Defining Conservation

**conservation**, n. [L. conservatio, from conservare, to keep; from com-, together, and servare, to keep, save.] The act of preserving, guarding, or protecting; preservation from loss, decay, injury or violation; the official care and protection of natural resources, as forests or water.

2008 Annual Report
Memphis Light, Gas and Water Division
Welcome to Memphis Light, Gas and Water Division. The company is governed and owned by the people of Memphis. Through a citizen Board of Commissioners and a president appointed by the elected mayor of the city of Memphis, policies are set that govern the largest, three-service public utility in the nation. A set of executive officers lead approximately 2,700 employees in providing utility services to the people of Memphis and Shelby County.

Most people are surprised to learn that the highly successful Memphis Light, Gas and Water Division (MLGW)—often simply referred to as the ‘Division’—is not that old. It was only born in 1939, even though organized utility service had been available for 87 years before MLGW came onto the scene. Maybe its success comes because it has never been ‘only’ a utility company. Born from a novel idea, the Division has always been a company of ideas, a company unafraid to plan and equally unafraid to place novel ideas into practical action.

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.

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Thoughts on 2008 at MLGW
by MLGW President and CEO Jerry Collins Jr.

We accomplished a great deal at MLGW in 2008. Despite the vast challenges facing Americans in 2009, I am confident that MLGW will survive the uncertain days ahead. Moreover, I believe we will grow stronger as individuals and as employees.

We will have a lot to do in 2009 and in future days. Specific goals include the proposal and passage of a city ordinance which will require rental property owners to make their structures more energy efficient. We will begin to measure everything we do in order to better track our results. Our corporate culture will return to a more results-oriented environment, in which we continue to care for our customers, but will place a renewed emphasis on caring for our fellow employees.

I believe our true mission at MLGW is to enhance the quality of life and the economic well-being of our community. We must earn complete trust from our customers. This mission will take some time to complete, but it can be done. It isn’t hard to find a person who will tell you that the best-tasting water in the nation is found at any water tap in Memphis. We will know our job is complete when a typical Memphian can be asked the question, ‘Which is the best utility in the nation?’ and simply replies, ‘No question—MLGW.’

Jerry R. Collins Jr.
MLGW Board of Commissioners

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. All these officers have a role in the governance of MLGW. The President is the Chief Executive Officer of the company. The Board of Commissioners sets the policies and guidelines that govern the activities of MLGW employees in supplying utility services to the people of Memphis and Shelby County. The Board of Commissioners conducts the business of MLGW at regularly scheduled open public meetings. Proposed agendas for those meetings are posted in the lobby of the MLGW David C. Hansen Administration Building and on www.MLGW.com at least 48 hours prior to each meeting. Any individual, public or private, may address the Board. The meetings are open to the public and to the media.

The Memphis City Council has a committee that regularly meets to discuss MLGW matters and to hear reports from MLGW executive officers. The Memphis City Council not only approves the MLGW budget, it also votes as a plenary body on certain actions and proposals by the MLGW Board of Commissioners.

V. Lynn Evans, Chair
Ms. Evans is owner of V. Lynn Evans, CPA, a certified public accounting and consulting firm.

Darrell T. Cobbins, Vice Chair
Mr. Cobbins established Universal Commercial Real Estate, LLC in 2007, as Memphis’ first African-American owned commercial real estate and community development services firm.

Rick Masson
For many years an executive administrator with city of Memphis government, Mr. Masson currently is the Executive Director of Shelby Farms.

Dedrick Brittenum
Mr. Brittenum is a partner in the law firm of Farris, Bobango and Branan, PLC.

Steven Wishnia
Mr. Wishnia is president and managing director of Highland Capital Management Corporation.
MLGW Executive Leadership

Jerry R. Collins Jr.
President and CEO

Christopher G. Bieber
Vice President of Customer Care

Charmiane G. Claxton
Vice President of Human Resources

John W. McCullough
Vice President, CFO and Secretary-Treasurer

Nicholas Newman
Vice President of Construction and Maintenance

Cheryl W. Patterson
Vice President and General Counsel

Linda K. Peppers
Vice President and Chief Technology Officer

Alonzo Weaver
Vice President of Engineering and Operations

Gale Jones Carson
Director of Corporate Communications

Clifford M. DeBerry
Director of Analysis, Strategy and Performance

Dana Jeanes
Controller

Lesa J. Walton
Director of Internal Audit

Anderson D. Williams
Executive Analyst
MLGW in 2008: Defining Conservation

Jerry Collins’ full first year as president redirected MLGW to take a more active approach to improving customer service. Employees have embraced an increased customer advocacy role for MLGW, with the company assuming ombudsman status in its relationship with local, state and federal governments. Employees at MLGW are encouraged to take advocacy positions for customers, and this practice can find employees fighting for customers on national television, such as on CNBC’s “Closing Bell,” and before congressional committees and commissions, such as the Federal Energy Regulatory Commission, and the U.S. House Energy and Commerce Subcommittee on Oversight and Investigations.

MLGW speaks out against rate increase

In 2008, the Tennessee Valley Authority approved its largest rate increase in nearly 35 years. The TVA increase was passed on to TVA distributors—including MLGW—effective October 1. Through its contract with TVA, MLGW was required to pass the rate increase through to customers. No distributor received additional revenue from this rate increase. President Collins was the sole member from the 159 TVA power distributors who attended the TVA Board meeting to speak out against the TVA base rate increase for MLGW customers.

PCB removal for the environment

Memphis will soon have a more environmentally friendly electric system for the community upon completion of an agreement between the Environmental Protection Agency (EPA) and MLGW to remove polychlorinated biphenyls (PCBs) from the electric grid. MLGW currently meets federal guidelines for PCB levels, but at the end of an upcoming three-year update to the grid MLGW will exceed regulatory standards.

MLGW introduces rental ordinance

MLGW fought hard in 2008 for a proposed rental property ordinance, which would require rental property owners to make their structures more energy efficient and help transform Memphis into a more energy-efficient community. The effort paid off as the Memphis City Council adopted the ordinance in early 2009.
The community responds to conservation

Plus-1

Our conservation programs for the community have been numerous and popular during 2008. Celebrities associated with the Memphis community, such as Samuel L. Jackson and the late Isaac Hayes, chose to participate in informational campaigns on energy conservation and the Plus-1 program. Plus-1 is funded by MLGW customers, employees and other supporters through one-time donations or by adding a dollar or more to their utility bills each month. Since its inception in 1982, Plus-1 has provided approximately $6 million in assistance to families in crisis in our community.

Community Conservation Day

With costs rising in virtually all sectors of the energy market and customers eager to learn how to best use energy in their daily lives, MLGW’s Community Conservation Day on October 10 was destined to be a success. MLGW, Exxon On the Run stores, and TVA teamed up to raise customer awareness of wise energy usage and to help those customers to find ways to curb their energy usage. Approximately 9,000 customers received energy conservation kits. The American Public Power Association honored the program with its Community Service Award for 2008. The program will be expanded in 2009.

United Way

Despite national economic upheaval throughout 2008, which unfortunately was reaching perfect-storm status during the 2008 MLGW/IBEW Local 1288 United Way campaign of Nov. 3-14, 2008, the commitment of MLGW employees to the community with their tough-minded approach to solving problems raised approximately $780,000 for the community. MLGW ranks 6th among the top 10 largest companies in the Mid-South in terms of donations to United Way, which are solely from employee contributions.

AC, fan donations

There’s not much we can do about the weather in Memphis—and it does fluctuate wildly. But we can do something to help those senior members of our community endure those legendary hot days of summer in Memphis. MLGW donated fans to the Aging Commission, which distributed those items to customers in need. MLGW also donated and installed window unit air conditioners to needy customers.

OK, Listen up!

This is Samuel L. Jackson and I want to talk to you about energy conservation. If your idea of energy conservation is sitting in a hammock underneath a tree, then I’m talking to you!

I want you to weatherstrip around windows and doors. Use compact fluorescent light bulbs. Repair leaky faucets and toilets. Don’t waste energy!

Don’t make me come to your house to inspect it. Call 544-MLGW for energy conservation tips. Or go to www.mlgw.com and tell them Samuel L. Jackson sent you.
Conservation for low and equitable rates

The 15-percent water rate increase passed in late 2007 was delayed with customers in mind. The increase went into effect with meters read after June 26, 2008. Despite the necessary increase, it added only about $1.71 on the typical residential customer bill.

In 2008 MLGW continued its conservation efforts seeking lower costs and a better product for the community. The 2008 Utility Bill Comparisons for Selected U.S. Cities: Electricity, Natural Gas, Water, and Wastewater showed that MLGW customers are fortunate to have the seventh-lowest residential utility bill compared to customers in 49 selected cities across the nation, including all major cities in Tennessee. In 2008, MLGW customers enjoyed a temporary electric rate decrease.

A 2008 Jacksonville Florida Energy Authority (JEA) survey of residential electric rates from 55 public and private utilities shows 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.

MLGW customers’ water and wastewater rates were found to be the lowest among 28 other similar-sized utilities according to a 2008 rate comparison conducted by Austin Water Utility in Austin, Texas. The Austin comparison study reviewed retail water and wastewater bills for customers within respective service areas of 28 selected cities.
Mr. Collins,

I reside on Cherokee Drive in Chickasaw Gardens. On March 1, we experienced intermittent power outages. I realized there might be a problem with my service. I reported this at a little after 10 p.m. on the automatic line. At 10:30, I received a return call asking for details. The woman said she’d try to get someone out immediately, but that the department closed at 11. I was thrilled when a few minutes later, a serviceman showed up. He found very loose bolts attaching the meter to the wires, tightened them and said “that should fix the problem.”

Thanks,
Herman P. Markell
Conservation means being more efficient for our customers

At MLGW, our policies and practices are designed with the customer in mind. We have many different types of customers, including private residents, landlords, large industrial customers, and small retail business owners. All of our customers, however, have similar wants and needs from MLGW. They all want low rates, consistent and fair credit and billing policies, responsive service, and protective stewardship of their utility infrastructure and resources.

To combat the potential monetary impact the 2008 TVA increase would have upon its customers, MLGW stepped up its efforts in 2008 to educate customers about how they can reduce their energy consumption. Energy-saving tips were placed on the MLGW Web site, and a new online bill analysis tool allows customers to receive detailed reports about their energy usage. MLGW’s new blog at www.mlgw.blogspot.com features in-depth discussion of conservation practices. MLGW and TVA increased the availability of EnergySmart Memphis conservation workshops for local neighborhood associations.
Conservation to protect our valuable resources

MLGW crews found themselves responding to two major storms in one week’s time at the beginning of 2008. The first storm began on the afternoon of January 29, with 60 mph winds causing extensive damage and outages throughout Shelby County. At the height of the outage as many as 60,000 customers were without power. Tornadoes ripped through the community one week later on February 5, causing power outages and extensive damage to poles, lines, and Electric Substation 71 (which serves much of the Hickory Hill area). During both storms, crews worked long hours to restore power to our customers and to repair the utility infrastructure, damage to which was estimated at $6.5 million.

MLGW’s newest electric substation—Substation 85—was dedicated with a ribbon cutting on Friday, Oct. 3. It currently serves approximately 8,000 customers in the Lakeland, Bartlett and Cordova areas, with the potential to serve a total of 27,000 customers. The lower-voltage section of the station is contained entirely in a state-of-the-art metal-clad switchgear complex, which reduces square footage of land required by nearly one-third. Nearly every piece of equipment at the station can be operated by remote control using fiber-optic communication cables from System Operations, which speeds up any restoration efforts.

In 2008, every commercial, industrial, and residential water customer was mailed MLGW’s 2007 Water Quality Report. This report presents the latest data confirming the superior quality of Memphis’ drinking water in addition to information on how the water MLGW distributes to its customers meets and/or exceeds all federal and state safety standards.

MLGW has had an alternative fuel strategy since 1995, and still possesses 60 natural-gas powered vehicles. But automakers have reduced the number of natural-gas powered vehicles that they manufacture. In 2008, MLGW purchased 24 pickups and 11 sedans that are fueled by a mixture of ethanol and gasoline. Since August 2007, MLGW has been using biodiesel fuel, as well.
Programs help customers monitor their conservation efforts

**MLGW Blog**

In 2008 MLGW increased its communication efforts with the greater community by launching its first blog site called ‘Bird on a Wire.’ Internet users now can visit www.mlgw.blogspot.com to catch up on the latest happenings at MLGW and engage in a written discourse with other bloggers about conservation issues.

**MLGW.com**

More of our customers now prefer to conduct their business with MLGW online. In 2008, we developed a new, more user-friendly main page at MLGW’s Web site, mlgw.com. The new features allow for quick customer access of utility information. A real-time outage map incorporates Google Maps, which uses a zoom application that allows for more specific outage locations. The new map also features a graph that displays an approximate range of the number of customers who are currently experiencing an outage. The new My Account feature enables our customers to receive their utility bills electronically and provides free access to their billing history.

**Customer Care Policy Enhancements**

The MLGW credit policy, renamed the Customer Care Policy, was completely revisited in 2008 to transform it into a more customer-friendly document. Changes were made to several areas, including deposits, definition of good pay customers, discount allowances, cutoffs, and deferred payment plans. In early 2008 more customers became eligible for Net Pay and SmartPay, two programs that provide alternative billing arrangements to pay their utility bills.

**EnergySmart Memphis**

MLGW is becoming extremely aggressive in teaching its customers how to save, from offering energy tips on bills and bill inserts, as well as designating more than $1 million in funds and services to the EnergySmart Memphis program, which teaches customers how to perform simple weatherization projects around the home and provides the materials to do so.

**Bill Enhancements**

Customers’ 2008 utility bills began to incorporate several enhancements. Residential bills incorporated a new Consumption Summary, comparing the current month’s electric, gas and water consumption to the previous month and the same month from the year prior. The meter reader on-site information was moved to the top of the bill for both Commercial and Residential bills.
Letter of Transmittal
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, 2008, 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, 2008 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, 2008, 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.

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 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 – Memphis, Tennessee, located in Shelby County in the southwest corner of Tennessee on the Mississippi River, is the nation’s 18th largest city. The MLGW service area comprises all of Shelby County, which in 2008 reported a population of 906,825. The eight-county Memphis Metro area provides a diverse range of employers, which contributes to the overall stability of the area.

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 fourth largest inland port in the United States. Home to major hubs for FedEx and UPS; world headquarters for Federal Express and a major thoroughfare for the trucking industry, Memphis is a vital epicenter of commerce. MLGW works diligently to maintain reliable power for these operations to ensure they run smoothly.

National Economy – Costs for electricity and natural gas remained volatile throughout 2008, mirroring a national economic rollercoaster of price rises and falls not seen in the United States since the Great Depression. 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. In early 2008 the Department of Energy predicted a significant percentage increase in natural gas costs for customers in the Southern region for the 2008-09 winter, at times predicting as much as a 30 percent cost increase over winter 2007-08. Predictions later in the year showed the volatility of natural gas prices throughout 2008. Percentage increases over winter 2008-09 for customers in the southern region averaged only around 1.6 percent by the end of December 2008.

In addition to the falling of natural gas costs at the end of 2008, another piece of encouraging news for MLGW customers came in the announcement that the Tennessee Valley Authority would cut electric rates by about 6 percent to account for lower fuel costs, starting January 1, 2009. The savings should equal about $4 to $8 a month per residential customer, depending on usage. The change reflected a 25 percent reduction in TVAs fuel cost charge, which is adjusted every three months. This would be the first decrease after three successive quarterly increases and would follow the 20 percent rate hike TVA enacted October 1, 2008.

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 eight 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 and will 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 and Corporate Communications department. 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 R. Collins Jr.
President and CEO

John McCullough
Vice President, CFO and Secretary-Treasurer
Financial Statements and Supplementary Information

Memphis Light, Gas and Water Division
Years ended December 31, 2008 and 2007
with report of Independent Auditors
INDEPENDENT AUDITORS' REPORT

To the Board of Commissioners and Management
Memphis Light, Gas and Water Division
Memphis, Tennessee

We have audited the accompanying balance sheets and the related statements of revenues, expenses and changes in net assets, and cash flows of the Electric, Gas and Water Divisions (the Divisions) of Memphis Light, Gas and Water Division, enterprise funds of the City of Memphis, Tennessee, as of and for the years ended December 31, 2008 and 2007, as listed in the table of contents. These financial statements are the responsibility of the Divisions' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Electric, Gas and Water Divisions of Memphis Light, Gas and Water Division and do not purport to, and do not, present fairly the financial position of the City of Memphis, Tennessee, as of December 31, 2008 and 2007, and the changes in its financial position, or, where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Electric, Gas and Water Divisions of Memphis Light, Gas and Water Division as of December 31, 2008 and 2007, and the changes in their financial position and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.
In accordance with *Government Auditing Standards*, we have also issued our report dated May 7, 2009, on our consideration of the Divisions' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

The management's discussion and analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of each of the Divisions. The introductory section and supplementary information as shown in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements. The supplementary information shown as the schedule of additions and retirements to utility plant; schedule of deposits and investments; schedule of long term debt, principal, and interest requirements; schedule of funding progress for OPEB; schedule of employer contributions; schedule of funding progress for pension plan; and schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and supplementary information shown as the schedule of current utility rates; schedule of insurance; and schedule of unaccounted for water have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Memphis, Tennessee
May 7, 2009
The following management discussion and analysis (MD&A) for Memphis Light, Gas and Water Division ("MLGW") is intended as an introduction and should be read in conjunction with the financial statements and the notes that follow this section.

Overview of the Financial Statements

MLGW’s financial statements are comprised of the Balance Sheets; the Statements of Revenues, Expenses, and Changes in Net Assets; the Statements of Cash Flows; and the accompanying Notes. This report also contains required supplementary information in addition to the basic financial statements.

MLGW is an Enterprise Fund of the City of Memphis, Tennessee. MLGW’s statements are provided to the City of Memphis and reformatted to conform to the City’s format for Enterprise Funds. The City of Memphis incorporates MLGW’s statements ending December 31 into its statements ending June 30.

By Charter, MLGW is required to account separately for its electric, gas, and water divisions. Costs are allocated to the three divisions in a manner that ensures results of operations and changes in financial position are presented fairly and consistently from year to year.

Bond Ratings

During June 2008, MLGW issued 2008 Electric System Revenue Refunding bonds which refunded the 2003B Series bonds. On June 13, 2008, the MLGW Electric Division Series 2002 and 2003A Revenue bonds received credit upgrades from Standard & Poor’s ("S&P"). S&P raised its rating on the 2002 Revenue bonds to AA+ from AA, and raised its rating on the 2003A Revenue bonds to AA+ from AA-. S&P also assigned AA+ rating to the Series 2008 Revenue bonds. Fitch assigned an AA rating to the Series 2008 Revenue bonds, and Moody’s assigned Aa2 to the Series 2008 bonds. The Water Division continues to hold the highest possible bond ratings which are Aaa from Moody’s Investors Service and AAA from S&P. The Gas Division currently has no debt that is credit rated. When issuing bond ratings, agencies typically look at financial operations, management practices, rates, and debt ratios. Higher ratings result in the ability to issue and refinance debt at lower interest costs than companies with lower ratings.

The following tables show MLGW bond ratings and debt administration for the Electric and Water Divisions in 2008:

**Figure 1: Bond Ratings and Debt Administration for Electric and Water Divisions**

<table>
<thead>
<tr>
<th>MLGW Bond Ratings</th>
<th>Debt Administration</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Electric</strong></td>
<td><strong>Outstanding Balance</strong></td>
</tr>
<tr>
<td>2002</td>
<td>AA+</td>
</tr>
<tr>
<td>2003A</td>
<td>AA+</td>
</tr>
<tr>
<td>2008</td>
<td>AA+</td>
</tr>
<tr>
<td><strong>Water</strong></td>
<td>AAA</td>
</tr>
</tbody>
</table>
Analysis of the Electric Division’s Balance Sheet

Condensed financial information comparing the Electric Division’s net assets for the past three fiscal years is presented below:

<table>
<thead>
<tr>
<th>FY06</th>
<th>FY07</th>
<th>Change</th>
<th>FY08 - FY07</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current assets (excluding restricted funds)</td>
<td>$468,684</td>
<td>$426,611</td>
<td>9.9%</td>
<td>$369,196</td>
</tr>
<tr>
<td>Restricted assets</td>
<td>56,149</td>
<td>54,577</td>
<td>2.9%</td>
<td>84,832</td>
</tr>
<tr>
<td>Other assets</td>
<td>11,552</td>
<td>11,988</td>
<td>-3.6%</td>
<td>16,147</td>
</tr>
<tr>
<td>Prepaid power costs - long-term</td>
<td>982,550</td>
<td>1,074,909</td>
<td>-8.6%</td>
<td>1,163,662</td>
</tr>
<tr>
<td>Utility plant</td>
<td>880,961</td>
<td>854,680</td>
<td>3.1%</td>
<td>801,033</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td><strong>2,399,896</strong></td>
<td><strong>2,422,765</strong></td>
<td><strong>-0.9%</strong></td>
<td><strong>2,434,870</strong></td>
</tr>
<tr>
<td>Current liabilities payable from current assets</td>
<td>295,185</td>
<td>249,485</td>
<td>18.3%</td>
<td>235,512</td>
</tr>
<tr>
<td>Current liabilities payable from restricted assets</td>
<td>32,846</td>
<td>31,076</td>
<td>5.7%</td>
<td>31,378</td>
</tr>
<tr>
<td>Long-term debt</td>
<td>1,014,310</td>
<td>1,113,829</td>
<td>-8.9%</td>
<td>1,211,158</td>
</tr>
<tr>
<td>Non-current liabilities</td>
<td>46,883</td>
<td>50,201</td>
<td>-6.6%</td>
<td>22,138</td>
</tr>
<tr>
<td><strong>Total liabilities</strong></td>
<td><strong>1,389,224</strong></td>
<td><strong>1,444,591</strong></td>
<td><strong>-3.8%</strong></td>
<td><strong>1,500,186</strong></td>
</tr>
<tr>
<td>Net assets:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Invested in utility plant, net of related debt</td>
<td>869,504</td>
<td>837,840</td>
<td>3.8%</td>
<td>778,989</td>
</tr>
<tr>
<td>Restricted</td>
<td>14,830</td>
<td>15,412</td>
<td>-3.8%</td>
<td>46,160</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>126,338</td>
<td>124,922</td>
<td>1.1%</td>
<td>109,535</td>
</tr>
<tr>
<td><strong>Total net assets</strong></td>
<td><strong>$1,010,672</strong></td>
<td><strong>$978,174</strong></td>
<td><strong>3.3%</strong></td>
<td><strong>$934,684</strong></td>
</tr>
</tbody>
</table>

**Assets**

At December 31, total assets were $2.4 billion, a decrease of $22.9 million (-0.9%) compared to fiscal year 2007. This decrease is due in part to a decrease in prepaid power cost by $92.4 million due to amortization (See Note 11). Current assets increased by approximately $42.1 million, due in part to higher levels of cash and current accounts receivable resulting from Tennessee Valley Authority (“TVA”) rate increases in April and October of 2008 passed through to retail customers. Restricted assets increased by $1.6 million primarily due to an increase in the accrual of medical benefits of $1.2 million.

At December 31, 2007, total assets were $2.4 billion. Total assets decreased by $12.1 million compared to December 31, 2006. This decrease is due in part to a decrease in prepaid power cost by $88.8 million due to amortization (See Note 11). Restricted assets decreased by $30.3 million due to the reduction of renewal and replacement funds used for capital construction expenses. The sale of Memphis Networx resulted in a $1.4 million decrease in other assets. This decrease was offset by an increase in current assets of $57.4 million.
Capital Assets and Construction Activities

The Electric Division had approximately $881.0 million in utility plant assets net of accumulated depreciation at December 31, 2008, an increase of 3.1% over fiscal year 2007. During 2008, the Electric Division expended $66.9 million on capital equipment purchases and construction activities, a decrease of $3.0 million (-4.3%) compared to fiscal year 2007. Major Electric Division construction expenditures included: substation and transmission projects ($21.3 million), extensions to serve new customers ($12.1 million), and street light and leased outdoor lighting installations ($7.8 million). Other significant Electric Division capital expenditures included the following: meters and equipment ($3.8 million), transformers ($2.7 million), a mainframe system replacement project ($2.2 million), transportation and power operated equipment ($2.0 million), and communication network equipment ($1.1 million).

The Electric Division had approximately $854.7 million in utility plant assets net of accumulated depreciation at December 31, 2007, an increase of 6.7% over fiscal year 2006. During 2007, the Electric Division expended $69.9 million on capital equipment and construction activities, an increase of 2.8% over fiscal year 2006. Major Electric Division construction expenditures included: extensions to serve new customers ($16.6 million), substation and transmission projects ($21.1 million), and street light and leased outdoor lighting installations ($8.5 million). Other significant Electric Division capital expenditures included: transformers ($7.0 million), meters and equipment ($2.8 million), transportation and power operated equipment ($2.4 million), communication network equipment ($1.9 million), a mainframe system replacement project ($1.1 million) and buildings and structures upgrades ($1.0 million).

Liabilities

Total liabilities were $1.4 billion at December 31, 2008 representing a decrease of $55.4 million as compared to December 31, 2007. This decrease is primarily the result of the payment of $99.5 million of long-term debt associated with prepaid power transactions and the reduction of liabilities related to the pollution remediation obligation (See Note 17). This decrease was offset by an increase in current liabilities as a result of the TVA rate increases in 2008.

For fiscal year 2007, total liabilities decreased by $55.6 million. This decrease was primarily the result of annual payments of long-term debt associated with the prepaid power transaction. This decrease was offset by an increase in current liabilities payable from current assets by $14.0 million due primarily to an increase in energy and demand charges from TVA. Current liabilities payable from restricted assets decreased by $0.3 million. Non-current liabilities increased by $28.1 million due primarily to recognition of the pollution remediation obligation.

Net Assets

At December 31, 2008, the Electric Division’s total assets exceeded total liabilities by $1.0 billion, an increase of $32.5 million, or 3.3%, from $978.2 million at December 31, 2007. Eighty-six percent of the net assets were related to utility plant, net of related debt (property, plant and construction work in progress). For fiscal year 2007, total net assets (total assets less total liabilities) increased by $43.5 million. This represents a 4.7% increase over total net assets compared to fiscal year 2006. Utility plant accounts for $58.9 million of the increase and unrestricted net assets attributes another $15.4 million to the increase in total net assets, offset by a $30.7 million decline in restricted net assets.

An adjustment was made to the beginning net assets balance for 2007. Also, restatements were made to non-current liabilities and unrestricted net assets. The adjustments made were related to the cost associated with the pollution remediation obligation per implementation of GASB Statement No. 49, Pollution Remediation Obligations (See Note 17).
Analysis of the Electric Division’s Statement of Revenues, Expenses, and Changes in Net Assets

Condensed financial information comparing the Electric Division’s revenues, expenses, and changes in net assets for the past three fiscal years is presented below:

### Table 2
Electric Division
Condensed Statements of Revenues, Expenses, and Changes in Net Assets
(In Thousands)

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
<th>FY08 - FY07 Percentage Change</th>
<th>2007</th>
<th>FY07 - FY06 Percentage Change</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenues:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating revenues</td>
<td>$1,214,046 $1,128,491</td>
<td>7.6%</td>
<td>$1,092,979 $87,273</td>
<td>3.2%</td>
<td></td>
</tr>
<tr>
<td>Non-operating revenues</td>
<td>82,712 $88,905</td>
<td>-7.0%</td>
<td>72,490 $6,905</td>
<td>1.9%</td>
<td></td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td>1,296,758 $1,217,396</td>
<td>6.5%</td>
<td>1,180,252 $37,144</td>
<td>3.1%</td>
<td></td>
</tr>
<tr>
<td><strong>Expenses:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation expense</td>
<td>40,018 $37,183</td>
<td>7.6%</td>
<td>32,645 $4,538</td>
<td>13.9%</td>
<td></td>
</tr>
<tr>
<td>Purchased power</td>
<td>991,866 $878,396</td>
<td>12.9%</td>
<td>846,441 $45,925</td>
<td>5.3%</td>
<td></td>
</tr>
<tr>
<td>Other operating expense</td>
<td>152,270 $146,871</td>
<td>3.7%</td>
<td>143,996 $9,875</td>
<td>2.0%</td>
<td></td>
</tr>
<tr>
<td>Non-operating expense</td>
<td>45,843 $48,548</td>
<td>-5.6%</td>
<td>52,662 $7,113</td>
<td>14.0%</td>
<td></td>
</tr>
<tr>
<td><strong>Total expenses</strong></td>
<td>1,229,997 $1,110,998</td>
<td>10.7%</td>
<td>1,075,744 $45,254</td>
<td>3.3%</td>
<td></td>
</tr>
<tr>
<td><strong>Income (loss) before contributions in aid of construction and transfers</strong></td>
<td>66,761 $106,398</td>
<td>-37.3%</td>
<td>104,508 $37,144</td>
<td>3.5%</td>
<td></td>
</tr>
<tr>
<td>Contributions in aid of construction</td>
<td>11,675 $15,776</td>
<td>-26.0%</td>
<td>22,726 $7,950</td>
<td>-32.6%</td>
<td></td>
</tr>
<tr>
<td>Reduction of plant costs recovered through contributions in aid of construction</td>
<td>(11,675) (15,776)</td>
<td>26.0%</td>
<td>(22,726) (5,950)</td>
<td>30.6%</td>
<td></td>
</tr>
<tr>
<td><strong>Transfers to City</strong></td>
<td>(34,263) (37,397)</td>
<td>-8.4%</td>
<td>(34,141) (2,256)</td>
<td>9.5%</td>
<td></td>
</tr>
<tr>
<td><strong>Change in net assets</strong></td>
<td>32,498 $69,001</td>
<td>-52.9%</td>
<td>70,367 $31,366</td>
<td>-1.9%</td>
<td></td>
</tr>
<tr>
<td><strong>Beginning net assets</strong></td>
<td>978,174 $934,684</td>
<td>4.7%</td>
<td>864,317 $1,767</td>
<td>0.2%</td>
<td></td>
</tr>
<tr>
<td>Adjustments to beginning net assets, as previously reported</td>
<td>- (25,511)</td>
<td>-100.0%</td>
<td>- -</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td><strong>Beginning net assets as adjusted</strong></td>
<td>978,174 $909,173</td>
<td>7.6%</td>
<td>864,317 $34,856</td>
<td>5.2%</td>
<td></td>
</tr>
<tr>
<td><strong>Ending net assets</strong></td>
<td>$1,010,672 $978,174</td>
<td>3.3%</td>
<td>$934,684 $56,500</td>
<td>4.7%</td>
<td></td>
</tr>
</tbody>
</table>

At December 31, 2008, the change in net assets decreased by $36.5 million to $32.5 million, a decrease of 52.9% compared to 2007. A one-year temporary rate reduction in 2008 accounted for the majority of the decrease. The change in net assets decreased by $1.4 million (-1.9%) to $69.0 million at December 31, 2007 from $70.4 million at December 31, 2006.

For fiscal year 2008, total revenues were $1.3 billion, an increase of 6.5% over fiscal year 2007. Operating revenues were $1.2 billion in 2008, increasing by $85.6 million over 2007. Wholesale rate adjustments increased sales and service revenues by $85.0 million, despite a 3.5% decrease in 2008 electricity sales. There was a corresponding increase in purchased power cost of $113.5 million. Other operating revenue increased by $0.5 million in 2008 as a result of a $0.5 million increase in rent from property. Non-operating revenues decreased by 7.0% in 2008 as a result of a decrease in investment income.
Total revenues were $1.2 billion for fiscal year 2007, an increase of 3.1% over fiscal year 2006. Operating revenues were $1.1 billion in 2007, an increase of $35.5 million. TVA’s wholesale rate adjustments effective January 1, 2007, April 1, 2007, July 1, 2007 and October 1, 2007 were passed through to retail customers. This, combined with an increase of electricity sales of 3.2% over 2006, increased sales and service revenues by $28.2 million. There was a corresponding increase in purchased power cost of $32.0 million. Other operating revenue increased $7.3 million in 2007 resulting primarily from a $4.0 million increase in miscellaneous service revenue and a $2.7 million increase in rent from property. Non-operating revenue increased by 1.9% in 2007 as a result of increases in the TVA Transmission Credit and investment income.

Figure 2: Electric Division’s Operating Revenue

For fiscal year 2008, total expenses were $1.2 billion, an increase of 10.7% compared to 2007. This increase resulted from a 12.9% increase in purchased power costs, a 7.6% increase in depreciation expense, and a 3.7% increase in other operating expenses. The overall increase in total expenses was slightly offset by a 5.6% decrease in non-operating expenses resulting from the continuing decline in interest expense on long-term debt from Electric Prepay Bonds.

Total expenses were $1.1 billion for fiscal year 2007, an increase of 3.3% compared to 2006. The increase was primarily a result of a 3.8% increase in purchased power costs, a 13.9% increase in depreciation expense, and a 2.0% increase in other operating expenses. The higher-than-normal increase in depreciation expense was due to the ownership transfer of the Customer Information System (“CIS”) asset from the Gas Division to the Electric Division in June 2007. The overall increase in total expenses was slightly offset by a 7.8% decrease in non-operating expenses that resulted from the continuing decline in interest expense on long-term debt from Electric Prepay Bonds.

Contributions in aid of construction (“CIAC”) were $11.7 million in 2008, a decrease from 2007 of $4.1 million (-26.0%) as a result of decline in development and construction activity. In 2007, CIAC were $15.8 million; this represents a decrease of $7.0 million from $22.7 million in 2006. CIAC were lower in 2007 as a result of lower construction activity by developers, reduced highway construction and utility relocation required by the State of Tennessee.
MLGW’s transfer to the City of Memphis is based on the formula provided by the State of Tennessee Municipal Electric System Tax Equivalent Law of 1987. The formula includes a property tax equivalency calculation plus 4% of operating revenue less power costs (three-year average). Transfers to the City represent the Electric Division’s in lieu of tax payment of $34.3 million in 2008. This amount represents an 8.4% decrease compared to 2007, with 2007 being 9.5% higher than 2006. The $3.1 million decrease in 2008 can be attributed to a change in tax rates. In 2007, Transfers to the City were $37.4 million. This represents a $3.3 million increase over 2006 primarily due to an increase in net plant.

Analysis of the Gas Division’s Balance Sheet

Condensed financial information comparing the Gas Division’s net assets for the past three fiscal years is presented below:

<table>
<thead>
<tr>
<th></th>
<th>FY 08</th>
<th>FY 07</th>
<th>Change</th>
<th>FY 06</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current assets (excluding restricted funds)</td>
<td>$194,417</td>
<td>$178,158</td>
<td>9.1%</td>
<td>$170,969</td>
<td>4.2%</td>
</tr>
<tr>
<td>Restricted assets</td>
<td>35,639</td>
<td>33,260</td>
<td>7.2%</td>
<td>30,423</td>
<td>9.3%</td>
</tr>
<tr>
<td>Other assets</td>
<td>12,435</td>
<td>13,622</td>
<td>-8.7%</td>
<td>15,354</td>
<td>-11.3%</td>
</tr>
<tr>
<td>Utility plant</td>
<td>294,643</td>
<td>295,424</td>
<td>0.3%</td>
<td>323,338</td>
<td>-8.6%</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td>$537,134</td>
<td>$520,464</td>
<td>3.2%</td>
<td>$540,084</td>
<td>-3.6%</td>
</tr>
<tr>
<td>Current liabilities payable from current assets</td>
<td>$103,528</td>
<td>$116,036</td>
<td>-10.8%</td>
<td>$123,764</td>
<td>-6.2%</td>
</tr>
<tr>
<td>Current liabilities payable from restricted assets</td>
<td>7,980</td>
<td>7,046</td>
<td>13.3%</td>
<td>7,364</td>
<td>-4.3%</td>
</tr>
<tr>
<td>Non-current liabilities</td>
<td>14,796</td>
<td>16,708</td>
<td>-11.4%</td>
<td>13,356</td>
<td>25.1%</td>
</tr>
<tr>
<td><strong>Total liabilities</strong></td>
<td>$126,304</td>
<td>$139,790</td>
<td>-9.6%</td>
<td>$144,484</td>
<td>-3.2%</td>
</tr>
<tr>
<td>Net assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Invested in utility plant, net of related debt</td>
<td>$294,643</td>
<td>$295,424</td>
<td>0.3%</td>
<td>$323,338</td>
<td>-8.6%</td>
</tr>
<tr>
<td>Restricted</td>
<td>24,150</td>
<td>22,566</td>
<td>7.0%</td>
<td>19,346</td>
<td>16.6%</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>92,037</td>
<td>62,684</td>
<td>46.8%</td>
<td>52,916</td>
<td>18.5%</td>
</tr>
<tr>
<td><strong>Total net assets</strong></td>
<td>$410,830</td>
<td>$380,674</td>
<td>7.9%</td>
<td>$395,600</td>
<td>-3.8%</td>
</tr>
</tbody>
</table>

**Assets**

Total assets increased by $16.7 million to $537.1 million for fiscal year 2008 as compared to $520.5 million for fiscal year 2007. The increase in total assets is a reflection of an 8.8% increase in current and restricted assets due to an increase in accounts receivable because of lower cash receipts and also an increase in the inventory of stored gas. This increase was offset by a decrease in other assets by 8.7% and utility plant by 0.3%.

At December 31, 2007, total assets were $520.5 million; this represents a decline of 3.6% compared to December 31, 2006. The reduction in total assets is a reflection of an 11.3% decrease in other assets due to a decrease in notes receivable related to a pipeline lease and an 8.6% decrease in utility plant due to the sale of the CIS to the Electric...
Division. This decrease was partially offset by an increase in current assets by 4.2% attributable to less funding to margin accounts, an increase in restricted assets by 9.3%, and an increase in cash available and investments as a result of the sale of the CIS to the Electric Division.

Capital Assets and Construction Activities

The Gas Division had approximately $294.6 million in utility plant assets net of accumulated depreciation at December 31, 2008, a decrease of $0.8 million (-0.3%) from fiscal year 2007. During 2008, the Gas Division expended $14.4 million on capital equipment purchases and construction activities, resulting in an increase of $3.4 million, or 30.9%, in comparison to fiscal year 2007. The Gas Division’s major construction expenditures included: extensions to serve new customers ($2.5 million) and a cast iron pipe replacement project ($2.3 million). A substantial portion of the Gas Division capital expenditures were related to transportation and power operated equipment ($2.9 million), meters and equipment ($2.1 million), and buildings and structures upgrades ($1.9 million).

The Gas Division had approximately $295.4 million in utility plant assets net of accumulated depreciation at December 31, 2007 a decrease of $27.9 million from fiscal year 2006. This decrease included a transfer of the CIS from the Gas Division to the Electric Division at a net transfer of $22.5 million. During 2007, the Gas Division expended $11.0 million on capital equipment and construction activities, resulting in a decrease of 29.5% in comparison to fiscal year 2006. The Gas Division major construction expenditures included: extensions to serve new customers ($3.6 million) and a cast iron pipe replacement project ($2.1 million). A substantial portion of the Gas Division capital expenditures were related to transportation and power operated equipment ($1.5 million), meters and equipment ($1.4 million), and buildings and structures upgrades ($1.0 million).

Liabilities

At December 31, 2008, total liabilities were $126.3 million as compared to $139.8 million for fiscal year 2007, a decrease of 9.6%. Current liabilities payable from current assets were a major contributor to this decrease. Current liabilities payable from current assets decreased by $12.5 million (-10.8%) as a result of the decline in net storage withdrawals on the Texas Gas pipeline. Current liabilities payable from restricted assets increased due to an increase in accrued reserves for medical benefits and insurance reserves-injuries and damages. Decreased financial liabilities for the pollution remediation obligation and the Premcor Pipeline lease interest contributed to the decrease in non-current liabilities of $1.9 million (-11.4%).

For fiscal year 2007, total liabilities decreased to $139.8 million as compared to $144.5 million for fiscal year 2006. Current liabilities payable from current assets were a major contributor to this decrease. Current liabilities payable from current assets decreased by $7.7 million as a result of the decline in accounts payable for purchased gas due to less consumption because of to higher than normal temperatures (a mild December 2007). Total liabilities also decreased as a result of a decrease in other accounts payable, accrued expenses and other deferrals due primarily to a decrease in other deferred credits related to purchase gas adjustments. These declines were offset in part due to a $40.0 million note payable related to the purchase of natural gas for storage.

Net Assets

Total net assets (total assets minus total liabilities) for fiscal year 2008 increased by $30.2 million, or 7.9%, over fiscal year 2007. This increase was a result of an increase in operating revenue due to a 6.8% gas rate increase effective December 26, 2007. Over 72% of the net assets were related to utility plant, net of related debt (property, plant and construction work in progress). At December 31, 2007, total net assets were $380.7 million; this is a decrease of $14.9 million (-3.8%) as compared to December 31, 2006. Seventy-eight percent of these assets are related to property, plant, and construction work in progress (utility plant). Restricted net assets increased by $3.2
million, or 16.6%, due in part to an increase in the amount of funding for renewals and replacements. Unrestricted net assets increased by $9.8 million, or 18.5%, in part due to the increase in cash resulting from the sale of the CIS to the Electric Division.

An adjustment was made to the beginning net assets balance for 2007. Also, restatements were made to non-current liabilities and unrestricted net assets. The adjustments made were related to the cost associated with the pollution remediation obligation per implementation of GASB Statement No. 49, *Pollution Remediation Obligations* (See Note 17).

### Analysis of the Gas Division’s Statement of Revenues, Expenses, and Changes in Net Assets

Condensed financial information comparing the Gas Division’s revenues, expenses, and changes in net assets for the past three fiscal years is presented below:

<table>
<thead>
<tr>
<th></th>
<th>FY08 - FY07 Change</th>
<th>FY07 - FY06 Change</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenues:</strong></td>
<td>FY08 - FY07</td>
<td>FY07 - FY06</td>
</tr>
<tr>
<td>Sales, service and other operating revenues</td>
<td>$518,780</td>
<td>$438,930</td>
</tr>
<tr>
<td>Transported gas revenue</td>
<td>4,537</td>
<td>3,452</td>
</tr>
<tr>
<td>Non-operating revenues</td>
<td>3,785</td>
<td>5,876</td>
</tr>
<tr>
<td>Total revenues</td>
<td>527,102</td>
<td>448,258</td>
</tr>
<tr>
<td><strong>Expenses:</strong></td>
<td>FY08 - FY07</td>
<td>FY07 - FY06</td>
</tr>
<tr>
<td>Depreciation expense</td>
<td>12,377</td>
<td>13,286</td>
</tr>
<tr>
<td>Purchased gas</td>
<td>394,023</td>
<td>351,164</td>
</tr>
<tr>
<td>Other operating expense</td>
<td>76,570</td>
<td>79,161</td>
</tr>
<tr>
<td>Non-operating expense</td>
<td>1,149</td>
<td>720</td>
</tr>
<tr>
<td>Total expenses</td>
<td>484,119</td>
<td>444,331</td>
</tr>
<tr>
<td><strong>Income (loss) before contributions in aid of construction and transfers</strong></td>
<td>42,983</td>
<td>3,927</td>
</tr>
<tr>
<td>Contributions in aid of construction</td>
<td>1,568</td>
<td>1,839</td>
</tr>
<tr>
<td>Reduction of plant costs recovered through contributions in aid of construction</td>
<td>(1,568)</td>
<td>(1,839)</td>
</tr>
<tr>
<td>Transfers to City</td>
<td>(12,827)</td>
<td>(14,638)</td>
</tr>
<tr>
<td>Change in net assets</td>
<td>30,156</td>
<td>(10,711)</td>
</tr>
<tr>
<td><strong>Beginning net assets</strong></td>
<td>$380,674</td>
<td>$395,600</td>
</tr>
<tr>
<td>Adjustments to beginning net assets, as previously reported</td>
<td>-</td>
<td>(4,215)</td>
</tr>
<tr>
<td>Beginning net assets as adjusted</td>
<td>$380,674</td>
<td>$391,385</td>
</tr>
<tr>
<td><strong>Ending net assets</strong></td>
<td>$410,830</td>
<td>$395,600</td>
</tr>
</tbody>
</table>

Table 4
Gas Division
Condensed Statements of Revenues, Expenses, and Changes in Net Assets
(In Thousands)
At December 31, 2008, the change in net assets was $30.2 million. This represents an increase of $40.9 million, or 381.6%. This increase is primarily related to an increase in revenue from sales, service and other operating revenue as a result of an increase in both sales volume and gas rates. The change in net assets increased by $1.9 million, or 15.0%, to $-10.7 million at December 31, 2007 from $-12.6 million at December 31, 2006. This increase in net assets is attributable to a combination of a slight increase in natural gas sales of 1.4%, a substantial increase in non-operating revenues of 113.8%, and a considerable decrease in depreciation expenses by $1.9 million (-12.3%).

For fiscal year 2008, total revenues were $527.1 million, an increase of 17.6% compared to fiscal year 2007. There was an 18.2% increase in sales, service and other operating revenues in 2008, which can be attributed to a 9.8% increase in sales volume and the Division’s Gas Rate increase of 6.8% effective December 26, 2007. Transferred gas revenue increased by 31.4% in 2008 resulting from an 8.8% increase in volumes transported. A corresponding 12.2% increase in purchased gas cost occurred as a result of the increase in total sales volume. The 35.6% decrease in non-operating revenues is a result of a decrease in other income and investment income.

Total revenues were $448.3 million for fiscal year 2007, an increase of 2.9% over fiscal year 2006. There was a 2.3% increase in sales, service and other operating revenues in 2007, attributed to 0.6% increase in sales volume and higher wholesale gas prices. In addition, there was a corresponding increase in purchased gas cost. The 113.8% increase in 2007 non-operating revenues is attributed to interest earned from investments.

Figure 3: Gas Division’s Operating Revenue

For fiscal year 2008, total expenses increased to $484.1 million, an increase of 9.0% compared to 2007. The increase in total expenses resulted from a $42.9 million increase in purchased gas cost and was partially offset by a $0.9 million decrease in depreciation expense and a $2.6 million decrease in other operating expense. Total expenses increased to $444.3 million in 2007 from $432.7 million in 2006. This $11.7 million increase can be accredited to a $7.4 million increase in purchased gas, a $5.4 million increase in other operating expenses and offset in part by a $1.9 million decrease in depreciation expense.

In 2008, contributions in aid of construction decreased $0.3 million (-14.7%) to $1.6 million. This decrease was due to a reduction in construction activity during 2008.
MLGW’s transfer to the City of Memphis is based on the formula provided by the State of Tennessee Municipal Gas System Tax Equivalent Law of 1987. The formula includes a property tax equivalency calculation plus 4% of operating revenue less gas costs (three-year average). The Gas Division’s transfers to the City (in lieu of tax payments) were $12.8 million in 2008. This amount represents a decrease of $1.8 million compared to 2007. This decrease can be attributed to a change in tax rates. In 2007, transfers to the City decreased by $1.0 million as compared to 2006 as a result of a decline in net assets in the Gas division.

Analysis of the Water Division’s Balance Sheet

Condensed financial information comparing the Water Division’s net assets for the past three fiscal years is presented below:

<table>
<thead>
<tr>
<th>Table 5 Water Division Condensed Balance Sheets</th>
<th>FY08 - FY07 Percentage Change</th>
<th>FY07 - FY06 Percentage Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 08 - FY07 FY 07 - FY06</td>
<td>2008 As Restated</td>
<td>2007</td>
</tr>
<tr>
<td>Current assets (excluding restricted funds)</td>
<td>-17.0%</td>
<td>$ 33,882</td>
</tr>
<tr>
<td>Restricted assets</td>
<td>9.2%</td>
<td>26,529</td>
</tr>
<tr>
<td>Other assets</td>
<td>85.5%</td>
<td>2,501</td>
</tr>
<tr>
<td>Utility plant</td>
<td>0.5%</td>
<td>251,315</td>
</tr>
<tr>
<td>Total assets</td>
<td>-0.8%</td>
<td>314,227</td>
</tr>
<tr>
<td>Current liabilities payable from current assets</td>
<td>-14.4%</td>
<td>11,723</td>
</tr>
<tr>
<td>Current liabilities payable from restricted assets</td>
<td>18.5%</td>
<td>8,992</td>
</tr>
<tr>
<td>Long-term debt</td>
<td>-41.3%</td>
<td>4,546</td>
</tr>
<tr>
<td>Non-current liabilities</td>
<td>-25.1%</td>
<td>6,506</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>-15.8%</td>
<td>31,767</td>
</tr>
<tr>
<td>Net assets</td>
<td></td>
<td>Invested in utility plant, net of related debt</td>
</tr>
<tr>
<td>Restricted</td>
<td>5.0%</td>
<td>20,227</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>-7.9%</td>
<td>18,699</td>
</tr>
<tr>
<td>Total net assets</td>
<td>1.3%</td>
<td>$ 282,460</td>
</tr>
</tbody>
</table>

Assets

At December 31, 200, total assets were $314.2 million, a decrease of $2.4 million compared to $316.6 million at December 31, 2007. This decrease is the result of a decline in investments, cash and cash equivalents and collateral held in trust for securities. This decrease was offset by an increase in restricted assets due to increases in the construction funds and insurance reserves funds combined with an increase in utility plant.

Total assets for fiscal year 2007 increased by $3.8 million to $316.6 million, an increase of 1.2% compared to $312.9 million for fiscal year 2006. This change was due to an increase in utility plant of $4.1 million and an increase in current assets of $1.9 million due to investments. The increase in total assets was offset by a decline in restricted assets by $2.3 million due to a decrease in renewal and replacement funds.
Capital Assets and Construction Activities

The Water Division had approximately $251.3 million in utility plant assets net of accumulated depreciation at December 31, 2008, an increase of 0.5% over fiscal year 2007. During 2008, the Water Division expended $11.9 million on capital equipment purchases and construction activities, which was a decrease of $3.1 million (-20.7%) in comparison to fiscal year 2007. The Water Division’s major construction expenditures included: extensions to serve new customers ($2.2 million), relocation of facilities to accommodate road improvements ($1.2 million), upgrades to the Mallory Pumping Station ($1.0 million), upgrades to the Sheahan Pumping Station ($0.7 million), and upgrades to the Allen Pumping Station ($0.7 million). The Water Division equipment purchases included: data processing equipment ($2.0 million), meters ($1.0 million), and transportation and power operated equipment ($0.4 million).

The Water Division had approximately $250.2 million in utility plant assets net of accumulated depreciation at December 31, 2007, an increase of 1.7% over fiscal year 2006. During 2007, the Water Division expended $15.0 million on capital equipment purchases and construction activities, which was an increase of 30.4% in comparison to fiscal year 2006. The Water Division’s major construction expenditures included: extensions to serve new customers ($3.0 million), relocation of facilities to accommodate road improvements ($1.2 million), upgrades to the Sheahan Pumping Station ($0.7 million), and upgrades to the Morton Pumping Station ($0.6 million). The Water Division equipment purchases included: data processing equipment ($2.2 million), meters ($1.1 million), and transportation and power operated equipment ($0.6 million).

Liabilities

Total liabilities decreased by $6.0 million to $31.8 million for fiscal year 2008 as compared to fiscal year 2007. This is due to a decrease in current liabilities payable from current assets by $2.0 million primarily as a result of a decrease in securities lending of $1.1 million. Long-term debt decreased by $3.2 million primarily due to the amortization of Series 2001 and 1998 Revenue bonds. Non-current liabilities decreased by $2.2 million. This decrease is mainly a result of $1.4 million being expended on the pollution remediation liability. An increase in current liabilities payable from restricted assets of $1.4 million offset the decrease in total liabilities. Current liabilities from restricted assets increased due primarily to a $0.7 million increase in insurance reserves-injuries and damages and a $0.4 million increase in accrued medical benefits.

At December 31, 2007, total liabilities increased by $6.1 million compared to December 31, 2006. This increase is a result of an adjustment to beginning net assets due to the pollution remediation obligation (See Note 17).

Net Assets

Total net assets (total assets minus total liabilities) were $282.5 million for fiscal year 2008; this represents an increase of $3.6 million over fiscal year 2007. A $4.2 million increase in utility plant, net of related debt, contributed to this increase and was offset by a reduction in unrestricted assets as a result of the decline in liability associated with the pollution remediation obligation (See Note 17). Restricted Assets increased by $1.0 million as a result of an increase in insurance reserves-injuries, damages and insurance of $0.7 million and medical benefits of $0.4 million.

Total net assets (total assets minus total liabilities) decreased by $2.3 million to $278.9 million at December 31, 2007, representing a 0.8% decrease compared to December 31, 2006. This decrease is due mainly in part to the pollution remediation obligation which significantly decreased unrestricted net assets. This decrease was partially offset by a $7.0 million increase in utility plant, net of related debt (property, plant and construction work in progress) which represents approximately 85% of total net assets.
An adjustment was made to the beginning net assets balance for 2007. Also, restatements were made to non-current liabilities and unrestricted net assets. The adjustments made were related to the cost associated with the pollution remediation obligation per implementation of GASB Statement No. 49, *Pollution Remediation Obligations* (See Note 17).

**Analysis of the Water Division’s Statement of Revenues, Expenses, and Changes in Net Assets**

Condensed financial information comparing the Water Division’s revenues, expenses, and changes in net assets for the past three fiscal years is presented below:

<table>
<thead>
<tr>
<th></th>
<th>FY08 - FY07</th>
<th>FY07 - FY06</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Percentage</td>
<td>Percentage</td>
</tr>
<tr>
<td></td>
<td>Change</td>
<td>Change</td>
</tr>
<tr>
<td>Revenues:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating revenues</td>
<td>$80,741</td>
<td>$78,505</td>
</tr>
<tr>
<td>Non-operating revenues</td>
<td>1,692</td>
<td>2,670</td>
</tr>
<tr>
<td>Total revenues</td>
<td>$82,433</td>
<td>$81,175</td>
</tr>
<tr>
<td>Expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation expense</td>
<td>10,493</td>
<td>10,446</td>
</tr>
<tr>
<td>Other operating expense</td>
<td>65,470</td>
<td>63,471</td>
</tr>
<tr>
<td>Non-operating expense</td>
<td>420</td>
<td>557</td>
</tr>
<tr>
<td>Total expenses</td>
<td>$76,383</td>
<td>$74,474</td>
</tr>
<tr>
<td>Income (loss) before contributions in aid of construction and transfers</td>
<td>6,050</td>
<td>6,701</td>
</tr>
<tr>
<td>Contributions in aid of construction</td>
<td>4,589</td>
<td>5,094</td>
</tr>
<tr>
<td>Reduction of plant costs recovered through contributions in aid of construction</td>
<td>(4,589)</td>
<td>(5,094)</td>
</tr>
<tr>
<td>Transfers to City</td>
<td>(2,500)</td>
<td>(2,500)</td>
</tr>
<tr>
<td>Change in net assets</td>
<td>3,550</td>
<td>4,201</td>
</tr>
<tr>
<td>Beginning net assets</td>
<td>278,910</td>
<td>281,231</td>
</tr>
<tr>
<td>Adjustments to beginning net assets, as previously reported</td>
<td>-</td>
<td>(6,522)</td>
</tr>
<tr>
<td>Beginning net assets as adjusted</td>
<td>278,910</td>
<td>274,709</td>
</tr>
<tr>
<td>Ending net assets</td>
<td>$282,460</td>
<td>$278,910</td>
</tr>
</tbody>
</table>

The change in net assets was $3.6 million at December 31, 2008. This is a decrease of $0.7 million (-15.5%) compared to December 31, 2007. This decline is a result of the continued growth of expenses relative to revenue. The change in net assets decreased by 47.2%, or $3.8 million, from $8.0 million in 2006 to $4.2 million in 2007. During 2007, other operating expenses increased 8.3%. Additionally, depreciation expense for 2007 increased 6.6% over 2006.
For fiscal year 2008, total revenues were $82.4 million, an increase of $1.3 million, or 1.5%, over fiscal year 2007. Water sales decreased by 3.3% in 2008. Operating revenues increased by 2.8% in 2008 and is attributed to the Division’s 14.9% water rate increase effective June 26, 2008. Non-operating revenues decreased by $1.0 million in 2008 as a result of a decrease in interest earned on investments.

Total revenues were $81.2 million for fiscal year 2007, an increase of $1.6 million over fiscal year 2006. Water sales increased 4.2% from 2006. The growth in sales contributed $1.0 million to the increase in operating revenues. Non-operating revenues increased $0.6 million in 2007, which can be attributed to interest income from investments.

Figure 4: Water Division’s Operating Revenue

Total expenses for the Water Division in 2008 were $76.4 million, an increase of $1.9 million, or 2.6%, over fiscal year 2007. Other operating expenses increased by 3.1% from 2007, attributable to the effects of electric rate increases on production costs. Non-operating expense decreased 24.6% in 2008 as a result of the continuing decline in interest expense on long-term debt. Total expenses for the Water Division in 2007 were $74.5 million, representing a $5.4 million increase over 2006. This was the result of an increase in other operating expenses of $4.9 million and depreciation expense of $0.6 million that were partially offset by a decrease of $0.1 million in non-operating expenses.

For fiscal year 2008, contributions in aid of construction decreased by 0.5 million to $4.6 million.

Transfers to the City are per an agreement with the City of Memphis to provide payments in the amount of $2.5 million per year. The agreement is effective through the year 2028.

Additional Financial Information

This discussion is designed to provide MLGW’s customers, investors, and other interested parties with a general overview of the financial position and results of operations. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Manager of General Accounting, Memphis Light, Gas and Water Division, P.O. Box 430, Memphis, TN 38101, or call 901-528-4221.
## BALANCE SHEETS

(Dollars in Thousands)

**DECEMBER 31, 2008 AND 2007**

<table>
<thead>
<tr>
<th>Assets</th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current assets:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$ 119,657</td>
<td>$ 111,912</td>
<td>$ 26,295</td>
</tr>
<tr>
<td>Investments</td>
<td>57,026</td>
<td>49,038</td>
<td>11,090</td>
</tr>
<tr>
<td>Restricted funds - current</td>
<td>32,846</td>
<td>32,117</td>
<td>27,613</td>
</tr>
<tr>
<td>Accounts receivable, less allowance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>for doubtful accounts</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unbilled revenues</td>
<td>58,913</td>
<td>60,189</td>
<td>37,960</td>
</tr>
<tr>
<td>Prepaid power cost</td>
<td>92,155</td>
<td>88,783</td>
<td></td>
</tr>
<tr>
<td>Unrecovered purchased gas cost</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inventories</td>
<td>23,757</td>
<td>22,708</td>
<td>273</td>
</tr>
<tr>
<td>Collateral held in trust for securities on loan</td>
<td>20,096</td>
<td>24,996</td>
<td>17,078</td>
</tr>
<tr>
<td>Other current assets</td>
<td>3,068</td>
<td>2,353</td>
<td>23,846</td>
</tr>
<tr>
<td><strong>Total current assets:</strong></td>
<td>501,530</td>
<td>458,728</td>
<td>222,030</td>
</tr>
<tr>
<td><strong>Non-current assets:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Restricted funds:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Futures margin deposits</td>
<td></td>
<td></td>
<td>3,546</td>
</tr>
<tr>
<td>Construction</td>
<td>2,011</td>
<td>2,772</td>
<td>17,078</td>
</tr>
<tr>
<td>Insurance reserves - injuries and damages</td>
<td>6,969</td>
<td>7,250</td>
<td>20,247</td>
</tr>
<tr>
<td>Insurance reserves - casualties and general</td>
<td>14,830</td>
<td>14,372</td>
<td>14,372</td>
</tr>
<tr>
<td>Medical benefit</td>
<td>6,756</td>
<td>5,575</td>
<td>3,013</td>
</tr>
<tr>
<td>Customer deposits</td>
<td>13,889</td>
<td>13,260</td>
<td>5,462</td>
</tr>
<tr>
<td>Bond reserve and debt service</td>
<td>11,694</td>
<td>11,348</td>
<td></td>
</tr>
<tr>
<td><strong>Total restricted funds:</strong></td>
<td>56,149</td>
<td>54,577</td>
<td>35,639</td>
</tr>
<tr>
<td>Less restricted funds – current</td>
<td>(32,846)</td>
<td>(32,117)</td>
<td>(27,613)</td>
</tr>
<tr>
<td><strong>Restricted funds – non-current:</strong></td>
<td>23,303</td>
<td>22,460</td>
<td>8,026</td>
</tr>
<tr>
<td><strong>Other assets:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prepaid power cost – long term</td>
<td>982,550</td>
<td>1,074,909</td>
<td></td>
</tr>
<tr>
<td>Prepayments In Lieu of Taxes</td>
<td>1,444</td>
<td>1,450</td>
<td>463</td>
</tr>
<tr>
<td>Unamortized debt expense</td>
<td>7,333</td>
<td>7,874</td>
<td></td>
</tr>
<tr>
<td>Notes receivable</td>
<td>1,107</td>
<td>2,664</td>
<td>11,412</td>
</tr>
<tr>
<td>Other prepayments</td>
<td>1,668</td>
<td></td>
<td>560</td>
</tr>
<tr>
<td><strong>Total other assets:</strong></td>
<td>994,102</td>
<td>1,086,897</td>
<td>12,435</td>
</tr>
<tr>
<td>Utility plant</td>
<td>1,405,585</td>
<td>1,348,472</td>
<td>535,359</td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>(524,624)</td>
<td>(493,792)</td>
<td>(240,716)</td>
</tr>
<tr>
<td>Utility plant, net</td>
<td>880,961</td>
<td>854,680</td>
<td>294,643</td>
</tr>
<tr>
<td><strong>Total non-current assets:</strong></td>
<td>1,898,366</td>
<td>1,964,037</td>
<td>315,104</td>
</tr>
</tbody>
</table>

**Total assets**

$ 2,399,896 $ 2,422,765 $ 537,134 $ 520,464 $ 314,227 $ 316,627

See accompanying notes.
### BALANCE SHEETS
(Dollars in Thousands)
DECEMBER 31, 2008 AND 2007
(Continued)

#### Electric Division Gas Division Water Division

<table>
<thead>
<tr>
<th></th>
<th>2008 As Restated</th>
<th>2007 As Restated</th>
<th>2008 As Restated</th>
<th>2007 As Restated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liabilities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current liabilities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts payable - purchased power and gas</td>
<td>$146,342</td>
<td>$104,581</td>
<td>$44,957</td>
<td>$49,576</td>
</tr>
<tr>
<td>Other accounts payable, accrued expenses, and deferrals</td>
<td>$46,435</td>
<td>$41,670</td>
<td>$16,712</td>
<td>$15,910</td>
</tr>
<tr>
<td>Derivative Financial Instruments</td>
<td>−</td>
<td>−</td>
<td>$1,252</td>
<td>1,464</td>
</tr>
<tr>
<td>Bonds and notes payable</td>
<td>$81,976</td>
<td>$78,238</td>
<td>$35,000</td>
<td>$40,000</td>
</tr>
<tr>
<td>Collateral subject to return to borrowers</td>
<td>$20,432</td>
<td>$24,996</td>
<td>$5,607</td>
<td>$9,086</td>
</tr>
<tr>
<td>Total current liabilities payable from current assets</td>
<td>$295,185</td>
<td>$249,485</td>
<td>$103,528</td>
<td>$116,036</td>
</tr>
<tr>
<td>Current liabilities payable from restricted assets:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Construction</td>
<td>$2,011</td>
<td>$1,732</td>
<td>$991</td>
<td>$568</td>
</tr>
<tr>
<td>Customer deposits</td>
<td>$5,416</td>
<td>$5,171</td>
<td>$1,952</td>
<td>$2,209</td>
</tr>
<tr>
<td>Medical benefit accrual</td>
<td>$6,756</td>
<td>$5,575</td>
<td>$3,013</td>
<td>$2,655</td>
</tr>
<tr>
<td>Insurance reserves - injuries and damages</td>
<td>$6,969</td>
<td>$7,250</td>
<td>$2,024</td>
<td>$1,614</td>
</tr>
<tr>
<td>Bonds payable – accrued interest</td>
<td>$4,304</td>
<td>$4,274</td>
<td>−</td>
<td>−</td>
</tr>
<tr>
<td>Bonds payable – principal</td>
<td>$7,390</td>
<td>$7,074</td>
<td>−</td>
<td>−</td>
</tr>
<tr>
<td>Total current liabilities payable from restricted assets</td>
<td>$32,846</td>
<td>$31,076</td>
<td>$7,980</td>
<td>$7,046</td>
</tr>
<tr>
<td>Total current liabilities</td>
<td>$328,031</td>
<td>$280,561</td>
<td>$111,508</td>
<td>$123,082</td>
</tr>
<tr>
<td>Non-current liabilities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customer advances for construction</td>
<td>$9,747</td>
<td>$9,355</td>
<td>$1,159</td>
<td>$817</td>
</tr>
<tr>
<td>Customer deposits</td>
<td>$8,472</td>
<td>$8,088</td>
<td>$3,510</td>
<td>$3,649</td>
</tr>
<tr>
<td>Other</td>
<td>$28,664</td>
<td>$32,758</td>
<td>$10,127</td>
<td>$12,242</td>
</tr>
<tr>
<td>Long-term debt</td>
<td>$1,014,310</td>
<td>$1,113,829</td>
<td>$14,796</td>
<td>$16,708</td>
</tr>
<tr>
<td>Total non-current liabilities</td>
<td>$1,061,193</td>
<td>$1,164,030</td>
<td>$126,304</td>
<td>$139,790</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>$1,389,224</td>
<td>$1,344,591</td>
<td>$126,304</td>
<td>$139,790</td>
</tr>
<tr>
<td>Net assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Invested in capital assets, net of related debt</td>
<td>$869,504</td>
<td>$837,840</td>
<td>$294,643</td>
<td>$295,424</td>
</tr>
<tr>
<td>Restricted for debt service and construction</td>
<td>$14,830</td>
<td>$15,412</td>
<td>$24,150</td>
<td>$22,566</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>$126,338</td>
<td>$124,922</td>
<td>$92,037</td>
<td>$62,684</td>
</tr>
<tr>
<td>Total net assets</td>
<td>$1,010,672</td>
<td>$978,174</td>
<td>$410,830</td>
<td>$380,674</td>
</tr>
<tr>
<td>Total liabilities and net assets</td>
<td>$2,399,896</td>
<td>$2,422,765</td>
<td>$537,134</td>
<td>$520,464</td>
</tr>
</tbody>
</table>

See accompanying notes.
## STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
(Dollars in Thousands)
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

<table>
<thead>
<tr>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>As Restated</td>
<td>As Restated</td>
</tr>
<tr>
<td>Operating revenues:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales and service revenues</td>
<td>$1,183,386</td>
<td>$1,098,338</td>
</tr>
<tr>
<td>Transported gas revenue</td>
<td>$4,537</td>
<td>$3,452</td>
</tr>
<tr>
<td>Other revenues</td>
<td>30,660</td>
<td>30,153</td>
</tr>
<tr>
<td>Total operating revenues</td>
<td>1,214,046</td>
<td>1,128,491</td>
</tr>
<tr>
<td>Operating expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchased power and gas for resale</td>
<td>991,866</td>
<td>878,396</td>
</tr>
<tr>
<td>Production</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Operation</td>
<td>109,436</td>
<td>106,488</td>
</tr>
<tr>
<td>Maintenance</td>
<td>42,318</td>
<td>39,819</td>
</tr>
<tr>
<td>Depreciation</td>
<td>40,018</td>
<td>37,183</td>
</tr>
<tr>
<td>Payments in lieu of taxes</td>
<td>516</td>
<td>564</td>
</tr>
<tr>
<td>Total operating expenses</td>
<td>1,184,154</td>
<td>1,062,450</td>
</tr>
<tr>
<td>Operating income (loss)</td>
<td>29,892</td>
<td>66,041</td>
</tr>
<tr>
<td>Non-operating revenues (expenses):</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributions in aid of construction</td>
<td>11,675</td>
<td>15,776</td>
</tr>
<tr>
<td>Reduction of plant costs recovered through contributions in aid of construction</td>
<td>(11,675)</td>
<td>(15,776)</td>
</tr>
<tr>
<td>Transmission credits</td>
<td>26,493</td>
<td>24,897</td>
</tr>
<tr>
<td>Investment and other income</td>
<td>56,219</td>
<td>64,008</td>
</tr>
<tr>
<td>Interest expense</td>
<td>(45,843)</td>
<td>(47,899)</td>
</tr>
<tr>
<td>Telecommunications division loss</td>
<td>–</td>
<td>(649)</td>
</tr>
<tr>
<td>Total non-operating revenues (expenses)</td>
<td>36,869</td>
<td>40,357</td>
</tr>
<tr>
<td>Income before transfers</td>
<td>66,761</td>
<td>106,398</td>
</tr>
<tr>
<td>Transfer out</td>
<td>(34,263)</td>
<td>(37,397)</td>
</tr>
<tr>
<td>Change in net assets</td>
<td>$32,498</td>
<td>$69,001</td>
</tr>
</tbody>
</table>

Net assets, beginning of year | $978,174 | $934,684 | $380,674 | $395,600 | $278,910 | $281,231 |

Adjustments to beginning net assets, as previously reported | – | (25,511) | – | (4,215) | – | (6,522) |

Net assets, beginning of year as adjusted | $978,174 | 909,173 | $380,674 | 391,385 | $278,910 | 274,709 |

Change in net assets | 32,498 | 69,001 | 30,156 | 10,711 | 3,550 | 4,201 |

Net assets, end of year | $1,010,672 | $978,174 | $410,830 | $380,674 | $282,460 | $278,910 |

See accompanying notes.
## Statements of Cash Flows
(Dollars in Thousands)

FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

<table>
<thead>
<tr>
<th></th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cash flow from operating activities:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Receipts from customers and users</td>
<td>$ 1,201,126</td>
<td>$ 1,137,471</td>
<td>$ 513,242</td>
</tr>
<tr>
<td>Payments to suppliers</td>
<td>(859,377)</td>
<td>(785,296)</td>
<td>(446,989)</td>
</tr>
<tr>
<td>Payments to employees</td>
<td>(89,775)</td>
<td>(80,629)</td>
<td>(47,439)</td>
</tr>
<tr>
<td>Payments from (to) other Division funds</td>
<td>(313)</td>
<td>(2,103)</td>
<td>(972)</td>
</tr>
<tr>
<td>Payments for taxes</td>
<td>(480)</td>
<td>(510)</td>
<td>(197)</td>
</tr>
<tr>
<td>Other receipts (payments)</td>
<td>243</td>
<td>314</td>
<td></td>
</tr>
<tr>
<td><strong>Net cash provided (used) by operating activities</strong></td>
<td>251,424</td>
<td>269,247</td>
<td>17,645</td>
</tr>
</tbody>
</table>

| **Cash flows from noncapital financing activities:** |                   |              |               |               |
| Transfers to City       | (34,263)          | (37,397)     | (12,827)      | (14,638)      |
| Proceeds from issuance of long-term debt | 100,479           | 74,795       |               |               |
| Principal payments on long-term debt | (178,440)        | (15,986)     |               |               |
| Interest expense on bonds | (55,016)         | (57,731)     |               |               |
| Proceeds from issuance of notes payable | -                | 35,000       | 40,000        |               |
| Principal payment on notes payable | -                | -            | (40,000)      |               |
| Interest Expense on notes payable | -                | -            | (1,255)       |               |
| **Net cash provided (used) by noncapital financing activities**  | (167,240)         | (169,923)    | (19,082)      | 25,037        |

| **Cash flows from capital and related financing activities:** |                   |              |               |               |
| Purchase and construction of utility plant | (80,791)          | (84,789)     | (15,986)      | (12,447)      |
| Contributions in aid of construction | 11,675            | 15,776       | 1,568         | 1,839         |
| Sale(Purchase)of utility plant to/from other Divisions | (6)              | (22,474)     |               | 22,474        |
| Proceeds from issuance of long-term debt | -                | -            | -             | -             |
| Principal payments on long-term debt | (6,820)           | (6,548)      |               | (3,100)       |
| Interest expense on debt | (1,023)           | (1,295)      |               | (445)         |
| **Net cash provided (used) by capital and related financing activities**  | (76,965)          | (99,330)     | (14,419)      | 11,866        |

| **Cash flows from investing activities:** |                   |              |               |               |
| Sales and maturities of investments | 27,104            | 44,820       | 15,574        | 335           |
| Purchase of investments | (35,345)          | (39,621)     | (13,719)      | (14,659)      |
| Payments received on notes receivable | 1,708             | 1,709        | 1,944         | 1,967         |
| Issuance of notes receivable | -                | -            | -             | (795)         |
| Investment income earned on investments | 8,378            | 14,174       | 3,547         | 5,679         |
| Investment in Memphis Networx | -                | 355          | -             | -             |
| **Net cash provided (used) by investing activities**  | 1,845             | 21,437       | 7,346         | (6,678)       |

| Increase (decrease) in cash and cash equivalents | 9,064             | 21,431       | (8,510)       | 21,865        |
| Cash and cash equivalents, beginning of year | 159,049           | 137,618      | 62,813        | 40,948        |
| Cash and cash equivalents, end of year | $ 168,113         | $ 159,049    | $ 54,303      | $ 62,813      |

See accompanying notes.
STATEMENTS OF CASH FLOWS
(Dollars in Thousands)
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007
(Continued)

Reconciliation of operating income (loss) to net cash provided (used) by operating activities:

<table>
<thead>
<tr>
<th></th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating income (loss)</td>
<td>$ 29,892</td>
<td>$ 66,041</td>
<td>$ 40,347</td>
</tr>
</tbody>
</table>
| Adjustments to reconcile operating income (loss)  
| Depreciation of utility plant | 42,841  | 37,840   | 15,200 | 16,048 | 11,245  | 10,835  |
| Transmission credits | 26,493  | 24,897   | –      | –      | –      | –      |
| Prepay power credits | 44,542  | 46,574   | –      | –      | –      | –      |
| Other income | 3,367   | 2,887   | 155    | (55)   | 467    | 264    |
| (Increase) decrease in assets:  
| Accounts receivable | (27,380) | (4,883) | (25,212) | 14,010 | (1,815) | 617 |
| Unbilled revenues | 1,276   | (2,350) | 11,724 | 353    | 292    | 184    |
| Prepaid power cost | 88,987  | 85,841   | –      | –      | –      | –      |
| Prepayments – In Lieu of Taxes | 6       | 6      | 35     | 19     | –      | –      |
| Deferred purchase power and gas cost | –      | –      | 2,555  | (2,828) | –      | –      |
| Inventories | (1,049) | (5,773) | (6,750) | (10,319) | (130) | (63) |
| Other assets | (599)   | 1,131   | (15,161) | 14,724 | –      | –      |
| Increase (decrease) in liabilities:  
| Accounts payable - purchased power and gas | 41,761  | 10,872 | (4,619) | (12,054) | –      | –      |
| Other accounts payable and accrued expenses | 5,524   | 1,996   | 1,673  | (26,673) | (614) | 841 |
| Customer deposits | 629     | 1,301   | (396)  | (21)   | 29     | 25     |
| Insurance reserves | (281)   | 1,335   | 410    | 341    | 667    | (67)   |
| Medical benefit accrual | 1,181   | 1,253   | 358    | 351    | 444    | 344    |
| Other | (5,766) | 279     | (2,675) | (1,027) | (2,571) | 47     |
| Total adjustments | 221,532 | 203,206 | (22,702) | (7,131) | 8,014  | 13,027 |
| Net cash provided (used) by operating activities | $ 251,424 | $ 269,247 | $ 17,645 | (8,360) | $ 12,792 | $ 17,615 |

Reconciliation of cash and cash equivalents per statements of cash flows to the balance sheets:

<table>
<thead>
<tr>
<th></th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Restricted funds</td>
<td>$ 56,149</td>
<td>$ 54,577</td>
<td>$ 35,639</td>
</tr>
<tr>
<td>Less investments included in restricted funds</td>
<td>(7,693)</td>
<td>(7,440)</td>
<td>(7,631)</td>
</tr>
<tr>
<td>Cash and cash equivalents included in restricted funds</td>
<td>48,456</td>
<td>47,137</td>
<td>28,008</td>
</tr>
<tr>
<td>Current assets - cash and cash equivalents</td>
<td>119,657</td>
<td>111,912</td>
<td>26,295</td>
</tr>
<tr>
<td>Total cash and cash equivalents</td>
<td>$ 168,113</td>
<td>$ 159,049</td>
<td>$ 54,303</td>
</tr>
</tbody>
</table>

See accompanying notes.
1. Summary of Significant Accounting Policies

Organization

Memphis Light, Gas and Water Division ("MLGW"), a division of the City of Memphis, Tennessee (the "City"), was created by an amendment to the City Charter by Chapter 381 of the Private Acts of the General Assembly of Tennessee (the "Charter"), adopted March 9, 1939, as amended. MLGW is managed by its President and a five member Board of Commissioners that are nominated by the City Mayor and approved by the Memphis City Council (the "Council"). MLGW, through its three divisions, provides electricity, gas and water to customers in Shelby County, Tennessee, which includes the City. MLGW’s annual budget and electric, gas and water rates require the approval of the Council. MLGW must also obtain the approval of the Council before incurring certain obligations.

Basis of Presentation

The financial statements present only the Electric, Gas and Water Divisions of MLGW in conformity with accounting principles generally accepted in the United States that are applicable to a proprietary fund of a government unit. The accompanying financial statements present the separate financial positions, results of operations, and the cash flows of each of the three divisions—Electric, Gas and Water—(the Divisions) of MLGW, but do not present the financial position, results of operations, and the cash flows of MLGW, an enterprise fund of the City of Memphis. Accordingly, the accompanying disclosures relate separately to the Divisions, as applicable, and not collectively to MLGW. Unless expressly stated, each disclosure, including references to “MLGW” herein, applies solely to each of the separate divisions on an individual basis. These statements are not intended to present the financial position of the City, the results of the City’s operations and the cash flows of the City’s funds, nor do they represent the financial position, results of operations, or cash flows of MLGW’s Retirement and Pension System discussed in Note 5 and the Other Post-Employment Benefits ("OPEB") discussed in Note 7.

Basis of Accounting

MLGW is required by state statute and the Charter to maintain separate accounting for each division and to allocate among the divisions, on an equitable basis, joint expenses, including those related to common facilities. MLGW utilizes direct cost methods where applicable. For expenses not directly charged to a specific division, internally developed cost allocation methods are used based on the function performed. Each division is separately financed, and its indebtedness is repayable from its net revenues.

MLGW’s accounting policies are in conformity with accounting principles generally accepted in the United States. Where applicable, the Federal Energy Regulatory Commission’s (FERC) (Electric and Gas Divisions) and the National Association of Regulatory Utility Commissioners’ (NARUC) (Water Division) Uniform Systems of Accounts are used. MLGW is not subject to the jurisdiction of federal or state regulatory commissions. The Electric Division’s investment in Memphis Networx was regulated by the Tennessee Regulatory Authority until it was sold in July 2007. See Note 10.
1. Summary of Significant Accounting Policies (continued)

Basis of Accounting (continued)


Recent Accounting Standards

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. The objective of this statement is to establish accounting and financial reporting for intangible assets that will reduce inconsistencies among governments in the areas of recognition, initial measurement and amortization of intangible assets. This statement requires intangible assets not specifically excluded by its scope provisions be classified as capital assets. The requirements of this statement are effective for periods beginning after June 15, 2009 and should be applied retroactively to intangible assets acquired in fiscal years ending after June 30, 1980, except for those assets considered to have indefinite useful lives as of the effective date of this Statement and those that would be considered internally generated. MLGW has not completed the process of evaluating the impact of this statement on its financial statements. MLGW has not elected early implementation of this statement.

In June 2008, GASB issued GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. Statement 53 is intended to improve how state and local governments report information about derivative instruments—financial arrangements used by governments to manage specific risks or make investments—in their financial statements. The Statement specifically requires governments to measure most derivative instruments at fair value in their financial statements that are prepared using the economic resources measurement focus and the accrual basis of accounting. The guidance in this Statement also addresses hedge accounting requirements and is effective for financial statements for reporting periods beginning after June 15, 2009. MLGW has not elected early implementation of this statement, and does not believe it will have a material effect on the financial statements.

Regulatory Accounting

MLGW prepares its financial statements in accordance with the provisions of Statement of Financial Accounting Standards No. 71, *Accounting for the Effects of Certain Types of Regulation* (SFAS 71). In general, SFAS 71 recognizes that accounting for rate regulated enterprises should reflect the relationship of costs and revenues introduced by rate regulation. As a result, a regulated utility may defer recognition of a cost (a regulatory asset) or recognize an obligation (a regulatory liability) if it is probable that through the rate making process, there will be a corresponding increase or decrease in future revenues. Accordingly, MLGW has recognized certain regulatory assets and regulatory liabilities in the accompanying balance sheets. In the event operations are no longer subject to the provisions of SFAS 71
1. Summary of Significant Accounting Policies (continued)

Regulatory Accounting (continued)

as a result of a change in regulation or the effects of competition, MLGW would be required to recognize the effects of any regulatory change in assets or liabilities in its statement of revenues and expenses. The following are the regulatory assets and liabilities included on the balance sheets:

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gas Division</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deferred loss on futures/swaps</td>
<td>$21,019</td>
<td>$6,069</td>
</tr>
<tr>
<td>Unrecovered purchased gas cost</td>
<td>273</td>
<td>2,828</td>
</tr>
<tr>
<td><strong>Liabilities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gas Division</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deferred gains-gas futures/swaps</td>
<td>$-</td>
<td>$737</td>
</tr>
<tr>
<td>Deferred credits-PGA/storage</td>
<td>2,475</td>
<td>-</td>
</tr>
</tbody>
</table>

Use of Estimates

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Fair Value of Financial Instruments

The carrying amounts of cash and cash equivalents, investments, restricted fund investments, accounts receivable and accounts payable are a reasonable estimate of their fair values. The estimated fair values of MLGW’s other financial instruments have been determined by MLGW using available market information. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the fair values are not necessarily indicative of the amounts that MLGW could realize in a current market exchange. The use of different market assumptions may have a material effect on the estimated fair value amounts. The estimated fair value of long-term debt for the Electric Division and the Water Division based on quoted market prices is as follows as of December 31, 2008 and 2007:

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electric Division</td>
<td>$1,103,494</td>
<td>$1,192,861</td>
</tr>
<tr>
<td>Water Division</td>
<td>8,157</td>
<td>11,275</td>
</tr>
</tbody>
</table>
1. Summary of Significant Accounting Policies (continued)

Investments

Investments are carried at their fair value based on quoted market prices. See Note 2. All changes in the fair value of investments are included in investment income in the accompanying statements of revenues, expenses and changes in net assets.

Accounts Receivable

As of December 31, 2008 and 2007, accounts receivable and allowances for doubtful accounts were as follows:

<table>
<thead>
<tr>
<th></th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts receivable</td>
<td>$ 106,300</td>
<td>$ 77,978</td>
<td>$ 60,515</td>
</tr>
<tr>
<td>Less: Allowance for doubtful accounts</td>
<td>(12,288)</td>
<td>(11,346)</td>
<td>(2,568)</td>
</tr>
<tr>
<td>TOTAL</td>
<td>$ 94,012</td>
<td>$ 66,632</td>
<td>$ 57,947</td>
</tr>
</tbody>
</table>

MLGW performs a monthly analysis of outstanding trade receivables to assess the likelihood of collection. For aged receivable balances, MLGW records an allowance to adjust the trade receivable to MLGW’s best estimate of the amount it will ultimately collect. Such allowances are netted against operating revenues.

MLGW’s policy is to write off trade receivables after 120 days of non-payment. The bad debt expense amounts netted against operating revenues are as follows:

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electric</td>
<td>$ 10,813</td>
<td>$ 7,759</td>
</tr>
<tr>
<td>Gas</td>
<td>5,346</td>
<td>4,057</td>
</tr>
<tr>
<td>Water</td>
<td>1,235</td>
<td>924</td>
</tr>
</tbody>
</table>

Concentration of Credit Risk

MLGW’s financial instruments that are potentially exposed to concentrations of credit risk primarily consist of trade receivables. MLGW’s trade receivables result from its operations and include wholesale, commercial, industrial and government customers in the Memphis, Tennessee, geographic area. As a general policy, customer deposits are required for receivables unless or until the customer has established good credit history. Customers’ financial condition and credit worthiness are evaluated regularly.

Management of MLGW does not believe that it has a significant credit risk on its derivative instruments. MLGW’s derivatives transactions are mostly conducted directly or indirectly with the New York
1. Summary of Significant Accounting Policies (continued)

Concentration of Credit Risk (continued)

Mercantile Exchange ("NYMEX"). Using NYMEX largely minimizes MLGW’s exposure to credit risk for such transactions.

Prepaid Power Cost

Electric Division prepaid power cost represents the unamortized amount of prepaid power under the prepaid electricity agreement signed with Tennessee Valley Authority ("TVA") on November 19, 2003. See Note 11. Under the prepay agreement, MLGW issued revenue bonds with a face value of $1,392,170 and a premium of $121,247 to make an upfront payment of $1,500,000 to TVA. Under the terms of the agreement, MLGW receives a fixed discount on the monthly power purchased for the fifteen year term of the agreement. The total fixed discount under the agreement is sufficient to meet the debt service requirements and yield approximately $13,000 in annual power cost savings. The monthly fixed discount is allocated to prepaid power cost and other income under the interest method based on the debt service requirements of the associated debt.

Inventories

Inventories, consisting primarily of materials and supplies inventory and stored natural gas, are valued at the lower of cost or market using the average cost method.

Property

The costs of additions and replacements of units of property are capitalized. Costs include contracted work, direct labor and materials, allocable overhead and, where applicable, allowances for borrowed funds used during construction and are reduced by contributions in aid of construction. When property units are retired, original cost, plus removal cost, less salvage is charged to accumulated depreciation. The units of property adopted are related to those suggested by FERC for the Electric and Gas Divisions and NARUC for the Water Division, which allow for the reduction of plant cost recovered through contributions in aid of construction as opposed to recovery of costs through future regulatory rates.

An allowance for borrowed funds used during construction is computed at actual interest rates to the extent major projects are financed by specific long-term debt. In 2008 and 2007, no construction projects were financed with specific long-term debt. Interest on other debt is not capitalized as it is recovered through current revenues.

Depreciation is computed by the straight-line method based on estimated service lives of various classes of property at rates equivalent to annual composite rates of approximately 3% for the electric division, 2.4% for the gas division and 2.6% for the water division. Computations of the estimated service lives are the result of various depreciation studies and comparisons with industry standards.

For assets owned by one division, but jointly used by more than one division, the other divisions share the costs by paying rent to the owning division to cover depreciation, interest, in lieu of taxes, and transfers.
1. Summary of Significant Accounting Policies (continued)

Bond Premiums, Discounts and Issuance Costs

Bond premiums and discounts, as well as issuance costs, are deferred and amortized by the interest method over the lives of the applicable bond issues. Long-term debt is reported net of the applicable bond premium or discount. Bond issue costs are reported as deferred charges and amortized over the term of the related debt.

Reserves and Related Restricted Funds

Certain MLGW assets are restricted for specific purposes. Legal and contractual agreements restrict amounts for debt service, refund of customer deposits, futures margin requirements, and capital improvements while Board of Commissioners enacted provisions restrict funds for self-insurance and additional capital improvements. Restricted funds are first used for expenses when available, with the exception of the insurance reserve fund for casualties which is used at the discretion of management, depending on the severity of the catastrophe and the availability of funds.

The Gas Division maintains a cash margin account with its futures clearing member. The clearing member requires that a minimum cash margin be maintained based on the value of the Gas Division’s outstanding futures positions. The minimum cash margin requirements are considered restricted and are reflected in restricted assets in the accompanying balance sheets. The amounts of cash in excess of the minimum cash margin requirement are included in cash and cash equivalents.

Construction funds are maintained for the purpose of paying certain repairs and capital additions and improvements. The respective bond resolutions of the Electric, Gas and Water Divisions provide for funding for future construction. Additional construction funds are periodically authorized by the Board of Commissioners.

The insurance reserves for injuries and damages are maintained for estimated liabilities incurred and risks assumed on claims for injuries and damages and on recurring property losses. The insurance reserves for casualties are maintained at discretionary amounts to partially cover losses of a catastrophic nature which are not ordinarily insurable or which are not insurable on an economical basis. Since MLGW is self-insured for these liabilities, the Board of Commissioners has authorized the restriction of assets equal to the computed reserves.

Medical benefit reserves are maintained for MLGW’s medical insurance program, which serves employees and retirees. The medical benefit reserves represent the estimated costs incurred but not yet paid for in providing medical benefits to employees and retirees which are not insured by third party providers. Since MLGW is self-insured for these costs, the Board of Commissioners has authorized the restriction of assets equal to the computed reserves.

Customer deposit funds are maintained for the future repayment of deposits collected from customers without adequate credit history in accordance with MLGW’s policy and the respective customer service agreement.
1. Summary of Significant Accounting Policies (continued)

Reserves and Related Restricted Funds (continued)

Bond reserve and debt service funds are restricted under the terms of the respective bond indentures to pay current bond principal and interest as they become due.

Futures, Options and Swap Contracts

The Gas Division enters into futures contracts, swaps, and options on futures contracts to manage the risk of volatility in the market price of gas on anticipated purchase transactions. Open futures, swaps, and option on futures contracts as of December 31, 2008 and 2007, are reported at market values of ($1,252) and ($1,464) respectively. Notional values of the open futures as of December 31, 2008 and 2007 were $6,444 and $28,609, respectively. Margin account balances with MLGW’s New York Mercantile Exchange clearing member as of December 31, 2008 and 2007, were $6,610 and $7,411, respectively.

Because MLGW prepares its statements in accordance with Statement of Financial Accounting Standards No. 71, Accounting for the Effects of Certain Types of Regulation, gains or losses on futures contracts and swaps and option costs are included in deferred purchased gas costs until they are charged to gas costs through the purchased gas adjustment. Gains or losses on futures contracts entered into on behalf of specified customers are charged to that specific customer.

Deferred gains (losses) at year end associated with recording derivatives at fair market value were ($1,252) and ($1,464) for the years ending 2008 and 2007, respectively. Deferred costs at year end associated with gains (losses) on closed positions for the years ending 2008 and 2007 were ($19,762) and ($3,871) respectively.
1. Summary of Significant Accounting Policies (continued)

Net Assets

Net assets are classified into three components – invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

- Restricted net assets – This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), contributors, or laws or regulations of governments or constraints imposed by law through constitutional provisions or enabling legislation.

- Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

Revenues and Expenses

Revenues are recognized when earned. Customer meters are read and bills are rendered monthly. MLGW records an estimate for unbilled revenues earned from the dates its customers were last billed to the end of the month.

MLGW distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with an enterprise fund’s principal operations. The principal operating revenues of MLGW consist of electric, gas and water sales and related activities. Non-operating revenues consist of transmission credits, the non-power cost portion of the prepaid electricity discount, investment income and other ancillary activities. Transmission credits are fees paid by Tennessee Valley Authority for its use of the Electric Division’s power transmission facilities in supplying power to MLGW.

Operating expenses include the cost of purchased power and gas, water production costs, operation and maintenance expenses, depreciation on capital assets and payments in lieu of taxes. Expenses not meeting this definition are reported as non-operating expenses.

Investment and other income includes prepay credit income related to the prepaid power agreement with TVA of $44,542 and $46,574 for the years ended December 31, 2008 and 2007, respectively.
1. Summary of Significant Accounting Policies (continued)

Customer Deposits

Customers that do not have adequate credit history are required to make a utility deposit before services are provided. Deposits are refunded or applied toward the customer’s bill after a 24 month good pay status. Deposits are allocated to the Electric, Gas and Water Divisions based upon each division’s percentage of total sales revenue of the previous year end.

Statements of Cash Flows

MLGW considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents.

Related Parties

MLGW conducts business with its related parties as “arm’s length” transactions. Major related party entities include the City of Memphis government. Generally, MLGW provides utility and related services to these parties and receives payments in the same manner as other customers. For the years ending 2008 and 2007, receivables from related parties for utility construction, pole rentals and utility related services excluding utility bills were $5,404 and $4,445. The only free service provided to the City, under the Charter, is water for public purposes, such as Memphis City Schools and fire hydrants. The free water provided to the City is estimated to be $2,422 and $1,597 for 2008 and 2007, respectively.
2. Deposits and Investments

On September 17, 1998, revised on June 20, 2002, the MLGW Statement of Investment Policy was adopted and approved by the MLGW Board of Commissioners. The purpose of this policy is to set forth the investment and operational policies for the management of the public funds of MLGW. The Board of Commissioners has the power to invest and reinvest MLGW funds in accordance with the prudent investor rule. The Board members exercise authority and control over MLGW’s investment portfolio by setting policies which MLGW’s investment staff executes either internally, or through the use of external prudent experts.

Custodial Credit Risk

Deposits

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, MLGW will not be able to recover its deposits or will not be able to recover collateral securities that are in possession of an outside party. Deposits are exposed to custodial credit risk if they are not covered by depository insurance and are uncollateralized, collateralized with securities held by the pledging financial institution, or collateralized with securities held by the pledging financial institution’s trust department or agent but not in the depository-government’s name.

MLGW deposits include bank deposits and gas margin deposits. In accordance with MLGW’s Investment Policy: bank deposits are insured up to $250 by the Federal Deposit Insurance Corporation (“FDIC”) and the remainder is covered by the State of Tennessee Collateral Pool; certificates of deposit must be placed directly with depository institutions. The depository bank shall provide collateral for MLGW deposits in accordance with requirements for public funds deposits in Tennessee. The market value of the pledged securities in the collateral pool must equal at least 105% of the value of the deposit secured, less the amount protected by federal deposit insurance. As of December 31, 2008, MLGW deposits with financial institutions were $9,861 and gas margin deposits were $6,607. Of these, $9,861 were maintained in collateralized accounts or covered by federal depository insurance; therefore, they are not exposed to custodial credit risk and $6,607 were exposed to custodial credit risk as uninsured and uncollateralized.
2. Deposits and Investments (continued)

Investments

The investment policy governs the overall administration and investment management of the funds held in the MLGW investment portfolio. MLGW is authorized by the Board of Commissioners according to MLGW Charter Section 694 to invest in the following investments as authorized by state law and as it deems proper: U.S. Treasury; U.S. government obligations; repurchase agreements; commercial paper with specified ratings; bankers’ acceptances with specified ratings; corporate bonds/notes with specified ratings; municipal obligations with specified ratings; bank deposits; certificates of deposit; state pool; mutual funds with specified ratings; and asset-backed securities with specified ratings. MLGW is prohibited from investing in the following securities: purchases on margin or short sales; investment in reverse repurchase agreements; and “exotic” derivatives such as range notes, dual index notes, inverse floating rate notes and deleveraged notes, or notes linked to lagging indices or to long-term indices.

The following table presents the investments and maturities of MLGW’s investment portfolio as of December 31, 2008:

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Fair Value</th>
<th>Maturities</th>
<th>Remaining Maturities (in Years)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>&lt; 1 year</td>
<td>1 to 5 years</td>
</tr>
<tr>
<td>U.S. Treasuries</td>
<td>$ 3,181</td>
<td>-</td>
<td>$ 3,181</td>
</tr>
<tr>
<td>Federal Agency (Fixed Rate)</td>
<td>34,725</td>
<td>4,615</td>
<td>30,110</td>
</tr>
<tr>
<td>Federal Agency (Callable)</td>
<td>4,089</td>
<td>-</td>
<td>3,569</td>
</tr>
<tr>
<td>Corporate Bonds/Notes (medium term)</td>
<td>10,419</td>
<td>3,542</td>
<td>6,877</td>
</tr>
<tr>
<td>Asset - Backed Securities</td>
<td>10,866</td>
<td>-</td>
<td>10,866</td>
</tr>
<tr>
<td>Money Market Mutual Funds</td>
<td>238,401</td>
<td>238,401</td>
<td>-</td>
</tr>
<tr>
<td>Securities held by Brokers-Dealers under Securities Loans for Cash Collateral:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. Treasuries</td>
<td>19,129</td>
<td>3,086</td>
<td>16,043</td>
</tr>
<tr>
<td>Federal Agency (Fixed Rate)</td>
<td>3,278</td>
<td>1,928</td>
<td>1,350</td>
</tr>
<tr>
<td>Corporate Bonds/Notes (medium term)</td>
<td>5,782</td>
<td>500</td>
<td>5,282</td>
</tr>
<tr>
<td><strong>Total Investments</strong></td>
<td><strong>$ 329,870</strong></td>
<td><strong>$ 252,072</strong></td>
<td><strong>$ 77,278</strong></td>
</tr>
</tbody>
</table>

¹ $751 of these bonds mature in 2010; callable in 2009.
² $520 of these bonds mature in 2015; callable in 2010.
2. Deposits and Investments (continued)

Investments (continued)

Custodial credit risk for investments is the risk that, in the event of failure of the counterparty to a transaction, MLGW will not be able to recover the value of its investment or collateral securities that are in the possession of another party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government, and are held by either the counterparty, or the counterparty’s trust department or agent but not in the name of MLGW. Investments in external investment pools and in open-end mutual funds are not exposed to custodial credit risks because their existence is not evidenced by securities that exist in physical or book entry form. The underlying securities for securities on loan are not subject to custodial credit risk because the collateral for those loans is reported on the balance sheets. To limit its exposure, MLGW investment policy requires that all securities purchased by MLGW shall be held in safekeeping by a third-party custodial bank or financial institutions. Therefore, none of MLGW investments at December 31, 2008 were exposed to custodial credit risk.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment in debt securities. Generally, the longer the maturity of an investment the greater the sensitivity of its fair value to changes in market interest rates. MLGW’s investment policy does not limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. However, the investment policy states no investment will have a maturity of greater than five years from date of purchase, except U.S. Treasury Securities which shall have a maturity not to exceed ten years. MLGW uses the segmented time distribution method of disclosure to identify this risk. MLGW debt securities that were subject to interest rate risk were $27,067, or 8.2% of total investments. Of this amount $4,042 has a remaining maturity of one year or less.

Some investments can be highly sensitive to changes in interest rates due to their terms or characteristics. In MLGW’s investment portfolio, asset-backed and government mortgage backed securities are most sensitive to changes in interest rates as their repayments can vary significantly with interest rate changes. These securities represent 4.1% of the total investment portfolio with a fair market value of $13,475 at year-end 2008.

Credit Risk

Credit risk is the risk that an issuer of a debt security will not fulfill its obligation. This credit risk is measured by the credit quality of investments in debt securities as described by nationally recognized statistical rating organizations. Investments in obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk. To minimize credit risk, MLGW’s investment policy authorizes the purchases of commercial paper having a minimum rating of AA for long-term and A for short-term for corporations with senior long-term debt or A1 for corporations with no long-term debt rating; corporate bonds/notes having at least AA for long-term; bankers acceptances that are eligible for purchase by the Federal Reserve Bank and have a letter of credit.
2. Deposits and Investments (continued)

Credit Risk (continued)

rating of AA or better; mutual funds must have at least one of the two ratings: AAm or AAm-G; and asset-backed securities shall have a rating of Aaa by Moody’s or AAA by Standard and Poor’s. MLGW’s ratings and policy limits as of December 31, 2008 are as follows:

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Fair Value</th>
<th>S&amp;P Rating</th>
<th>Moody Rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate Bonds/Notes</td>
<td>$489</td>
<td>AA-</td>
<td>Aa1</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>10,337</td>
<td>AAA</td>
<td>Aaa</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>2,317</td>
<td>AA</td>
<td>Aa2</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>500</td>
<td>A+</td>
<td>Aa1</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>543</td>
<td>AA</td>
<td>Aa1</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>781</td>
<td>AA+</td>
<td>Aaa</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>542</td>
<td>AAA</td>
<td>Aa1</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>541</td>
<td>AA</td>
<td>Aa3</td>
</tr>
<tr>
<td>Corporate Bonds/Notes</td>
<td>151</td>
<td>AAA</td>
<td>NA</td>
</tr>
<tr>
<td>Asset-Backed Securities</td>
<td>10,866</td>
<td>AAA</td>
<td>Aaa</td>
</tr>
</tbody>
</table>

Total credit risk debt securities 27,067

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Fair Value</th>
<th>S&amp;P Rating</th>
<th>Moody Rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Treasuries</td>
<td>25,372</td>
<td>AAm</td>
<td>Aaa</td>
</tr>
<tr>
<td>U.S. Treasuries (explicitly guaranteed)</td>
<td>15,914</td>
<td>AAA</td>
<td>Aaa</td>
</tr>
<tr>
<td>Federal Agency (Fixed Rate)</td>
<td>213,029</td>
<td>AAm</td>
<td>Aaa</td>
</tr>
<tr>
<td>Federal Agency (Fixed Rate)</td>
<td>31,302</td>
<td>AAA</td>
<td>Aaa</td>
</tr>
<tr>
<td>Federal Agency (Fixed Rate)</td>
<td>1,058</td>
<td>AAAe</td>
<td>Aaa</td>
</tr>
<tr>
<td>Federal Agency (Fixed Rate - implicitly guaranteed)</td>
<td>516</td>
<td>AAAe</td>
<td>Aaa</td>
</tr>
<tr>
<td>Federal Agency (Callable)</td>
<td>4,089</td>
<td>AAA</td>
<td>Aaa</td>
</tr>
</tbody>
</table>

Total debt securities investments $329,870

<table>
<thead>
<tr>
<th>Non-Ratings Descriptions</th>
</tr>
</thead>
<tbody>
<tr>
<td>NA</td>
</tr>
<tr>
<td>NR</td>
</tr>
<tr>
<td>WR</td>
</tr>
</tbody>
</table>

¹ Money Market Treasury Fund primarily consists of U.S. Treasury securities.
² Government/Agency Money Market Fund primarily consists of U.S. government/agencies securities.
2. Deposits and Investments (continued)

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government’s investment in a single issuer. Investments in any one issuer that represent five percent or more of total investments must be disclosed by amount and issuer. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement. Of the investments subject to concentration of credit risk, there were no investments in any one issuer that represented 5% or more of MLGW’s investments on December 31, 2008.

In accordance with the investment policy, no more than 10% of MLGW’s portfolio will be invested in the securities of any single issuer with the following exceptions: U.S. Government Obligations 100%; and the amount invested in corporate bonds/notes will not exceed 5% of the portfolio book value for any single issuer. In addition, MLGW’s investment policy seeks to diversify its portfolio by limiting the percentage of the portfolio that may be invested in any one type of instrument as follows:

- U.S. Treasuries: 100% maximum
- Federal Agency (fixed rate): 100% maximum
- Federal Agency (callable): 50% maximum
- Repurchase Agreements: 50% maximum
- Commercial Paper (rated AA or higher): 90% maximum
- Bankers’ Acceptances (rated AA or higher): 60% maximum
- Corporate Notes (medium term): 15% maximum
- Certificates of Deposit: 20% maximum
- Municipal Obligations: 20% maximum
- Tennessee LGIP and Mutual Funds: 40% maximum
- Asset - Backed Securities: 50% maximum
2. Deposits and Investments (continued)

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. MLGW does not have a formal investment policy for foreign currency risk. As of December 31, 2008, MLGW had no investments that were denominated in foreign currencies; therefore, there is no foreign currency risk.

Securities Lending

MLGW has authorized The Northern Trust Company (“the Agent”) to enter into, on behalf of MLGW, securities lending transactions comprised of loans of securities to broker-dealers and other entities for collateral with a simultaneous agreement to return the collateral for the same securities in the future. Initial collateral levels, consisting of cash and securities, levels must be at least 102% of the market value of borrowed securities, or at least 105% if the borrowed securities and collateral are denominated in different currencies.

At December 31, 2008, MLGW has no credit risk exposure to borrowers because the amounts MLGW owe the borrowers exceed the amounts the borrowers owe MLGW. The borrower is required to deliver additional collateral when necessary so that the total collateral held by the Agent for all loans to the borrower will at least equal the market value of the securities without a borrower default. MLGW does not have the ability to pledge or sell collateral securities without a borrower default. MLGW is indemnified against any losses, damages, costs and expenses should the Agent be unable to recover borrowed securities and distributions due borrower filing for bankruptcy or similar relief or failure of the Agent to properly evaluate the creditworthiness of the borrower. In addition, MLGW is indemnified against loss should the Agent fail to demand adequate and appropriate collateral on a timely basis.

During fiscal year 2008, losses in the financial market affected the securities lending collateral pool held by The Northern Trust Company. The securities lending collateral pool has relatively high levels of overnight liquid and high-quality assets, but the unprecedented market events drove the markets into a highly illiquid condition. The impact of the highly illiquid market caused a decline in the market value of the securities lending collateral pool, resulting in a collateral deficiency declared on September 19, 2008. As of December 31, 2008, MLGW has an outstanding collateral deficiency liability of $476.
2. Deposits and Investments (continued)

Securities Lending (continued)

As of December 31, 2008, MLGW investments held by broker-dealers under securities loans consist of the following:

<table>
<thead>
<tr>
<th>Securities on Loan</th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Agencies</td>
<td>2,314</td>
<td>635</td>
<td>329</td>
<td>3,278</td>
</tr>
<tr>
<td>U.S. Corporate Fixed</td>
<td>4,082</td>
<td>1,121</td>
<td>579</td>
<td>5,782</td>
</tr>
<tr>
<td>U.S. Government Fixed</td>
<td>13,505</td>
<td>3,707</td>
<td>1,917</td>
<td>19,129</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>19,901</strong></td>
<td><strong>5,463</strong></td>
<td><strong>2,825</strong></td>
<td><strong>28,189</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Securities on Loan</th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash Collateral Received</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electric Division</td>
<td>2,151</td>
<td>589</td>
<td>305</td>
<td>3,045</td>
</tr>
<tr>
<td>Gas Division</td>
<td>4,112</td>
<td>1,129</td>
<td>584</td>
<td>5,825</td>
</tr>
<tr>
<td>Water Division</td>
<td>13,833</td>
<td>3,797</td>
<td>1,963</td>
<td>19,593</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>20,096</strong></td>
<td><strong>5,515</strong></td>
<td><strong>2,852</strong></td>
<td><strong>28,463</strong></td>
</tr>
</tbody>
</table>

Restricted and Unrestricted Funds

Restricted funds, cash and cash equivalents, and investments consisted of the following as of December 31, 2008 and 2007:

<table>
<thead>
<tr>
<th></th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Restricted funds:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$ 48,456</td>
<td>$ 47,137</td>
<td>$ 28,008</td>
</tr>
<tr>
<td>Investments</td>
<td>7,693</td>
<td>7,440</td>
<td>7,631</td>
</tr>
<tr>
<td>Total restricted funds</td>
<td>$ 56,149</td>
<td>$ 54,577</td>
<td>$ 35,639</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unrestricted funds:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$ 119,657</td>
<td>$ 111,912</td>
<td>$ 26,295</td>
</tr>
<tr>
<td>Investments</td>
<td>57,026</td>
<td>49,038</td>
<td>11,090</td>
</tr>
<tr>
<td>Total unrestricted funds</td>
<td>$ 176,683</td>
<td>$ 160,950</td>
<td>$ 37,385</td>
</tr>
</tbody>
</table>
3. Long-Term Receivables

The Electric Division has an unsecured note receivable from a government agency, which amounted to $2,663 and $4,105 as of December 31, 2008 and 2007, respectively. Interest is earned at a fixed rate of 7.723% per annum. The note provides for monthly payments of principal and interest and has a maturity date of August 1, 2010. The note receivable secures an Electric Division note payable (see Note 8).

Scheduled maturities of the note receivable are as follows for the years ending December 31:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount (in Thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>$1,557</td>
</tr>
<tr>
<td>2010</td>
<td>$1,106</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong> $2,663</td>
</tr>
</tbody>
</table>

The government agency note receivable is included in notes receivable in the accompanying 2008 Electric Division balance sheet, except for the current portion of $1,557, which is included in other current assets.

In 2002, MLGW and the Valero Refining Group (“Valero”) (formerly Premcor Refining Group, Inc. and Williams Refining and Marketing, LLC) entered into an agreement, whereby MLGW would provide for the construction of two pipelines and lease them to Valero for the purpose of transporting crude oil and refinery products. The lease provides for monthly payments of principal and interest and has an initial term of 15 years, ending on October 1, 2016.

Scheduled lease payments receivable are as follows for the years ending December 31:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount (in Thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>$1,712</td>
</tr>
<tr>
<td>2010</td>
<td>$1,712</td>
</tr>
<tr>
<td>2011</td>
<td>$1,712</td>
</tr>
<tr>
<td>2012</td>
<td>$1,712</td>
</tr>
<tr>
<td>2013</td>
<td>$1,712</td>
</tr>
<tr>
<td>Thereafter</td>
<td>$4,564</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong> $13,124</td>
</tr>
</tbody>
</table>

The Valero lease receivable is included in notes receivable in the accompanying 2008 Gas Division’s balance sheet, except for the current portion of $1,712, which is included in other current assets.
4. Utility Plant

Utility plant activity for the years ended December 31, 2008 and 2007 was as follows:

<table>
<thead>
<tr>
<th>Year ended December 31, 2008</th>
<th>Electric Division</th>
<th>Gas Division</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Beginning Balance</td>
<td>Increases</td>
</tr>
<tr>
<td></td>
<td>Balance</td>
<td></td>
</tr>
<tr>
<td>Electric Division</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital assets not being depreciated:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$ 44,100</td>
<td>$ 132</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>55,857</td>
<td>66,923</td>
</tr>
<tr>
<td>Total capital assets not being depreciated</td>
<td>99,957</td>
<td>67,055</td>
</tr>
<tr>
<td>Capital assets being depreciated:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Structures and improvements</td>
<td>53,748</td>
<td>1,076</td>
</tr>
<tr>
<td>Transmission and</td>
<td>1,057,561</td>
<td>54,005</td>
</tr>
<tr>
<td>distribution plant equipment</td>
<td>137,206</td>
<td>7,798</td>
</tr>
<tr>
<td>General plant equipment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total capital assets being depreciated</td>
<td>1,248,515</td>
<td>62,879</td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>(493,792)</td>
<td>(47,375)</td>
</tr>
<tr>
<td>Total capital assets being depreciated, net</td>
<td>754,723</td>
<td>15,504</td>
</tr>
<tr>
<td>Total capital assets, net</td>
<td>$ 854,680</td>
<td>$ 82,559</td>
</tr>
</tbody>
</table>

Gas Division

Capital assets not being depreciated:

<table>
<thead>
<tr>
<th></th>
<th>Beginning Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Ending Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Balance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$ 7,368</td>
<td>$ -</td>
<td>$ -</td>
<td>$ 7,368</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>10,667</td>
<td>14,436</td>
<td>(14,183)</td>
<td>10,920</td>
</tr>
<tr>
<td>Plant held for future use</td>
<td>212</td>
<td>-</td>
<td>-</td>
<td>212</td>
</tr>
<tr>
<td>Total capital assets not being depreciated</td>
<td>18,247</td>
<td>14,436</td>
<td>(14,183)</td>
<td>18,500</td>
</tr>
</tbody>
</table>

Capital assets being depreciated:

<table>
<thead>
<tr>
<th></th>
<th>Beginning Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Ending Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Balance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Structures and improvements</td>
<td>52,696</td>
<td>1,320</td>
<td>-</td>
<td>54,016</td>
</tr>
<tr>
<td>Processing and distribution plant equipment</td>
<td>390,642</td>
<td>9,369</td>
<td>(449)</td>
<td>399,562</td>
</tr>
<tr>
<td>General plant equipment</td>
<td>59,978</td>
<td>3,494</td>
<td>(392)</td>
<td>63,080</td>
</tr>
<tr>
<td>Non-utility plant equipment</td>
<td>200</td>
<td>-</td>
<td>-</td>
<td>200</td>
</tr>
<tr>
<td>Total capital assets being depreciated</td>
<td>503,516</td>
<td>14,183</td>
<td>(841)</td>
<td>516,858</td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>(226,339)</td>
<td>(15,316)</td>
<td>940</td>
<td>(240,715)</td>
</tr>
<tr>
<td>Total capital assets being depreciated, net</td>
<td>277,177</td>
<td>(1,133)</td>
<td>99</td>
<td>276,143</td>
</tr>
<tr>
<td>Total capital assets, net</td>
<td>$ 295,424</td>
<td>$ 13,303</td>
<td>(14,084)</td>
<td>$ 294,643</td>
</tr>
</tbody>
</table>
### 4. Utility Plant (continued)

<table>
<thead>
<tr>
<th></th>
<th>Beginning Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Ending Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Year ended December 31, 2008</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Water Division</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital assets not being depreciated:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$ 3,247</td>
<td>$ 22</td>
<td>-</td>
<td>$ 3,269</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>13,279</td>
<td>11,919</td>
<td>(9,328)</td>
<td>15,870</td>
</tr>
<tr>
<td>Total capital assets not being depreciated</td>
<td>16,526</td>
<td>11,941</td>
<td>(9,328)</td>
<td>19,139</td>
</tr>
<tr>
<td>Capital assets being depreciated:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Structures and improvements</td>
<td>46,895</td>
<td>383</td>
<td>(6)</td>
<td>47,272</td>
</tr>
<tr>
<td>Pumping, transmission and distribution plant equipment</td>
<td>293,618</td>
<td>6,006</td>
<td>(1,001)</td>
<td>298,623</td>
</tr>
<tr>
<td>General plant equipment</td>
<td>63,929</td>
<td>2,917</td>
<td>(781)</td>
<td>66,065</td>
</tr>
<tr>
<td>Total capital assets being depreciated</td>
<td>404,442</td>
<td>9,306</td>
<td>(1,788)</td>
<td>411,960</td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>(159,707)</td>
<td>(12,240)</td>
<td>2,279</td>
<td>(169,668)</td>
</tr>
<tr>
<td>Less acquisition adjustment</td>
<td>(11,080)</td>
<td>-</td>
<td>964</td>
<td>(10,116)</td>
</tr>
<tr>
<td>Total capital assets being depreciated, net</td>
<td>233,655</td>
<td>(2,934)</td>
<td>1,455</td>
<td>232,176</td>
</tr>
<tr>
<td>Total capital assets, net</td>
<td>$ 250,181</td>
<td>$ 9,007</td>
<td>$ (7,873)</td>
<td>$ 251,315</td>
</tr>
</tbody>
</table>

| **Year ended December 31, 2007** |                   |            |           |                |
|**Electric Division**|                   |            |           |                |
| Capital assets not being depreciated: |                   |            |           |                |
| Land                 | $ 40,774           | $ 3,326    | -         | $ 44,100       |
| Construction in progress | 55,190            | 84,407     | (83,740)  | 55,857         |
| Total capital assets not being depreciated | 95,964            | 87,733     | (83,740)  | 99,957         |
| Capital assets being depreciated: |                   |            |           |                |
| Structures and improvements | 48,859            | 5,112      | (223)     | 53,748         |
| Transmission and distribution plant equipment | 1,014,776         | 52,187     | (9,402)   | 1,057,561      |
| General plant equipment | 96,229            | 44,024     | (3,047)   | 137,206        |
| Total capital assets being depreciated | 1,159,864         | 101,323    | (12,672)  | 1,248,515      |
| Less accumulated depreciation | (454,795)         | (60,315)   | 21,318    | (493,792)      |
| Total capital assets being depreciated, net | 705,069           | 41,008     | 8,646     | 754,723        |
| Total capital assets, net | $ 801,033          | $ 128,741  | $ (75,094) | $ 854,680      |
4. Utility Plant (continued)

<table>
<thead>
<tr>
<th></th>
<th>Beginning Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Ending Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Year ended December 31, 2007</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Gas Division</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital assets not being depreciated:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$ 7,584</td>
<td>$ 78</td>
<td>$(294)</td>
<td>$ 7,368</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>12,220</td>
<td>17,686</td>
<td>(19,239)</td>
<td>10,667</td>
</tr>
<tr>
<td>Plant held for future use</td>
<td>212</td>
<td>-</td>
<td>-</td>
<td>212</td>
</tr>
<tr>
<td>Total capital assets not being depreciated</td>
<td>$20,016</td>
<td>17,764</td>
<td>(19,533)</td>
<td>18,247</td>
</tr>
<tr>
<td>Capital assets being depreciated:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Structures and improvements</td>
<td>52,271</td>
<td>425</td>
<td>-</td>
<td>52,696</td>
</tr>
<tr>
<td>Processing and distribution plant equipment</td>
<td>381,690</td>
<td>9,715</td>
<td>(763)</td>
<td>390,642</td>
</tr>
<tr>
<td>General plant equipment</td>
<td>95,735</td>
<td>(11,886)</td>
<td>(23,871)</td>
<td>59,978</td>
</tr>
<tr>
<td>Non-utility plant equipment</td>
<td>200</td>
<td>-</td>
<td>-</td>
<td>200</td>
</tr>
<tr>
<td>Total capital assets being depreciated</td>
<td>$529,896</td>
<td>(1,746)</td>
<td>(24,634)</td>
<td>503,516</td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>(226,574)</td>
<td>(16,961)</td>
<td>17,196</td>
<td>(226,339)</td>
</tr>
<tr>
<td>Total capital assets being depreciated, net</td>
<td>$303,322</td>
<td>(18,707)</td>
<td>(7,438)</td>
<td>277,177</td>
</tr>
<tr>
<td>Total capital assets, net</td>
<td>$323,338</td>
<td>(943)</td>
<td>(26,971)</td>
<td>$295,424</td>
</tr>
<tr>
<td><strong>Water Division</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital assets not being depreciated:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$ 3,247</td>
<td>-</td>
<td>-</td>
<td>$ 3,247</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>11,448</td>
<td>14,969</td>
<td>(13,138)</td>
<td>13,279</td>
</tr>
<tr>
<td>Total capital assets not being depreciated</td>
<td>$14,695</td>
<td>14,969</td>
<td>(13,138)</td>
<td>16,526</td>
</tr>
<tr>
<td>Capital assets being depreciated:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Structures and improvements</td>
<td>46,208</td>
<td>687</td>
<td>-</td>
<td>46,895</td>
</tr>
<tr>
<td>Pumping, transmission and distribution plant equipment</td>
<td>284,595</td>
<td>10,206</td>
<td>(1,183)</td>
<td>293,618</td>
</tr>
<tr>
<td>General plant equipment</td>
<td>63,205</td>
<td>2,245</td>
<td>(1,521)</td>
<td>63,929</td>
</tr>
<tr>
<td>Total capital assets being depreciated</td>
<td>$394,008</td>
<td>13,138</td>
<td>(2,704)</td>
<td>404,442</td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>(150,581)</td>
<td>(12,635)</td>
<td>3,509</td>
<td>(159,707)</td>
</tr>
<tr>
<td>Less acquisition adjustment</td>
<td>(12,044)</td>
<td>-</td>
<td>964</td>
<td>(11,080)</td>
</tr>
<tr>
<td>Total capital assets being depreciated, net</td>
<td>$231,383</td>
<td>503</td>
<td>1,769</td>
<td>233,655</td>
</tr>
<tr>
<td>Total capital assets, net</td>
<td>$246,078</td>
<td>15,472</td>
<td>(11,369)</td>
<td>$250,181</td>
</tr>
</tbody>
</table>
4. Utility Plant (continued)

Total net capital asset changes include additions to construction in progress, transfers to or from other accounts, depreciation and amortization and the effects of sales, retirements, and contribution in aid of construction.

MLGW’s planned construction program expenditures for 2009 are estimated as follows (unaudited):

<table>
<thead>
<tr>
<th>Division</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electric Division</td>
<td>$80,978</td>
</tr>
<tr>
<td>Gas Division</td>
<td>20,817</td>
</tr>
<tr>
<td>Water Division</td>
<td>20,054</td>
</tr>
</tbody>
</table>

In June 1999, the Water Division purchased the Shelby County Water Distribution System and related assets from Shelby County, Tennessee. The difference between the purchase price and the net book value of the assets acquired (the “acquisition adjustment”) is being amortized over twenty years by the Water Division. Under the purchase agreement, MLGW agreed to decrease the water rates for the acquired customers by 3% per year through the year 2003 and committed to expenditures of at least $15 million over twenty years beginning in 1999 to upgrade and extend the acquired water system.

5. Employee Retirement System

Effective for the 2008 fiscal year, MLGW adopted GASB Statement No. 50, *Pension Disclosures*, an amendment of GASB statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 27, *Accounting for Pensions by State and Local Governmental Employers*. This Statement establishes and modifies requirements related to financial reporting by pension plans and by employers that provide defined benefit and defined contribution pensions. This Statement more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits (“OPEB”) and, in doing so, enhances information disclosed in notes to financial statements or presented as required supplementary information (“RSI”) by pension plans and by employers that provide pension benefits.

**Plan Description**

Memphis Light, Gas and Water Retirement and Pension System (the “MLGW Pension Plan”) is a single-employer defined benefit pension plan administered by the MLGW Pension Board. The MLGW Pension Plan was established to provide retirement benefits for its plan members and beneficiaries, who meet the eligibility requirements. MLGW issues a separate audited financial report for the MLGW Pension Plan that includes financial statements and required supplementary information. That report may be obtained by writing to: Manager, Risk Management, P. O. Box 430, Memphis, TN 38101.

The MLGW Pension Plan provides retirement, disability and death benefits to participants and their beneficiaries. The MLGW Pension Plan also provides for a cost of living adjustment beginning at age 56 for retired members and surviving spouses, and at any age for disabled members on a graded scale up to 5% per annum based on the National Consumer Price Index. The MLGW Pension Board has the authority to establish and amend benefit provisions of the pension plan.
5. Employee Retirement System (continued)

Plan Description (continued)

The MLGW Pension Plan covers permanent full time employees and appointed officials of MLGW. Membership consisted of the following as of December 31, 2008 and 2007:

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retirees and beneficiaries receiving benefits</td>
<td>2,472</td>
<td>2,460</td>
</tr>
<tr>
<td>Terminated plan members entitled to but not yet receiving benefits</td>
<td>16</td>
<td>17</td>
</tr>
<tr>
<td>Active members</td>
<td>2,605</td>
<td>2,590</td>
</tr>
<tr>
<td></td>
<td><strong>5,093</strong></td>
<td><strong>5,067</strong></td>
</tr>
</tbody>
</table>

Funding Policy

The contribution requirements of pension plan members and MLGW are established and may be amended and approved by the MLGW Board of Commissioners and the Memphis City Council. Pension plan members are required to contribute 8% of their annual covered salary. MLGW currently contributes 8% of the annual covered payroll, as defined under the MLGW Pension Plan. MLGW also funds the 8% pension plan member’s contribution on behalf of the president and vice presidents. However, under Article III, Section 3.2 of the pension plan, MLGW shall contribute to the pension fund such amounts as from time to time are estimated by the actuary. For fiscal year 2008, MLGW contributed 12.3% of the annual covered payroll.
5. Employee Retirement System (continued)

Annual Pension Cost and Net Pension Obligation

MLGW’s annual pension cost (“APC”) and net pension asset for the MLGW Pension Plan consisted of the following for fiscal year 2008 and 2007:

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual required contribution (&quot;ARC&quot;)</td>
<td>$10,541</td>
<td>$17,217</td>
</tr>
<tr>
<td>Interest on net pension obligation (asset)</td>
<td>(855)</td>
<td>(884)</td>
</tr>
<tr>
<td>Adjustment to annual required contribution</td>
<td>1,227</td>
<td>1,263</td>
</tr>
<tr>
<td>Annual pension cost</td>
<td>10,913</td>
<td>17,596</td>
</tr>
<tr>
<td>Contributions made</td>
<td>(18,466)</td>
<td>(17,230)</td>
</tr>
<tr>
<td>Change in net pension obligation (asset)</td>
<td>(7,553)</td>
<td>366</td>
</tr>
<tr>
<td>Net pension obligation (asset) at beginning of fiscal year</td>
<td>(10,684)</td>
<td>(11,050)</td>
</tr>
<tr>
<td>Net pension obligation (asset) at end of fiscal year</td>
<td>$ (18,237)</td>
<td>$ (10,684)</td>
</tr>
</tbody>
</table>

Three-Year Trend Information

<table>
<thead>
<tr>
<th>Fiscal Year Ending</th>
<th>Annual Pension Cost</th>
<th>Percentage of APC Contributed</th>
<th>Net Pension Obligation (Asset)</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 31, 2008</td>
<td>$10,913</td>
<td>169.2%</td>
<td>$ (18,237)</td>
</tr>
<tr>
<td>December 31, 2007</td>
<td>$17,596</td>
<td>97.9%</td>
<td>$10,684</td>
</tr>
<tr>
<td>December 31, 2006</td>
<td>$19,850</td>
<td>98.9%</td>
<td>$11,050</td>
</tr>
</tbody>
</table>

Funded Status and Funding Progress

As of January 1, 2009, the most recent actuarial valuation date, the MLGW Pension Plan was 90% funded. The actuarial accrued liability (“AAL”) for benefits was $1,303,190, and the actuarial value of assets was $1,172,879, resulting in an unfunded actuarial accrued liability (“UAAL”) of $130,311. The covered payroll (annual payroll of active employees covered by the pension plan) was $150,253, and the ratio of the UAAL to the covered payroll was 86.7%.
5. Employee Retirement System (continued)

Funded Status and Funding Progress (continued)

The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, presents multiyear trend information indicating whether the actuarial value of pension plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions

The annual required contribution for the current year was determined as part of the January 1, 2009 actuarial valuation using the aggregate actuarial cost method. The aggregate actuarial cost method does not identify or separately amortize unfunded actuarial liabilities. The information about funded status and funding progress has been prepared using the entry age normal actuarial cost method for that purpose and the information presented is intended to serve as a surrogate for the funded status and funding progress of the pension plan. Actuarial methods and significant assumptions were as follows:

<table>
<thead>
<tr>
<th>Valuation Date</th>
<th>January 1, 2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actuarial Cost Method</td>
<td>Aggregate Cost Method</td>
</tr>
<tr>
<td>Amortization Method</td>
<td>N/A</td>
</tr>
<tr>
<td>Remaining Amortization Period</td>
<td>N/A</td>
</tr>
<tr>
<td>Asset Valuation Method</td>
<td>5-year weighted index</td>
</tr>
<tr>
<td>Actuarial Assumptions:</td>
<td></td>
</tr>
<tr>
<td>Investment Rate of Return</td>
<td>8.00%</td>
</tr>
<tr>
<td>Inflation Rate</td>
<td>4.00%</td>
</tr>
<tr>
<td>Projected Salary Increases</td>
<td>Varies by age</td>
</tr>
<tr>
<td>Cost of Living Adjustments</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1.05% for ages 56 - 58</td>
</tr>
<tr>
<td></td>
<td>2.10% for ages 59 - 61</td>
</tr>
<tr>
<td></td>
<td>2.63% for ages 62 and older, and all disabled participants</td>
</tr>
</tbody>
</table>
6. Deferred Compensation Plan

MLGW offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all MLGW employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

During 1997, the plan was amended to meet the requirements of Internal Revenue Code Section 457. The amended plan provides that assets or income of the plan shall be used for the exclusive purpose of providing benefits for participants and their beneficiaries or defraying reasonable expenses of administration of the plan. Since the assets of the amended plan are held in custodial and annuity accounts for the exclusive benefit of plan participants, the related assets of the plan are not reflected on MLGW’s balance sheets.

7. Other Postemployment Benefits

Effective for the 2007 fiscal year, MLGW adopted GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions. This Statement establishes standards for the measurement, recognition, and display of other postemployment benefits (OPEB) expenses/expenditures and related liabilities (assets), note disclosures, and required supplementary information. This Statement requires recognition of the cost of other postemployment benefits during the periods when employees render their services and disclosure about actuarially accrued liabilities related to past services and the status and progress of funding the benefits.

As a result of the adoption of GASB Statement No. 45, MLGW established a new OPEB trust fund. MLGW, by resolution of its Board of Commissioners (adopted on December 4, 2007, but effective as of the fiscal year beginning January 1, 2007), established the Memphis Light, Gas and Water Division OPEB Trust (“OPEB Trust”). The OPEB Trust was established for the exclusive benefit of MLGW’s retired employees and their dependents, who meet the eligibility requirements, to fund the postemployment benefits provided through the health and welfare benefit plan. Amounts contributed to the OPEB Trust by MLGW are held in trust and are irrevocable and are for the sole and exclusive purpose of funding for health and welfare benefits of the eligible participants, and the cost of operating and administering this Trust. Funds from the existing trust were transferred to the new trust when the trust was established.

Plan Description

Memphis Light, Gas and Water Division, by resolution of its Board of Commissioners, has established, adopted, and maintains a medical benefits (health and welfare) plan (the “Plan”) for its retired employees and their eligible dependants. The Plan is a single-employer defined benefit healthcare plan administered by MLGW. MLGW issues a separate audited financial report for the OPEB Trust that includes financial statements and required supplementary information. That report may be obtained by writing to: Manager, General Accounting, P.O. Box 430, Memphis, Tennessee 38101-0430.
7. Other Postemployment Benefits (continued)

Plan Description (continued)

The Plan provides postemployment health care, life insurance, accident/death and dismemberment (AD&D), medical and prescription drugs to eligible retirees and their dependents. Benefits are payable to retirees and their spouses for their lifetime. Qualified dependents will continue to receive benefits as long as they are qualified under the Plan. Dental, dependent life insurance, cancer, accident, and long-term care benefits are available, but are 100% paid by the retiree.

Employees retired under the MLGW Pension Plan, or disabled with five years of service at any age, or disabled in the line of duty at any age with no years of service restriction are eligible for OPEB benefits. Health care benefits are also offered to qualifying survivors of active employees, who are eligible to retire at the time of death. Currently, 2,472 retirees and beneficiaries are eligible for postemployment benefits.

Funding Policy

The contribution requirements of plan members and MLGW are established and may be amended by the MLGW Board of Commissioners. Retiree and spouse contribution rates are periodically reset and are currently at 25% of costs for medical and drug benefits. For life insurance and AD&D, retirees contribute 40% of the cost.

The Board of Commissioners has set the employer contribution rate based on the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities of the plan over a period not to exceed thirty years. For fiscal year 2008, employer contributions were $66,881 to the Plan. Plan members receiving benefits contributed $3,931 through their required contribution of $32.19 to $363.24 (dollars) per month depending on the coverage (employee only, employee and spouse, or family) and the health plan selected.

MLGW’s receipt of Medicare Part D prescription drug subsidies is included in non-operating income. Subsidies in future years cannot be recognized as a reduction in the actuarial accrued liability.
7. Other Postemployment Benefits (continued)

Annual OPEB Cost and Net OPEB Obligation

An actuarial valuation of MLGW’s postemployment welfare benefit program was performed for the Plan as of December 31, 2007. MLGW’s annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC). The following table presents the OPEB cost for the year, the amount contributed to the plan, and changes in the net OPEB obligation as of December 31, 2008 and 2007:

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual required contribution</td>
<td>$57,991</td>
<td>$57,991</td>
</tr>
<tr>
<td>Interest on net OPEB obligation (asset)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Adjustment to annual required contribution</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Annual OPEB cost (expense)</td>
<td>$57,991</td>
<td>$57,991</td>
</tr>
<tr>
<td>Contributions made</td>
<td>$66,881</td>
<td>$51,253</td>
</tr>
<tr>
<td>Change in net OPEB obligation (asset)</td>
<td>$(8,890)</td>
<td>6,738</td>
</tr>
<tr>
<td>Net OPEB obligation (asset) at beginning of fiscal year</td>
<td>6,738</td>
<td>-</td>
</tr>
<tr>
<td>Net OPEB obligation (asset) at end of fiscal year</td>
<td>$ (2,152)</td>
<td>$6,738</td>
</tr>
</tbody>
</table>

MLGW’s annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for fiscal years 2008 and 2007 were as follows:

<table>
<thead>
<tr>
<th>Fiscal Year Ended</th>
<th>Annual OPEB Cost</th>
<th>Employer Contributions</th>
<th>Percentage of Annual OPEB Cost Contributed</th>
<th>Net OPEB Obligation (Asset)</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 31, 2008</td>
<td>$57,991</td>
<td>$66,881</td>
<td>115.3%</td>
<td>$ (2,152)</td>
</tr>
<tr>
<td>December 31, 2007</td>
<td>57,991</td>
<td>51,253</td>
<td>88.4%</td>
<td>6,738</td>
</tr>
</tbody>
</table>
7. Other Postemployment Benefits (continued)

Funded Status and Funding Progress

As of December 31, 2007, the most recent actuarial valuation date, the plan was 2.2% funded. The actuarial accrued liability (AAL) for benefits was $694,574 and the actuarial value of assets was $15,097, resulting in an unfunded actuarial accrued liability (UAAL) of $679,477. The covered payroll (annual payroll of active employees covered by the Plan) was $144,756, and the ratio of the UAAL to the covered payroll was 469.4%.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information indicating whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.
7. Other Postemployment Benefits (continued)

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of calculations. Actuarial methods and significant assumptions were as follows:

<table>
<thead>
<tr>
<th>Valuation Date</th>
<th>December 31, 2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actuarial Cost Method</td>
<td>Entry Age Normal</td>
</tr>
<tr>
<td>Amortization Method</td>
<td>Level percent of pay, 30 years</td>
</tr>
<tr>
<td>Remaining Amortization Period</td>
<td>29 years as of December 31, 2007</td>
</tr>
<tr>
<td>Asset Valuation Method</td>
<td>Market value</td>
</tr>
<tr>
<td>Actuarial Assumptions:</td>
<td></td>
</tr>
<tr>
<td>Investment Rate of Return</td>
<td>8.00%</td>
</tr>
<tr>
<td>Inflation Rate</td>
<td>4.00%</td>
</tr>
<tr>
<td>Projected Salary Increases</td>
<td>7.66% at age 20 graded to 4.0% at age 43 and older</td>
</tr>
<tr>
<td>Medical Cost Trend Rate for PPO, POS and HMO (starting at 1/1/2008)</td>
<td>8.5% graded to 5.00% over 7 years</td>
</tr>
<tr>
<td>Drug Cost Trend Rate</td>
<td>8.0% graded to 5.00% over 6 years</td>
</tr>
</tbody>
</table>
8. Debt

Long-term debt as of December 31, 2008 and 2007 consists of the following:

<table>
<thead>
<tr>
<th>Electric Division: Electric System Revenue Bonds:</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Series 2002, due serially 2006-2010</td>
<td>3.00-5.00%</td>
<td>$11,490</td>
</tr>
<tr>
<td>Series 2003A, due serially 2006-2018</td>
<td>3.00-5.00%</td>
<td>931,590</td>
</tr>
<tr>
<td>Series 2003B, due 2017-2018</td>
<td>Variable</td>
<td>-</td>
</tr>
<tr>
<td>Series 2008, due 2017-2018</td>
<td>4.00-5.00%</td>
<td>96,930</td>
</tr>
<tr>
<td>Premium on revenue bonds</td>
<td></td>
<td>60,800</td>
</tr>
<tr>
<td>Unamortized deferred cost on bond refunding</td>
<td></td>
<td>(154)</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>1,100,656</td>
</tr>
<tr>
<td>Note payable with bank, due serially through 2010</td>
<td>7.58%</td>
<td>3,020</td>
</tr>
<tr>
<td>Less: current portion of bonds and notes payable</td>
<td></td>
<td>(89,366)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Water Division: Revenue Refunding Bonds:</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Series 1998, due serially 2006-2012</td>
<td>3.90-5.25%</td>
<td>$6,035</td>
</tr>
<tr>
<td>Series 2001, due serially 2006-2009</td>
<td>4.00-5.00%</td>
<td>1,830</td>
</tr>
<tr>
<td>Premium on revenue bonds</td>
<td></td>
<td>5</td>
</tr>
<tr>
<td>Unamortized deferred cost on bond refunding</td>
<td></td>
<td>(89)</td>
</tr>
<tr>
<td>Less: current portion of bonds and notes payable</td>
<td></td>
<td>7,781</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(3,235)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$4,546</td>
</tr>
</tbody>
</table>

Principal payments on bonds are due annually on January 1 or December 1. Debt service requirements, including notes payable, as of December 31, 2008, are as follows:

<table>
<thead>
<tr>
<th>Electric Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Principal</td>
<td>Interest</td>
</tr>
<tr>
<td>2009</td>
<td>$89,366</td>
</tr>
<tr>
<td>2010</td>
<td>93,849</td>
</tr>
<tr>
<td>2011</td>
<td>90,420</td>
</tr>
<tr>
<td>2012</td>
<td>95,190</td>
</tr>
<tr>
<td>2013</td>
<td>99,700</td>
</tr>
<tr>
<td>2014-2018</td>
<td>574,505</td>
</tr>
<tr>
<td>Total</td>
<td>$1,043,030</td>
</tr>
</tbody>
</table>

MLGW, at its option, may redeem bonds prior to maturity at premiums and prices specified in the indentures. The Series 2003A and Series 2008 bonds are subject to mandatory redemption upon early termination of the Supplement to the Power Contract (“Supplement”) with TVA as discussed in Note 11.

Bonds are secured by the pledge of the respective division’s revenues, by funds established by the bond resolutions and, in certain circumstances, proceeds from the sale of certain division assets.
8. Debt (continued)

During 2008, the Electric Division issued $96,930 in revenue bonds to refund $100,000 of Series 2003B revenue bonds. The refunding was undertaken to convert the 2003B auction rate securities into fixed rate securities of the same maturity. The Series 2008 revenue bonds bear interest at annual fixed rates ranging from 4.00% to 5.00%.

During 2003, the Electric Division issued $1,292,170 of Series 2003A and $100,000 of Series 2003B revenue bonds to prepay future power purchases from TVA under the Supplement. See Note 11. The Series 2003A revenue bonds bear interest at annual fixed rates ranging from 2.00% to 5.00%. The Series 2003B revenue bonds were auction rate securities, bear interest for 35-day auction periods. The Series 2003B revenue bonds were refunded in 2008, as discussed above.

During 2003, the Electric Division deposited $26,658 with an escrow agent to satisfy the future principal and interest requirements of the remaining $25,015 of Series 1992 refunding bonds. The escrowed funds plus future interest are sufficient to meet the debt service requirements of the Series 1992 bonds and the bonds are considered to be defeased. Therefore, the liability for such bonds has been removed from the accounts of the Electric Division. The difference between the reacquisition price and the net carrying amount of the old debt of $1,067 is reflected as a decrease to bonds payable and is being charged to operations over the original life of the defeased bonds.

During 2002, the Electric Division issued $41,625 in revenue bonds to refund $41,905 of Series 1993 revenue bonds. An additional, $4,270 of the 1993 revenue bonds was not refunded, but was repaid on January 1, 2003. The refunding was undertaken to reduce total future debt service payments. The reacquisition price exceeded the net carrying value of the old debt by $462. This amount is netted against the carrying value of the new debt and is being amortized over the life of the new debt, which was shorter than the life of the refunded debt.

MLGW’s Electric Division bond covenants require that for Series 2002 Bonds, the ratio of net revenues available for debt service to the maximum amount of principal and interest for any fiscal year (“electric coverage”) must not be less than 1.20. For Series 2003A and 2008 Bonds, the ratio of net revenues to maximum amount of principal and interest for any fiscal year must not be less than 1.00. The composite electric coverage as of December 31, 2008, was 1.74.

The Water Division bond covenant requires that the ratio of net revenues available for debt service to the maximum amount of principal and interest for any fiscal year (“water coverage”) must not be less than 1.20. Water coverage as of December 31, 2008, was 4.42.

MLGW buys and stores natural gas during the off-season (summer) to use in the upcoming winter months. In September 2008, the Gas Division issued a revenue anticipation note in the amount of $35,000 with a yield rate of 3.30% to provide funds for the purchase of gas and related costs for storage. The note is due in April 2009. In July 2007, the Gas Division issued a revenue anticipation note in the amount of $40,000 with a yield rate of 3.95% to provide funds for the purchase of gas and related costs for storage. The note was repaid in full in July 2008.
### 8. Debt (continued)

Long-term debt activity for the years ended December 31, 2008 and 2007 was as follows:

<table>
<thead>
<tr>
<th></th>
<th>Beginning Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Ending Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Year ended December 31, 2008:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Electric Division</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bonds and notes payable:</td>
<td>68,075 4,430</td>
<td>4,260 (11,535) 3,020</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>$1,126,930</td>
<td>$96,930 (183,850) $1,040,010</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Premium on revenue bonds</td>
<td>68,075</td>
<td>4,260 (11,535) 3,020</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Notes payable</td>
<td>4,430</td>
<td></td>
<td>(1,410) 3,020</td>
<td></td>
</tr>
<tr>
<td>Less deferred amounts:</td>
<td>(294)</td>
<td></td>
<td>140 (154)</td>
<td></td>
</tr>
<tr>
<td>For issuance discounts and on refunding</td>
<td>(294)</td>
<td></td>
<td>140 (154)</td>
<td></td>
</tr>
<tr>
<td>Total bonds and notes payable</td>
<td>$1,199,141</td>
<td>$101,190 (196,655) $1,103,676</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Water Division</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bonds payable:</td>
<td>27 (22)</td>
<td></td>
<td>5 (89)</td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>$10,965</td>
<td></td>
<td>(3,100) 7,865</td>
<td></td>
</tr>
<tr>
<td>Premium on revenue bonds</td>
<td>27</td>
<td></td>
<td>(22) 5</td>
<td></td>
</tr>
<tr>
<td>Less deferred amounts:</td>
<td>(151)</td>
<td></td>
<td>62 (89)</td>
<td></td>
</tr>
<tr>
<td>For issuance discounts and on refunding</td>
<td>(151)</td>
<td></td>
<td>62 (89)</td>
<td></td>
</tr>
<tr>
<td>Total bonds payable</td>
<td>$10,841</td>
<td></td>
<td>(3,060) 7,781</td>
<td></td>
</tr>
<tr>
<td><strong>Year ended December 31, 2007:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Electric Division</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bonds and notes payable:</td>
<td>5,737 4,430</td>
<td>(1,307) 4,430</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>$1,206,965</td>
<td></td>
<td>(80,035) 1,126,930</td>
<td></td>
</tr>
<tr>
<td>Premium on revenue bonds</td>
<td>80,290</td>
<td></td>
<td>(12,215) 68,075</td>
<td></td>
</tr>
<tr>
<td>Note payable</td>
<td>5,737</td>
<td></td>
<td>(1,307) 4,430</td>
<td></td>
</tr>
<tr>
<td>Less deferred amounts:</td>
<td>(467)</td>
<td></td>
<td>173 (294)</td>
<td></td>
</tr>
<tr>
<td>For issuance discounts and on refunding</td>
<td>(467)</td>
<td></td>
<td>173 (294)</td>
<td></td>
</tr>
<tr>
<td>Total bonds and notes payable</td>
<td>$1,292,525</td>
<td>$93,384 (93,384) $1,199,141</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Water Division</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bonds payable:</td>
<td>64 (37)</td>
<td></td>
<td>27 (151)</td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>$13,940</td>
<td></td>
<td>(2,975) 10,965</td>
<td></td>
</tr>
<tr>
<td>Premium on revenue bonds</td>
<td>64</td>
<td></td>
<td>(37) 27</td>
<td></td>
</tr>
<tr>
<td>Less deferred amounts:</td>
<td>(233)</td>
<td></td>
<td>82 (151)</td>
<td></td>
</tr>
<tr>
<td>For issuance discounts and on refunding</td>
<td>(233)</td>
<td></td>
<td>82 (151)</td>
<td></td>
</tr>
<tr>
<td>Total bonds payable</td>
<td>$13,771</td>
<td></td>
<td>(2,930) 10,841</td>
<td></td>
</tr>
</tbody>
</table>
9. Insurance Reserves for Medical Benefits and Injuries and Damages

MLGW is self-insured for health and medical benefits and for injuries and damages including workers compensation and general liability claims. MLGW has established insurance reserves for the estimated liabilities, including an accrual for incurred but not reported claims, resulting from medical benefits and injuries and damages claims as established by a third party administrator and MLGW’s Legal Department. The medical benefits reserve and the costs and charges to the reserve are allocated to each division based on a standard administrative and general cost allocation.

The changes in the self-insurance reserves for medical benefits and injuries and damages for the years ended December 31, 2008 and 2007 are as follows:

<table>
<thead>
<tr>
<th></th>
<th>Medical Benefits</th>
<th></th>
<th>Injuries and Damages</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Electric Division</td>
<td>Gas Division</td>
<td>Water Division</td>
<td>Electric Division</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Gas Division</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Water Division</td>
</tr>
<tr>
<td>Balance – December 31, 2006</td>
<td>$ 4,322</td>
<td>$ 2,303</td>
<td>$ 1,213</td>
<td>$ 5,915</td>
</tr>
<tr>
<td>Payments</td>
<td>(22,794)</td>
<td>(10,797)</td>
<td>(6,398)</td>
<td>(1,845)</td>
</tr>
<tr>
<td>Incurred claims expense</td>
<td>24,047</td>
<td>11,149</td>
<td>6,742</td>
<td>3,180</td>
</tr>
<tr>
<td>Balance – December 31, 2007</td>
<td>5,575</td>
<td>2,655</td>
<td>1,557</td>
<td>7,250</td>
</tr>
<tr>
<td>Payments</td>
<td>(22,465)</td>
<td>(10,019)</td>
<td>(6,653)</td>
<td>(1,954)</td>
</tr>
<tr>
<td>Incurred claims expense</td>
<td>23,484</td>
<td>10,474</td>
<td>6,955</td>
<td>1,613</td>
</tr>
<tr>
<td>Balance – December 31, 2008</td>
<td>$ 6,594</td>
<td>$ 3,110</td>
<td>$ 1,859</td>
<td>$ 6,969</td>
</tr>
</tbody>
</table>

10. Telecommunications Division

Memphis Networx, LLC (the “Company”) was organized under the Tennessee Limited Liability Act on November 8, 1999, to provide telecommunications services through the installation of broadband fiber optic cable in the Memphis, Tennessee area. The Company was a joint venture between the Telecommunications Division of MLGW’s Electric Division and Memphis Broadband, LLC, a Delaware limited liability company.

On August 9, 2001, the Tennessee Regulatory Authority (“TRA”) issued a final order approving the Company’s amended and restated operating agreement (dated November 29, 2000) and granting a certificate of public convenience and necessity for the State of Tennessee. In addition, MLGW received approval from the State Comptroller’s office to release funds from the previously approved $20,000 loan from the Electric Division to the Telecommunications Division. In the third quarter of 2002, MLGW’s Board of Commissioners, at the request of management, increased the approved level of investment in the Company to $32,000.

Under the terms of the Company’s Operating Agreement, capital contributions and costs incurred by the Company prior to its formation and through the date of TRA approval were to be shared equally by the members. Per the Operating Agreement, allocations of net operating income or loss and distributions were based on cumulative members’ contributions, accumulated members’ equity (loss), and the sharing ratios.
10. Telecommunications Division (continued)

Effective April 1, 2002, MLGW entered into a Capital Contribution Agreement with Memphis Broadband, LLC. The agreement established planned monthly capital contributions through 2004 for both members.

The agreement also amended the Operating Agreement to allow one member to contribute the required capital on behalf of the other member. If a member makes such a disproportionate contribution, the agreement allowed the contributing member to charge the other member interest on the disproportionate contribution or increase its ownership percentage and voting interest. On the contribution date, the sharing ratio of net operating income or loss and distributions would be adjusted to reflect the increased capital contribution.

On December 30, 2004, a Note and Warrant Purchase Agreement was entered into between Memphis Networx, LLC; Memphis Broadband, LLC; and MLGW. This agreement specified that Memphis Broadband and MLGW would provide bridge loan financing to the Company in an amount up to $375 each, for a total of $750. Promissory notes were issued bearing interest at 8% per annum, due and payable on or before July 1, 2005. The promissory notes were secured by a first lien security interest in all assets of the Company and provided for the issuance of warrants, representing, in the aggregate, the right to purchase up to 750,000 units of the Company or an additional 7.5% share in the Company in the event the bridge loan was not paid on or before July 1, 2005. MLGW funded its portion of the bridge loan on January 7, 2005.

On April 7, 2005, MLGW agreed to provide an additional ninety-day bridge loan of up to $750 to Memphis Networx, such loan to bear interest at 8% per annum. Funding of $500 was made on April 25, 2005, and additional funding of $150 was made on May 18, 2005. All of the bridge loans were repaid in full on June 27, 2005.

On June 21, 2005, Memphis Broadband and MLGW entered into a Capital Contribution Allowance Agreement. Under this agreement, Memphis Broadband agreed to provide a guaranty for a loan by the Company of $4,916. The sharing ratios were adjusted from 83.73% and 16.27% for MLGW and Memphis Broadband, respectively to 56.14% and 43.86%. The Capital Contribution Agreement of April 1, 2002, was also terminated.

In March 2006, also pursuant to provisions in the June 21, 2005 agreement, Memphis Broadband provided additional loan guaranties for the Company in the amount of $2,085. The sharing ratios were adjusted from 56.14% and 43.86% for MLGW and Memphis Broadband, respectively to 49.25% and 50.75%.

In July 2007, MLGW sold its investment in Memphis Networx to Communications Infrastructure Investments Holdco, Inc. MLGW received $432 for the sale plus $460 receivables from Memphis Networx. In addition, $368 is being held in escrow on MLGW’s behalf.
10. Telecommunications Division (continued)

Results of operations of the Company for the year ended December 31, 2007 are as follows:

| Net loss, Jan-July 2007 | $ (1,410) |

The equity method of accounting was used for the Telecommunications Division’s investment in the Company since the Telecommunications Division had significant influence over operating and financial policies but did not have control over policy and operations. Telecommunications Division’s results for the years ended December 31 were as follows:

<table>
<thead>
<tr>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share of the Company’s loss</td>
<td>$ -</td>
</tr>
<tr>
<td>Investment reduction – Equity Transfer to Memphis Broadband per June 21, 2005 Capital Contribution Agreement</td>
<td>-</td>
</tr>
<tr>
<td>Gain on Sale of Memphis Networx</td>
<td>-</td>
</tr>
<tr>
<td>General and administrative expenses</td>
<td>-</td>
</tr>
<tr>
<td>Total Telecommunications Division loss</td>
<td>$ -</td>
</tr>
</tbody>
</table>

The Telecommunication Division’s investment was $0 as of December 31, 2007 due to the sale of the investment in July 2007.

11. Energy Supplies

The TVA currently supplies all of MLGW’s electric power requirements pursuant to a power contract. On November 19, 2003, MLGW entered into a Supplement to the Power Contract (“Supplement”) with TVA under which MLGW made a prepayment of $1,500,000 to TVA for capacity and related energy. In exchange for the prepayment and a commitment by MLGW to purchase a minimum amount of electric power from TVA over the term of the Supplement (15 years), TVA will supply a specified amount of electricity over the term and provide a fixed credit to its wholesale power rates otherwise in effect. To finance the prepayment, MLGW issued the Series 2003A and Series 2003B Bonds. See Note 1 (Prepaid Power Cost) and Note 8 (Debt).

Under the terms of the TVA power contract, MLGW may terminate its supply arrangement with TVA upon five years’ prior written notice. TVA may terminate on not less than ten years’ prior written notice. However, such notice of termination cannot be given by either party before November 19, 2013, under the terms of the Supplement.
11. Energy Supplies (continued)

MLGW purchases natural gas from multiple suppliers on multiple pipelines in order to minimize operational and performance risk. MLGW has some short-term purchase commitments which are normally for one year or less. MLGW and the Tennessee Energy Acquisition Corporation (“TEAC”) entered into a 20 year long term gas purchase contract starting January 1, 2007 with volume commitments for the period. In June 2006, Public Energy Authority of Kentucky, Inc. (“PEAK”) and MLGW entered into a 5 year term gas purchase contract with volume commitments for the period. Both TEAC and PEAK deals are paid monthly after the gas is received by MLGW for its customers, and therefore these deals present no increased cash flow risk compared to normal physical gas purchases.

12. Rates

Electric, gas and water rates are established by MLGW and rate changes are subject to approval by the City Council of Memphis, Tennessee. The City Council has approved mechanisms for pass-through of wholesale electric rate changes from TVA and natural gas price changes from suppliers without requiring additional specific approval.

Effective with meters read on or after December 26, 2007, MLGW implemented an electric temporary weather credit (one-year rate decrease) for residential customers and for commercial and industrial customers with contracts less than 5,001 kilowatts of demand. The retail effects of the decrease varied by customer class, with the approximate decreases being 4.4% for residential and 2.8% for commercial and industrial customers.

TVA implemented a rate adjustment effective with the April 2008 revenue month, increasing the cost of wholesale power purchased by MLGW by approximately 7.0%. MLGW implemented changes to its retail rate schedules effective with meters read on or after March 28, 2008, to recover the increased cost of wholesale power from its retail customers. The retail effects of the rate adjustment varied by customer class, with the approximate increases being 5.5% for residential customers, 5.9% for commercial customers and 6.5% for industrial customers.

TVA implemented a second adjustment within the year that became effective with the October 2008 revenue month, increasing the cost of wholesale power purchased by MLGW by approximately 3.5%. MLGW implemented changes to its retail rate schedules effective with meters read on or after September 25, 2008, to recover the increased cost of wholesale power from its retail customers. The retail effects of the increase varied by customer class, with the approximate increases being 2.7% for residential, 2.9% for commercial customers and 3.2% for industrial customers.

MLGW retail electric rates are adjusted quarterly for TVA’s Fuel Cost Adjustor (“FCA”). The FCA is a variable wholesale energy rate that can fluctuate each quarter with TVA’s cost of fuel for electricity generation and purchased power costs. The FCA affects energy (per kilowatt-hour) charges for all retail customers who are not on interruptible rate schedules.
12. Rates (continued)

Effective with meters read on or after December 26, 2007, MLGW implemented structural changes to its gas rate schedules to mitigate impacts of weather fluctuations on MLGW’s margin (difference between sales revenue and gas costs) and to encourage customer conservation. In addition, MLGW implemented a gas rate increase effective with meters read on or after December 26, 2007. The rate increase is due to the effects of inflation on general operating expenses, reduced cash balances, and capital expenditures for system improvements. The retail effects of the increase varied by customer class, with the approximate increases being 7.5% for residential, 5.6% for commercial and industrial firm sales customers and 6.9% for commercial and industrial interruptible sales customers.

MLGW retail natural gas rates are adjusted monthly for the Purchased Gas Adjustment (“PGA”) rider. MLGW gas rate schedules have a projected price of natural gas and related gas storage and transportation. In addition, a PGA is applied to customer bills to reflect the difference between the actual cost of gas, storage and transportation in a given month and the projected levels built into the base rate schedules.

In 2007, the Memphis City Council approved a water rate increase effective with meters read on or after June 26, 2008. The approximate retail rate impact is 15%.

13. Commitments and Contingencies

The Gas Division has contracts and swap agreements, from which risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in gas prices. The Gas Division’s exposure to credit loss in the event of nonperformance by the other party is represented by the fair value of the open futures contracts. However, there is no counterparty financial risk for contracts transacted through NYMEX or the International Petroleum Exchange.

MLGW pays a Transfer to the City and in lieu of taxes to the incorporated towns of Shelby County for the Electric and Gas Divisions based on the Tennessee Municipal Electric and Gas System Tax Equivalent Laws of 1987. MLGW pays a Transfer to the City for the Water Division based upon an agreement with the City which calls for a payment of $2,500 for each of the fiscal years through 2028.

MLGW is party to various legal proceedings incidental to its business. In the opinion of management, MLGW’s liability, if any, in all pending litigation or other proceedings, taken as a whole after consideration of amounts accrued, insurance coverage, or other indemnification arrangements, will not have a material adverse effect on its financial position or results of operations.

See Note 11 for discussions of MLGW’s power contract with TVA and gas purchase commitments.

14. Self-Insurance

MLGW is self-insured. The Tennessee Governmental Tort Liability Act applies to all tort actions against MLGW arising in the State of Tennessee and establishes limits of liability. The current limits of liability for actions arising on or after July 1, 2007, for personal injuries are $300 per person and $700 for two or more persons per accident. Property damages are limited to $100 per accident.
15. Transfers to City

The Electric, Gas and Water Divisions make Transfers to the City of Memphis.

The Electric Division transfer is based on the formula provided by the State of Tennessee Municipal Electric System Tax Equivalent Law of 1987. The formula includes a property tax equivalency calculation plus 4% of operating revenue less power costs (three year average).

The Gas Division transfer is based on the formula provided by the Municipal Gas System Tax Equivalent Law of 1987. The formula includes a property tax equivalency calculation plus 4% of operating revenue less gas costs (three year average).

The Water Division, through an agreement with the City of Memphis, transfers a payment in the amount of $2,500 per year. The agreement is effective through the year 2028.

16. Federal Grant Contributions

During February 2008, severe storms and tornadoes caused damage to transmission towers, a substation, and portions of MLGW’s electric distribution system. As a result of the storms, additional expenses were incurred for the operation of the Water pumping stations during the period of the electrical power outage. As of December 31, 2008, the total expenditures for all Divisions related to the storm were $3,917. Of these costs, $3,860 was in the Electric Division, including a $2,253 addition to plant for capital asset replacements and $1,607 in Electric Division operating and maintenance expenses. MLGW received insurance proceeds in the amount of $288 for these expenditures which is accounted for as a contribution in aid of construction in the Electric Division. MLGW has been approved to receive reimbursement from the Federal Emergency Management Agency (“FEMA”) totaling $2,427 (or 75%) of eligible expenses. Of this amount, $1,383 was accounted for as a contribution in aid of construction in the Electric Division and $1,044 as Electric miscellaneous non-operating income. In November 2008, a payment of $2,318 was received leaving a balance as of fiscal year end 2008 of $109, which is included in other current assets of the accompanying balance sheet.

The Water Division incurred total operating and maintenance expenditures of $42 due to the lost of power to the pumping stations during the storms. MLGW has been approved to receive reimbursement from FEMA totaling $25 (or 75%) of eligible expenses. In August 2008, a payment of $19 was received leaving a balance as of fiscal year end 2008 of $6, which is included in other current assets of the accompanying balance sheet.

During 2007, MLGW began design and engineering activities on the Sheahan Water Pumping Station Pre-Disaster Mitigation project. As of 2008 year end, total expenditures (inception to date) were $161, of which $121 (or 75%) is eligible for federal reimbursement. In November 2008, MLGW submitted a payment request to the Tennessee Emergency Management Agency (“TEMA”) for eligible costs incurred. In December 2008, MLGW received $110 in federal reimbursement, representing a partial payment for this project. The remaining receivable balance for this project as of fiscal year end 2008 is $11.
16. Federal Grant Contributions (continued)

In January 2008, MLGW submitted an application to TEMA for a High Voltage Transformer Seismic Retrofit Project under the Pre-Disaster Mitigation Competitive Program. In October 2008, the FEMA announced the project approval for nearly $2,700, of which $2,000 will be federally funded. Fiscal year 2008 expenditures totaled $19, with $14 (or 75%) eligible for federal reimbursement.

17. Pollution Remediation Obligation

Effective for the 2008 fiscal year, MLGW adopted GASB Statement No. 49, *Pollution Remediation Obligations*, which addresses accounting and financial standards for pollution remediation liabilities. GASB Statement No. 49 requires measurement of the liabilities at the beginning of the reported period so beginning net assets can be restated. As a result, beginning net assets for 2007 were reduced for the Electric, Gas and Water Division liabilities by $25,511, $4,215 and $6,522, respectively. The liabilities remaining after expenditures as of December 2008, for the Electric, Gas and Water Divisions were $24,609, $3,923 and $5,155, respectively.

MLGW has a contract with a state licensed environmental remediation company. The liabilities to remove asbestos, mold and lead from various substations and equipment because of imminent danger were derived from the environmental remediation contractor’s estimate. The liability assumes no unexpected change orders.

MLGW is under a Consent and Final Order from the United States Environmental Protection Agency (“EPA”) to perform a Supplemental Environmental Project (“SEP”) over the next three years. The SEP consists of a voluntary accelerated polychlorinated biphenyls (“PCBs”) removal program that will significantly reduce the number of PCB transformers, PCB-contaminated transformers, PCB capacitors, and associated PCB oils in its possession that are in use, stored for reuse, or stored for disposal. This project was undertaken in connection with the settlement of an enforcement action taken by the U.S. Environmental Protection Agency for violations of Section 6(e) of TSCA, 15 U.S.C. § 2605. A liability of $10,094 for the cost of performing this work was derived from the Consent and Final Order from EPA. Therefore, an additional $2,135 liability for the cost of clean-up was derived from previous experience in PCB remediation associated with transformers. This amount assumes no expected change orders.
17. Pollution Remediation Obligation (continued)

The schedule below shows the balance for each pollution liability by Division for each period presented.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Electric</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>PCB</td>
<td>$12,229</td>
<td>$12,229</td>
<td>$12,094</td>
</tr>
<tr>
<td>Mold</td>
<td>10</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>Asbestos</td>
<td>1,229</td>
<td>1,229</td>
<td>1,149</td>
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<tr>
<td>Lead</td>
<td>12,043</td>
<td>12,043</td>
<td>11,366</td>
</tr>
<tr>
<td>Total</td>
<td>25,511</td>
<td>25,511</td>
<td>24,609</td>
</tr>
<tr>
<td>Gas</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mold</td>
<td>150</td>
<td>150</td>
<td>145</td>
</tr>
<tr>
<td>Asbestos</td>
<td>83</td>
<td>83</td>
<td>29</td>
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<tr>
<td>Lead</td>
<td>3,982</td>
<td>3,982</td>
<td>3,749</td>
</tr>
<tr>
<td>Total</td>
<td>4,215</td>
<td>4,215</td>
<td>3,923</td>
</tr>
<tr>
<td>Water</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mold</td>
<td>446</td>
<td>446</td>
<td>339</td>
</tr>
<tr>
<td>Asbestos</td>
<td>1,402</td>
<td>1,402</td>
<td>1,250</td>
</tr>
<tr>
<td>Lead</td>
<td>4,674</td>
<td>4,674</td>
<td>3,566</td>
</tr>
<tr>
<td>Total</td>
<td>6,522</td>
<td>6,522</td>
<td>5,155</td>
</tr>
<tr>
<td>Total Liability</td>
<td>$36,248</td>
<td>$36,248</td>
<td>$33,687</td>
</tr>
<tr>
<td>Total PCB</td>
<td>$12,229</td>
<td>$12,229</td>
<td>$12,094</td>
</tr>
<tr>
<td>Total Mold</td>
<td>606</td>
<td>606</td>
<td>484</td>
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<tr>
<td>Total Asbestos</td>
<td>2,714</td>
<td>2,714</td>
<td>2,428</td>
</tr>
<tr>
<td>Total Lead</td>
<td>20,699</td>
<td>20,699</td>
<td>18,681</td>
</tr>
<tr>
<td>Total Liability</td>
<td>$36,248</td>
<td>$36,248</td>
<td>$33,687</td>
</tr>
</tbody>
</table>
## SCHEDULE OF ADDITIONS AND RETIREMENTS TO UTILITY PLANT

(Dollars in Thousands)

DECEMBER 31, 2008

<table>
<thead>
<tr>
<th></th>
<th>Electric Division</th>
<th>Gas Division</th>
<th>Water Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Utility plant in service, December 31, 2007</td>
<td>$1,277,270</td>
<td>$510,618</td>
<td>$396,611</td>
</tr>
<tr>
<td>Additions</td>
<td>63,005</td>
<td>14,183</td>
<td>10,291</td>
</tr>
<tr>
<td>Retirements</td>
<td>(9,815)</td>
<td>(841)</td>
<td>(1,783)</td>
</tr>
<tr>
<td>Transfers</td>
<td>6</td>
<td>-</td>
<td>(6)</td>
</tr>
<tr>
<td>Utility plant in service, December 31, 2008</td>
<td>$1,330,466</td>
<td>$523,960</td>
<td>$405,113</td>
</tr>
</tbody>
</table>

Note: Utility plant in service balances exclude amounts for construction work in process, non-utility property and land held for future use.
### SCHEDULE OF DEPOSITS AND INVESTMENTS
(Dollars in Thousands)
DECEMBER 31, 2008

<table>
<thead>
<tr>
<th>MONEY MARKET MUTUAL FUNDS</th>
<th>ACCRUAL YIELD</th>
<th>MATURITY DATE</th>
<th>FAIR VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Institutional Government Select Funds</td>
<td></td>
<td></td>
<td>$ 213,029</td>
</tr>
<tr>
<td>Federated Treas Obligations FD 398</td>
<td></td>
<td></td>
<td>25,372</td>
</tr>
<tr>
<td>Total Money Market Mutual Funds</td>
<td></td>
<td></td>
<td>$ 238,401</td>
</tr>
</tbody>
</table>

| CASH | | | |
| Bank Deposits | | | $ 16,468 |
| Total Cash | | | $ 16,468 |

| ACCRUED INTEREST | | | $ 974 |

| TOTAL CASH AND CASH EQUIVALENTS | | | $ 255,843 |

| TREASURY NOTE | (0.356) | 06/30/2010 | $ 503 |
| Total Treasury Note | | | $ 503 |

| U. S. GOVERNMENT BONDS | | | |
| 3.875 09/15/2010 | | | $ 1,059 |
| 4.500 11/15/2010 | | | 537 |
| 4.875 04/30/2011 | | | 548 |
| 4.875 07/31/2011 | | | 1,656 |
| 4.875 08/15/2009 | | | 206 |
| 4.500 09/30/2011 | | | 823 |
| 3.625 10/31/2009 | | | 308 |
| 3.875 10/31/2012 | | | 55 |
| 3.125 11/30/2009 | | | 1,025 |
| 3.375 11/30/2012 | | | 573 |
| 3.250 12/31/2009 | | | 1,029 |
| 3.875 05/15/2010 | | | 786 |
| 2.625 05/31/2010 | | | 2,060 |
| 4.250 10/15/2010 | | | 1,068 |
| 4.375 12/15/2010 | | | 805 |
| 2.125 04/30/2010 | | | 2,560 |
| 3.375 07/31/2013 | | | 737 |
| 3.125 04/30/2013 | | | 812 |
| 2.875 06/30/2010 | | | 1,553 |
| 4.750 01/31/2012 | | | 595 |
| 4.625 07/31/2012 | | | 448 |
| 4.625 11/15/2009 | | | 518 |
| 1.750 11/15/2011 | | | 2,046 |

Total U.S. Government Bonds | | | $ 21,807 |
## Schedule of Deposits and Investments

**Dollars in Thousands**

**December 31, 2008**

(Continued)

<table>
<thead>
<tr>
<th>SCHEDULE OF DEPOSITS AND INVESTMENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>U.S. GOVERNMENT AGENCIES</strong></td>
</tr>
</tbody>
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<table>
<thead>
<tr>
<th>ACCRUAL MATURITY FAIR YIELD</th>
<th>MATURITY DATE</th>
<th>FAIR VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td>8.375 09/15/2009</td>
<td>$ 409</td>
<td></td>
</tr>
<tr>
<td>5.125 08/23/2010</td>
<td>1,065</td>
<td></td>
</tr>
<tr>
<td>4.375 09/28/2009</td>
<td>1,285</td>
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</tr>
<tr>
<td>4.875 11/18/2011</td>
<td>1,638</td>
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</tr>
<tr>
<td>5.000 03/12/2010</td>
<td>1,050</td>
<td></td>
</tr>
<tr>
<td>5.000 12/11/2009</td>
<td>1,327</td>
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</tr>
<tr>
<td>5.250 06/11/2010</td>
<td>1,594</td>
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</tr>
<tr>
<td>5.670 02/26/2009</td>
<td>81</td>
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</tr>
<tr>
<td>5.020 05/03/2012</td>
<td>331</td>
<td></td>
</tr>
<tr>
<td>5.000 09/14/2012</td>
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</tr>
<tr>
<td>4.500 12/14/2012</td>
<td>257</td>
<td></td>
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<tr>
<td>5.545 02/17/2009</td>
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<tr>
<td>3.625 09/16/2011</td>
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<tr>
<td>3.625 07/01/2011</td>
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<tr>
<td>5.400 06/01/2012</td>
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<tr>
<td>4.875 11/15/2011</td>
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<tr>
<td>5.250 03/19/2014</td>
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<td></td>
</tr>
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<td>5.000 03/25/2011</td>
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<td>5.900 03/26/2009</td>
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<td>6.135 02/15/2011</td>
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<td>4.125 04/01/2013</td>
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<td>3.000 04/01/2011</td>
<td>1,005</td>
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<td>4.125 10/18/2010</td>
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<td>4.750 01/18/2011</td>
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<tr>
<td>5.125 07/15/2012</td>
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<tr>
<td>5.250 05/21/2009</td>
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<tr>
<td>5.000 06/11/2009</td>
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<tr>
<td>5.500 08/20/2012</td>
<td>2,232</td>
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<tr>
<td>4.125 11/30/2009</td>
<td>514</td>
<td></td>
</tr>
<tr>
<td>4.500 11/18/2009</td>
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<tr>
<td>3.900 04/01/2013</td>
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</tr>
<tr>
<td>5.500 03/15/2011</td>
<td>820</td>
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<tr>
<td>6.410 11/13/2012</td>
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<td>5.250 01/15/2009</td>
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<td>6.125 03/15/2012</td>
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<td>4.750 11/19/2012</td>
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<td>4.750 12/15/2010</td>
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</tbody>
</table>
**SCHEDULE OF DEPOSITS AND INVESTMENTS**
(Dollars in Thousands)
DECEMBER 31, 2008
(Continued)

<table>
<thead>
<tr>
<th>U. S. GOVERNMENT AGENCIES (cont.)</th>
<th>ACCRUAL YIELD</th>
<th>MATURITY DATE</th>
<th>FAIR VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>4.125</td>
<td>05/15/2010</td>
<td>$ 935</td>
</tr>
<tr>
<td></td>
<td>5.125</td>
<td>04/15/2011</td>
<td>$ 1,623</td>
</tr>
<tr>
<td></td>
<td>4.125</td>
<td>02/17/2011</td>
<td>$ 530</td>
</tr>
</tbody>
</table>

Total U.S. Government Agencies $ 39,483

**CORPORATE BONDS**

|                                    | ACCRUAL YIELD | MATURITY DATE | FAIR VALUE |
|                                    | 4.000         | 09/15/2009    | $ 490      |
| PVTPL HBOS                         | 3.875         | 01/15/2009    | 500        |
| Credit Suisse                      | 7.375         | 01/19/2010    | 2,261      |
| Gen Elec Cap                       | 5.850         | 03/15/2009    | 151        |
| Leland Stanford                    | 3.550         | 04/15/2013    | 781        |
| Private Expt                       | 5.620         | 07/15/2009    | 43         |
| PVTPL CMO                          | 7.900         | 07/02/2010    | 542        |
| PVTPL Hancock                      | 4.375         | 07/30/2009    | 541        |
| Wal-Mart Stores Inc                | 6.875         | 08/10/2009    | 2,317      |
| Wells Fargo                        | 4.875         | 01/12/2011    | 500        |

Total Corporate Bonds $ 8,126

**ASSET-BACKED SECURITIES**

|                                    | ACCRUAL YIELD | MATURITY DATE | FAIR VALUE |
|                                    | 4.460         | 04/16/2012    | $ 934      |
| Asset Backed                       | 4.080         | 04/18/2010    | 186        |
| Bank of America                    | 5.040         | 05/17/2010    | 1,104      |
| Cap Auto Receivables               | 4.890         | 02/15/2012    | 988        |
| Cap 1 Prime Auto Receivables       | 4.910         | 01/18/2011    | 1,142      |
| Carmax Auto                        | 5.570         | 05/25/2010    | 71         |
| Caterpillar Finl Asset             | 5.300         | 05/20/2011    | 1,295      |
| Citibank                           | 4.710         | 09/08/2012    | 463        |
| Daimler Chrysler Auto              | 4.574         | 04/14/2010    | 986        |
| GE Equip Midticket                 | 5.110         | 04/15/2012    | 1,242      |
| Honda Auto Receivables             | 5.380         | 07/15/2010    | 25         |
| John Deere                         | 4.900         | 02/15/2012    | 988        |
| USAA Auto                          | 3.910         | 01/15/2011    | 494        |
| Volkswagen Auto                    | 4.500         | 07/20/2012    | 948        |

Total Asset-Backed Securities $ 10,866
## SCHEDULE OF DEPOSITS AND INVESTMENTS

(Dollars in Thousands)

### DECEMBER 31, 2008

(Continued)

<table>
<thead>
<tr>
<th>ACCRUAL YIELD</th>
<th>MATURITY DATE</th>
<th>FAIR VALUE</th>
</tr>
</thead>
</table>

### GOVERNMENT MORTGAGE BACKED SECURITIES

<table>
<thead>
<tr>
<th>Security Description</th>
<th>Yield</th>
<th>Maturity Date</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Home LN Mtg</td>
<td>4.000</td>
<td>06/01/2011</td>
<td>$ 413</td>
</tr>
<tr>
<td>FNMA Pool</td>
<td>5.500</td>
<td>04/01/2009</td>
<td>158</td>
</tr>
<tr>
<td>FNMA Pool</td>
<td>5.500</td>
<td>05/01/2009</td>
<td>28</td>
</tr>
<tr>
<td>FNMA Pool</td>
<td>5.500</td>
<td>06/01/2009</td>
<td>33</td>
</tr>
<tr>
<td>FNMA Pool</td>
<td>5.500</td>
<td>09/01/2009</td>
<td>11</td>
</tr>
<tr>
<td>FNMA Pool</td>
<td>5.500</td>
<td>12/01/2009</td>
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</tr>
<tr>
<td>FNMA Pool</td>
<td>4.000</td>
<td>06/01/2010</td>
<td>966</td>
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Total Government Mortgage Backed Securities $ 2,609

### GUARANTEED FIXED INCOME

<table>
<thead>
<tr>
<th>Security Description</th>
<th>Yield</th>
<th>Maturity Date</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America</td>
<td>1.700</td>
<td>12/23/2010</td>
<td>$ 5,015</td>
</tr>
<tr>
<td>JP Morgan Chase</td>
<td>2.625</td>
<td>12/01/2010</td>
<td>3,060</td>
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</table>

Total Guaranteed Fixed Income $ 8,075

### FAIR VALUE OF INVESTMENTS

$ 14

### TOTAL CASH AND INVESTMENTS

$ 347,326
SCHEDULE OF LONG TERM DEBT,
PRINCIPAL AND INTEREST REQUIREMENTS
(Dollars in Thousands)
DECEMBER 31, 2008

### Electric Division:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>$ 5,635</td>
<td>$ 82,210</td>
<td>$ 104,675</td>
<td>$ 518</td>
<td>$ 46,171</td>
<td>- $ 4,564</td>
</tr>
<tr>
<td>2010</td>
<td>5,855</td>
<td>86,495</td>
<td>99,700</td>
<td>293</td>
<td>37,848</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2011</td>
<td>90,420</td>
<td>95,190</td>
<td>104,675</td>
<td>2011</td>
<td>28,677</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2012</td>
<td>95,190</td>
<td>104,675</td>
<td>109,905</td>
<td>90,420</td>
<td>23,817</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2013</td>
<td>99,700</td>
<td>104,675</td>
<td>115,270</td>
<td>2012</td>
<td>18,584</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2014</td>
<td>115,270</td>
<td>104,675</td>
<td>99,700</td>
<td>2013</td>
<td>13,110</td>
<td>- 4,564</td>
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<tr>
<td>2015</td>
<td>2014</td>
<td>2015</td>
<td>2015</td>
<td>88,075</td>
<td>28,677</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2016</td>
<td>88,075</td>
<td>2016</td>
<td>2016</td>
<td>99,700</td>
<td>7,347</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2017</td>
<td>99,700</td>
<td>2017</td>
<td>2017</td>
<td>104,675</td>
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<td>- 4,564</td>
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<tr>
<td>2018</td>
<td>104,675</td>
<td>2018</td>
<td>2018</td>
<td>109,905</td>
<td>65,305</td>
<td>- 4,564</td>
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<tr>
<td>Total</td>
<td>$ 11,490</td>
<td>$ 931,590</td>
<td>$ 96,930</td>
<td>$ 811</td>
<td>$ 254,043</td>
<td>$ 44,119</td>
</tr>
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</table>

### Note Payable – Bank

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>$ 1,521</td>
<td>$ 82,210</td>
<td>$ 104,675</td>
<td>$ 518</td>
<td>$ 46,171</td>
<td>- $ 4,564</td>
</tr>
<tr>
<td>2010</td>
<td>1,499</td>
<td>86,495</td>
<td>99,700</td>
<td>293</td>
<td>37,848</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2011</td>
<td>90,420</td>
<td>95,190</td>
<td>104,675</td>
<td>2011</td>
<td>28,677</td>
<td>- 4,564</td>
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<tr>
<td>2012</td>
<td>95,190</td>
<td>104,675</td>
<td>104,675</td>
<td>2012</td>
<td>23,817</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2013</td>
<td>99,700</td>
<td>104,675</td>
<td>109,905</td>
<td>2013</td>
<td>18,584</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2014</td>
<td>115,270</td>
<td>104,675</td>
<td>115,270</td>
<td>2014</td>
<td>13,110</td>
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<td>2016</td>
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<td>2016</td>
<td>2016</td>
<td>99,700</td>
<td>2,965</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2017</td>
<td>99,700</td>
<td>2017</td>
<td>2017</td>
<td>104,675</td>
<td>65,305</td>
<td>- 4,564</td>
</tr>
<tr>
<td>2018</td>
<td>104,675</td>
<td>2018</td>
<td>2018</td>
<td>109,905</td>
<td>31,625</td>
<td>- 4,564</td>
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<tr>
<td>Total</td>
<td>$ 3,020</td>
<td>$ 254,043</td>
<td>$ 96,930</td>
<td>$ 234</td>
<td>$ 65,305</td>
<td>$ 44,119</td>
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### SCHEDULE OF LONG TERM DEBT,
PRINCIPAL AND INTEREST REQUIREMENTS
(Dollars in Thousands)
DECEMBER 31, 2008
(Continued)

<table>
<thead>
<tr>
<th></th>
<th>Series 1998</th>
<th></th>
<th>Series 2001</th>
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<tr>
<td></td>
<td>Principal</td>
<td>Interest</td>
<td>Principal</td>
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<tr>
<td>Water Division:</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>$ 1,405</td>
<td>$ 272</td>
<td>$ 1,830</td>
<td>$ 39</td>
</tr>
<tr>
<td>2010</td>
<td>1,465</td>
<td>205</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>1,540</td>
<td>126</td>
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<tr>
<td>2012</td>
<td>1,625</td>
<td>43</td>
<td></td>
<td></td>
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<tr>
<td>Total</td>
<td>$ 6,035</td>
<td>$ 646</td>
<td>$ 1,830</td>
<td>$ 39</td>
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</table>
### Electric Division Rate Class

<table>
<thead>
<tr>
<th>Rate Class</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Residential – Schedule RS</td>
<td>Effective meters read on or after September 25, 2008.</td>
<td>361,399</td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$11.20 per month, less hydro allocation credit: $1.71</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>First 2,000 kWh per month at 7.481 cents per kWh; Additional kWh per month at 8.335 cents per kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.</td>
<td></td>
</tr>
<tr>
<td>General Service – Schedule GSA</td>
<td>Effective meters read on or after September 25, 2008.</td>
<td>43,733</td>
</tr>
<tr>
<td>If (a) the higher of (i) the customer’s currently effective contract demand, if any, or (ii) its highest billing demand during the latest twelve-month period is not more than 50 kW, and (b) customer’s monthly energy taking for any month during such period does not exceed 15,000 kWh:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$15.52 per delivery point per month</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>8.614 cents per kWh</td>
<td></td>
</tr>
<tr>
<td>If (a) the higher of (i) the customer’s currently effective contract demand or (ii) its highest billing demand during the latest twelve-month period is greater than 50kW but not more than 1,000 kW, or (b) if the customer’s billing demand is less than 50kW and its energy takings for any month during such period exceed 15,000 kWh.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$53.42 per delivery point per month</td>
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</tr>
<tr>
<td>Demand charge:</td>
<td>First 50kW of billing demand per month, no demand charge</td>
<td></td>
</tr>
<tr>
<td>Excess over 50kW of billing demand per month, at $12.91 per kW</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>First 15,000 kWh per month at 9.198 cents per kWh; Additional kWh per month at 4.347 cents per kWh</td>
<td></td>
</tr>
<tr>
<td>If the higher of the customer’s currently effective contract demand or its highest billing demand during the latest twelve-month period is greater than 1,000 kW.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$191.84 per delivery point per month</td>
<td></td>
</tr>
<tr>
<td>Electric Division Rate Class (cont.)</td>
<td>Base Charge</td>
<td>Customers</td>
</tr>
<tr>
<td>-------------------------------------</td>
<td>-----------------------------------------------------------------------------</td>
<td>-----------</td>
</tr>
<tr>
<td>Demand charge:</td>
<td>First 1,000 kW of billing demand per month, at $12.49 per kW</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Excess over 1,000 kW of billing demand per month, at $14.32 per kW, plus an additional $14.32 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds the higher of 2,500 kW or its contract demand</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>4.647 cents per kWh per month</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.</td>
<td></td>
</tr>
<tr>
<td>General Service – Schedule GSB</td>
<td>Effective meters read on or after September 25, 2008.</td>
<td>26</td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$1,500 per delivery point per month</td>
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</tr>
<tr>
<td>Demand charge:</td>
<td>$14.67 per kW of billing demand per month, plus an additional $14.67 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>First 620 hours use of metered demand per month at 3.918 cents per kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Additional kWh per month at 3.199 cents per kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.</td>
<td></td>
</tr>
<tr>
<td>General Service – Schedule GSC</td>
<td>Effective meters read on or after September 25, 2008.</td>
<td>0</td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$1,500 per delivery point per month</td>
<td></td>
</tr>
<tr>
<td>Demand charge:</td>
<td>$14.14 per kW of billing demand per month, plus an additional $14.14 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>First 620 hours use of metered demand per month at 3.918 cents per kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Additional kWh per month at 3.199 cents per kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.</td>
<td></td>
</tr>
<tr>
<td>General Service – Schedule GSD</td>
<td>Effective meters read on or after September 25, 2008.</td>
<td>0</td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$1,500 per delivery point per month</td>
<td></td>
</tr>
</tbody>
</table>
# SCHEDULE OF CURRENT UTILITY RATES
## DECEMBER 31, 2008
(Continued)

<table>
<thead>
<tr>
<th>Electric Division Rate Class (cont.)</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Demand charge:</td>
<td>$17.06 per kW of billing demand per month, plus an additional $17.06 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>3.075 cents per kWh per month</td>
<td></td>
</tr>
</tbody>
</table>

The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.

**Manufacturing – Schedule MSB**

Effective meters read on or after September 25, 2008.

If the customer’s metered demand for the month is not more than 5,000 kW:

- **Customer charge:** $1,500 per delivery point per month
- **Demand charge:** $12.60 per kW of billing demand per month, plus an additional $12.60 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand
- **Energy charge:** First 620 hours use of metered demand per month at 3.320 cents per kWh
  - Additional kWh per month at 2.710 cents per kWh

If the customer’s metered demand for the month is greater than 5,000 kW:

- **Customer charge:** $1,500.00 per delivery point per month
- **Demand charge:** $11.97 per kW of billing demand per month, plus an additional $11.97 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand
- **Energy charge:** First 620 hours use of metered demand per month at 3.155 cents per kWh
  - Additional kWh per month at 2.577 cents per kWh

The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.

**Manufacturing – Schedule MSC**

Effective meters read on or after September 25, 2008.

- **Customer charge:** $1,500 per delivery point per month
- **Demand charge:** $11.44 per kW of billing demand per month, plus an additional $11.44 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand
<table>
<thead>
<tr>
<th>Electric Division Rate Class (cont.)</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Manufacturing – Schedule MSD</strong></td>
<td>Effective meters read on or after September 25, 2008.</td>
<td>4</td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$1,500 per delivery point per month</td>
<td></td>
</tr>
<tr>
<td>Demand charge:</td>
<td>$13.77 per kW of billing demand per month, plus an additional $13.77 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>2.487 cents per kWh per month</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.</td>
<td></td>
</tr>
<tr>
<td><strong>Time-Of-Day – Schedule TGSA</strong></td>
<td>Effective meters read on or after September 25, 2008.</td>
<td>1</td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$198.95 per delivery point per month.</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>14.812 cents per kWh per month for all onpeak kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4.820 cents per kWh per month for all offpeak kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>If the higher of (1) the higher of the customer’s currently effective onpeak or offpeak contract demand or (2) its highest onpeak or offpeak billing demand during the latest 12 month period is not more than 50 kW:</td>
<td></td>
</tr>
<tr>
<td>Customer charge:</td>
<td>$198.95 per delivery point per month.</td>
<td></td>
</tr>
<tr>
<td>Demand charge:</td>
<td>$13.28 per kW of the customer’s onpeak billing demand, plus $4.05 per month for each kW, if any, of the amount by which the customer’s offpeak billing demand exceeds its onpeak billing demand.</td>
<td></td>
</tr>
<tr>
<td>Energy charge:</td>
<td>6.135 cents per kWh per month for all onpeak kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3.911 cents per kWh per month for all offpeak kWh</td>
<td></td>
</tr>
<tr>
<td></td>
<td>If the higher of (1) the higher of the customer’s currently effective onpeak or offpeak contract demand or (2) the customer’s highest onpeak or offpeak billing demand during the latest 12-month period is greater than 1,000 kW:</td>
<td></td>
</tr>
</tbody>
</table>
Electric Division Rate Class (cont.)  Base Charge  Customers

Customer charge:  $198.95 per delivery point per month

Demand charge:  $13.98 per kW per month of the customer’s onpeak billing demand, plus $2.90 per month for each kW, if any, of the amount by which (1) the customer’s onpeak billing demand exceeds the higher of 2,500 kW or its onpeak contract demand or (2) the customer’s offpeak billing demand exceeds the higher of 2,500 kW or its offpeak contract demand, whichever is higher.

Energy charge:  5.958 cents per kWh per month for all onpeak kWh
3.718 cents per kWh per month for all offpeak kWh

Outdoor Lighting- Schedule LS  Effective meters read on or after September 25, 2008.  17,017

Part A – Charges for street and park lighting systems, traffic signal systems, and athletic field lighting installations.

Energy charge:  5.718 cents per kWh per month
This rate is subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.
### Electric Division Rate Class (cont.)

<table>
<thead>
<tr>
<th>Outdoor Lighting Facilities charge:</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td>The annual facility charge shall be 9.84% of the installed cost to the Division’s electric system of the facility devoted to street and park lighting service specified in this Part A. Such installed cost shall be recomputed on July 1 of each year, or more often if substantial changes in the facilities are made. Each month, one-twelfth of the then total annual facility charge shall be billed to the customer. If any part of the facilities has not been provided at the electric system’s expense or if the installed cost of any portion thereof is reflected on the books of another municipality or agency or department, the annual facility charge shall be adjusted to reflect properly the remaining cost to be borne by the electric system.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Traffic signal systems and athletic field lighting installations shall be provided, owned, and maintained by and at the expense for the customer, except as Division may agree otherwise in accordance with the provisions of the paragraph next following in this section. The facilities necessary to provide service to such systems and installations shall be provided by and at the expense of Division’s electric system, and the annual facility charge provided for first above in this section shall apply to the installed cost of such facilities.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>When so authorized by policy duly adopted by Division’s governing board, traffic signal systems and athletic field lighting installations may be provided, owned and maintained by Division’s electric system for the customer’s benefit. In such cases Division may require reimbursement from the customer for a portion of the initial installed cost of any such system or installation and shall require payment by the customer of a facility charge sufficient to cover all of Division’s costs (except reimbursed costs), including appropriate overheads, of providing, owning, and maintaining such system or installation; provided that, for athletic field lighting installations, such facility charge shall in no case be less than 12% per year of such costs. Said facility charge will be in addition to the annual facility charge on the facilities necessary to provide service to such system or installation as provided for in the preceding paragraph.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Electric Division Rate Class (cont.)

<table>
<thead>
<tr>
<th>Part B – Charges for outdoor lighting for individual customers – charges per fixture per month</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Watts</th>
<th>Lamp Size (Lumens)</th>
<th>Rated (kWh)</th>
<th>Charge</th>
</tr>
</thead>
<tbody>
<tr>
<td>175</td>
<td>7,650</td>
<td>70</td>
<td>$2.95</td>
</tr>
<tr>
<td>250</td>
<td>10,400</td>
<td>98</td>
<td>3.49</td>
</tr>
<tr>
<td>400</td>
<td>19,100</td>
<td>155</td>
<td>4.42</td>
</tr>
<tr>
<td>700</td>
<td>33,600</td>
<td>266</td>
<td>5.96</td>
</tr>
<tr>
<td>1,000</td>
<td>47,500</td>
<td>378</td>
<td>7.59</td>
</tr>
</tbody>
</table>

(a) Type of fixture

- **Mercury Vapor or Incandescent**
  - 175 Watts, 7,650 Lumens, 70 kWh, $2.95
  - 250 Watts, 10,400 Lumens, 98 kWh, 3.49
  - 400 Watts, 19,100 Lumens, 155 kWh, 4.42
  - 700 Watts, 33,600 Lumens, 266 kWh, 5.96
  - 1,000 Watts, 47,500 Lumens, 378 kWh, 7.59

- **Metal Halide**
  - 175 Watts, 8,300 Lumens, 70 kWh, 2.95
  - 250 Watts, 14,000 Lumens, 98 kWh, 3.49
  - 400 Watts, 22,600 Lumens, 155 kWh, 4.42
  - 1,000 Watts, 88,000 Lumens, 378 kWh, 7.59

- **High Pressure Sodium**
  - 50 Watts, 3,285 Lumens, 22 kWh, 4.19
  - 100 Watts, 8,550 Lumens, 42 kWh, 4.48
  - 150 Watts, 14,400 Lumens, 63 kWh, 4.61
  - 200 Watts, 18,900 Lumens, 82 kWh, 5.01
  - 250 Watts, 23,000 Lumens, 105 kWh, 5.30
  - 400 Watts, 45,000 Lumens, 165 kWh, 6.29
  - 1,000 Watts, 126,000 Lumens, 385 kWh, 10.05

### Gas Division Rate Class

<table>
<thead>
<tr>
<th>Gas Division Rate Class</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Residential G-1 &amp; G-3</td>
<td>Effective meters read on or after December 26, 2007</td>
<td>293,272</td>
</tr>
<tr>
<td></td>
<td>Schedule G-1 is available for domestic use to residential customers in individual private residences or other individual dwelling units situated within the corporate limits of the City of Memphis, Tennessee. Schedule G-3 is available for domestic use to residential customers in individual private residences or other individual dwelling units situated outside the corporate limits of the City of Memphis, Tennessee.</td>
<td></td>
</tr>
<tr>
<td>Service charge:</td>
<td>$10.00 per month plus</td>
<td></td>
</tr>
<tr>
<td>Commodity charge:</td>
<td>First 100 ccf per month @ $1.081 per ccf</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Excess over 100 ccf per month @ $0.991 per ccf, plus the above rates are subject to adjustment under the provisions of the Purchased Gas Adjustment Rider.</td>
<td></td>
</tr>
<tr>
<td>Minimum bill:</td>
<td>$10.00 per meter per month</td>
<td></td>
</tr>
<tr>
<td>Small General Service G-7</td>
<td>Effective meters read on or after December 26, 2007</td>
<td>22,184</td>
</tr>
<tr>
<td></td>
<td>This rate schedule is available for gas service to all gas customers except residential</td>
<td></td>
</tr>
</tbody>
</table>
### Gas Division Rate Class (cont.)

<table>
<thead>
<tr>
<th>Service charge:</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>For 0 to 250 ccf meter, $25.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Over 250 to 1,000 ccf meter, $50.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Over 1,000 ccf meter, $100.00 per month plus,</td>
<td></td>
</tr>
</tbody>
</table>

| Commodity charge: | All gas consumed: $1.021 per Ccf per month, plus |
|                  | The above rates are subject to adjustment under the provisions of the Purchased Gas Adjustment Rider. |

| Minimum bill: | The minimum monthly bill shall be $0.654 for each Ccf of the higher of: |
|              | (1) The maximum daily demand during the preceding eleven months, or |
|              | (2) The daily contract demand, but in no case less than the Service charge listed above. |

#### Large General Service Firm on-peak G-8 and G-9

- Effective meters on or after December 26, 2007
- This rate schedule is available for gas service to all customers contracting for not less than 100 Ccf of maximum daily demand.
- Demand charge: $0.251 Ccf per month of contract demand or maximum daily demand during the twelve (12) months ending with the billing month, whichever is higher, plus
- Commodity Charge: First 200,000 Ccf per month @ $0.978 ccf
- Excess over 200,000 Ccf per month @ $0.864 ccf, plus
- The above rates are subject to adjustment under the provisions of the Purchased Gas Adjustment Rider.
- Minimum bill: The minimum bill shall be $0.904 for Ccf of the higher of: (1) the maximum Daily Demand during the twelve (12) months ending with the billing month, or (2) the Daily Contract Demand.

#### Large General Service Interruptible Off-peak G-10 and G-12

- Effective December 26, 2007
- This rate schedule is available for gas service to all customers contracting for not less than 1,500 Ccf of maximum daily demand and providing oil or other alternate fuel facilities approved by the Division as being adequate in design and capacity.
### Gas Division Rate Class

#### Base Charge
- **Customers**: $500.00 per month, plus
  - First 200,000 Ccf per month @ $0.948 Ccf
  - Excess over 200,000 Ccf per month @ $0.864 per Ccf, plus

#### Minimum bill:
- The minimum monthly bill shall be $0.350 for each Ccf of the higher of (1) the maximum daily demand during the twelve months ending with the billing month, or (2) the daily contract demand, but in no event less than $500.00.

### Water Division Rate Class

<table>
<thead>
<tr>
<th>Class</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Residential – Inside City Rate</td>
<td>Effective meters read on or after June 26, 2008 For water furnished to premises entirely within the corporate limits of the City of Memphis</td>
<td>186,671</td>
</tr>
<tr>
<td>Commodity charge:</td>
<td>All water consumed: $1.31 per Ccf per month</td>
<td></td>
</tr>
<tr>
<td>Minimum bill:</td>
<td>The minimum monthly bill shall be determined by the size of the meter installed, as follows:</td>
<td></td>
</tr>
<tr>
<td>5/8&quot; meter</td>
<td>$ 5.54</td>
<td></td>
</tr>
<tr>
<td>3/4&quot; meter</td>
<td>7.99</td>
<td></td>
</tr>
<tr>
<td>1&quot; meter</td>
<td>14.18</td>
<td></td>
</tr>
<tr>
<td>1-1/2&quot; meter</td>
<td>31.91</td>
<td></td>
</tr>
<tr>
<td>2&quot; meter</td>
<td>56.72</td>
<td></td>
</tr>
</tbody>
</table>

| Residential – Outside City Rate | Effective meters read on or after June 26, 2008 For water furnished to premises outside the corporate limits of the City of Memphis | 21,701 |
| Commodity charge:              | All water consumed: $2.04 per Ccf per month                                  |         |
| Minimum bill:                  | The minimum monthly bill shall be determined by the size of the meter installed, as follows: |         |
| 5/8" meter                    | $ 7.71                                                                      |           |
| 3/4" meter                    | 11.09                                                                       |           |
| 1" meter                      | 19.74                                                                       |           |
| 1-1/2" meter                  | 44.39                                                                       |           |
| 2" meter                      | 78.91                                                                       |           |
### SCHEDULE OF CURRENT UTILITY RATES

**DECEMBER 31, 2008**

(Continued)

<table>
<thead>
<tr>
<th>Water Division Rate Class (cont.)</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>General Service – Inside City Rate</strong></td>
<td>Effective meters read on or after June 26, 2008</td>
<td>18,781</td>
</tr>
<tr>
<td>For water service to all customers within the corporate limits of the City of Memphis, except residential customers</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Commodity charge:</strong></td>
<td>Water consumed per month:</td>
<td></td>
</tr>
<tr>
<td>First 30 Ccf</td>
<td>$1.67 per Ccf</td>
<td></td>
</tr>
<tr>
<td>Next 70 Ccf</td>
<td>$1.42 per Ccf</td>
<td></td>
</tr>
<tr>
<td>Next 100 Ccf</td>
<td>$1.08 per Ccf</td>
<td></td>
</tr>
<tr>
<td>Next 400 Ccf</td>
<td>$0.90 per Ccf</td>
<td></td>
</tr>
<tr>
<td>Next 5,400 Ccf</td>
<td>$0.70 per Ccf</td>
<td></td>
</tr>
<tr>
<td>Excess over 6,000 Ccf</td>
<td>$0.73 per Ccf</td>
<td></td>
</tr>
</tbody>
</table>

**Minimum bill:**

The minimum monthly bill shall be determined by the size of the meter installed, as follows:

<table>
<thead>
<tr>
<th>Size of Meter</th>
<th>Minimum Bill</th>
</tr>
</thead>
<tbody>
<tr>
<td>5/8&quot; meter</td>
<td>$10.62</td>
</tr>
<tr>
<td>3/4&quot; meter</td>
<td>12.37</td>
</tr>
<tr>
<td>1&quot; meter</td>
<td>21.21</td>
</tr>
<tr>
<td>1-1/2&quot; meter</td>
<td>42.44</td>
</tr>
<tr>
<td>2&quot; meter</td>
<td>88.45</td>
</tr>
<tr>
<td>3&quot; meter</td>
<td>176.84</td>
</tr>
<tr>
<td>4&quot; meter</td>
<td>264.45</td>
</tr>
<tr>
<td>6&quot; meter</td>
<td>334.53</td>
</tr>
<tr>
<td>8&quot; meter</td>
<td>404.63</td>
</tr>
<tr>
<td>10&quot; meter</td>
<td>838.18</td>
</tr>
<tr>
<td>12&quot; meter</td>
<td>1,169.54</td>
</tr>
<tr>
<td>14&quot; meter</td>
<td>1,608.13</td>
</tr>
</tbody>
</table>

Battery of 2-2" meters | 176.84  |
Battery of 3-2" meters | 264.45  |

<p>| <strong>General Service – Outside City Rate</strong> | Effective meters read on or after June 26, 2008 | 776 |
| For water service to all customers outside the corporate limits of the City of Memphis, except residential customers |
| <strong>Commodity charge:</strong> | Water consumed per month: |
| First 30 Ccf | $2.51 per Ccf |
| Next 70 Ccf | $2.11 per Ccf |
| Next 100 Ccf | $1.61 per Ccf |
| Next 400 Ccf | $1.35 per Ccf |
| Next 5,400 Ccf | $1.06 per Ccf |
| Excess over 6,000 Ccf | $1.10 per Ccf |</p>
<table>
<thead>
<tr>
<th>Water Division Rate Class (cont.)</th>
<th>Base Charge</th>
<th>Customers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum bill:</td>
<td>The minimum monthly bill shall be determined by the size of the meter installed, as follows:</td>
<td></td>
</tr>
<tr>
<td>5/8&quot; meter</td>
<td>$16.22</td>
<td></td>
</tr>
<tr>
<td>3/4&quot; meter</td>
<td>18.93</td>
<td></td>
</tr>
<tr>
<td>1&quot; meter</td>
<td>32.45</td>
<td></td>
</tr>
<tr>
<td>1-1/2&quot; meter</td>
<td>64.88</td>
<td></td>
</tr>
<tr>
<td>2&quot; meter</td>
<td>135.18</td>
<td></td>
</tr>
<tr>
<td>3&quot; meter</td>
<td>270.39</td>
<td></td>
</tr>
<tr>
<td>4&quot; meter</td>
<td>404.09</td>
<td></td>
</tr>
<tr>
<td>6&quot; meter</td>
<td>511.20</td>
<td></td>
</tr>
<tr>
<td>8&quot; meter</td>
<td>618.30</td>
<td></td>
</tr>
<tr>
<td>10&quot; meter</td>
<td>1,280.82</td>
<td></td>
</tr>
<tr>
<td>12&quot; meter</td>
<td>1,787.17</td>
<td></td>
</tr>
<tr>
<td>14&quot; meter</td>
<td>2,455.69</td>
<td></td>
</tr>
<tr>
<td>Battery of 2-2&quot; meters</td>
<td>270.39</td>
<td></td>
</tr>
<tr>
<td>Battery of 3-2&quot; meters</td>
<td>404.09</td>
<td></td>
</tr>
</tbody>
</table>

### Residential – Shelby County Water Distribution System

Effective meters read on or after June 26, 2008  
20,695

For water service within the area served by the Shelby County Water Distribution System at the time of its acquisition on June 30, 1999, for domestic uses to residential customers in individual private residences or other individual dwelling places.

Monthly rate:  
All water consumed $2.04 per Ccf per month

Minimum bill:  
The minimum monthly bill shall be determined by the size of the meter installed, as follows:

| 5/8\" meter | $7.71 |
| 3/4\" meter | 11.09 |
| 1\" meter   | 19.74 |
| 1-1/2\" meter | 44.39 |
| 2\" meter   | 78.91 |

Residential customers shall be served through a single meter not larger than 2\" in size.
### Water Division Rate Class (cont.)

<table>
<thead>
<tr>
<th>Base Charge</th>
<th>Customers</th>
<th>Effective meters read on or after June 26, 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial - Industrial – Shelby County</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Water Distribution System</td>
<td></td>
<td></td>
</tr>
<tr>
<td>For water service within the area served by the</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Shelby County Water Distribution System at the</td>
<td></td>
<td></td>
</tr>
<tr>
<td>time of its acquisition on June 30, 1999, for</td>
<td></td>
<td></td>
</tr>
<tr>
<td>all customers except residential customers using</td>
<td></td>
<td></td>
</tr>
<tr>
<td>service exclusive for domestic use.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Monthly rate:

- **Water consumed per month:**
  - First 30 Ccf: $2.51 per Ccf
  - Next 70 Ccf: $2.11 per Ccf
  - Next 100 Ccf: $1.61 per Ccf
  - Next 400 Ccf: $1.35 per Ccf
  - Next 5,400 Ccf: $1.06 per Ccf
  - Excess over 6000 Ccf: $1.10 per Ccf

#### Minimum bill:

The minimum monthly bill shall be determined by the size of the meter installed, as follows:

- 5/8" meter: $16.22
- 3/4" meter: $18.93
- 1" meter: $32.45
- 1-1/2" meter: $64.88
- 2" meter: $135.18
- 3" meter: $270.39
- 4" meter: $404.09
- 6" meter: $511.20
- 8" meter: $618.30
- 10" meter: $1,280.82
- 12" meter: $1,787.17
- 14" meter: $2,455.69
### SCHEDULE OF INSURANCE

(Dollars in Thousands)

**DECEMBER 31, 2008**

<table>
<thead>
<tr>
<th>Type of Coverage</th>
<th>Amount of Coverage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property</td>
<td>$500,000</td>
</tr>
<tr>
<td>LNG Plants</td>
<td>80,615</td>
</tr>
<tr>
<td>Crime</td>
<td>1,000</td>
</tr>
<tr>
<td>Travel Accident</td>
<td>1,000</td>
</tr>
</tbody>
</table>
## Required Schedule of Funding Progress for OPEB
### December 31, 2008
(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Actuarial Valuation Date</th>
<th>Actuarial Value of Assets (a)</th>
<th>Actuarial Accrued Liability (AAL) Entry-Age Normal (b)</th>
<th>Unfunded AAL (UAAL) (b - a)</th>
<th>Funded Ratio (a / b)</th>
<th>Covered Payroll (c)</th>
<th>UAAL as a Percentage of Covered Payroll ((b - a) / c)</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 31, 2007</td>
<td>$15,097</td>
<td>$694,574</td>
<td>$679,477</td>
<td>2.2%</td>
<td>$144,756</td>
<td>469.4%</td>
</tr>
<tr>
<td>December 31, 2006*</td>
<td>-</td>
<td>743,484</td>
<td>743,484</td>
<td>0.0%</td>
<td>148,219</td>
<td>501.6%</td>
</tr>
</tbody>
</table>

* Projected from 12/31/05 valuation
** Projected from 2006 payroll
### Required Schedule of Employer Contributions

**December 31, 2008**

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Fiscal Year Ended</th>
<th>Annual OPEB Cost</th>
<th>Employer Contributions</th>
<th>Percentage of Annual OPEB Cost Contributed</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 31, 2008</td>
<td>$ 57,991</td>
<td>$ 66,881</td>
<td>115.3%</td>
</tr>
<tr>
<td>December 31, 2007</td>
<td>57,991</td>
<td>51,253</td>
<td>88.4%</td>
</tr>
</tbody>
</table>
### Actuarial Funding Progress

<table>
<thead>
<tr>
<th>Actuarial Valuation Date</th>
<th>Actuarial Value of Assets (a)</th>
<th>Actuarial Accrued Liability (AAL)¹</th>
<th>Unfunded/Overfunded (b - a)</th>
<th>Funded Ratio (a / b)</th>
<th>Covered Payroll (c)</th>
<th>UAAL as a Percentage of Covered Payroll* ((b - a) / c)</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 1, 2009</td>
<td>$1,172,879</td>
<td>$1,303,190</td>
<td>$130,311</td>
<td>90.0%</td>
<td>$150,253</td>
<td>86.7%</td>
</tr>
<tr>
<td>January 1, 2008</td>
<td>1,258,670</td>
<td>1,240,867</td>
<td>(17,803)</td>
<td>101.4%</td>
<td>146,830</td>
<td>0.0%</td>
</tr>
<tr>
<td>January 1, 2007</td>
<td>1,194,563</td>
<td>1,237,459</td>
<td>42,896</td>
<td>96.5%</td>
<td>143,929</td>
<td>29.8%</td>
</tr>
</tbody>
</table>

* Not less than zero

¹ The aggregate actuarial cost method is used to determine the annual required contribution of MLGW's Pension Plan. Because the method does not identify or separately amortize unfunded actuarial liabilities, information about the funded status and funding progress is prepared using the entry age normal actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress of the MLGW Pension Plan.
<table>
<thead>
<tr>
<th></th>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Water Treated and Purchased:</td>
<td></td>
</tr>
<tr>
<td>B</td>
<td>Water Pumped (potable)</td>
<td>52,364,108,000</td>
</tr>
<tr>
<td>C</td>
<td>Water Purchased</td>
<td>-</td>
</tr>
<tr>
<td>D</td>
<td><strong>Total Water Treated and Purchased</strong></td>
<td>52,364,108,000</td>
</tr>
<tr>
<td>E</td>
<td>Accounted for Water:</td>
<td></td>
</tr>
<tr>
<td>F</td>
<td>Water Sold (includes free water for City of Memphis, bulk sales, and water bill adjustments)</td>
<td>45,479,339,991</td>
</tr>
<tr>
<td>G</td>
<td>Metered for Consumption (in house usage)</td>
<td>410,400,000</td>
</tr>
<tr>
<td>H</td>
<td>Fire Department Usage</td>
<td>13,396,287</td>
</tr>
<tr>
<td>I</td>
<td>Flushing</td>
<td>10,242,000</td>
</tr>
<tr>
<td>J</td>
<td>Tank Cleaning/Filling</td>
<td>-</td>
</tr>
<tr>
<td>K</td>
<td>Street Cleaning</td>
<td>395,570</td>
</tr>
<tr>
<td>L</td>
<td>Bulk Sales</td>
<td>-</td>
</tr>
<tr>
<td>M</td>
<td>Water Bill Adjustments</td>
<td>-</td>
</tr>
<tr>
<td>N</td>
<td>Other (explain)</td>
<td>-</td>
</tr>
<tr>
<td>O</td>
<td><strong>Total Accounted for Water</strong></td>
<td>45,913,773,848</td>
</tr>
<tr>
<td>P</td>
<td>Unaccounted for Water</td>
<td>6,450,334,152</td>
</tr>
<tr>
<td>Q</td>
<td>Percent Unaccounted for Water</td>
<td>12.3%</td>
</tr>
<tr>
<td>R</td>
<td>Cost per 1,000 gallons</td>
<td>$ 0.247</td>
</tr>
<tr>
<td>S</td>
<td>Cost of Unaccounted for Water</td>
<td>$ 1,592,043.31</td>
</tr>
</tbody>
</table>

**Explained Other:**
INDEPENDENT AUDITORS’ REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Commissioners and Management
Memphis Light, Gas and Water Division
Memphis, Tennessee

We have audited the financial statements of the Electric, Gas, and Water Divisions (the Divisions) of Memphis Light, Gas and Water Division, enterprise funds of the City of Memphis, Tennessee, as of and for the year ended December 31, 2008, and have issued our report thereon dated May 7, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Divisions’ internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Divisions’ internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Divisions’ internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Divisions’ ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Divisions’ financial statements that is more than inconsequential will not be prevented or detected by the Divisions’ internal control.

1661 Aaron Brenner Drive, Ste. 300 • Memphis, Tennessee 38120 (901) 761-2720 • Fax: (901) 683-1120 • www.wucpas.com
A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Divisions' internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Divisions' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

We noted certain matters that we reported to management of the Divisions in a separate letter dated May 7, 2009.

This report is intended solely for the information and use of the Audit Committee, Board of Commissioners, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Memphis, Tennessee
May 7, 2009
INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Commissioners and Management
Memphis Light, Gas and Water Division
Memphis, Tennessee

Compliance

We have audited the compliance of the Electric, Gas, and Water Divisions (the Divisions) of Memphis Light, Gas and Water Division, enterprise funds of the City of Memphis, Tennessee, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal program for the year ended December 31, 2008. The Divisions’ major federal program is identified in the summary of auditors’ results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the Divisions’ management. Our responsibility is to express an opinion on the Divisions’ compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Divisions’ compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Divisions’ compliance with those requirements.

In our opinion, the Divisions complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2008.
Internal Control Over Compliance

The management of the Divisions is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Divisions' internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Divisions' internal control over compliance.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the Audit Committee, Board of Commissioners, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Memphis Tennessee
May 7, 2009
## SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2008
(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Federal Grantor/Pass-Through Grantor</th>
<th>CFDA Number</th>
<th>Contract Number</th>
<th>Beginning (Accrued)</th>
<th>Cash Receipts</th>
<th>Endng (Accrued)</th>
<th>Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Program 97.036</strong></td>
<td></td>
<td></td>
<td>$</td>
<td>-</td>
<td>$2,337</td>
<td>$2,452</td>
</tr>
<tr>
<td><strong>Total Federal Awards</strong></td>
<td></td>
<td></td>
<td>$(92)</td>
<td>$2,447</td>
<td>$2,495</td>
<td></td>
</tr>
</tbody>
</table>

### BASIS OF PRESENTATION

The schedule of Expenditures of Federal Awards (the Schedule) presents the grant activity of the federal award programs of the Electric, Gas and Water divisions of Memphis Light, Gas and Water Division, an enterprise fund of the City of Memphis, Tennessee, for the year ended December 31, 2008. The schedule is prepared on the accrual basis of accounting and is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. MLGW generally follows the Federal Energy Regulatory Commission’s Uniform System of Accounts prescribed for Public Utilities.
MEMPHIS LIGHT, GAS AND WATER DIVISION

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For the Year Ended December 31, 2008

A. SUMMARY OF AUDITORS’ RESULTS

1. The auditors’ report expresses an unqualified opinion on the financial statements of the Electric, Gas and Water Divisions (the Divisions) of Memphis Light, Gas and Water Division, enterprise funds of the City of Memphis, Tennessee.

2. No significant deficiencies relating to the audit of the financial statements are reported.

3. No instances of noncompliance material to the financial statements of the Divisions were disclosed during the audit.

4. No significant deficiencies relating to the audit of the major federal award program are reported.

5. The auditors’ report on compliance for the major federal award program expresses an unqualified opinion.

6. The audit did not disclose any audit findings related to the major program that are required to be reported under Section 510(a) of OMB Circular A-133.

7. The program tested as a major program was: Department of Homeland Security, CFDA 97.036 – Public Assistance.

8. The threshold for distinguishing Types A and B programs was $300,000.

9. The Divisions were not determined to be a low risk auditee.

B. FINDINGS – FINANCIAL STATEMENTS AUDIT

None reported

C. FINDINGS AND QUESTIONED COSTS – MAJOR FEDERAL AWARD PROGRAM AUDIT

None reported