

In Focus...



2007 Annual Report

Memphis Light, Gas and Water Division

Board of Commissioners

Rick Masson,
Chairman

V. Lynn Evans,
Vice-Chairman

Nick Clark

William Taylor

2007 Executive Leadership Team

Jerry Collins
President and CEO

Christopher Bieber
Vice President of Customer Care

Charlotte Knight-Griffin
Acting General Counsel

John McCullough
Vice President, CFO and Secretary-Treasurer

Linda Peppers
Vice President and Chief Technology Officer

Nick Newman
Vice President of Construction and Maintenance

Armstead Ward
Vice President of Human Resources

Alonzo Weaver
Vice President of Engineering and Operations

About MLGW

Memphis Light, Gas and Water Division is the nation's largest three-service municipal utility. Since 1939, MLGW has met the needs of Memphis and Shelby County residents by delivering reliable and affordable electric, natural gas and water services.

Electricity is supplied to MLGW by the Tennessee Valley Authority (TVA), while natural gas is purchased from a variety of suppliers and transported by three pipeline companies, Texas Gas Transmission Corporation, CMS Trunkline Gas Company and ANR Pipeline Company. Memphis receives its water from one of the largest artesian water systems in the world.

MLGW is led by a President and a five-member Board of Commissioners who are appointed by the Mayor of Memphis and approved by the Memphis City Council.





DAVID F. HANSEN
ADMINISTRATION BUILDING
MEMPHIS LIGHT GAS AND WATER DIVISION

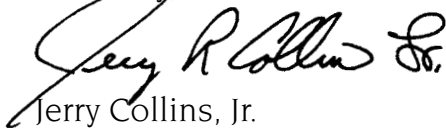
Letter from the President

2007 could best be described as a year of transformation for Memphis Light, Gas and Water. Our challenges pushed us to reach for greater success and our accomplishments reminded us to not rest on our laurels. And throughout it all we continued to keep our focus on the business at hand: providing service to our customers. Service remains the backbone of MLGW's success, and providing reliable and affordable electricity, gas and water is our goal. Because we are a community-oriented company, we must always strike a fine balance between being compassionate toward our community and continuing to run our business efficiently.

While sticking to our hometown values, MLGW still manages to provide world-class service. Looking at our accomplishments over the last year, we have surely laid groundwork toward continued success. We will continue to work toward our vision of being a trusted leader and a positive influence in our community, to satisfy our customers' needs and to contribute to the prosperity of our city.

I hope that you will see in the pages ahead that MLGW is truly a leader in the utility industry and our 2,700 employees are dedicated men and women who will continue to strive for success.

Sincerely,



Jerry Collins, Jr.

President and CEO

Memphis Light, Gas and Water Division



Focus on Service

As an industry leader, our commitment to customer service defines us as an organization and directs our decisions each and every day. As public servants, being responsive to customers' needs is more than a philosophy; it's a way of life. We strive to exceed customers' expectations. Last year we made revisions to our customer credit policy that we believe would strike a balance between good business practices for us while helping our customers facing financial hardships to meet their obligations. The policy changes allow us to be flexible and give customers the opportunity to find a payment plan that will meet their needs.

In our fast paced, hectic lives, having convenient services is important. Customers told us what they wanted, and we listened and responded. Because we live in a virtual world of on demand service, we were so excited to unveil a new dimension to our Web site mlgw.com. The new interactive tool "My Account" went live in October. This component to our Web site enables customers to view and compare up to 24 months of utility bills, as well as determine reasons for bill fluctuations and ways to reduce energy consumption based on their home's profile.

In conjunction with this very useful tool, several months later MLGW's Electronic Bill Presentment and Payment service went live enabling customers to view an exact replica of their bills and payment history. Customers who enrolled for this optional service, which allows MLGW to stop printing and mailing their utility bills, can make secure, no-fee payments online from a bank account.

It's services like these that helps MLGW better connect with its customers. By opening avenues of advanced communication, MLGW is ready to take on the challenges of meeting the demands of today's technologically advanced customers. But we haven't forgotten those who prefer a much simpler way of doing business.

A major asset to MLGW's business operations is its five business offices located throughout the city to serve customers. Our business offices have been a long standing staple to doing business with a large population of our customers. Not only can customers visit us here during normal business hours, they also have access to our 24-hour automated pay stations inside each business office to make payments.

And for the customer looking for extended payment options, MLGW teamed up with TIO Networks to bring user-friendly payment kiosks to more than 40 Exxon on the Run stores. At these locations, customers can make real-time self-serve automated bill payments, 24-hours-a-day for a small fee. We have also added these kiosks at 10 Dollar General stores, which are available during store hours.





Focus on Operational Excellence

Even as we continued to hone in and focus on what matters most, 2007 was a time of transition for MLGW, and the utility welcomed its 10th president, Jerry Collins, Jr. His mission for the utility is to continue to deliver exceptional service at affordable rates.

MLGW's operational excellence sometimes goes beyond serving customers within our territory. When ice storms hit Springfield, MO, four MLGW line crews traveled several hundred miles to assist in their power restoration efforts. Working 16-hour days, resetting utility poles and restringing power lines was a testament that our employees often go beyond the call of duty for a sister utility.





Laura Campbell, MLGW Assistant Manager of Energy Resources, testifies before the Commodity Futures Trading Commission.

In the Spotlight

MLGW made the national spotlight on several occasions in 2007. In September, the utility testified on behalf of the American Public Gas Association (APGA) before the Commodity Futures Trading Commission in defense of a fair market place for natural gas customers. The commission had called the hearing to examine the important issues of trading on regulated exchanges and exempt commercial markets. With MLGW's testimony, the APGA sought passage of the Market Trust Act of 2007, which would protect consumers by requiring the reporting of large positions in financial contracts for natural gas held in all segments of the market.

In June, MLGW joined 48 of the nation's more than 2,000 public power utilities by earning the American Public Power Association's (APPA) Reliable Public Power Provider (RP3) Award. The RP3 awards are bestowed upon APPA-member utilities that demonstrate sound business practices and provide their customers with the highest degree of reliable and safe electric service.

Another notable achievement was the results of the Jacksonville Energy Authority (JEA) survey of residential electric rates from 55 public and private utilities. This survey showed that MLGW customers pay some of the lowest rates in the nation. Of the 55 utilities surveyed, MLGW rates were the ninth lowest. The survey compared the cost for 1,000 kilowatts of electricity (a universal standard of measure), and not average utility bills.

Whether we're training to string wires faster or to answer phones in a more timely manner, MLGW employees are striving

to meet those demands, and nothing emphasizes this message more than the International Quality & Productivity Center recognizing MLGW University with its CUBIC award as the "Best New Corporate University." MLGW University is designed to enhance the professional and personal development of MLGW employees by offering courses that improve their skill sets.

We were challenged to improve in 2008 by the results of J.D. Power's 2007 Power & Associates Electric Utility Residential Customer Satisfaction Survey. The survey ranked MLGW at the bottom of medium-sized utilities. Not satisfied with these results, MLGW set out on a mission to implement a comprehensive strategy aimed at addressing the six areas of improvement the survey focused on: power and reliability, image, price, communication, billing and payment, and customer service.





This Year's Pledge
\$770,649.84

UNITED
we
light
the
WAY



MLGW/IBEW Local 1288
2007-2008 United Way Campaign

Last Year's Pledge
\$802,530.37
This Year's Goal
\$810,000.00

MLGW United Way campaign leaders: Dana Massey, J.R. Whitaker and Tjuan Redmond.

Focus On Giving Back

MLGW employees are uniquely committed to the well-being of our community. Even with the dip in the economy, employees still make giving back a priority in their lives. MLGW employees annually give more than \$1 million in goods and services. Employees often give of themselves donating their time and money to help those in need. Community outreach isn't just a catchphrase at MLGW, it's a reality. Our employee base is made of compassionate individuals who give back to the community in which they live. When employees are volunteering with Special Olympics or building homes for Habitat for Humanity, they're digging into their pockets or giving time to contribute to a better community.

MLGW was among the Top Five corporate donors in Memphis to the United Way of the Mid-South. MLGW employees raised \$770,649.84 for the organization. Among

other organizations benefiting from the generosity of MLGW's employees: The Food Bank, American Cancer Society, Junior Achievement, LifeBlood and Plus-1, MLGW's utility assistance program funded by customers.

Late summer 2007 saw some of the hottest days on record as the City of Good Abode experienced temperatures breaking the 100 degree mark for 10 straight days. With compassion in our hearts for our neighbors in need, MLGW donated 300 box fans and 200 air conditioning units to local organizations to distribute to senior and disabled customers. The utility also donated bottled water to eight Memphis Community Centers that served as cooling shelters. Our hope was that this simple gesture would help take away some of the burden our financially challenged customers faced and keep them safe and healthy at the same time.





Focus on the

As good stewards of the Earth, it is imperative that MLGW take an active role in contributing to the environment in which we live. Since 2002, we have offered EcoBuild, a green building program that certifies homes, apartments and commercial buildings as being “green” or sustainable. After certifying more than 300 homes since that time, last year MLGW provided a \$20,000 grant to help 12 Habitat for Humanity Homes become more energy efficient through the program. These Habitat homeowners were the first in the area to receive energy efficient upgrades to their homes.

But MLGW’s green movement didn’t stop there. We carried the green theme throughout the year to various community events around town. Our “Go Green” message was a huge hit with audiences since



Environment

they got a chance to play holes of putt-putt and win energy efficient prizes like compact fluorescent light bulbs and solar calculators. Employee volunteers also shared energy efficient tips with customers.

Customers have also benefited from EnergySmart Memphis, which is a year-long energy education and home improvement initiative designed to help Memphians save money on their energy costs. Working with TVA, MLGW is offering workshops throughout Shelby County that focus on teaching energy basics. Since the fall of 2007, 1,750 customers have attended 44 EnergySmart workshops. The workshops are held throughout the community for neighborhood associations and other organizations, and teach practical ways to save energy. An estimated 3,000 local residents will receive in-depth energy conservation training through the EnergySmart Memphis program.



Earnest Holliday speaks to school children about electricity as MLGW's "Terminator".

Focus on Community Investment

At MLGW, we are the citizens we serve and to ensure that our community thrives, we have placed a special emphasis on our future customers. In partnership with Memphis City Schools, MLGW began the annual “MLGW Goes to School” program. During one week each year, MLGW employees speak to students to encourage them to explore career opportunities in the utility business.

MLGW has contributed to local education efforts for many years, with particular emphasis on the needs, support and training of students in Memphis City Schools. MLGW supports such activities as summer internships, Memphis Weekend Academy, Junior Achievement and Explorer posts, and sponsors many programs at its adopted school, Carver High.

MLGW also teamed up with the Children’s Museum of Memphis to develop an energy education program for students in grades 2-5. The program, called the Energy IQ Traveling Lab is available to all teachers in the Memphis City and Shelby County school districts. Children learn where energy comes from and how it works, how to become a smarter consumer, and how to estimate and better control their family’s energy usage in order to save energy and help to lower their family’s utility bill.





MIGW



Robert E. ...
Secretary of the Treasury

Focus on Financial Excellence

Fitch Ratings, a leading global rating agency of bond issues, affirmed its “AA” rating of MLGW’s electric division. The “AA” rating makes MLGW one of Fitch’s most highly rated electric systems. Quality of management, economic diversity of the service territory and the ability to pay down debt were a few of the factors the ratings agency looked at in determining the rating.

MLGW also entered into an agreement with the Tennessee Energy Acquisition Corporation (TEAC) to purchase a portion of MLGW’s natural gas supply at a discounted rate below market index costs. MLGW expects to realize a savings of \$102 million over the agreement’s 20-year term, with no up-front investment.

The agreement does not set the price of natural gas, but rather provides MLGW with a pre-determined discount for all gas purchased through TEAC.

Thanks to MLGW’s efforts, Memphis ranked first among selected cities across the nation for having the lowest water and wastewater rates according to the “2007 Utility Bill Comparisons for Selected U.S. Cities,” a report compiled from surveys conducted annually by MLGW.

MLGW’s drinking water was ranked as one of the top five of 100 selected U.S. cities according to an article in the May edition of *Men’s Health* magazine. According to the publication, the ranking is based on recent data regarding levels of arsenic, lead, haloacetic acids, total trihalomethanes, total coliform bacteria and the number of EPA violations for each city’s water system from 1995 to 2005.





Jane Segal and **Chris Stanley** host MLGW's TV program, "Memphis Energized."

Focus on Communications

Great relationships are based on two-way communications. At MLGW we realize that Communication is key to successfully meeting customers' expectations.

MLGW offers more ways for customers to receive valuable training that can help them take control of their energy costs. "Memphis Energized," a half-hour television program produced by MLGW, gives customers some how-to tips for saving energy as well as information on green power breakthroughs, an inside look at how service works at their home and the latest news and information about their utility company. This innovative public service program is shown more than 20 times per month on local broadcast and cable outlets, and provides a wealth of conservation information to our customers.

MLGW meter readers had a new look in 2007, when they donned new shirts and jackets with a color that improved safety and recognition. All shirts and jackets are a highly visible yellow with reflective striping. The change in uniform color was made to help customers readily identify meter readers working in neighborhoods and backyards, and for the general safety of the meter readers.

MLGW was even able to recruit some local and national celebrities to promote MLGW services and programs through a series of public service announcements. Nationally known sports figure John Calipiri, head basketball coach at the University of Memphis, and Rudy Gay, star of the NBA's Memphis Grizzlies, joined actor Samuel L. Jackson and actor/musician Isaac Hayes. All celebrities donated their time for free.

Customers expect new ways to communicate, and MLGW offers various communication tools to give customers the most accessible

means to reach us to let us know what they want. With this in mind, MLGW launched a new blog, "Bird on a Wire" (mlgw.blogspot.com). "Bird on a Wire" provides our customers with a convenient forum where they can express comments or ideas and engage in dialog with other customers about utility-related issues. MLGW regularly posts information on an array of topics including energy conservation tips, assistance programs, MLGW leadership, and legislative efforts that may affect our customers and much more.

The MLGW media relations team has launched an online newsroom to assist the media with stories pertaining to MLGW. The newsroom can be found at www.mlgw.com/newsroom. Among other tools, members of the media can find the latest news releases and get fast facts to assist in the writing of stories. There is also a glossary of electric, gas and water terms, links to other utility industry web sites and downloadable logos and photos.



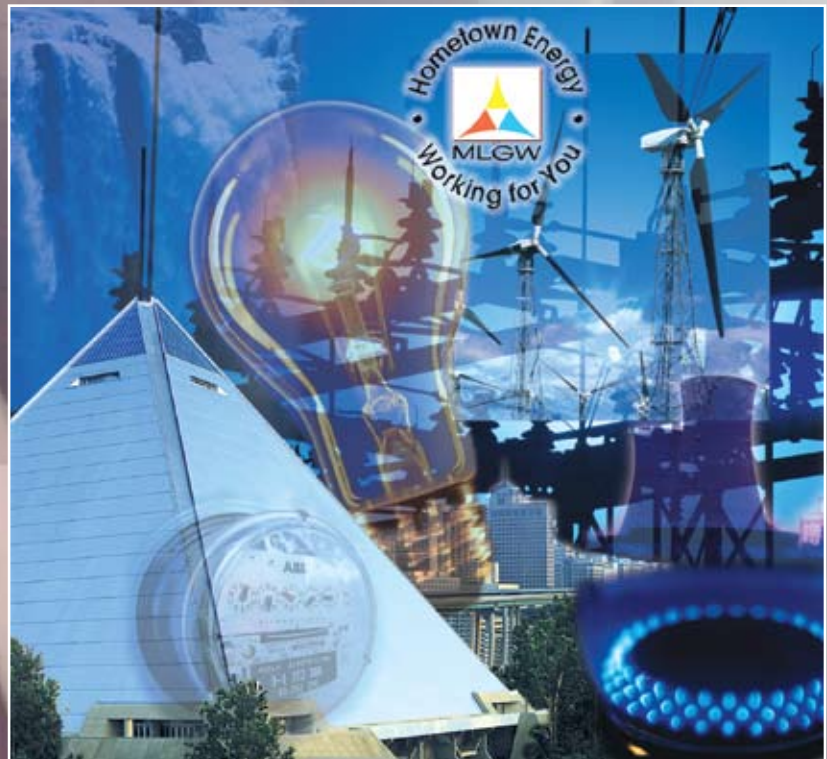
Focus on Reliability

While providing customers with enhancements to make life a little easier is important, it is just as vital that the necessities remain predictable. Our customers rely on us to keep their services on with as few interruptions as possible. Helping us achieve this goal is our technologically advanced SCADA system (Supervisory Control and Data Acquisition) installed in 1998. This system along with the consolidation of our electric, gas and water dispatching areas and our CARES system (Computer Aided Restoration of Electric Service) have reduced our restoration time and greatly enhanced our operational efficiency.

MLGW now has a state-of-the-art Emergency Operations Center (EOC) that allows customer's services to be restored faster. This control hub was built to give our crisis teams one location that all essential personnel can assemble to tackle the task of restoring our systems/processes back to normal after an event. The need of this room was realized from prior experience dealing with major outages, when all crisis team personnel were operating out of the System Operations Building and space was limited. The room is equipped with five large-screen monitors so MLGW managers can lead restoration progress as well as special phone lines and radios so staff members can quickly obtain extra crews, additional materials and other supplies that would be needed in the event of an emergency.

Focus on the Future

Looking ahead, our future is very bright. Our goal of being the best company for our customers will propel us to be the nation's number one public power company. We will think outside the box and go beyond the traditional utility responsibilities. We will continue to look for new ways to empower our community and improve our operations. We are in our best position to heighten our level of customer and community service. Most importantly, the financial stability that we currently enjoy will afford us the privilege of further improving the safety, affordability and reliability of our services. This stability allows us to do what we do best- deliver exceptional customer service.





MEMPHIS LIGHT GAS AND WATER DIVISION

To The Board of Commissioners and Valued Stakeholders:

We are pleased to submit the Annual Report of Memphis Light, Gas and Water Division (MLGW) for the fiscal year ended December 31, 2007, as required by the Charter Provisions of the City of Memphis (City) creating the Memphis Light, Gas and Water Division. This report has been prepared in conformity with generally accepted accounting principles (GAAP), under the rules and regulations of the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB). MLGW is also subject to the federally mandated Single Audit, and the findings for internal controls and compliance are herein presented.

Responsibility for the accuracy and presentation of the information provided is the full responsibility of the management of MLGW. Disclosures necessary to assist the reader in the understanding of the financial statements have been included.

MLGW's financial statements have been audited by Watkins Uiberall, PLLC and Banks, Finley, White and Company, licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of MLGW for the fiscal year ended December 31, 2007 are free of material misstatement. The independent audit involved 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. The independent auditors concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that MLGW's financial statements for the fiscal year ended December 31, 2007, are fairly presented in conformity with generally accepted accounting principles (GAAP). The independent auditor's report is presented as the first component of the financial section of the report.

The independent audit of the financial statements of MLGW was part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing Single Audit engagements require the independent auditor to report not only on the fair presentation of the financial statements, but also on the audited government's internal controls and compliance with legal requirements, with special emphasis on internal controls and legal requirements involving the administration of federal awards. These reports are available in MLGW's separately issued Single Audit Report.

Generally accepted accounting principles require that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of a Management Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. MLGW's MD&A can be found immediately following the report of the independent auditors.

Profile of the Government--MLGW was created by an amendment to the City Charter by Chapter 381 of the Private Acts of the General Assembly of Tennessee, adopted March 9, 1939, as amended (the "Private Act"). MLGW operates three separate utilities, as divisions, providing electricity and gas in the City and Shelby County. Water service is provided by MLGW in the

City and, together with other municipal systems, in Shelby County. Each division operates as a separate entity for accounting and financial purposes in accordance with the Private Act. For economic reasons, activities common to all three divisions are administered jointly and costs are prorated monthly among the divisions. A 1981 amendment to the City Charter permits the establishment of additional divisions to provide other energy services.

MLGW controls the administration of its activities and business affairs. It operates independently, manages its own finances and is responsible for obligations incurred in such operations, including indebtedness payable from operations of the Division. MLGW must have the approval of the City Council before incurring certain obligations, including purchasing real estate and exercising the right of eminent domain; also the annual budget is subject to approval by the City Council.

MLGW is managed by a Board, which consists of five members nominated by the Mayor and approved by the City Council. Under the Private Act, the Board is responsible for doing all things necessary to supply the Division's service area with electricity, gas and water. The members of the Board serve staggered terms of three years each. The Board elects annually a Chairman and Vice Chairman whose terms begin June 1 of each year. The Chairman, Vice Chairman and Board Members continue to serve until a new Chairman, Vice Chairman or Board Member is elected or appointed by the Mayor.

The daily operation of MLGW is managed by the President and Chief Executive Officer, who is nominated for a five-year term by the Mayor and approved by the City Council. Under the Private Act, the President generally supervises the operation of MLGW and all of its officers and employees.

Local Economy—(Information provided by Memphis Regional Chamber Website)--Memphis, Tennessee, located in the southwest corner of Tennessee on the Mississippi River, is the nation's 17th largest city. The latest population estimates in 2007 reported a Shelby County population of 910,100, of which, all households utilize MLGW's services. The eight-county Memphis Metro area provides a diverse range of employers which contributes to the overall stability of the area and to MLGW's customer base. As of 2006, government employment (14%) comprised the largest percentage of non-farm employment, followed by professional and business services and educational and health services (each adding 13% and 12% respectively); retail trade and leisure and hospitality (11% each); and transportation, warehousing and utilities (10%) rounding out sectors of 10 percent or greater.

Memphis' central location, which is traversed by seven federal and two interstate highways, and flanked by the Mississippi River, makes it a prime location for distribution. MLGW's low utility rates, as well as the city's low cost of living, inexpensive real estate and aggressive corporate incentives has helped foster a business environment amenable to the distribution industry. As a result, Memphis has become known as America's Distribution Center and a global logistics hub, claiming the world's largest air cargo airport since 1991, and boasting the third largest rail center and the 4th largest inland port in the U.S. Home to major hubs for FedEx, UPS, DHL, and Northwest Airlines; world headquarters for Federal Express and a major thoroughfare for the trucking industry, Memphis is a vital epicenter of commerce and MLGW works diligently to maintain reliable power for these operations to ensure they run smoothly.

National Economy—The continued increase in energy prices continues to put financial pressure on MLGW customers already strained by a host of national economic burdens including

rising gasoline prices and home foreclosure issues. MLGW customers have been subjected to sharply rising energy costs for reasons beyond MLGW's control including increases in the natural gas market and a series of rate increases imposed by MLGW's wholesale electric provider, the Tennessee Valley Authority (TVA). Since 2005, TVA has approved three electric rate increases as follows: 7.5 percent on September 26, 2005, 9.95 percent on March 27, 2006 and 7 percent on February 15, 2008. On October 1, 2006, TVA also implemented a fuel cost adjustment mechanism that allows TVA to automatically adjust rates up or down as fuel and purchased power costs rise and fall. MLGW continues to implement strategies and plans to help shape the direction of federal and state electric restructuring to ensure continued access to reliable, low-cost electricity supplies.

Wholesale natural gas prices have tripled over a ten-year period and continue to rise. The Gas Division purchases its gas requirements in the open market from a variety of suppliers using short- and long-term purchases, hedging, and management of storage and LNG supplies.

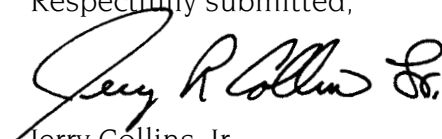
Financial Policies and Major Initiatives--MLGW maintains a comprehensive cash flow model which assesses the growth of the separate divisions and determines future rate increase requirements. MLGW also incorporates a 10-year capital financial plan in its budgeting process. MLGW's Electric, Gas and Water Engineering Departments develop detailed technical master plans for their respective systems which are then correlated with the financial plan. The 10-year capital plans are updated periodically during the year in order to provide the most current possible cash flow projections.

Among the three divisions, MLGW averages more than \$100 million in capital expenditures throughout the year. Major electric projects planned for the 10-year period include construction of South Collierville and East Shelby County substations needed to provide for expected residential and industrial growth in these areas. Gas division plans include installation of approximately 17 miles of transmission main, 202 miles of distribution main, and 8 regulator stations over the next 10 years, and the Water division plans for the continuation of seismic retrofit to pumping facilities and the construction of an additional plant in the projected growth area of Northeast Shelby County.

MLGW also has a formal five-year Strategic Plan that is committed to cost control and is discussed in other sections of this financial report. MLGW will also work with the City of Memphis, TVA, and other stakeholders when possible to streamline costs through collaborative efforts.

Acknowledgements--The preparation of this report was made possible by the overall dedication of MLGW's Finance Division. We would like to express our appreciation to all members of the Finance Division who assisted and contributed to the preparation of this report. Special thanks must also be given to Watkins Uiberall, PLLC and Banks, Finley, White and Company for their efficient and timely completion of this year's audit.

Respectfully submitted,


Jerry Collins, Jr.
President and CEO


John McCullough
Vice President, CFO and Secretary-Treasurer

