the duration of the contract. In addition, six of the large power customers purchase a combined total of 200 MW of interruptible service pursuant to contractual commitments and an interruptible rate schedule. Under this schedule and pursuant to contractual commitments, the Company has the right to serve 100 MW of these customers' needs through Oct. 31, 2008, and another 100 MW of these customers' needs through April 30, 2010. The Company has the right of first refusal to serve an additional 200 MW during these same time periods.

Contract termination dates range from October 1999 to July 2008. Each contract continues after the contract termination date, unless the required four-year advance notice of cancellation has been given. These contract termination dates exclude any interruptible service commitments. Minnesota Power has implemented a key account management process and anticipates continuing negotiations with its large industrial and commercial customers to explore contractual options to lower energy costs. During 1996 and 1997 the Company successfully negotiated extended contracts with six of its large power customers. Contract extensions with two more large power customers are pending MPUC approvals.

[Graphic Material Omitted]

Average Cost of Fuel
For Electric Generation
Cents per Million Btu's

	Total Electric Utility Industry	West North Central Region	Minnesota Power
1992	166.6	118.7	118.9
93	166.6	111.9	115.6
94	152.6	100.9	97.0
95	145.2	97.6	99.4
96	151.9	94.6	96.5
97	N/A	N/A	99.6

FUEL. The cost of coal is the Company's largest single operating expense in generating electricity. Coal consumption at the Company's generating stations in 1997 was 4.1 million tons. Minnesota Power currently has three coal supply agreements in place with Montana suppliers. Two terminate in December 1999 and the other in December 2000. Under these agreements the Company has the tonnage flexibility to procure 70% to 100% of its total coal requirements. The Company uses this flexibility to purchase coal under spot-market agreements when favorable market conditions exist. The Company is exploring future supply options and believes that adequate supplies of low-sulfur, sub-bituminous coal will continue to be available. The Company has contracts with Burlington Northern Santa Fe Railroad to deliver coal from Montana and Wyoming to the Company's generating facilities in Minnesota through December 2003.

PURCHASED POWER CONTRACT. Under an agreement extending through 2007 with Square Butte, Minnesota Power purchases 71% (about 317 MW during the summer months and 322 MW during the winter months) of the output of a mine-mouth generating unit located near Center, North Dakota. The Square Butte unit is one of two lignite-fired units at Minnkota Power Cooperative's Milton R. Young Generating Station.

Square Butte has the option, upon a five year advance notice, to reduce the Company's share of the unit's output to 49%. Minnesota Power has the option, though not the obligation, to continue to purchase 49% of the output at market-based prices after 2007 to the end of the plant's economic life. Minnesota Power must pay any Square Butte costs and expenses that have not been paid by Square Butte when due, regardless of whether or not the Company receives any power from that unit.

COMPETITION. The electric utility industry continues to evolve at both the wholesale and retail levels. This has resulted in a more competitive market for electricity generally and particularly in wholesale markets. Retail deregulation of the industry is being considered at both the federal and state level, and affects the way the Company strategically views the future. With electric rates among the lowest in the U.S. and with long-term wholesale and large power retail contracts in place, Minnesota Power believes its Electric Operations are well positioned to address and benefit from competitive pressures.

WHOLESALE. Minnesota Power's MPEX division conducts an active wholesale power marketing and trading business. On Dec. 15, 1997, Manitoba Hydro and Minnesota Power jointly announced the signing of a three-year agreement whereby MPEX will provide Manitoba Hydro with hourly power trading and energy scheduling services in the U.S. This agreement became effective Jan. 1, 1998. Manitoba Hydro is the fourth largest electric utility in Canada. More than a third of Manitoba Hydro's electric sales represent exports of renewable hydroelectricity to the U.S. and neighboring provinces in Canada. MPEX is reviewing new strategic opportunities for its wholesale marketing operations in light of the new Open Access Transmission Rules enacted by FERC in 1996. Wholesale contracts with a number of municipal customers have been extended and modified.

In 1996 the Company completed functional unbundling of its operations under FERC Order No. 888, "Open Access Transmission Rules." This order required public utilities to take transmission service for their own wholesale transactions under the same terms and conditions on which transmission service is provided to third parties. Also in 1996, the Company filed its "Code of Conduct" under FERC Order No. 889, "Open Access Same Time Information System and Standards of Conduct," which formalized the functional separation of generation from transmission within the organization.

The transmission component of Electric Operations is organized for and conducting business under these new federal regulatory requirements.

RETAIL. In 1995 the MPUC initiated an investigation into structural and regulatory issues of the electric utility industry. To make certain that delivery of electric service will be efficient following any restructuring, the MPUC adopted 15 principles to guide a deliberate and orderly approach to developing reasonable restructuring alternatives that ensure the fairness of a competitive market and protect the public interest. In January 1996 the MPUC established a competition working group in which company representatives have participated in addressing issues related to wholesale and retail competition. That group issued a Wholesale Competition Report in October 1996 and a Retail Competition Report in November 1997. The MPUC is expected to begin identifying the steps that are necessary to successfully implement restructuring upon receipt of a legislative mandate.

LEGISLATION. During 1998 Congress is expected to continue to debate proposed legislation which, if enacted, would promote retail customer choice and a more competitive electric market. The Company is actively participating in the dialogue and debate on these issues in various forums, principally to advocate fairness and parity for all power and energy competitors in deregulated markets that may be created by new legislation. While Congress is not expected to pass legislation in 1998, the Company cannot predict the timing or substance of any future legislation which might ultimately be enacted. However, the Company will take the necessary steps to maintain its competitive position as both a low-cost supplier and a long-term supplier to large industrial customers. The Company is also promoting property tax reform before the Minnesota legislature in order to eliminate the taxation of personal property that results in an inequitable tax burden among current and potential competitors in local markets.

Legislative activity is evolving both in Minnesota and Wisconsin. An Electric Energy Task Force comprised of representatives of both houses of the Minnesota legislature continues to study a variety of issues related to industry restructuring. The Wisconsin legislature is pursuing electric utility industry restructuring, including the possible formation of an independent transmission system operator within the state. In Minnesota legislation has been introduced, but the Governor and legislative leadership have indicated that no action to restructure the industry will be taken in 1998.

CONSERVATION. Minnesota requires electric utilities to spend a minimum of 1.5% of annual retail electric revenue on conservation improvement programs (CIP) each year. An annually approved billing adjustment combined with retail base rates allows the Company to recover both costs of energy-saving programs and lost margins associated with power saved as a result of such programs. The Company's largest conservation programs are targeted at taconite and paper customers to promote their efficient use of energy. CIP also provides demand-side management grants on a competitive basis to commercial and small industrial customers, low-cost financing for energy-saving investments, and promotes energy conservation for residential and commercial customers. SWL&P also offers electric and gas conservation programs to qualified customers as approved by the PSCW.

ENVIRONMENTAL. CLEAN AIR ACT. By burning low sulfur coal in units equipped with pollution control equipment, the Company's power plants presently operate well below the sulfur dioxide emission limits set for the year 2000 by the federal Clean Air Act. The Company has spent $4.2 million and will spend an additional $1.8 million in 1998 on advanced low emission burner technology and associated control equipment to operate at or below the compliance standards for nitrogen oxide emissions required by the Clean Air Act. The final stage of this project is expected to be completed by mid-1998.

KYOTO PROTOCOL. On Dec. 11, 1997, the United Nations Framework Convention on Climate Change agreed upon a draft international treaty, the Kyoto Protocol, (Protocol) which, if ratified, would call for reductions in greenhouse gas emissions. The United States' target is to achieve a 7% reduction below 1990 emission levels by the period 2008-2012. The Protocol must be ratified by the U.S. Senate by March 15, 1999; however, the treaty does not currently satisfy the guidance provided in a 1997 Senate resolution. The Company currently cannot predict when or if the Protocol will be ratified nor can it determine the impact such ratification would have on the Company.

1997 TO 1996 COMPARISON. Operating revenue and income from Electric Operations were up $12.7 million in 1997. The demand for electricity by all customer classes continued to be strong in 1997, as did the marketing of sales to other power suppliers. Revenue from sales to other power suppliers was 4% lower in 1997 because less power was available. Less power was available for sale because of higher prices for purchased power, reduction in transmission capability damaged by severe spring storms in the Midwest, various generating unit outages at Company and other plants in the Midwest, and less hydro generation in Canada. While total revenue from sales to other power suppliers was lower in 1997, higher profit margins were realized on these sales. To ensure the preservation of wilderness lands, in 1997 the Company sold property along the St. Louis River to the State of Minnesota. The Company also sold rights to microwave frequencies in accordance with a federal mandate. Pre-tax gains totaling $4.3 million from these two sales were included in 1997 operating revenue and income. Total operating expenses from Electric Operations increased $4.6 million in 1997. Purchased power expenses and depreciation expense both increased $3 million, while the recent reform of the Minnesota property tax system reduced property taxes by $2.8 million in 1997. Start-up costs associated with strategic initiatives and incentive compensation awards related to total shareholder return performance also contributed to higher operating expenses in 1997. Interest expense was $1.2 million lower in 1997 as a result of debt refinanced at lower rates.

1996 TO 1995 COMPARISON. Operating revenue and income from Electric Operations were $25.7 million higher in 1996 due to a 14% increase in total kWh sales. The increase in sales was primarily attributed to the Company's marketing of power to other power suppliers. Extreme winter weather in 1996 compared to the milder winter in 1995 increased sales to residential and commercial customers, and reduced sales to taconite producers. While revenue from sales of electricity was higher in 1996, lower margins were realized because the cooler summer weather in 1996 resulted in lower wholesale pricing. Total electric operating expenses were $29.2 million higher in 1996. The $13.9 million increase in fuel and purchased power expenses in 1996 was attributed to the 14% increase in total kWh sales. In addition, Square Butte, one of Minnesota Power's low priced sources of energy, produced 23% more energy in 1996 after being down for scheduled maintenance in 1995. Operations expenses included costs associated with the mid-1995 early retirement offering which was part of the Company's ongoing efforts to control costs and maintain low electric rates. The cost of the offering was $15 million and is being amortized over 3 years. Expenses in 1996 included twelve months of amortization, while 1995 included only five months. Employee and customer related expenses were also higher in 1996.

OUTLOOK. The contribution from Electric Operations is expected to remain stable as the industry continues to restructure. Electric Operations intend to seek additional cost saving alternatives and efficiencies, and expand non-regulated services to maintain its contribution to net income. MP Enterprises, a wholly owned subsidiary of the Company, was created in 1996 to facilitate the development of the non-regulated services of Electric Operations. It provides the required expertise necessary to offer these services within and outside the Company's electric service territory. The Company's newest non-regulated subsidiary, MP Telecom, was established in 1997 to provide high volume fiber optic and microwave communications to businesses across the Company's service territory.

WATER SERVICES

Water Services are comprised of regulated and non-regulated wholly owned subsidiaries of the Company. REGULATED SUBSIDIARIES. Florida Water, the largest investor owned water supplier in Florida, provides water to 119,000 customers and wastewater treatment services to 52,000 customers in Florida. Heater provides water to 28,000 customers and wastewater treatment services to 2,000 customers in North Carolina and South Carolina. NON-REGULATED SUBSIDIARIES. Instrumentation Services, Inc. and U.S. Maintenance and Management provide predictive maintenance services to water utility companies and other industrial operations in several southern states. Headquartered in Chicago, Illinois, Americas' Water offers contract management, operations and maintenance services to governments and industries throughout the Americas.

Water Services contributed net income of $8.2 million in 1997 ($5.4 million in 1996; $(1.0) million in 1995). Financial performance for 1997 reflected improved operating efficiencies at Florida Water, a full year of rate relief and a gain from the strategic sale of certain water assets.

[Graphic Material Omitted]

Water Services
Operating Revenue
and Income

	Millions
1995	$66.1
96	$85.2
97	$95.5

WATER AND WASTEWATER RATES. 1995 RATE CASE. Florida Water requested an $18.1 million rate increase in June 1995 for all water and wastewater customers of Florida Water regulated by the FPSC. In October 1996 the FPSC issued its final order approving an $11.1 million annual increase. In November 1996 Florida Water filed with the Florida First District Court of Appeals (Court of Appeals) an appeal of the final order seeking judicial review of issues relating to the amount of investment in utility facilities recoverable in rates from current customers. Other parties to the rate case also filed appeals. In June 1997, as part of the review process, the FPSC allowed Florida Water to resume collecting approximately $1 million, on an annual basis, in new customer connection fees. The Company is unable to predict the timing or outcome of the appeals process.

1991 RATE CASE REFUNDS. In 1995 the Court of Appeals reversed a 1993 FPSC order establishing uniform rates for most of Florida Water's service areas. With "uniform rates," all customers in a uniform rate area pay the same rates for water and wastewater services. In response to the Court of Appeals' order, in August 1996 the FPSC ordered Florida Water to issue refunds to those customers who paid more since October 1993 under uniform rates than they would have paid under stand-alone rates. This order did not permit a balancing surcharge to customers who paid less under uniform rates. Florida Water appealed, and the Court of Appeals ruled in June 1997 that the FPSC could not order refunds without balancing surcharges. In response to the Court of Appeals' ruling, the FPSC issued an order on Jan. 26, 1998, that would not require Florida Water to refund about $12.5 million, which included interest, to customers who paid more under uniform rates.

Also on Jan. 26, 1998, the FPSC ordered Florida Water to refund $2.5 million, the amount paid by customers in the Spring Hill service area from January 1996 through June 1997 under uniform rates which exceeded the amount these customers would have paid under a modified stand-alone rate structure. No balancing surcharge was permitted. The FPSC ordered this refund because Spring Hill customers continued to pay uniform rates after other customers began paying modified stand-alone rates effective January 1996 pursuant to the FPSC's interim rate order in Florida Water's 1995 Rate Case. The FPSC did not include Spring Hill in this interim rate order because Hernando County had assumed jurisdiction over Spring Hill's rates. In June 1997 Florida Water reached an agreement with Hernando County to revert to stand-alone rates for Spring Hill customers. The Company intends to appeal the $2.5 million refund. No provision for refund has been recorded.

COMPETITION. Water Services provide water and wastewater utility services at regulated rates within exclusive service territories granted by regulators.

1997 TO 1996 COMPARISON. Operating revenue and income from Water Services were $10.3 million higher in 1997 because of increased rates approved by the FPSC in 1996 for Florida Water customers and a $7.3 million pre-tax gain from the strategic sale of water and wastewater assets to Orange County, Florida, in December 1997. These assets served about 4,000 customers. Also in 1997, Heater acquired LaGrange, a water utility near Fayetteville, North Carolina, for $3.4 million. The acquisition added 5,300 water customers and contributed $0.9 million in revenue. The increase in revenue was partially offset by lower revenue following the sale of two water systems in South Carolina in 1996. Together the two strategic sales resulted in pre-tax gains of $1.7 million during 1996. Sales were up 3% in 1997, despite heavy rainfall and continued water conservation efforts by customers. Non-regulated water subsidiaries contributed $1.2 million more to revenue in 1997. Total operating expenses from Water Services were $5.7 million higher in 1997 primarily due to start-up costs associated with the Company's non-regulated water subsidiaries. Approximately $2 million of one-time charges relating to the amount of investment in utility facilities were also included in operating expenses in 1997. These higher operating expenses were tempered by improved operating efficiencies at Florida Water. Interest expense decreased $1.5 million in 1997 due to lower interest rates on refinanced debt.

1996 TO 1995 COMPARISON. Operating revenue and income from Water Services were $19.1 million higher in 1996. Rate relief and a 9% increase in sales in 1996 are primarily responsible for the increase. A 2% growth in customers and the return of more typical weather in Florida both contributed to higher sales in 1996. The increase in sales was tempered by continued customer conservation efforts. Florida Water added 17,000 new water and wastewater customers as a result of the December 1995 purchase of the assets of Orange Osceola Utilities in Florida. As part of a strategic decision to withdraw from South Carolina, Heater sold the majority of its assets in that state and recognized $1.7 million in pre-tax gains during 1996. Non-regulated water subsidiaries contributed $5.3 million to revenue in 1996. Total operating expenses from Water Services were $8.7 million higher in 1996 primarily due to the acquisition of Orange Osceola Utilities. The addition of non-regulated operations also increased operating expenses in 1996.

OUTLOOK. Florida Water and Heater continue to position themselves for further expansion by selectively acquiring and selling targeted water systems. The strategic emphasis at Heater is growth and consolidation in North Carolina. Water Services has been laying the groundwork for future growth in several new areas of the water business. Non-regulated subsidiaries have initiated marketing the Company's water expertise outside traditional utility boundaries.

AUTOMOTIVE SERVICES

Automotive Services include wholly owned subsidiaries: ADESA, a vehicle auction business; AFC, a finance company; and Great Rigs, an auto transport company.

ADESA is the third largest vehicle auction business in the U.S. Headquartered in Indianapolis, Indiana, ADESA owns and operates 25 vehicle auctions in the U.S. and Canada through which used cars and other vehicles are purchased and sold by franchised automobile dealers and licensed used car dealers. Sellers at ADESA's auctions include domestic and foreign auto manufacturers, car dealers, automotive fleet/lease companies, banks and finance companies. ADESA's Professional Auto Remarketing (PAR) division provides customized remarketing services to various businesses with fleet operations.

AFC provides inventory financing for wholesale and retail automobile dealers who purchase vehicles from

ADESA auctions, independent auctions and other auction chains. Headquartered in Indianapolis, Indiana, AFC has 57 loan production offices. From these offices car dealers obtain credit to purchase vehicles at any of the over 300 auctions approved by AFC.

Great Rigs, headquartered in Moody, Alabama, is one of the nation's largest independent used automobile transport companies. It offers customers pick up and delivery service through 11 strategically located transportation hubs. Customers of Great Rigs include ADESA auctions, car dealerships, vehicle manufacturers, leasing companies, finance companies and other auctions.

The Company acquired 80% of ADESA on July 1, 1995. On Jan. 31, 1996, the Company provided additional capital in exchange for 3% of ADESA. On Aug. 21, 1996, the Company acquired the remaining 17% ownership interest of ADESA from the ADESA management shareholders.

Automotive Services contributed net income of $14.0 million in 1997 ($3.7 million in 1996; $0.0 million for the six months of ownership in 1995). Financial performance for 1997 reflected increased vehicle sales and services, improved operating efficiencies at ADESA auctions and growth of the financing business.

[Graphic Material Omitted]

Number of Vehicles Sold
Thousands

	Minnesota Power	Predecessor
1995	230	240
96	637	
97	769	

COMPETITION. Within the automobile auction industry, ADESA's competition includes independently owned auctions as well as major chains and associations with auctions in geographic proximity. ADESA competes with other auctions for a supply of automobiles to be sold on consignment for automobile dealers, financial institutions and other sellers. ADESA also competes for a supply of rental repurchase vehicles from automobile manufacturers for auction at factory sales. The automobile manufacturers often choose between auctions across multi-state areas in distributing rental repurchase vehicles. ADESA competes for these sellers of automobiles by attempting to attract a large number of dealers to purchase vehicles, which ensures competitive prices and supports the volume of vehicles auctioned. ADESA also competes by providing a full range of services including reconditioning services which prepare vehicles for auction, transporting vehicles and the prompt processing of sale transactions. In 1997 ADESA agreed with another U.S. auction company to jointly sell Toyota Motor Credit Corporation (TMCC) vehicles through a common Internet "Cyberlot." The Cyberlot provides descriptions and photos of vehicles along with the price established by TMCC. This gives dealers the opportunity to buy vehicles through the Internet. Another factor affecting the industry, the impact of which is yet to be determined, is the entrance of the large used car dealerships called "superstores" that have emerged in densely populated markets.

AFC is well positioned as a provider of floorplan financing services to the used vehicle industry. AFC's competition includes other specialty lenders, as well as banks and other financial institutions. AFC competes with other floorplan providers and strives to distinguish itself based upon convenience and quality of service. A key component of AFC's program is conveniently located loan production offices with personnel available to assist automobile dealers with their financing needs. As part of AFC's continued effort to focus on providing other financing services to dealers, in 1997 AFC entered into an agreement with ACC Consumer Finance Corp. (ACC). Together these two companies will test a program designed to promote ACC's purchase of installment contracts that finance the purchase of vehicles floorplanned by AFC.

1997 TO 1996 COMPARISON. Operating revenue and income from Automotive Services were $71.6 million higher in 1997 primarily due to increased vehicle sales and ancillary services, such as reconditioning and transportation, at ADESA auction facilities. ADESA sold 769,000 vehicles in 1997 (637,000 in 1996).

Auction facilities added in 1996 contributed to higher vehicle sales in 1997. Operating revenue from AFC in 1997 reflected the growth of the floorplan financing business through expansion of existing loan production offices and the addition of 25 new office locations. The increase in AFC's dealer/customer base to 10,000 (4,000 in 1996) enabled AFC to finance 300,000 vehicles (140,000 in 1996). Pre-tax gains totaling $5.7 million from the sale of an auction facility and excess land were also included in 1997 operating revenue and income. Total operating expenses at Automotive Services were $50.9 million higher in 1997. Operating expenses associated with the auction facilities reflected the 21% increase in vehicles sold and increased ancillary services. These operating expenses were tempered by improved efficiencies and cost controls at auction facilities. The expansion of AFC's floorplan financing business and a more conservative allowance for bad debts also contributed to higher operating expenses in 1997.

1996 TO 1995 COMPARISON. Financial results for Automotive Services reflected a full year of operations in 1996, while 1995 only included operations as of July 1, 1995, the purchase date of ADESA. Operating revenue and income from Automotive Services were higher in 1996 because ADESA added eight new auction facilities during the year. ADESA sold 637,000 vehicles in 1996 compared to 230,000 vehicles during the last six months of 1995 (470,000 vehicles in total were sold by ADESA in 1995). Increased ancillary services and the expansion of AFC also contributed to revenue growth in 1996. Total operating expenses at Automotive Services were higher in 1996 due to the addition of eight auction facilities which caused ADESA to incur additional financing expenses and significant start-up costs. Start-up losses associated with two auction facilities had a negative impact on profitability of Automotive Services through 1996.

For the six months ended Dec. 31, 1995, operating revenue was $61.6 million with no net income contribution. Financial results in 1995 were adversely impacted by auction cancellations due to severe weather conditions on the east coast in December 1995, as well as start-up losses associated with major construction projects.

OUTLOOK. Auto auction sales for the industry are expected to rise at a rate of 6% to 8% annually. With the increased popularity of leasing and the high cost of new vehicles, the same vehicles may come to auction more than once. Automotive Services expects to participate in the industry's growth through selective acquisitions and expanded services. ADESA and AFC continue to focus on growth in the volume of vehicles sold and financed, increased ancillary services, and operating and technological efficiencies. The expansion of the Great Rigs fleet of automobile carriers to 150 by the end of second quarter 1998 is also expected to contribute to future growth.

INVESTMENTS

Investments include a securities portfolio, a 21% equity investment in a financial guaranty reinsurance and insurance company, and an 80% interest in a Florida real estate company.

Investments contributed net income of $32.1 million in 1997 ($38.1 million in 1996; $41.3 million in 1995). Financial performance for 1997 reflected a consistent return on the securities portfolio, an increase in earnings from Capital Re and an increase in real estate sales. Net income was lower in 1997 because tax benefits were recognized in 1996 and 1995 from real estate operations.

PORTFOLIO AND REINSURANCE. The Company's securities portfolio is managed by selected outside managers as well as internal managers. The securities portfolio is intended to provide stable earnings and liquidity, and is available for investment in existing businesses, acquisitions and other corporate purposes. The majority of the portfolio consists of stocks of other utility companies that have investment grade debt securities. Additionally, the Company sells common stock securities short and enters into short sales of treasury futures contracts as part of an overall investment portfolio hedge strategy.

The Company's investment in the securities portfolio at Dec. 31, 1997, was approximately $184 million ($155 million at Dec. 31, 1996).

Capital Re is a Delaware holding company engaged in reinsurance and insurance through its wholly owned subsidiaries. The market value of the Company's $119 million equity investment in Capital Re was $203 million at Dec. 31, 1997 ($152 million at Dec. 31, 1996).

1997 TO 1996 COMPARISON. Operating revenue and income from the securities portfolio were $1.4 million higher in 1997 because the Company's average portfolio balance was larger. Income tax expense was $5.7 million higher in 1997 because of increased operating income. In addition, 1996 reflected a one-time tax benefit for an IRS audit adjustment. Together, the Company's securities portfolio and its equity investment in Capital Re earned an annualized after-tax return of 8.6% in 1997 (8.8% in 1996). Income from equity investments included $14.8 million in 1997 ($11.8 million in 1996) of income from the Company's investment in Capital Re.

1996 TO 1995 COMPARISON. Operating revenue and income from the securities portfolio were $3.5 million lower in 1996 due to a smaller average portfolio balance. In 1995 the Company sold approximately $60 million of securities to finance the purchase of ADESA. Income tax expense reflected a one-time tax benefit for an IRS audit adjustment in 1996. Together, the Company's securities portfolio and its equity investment in Capital Re earned an annualized after-tax return of 8.8% in 1996 (9.2% in 1995). Income from equity investments included $11.8 million of income in 1996 ($9.8 million in 1995) from the Company's investment in Capital Re.

OUTLOOK. The Company's objective is to maintain corporate liquidity between 7% and 10% of total assets ($150 to $200 million). The Company plans to continue to concentrate in market-neutral investment strategies designed to provide stable and acceptable returns without sacrificing needed liquidity. The portfolio is hedged against market downturns and aimed at an after-tax return between 7% and 9%. While these returns may seem modest compared to broader market indices over the past three years, the Company believes its hedge strategy is a wise course in a volatile economic environment. Actual returns will be partially dependent on general market conditions. Capital Re will continue to be a core component of the Company's Investments segment.

[Graphic Material Omitted]

Investments
Millions

	Portfolio	Reinsurance	Real Estate
1995	$116.1	$92.9	$34.5
96	$153.4	$102.3	$64.7
97	$169.4	$118.8	$66.7

REAL ESTATE OPERATIONS. The Company owns 80% of Lehigh, a real estate company in Florida. Lehigh owns 2,500 acres of land and approximately 4,000 home sites near Fort Myers, Florida, 1,000 home sites in Citrus County, Florida, and 2,700 home sites and 12,000 acres of residential, commercial and industrial land at Palm Coast, Florida.

TAX BENEFITS. The Company, through Lehigh, acquired the stock of Lehigh Corporation in a bargain purchase in 1991. The carried-over tax bases of the underlying assets exceeded the book bases assigned in purchase accounting. The Internal Revenue Code (IRC) limits the use of tax losses resulting from the higher tax basis.

SFAS 109, "Accounting for Income Taxes," was adopted on a prospective basis effective Jan. 1, 1993. Upon adoption, a valuation reserve was established for the entire amount of the tax benefits attributable to the bases differences and alternative minimum tax credits because, in management's judgment, realization of the tax benefits was not "more likely than not." This judgment was based on the unlikelihood of realizing the tax benefits due to the IRC restrictions in light of management's existing five year property disposal plan.

In 1995 based on a detailed analysis of projected cash flow, Lehigh implemented a business strategy which called for Lehigh to dispose of its remaining real estate assets with a specific view towards maximizing realization of the tax benefits. Accordingly, in 1995 the valuation reserve was reduced by $18.4 million. In 1996 the remaining $8.2 million valuation reserve was reversed as a result of the projected positive impact the 1996 Palm Coast acquisition would have on Lehigh's taxable income.

1997 TO 1996 COMPARISON. Financial results for real estate operations reflected twelve months of Palm Coast operations in 1997 compared to less than nine months in 1996. Operating revenue and income from real estate operations were $9.6 million higher in 1997 primarily due to increased sales from Palm Coast operations. In 1996 operating revenue and income included $3.7 million from the sale of Lehigh's joint venture investment in a resort and golf course. Total operating expenses (excluding minority interest) from real estate operations were $5.7 million higher in 1997. The increase was attributed to more sales activity and additional expenses as a result of Palm Coast operations. Income tax expense in 1996 included the recognition of $8.2 million of tax benefits at Lehigh. The Company's portion of the tax benefits was $6.6 million in 1996.

1996 TO 1995 COMPARISON. Operating revenue and income from real estate operations were $9.7 million higher in 1996 due primarily to increased real estate sales from the Palm Coast operations and $3.7 million from the sale of Lehigh's joint venture in a resort and golf course. In 1996 Lehigh purchased properties at Palm Coast, Florida, and expanded its marketing program nationwide. Total operating expenses (excluding minority interest) from real estate operations were $1.7 million lower in 1996. The decrease was attributed to exiting several auxiliary businesses and cost containment efforts. Income tax expense included the recognition of $8.2 million of tax benefits in 1996 ($18.4 million in 1995). The Company's portion of the tax benefits was $6.6 million in 1996 ($14.7 million in 1995).

OUTLOOK. The real estate strategy is to continue to acquire large residential community properties at low cost, add value and sell them at current market prices.

LIQUIDITY AND CAPITAL RESOURCES

Cash flow from operations improved significantly during 1997 due to better management of working capital throughout the Company and capital expenditure discipline. Cash flow after funding capital expenditures was $117 million in 1997 ($35 million in 1996). Automotive Services experienced a major turnaround in cash flow generating $23 million in 1997 ($(34) million in 1996).

Working capital, if and when needed, generally is provided by the sale of commercial paper. In addition, securities investments can be liquidated to provide funds for reinvestment in existing businesses or acquisition of new businesses, and approximately 4 million original issue shares of common stock are available for issuance through the DRIP. Minnesota Power's $60 million bank lines of credit provide liquidity for the Company's commercial paper program. The amount and timing of future sales of the Company's securities will depend upon market conditions and the specific needs of the Company. The Company may from time to time sell securities to meet capital requirements, to provide for the retirement or early redemption of issues of long-term debt and preferred stock, to reduce short-term debt and for other corporate purposes.

A substantial amount of ADESA's working capital is generated internally from payments made by vehicle purchasers. However, ADESA uses commercial paper issued by the Company to meet short-term working capital requirements arising from the timing of payment obligations to vehicle sellers and the availability of funds from vehicle purchasers. During the sales process, ADESA does not typically take title to vehicles.

AFC also uses commercial paper issued by the Company to meet its operational requirements. AFC offers short-term on-site financing for dealers to purchase vehicles at auctions in exchange for a security interest in those vehicles. The financing is provided through the earlier of the date the dealer sells the vehicle or a general borrowing term of 30-60 days. As a result of AFC's continued expansion of the financing program for dealers, AFC has sold $124 million of receivables to a third party purchaser as of Dec. 31, 1997 ($50 million as of Dec. 31, 1996). Under the terms of a five-year agreement amended in August 1997, the purchaser agrees to purchase receivables aggregating $225 million, at any one time outstanding, to the extent that such purchases are supported by eligible receivables. Proceeds from the sale of the receivables were used to repay borrowings from the Company and fund vehicle inventory purchases for AFC's customers.

During 1997 the Company sold $60 million of First Mortgage Bonds, 7% Series due Feb. 15, 2007, and $20 million of First Mortgage Bonds, 6.68% Series due Nov. 15, 2007. The proceeds were used for the retirement of $60 million in principal amount of the Company's First Mortgage Bonds, 7 3/8% Series due March 1, 1997, and $18 million in principal amount First Mortgage Bonds, 6 1/2% Series redeemed in December. The remaining proceeds were used for general corporate purposes.

In June 1997 Minnesota Power refinanced $10 million of industrial development revenue bonds and $29 million of pollution control bonds with $39 million of Variable Rate Demand Revenue Refunding Bonds Series 1997A due June 1, 2020, Series 1997B and Series 1997C due June 1, 2013, and Series 1997D due Dec. 1, 2007.

In May 1997 MP Water Resources' $30 million 10.44% long-term note payable was replaced with $28 million of Florida Water's First Mortgage Bonds, 8.01% Series due May 30, 2017, and $7 million of Heater's First Mortgage Bonds, 7.05% due June 20, 2022. The remaining proceeds were used for general corporate purposes.

Minnesota Power's electric utility first mortgage bonds and secured pollution control bonds are currently rated investment grade Baa1 by Moody's Investor Services and A by Standard and Poor's. The Company's investment rating is currently Baa1 by Moody's Investor Services and BBB+ by Standard and Poor's. The disclosure of these securities ratings is not a recommendation to buy, sell or hold the Company's securities.

In 1997 the Company paid out 83% (89% in 1996; 94% in 1995) of its per-share earnings in dividends. Over the longer term, Minnesota Power's goal is to reduce dividend payout to 75%-80% of earnings.

[Graphic Material Omitted]

Capital Expenditures
Millions

	Actual	Projected
1995	$115	
96	$101	
97	$72	
98		$90
99		$89
2000		$76
1		$66
2		$70

CAPITAL REQUIREMENTS. Consolidated capital expenditures totaled $72 million in 1997 ($101 million in 1996; $115 million in 1995). Expenditures in 1997 included $35 million for Electric Operations, $22 million for Water Services, $11 million for Automotive Services and $4 million for corporate purposes. Internally generated funds were the primary source for funding capital expenditures.

Capital expenditures are expected to be $90 million in 1998 and total about $301 million for 1999 through 2002. The 1998 amount includes $45 million for electric system component replacement and upgrades, telecommunication fiber, and coal handling equipment, $24 million to meet environmental standards, expand water and wastewater treatment facilities to accommodate customer growth, and for water conservation initiatives and $21 million for on-going improvements at existing vehicle auction facilities and associated computer systems. The Company expects to use internally generated funds and original issue equity securities to fund these capital expenditures.

YEAR 2000. The Year 2000 issue relates to computer systems that recognize the year using the last two digits. Unless corrected, the year 2000 may be interpreted as 1900 causing errors or shutdowns in computer systems. In recent years the Company has replaced its major systems with systems considered to be Year 2000 compliant. A project team is coordinating a comprehensive review of all the Company's remaining software systems and micro-based systems for Year 2000 compliance. The review process includes key outside entities with which the Company interacts. The Company anticipates having all systems reviewed and an estimate of the Company's cost to meet Year 2000 compliance by mid-1998. A significant proportion of these costs are not likely to be incremental costs to the Company, but rather will represent the redeployment of existing information technology resources.

The Year 2000 issue may impact other entities with which the Company transacts business. The Company cannot estimate or predict the potential adverse consequences, if any, that could result from such entities' failure to address this issue.

SAFEHARBOR STATEMENT. In connection with the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 (Reform Act), the Company is hereby filing cautionary statements identifying important factors that could cause the Company's actual results to differ materially from those projected in forward-looking statements (as such term is defined in the Reform Act) made by or on behalf of the Company in this Annual Report, in presentations, in response to questions or otherwise. Any statements that express, or involve discussions as to expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, through the use of words or phrases such as "anticipates", "estimates", "expects", "intends", "plans", "predicts", "projects", "will likely result", "will continue", and similar expressions) are not statements of historical facts and may be forward-looking.

Forward-looking statements involve estimates, assumptions, and uncertainties and are qualified in their entirety by reference to, and are accompanied by, the following important factors, which are difficult to predict, contain uncertainties, are beyond the control of the Company and may cause actual results to differ materially from those contained in forward-looking statements: (i) prevailing governmental policies and regulatory actions, including those of the FERC, the MPUC, the FPSC, the NCUC, and the PSCW, with respect to allowed rates of return, industry and rate structure, acquisition and disposal of assets and facilities, operation, and construction of plant facilities, recovery of purchased power, and present or prospective wholesale and retail competition (including but not limited to retail wheeling and transmission costs); (ii) economic and geographic factors including political and economic risks; (iii) changes in and compliance with environmental and safety laws and policies; (iv) weather conditions; (v) population growth rates and demographic patterns; (vi) competition for retail and wholesale customers; (vii) pricing and transportation of commodities; (viii) market demand, including structural market changes; (ix) changes in tax rates or policies or in rates of inflation; (x) changes in project costs; (xi) unanticipated changes in operating expenses and capital expenditures; (xii) capital market conditions; (xiii) competition for new energy development opportunities; and (xiv) legal and administrative proceedings (whether civil or criminal) and settlements that influence the business and profitability of the Company.

Any forward-looking statement speaks only as of the date on which such statement is made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such 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 such factors, nor can it assess the impact of each such factor on the business or the extent to which any factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement.

INDEPENDENT ACCOUNTANTS

To the Shareholders and
Board of Directors of Minnesota Power

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of income, of retained earnings and of cash flows present fairly, in all material respects, the financial position of Minnesota Power and its subsidiaries at December 31, 1997 and 1996, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1997, in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

Price Waterhouse LLP

Price Waterhouse LLP

Minneapolis, Minnesota
January 26, 1998

MANAGEMENT

The consolidated financial statements and other financial information were prepared by management, which is responsible for their integrity and objectivity. The financial statements have been prepared in conformity with generally accepted accounting principles and necessarily include some amounts that are based on informed judgments and best estimates and assumptions of management.

To meet its responsibilities with respect to financial information, management maintains and enforces a system of internal accounting controls designed to provide assurance, on a cost effective basis, that transactions are carried out in accordance with management's authorizations and that assets are safeguarded against loss from unauthorized use or disposition. The system includes an organizational structure which provides an appropriate segregation of responsibilities, careful selection and training of personnel, written policies and procedures, and periodic reviews by the internal audit department. In addition, the Company has a personnel policy which requires all employees to maintain a high standard of ethical conduct. Management believes the system is effective and provides reasonable assurance that all transactions are properly recorded and have been executed in accordance with management's authorization. Management modifies and improves its system of internal accounting controls in response to changes in business conditions. The Company's internal audit staff is charged with the responsibility for determining compliance with Company procedures.

Four directors of the Company, not members of management, serve as the Audit Committee. The Board of Directors, through its Audit Committee, oversees management's responsibilities for financial reporting. The Audit Committee meets regularly with management, the internal auditors and the independent accountants to discuss auditing and financial matters and to assure that each is carrying out its responsibilities. The internal auditors and the independent accountants have full and free access to the Audit Committee without management present.

Price Waterhouse LLP, independent accountants, are engaged to express an opinion on the financial statements. Their audit is conducted in accordance with generally accepted auditing standards and includes a review of internal controls and tests of transactions to the extent necessary to allow them to report on the fairness of the operating results and financial condition of the Company.

Edwin L. Russell

Edwin L. Russell
Chairman, President and Chief Executive Officer

David G. Gartzke

David G. Gartzke
Chief Financial Officer

CONSOLIDATED FINANCIAL STATEMENTS

MINNESOTA POWER CONSOLIDATED BALANCE SHEET

December 31	1997	1996
	Millions	
Assets		
Plant and Investments		
Electric operations	$ 783.5	$ 796.0
Water services	322.2	323.9
Automotive services	167.1	167.3
Investments	252.9	236.5
Total plant and investments	1,525.7	1,523.7
Current Assets		
Cash and cash equivalents	41.8	40.1
Trading securities	123.5	86.8
Accounts receivable (less reserve of $12.6 and $6.6)	158.5	164.8
Fuel, material and supplies	25.0	23.2
Prepayments and other	19.9	17.2
Total current assets	368.7	332.1
Other Assets		
Goodwill	158.9	167.0
Deferred regulatory charges	64.4	83.5
Other	54.6	39.7
Total other assets	277.9	290.2
Total Assets	$2,172.3	$2,146.0
Capitalization and Liabilities		
Capitalization		
Common stock, without par value, 65.0 shares authorized; 33.6 and 32.8 shares outstanding	$ 416.0	$ 394.2
Unearned ESOP shares	(65.9)	(69.1)
Net unrealized gain on securities investments	5.5	2.7
Cumulative foreign translation adjustment	(0.8)	-
Retained earnings	296.1	283.0
Total common stock equity	650.9	610.8
Cumulative preferred stock	11.5	11.5
Redeemable serial preferred stock	20.0	20.0
Company obligated mandatorily redeemable preferred securities of subsidiary MP&L Capital I which holds solely Company Junior Subordinated Debentures	75.0	75.0
Long-term debt	685.4	694.4
Total capitalization	1,442.8	1,411.7
Current Liabilities		
Accounts payable	78.7	72.8
Accrued taxes, interest and dividends	67.3	63.7
Notes payable and long-term debt due within one year	133.8	162.9
Other	45.3	37.6
Total current liabilities	325.1	337.0
Other Liabilities		
Accumulated deferred income taxes	151.3	148.9
Contributions in aid of construction	102.6	98.4
Deferred regulatory credits	60.7	64.4
Other	89.8	85.6
Total other liabilities	404.4	397.3
Commitments and Contingencies		
Total Capitalization and Liabilities	$2,172.3	$2,146.0

The accompanying notes are an integral part of these statements.

MINNESOTA POWER CONSOLIDATED STATEMENT OF INCOME

For the Year Ended December 31	1997	1996	1995
		Millions except per share amounts	
Operating Revenue and Income			
Electric operations	$541.9	$529.2	$503.5
Water services	95.5	85.2	66.1
Automotive services	255.5	183.9	61.6
Investments	60.7	48.6	41.7
Total operating revenue and income	953.6	846.9	672.9
Operating Expenses			
Fuel and purchased power	194.1	190.9	177.0
Operations	579.9	512.2	389.1
Interest expense	64.2	62.1	48.0
Total operating expenses	838.2	765.2	614.1
Income from Equity Investments	14.8	11.8	4.2
Operating Income	130.2	93.5	63.0
Distributions on Redeemable Preferred Securities of Subsidiary	6.0	4.7	-
Income Tax Expense	46.6	19.6	1.1
Income from Continuing Operations	77.6	69.2	61.9
Income from Discontinued Operations	-	-	2.8
Net Income	77.6	69.2	64.7
Dividends on Preferred Stock	2.0	2.4	3.2
Earnings Available for Common Stock	$ 75.6	$ 66.8	$ 61.5
Average Shares of Common Stock	30.6	29.3	28.5
Basic and Diluted Earnings Per Share of Common Stock			
Continuing operations	$2.47	$2.28	$2.06
Discontinued operations	-	-	.10
Total	$2.47	$2.28	$2.16
Dividends Per Share of Common Stock	$2.04	$2.04	$2.04

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

For the Year Ended December 31	1997	1996	1995
		Millions	
Balance at Beginning of Year	$283.0	$276.2	$272.6
Net income	77.6	69.2	64.7
Redemption of preferred stock	-	(0.4)	-
Total	360.6	345.0	337.3
Dividends Declared			
Preferred stock	2.0	2.4	3.2
Common stock	62.5	59.6	57.9
Total	64.5	62.0	61.1
Balance at End of Year	$296.1	$283.0	$276.2

The accompanying notes are an integral part of these statements.

MINNESOTA POWER CONSOLIDATED STATEMENT OF CASH FLOWS

For the Year Ended December 31	1997	1996	1995
		Millions	
Operating Activities			
Net income	$ 77.6	$ 69.2	$ 64.7
Income from equity investments -- net of dividends received	(13.9)	(11.0)	(10.7)
Depreciation and amortization	70.8	65.1	59.5
Deferred income taxes	2.0	(11.8)	(26.9)
Pre-tax (gain) loss on sale of plant	(14.0)	(1.6)	1.8
Changes in operating assets and liabilities net of the effects of discontinued operations and subsidiary acquisitions			
Trading securities	(36.7)	(46.8)	34.0
Notes and accounts receivable	7.9	(17.5)	(13.0)
Fuel, material and supplies	(1.8)	3.2	(3.2)
Accounts payable	5.4	(2.8)	(9.8)
Other current assets and liabilities	8.8	14.8	15.9
Other -- net	11.2	16.2	0.9
Cash from operating activities	117.3	77.0	113.2
Investing Activities			
Proceeds from sale of investments in securities	47.7	43.1	103.2
Proceeds from sale of discontinued operations -- net of cash sold	-	-	107.6
Proceeds from sale of plant	19.4	8.8	-
Additions to investments	(42.5)	(76.7)	(50.3)
Additions to plant	(53.3)	(94.1)	(117.7)
Acquisition of subsidiaries -- net of cash acquired	(2.4)	(66.9)	(129.6)
Changes to other assets -- net	(1.4)	(0.9)	(1.0)
Cash for investing activities	(32.5)	(186.7)	(87.8)
Financing Activities			
Issuance of long-term debt	176.7	205.5	28.1
Issuance of preferred securities of subsidiary	-	72.3	-
Issuance of common stock	19.7	19.0	6.4
Changes in notes payable -- net	(27.2)	56.3	16.7
Reductions of long-term debt	(187.8)	(155.3)	(10.9)
Redemption of preferred stock	-	(17.6)	-
Dividends on preferred and common stock	(64.5)	(62.0)	(61.1)
Cash from (for) financing activities	(83.1)	118.2	(20.8)
Change in Cash and Cash Equivalents	1.7	8.5	4.6
Cash and Cash Equivalents at Beginning of Period	40.1	31.6	27.0
Cash and Cash Equivalents at End of Period	$ 41.8	$ 40.1	$ 31.6
Supplemental Cash Flow Information			
Cash paid during the period for			
Interest (net of capitalized)	$ 66.2	$ 54.4	$ 48.9
Income taxes	$ 31.3	$ 25.5	$ 25.0

The accompanying notes are an integral part of these statements.

1

BUSINESS SEGMENTS
Millions

For the Year Ended December 31	Consolidated	Electric Operations	Water Services	Automotive Services	Investments: Portfolio & Reinsurance	Investments: Real Estate	Corporate Charges
1997							
Operating revenue and income	$ 953.6	$541.9	$ 95.5	$255.5	$ 22.1	$38.8	$ (0.2)
Operation and other expense	703.2	403.7	60.6	203.2	2.1	21.9	11.7
Depreciation and amortization expense	70.8	45.2	11.2	14.0	-	0.1	0.3
Interest expense	64.2	21.3	11.0	9.9	-	0.8	21.2
Income from equity investments	14.8	-	-	-	14.8	-	-
Operating income (loss)	130.2	71.7	12.7	28.4	34.8	16.0	(33.4)
Distributions on redeemable preferred securities of subsidiary	6.0	1.6	-	-	-	-	4.4
Income tax expense (benefit)	46.6	27.0	4.5	14.4	12.1	6.6	(18.0)
Net income (loss)	$ 77.6	$ 43.1	$ 8.2	$ 14.0	$ 22.7	$ 9.4	$(19.8)
Total assets	$2,172.3	$973.9	$384.7	$458.1	$288.2	$66.7	$ 0.7
Accumulated depreciation	$ 697.5	$562.1	$122.9	$ 12.5	-	-	-
Accumulated amortization	$ 15.7	-	-	$ 14.4	-	$ 1.3	-
Construction work in progress	$ 26.2	$ 11.2	$ 9.6	$ 5.4	-	-	-
1996							
Operating revenue and income	$ 846.9	$529.2	$ 85.2	$183.9	$ 20.7	$29.2	$ (1.3)
Operation and other expense	638.0	400.9	53.6	152.8	2.7	17.1	10.9
Depreciation and amortization expense	65.1	42.2	11.0	11.7	-	0.2	-
Interest expense	62.1	22.5	12.5	11.7	-	1.2	14.2
Income from equity investments	11.8	-	-	-	11.8	-	-
Operating income (loss)	93.5	63.6	8.1	7.7	29.8	10.7	(26.4)
Distributions on redeemable preferred securities of subsidiary	4.7	1.3	-	-	-	-	3.4
Income tax expense (benefit)	19.6	22.9	2.7	4.0	6.4	(4.0)	(12.4)
Net income (loss)	$ 69.2	$ 39.4	$ 5.4	$ 3.7	$ 23.4	$14.7	$(17.4)
Total assets	$2,146.0	$995.8	$371.2	$456.8	$255.7	$64.7	$ 1.8
Accumulated depreciation	$ 653.8	$533.5	$113.8	$ 6.5	-	-	-
Accumulated amortization	$ 8.6	-	-	$ 7.6	-	$ 1.0	-
Construction work in progress	$ 22.7	$ 4.0	$ 7.1	$ 11.6	-	-	-
1995							
Operating revenue and income	$ 672.9	$503.5	$ 66.1	$ 61.6	$ 24.2	$19.5	$ (2.0)
Operation and other expense	508.8	373.7	46.0	55.3	3.2	20.3	10.3
Depreciation and amortization expense	57.3	40.3	12.3	4.4	-	0.3	-
Interest expense	48.0	22.4	10.1	0.7	-	-	14.8
Income (loss) from equity investments	4.2	-	-	-	9.8	-	(5.6)
Operating income (loss)	63.0	67.1	(2.3)	1.2	30.8	(1.1)	(32.7)
Income tax expense (benefit)	1.1	26.1	(1.3)	1.2	5.8	(17.4)	(13.3)
Income (loss) from continuing operations	61.9	$ 41.0	$ (1.0)	$ -	$ 25.0	$16.3	$(19.4)
Income from discontinued operations	2.8						
Net income	$ 64.7						
Total assets	$1,947.6	$992.6	$355.2	$355.8	$209.0	$34.5	$ 0.5
Accumulated depreciation	$ 619.3	$508.5	$108.8	$ 2.0	-	-	-
Accumulated amortization	$ 3.0	-	-	$ 2.3	-	$ 0.7	-
Construction work in progress	$ 56.0	$ 5.7	$ 12.0	$ 38.3	-	-	-

Purchased July 1, 1995.
Includes $2.3 million of minority interest in 1997 ($3.7 million in 1996; $4.1 million in 1995).
Includes $8.2 million of tax benefits in 1996 ($18.4million in 1995). See Note 15.
Includes a $6.4 million pre-tax provision from exiting the equipment manufacturing business.

OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

FINANCIAL STATEMENT PREPARATION. Minnesota Power prepares its financial statements in conformity with generally accepted accounting principles. These principles require management to make informed judgments and best estimates and assumptions that (1) affect the reported amounts of assets and liabilities, (2) disclose contingent assets and liabilities at the date of the financial statements, and (3) report amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Abbreviations and acronyms are defined on page 50.

PRINCIPLES OF CONSOLIDATION. The consolidated financial statements include the accounts of the Company and all of its majority owned subsidiary companies. All material intercompany balances and transactions have been eliminated in consolidation. Information for prior periods has been reclassified to present comparable information for all periods.

NATURE OF OPERATIONS AND REVENUE RECOGNITION. Minnesota Power is a broadly diversified service company that has operations in four principal business segments. Corporate charges consist of expenses incurred by the Company's corporate headquarters and interest and preferred stock expense not specifically identifiable to a business segment. Management's policy is to not allocate these expenses to business segments.

ELECTRIC OPERATIONS. Electric Operations generate, transmit, distribute and market electricity. Electric service is provided to 136,000 customers in northeastern Minnesota and northwestern Wisconsin. Large power customers, which include five taconite producers, four paper and pulp mills and two pipeline companies, purchase under contracts, which extend from October 1999 through July 2008, about half of the electricity the Company sells. BNI Coal, a wholly owned subsidiary, mines and sells lignite coal to two North Dakota mine-mouth generating units, one of which is Square Butte. Square Butte supplies Minnesota Power with 71% of its output under a long-term contract. (See Note 5.)

Electric rates are under the jurisdiction of various state and federal regulatory authorities. Billings are rendered on a cycle basis. Revenue is accrued for service provided but not billed. Electric rates include adjustment clauses which bill or credit customers for fuel and purchased energy costs above or below the base levels in rate schedules and bill retail customers for the recovery of CIP expenditures not collected in base rates.

During 1997 revenue derived from one major customer was $56.5 million ($57.1 million in 1996; $60.4 million in 1995). Revenue derived from another major customer was $42.7 million in 1997 ($41.2 million in 1996; $44.9 million in 1995).

WATER SERVICES. Water Services include several wholly owned subsidiaries of the Company. Florida Water is the largest investor owned supplier of water and wastewater utility services in Florida. Heater provides water and wastewater services primarily in North Carolina. In total, 147,000 water and 54,000 wastewater treatment customers are served. Water and wastewater rates are under the jurisdiction of various state and county regulatory authorities. Bills are rendered on a cycle basis. Revenue is accrued for services provided but not billed. Instrumentation Services, Inc. and U.S. Maintenance and Management provide predictive maintenance services to water utility companies and other industrial operations in several southern states. Americas' Water offers contract management, operations and maintenance services to governments and industries throughout the Americas.

AUTOMOTIVE SERVICES. Automotive Services include wholly owned subsidiaries: ADESA, a vehicle auction business; AFC, a finance company; and Great Rigs, an auto transport company. ADESA is the third largest vehicle auction business in the U.S. ADESA owns and operates 25 vehicle auctions in the U.S. and Canada through which used cars and other vehicles are purchased and sold by franchised automobile dealers and licensed used car dealers. Sellers at ADESA's auctions include domestic and foreign auto manufacturers, car dealers, automotive fleet/lease companies, banks and finance companies. AFC provides inventory financing for wholesale and retail automobile dealers who purchase vehicles from ADESA auctions, independent auctions and other auction chains. AFC has 57 loan production offices. From these offices car dealers obtain credit to purchase vehicles at any of the over 300 auctions approved by AFC. Great Rigs is one of the nation's largest independent used automobile transport companies. It offers customers pick up and delivery service through 11 strategically located transportation hubs. Revenue is recognized when services are performed.

INVESTMENTS. The Company's securities portfolio is intended to provide stable earnings and liquidity, and is available for reinvestment in existing businesses, acquisitions and other corporate purposes. The Company has a 21% ownership in Capital Re, a financial guaranty reinsurance and insurance company, accounted for using the equity method. The Company also has an 80% ownership in Lehigh, a Florida real estate business. Real estate revenue is recognized on the accrual basis.

PLANT DEPRECIATION. Plant is recorded at original cost, and is reported on the balance sheet net of accumulated depreciation. Expenditures for additions and significant replacements and improvements are capitalized; maintenance and repair costs are expensed as incurred. When utility plant is retired or otherwise disposed of, the cost less net proceeds is normally charged to accumulated depreciation and no gain or loss is recognized. Contributions in aid of construction relate to water utility assets, and are amortized over the estimated life of the associated asset. This amortization reduces depreciation expense.

Depreciation is computed using the estimated useful lives of the various classes of plant. In 1997 average depreciation rates for the electric, water and automotive segments were 3.4%, 2.7% and 4.1%, respectively (3.2%, 2.6% and 3.5%, respectively in 1996; 3.1%, 2.9% and 4.7%, respectively in 1995).

FUEL, MATERIAL AND SUPPLIES. Fuel, material and supplies are stated at the lower of cost or market. Cost is determined by the average cost method.

GOODWILL. Goodwill represents the excess of cost over net assets of businesses acquired and is amortized on a straight-line basis over a 40 year period.

DEFERRED REGULATORY CHARGES AND CREDITS. The Company's utility operations are subject to the provisions of SFAS 71, "Accounting for the Effects of Certain Types of Regulation." The Company capitalizes as deferred regulatory charges incurred costs which are probable of recovery in future utility rates. Deferred regulatory credits represent amounts expected to be credited to customers in rates. (See Note 4.)

UNAMORTIZED EXPENSE, DISCOUNT AND PREMIUM ON DEBT. Expense, discount and premium on debt are deferred and amortized over the lives of the related issues.

CASH AND CASH EQUIVALENTS. The Company considers all investments purchased with maturities of three months or less to be cash equivalents.

FOREIGN CURRENCY TRANSLATION. Results of operations for Automotive Services' Canadian subsidiaries are translated into U.S. dollars using the average exchange rates during the period. Assets and liabilities are translated into U.S. dollars using the exchange rate on the balance sheet date, except for intangibles and fixed assets, which are translated at historical rates.

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ACQUISITIONS AND DIVESTITURES

SALE OF WATER PLANT ASSETS. On Dec. 30, 1997, Florida Water sold water and wastewater assets to Orange County in Florida for $13.1 million. The facilities served about 4,000 customers. The transaction resulted in a $4.7 million after-tax gain which is included in the Company's 1997 earnings.

In March 1996 Heater of Seabrook, Inc., a wholly owned subsidiary of Heater, sold all of its water and wastewater utility assets to the Town of Seabrook Island, South Carolina for $5.9 million. This sale was negotiated in anticipation of an eminent domain action by the Town of Seabrook Island, South Carolina. In December 1996 Heater sold its Columbia, South Carolina area water systems to South Carolina Water and Sewer, L.L.C. The Seabrook and Columbia systems served a total of 6,500 customers. The transactions resulted in a $1 million after-tax gain which was included in the Company's 1996 earnings.

ACQUISITION OF LAGRANGE. In 1997 the NCUC approved the transfer of LaGrange Waterworks Corporation, a water utility near Fayetteville, North Carolina, to Heater. The Company exchanged 96,000 shares of common stock, with a market value of approximately $3.4 million, for the outstanding shares of LaGrange and accounted for the transaction as a pooling of interest. The acquisition added 5,300 water customers. Financial results prior to the acquisition were not restated due to immateriality.

ACQUISITION OF PALM COAST. In April 1996 Palm Coast Holdings, Inc., a wholly owned subsidiary of Lehigh Acquisition Corporation, acquired real estate assets (Palm Coast) from ITT Community Development Corp. and other affiliates of ITT Industries, Inc. (ITT) for $34 million. These assets included developed residential lots, a real estate contract receivables portfolio and approximately 13,000 acres of commercial and other land. Palm Coast is a planned community located between St. Augustine and Daytona Beach, Florida.

ITT's wholly owned subsidiary, Palm Coast Utility Corporation (PCUC), has granted an option to the Company to acquire PCUC's water and wastewater utility assets in Palm Coast. PCUC provides services to approximately 12,000 customers in Flagler County, Florida. The option expires during 1998. If the option is exercised, closing of the transaction will be subject to various regulatory approvals.

ACQUISITION OF ISI. In April 1996 MP Water Resources acquired all the outstanding common stock of Instrumentation Services, Inc., a predictive maintenance service business, in exchange for 96,526 shares of Minnesota Power common stock. The acquisition was accounted for as a pooling of interest. Financial results prior to the acquisition were not restated due to immateriality.

ACQUISITION OF ORANGE OSCEOLA. In December 1995 Florida Water acquired the operating assets of Orange Osceola Utilities for approximately $13 million. The acquisition added over 17,000 water customers.

ACQUISITION OF ADESA. The Company acquired 80% of ADESA on July 1, 1995, increased its ownership interest to 83% in January 1996 and acquired the remaining 17% interest in August 1996. The total purchase price was $227 million. The step acquisitions were accounted for by the purchase method. Accordingly, ADESA earnings have been included in the Company's consolidated financial statements based on the ownership interest as of the date of each acquisition. Acquired goodwill and other intangible assets are being amortized using the straight line method. Pro forma disclosures for the acquisition are not presented as the impact on consolidated 1996 and 1995 operating results is immaterial.

In September 1996 Minnesota Power exchanged 473,006 shares of its common stock for all the outstanding common stock of Alamo Auto Auction, Inc. and Alamo Auto Auction Houston, Inc. These acquisitions were accounted for as pooling of interests. Financial results prior to the acquisitions were not restated due to immateriality.

DISCONTINUED OPERATIONS. On June 30, 1995, Minnesota Power sold its interest in the paper and pulp business to Consolidated Papers, Inc. (CPI) for $118 million in cash, plus CPI's assumption of certain debt and lease obligations. The financial results of the paper and pulp business, including the loss on disposition, were accounted for as discontinued operations.

Discontinued Operations Year Ended December 31	1995
	Millions
Operating revenue and income	$44.3
Income from equity investments	$7.5
Income from operations	$7.5
Income tax expense	3.2
	4.3
Loss on disposal	(1.8)
Income tax benefit	0.3
	(1.5)
Income from discontinued operations	$2.8

EXIT FROM EQUIPMENT MANUFACTURING BUSINESS. In June 1995 Reach All Partnership ceased operations and sold its operating assets. The pre-tax loss from Reach All Partnership was $6.4 million in 1995.

REGULATORY MATTERS

The Company files for periodic rate revisions with the Minnesota Public Utilities Commission (MPUC), the Federal Energy Regulatory Commission (FERC), the Florida Public Service Commission (FPSC) and other state and county regulatory authorities. The MPUC had regulatory authority over approximately 68% in 1997 (69% in 1996; 73% in 1995) of the Company's total electric operating revenue. Interim rates in Minnesota and Florida are placed into effect, subject to refund with interest, pending a final decision by the appropriate commission.

WATER AND WASTEWATER RATES. 1995 RATE CASE. Florida Water requested an $18.1 million rate increase in June 1995 for all water and wastewater customers of Florida Water regulated by the FPSC. In October 1996 the FPSC issued its final order approving an $11.1 million annual increase. In November 1996 Florida Water filed with the Florida First District Court of Appeals (Court of Appeals) an appeal of the final order seeking judicial review of issues relating to the amount of investment in utility facilities recoverable in rates from current customers. Other parties to the rate case also filed appeals. In June 1997, as part of the review process, the FPSC allowed Florida Water to resume collecting approximately $1 million, on an annual basis, in new customer connection fees. The Company is unable to predict the timing or outcome of the appeals process.

1991 RATE CASE REFUNDS. In 1995 the Court of Appeals reversed a 1993 FPSC order establishing uniform rates for most of Florida Water's service areas. With "uniform rates," all customers in a uniform rate area pay the same rates for water and wastewater services. In response to the Court of Appeals' order, in August 1996 the FPSC ordered Florida Water to issue refunds to those customers who paid more since October 1993 under uniform rates than they would have paid under stand-alone rates. This order did not permit a balancing surcharge to customers who paid less under uniform rates. Florida Water appealed, and the Court of Appeals ruled in June 1997 that the FPSC could not order refunds without balancing surcharges. In response to the Court of Appeals' ruling, the FPSC issued an order on Jan. 26, 1998, that would not require Florida Water to refund about $12.5 million, which included interest, to customers who paid more under uniform rates.

Also on Jan. 26, 1998, the FPSC ordered Florida Water to refund $2.5 million, the amount paid by customers in the Spring Hill service area from January 1996 through June 1997 under uniform rates which exceeded the amount these customers would have paid under a modified stand-alone rate structure. No balancing surcharge was permitted. The FPSC ordered this refund because Spring Hill customers continued to pay uniform rates after other customers began paying modified stand-alone rates effective January 1996 pursuant to the FPSC's interim rate order in Florida Water's 1995 Rate Case. The FPSC did not include Spring Hill in this interim rate order because Hernando County had assumed jurisdiction over Spring Hill's rates. In June 1997 Florida Water reached an agreement with Hernando County to revert to stand-alone rates for Spring Hill customers. The Company intends to appeal the $2.5 million refund. No provision for refund has been recorded.

DEFERRED REGULATORY CHARGES AND CREDITS. Based on current rate treatment, the Company believes all deferred regulatory charges are probable of recovery.

Deferred Regulatory Charges and Credits December 31	1997	1996
	Millions	
Deferred charges		
Income taxes	$21.5	$22.1
Conservation improvement programs	17.7	21.3
Early retirement plan	2.8	8.2
Postretirement benefits	5.4	8.1
Premium on reacquired debt	6.9	7.5
Other	10.1	16.3
	64.4	83.5
Deferred credits		
Income taxes	60.7	64.4
Net deferred regulatory charges	$ 3.7	$19.1

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SQUARE BUTTE PURCHASED POWER CONTRACT

Under the terms of a 30-year contract with Square Butte that extends through 2007, the Company is purchasing 71% of the output from a mine-mouth, lignite-fired generating plant capable of generating up to 455 MW. This generating unit (Project) is located near Center, North Dakota. Reductions to about 49% of the output are provided for in the contract and, at the option of Square Butte, could begin after a five-year advance notice to the Company and continue for the remaining economic life of the Project. The Company has the option but not the obligation to continue to purchase 49% of the output after 2007.

The Project is leased to Square Butte through Dec. 31, 2007, by certain banks and their affiliates which have beneficial ownership in the Project. Square Butte has options to renew the lease after 2007 for essentially the entire remaining economic life of the Project.

The Company is obligated to pay Square Butte all Square Butte's leasing, operating and debt service costs (less any amounts collected from the sale of power or energy to others) that shall not have been paid by Square Butte when due. These costs include the price of lignite coal purchased by Square Butte under a cost-plus contract with BNI Coal. The Company's cost of power and energy purchased from Square Butte during 1997 was $56.9 million ($58.2 million in 1996; $57.6 million in 1995). The leasing costs of Square Butte included in the cost of power delivered to the Company totaled $17.1 million in 1997 ($17.7 million in 1996; $19.3 million in 1995), which included approximately $9 million ($10.2 million in 1996; $11 million in 1995) of interest expense. The annual fixed lease obligations of the Company for Square Butte are $17.2 million from 1998 through 2002. At Dec. 31, 1997, Square Butte had total debt outstanding of $250 million. The Company's obligation is absolute and unconditional whether or not any power is actually delivered to the Company.

The Company's payments to Square Butte for power and energy are approved as purchased power expense for ratemaking purposes by both the MPUC and FERC.

One principal reason the Company entered into the agreement with Square Butte was to obtain a power supply for large industrial customers. Present electric service contracts with these customers require payment of minimum monthly demand charges that cover a portion of the fixed costs associated with having capacity available to serve them. These contracts minimize the negative impact on earnings that could result from significant reductions in kilowatthour sales to industrial customers. The initial minimum contract term for the large power customers is 10 years, with a four-year cancellation notice required for termination of the contract at or beyond the end of the tenth year. Under the terms of existing contracts as of Feb. 1, 1998, the Company would collect approximately $92.1 million under current rate levels for firm power during 1998 ($78.3 million in 1999; $69.2 million in 2000; $66.5 million in 2001; and $47.3 million in 2002), even if no power or energy were supplied to these customers after Dec. 31, 1997. The minimum contract provisions are expressed in megawatts of demand, and if rates change, the amounts the Company would collect under the contracts will change in proportion to the change in the demand rate.

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JOINTLY OWNED ELECTRIC FACILITY

The Company owns 80% of Boswell Energy Center Unit 4 (Boswell Unit 4). While the Company operates the plant, certain decisions with respect to the operations of Boswell Unit 4 are subject to the oversight of a committee on which the Company and Wisconsin Public Power, Inc. SYSTEM (WPPI), the owner of the other 20% of Boswell Unit 4, have equal representation and voting rights. Each owner must provide its own financing and is obligated to pay its ownership share of operating costs. The Company's share of direct operating expenses of Boswell Unit 4 is included in operating expense on the consolidated statement of income. The Company's 80% share of the original cost included in electric plant at Dec. 31, 1997 was $305 million ($304 million at Dec. 31, 1996). The corresponding provision for accumulated depreciation was $136 million ($129 million at Dec. 31, 1996).

FINANCIAL INSTRUMENTS

SECURITIES INVESTMENTS. Securities investments, managed internally and also by external fund managers, consist primarily of equity securities of other utilities with investment grade debt ratings. Investments held principally for near-term sale are classified as trading securities and included in current assets at fair value. Changes in the fair value of trading securities are recognized currently in earnings. Investments held for an indefinite period of time are classified as available-for-sale securities and included in plant and investments at fair value. Unrealized gains and losses on available-for-sale securities are included in common stock equity, net of tax. Unrealized losses on available-for-sale securities that are other than temporary are recognized in earnings. Realized gains and losses are computed on each specific investment sold.

Available-For-Sale Securities

	Cost	Gross Unrealized Gain	Gross Unrealized (Loss)	Fair Value
		Millions		
Equity securities				
Dec. 31, 1997	$60.5	$4.3	$(3.5)	$61.3
Dec. 31, 1996	$68.0	$1.9	$(2.1)	$67.8

Year Ended December 31	1997	1996	1995
		Millions	
Proceeds from sales	$47.7	$43.1	$97.1
Gross realized gains	$0.7	$0.9	$3.0
Gross realized (losses)	$(1.4)	$(1.4)	$(3.3)
Net unrealized holding gains in common stock equity	$0.2	$1.0	$0.9

At Dec. 31, 1997, the net unrealized gain on securities investments recorded in common stock equity also included $5 million ($2.8 million at Dec. 31, 1996) reflecting the Company's share of Capital Re's net unrealized holding gains. The net unrealized holding gains included in earnings for trading securities in 1997 were $2 million ($0.9 million in 1996; $1.5 million in 1995).

FAIR VALUE OF FINANCIAL INSTRUMENTS. With the exception of the items listed below, the estimated fair values of all financial instruments approximate the carrying amount. The fair values for the items below were based on quoted market prices for the same or similar instruments.

Financial Instruments

December 31	1997		1996	
		Millions		
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt	$685.4	$707.4	$694.4	$690.7
Redeemable serial preferred stock	$20.0	$21.5	$20.0	$21.2
Quarterly income preferred securities	$75.0	$76.9	$75.0	$73.9

CONCENTRATION OF CREDIT RISK. Financial instruments that subject the Company to concentrations of credit risk consist primarily of accounts receivable. The Company sells electricity to about 15 customers in northern Minnesota's taconite, pipeline, paper and wood products industries. At Dec. 31, 1997, receivables from these customers totaled approximately $9 million ($8 million in 1996). The Company does not obtain collateral to support utility receivables, but monitors the credit standing of major customers. The Company has not incurred and does not expect to incur significant credit losses.

SALE OF FINANCE RECEIVABLES. In 1997 AFC amended an agreement to allow sales up to $225 million, previously $100 million, of finance receivables to a third party. Pursuant to this agreement, AFC has sold $124 million of receivables as of Dec. 31, 1997 ($50 million as of Dec. 31, 1996). The agreement expires at the end of 2001.

OFF-BALANCE-SHEET FINANCIAL INSTRUMENTS AND RISKS. In portfolio strategies designed to reduce market risks, the Company sells common stock securities short and enters into short sales of treasury futures contracts. Selling common stock securities short is intended to reduce market price risks associated with holding common stock securities in the Company's trading securities portfolio. Realized and unrealized gains and losses from short sales of common stock securities are included in investment income. Treasury futures are used as a hedge to reduce interest rate risks associated with holding fixed dividend preferred stocks included in the Company's available-for-sale portfolio. Changes in market values of treasury futures are recognized as an adjustment to the carrying amount of the underlying hedged item. Gains and losses on treasury futures are deferred and recognized in investment income concurrently with gains and losses arising from the under-

lying hedged item. Generally, treasury futures contracts entered into have a maturity date of 90 days.

In 1997 Florida Water restructured an interest rate swap agreement to take advantage of more favorable terms. Under the new five-year agreement, Florida Water will make quarterly payments at a variable rate based upon an average of various foreign LIBOR rates (3.7% at Dec. 31, 1997), and receive payments based on a fixed rate of 4.8%. This agreement is subject to market risk due to interest rate fluctuation.

The notional amounts summarized below do not represent amounts exchanged and are not a measure of the Company's financial exposure. The amounts exchanged are calculated on the basis of these notional amounts and other terms which relate to the change in interest rates or securities prices. The Company continually evaluates the credit standing of counterparties and market conditions, and does not expect any material adverse impact to its financial position from these financial instruments.

Off-Balance-Sheet Financial Instruments December 31	1997		1996	
Millions				
	Notional Amount	Fair Value Benefit (Obligation)	Notional Amount	Fair Value Benefit (Obligation)
Short stock sales outstanding	$54.0	$(2.7)	$31.7	$ 0.0
Treasury futures	$22.8	$(0.4)	$20.8	$(0.1)
Interest rate swap	$30.0	$(0.2)	$30.0	$0.1

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SHORT-TERM BORROWINGS AND COMPENSATING BALANCES

The Company has bank lines of credit, which make short-term financing available through short-term bank loans and provide support for commercial paper. At Dec. 31, 1997 and 1996, the Company had bank lines of credit aggregating $84 million. At the end of 1997 and 1996, $84 million was available for use. At Dec. 31, 1997, the Company had issued commercial paper with a face value of $130 million ($155 million in 1996), with liquidity provided by bank lines of credit and the Company's securities portfolio.

Certain lines of credit require a commitment fee of 1/10 of 1% and/or a 5% compensating balance. Interest rates on commercial paper and borrowings under the lines of credit ranged from 6.1% to 8.5% at Dec. 31, 1997 (5.6% to 8.3% at Dec. 31, 1996). The weighted average interest rate on short-term borrowings at Dec. 31, 1997, was 6.3% (5.7% at Dec. 31, 1996). The total amount of compensating balances at Dec. 31, 1997 and 1996, was immaterial.

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INVESTMENT IN CAPITAL RE

The Company has a 21% equity investment in Capital Re, a company engaged in financial guaranty reinsurance and insurance. The Company uses the equity method to account for this investment.

Capital Re Financial Information Year Ended December 31	1997	1996	1995
Millions			
Capital Re			
Investment portfolio	$1,011.1	$901.1	$771.8
Other assets	$376.9	$255.3	$210.1
Liabilities	$341.9	$255.0	$180.5
Deferred revenue	$402.1	$337.1	$314.5
Net revenue	$201.7	$144.9	$107.0
Net income	$70.1	$56.5	$45.5
Minnesota Power's Interest			
Equity in earnings	$14.8	$11.8	$9.8
Accumulated equity in undistributed earnings	$67.5	$53.7	$42.8
Equity investment	$118.8	$102.3	$92.9
Fair value of investment	$202.6	$152.3	$100.4
Equity ownership	21%	21%	22%

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COMMON STOCK AND RETAINED EARNINGS

The Articles of Incorporation, mortgage, and preferred stock purchase agreements contain provisions that, under certain circumstances, would restrict the payment of common stock dividends. As of Dec. 31, 1997, no retained earnings were restricted as a result of these provisions.

Summary of Common Stock	Shares	Equity
	Millions	
Balance Dec. 31, 1994	31.3	$371.2
1995 ESPP	-	0.8
DRIP	0.2	5.7
Balance Dec. 31, 1995	31.5	377.7
1996 ESPP	-	0.7
DRIP	0.7	18.5
Other	0.6	(2.7)
Balance Dec. 31, 1996	32.8	394.2
1997 ESPP	-	0.9
DRIP	0.6	18.6
Other	0.2	2.3
Balance Dec. 31, 1997	33.6	$416.0

SHAREHOLDER RIGHTS PLAN. On July 24, 1996, the Board of Directors of the Company adopted a rights plan (Rights Plan) pursuant to which it declared a dividend distribution of one preferred share purchase right (Right) for each outstanding share of common stock to shareholders of record at the close of business on July 24, 1996, (the Record Date) and authorized the issuance of one Right with respect to each share of common stock that becomes outstanding between the Record Date and July 23, 2006, or such earlier time as the Rights are redeemed.

Each Right will be exercisable to purchase one one-hundredth of a share of Junior Serial Preferred Stock A, without par value, at an exercise price of $90, subject to adjustment, following a distribution date which shall be the earlier to occur of (i) 10 days following a public announcement that a person or group (Acquiring Person) has acquired, or obtained the right to acquire, beneficial ownership of 15% or more of the outstanding shares of common stock (Stock Acquisition Date) or (ii) 15 business days (or such later date as may be determined by the Board of Directors prior to the time that any person becomes an Acquiring Person) following the commencement of, or a public announcement of an intention to make, a tender or exchange offer if, upon consummation thereof, such person would meet the 15% threshold.

Subject to certain exempt transactions, in the event that the 15% threshold is met, each holder of a Right (other than the Acquiring Person) will thereafter have the right to receive, upon exercise at the then current exercise price of the Right, common stock (or, in certain circumstances, cash, property or other securities of the Company) having a value equal to two times the exercise price of the Right. If, at any time following the Stock Acquisition Date, the Company is acquired in a merger or other business combination transaction or 50% or more of the Company's assets or earning power are sold, each Right will entitle the holder (other than the Acquiring Person) to receive, upon exercise at the then current exercise price of the Right, common stock of the acquiring or surviving company having a value equal to two times the exercise price of the Right. Certain stock acquisitions will also trigger a provision permitting the Board of Directors to exchange each Right for one share of common stock.

The Rights are nonvoting and expire on July 23, 2006, unless redeemed by the Company at a price of $.01 per Right at any time prior to the time a person becomes an Acquiring Person. The Board of Directors has authorized the reservation of one million shares of Junior Serial Preferred Stock A for issuance under the Rights Plan in the event of exercise of the Rights.

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PREFERRED STOCK

Preferred Stock December 31	1997	1996
	Millions	
Cumulative Preferred Stock		
Preferred stock, $100 par value,		
116,000 shares authorized;		
5% Series - 113,358 shares outstanding,		
callable at $102.50 per share	$11.5	$11.5
Redeemable Serial Preferred Stock		
Serial preferred stock A, without		
par value, 2,500,000 shares authorized;		
$6.70 Series - 100,000 shares		
outstanding, noncallable, redeemable		
in 2000 at $100 per share	$10.0	$10.0
$7.125 Series - 100,000 shares		
outstanding, noncallable, redeemable		
in 2000 at $100 per share	10.0	10.0

Total redeemable serial preferred stock	$20.0	$20.0

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MANDATORILY REDEEMABLE PREFERRED SECURITIES OF SUBSIDIARY

MP&L Capital I (Trust) was established as a wholly owned business trust of the Company for the purpose of issuing common and preferred securities (Trust Securities). In March 1996 the Trust publicly issued three million 8.05% Cumulative Quarterly Income Preferred Securities (QUIPS), representing preferred beneficial interests in the assets held by the Trust. The proceeds of the sale of the QUIPS, and of common securities of the Trust to the Company, were used by the Trust to purchase from the Company $77.5 million of 8.05% Junior Subordinated Debentures, Series A, Due 2015 (Subordinated Debentures), resulting in net proceeds to the Company of $72.3 million. Holders of the QUIPS are entitled to receive quarterly distributions at an annual rate of 8.05% of the liquidation preference value of $25 per security. The Company has the right to defer interest payments on the Subordinated Debentures which would result in the similar deferral of distributions on the QUIPS during extension periods up to 20 consecutive quarters. The Company is the owner of all the common trust securities, which constitute approximately 3% of the aggregate liquidation amount of all the Trust Securities. The sole asset of the Trust is Subordinated Debentures, interest on which is deductible by the Company for income tax purposes. The Trust will use interest payments received on the Subordinated Debentures it holds to make the quarterly cash distributions on the QUIPS.

The QUIPS are subject to mandatory redemption upon repayment of the Subordinated Debentures at maturity or upon redemption. The Company has the option to redeem the Subordinated Debentures upon the occurrence of certain events and, in any event, may do so at any time on or after March 20, 2001.

The Company has guaranteed, on a subordinated basis, payment of the Trust's obligations.

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LONG-TERM DEBT

Long-Term Debt December 31	1997	1996
	Millions	
Minnesota Power		
First mortgage bonds		
6 1/4% Series due 2003	$ 25.0	$ 25.0
6.68% Series due 2007	20.0	-
7% Series due 2007	60.0	-
7 1/2% Series due 2007	35.0	35.0
7 3/4% Series due 2007	55.0	55.0
7% Series due 2008	50.0	50.0
6 1/2% Series	-	18.0
7 3/8% Series	-	60.0
6% Pollution control series E due 2022	111.0	111.0
Variable demand revenue refunding bonds series 1997 A, B, C and D, due 2007-2020	39.0	-
Pollution control revenue bonds, 6.875%, due 2002	4.8	33.9
Leveraged ESOP loan, 9.125%, due 1998-2004	11.3	12.2
Other long-term debt, variable, due 2001-2013	7.3	17.3
Subsidiary companies		
First mortgage bonds, 8.46%, due 2013	54.9	45.0
Senior notes, series A, 7.70%, due 2006	90.0	90.0
Industrial development revenue bonds, 6.50%, due 2025	35.1	33.6
First mortgage bonds, 8.01%, due 2017	28.0	-
Note payable, 10.44%	-	30.0
Other long-term debt, 6.1-8 7/8%, due 1998-2026	63.7	85.6
Less due within one year	(4.7)	(7.2)
Total long-term debt	$685.4	$694.4

The aggregate amount of long-term debt maturing during 1998 is $4.7 million ($6.6 million in 1999; $9.6 million in 2000; $11.1 million in 2001; and $14.0 million in 2002). Substantially all Company electric and water plant is subject to the lien of the mortgages securing various first mortgage bonds.

At Dec. 31, 1997, subsidiaries of the Company had long-term bank lines of credit aggregating $20 million ($50 million at Dec. 31, 1996). Drawn portions on these lines of credit aggregate $4.5 million at Dec. 31, 1997 ($20 million at Dec. 31, 1996), and are included in subsidiary companies other long-term debt.

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LEASING AGREEMENTS

ADESA leases three auction facilities which have five year lease terms ending 2000 and no renewal options. At the beginning of the fourth year of the lease term, in the event ADESA does not exercise its purchase option at an aggregate price of $26.5 million, ADESA has guaranteed any deficiency in sales proceeds the lessor realizes in disposing of the leased properties should the selling price fall below $25.7 million. ADESA is entitled to any excess sales proceeds over the option price. ADESA has guaranteed the payment of principal and interest on the lessor's indebtedness which consists of $25.7 million of 9.82% mortgage notes, due Aug. 1, 2000.

The Company leases other properties and equipment in addition to those listed above pursuant to operating and capital lease agreements with terms expiring through 2009. The aggregate amount of future minimum lease payments for capital and operating leases during 1998 is $13.5 million ($14.2 million in 1999; $7.4 million in 2000; $4.8 million in 2001; and $4.1 million in 2002). Total rent expense was $10 million in 1997 ($7.4 million in 1996; $1.6 million in 1995).

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INCOME TAX EXPENSE

Income Tax Expense Year Ended December 31	1997	1996	1995
		Millions	
Continuing operations			
Current tax expense			
Federal	$31.9	$23.6	$ 8.5
Foreign	3.1	1.7	0.6
State	10.0	6.1	4.2
	45.0	31.4	13.3
Deferred tax expense (benefits)			
Federal	4.8	0.3	6.8
State	(1.5)	(1.9)	0.3
	3.3	(1.6)	7.1
Change in valuation allowance	(0.4)	(8.2)	(18.4)
Deferred tax credits	(1.3)	(2.0)	(0.9)
Income tax for			
Continuing operations	46.6	19.6	1.1
Discontinued operations	-	-	2.9
Total income tax expense	$46.6	$19.6	$ 4.0

Reconciliation of Taxes from Federal Statutory Rate to Total Income Tax Expense Year Ended December 31	1997	1996	1995
		Millions	
Tax computed at federal statutory rate	$43.5	$31.1	$24.0
Increase (decrease) in tax			
State income taxes, net of federal income tax benefit	5.6	2.9	3.5
Change in valuation allowance	(0.4)	(8.2)	(18.4)
Dividend received deduction	(2.0)	(1.9)	(2.3)
Tax credits	(2.2)	(1.9)	(1.9)
Other	2.1	(2.4)	(0.9)
Total income tax expense	$46.6	$19.6	$ 4.0

Deferred Tax Assets and Liabilities December 31	1997	1996
	Millions	
Deferred tax assets		
Contributions in aid of construction	$ 19.8	$ 18.8
Lehigh basis difference	15.3	23.6
Deferred compensation plans	15.6	12.1
Depreciation	12.9	15.0
Investment tax credits	22.2	22.8
Other	41.4	35.1
Gross deferred tax assets	127.2	127.4
Deferred tax asset valuation allowance	(0.3)	(0.7)
Total deferred tax assets	126.9	126.7

Deferred tax liabilities		
Depreciation	200.3	188.8
Allowance for funds used during construction	18.2	18.7
Income from unconsolidated subsidiaries	7.7	5.4
Investment tax credits	31.3	32.6
Other	20.7	30.1
Total deferred tax liabilities	278.2	275.6
Accumulated deferred income taxes	$151.3	$148.9

TAX BENEFITS. The Company, through Lehigh, acquired the stock of Lehigh Corporation in a bargain purchase in 1991. The carried-over tax bases of the underlying assets exceeded the book bases assigned in purchase accounting. The Internal Revenue Code (IRC) limits the use of tax losses resulting from the higher tax basis.

SFAS 109, "Accounting for Income Taxes," was adopted on a prospective basis effective Jan. 1, 1993. Upon adoption, a valuation reserve was established for the entire amount of the tax benefits attributable to the bases differences and alternative minimum tax credits because, in management's judgment, realization of the tax benefits was not "more likely than not." This judgment was based on the unlikelihood of realizing the tax benefits due to the IRC restrictions in light of management's existing five year property disposal plan.

In 1995 based on a detailed analysis of projected cash flow, Lehigh implemented a business strategy which called for Lehigh to dispose of its remaining real estate assets with a specific view towards maximizing realization of the tax benefits. Accordingly, in 1995 the valuation reserve was reduced by $18.4 million. In 1996 the remaining $8.2 million valuation reserve was reversed as a result of the projected positive impact the 1996 Palm Coast acquisition would have on Lehigh's taxable income.

UNDISTRIBUTED EARNINGS. No provision has been made for taxes on $19.1 million of pre-1993 undistributed earnings of Capital Re, an investment accounted for under the equity method. Those earnings have been and are expected to continue to be reinvested. The Company estimates that $7.9 million of tax would be payable on the pre-1993 undistributed earnings of Capital Re if the Company should sell its investment. The Company has recognized the income tax impact on undistributed earnings of Capital Re earned since Jan. 1, 1993.

Undistributed earnings of the Company's foreign subsidiaries were approximately $6.6 million at Dec. 31, 1997 ($4.2 million at Dec. 31, 1996). Foreign undistributed earnings are considered to be indefinitely reinvested, and, accordingly, no provision for U.S. federal and state income taxes has been provided thereon. Upon distribution of foreign undistributed earnings in the form of dividends or otherwise, the Company would be subject to both U.S. income tax (subject to an adjustment, for foreign tax credits) and withholding taxes payable to Canada. Determination of the amount of unrecognized deferred U.S. income tax liability is not practical due to the complexities associated with its hypothetical calculations; however, unrecognized foreign tax credit carryforwards would be available to reduce some portion of the U.S. liability. Withholding taxes of approximately $0.3 million would be payable upon remittance of all previously unremitted earnings at Dec. 31, 1997 ($0.2 million at Dec. 31, 1996).

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EMPLOYEE STOCK AND INCENTIVE PLANS

EMPLOYEE STOCK OWNERSHIP PLAN. The Company sponsors an Employee Stock Ownership Plan (ESOP) with two leveraged accounts.

A 1989 leveraged ESOP account covers all eligible nonunion Minnesota and Wisconsin utility and corporate employees. The ESOP used the proceeds from a $16.5 million loan (15 year term at 9.125%), guaranteed by the Company, to purchase 600,000 shares of Company common stock on the open market. These shares fund an annual benefit of not less than 2% of participants' salaries.

A 1990 leveraged ESOP account covers Minnesota and Wisconsin utility and corporate employees who participated in the non-leveraged ESOP plan prior to August 1989. In 1990 the ESOP issued a $75 million note (term not to exceed 25 years at 10.25%) to the Company as consideration for 2.8 million shares of newly issued common stock. These shares are used to fund an annual benefit at least equal to the value of (a) dividends on shares held in the 1990 leveraged ESOP which are used to make loan payments, and (b) tax benefits obtained from deducting eligible dividends.

The loans will be repaid with dividends received by the ESOP and with employer contributions. ESOP shares acquired with the loans were initially pledged as collateral for the loans. The ESOP shares are released from collateral and allocated to participants based on the portion of total debt service paid in the year. The ESOP shares that collateralize the loans are not included in the number of average shares used to calculate basic and diluted earnings per share.

ESOP Compensation and Interest Expense Year Ended December 31	1997	1996	1995
		Millions	
Interest expense	$1.1	$1.2	$1.3
Compensation expense	1.7	1.8	1.8
Total	$2.8	$3.0	$3.1

ESOP Shares

December 31	1997	1996
	Millions	
Allocated shares	1.8	1.8
Unreleased shares	2.5	2.6
Total ESOP shares	4.3	4.4
Fair value of unreleased shares	$108.5	$71.9

EMPLOYEE STOCK PURCHASE PLAN. The Company has an Employee Stock Purchase Plan that permits eligible employees to buy up to $23,750 per year of Company common stock at 95% of the market price. At Dec. 31, 1997, 476,000 shares had been issued under the plan, and 168,000 shares were held in reserve for future issuance.

STOCK OPTION AND AWARD PLANS. The Company has an Executive Long-Term Incentive Compensation Plan and a Director Long-Term Stock Incentive Plan, both of which became effective in January 1996. The Executive Plan allows for the grant of up to 2.1 million shares of common stock to key employees of the Company. To date, these grants have taken the form of stock options, performance share awards and restricted stock awards. The Director Plan allows for the grant of up to 150,000 shares of common stock to nonemployee directors of the Company. Each nonemployee director receives an annual grant of 725 stock options and a biennial grant of performance shares equal to $10,000 in value of common stock at the date of grant.

Stock options are exercisable at the market price of common shares on the date the options are granted, and vest in equal annual installments over two years with expiration ten years from the date of grant. Performance shares are earned over multi-year time periods and are contingent upon the attainment of certain performance goals of the Company. Restricted stock vests once certain periods of time have elapsed.

The Company has elected to account for its stock-based compensation plans in accordance with APB Opinion No. 25 "Accounting for Stock Issued to Employees," and accordingly, compensation expense has not been recognized for stock options granted. Compensation expense is recognized over the vesting periods for performance and restricted share awards based on the market value of the Company's stock, and was approximately $4 million in 1997 ($1 million in 1996). Pro forma net income and earnings per share under SFAS No. 123 "Accounting for Stock-Based Compensation" have not been presented because such amounts are not materially different from actual amounts reported. This may not be representative of the pro forma effects for future years if additional awards are granted.

In 1997 the Company granted approximately 244,000 stock options (127,000 in 1996), 26,000 performance share awards (74,000 in 1996), and 9,000 shares of restricted stock (24,000 in 1996). The average fair value of options granted was $6.54 ($6.76 in 1996). The average remaining contractual life of options outstanding at the end of 1997 was 8.7 years (9 years in 1996). In January 1998 the Company granted stock options to purchase approximately 185,000 shares of common stock and granted approximately 87,000 performance share awards.

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PENSION PLANS AND BENEFITS

The Company's Minnesota and Wisconsin utility and corporate operations have noncontributory defined benefit pension plans covering eligible employees. Pension benefits are based on an employee's years of service and earnings. The Company makes contributions to the plans consistent with the funding requirements of employee benefit and tax law. Plan assets are invested primarily in publicly traded equity and fixed income securities. At Dec. 31, 1997, approximately 8% of plan assets were invested in Company common stock. Benefits under the Company's noncontributory defined benefit pension plan for Florida utility operations were frozen as of Dec. 31, 1996.

Pension Costs

Year Ended December 31	1997	1996	1995
		Millions	
Service cost	$ 3.6	$ 3.7	$ 4.3
Interest cost	15.8	15.1	13.0
Actual return on assets	(51.1)	(21.2)	(34.5)
Net amortization and deferral	31.5	3.3	17.8
Amortization of early retirement cost	4.8	4.7	2.0
Net cost	$ 4.6	$ 5.6	$ 2.6

Pension Plans Funded Status October 1	1997	1996
	Millions	
Actuarial present value of benefit obligations		
Vested	$(175.9)	$(173.2)
Nonvested	(12.1)	(6.6)
Accumulated benefit obligation	(188.0)	(179.8)
Additional amounts related to future salary increases	(30.8)	(25.7)
Projected benefit obligation (PBO)	(218.8)	(205.5)
Plan assets at fair value	270.7	233.0
Plan assets in excess of PBO	51.9	27.5
Unrecognized net gain	(64.4)	(40.9)
Unrecognized prior service cost	5.2	5.7
Unrecognized transition obligation	1.4	1.7
Unrecognized early retirement cost	2.8	7.5
Pension asset (liability) included in other assets (liabilities)	$ (3.1)	$ 1.5
Actuarial assumptions		
Discount rate	7.75%	8.0%
Average salary increases	6.0%	6.0%
Long-term rate of return on assets	9.0%	9.0%

BNI Coal and subsidiaries in Automotive and Water Services have defined contribution pension plans covering eligible employees. The aggregate annual pension cost for these plans was $2.1 million ($0.9 million in 1996 and in 1995).

POSTRETIREMENT BENEFITS. The Company provides certain health care and life insurance benefits for retired employees. Company policy is to fund postretirement benefit costs, through Voluntary Employee Benefit Association (VEBA) trusts and an irrevocable grantor trust (IGT), as the amounts are collected in rates. Maximum tax deductible contributions are made to the VEBA trusts, with remaining funds placed in the IGT until such time as they become tax deductible. Funds in the IGT do not qualify as plan assets and are excluded from assets in the table below. Plan assets are invested primarily in publicly traded equity and fixed income securities. The regulatory asset for deferred postretirement benefits is being amortized in electric rates over a five year period which began in 1995.

Postretirement Benefit Costs Year Ended December 31	1997	1996	1995
		Millions	
Service cost	$ 2.6	$ 2.7	$ 2.6
Interest cost	4.1	4.2	3.6
Actual return on assets	(3.1)	(1.0)	(0.1)
Net amortization and deferral	3.7	2.5	1.2
Postretirement benefit cost	7.3	8.4	7.3
Amortization of regulatory asset	2.7	2.7	2.0
Net cost	$10.0	$11.1	$9.3

Postretirement Benefit Plan Funded Status October 1	1997	1996
	Millions	
Accumulated postretirement benefit obligation (APBO)		
Retirees	$(28.1)	$(29.6)
Fully eligible participants	(11.1)	(10.6)
Other active participants	(11.4)	(13.0)
APBO	(50.6)	(53.2)
Plan assets at fair value	20.3	10.8
APBO in excess of plan assets	(30.3)	(42.4)
Unrecognized gain	(22.9)	(15.4)
Unrecognized transition obligation	34.7	38.3
Postretirement liability included in other liabilities	$(18.5)	$(19.5)
Actuarial assumptions		
Discount rate	7.75%	8.0%
Long-term rate of return on assets	9.0%	9.0%

The assumed health care cost trend rate used was 9.4%, gradually decreasing to an ultimate rate of 5.3% by 2002. A 1% increase in the assumed health care cost trend rate would result in a $4.6 million increase in the accumulated postretirement benefit obligations (APBO) and a $0.8 million increase in total service and interest costs.

QUARTERLY FINANCIAL DATA (UNAUDITED)

Information for any one quarterly period is not necessarily indicative of the results which may be expected for the year.

Quarter Ended	March 31	June 30	Sept. 30	Dec. 31
	Millions except earnings per share			
1997				
Operating revenue and income	$222.1	$230.4	$246.2	$254.9
Operating income	$26.4	$32.8	$40.3	$30.7
Net income	$16.1	$18.7	$23.2	$19.6
Earnings available for common stock	$15.6	$18.2	$22.7	$19.1
Basic and diluted earnings per share of common stock	$0.52	$0.60	$0.73	$0.62
1996				
Operating revenue and income	$202.7	$208.5	$215.2	$220.6
Operating income	$28.8	$21.1	$21.7	$21.9
Net income	$18.3	$14.8	$17.5	$18.6
Earnings available for common stock	$17.5	$14.2	$17.0	$18.1
Basic and diluted earnings per share of common stock	$0.61	$0.49	$0.58	$0.60

DEFINITIONS

These abbreviations or acronyms are used throughout this document.

Abbreviations or Acronyms	Term
ADESA	ADESA Corporation
AFC	Automotive Finance Corporation
APB	Accounting Principles Board
Americas' Water	Americas' Water Services Corporation
BNI Coal	BNI Coal, Ltd.
Capital Re	Capital Re Corporation
CIP	Conservation Improvement Programs
Company	Minnesota Power & Light Company and its Subsidiaries
DRIP	Dividend Reinvestment and Stock Purchase Plan
ESOP	Employee Stock Ownership Plan
ESPP	Employee Stock Purchase Plan
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
Florida Water	Florida Water Services Corporation
FPSC	Florida Public Service Commission
Great Rigs	Great Rigs Incorporated
Heater	Heater Utilities, Inc.
ISI	Instrumentation Services, Inc.
kWh	Kilowatthour(s)
LaGrange	LaGrange Waterworks Corporation
Lehigh	Lehigh Acquisition Corporation
Minnesota Power	Minnesota Power & Light Company and its Subsidiaries
MP Enterprises	Minnesota Power Enterprises, Inc.
MP Telecom	Minnesota Power Telecom, Inc.
MP Water Resources	MP Water Resources Group, Inc.
MPUC	Minnesota Public Utilities Commission
MW	Megawatt(s)
NCUC	North Carolina Utilities Commission
Note ___	Note ___ to the consolidated financial statements in the Minnesota Power 1997 Annual Report
PSCW	Public Service Commission of Wisconsin
QUIPS	Quarterly Income Preferred Securities
SFAS	Statement of Financial Accounting Standards No.
Square Butte	Square Butte Electric Cooperative
SWL&P	Superior Water, Light and Power Company
U.S. Maintenance and Management	U.S. Maintenance and Management Services Corporation

Exhibit 23(a)

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statement on Form S-8 (Nos. 33-51989, 333-26755, 333-16463, 333-16445) of Minnesota Power & Light Company of our report dated January 26, 1998 appearing on page 32 of the Annual Report to Shareholders which is incorporated in this Annual Report on Form 10-K. We also consent to the incorporation by reference of our report on the Financial Statement Schedule, which appears on page 31 of this Form 10-K.

We also consent to the incorporation by reference in the Prospectus constituting part of the Registration Statement on Form S-3 (Nos. 333-07963, 333-02109, 333-40795, 333-40797, 33-45551) of Minnesota Power & Light Company of our report dated January 26, 1998 appearing on page 32 of the Annual Report to Shareholders which is incorporated in this Annual Report on Form 10-K. We also consent to the incorporation by reference of our report on the Financial Statement Schedule, which appears on page 31 of this Form 10-K.

Price Waterhouse LLP

PRICE WATERHOUSE LLP
Minneapolis, Minnesota
March 25, 1998

Exhibit 23(b)

CONSENT OF GENERAL COUNSEL

The statements of law and legal conclusions under "Item 1. Business" in the Company's Annual Report on Form 10-K for the year ended December 31, 1997, have been reviewed by me and are set forth therein in reliance upon my opinion as an expert.

I hereby consent to the incorporation by reference of such statements of law and legal conclusions in Registration Statement Nos. 333-07963, 333-02109, 333-40795, 333-40797 and 33-45551 on Form S-3, and Registration Statement Nos. 33-51989, 333-26755, 333-16463 and 333-16445 on Form S-8.

Philip R. Halverson

Philip R. Halverson
Duluth, Minnesota
March 25, 1998

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM MINNESOTA POWER'S CONSOLIDATED BALANCE SHEET, STATEMENT OF INCOME, AND STATEMENT OF CASH FLOW FOR THE PERIODS ENDED DECEMBER 31, 1997 AND 1996, AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

1,000,000

YEAR	YEAR
DEC-31-1997	DEC-31-1996
JAN-01-1997	JAN-01-1996
DEC-31-1997	DEC-31-1996
PER-BOOK	PER-BOOK
1,106	1,120
420	404
369	332
64	83
213	207
2,172	2,146
416	394
0	0
296	283
651	611
75	75
32	32
685	694
129	156
0	0
0	0
5	7
0	0
0	0
0	0
534	505
2,172	2,146
954	847
47	20
774	703
838	765
130	94
9	7
142	131
64	62
78	69
2	2
76	67
63	60
49	51
117	77
2.47	2.28
2.47	2.28

Includes $15 million of Income from Equity Investments and $6 million for Distributions on Redeemable Preferred Securities of Subsidiary.

Includes $12 million of Income from Equity Investments and $5 million for Distributions on Redeemable Preferred Securities of Subsidiary.