Here to Serve...

2011 ANNUAL REPORT

Memphis Light, Gas and Water Division

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"In every community, there is work to be done."

Author Marianne Williamson

Jerry Collins, MLGW President and CEO, volunteers annually as a guest speaker for Memphis City Schools' M^2 Career Day.

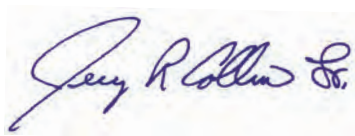
Letter from the President

The newly-christened MLGW mission statement, adopted early in the fiscal year, was a guiding tenet for 2011: To improve the quality of life for all Memphis and Shelby County customers through the efficient and safe delivery of electricity, natural gas and water.

But, what does the MLGW mission statement really mean? The bottom line is this: we are in the business of making Memphis a better place for everyone. Endeavoring to be the best utility for our customers, by its very definition, empowers our neighbors, friends and families in their daily pursuits. However, that's just the beginning. It also means that MLGW is a goodwill ambassador for the Bluff City.

Inherent in every decision, task or project is the underlying principle that we are here to serve for the betterment of our community. Going the extra mile. Exceeding customer expectations. Providing low rates. Assisting a neighbor in need. Promoting supplier diversity. Championing a worthwhile cause. These are the touchstones governing who we are as an organization.

As you read the 2011 Annual Report, examples of employees' resolve to fulfill our mission are clearly illustrated. Stories of inspiration, heroism, compassion, ingenuity—in some cases in the face of a formidable antagonist, Mother Nature—recap a year aligned with our mission. Moving forward, the challenge is to continue MLGW's focus on enhancing customer experiences, becoming more efficient, and on a broader scope serving the residents of Memphis and Shelby County; there's work to be done.



Mission Statement:

To improve the quality of life for all Memphis and Shelby County customers through the efficient and safe delivery of electricity, natural gas and water.

MLGW Board of Commissioners

(As of 12/31/2011)

Darrell T. Cobbins, 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. He served on the Memphis-Shelby County Economic Growth Planning Committee (Memphis Fast Forward) in 2006 and has served on Baptist Memorial Hospital's Memphis Community Advisory Board. In 1998, he was named among the "Top 40 under 40" on the Memphis Business Journal's prestigious list.

Dedrick Brittenum Jr., Vice Chair

Mr. Brittenum is a partner in the law firm of Brittenum Bruce PLLC. His practice concentrates in the areas of business litigation, construction, government and property. He has served as both a member of the Supreme Court of Tennessee Commission on Continuing Legal Education and as a member of the Memphis City Council. He currently chairs MLGW's Natural Gas Hedging Committee and serves on the utility's Audit Committee.

V. Lynn Evans

Ms. Evans is the owner of a certified public accounting and consulting firm providing professional services with an emphasis on small businesses, nonprofit organizations, local governmental units and the legal community. Evans served as Director of Internal Audit for The Regional Medical Center at Memphis for five years. Evans is a former Chairman of the MLGW Board of Commissioners. She currently chairs the MLGW Audit Committee and the MLGW Supplier Diversity Committee. Evans is also an Organizer and Director of First Alliance Bank.

Rick Masson

Rick Masson spent more than 20 years working for the City of Memphis. During his tenure with the city, Masson held several positions in the area of finance, including Director of Finance, Deputy Director of Finance and Budget Manager. Masson served as Chief Administrative Officer of the City of Memphis from 1996 to 2003. Since leaving the city, Masson served as the Executive Director of the Plough Foundation and as the Executive Director of the Shelby Farms Park Conservancy.

Steven Wishnia

As President and Managing Director of Highland Capital Management, Mr. Wishnia directs the company's management portfolios for pension plans, profit sharing plans, endowments and individuals. Wishnia is Trustee of the Plough Foundation and serves on the Board of Directors of Methodist Le Bonheur Healthcare and chairs MLGW's Finance Committee.

MLGW Executive Leadership

Jerry R. Collins Jr.
President and CEO

Christopher G. Bieber
Vice President of Customer Care

Von W. Goodloe
Vice President of Human Resources

Dana Jeanes
Vice President, CFO and Secretary-Treasurer

Nicholas Newman
Vice President of Construction and Maintenance

Cheryl W. Patterson
Vice President and General Counsel

Lashell Vaughn
Vice President and Chief Technology Officer

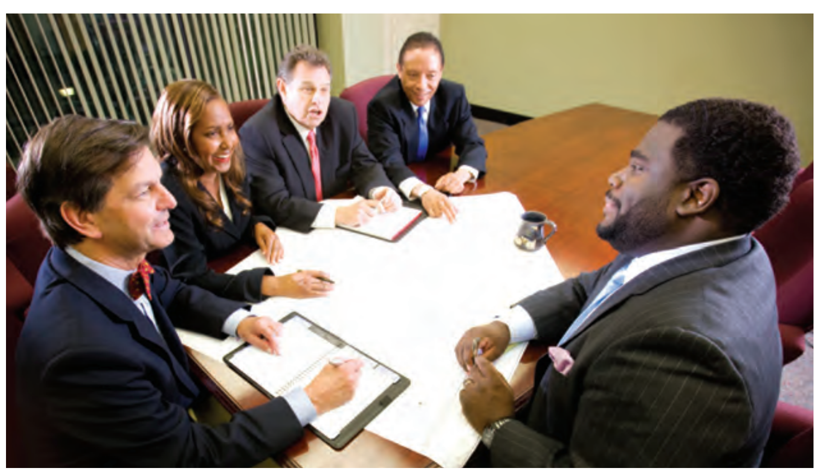
Alonzo Weaver III
Vice President of Engineering and Operations

Gale Jones Carson
Director of Corporate Communications

Clifford M. DeBerry
Director of Analysis, Strategy and Performance

Lesa J. Walton
Director of Internal Audit

Anderson D. Williams
Executive Analyst



Invested in the Community

In financial terms, when an individual invests in stocks or bonds, that person does so with the expectation that their initial outlay will reap a greater return. The same principle is at work with the investment MLGW makes in the Memphis community. Time, expertise and in some cases a helping hand, are the Division's commodities of trade. We anticipate future intangible dividends will positively impact the residents of Memphis and Shelby County in countless ways, improving their quality of life.


Project MAX has served low income seniors and the physically disabled since 1984.

Providing assistance to the elderly and disabled

One might expect a utility provider to offer payment assistance programs—and MLGW does—but with Project MAX, neighbors in need receive hands-on assistance that lasts way beyond a billing cycle. Since 1984, Project Max has provided assistance for qualifying low income elderly and physically disabled customers who cannot help themselves or have been turned away from other community service programs. Applicants must be 55 years or older, own and live in the home to be repaired and meet certain income guidelines. Types of repairs include attic insulation, window and door repairs, caulking and weather-stripping and plumbing repairs. In 2011, employees and volunteers weatherized 20 houses, built 9 wheelchair ramps and distributed 240 energy conservation kits.

Championing health causes

One measure of the vitality of a community is the overall health of its citizens. MLGW supports organizations that promote, educate and foster the well-being of the families in our service area. Employees raised funds cycling for Tour De Cure (American Diabetes Association) and Tour for a Cure (The Junior Diabetes Research Foundation) and walking for the American Heart Association, the March of Dimes and the National Kidney Foundation.

For the second consecutive year, Lifeblood named MLGW the Lifesaver of the Year. Employees donated 763 units of blood, making the Division a top donor organization. Potentially, Lifeblood could save 3,052 lives with MLGW blood donations, as one unit saves up to four lives.

The 13th annual Neighborhood Leaders Conference was attended by 150 grassroots leaders.

Mobilizing resources by giving the United Way

By supporting United Way, MLGW employees support the key areas the organization impacts: education, financial stability and health of area residents. While charitable giving is often an expense that is axed from personal budgets during economic downturns, employees continued their impressive tradition of generosity, earning a top six ranking in the employee-giving category for the 2011 United Way campaign, without any matching Division dollars.

Helping to build stronger communities

A vibrant city starts with strong neighborhoods. The 13th annual Neighborhood Leaders Conference (NLC) was a daylong event hosted by MLGW and designed to provide training and networking opportunities for 150 grassroots neighborhood association leaders in MLGW's service area. By equipping community leaders with information they can use to strengthen their areas—block by block—the net effect is a better home front for everyone. The 2011 theme was "Addressing Poverty." Educating the community about MLGW's policies, programs and services, while helping neighborhoods build stronger communities were goals of the event. Workshop topics ranged from working with ex-offenders to helping the homeless and from utility-cost cutting resources to fighting poverty with produce.

Reverend Keith Norman (far left) and Memphis Grizzlies forward Zach Randolph are congratulated on being 2011 recipients of the 2011 MLGW's Corporate Volunteer Award by Jerry Collins and MLGW Board Commissioner Darrell Cobbins.

Keeping the lights on for families in need

Doing the right thing is its own reward… Nonetheless, it's gratifying to be recognized. In 2011, Metropolitan Inter-Faith Association (MIFA) awarded MLGW the Corporate Volunteer of the Year Award. Since 1982, MLGW's customers and employees have donated millions to MIFA's utility assistance coffers by adding a few extra dollars to their utility bills earmarked for the Plus-1 program. Further, MLGW's EnergySmart program has been a valuable ally in MIFA's handyman improvement efforts for low-income senior homeowners by helping customers learn more about reducing energy usage.

Beacons of light

Metaphorically speaking, there are individuals who dispel the darkness—who inspire us with their charity. In the case of the 2011 Community Hero honorees, their philanthropic efforts—both figuratively and literally—light the way. Members of the community who give exemplary service and assistance to MLGW customers are honored by the MLGW Board of Commissioners with the MLGW Community Hero Award. Reverend Keith Norman, Senior Pastor of First Baptist Church-Broad and principal officer and founder of Greater Works, Inc., was recognized for his consistent, deep involvement in solving the needs of MLGW customers who are having difficulty paying their utility bills; many times with his own personal funds.

Zach Randolph, all-star forward for the Memphis Grizzlies, was honored for his generosity in paying utility bills for customers. Since 2010, Randolph has paid the utility bills of more than 100 customers during the winter months.

MLGW has been a sponsor of the Junior Fishing Rodeo for 10 years.

Junior Fishing Rodeo is more than a search for the biggest catch

For more than a decade, MLGW, Tennessee Wildlife Resources Agency (TWRA) and Germantown Parks & Recreation have sponsored the Junior Fishing Rodeo at Germantown's Johnson Road Park.

Nearly 400 want-to-be anglers, ages six to 12, participate in the event. While only one lucky child walks away with the grand prize–a lifetime hunting license and all expense paid trip–bicycles and other fun prizes are awarded. Every child gets something. Though the prizes are a big incentive, the family-oriented rodeo's real draw is a fun-filled day for kids and their caregivers to feel a connection with nature and the community.

Adopting Angels

The holiday season is supposed to be a time of good cheer. Yet, for families that are going through hard times it can be just the opposite.

Generously, MLGW employees made Christmas extra special for 65 children and 25 seniors by adopting 100 angels in the annual Salvation Army Angel Tree Drive. Employees from across the Division purchased 33 bikes, six microwaves, five televisions, clothes and small appliances, making the Christmas wishes of many a reality.

Vision:

To be the best utility for our customers.

Building Excellence Capital

Call it "raising the bar" or creating a new "gold standard," 2011 marked a year of building excellence capital by increasing the value of intangibles that improve the overall customer experience. Through corporate, team and individual efforts, MLGW's strategic objectives were taken to the next level by enlisting innovation, fiscal prudence and reliable service.

The spring storms of 2011 presented difficult challenges for MLGW crews working round-the-clock on restoration efforts.

MLGW earns American Public Power Association's (APPA) RP3®

For the third time in six years, Memphis Light, Gas and Water earned the American Public Power Association's (APPA) Reliable Public Power Provider (RP3 ®) recognition for providing consumers with the highest degree of reliable and safe electric service. A utility can qualify for the award once every two years.

In 2011, only 82 of the nation's more than 2,000 public power utilities earned recognition. The RP3® recognizes public power utilities that demonstrate proficiency in four key disciplines: reliability, safety, training and system improvement. Criteria within each category are based on sound business practices and represent a utility-wide commitment to safe and reliable delivery of electricity.

Weathering the storms

Reflecting on 2011, the defining events of the year can be summarized by five volatile spring storms, including three major storms in April and the subsequent historic flooding in May.

The three major storms of April 2011 impacted MLGW customers in record numbers, resulting in significant outages. Before 2011, MLGW had never sustained more than two such incidents in a single year. One storm in particular, on April 4, was the fifth strongest in recent history; 71,000 customers were affected.

Despite what appeared to be a number of seemingly endless weather challenges, 100 MLGW crews and 20 outside crews worked tirelessly to restore power to thousands of customers scattered across the county in a mere matter of days.

Utility peers rank MLGW as national social media leader

E Source, an independent research, advisory and information service for utility-related businesses, surveyed the nation's public utility providers and ranked MLGW second as a social media leader. Thanks to mobile applications, the Bird on a Wire blog, Twitter, Facebook and YouTube videos, MLGW trailed only Salt River Project in Phoenix, AZ.

Employees in MLGW's Electric Motor Shop designed and manufactured the Solid State Sump Pump pictured.

Representatives from E Source cited MLGW's proactive and customer-centric focus as reasons for the high rating.

Problem-solving innovation awarded U.S. patent

In the Fall of 2011, five employees from Electric Motor Shop, Transformers and Painting, received a patent for the Solid State Sump Pump Control they created. The people named in the patent were Al Bourell, then Supervisor of the Electric Motor Shop (now retired), Rick Cox, David Morton, Roderick Truitt and Curtis Washington. MLGW retains the intellectual property rights for the invention.

MLGW has an underground network transformer system. When water seeps in from underground ducts into transformer vaults and manholes, sump pumps are used to expel the water. The Electric Motor Shop used off-the-shelf controls that often became waterlogged and failed. The sump pump controls would have to be replaced and man-hours expended to get flooded transformers operational.

After investigating options from various vendors, the Shop began constructing its own Solid State Pump Control System with great success. The MLGW-created device's unique design features a protective cap and can withstand submersion in 25 feet of water—all at an approximate 33 percent cost savings compared to the off-the-shelf pumps.

In addition to saving money in the cost of producing the devices, the Division can potentially save thousands that would have gone to transformer vault maintenance expenses when the old units failed.

CNN study reveals Memphis' water has a low price-tag

People expect to pay a premium for quality. However, a March 2011 CNN investigative report revealed Memphis' great-tasting Artesian well purified aqua is a bargain. CNN cites a 2009/2010 study by Black & Veatch, a global consulting firm, which showed MLGW's water rates as the second lowest among the nation's 50 largest cities. Omaha was ranked number one and Nashville was 23rd on the list.

Values:

Customers,

Safety, Trust and Employees

Investing for the Future

Issues of energy conservation and sustainability are important to our customers—and they're important to us. The energy decisions made today will affect all of our tomorrows. MLGW and partners like TVA support initiatives that help save our ratepayers money and promote energy conservation.

Jason Simon, Supervisor, Substation Transmission Engineering, delivers a Smart Meter to customer Ginger Spickler.

Getting Smart

The Smart Grid Demonstration, begun in 2009, is a combination of equipment, communications and processes, employed to enhance internal operations, improve customer service and empower customers.

The project continued throughout 2011 with 1000 volunteers utilizing the Smart Meters to monitor utility usage and provide invaluable feedback on their experiences.

In addition, half of the participating Smart Grid volunteers qualified for free IHDs or In-home Display devices. Delivery occurred during the summer—a peak-time when participants can utilize information about individual electricity consumption to adjust usage. The IHD communicates wirelessly with the smart meter, providing almost instantaneous feedback on electricity status.

Memphis is on the EV Map

MLGW encourages the expanded use of electric vehicles (EV) as alternatives to petroleum-fueled vehicles. To that end, Memphis Mayor A C Wharton Jr., MLGW, TVA and ECOtality officially opened the first public EV charging station in July of 2011 at the Peabody Hotel. The charging station can accommodate all electric vehicles including the Tennessee-manufactured Nissan Leaf. The EV project is the largest deployment of electric vehicles and charge infrastructure in history.

MLGW has added four EV sedans to its fleet, and will add EV bucket trucks in 2012. MLGW is also collaborating with TVA and EPRI on an initiative to study incentives for adopting EVs in non-road applications. The Division's support for EV initiatives underscores MLGW's commitment to clean energy technology.

EnergySmart workshops held at area libraries reached 1,230 residents.

Teaching conservation at area libraries

Library users are information seekers. Library branches are located across the county, anchoring many communities—making perfect locales for energy-saving outreach. The Memphis Public Library and Information Center hosted 62 workshops conducted by energy technicians and attended by 1,230 residents.

The workshops imparted practical tips on simple, energy-efficient home improvements that can shave dollars off a homeowner's utility bill. To sweeten the deal, totes with helpful gadgets, including a caulk gun and compact fluorescent bulb, were given to all attendees.

Renewable Energy forum held at MLGW

Promoting the prosperity of our city, in an environmentally-responsible manner, is central to MLGW's values as an organization.

In that vein, the Division hosted the Tennessee Renewable Energy and Economic Development Council (TREEDC) Renewable Energy Forum targeted to businesses and clean energy stakeholders. Nearly 100 people attended the outreach event. TREEDC is a statewide grassroots coalition of 65 city and county mayors promoting the economic development and environmental benefits of renewable energy for all communities in Tennessee.

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, 2011, 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). Because MLGW receives federal funding above certain thresholds, MLGW is also subject to the federally mandated Single Audit, and findings for internal controls and compliance are herein presented.

The full responsibility for the accuracy and presentation of the information provided rests with 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 Mayer Hoffman McCann P.C. and Jones & Tuggle CPAs. The goal of the independent audit was to provide reasonable assurance that the financial statements of MLGW for the fiscal year ended December 31, 2011 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 fiscal year ended December 31, 2011, are fairly presented in conformity with generally accepted accounting principles. The auditor's report is presented as the first component of the financial section of the report.

Generally accepted accounting principles require that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of a Management Discussion and Analysis (MD&A). This letter of transmittal is designed to complement the 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 Memphis and Shelby County. Water service is provided by MLGW in Memphis and, together with other municipal systems, in Shelby County.

Each division operates as a separate entity for accounting and financial reporting purposes in accordance with the Private Act. For economic reasons, activities common to all three divisions are administered jointly and costs are prorated 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 Memphis City Council before incurring certain obligations, including purchasing real estate and exercising the right of eminent domain; the annual budget is also subject to approval by the Memphis City Council.

MLGW is managed by a Board, which consists of five members nominated by the Mayor and approved by the Memphis City Council. Under the Private Act, the Board is responsible for doing all things necessary to supply MLGW'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 operations 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 20th largest city with a population of 646,889. The MLGW service area comprises all of Shelby County, which in 2011 reported a population of 927,644. The eight-county Memphis Metro area provides a diverse range of employers, which contributes to 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, have 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 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 FedEx 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 – Although sluggish, the economy continued modest growth in 2011. Signs of economic life included a drop in unemployment down to 8.5 percent from 9.4 percent in 2010.

The Bureau of Economic Analysis reported an overall gain of 1.7 percent in GDP for the year. The modest gain was mainly attributed to inventory investment and consumer spending for durable goods. Additional good news for consumers included lower energy and food prices for the period.

While national indices inched upward, Memphis' economy continued to lag in 2011. To illustrate, Tennessee lost about 220,000 jobs at the height of the economic downturn; Memphis lost 60,000. With the economy at large moving into recovery mode, Memphis has regained close to 17 percent of its lost jobs in comparison to a more robust 25 percent pace for the state.

One bright spot has been the attraction of solid employers to the area. Electrolux, a global leader in home appliances, opted in 2011 to build a 700,000 square foot manufacturing center, representing an investment of more than $190 million. When fully operational, the plant is expected to employ about 1,200. Japanese powerhouse Mitsubishi Electric, also selected Memphis as a site for its new heavy electric equipment headquarters. Mitsubishi's 350,000 square foot facility is slated to open in 2013 and create 275 new jobs.

Though the housing market remains weak, the lower cost of living (of which housing is a major component) is 14 percent lower than the national average, making Memphis a relatively affordable city for its size.

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 five-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 five-year capital plans are updated periodically during the year in order to reflect the most current possible cash flow projections.

Among the three divisions, MLGW averages around $100 million in capital expenditures throughout the year. Major electric projects planned within the next five years include the installation of two substations near Collierville, a new substation in South Memphis to serve the increased industrial load, the rebuilding of a substation and a mainframe system replacement. Gas division plans include continued investment in our cast iron replacement system project, purchase of meters for replacement, liquefaction expansion at the Capleville LNG (liquid natural gas site), construction of additional CNG (compressed natural gas stations) and adding more CNG vehicles to the MLGW fleet. The Water division capital plan includes the construction of a new water lab, purchase of meters and improvements to the Allen and Lichterman water pumping stations within the next five years. MLGW also has a formal five-year Strategic Plan and engages in joint endeavors with the city of Memphis, the Tennessee Valley Authority 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, and we express our appreciation to all who assisted and contributed to the preparation of this report. Special thanks must also be given to Mayer Hoffman McCann P.C. and Jones & Tuggle CPAs for their efficient and timely completion of this year's audit.*

Respectfully submitted,

Jerry R. Collins Jr.
President and CEO

Dana Jeanes
Vice President, CFO and Secretary-Treasurer

MLGW

Financial Statements

and Supplementary Information

Memphis Light, Gas and Water Division

Years ended December 31, 2011 and 2010
with report of Independent Auditors

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Independent Auditor's Report

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

We have audited the accompanying 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, 2011, as listed in the table of contents. These financial statements are the responsibility of the Divisions' management. Our responsibility is to express opinions on these financial statements based on our audits. The financial statements of the Divisions as of December 31, 2010 were audited by Thompson Dunavant PLC, whose members became shareholders of Mayer Hoffman McCann P.C. as of August 1, 2011, and whose report dated May 19, 2011 expressed an unqualified opinion on those statements.

We conducted our audits in accordance with U.S. generally accepted auditing standards 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 audits 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 audits provide a reasonable basis for our opinions.

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, 2011, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

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, 2011, and the changes in financial position and cash flows thereof for the year then ended, in conformity with U.S. generally accepted accounting principles.

In accordance with *Governmental Auditing Standards*, we have also issued our report dated May 17, 2012, on our consideration of the Divisions' internal control over financial reporting and on our tests of their 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 assessing the results of our audits.

U.S. generally accepted accounting principles require that management's discussion and analysis; schedule of funding progress for OPEB; schedule of employer contributions - OPEB; and schedule of funding progress for pension plan, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with U.S. generally accepted auditing standards, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were conducted for the purpose of forming opinions on the basic financial statements of each Division. 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; and schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the financial statements themselves, and other additional procedures in accordance with U.S. generally accepted auditing standards. In our opinion, the information is 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 do not express an opinion or provide any assurance on them.

Mayer Hoffman McCann P.C.

Memphis, Tennessee
May 17, 2012

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.

The Balance Sheets report the assets (resources) and liabilities (obligations), with the difference being the net assets. Over time, increases or decreases in net assets may serve as an indicator of whether the financial position is improving or declining. The Statements of Revenues, Expenses and Changes in Net Assets show how net assets changed during the year based on revenues and expenses. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. The Statements of Cash Flows report changes in cash and cash equivalents summarized by net changes from operating, capital and related financing and investing activities. The Notes provide additional detailed information to support the financial statements. The statements present the current year and preceding year for comparison.

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

In December 2011, Fitch Ratings downgraded the Electric Division's 2003A, 2008 and 2010 Series Bonds from AAA to AA+. The action was an attempt to align ratings for systems with similar financial metrics, which are in the AA+ category. The Water Division continues to hold the highest possible bond ratings, which are Aaa from Moody's and AAA from Standard & Poor's. 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 favorable rates compared to companies with lower ratings.

The following tables show MLGW bond ratings and debt administration for the Electric and Water Divisions as of December 31, 2011:

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

MLGW Bond Ratings	S&P	Moody's	Fitch
Electric			
2003A	AA+	Aa2	AA+
2008	AA+	Aa2	AA+
2010	AA+	Aa2	AA+
Water	AAA	Aaa	

Debt Administration	Outstanding Balance	Coverage
Electric	$757,885	1.81
Water	$ 1,625	8.69

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 1
Electric Division Condensed Balance Sheets
December 31
(In Thousands)

	2011	2010	FY11 - FY10 Percentage Change	2009	FY10 - FY09 Percentage Change
Current assets (excluding restricted funds)	$ 486,796	$ 478,012	1.8%	$ 444,587	7.5%
Restricted assets	54,911	53,878	1.9%	53,670	0.4%
Other assets	5,781	7,566	-23.6%	8,945	-15.4%
Prepaid power costs - long-term	680,894	785,243	-13.3%	886,968	-11.5%
Utility plant	948,159	929,401	2.0%	908,976	2.2%
Total assets	2,176,541	2,254,100	-3.4%	2,303,146	-2.1%
Current liabilities payable from current assets	294,165	288,514	2.0%	271,898	6.1%
Current liabilities payable from restricted assets	28,703	28,301	1.4%	28,732	-1.5%
Long-term debt	701,531	807,287	-13.1%	909,690	-11.3%
Non-current liabilities	35,212	36,294	-3.0%	38,395	-5.5%
Total liabilities	1,059,611	1,160,396	-8.7%	1,248,715	-7.1%
Net assets:					
Invested in utility plant, net of related debt	948,159	929,401	2.0%	903,133	2.9%
Restricted	16,206	15,748	2.9%	15,295	3.0%
Unrestricted	152,565	148,555	2.7%	136,003	9.2%
Total net assets	$1,116,930	$1,093,704	2.1%	$1,054,431	3.7%

Assets

As of December 31, 2011, total assets were $2.18 billion, a decrease of $77.6 million, or -3.4%, compared to December 31, 2010. This decrease is due, in part, to a decrease in prepaid power cost of $100.5 million due to amortization (see Note 10). This decrease is partially offset by an $18.8 million increase in utility plant as a result of additions to electric plant in service and an increase in current assets of $8.8 million. These increases are primarily the results of increases in cash and cash equivalents ($5.4 million), investments ($12.2 million), and unbilled revenues ($5.2 million), partially offset by decreases in accounts receivable (-$16.6 million) and other current assets ($-1.5 million).

Total assets were $2.25 billion for fiscal year 2010, a decrease of $49.0 million, or -2.1%, compared to December 31, 2009. This decrease was due, in part, to a decrease in long-term prepaid power cost by $101.7 million due to amortization (see Note 10) and a decrease in other assets of $1.4 million due primarily to scheduled amortization of debt expenses. These decreases were partially offset by an increase in current assets of $33.0 million, caused by a $30.0 million increase in electric accounts receivable from customers. In addition, the decreases were partially offset by a $20.4 million increase in utility plant as a result of additions to electric plant in service.

Capital Assets and Construction Activities

The Electric Division's utility plant assets, net of accumulated depreciation were $948.2 million as of December 31, 2011, an increase of 2.0% over fiscal year 2010. During 2011, the Electric Division expended $60.9 million on capital equipment purchases and construction activities, a decrease of $0.4 million, or 1.2%, compared to fiscal year 2010. Major Electric Division construction activities included substation and transmission projects ($16.0 million), extensions to serve new customers ($6.0 million) and the purchase of transformers ($5.8 million). Other significant Electric Division capital expenditures consisted of street lighting and leased outdoor lighting ($4.7 million), replacement of feeder and defective cable ($3.3 million), the purchase of meters and metering equipment ($2.8 million) and Smart Grid, net of reimbursements ($2.4 million).

The Electric Division had approximately $929.4 million in utility plant assets, net of accumulated depreciation, as of December 31, 2010, an increase of 2.2% over fiscal year 2009. During 2010, the Electric Division expended $61.2 million on capital equipment purchases and construction activities, an increase of $1.7 million, or 2.8%, compared to fiscal year 2009. Major Electric Division construction activities included substation and transmission projects ($16.3 million), purchase of transformers ($6.8 million) and extensions to serve new customers ($6.6 million). Other significant Electric Division capital expenditures included street lighting and leased outdoor lighting ($4.6 million), new circuits out of substations ($2.8 million), purchase of transportation and power operated equipment ($2.7 million) and meters and metering equipment ($2.2 million).

Liabilities

As of December 31, 2011, total liabilities were $1.06 billion, a decrease of $100.8 million, or -8.7%, compared to $1.16 billion as of December 31, 2010. This decrease is due to a $105.8 million decrease (-13.1%) in long-term debt resulting from principal payments made in 2011, and premium amortization (see Note 8). This decrease was partially offset by a $5.7 million increase (2.0%) in current liabilities payable from current assets attributable primarily to a $1.6 million increase in other accounts payable, accrued expenses and deferrals. Non-current liabilities decreased by $1.1 million due to other deferred credit for long-term pollution remediation.

Total liabilities were $1.16 billion as of December 31, 2010, a decrease of $88.3 million, or -7.1%, compared to $1.25 billion as of December 31, 2009. This decrease was primarily the result of a $102.4 million, or -11.3%, decrease in long-term debt due to principal payments and refunding of the callable portion of the Series 2003A Revenue Bonds (see Note 8). This decrease was partially offset by a $16.6 million, or 6.1%, increase in current liabilities payable from current assets attributable primarily to a $15.4 million increase in collateral subject to return to borrowers.

Net Assets

As of December 31, 2011, the Electric Division's total net assets (total assets less total liabilities) were $1.12 billion, an increase of $23.2 million, or 2.1%, compared to December 31, 2010. Eighty-five percent of the net assets were related to utility plant, net of related debt, which accounts for $18.8 million of the increase and unrestricted net assets (used to finance day-to-day operations) contributed $4.0 million to the overall increase in total net assets. For fiscal year 2010, total net assets were $1.09 billion, an increase of $39.3 million, or 3.7%, increase over fiscal year 2009. Utility plant, net of related debt, accounts for $26.3 million of the increase and unrestricted net assets contributed $12.6 million to the overall total net assets.

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
Years Ended December 31, 2011, 2010 and 2009
(In Thousands)

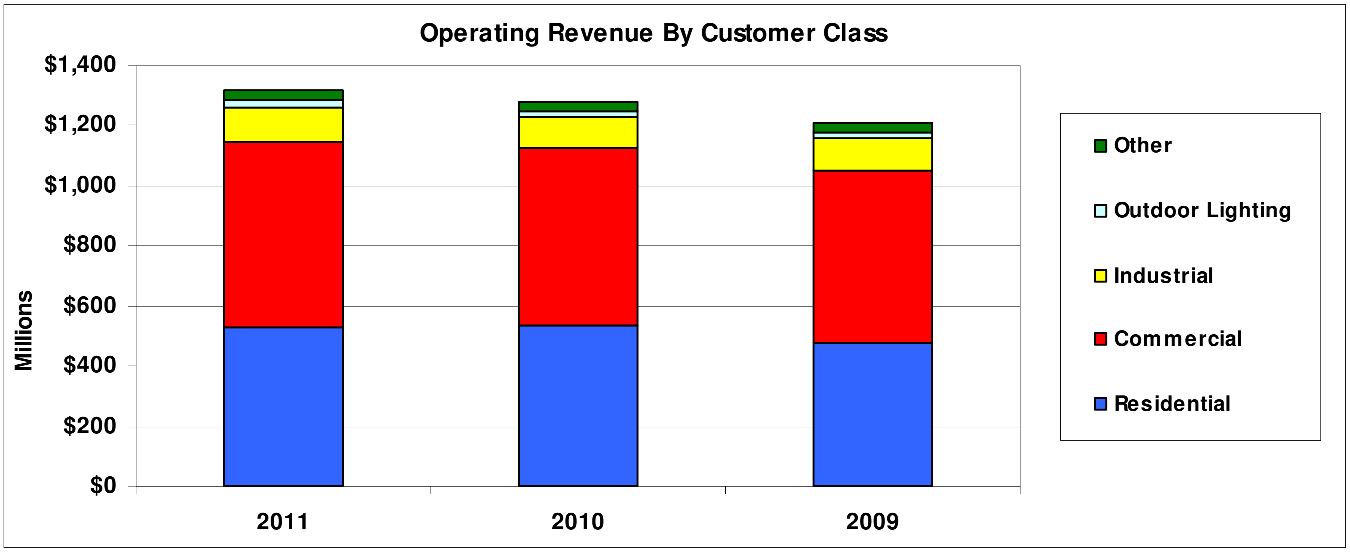
	2011	2010	FY11 - FY10 Percentage Change	2009	FY10 - FY09 Percentage Change
Revenues:					
Operating revenues	$ 1,319,030	$ 1,281,485	2.9%	$ 1,208,856	6.0%
Non-operating revenues	66,403	66,861	-0.7%	76,007	-12.0%
Total revenues	1,385,433	1,348,346	2.8%	1,284,863	4.9%
Expenses:					
Depreciation expense	43,833	42,100	4.1%	41,043	2.6%
Purchased power	1,073,538	1,032,960	3.9%	969,309	6.6%
Other operating expense	173,992	160,657	8.3%	165,512	-2.9%
Non-operating expense	31,405	34,948	-10.1%	41,536	-15.9%
Total expenses	1,322,768	1,270,665	4.1%	1,217,400	4.4%
Income (loss) before contributions in aid of construction and transfers	62,665	77,681	-19.3%	67,463	15.1%
Contributions in aid of construction	10,817	7,827	38.2%	10,532	-25.7%
Reduction of plant costs recovered through contributions in aid of construction	(10,817)	(7,827)	-38.2%	(10,532)	25.7%
Transfers to City	(39,439)	(38,408)	2.7%	(37,999)	1.1%
Change in net assets	23,226	39,273	-40.9%	29,464	33.3%
Beginning net assets	1,093,704	1,054,431	3.7%	1,024,967	2.9%
Ending net assets	$ 1,116,930	$ 1,093,704	2.1%	$ 1,054,431	3.7%

As of December 31, 2011, the change in net assets was $23.2 million representing a $16.0 million, or -40.9%, decrease, as compared to December 31, 2010. This decrease is mainly due to an increase in purchased power costs ($40.6 million) and operation and maintenance expenses ($13.2 million) partially offset by a $37.5 million increase in operating revenues. The change in net assets for fiscal year 2010 was $39.3 million representing a $9.8 million (33.3%) increase over fiscal year 2009. This increase was due mainly to an increase in operating margin (operating revenues less purchased power cost) of $9.0 million created by increased sales.

Total revenues were $1.39 billion for fiscal year 2011, an increase of $37.1 million (2.8 %) from fiscal year 2010. Operating revenues were $1.32 billion in 2011, increasing by $37.5 million over 2010. Wholesale rate adjustments increased sales revenues by $33.3 million, despite a 3.1% decrease in 2011 electricity sales. There was a corresponding increase in purchased power costs of $40.6 million. Non-operating revenues decreased by -0.7% in 2011 as a result of a $3.2 million decrease in other income prepay credit, related to the Electric Prepay Bonds, which was offset by a $2.2 million increase in miscellaneous non-operating income.

For fiscal year 2010, total revenues were $1.35 billion, an increase of $63.5 million (4.9%) from fiscal year 2009. This increase is a result of a 6.0% increase in electricity sales, which increased 2010 operating revenue by $72.6 million, partially offset by a decrease in non-operating revenue of $9.1 million. The decrease in non-operating revenue was mainly due to a $6.2 million decrease in other income prepay credit, related to the Electric Prepay Bonds.

Figure 2: Electric Division's Operating Revenue



For fiscal year 2011, total expenses were $1.32 billion, an increase of $52.1 million, or 4.1%, compared to fiscal year 2010. This increase resulted from a $40.6 million (3.9%) increase in purchased power costs and a $13.3 million (8.3%) increase in other operating expenses. Non-operating expenses decreased by $3.5 million, or -10.1%, which is the result of savings realized on interest expenses due to the advanced refunding of the Series 2003A Bonds. Other operating expenses increased $3.8 million due to four storms in the Memphis area. Depreciation expense also increased $1.7 million (4.1%).

As of December 31, 2010, total expenses were $1.27 billion, an increase of $53.3 million, or 4.4%, compared to fiscal year 2009. This increase resulted from a $63.6 million (6.6%) increase in purchased power costs, which was offset, in part, by a decrease in other operating expenses of $4.8 million. A decrease in non-operating expenses of $6.6 million helped to further offset the increase in purchased power, due in part, to refunding the callable portion of the Series 2003A Bonds.

Contributions in aid of construction ("CIAC") were $10.8 million for fiscal year 2011, an increase of $3.0 million (38.2%) from fiscal year 2010. This increase was mainly the result of a $3.0 million increase in reimbursements from the Federal Emergency Management Agency ("FEMA") for natural disasters and an increase of $1.5 million for economic development. Federal grants increased by $0.6 million. These increases were partially offset by a reduction in construction activity of $2.1 million. For fiscal year 2010, CIAC was $7.8 million, a decrease of $2.7 million (-25.7%) from fiscal year 2009. The decrease was due to a $3.0 million reduction in reimbursements from FEMA for natural disasters and a reduction of canceled contracts of $1.9 million. These decreases were partially offset by an increase of $1.3 million from the transfer of the Geographical Information System ("GIS") project from the Water Division, and increased construction activity by developers and other governmental agencies of $0.9 million.

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. For the year ended December 31, 2011, transfers to the City were $39.4 million. This represents a $1.0 million increase compared to fiscal year 2010. Of this, $0.5 million is attributed to an increase in net plant. The remaining $0.5 million is due to an increased three-year average net operating revenues. For the year ended December 31, 2010, transfers to the City were $38.4 million. This represents a $0.4 million increase from 2009. Of this, $0.5 million is attributed to an increase in net plant offset by a reduction of $0.1 million due to a lower three-year average net operating revenues.

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 3
Gas Division Condensed Balance Sheets
December 31
(In Thousands)

	2011	2010	FY11 - FY10 Percentage Change	2009	FY10 - FY09 Percentage Change
Current assets (excluding restricted funds)	$ 236,029	$ 264,336	-10.7%	$ 238,088	11.0%
Restricted assets	13,321	14,801	-10.0%	21,298	-30.5%
Other assets	5,280	6,530	-19.1%	7,798	-16.3%
Utility plant	306,255	299,687	2.2%	295,496	1.4%
Total assets	560,885	585,354	-4.2%	562,680	4.0%
Current liabilities payable from current assets	87,449	119,615	-26.9%	116,803	2.4%
Current liabilities payable from restricted assets	5,162	5,989	-13.8%	7,287	-17.8%
Non-current liabilities	8,066	8,567	-5.8%	8,322	2.9%
Total liabilites	100,677	134,171	-25.0%	132,412	1.3%
Net assets					
Invested in utility plant, net of related debt	306,255	299,687	2.2%	295,496	1.4%
Restricted	5,623	5,950	-5.5%	9,957	-40.2%
Unrestricted	148,330	145,546	1.9%	124,815	16.6%
Total net assets	$ 460,208	$ 451,183	2.0%	$ 430,268	4.9%

Assets

Total assets were $560.9 million as of December 31, 2011, a decrease of $24.5 million from December 31, 2010. Current assets decreased by $28.3 million for fiscal year 2011 due to decreases in cash and cash equivalents ($9.1 million), accounts receivable, less allowance for doubtful accounts ($4.4 million) and unbilled revenue ($15.9 million). This decrease was partially offset by an increase in other current assets ($0.8 million). Restricted assets decreased by $1.5 million for fiscal year 2011 due to decreases in insurance reserves – injuries and damages ($0.9 million) and customer deposits ($0.6 million). Other assets decreased by $1.3 million primarily as a result of the scheduled amortization activity associated with the Valero pipeline lease (see Note 3).

As of December 31, 2010, total assets were $585.4 million, an increase of $39.3 million, or 7.2%, compared to December 31, 2009. The increase in total assets was primarily due to an increase in current assets. Investments increased by $17.1 million, collateral held in trust for securities on loan increased by $9.4 million, unbilled revenue increased by $15.0 million and accounts receivable increased by $6.8 million. Partially offsetting these increases were decreases in restricted assets ($6.5 million) and other assets ($1.3 million). Restricted assets decreased due to reductions in broker-margin requirement by $3.6 million, construction by $1.1 million and customer deposits by

$1.9 million partially offset by an increase in insurance reserves-injuries and damages of $0.2 million. Other assets decreased in accordance with the amortization of the Valero pipeline lease (see Note 3).

Capital Assets and Construction Activities

The Gas Division's utility plant assets, net of accumulated depreciation, were $306.3 million as of December 31, 2011, an increase of $6.6 million (2.2%) over December 31, 2010. During 2011, the Gas Division expended $20.1 million on capital equipment purchases and construction activities, an increase of $0.9 million, or 4.7%, compared to fiscal year 2010. Major Gas Division construction activities included retrofit cast iron system and steel taps ($3.4 million), pipeline integrity ($1.4 million), extensions to serve customers ($0.9 million) and relocation of facilities to accommodate road improvements ($0.6 million). Additionally, a substantial portion of the Gas Division's expenditures was attributable to meters and metering equipment ($6.0 million), purchase of transportation and power operated equipment ($2.7 million) and buildings and structures ($1.4 million).

The Gas Division had approximately $299.7 million in utility plant assets, net of accumulated depreciation, as of December 31, 2010, an increase of $4.2 million, or 1.4%, from December 31, 2009. During 2010, the Gas Division expended $19.2 million on capital equipment purchases and construction activities, resulting in an increase of $2.7 million (16.4%) in comparison to fiscal year 2009. The Gas Division's major construction expenditures included retrofit cast iron system and steel taps ($4.3 million), pipeline integrity management ($2.3 million) and extensions to serve new customers ($0.7 million). A substantial portion of the Gas Division's expenditures was also attributable to meters and metering equipment ($5.7 million), transportation and power operated equipment ($2.0 million) and building and structures upgrades ($1.1 million).

Liabilities

As of December 31, 2011, total liabilities were $100.7 million as compared to $134.2 million as of December 31, 2010, a $33.5 million decrease (-25.0%). Current liabilities payable from current assets decreased by $32.2 million, or -26.9%, as a result of decreases in accounts payable for purchased gas (-$15.6 million) and other deferred credits related to purchased gas adjustments (-$18.2 million). This decrease was partially offset by a $1.3 million increase in collateral subject to return to borrowers. The $0.8 million decrease in current liabilities payable from restricted assets is due to decreases in insurance reserves – injuries and damages (-$0.9 million).

For fiscal year 2010, total liabilities were $134.2 million, an increase of $18.4 million (15.9%) from $115.8 million as of December 31, 2009. Current liabilities payable from current assets increased by $19.5 million, or 19.4%, primarily, due to an increase of $26.2 million in other deferred credits related to purchased gas adjustments and $9.4 million for collateral subject to return to borrowers. Partially offsetting this increase is the payment of $15.0 million on notes payable associated with the gas purchases for storage and a $3.1 million decrease in accounts payable for purchased gas. Current liabilities payable from restricted assets decreased by $1.3 million, which was attributable to a $0.7 million decrease in customer deposits.

Net Assets

As of December 31, 2011, net assets increased by $9.0 million, or 2.0% over fiscal year 2010. This increase is due to increases in utility plant, net of related debt ($6.6 million) and unrestricted net assets ($2.8 million) partially offset by a decrease in restricted net assets of $0.3 million. Utility plant, net of related debt, represents 66.5% of total net assets. Total net assets for fiscal year 2010 increased by $20.9 million, or 4.9%, over fiscal year 2009. The largest increase of $20.7 million was in unrestricted assets. Utility plant, net of related debt, represents 66.4% of total net assets.

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 4
Gas Division
Condensed Statements of Revenues, Expenses and Changes in Net Assets
Years Ended December 31, 2011, 2010 and 2009
(In Thousands)

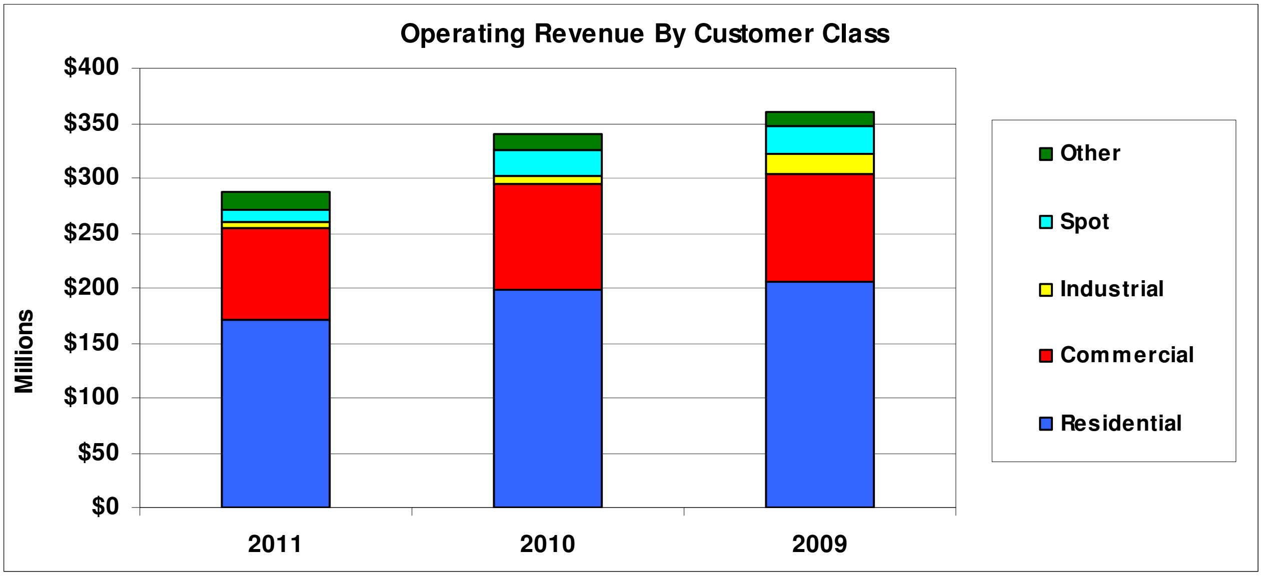
	2011	2010	FY11 - FY10 Percentage Change	2009	FY10 - FY09 Percentage Change
Revenues:					
Sales, service and other operating revenues	$ 281,124	$ 334,548	-16.0%	$ 356,024	-6.0%
Transported gas revenue	5,710	4,887	16.8%	3,657	33.6%
Non-operating revenues	1,575	1,915	-17.8%	1,590	20.4%
Total revenues	288,409	341,350	-15.5%	361,271	-5.5%
Expenses:					
Depreciation expense	12,709	12,266	3.6%	12,458	-1.5%
Purchased gas	168,189	213,538	-21.2%	240,518	-11.2%
Other operating expense	82,623	78,943	4.7%	73,695	7.1%
Non-operating expense	197	48	310.4%	463	-89.6%
Total expenses	263,718	304,795	-13.5%	327,134	-6.8%
Income (loss) before contributions in aid of construction and transfers	24,691	36,555	-32.5%	34,137	7.1%
Contributions in aid of construction	406	16	2437.5%	796	-98.0%
Reduction of plant costs recovered through contributions in aid of construction	(406)	(16)	-2437.5%	(796)	98.0%
Transfers to City	(15,666)	(15,640)	0.2%	(14,699)	-6.4%
Change in net assets	9,025	20,915	-56.8%	19,438	7.6%
Beginning net assets	451,183	430,268	4.9%	410,830	4.7%
Ending net assets	$ 460,208	$ 451,183	2.0%	$ 430,268	4.9%

As of December 31, 2011, the change in net assets was $9.0 million. This represents an $11.9 million, or -56.8%, decrease as compared to $20.9 million as of December 31, 2010. This decrease is attributable to a decrease in operating margin. The change in net assets was $20.9 million as of December 31, 2010. This represents a $1.5 million, or 7.6%, increase as compared to $19.4 million as of December 31, 2009. This increase is mainly the result of higher operating margin of $6.7 million generated from increased sales, offset, in part, by an increase in operations and maintenance expenses.

Total revenues were $288.4 million for 2011, a decrease of 15.5% from 2010. There was a 16.0% decrease in sales, service and other operating revenues in 2011, which can be attributed to lower wholesale gas prices and a 12.5% decrease in sales. A corresponding 21.2% decrease in purchased gas cost occurred. Transported gas revenue increased by 16.8% in 2011 resulting from a 5.4% increase in volumes transported. The 17.8% decrease in 2011 non-operating revenues is attributed to a decrease in other income.

Total revenues were $341.4 million for 2010, a decrease of 5.5% from 2009. There was a 6.0% decrease in sales, service and other operating revenues in 2010, which can be attributed to lower wholesale gas prices. A corresponding 11.2% decrease in purchased gas cost occurred. Transported gas revenue increased by 33.6% in 2010 resulting from a 10.9% increase in volumes transported.

Figure 3: Gas Division's Operating Revenue



For fiscal year 2011, total expenses were $263.7 million, a decrease of $41.1 million, or -13.5%, from fiscal year 2010. This decrease is mainly due to a $45.3 million decrease in purchased gas resulting from a significant decrease in the average cost of natural gas offset, in part, by an increase of $4.2 million in maintenance expenses. Non-operating expenses increased by $0.1 million in 2011 as a result of an increase in interest expense.

For fiscal year 2010, total expenses were $304.8 million, a decrease of $22.3 million (-6.8%) from fiscal year 2009. This decrease is due mainly to a $27.0 million decrease in purchased gas as the result of a significant decrease in the average cost of natural gas offset, in part, by an increase in other operating expense as a result of an increase in medical insurance cost and an increase in contributions to the pension fund. Non-operating expenses decreased by 89.6% in 2010 as a result of a decrease in interest expense.

For fiscal year 2011, CIAC increased by $0.4 million from fiscal year 2010 as a result of increased construction activity by developers and other agencies. For fiscal year 2010, CIAC decreased by $0.8 million from fiscal year 2009. Of this amount, $0.5 million was a reallocation from CIAC to operating and maintenance expense. A decrease of $0.3 million was the result of fewer construction projects from developers and other agencies.

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 power costs (three-year average). Transfers to the City represent the Gas Division's in lieu of tax payment. For fiscal year 2011, transfers to the City were $15.7 million. This represents a $0.03 million increase above prior year costs due to an increase in the three-year average revenues.

The Gas Division's transfers to the City (in lieu of tax payments) were $15.6 million in 2010. This represents a $0.9 million increase compared to fiscal year 2009. This increase is due to a $0.4 million increase in tax payments as a result of the three-year average revenues increase and $0.5 million is attributed to a reclassification of assets between tax districts.

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 5
Water Division Condensed Balance Sheets
December 31
(In Thousands)

	2011	2010	FY11 - FY10 Percentage Change	2009	FY10 - FY09 Percentage Change
Current assets (excluding restricted assets)	$ 40,043	$ 43,066	-7.0%	$ 33,108	30.1%
Restricted assets	17,691	13,669	29.4%	22,658	-39.7%
Other assets	1,682	1,849	-9.0%	2,653	-30.3%
Utility plant	255,211	254,329	0.3%	253,741	0.2%
Total assets	314,627	312,913	0.5%	312,160	0.2%
Current liabilities payable from current assets	18,731	19,042	-1.6%	14,092	35.1%
Current liabilities payable from restricted assets	6,390	3,412	87.3%	5,264	-35.2%
Long-term debt	-	1,612	-100.0%	3,127	-48.4%
Non-current liabilities	7,560	7,887	-4.1%	7,996	-1.4%
Total liabilites	32,681	31,953	2.3%	30,479	4.8%
Net assets					
Invested in utility plant, net of related debt	253,585	252,716	0.3%	250,613	0.8%
Restricted	10,663	9,624	10.8%	16,776	-42.6%
Unrestricted	17,698	18,620	-5.0%	14,292	30.3%
Total net assets	$ 281,946	$ 280,960	0.4%	$ 281,681	-0.3%

Assets

As of December 31, 2011, total assets were $314.6 million, an increase of $1.7 million as compared to December 31, 2010. This increase is due, in part, to an increase in restricted assets of $4.0 million, which was primarily the result of increases in construction ($2.2 million) and bond reserves and debt service ($1.7 million). These increases were partially offset by a decrease in cash and cash equivalents ($2.8 million).

Total assets were $312.9 million as of December 31, 2010, an increase of $0.8 million over December 31, 2009. Current assets increased by $10.0 million for fiscal year 2010 due to increases in investments and accounts receivable for sewer charges. Current assets were further increased due to an increase of collateral held in trust for securities on loan. These increases were partially offset by a $9.0 million decrease in restricted assets attributable to a decline in the master bond reserve fund.

Capital Assets and Construction Activities

The Water Division's utility plant assets, net of accumulated depreciation, were $255.2 million as of December 31, 2011, an increase of 0.3% as compared to December 31, 2010. During 2011, the Water Division expended $12.0 million on capital equipment purchases and construction activities, an increase of $0.2 million, or 1.7%, compared to fiscal year 2010. Major Water Division construction activities include upgrades to Lichterman Pumping Station ($1.8 million), extensions to serve new customers ($1.6 million) and the relocation of facilities to accommodate road improvements ($1.0 million). The Water Division's major equipment purchases were the purchase of data processing equipment ($1.4 million) and the purchase of transportation and power operated equipment ($0.6 million).

The Water Division had $254.3 million in utility plant assets, net of accumulated depreciation as of December 31, 2010, an increase of 0.2%. During 2010, the Water Division expended $11.8 million on capital equipment purchases and construction activities, which was a decrease of $1.9 million (-13.9%) in comparison to 2009. The Water Division's major construction expenditures included extensions to serve new customers ($2.0 million), upgrades to Shaw Pumping Station ($1.3 million), relocation of facilities to accommodate road improvements ($0.9 million), purchase of distribution right-of-way ($0.5 million), hydrant installation project for Southwind Annexation ($0.5 million) and 12" main installation project on Pleasant Ridge ($0.3 million). The Water Division's major equipment purchases included meters ($1.0 million) and tools and equipment ($0.8 million).

Liabilities

Total liabilities were $32.7 million as of December 31, 2011, an increase of $0.73 million, or 2.3 %, as compared to $32.0 million as of December 31, 2010. This increase is primarily the result of a $1.3 million increase in current liabilities payable from restricted assets due to an increase in construction. This increase was partially offset by a $0.2 million decrease in insurance reserves for injuries and damages.

As of December 31, 2010, total liabilities were $32.0 million, representing an increase of $1.5 million, or 4.8%, as compared to December 31, 2009. Total liabilities increased due to an increase in current liabilities payable from current assets as a result of a $3.3 million increase in accounts payable for sewer charges. Total liabilities were further increased by collateral subject to return to borrowers. These increases were offset by a $1.5 million reduction in long-term debt.

Net Assets

As of December 2011, total net assets increased by $1.0 million, or 0.4%, to $281.9 million from $281.0 million as of December 31, 2010. The increase in total net assets is mainly attributable to an increase in net assets invested in capital assets, net of related debt.

Total net assets decreased by $0.7 million, or -0.3%, to $281.0 million as of December 31, 2010, from $281.7 million as of December 31, 2009. The decrease in total net assets is reflected as a reduction in restricted net assets of $7.2 million due to a reduction in the master bond reserve offset by increases in utility plant, net of related debt ($2.1 million) and unrestricted net assets ($4.3 million).

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 6
Water Division
Condensed Statements of Revenues, Expenses and Changes in Net Assets
Years Ended December 31, 2011, 2010 and 2009
(In Thousands)

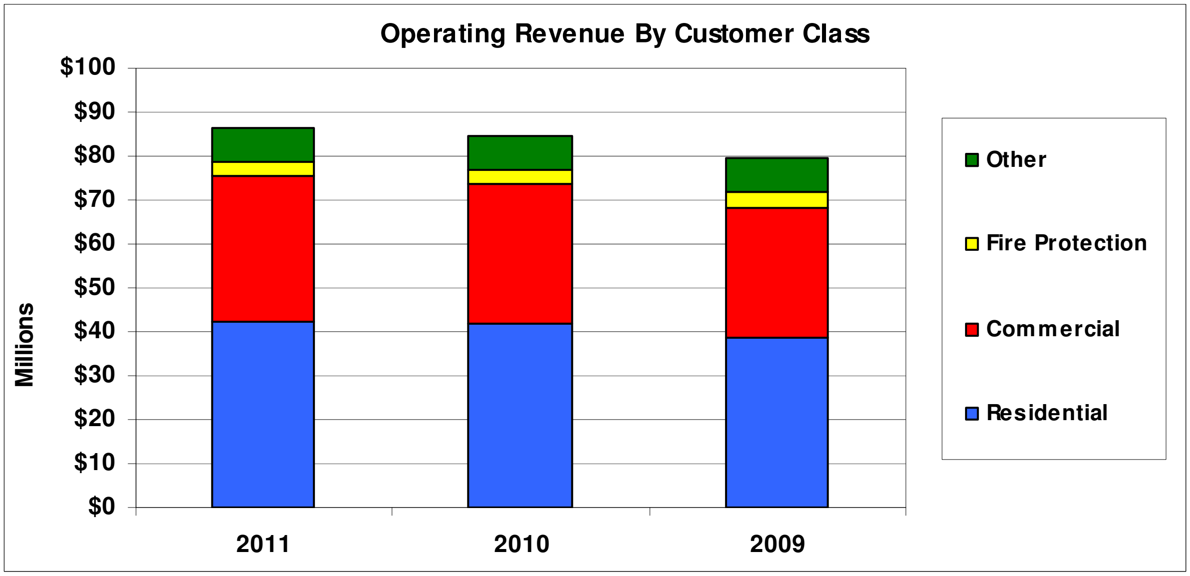
	2011	2010	FY11 - FY10 Percentage Change	2009	FY10 - FY09 Percentage Change
Revenues:					
Operating revenues	$ 86,382	$ 84,593	2.1%	$ 79,657	6.2%
Non-operating revenues	505	364	38.7%	638	-42.9%
Total Revenues	86,887	84,957	2.3%	80,295	5.8%
Expenses:					
Depreciation expense	11,274	11,079	1.8%	10,932	1.3%
Other operating expense	72,029	71,908	0.2%	66,382	8.3%
Non-operating expense	98	191	-48.7%	297	-35.7%
Total Expenses	83,401	83,178	0.3%	77,611	7.2%
Income (loss) before contributions in aid of construction and transfers	3,486	1,779	96.0%	2,684	-33.7%
Contributions in aid of construction	1,736	720	141.1%	3,152	-77.2%
Reduction of plant costs recovered through contributions in aid of construction	(1,736)	(720)	-141.1%	(3,152)	77.2%
Transfers to City	(2,500)	(2,500)	0.0%	(2,500)	0.0%
Change in net assets	986	(721)	236.8%	184	-491.8%
Beginning net assets	280,960	281,681	-0.3%	281,497	0.1%
Ending net assets	$ 281,946	$ 280,960	0.4%	$ 281,681	-0.3%

As of December 31, 2011, the change in net assets was $1.0 million, an increase of $1.7 million (236.8%) over fiscal year 2010. This increase is due primarily to a $1.8 million increase in operating revenues, partially offset by a $0.1 million increase in other operating expenses. As of December 31, 2010, the change in net assets was $-0.7 million, a decrease of $0.9 million (-491.8%) as compared to $0.2 million in fiscal year 2009. This decrease is due primarily to increased operation and maintenance costs, partially offset by an increase in operating revenue.

Total revenues were $86.9 million for fiscal year 2011, an increase of 2.3% from fiscal year 2010. Operating revenues increased by 2.1% in 2011 and is attributable to the Division's 5.0% water rate increase effective January 3, 2011 which was offset by a 6.0% decrease in water sales. Non-operating revenues increased by 38.7% in 2011, due to increases in interest income and miscellaneous non-operating income.

Total revenues were $85.0 million for fiscal year 2010, an increase of 5.8% from fiscal year 2009. Operating revenues increased by 6.2% in 2010 and is attributed to a 7.3% increase in sales and service revenue. Non-operating revenues decreased by 42.9% in 2010, which can be attributed to decreases in investment and other income.

Figure 4: Water Division's Operating Revenue



For fiscal year 2011, total expenses for the Water Division were $83.4 million, an increase of $0.22 million, or 0.3%, over fiscal year 2010. There was a $0.12 million (0.2%) increase in 2011 other operating expenses resulting from increases in operation costs, partially offset by decreases in production and maintenance costs. Non-operating expenses decreased by $0.09 million, or -48.7%, in 2011, which is attributed to lower interest expense on long-term debt; depreciation expense increased $0.2 million, or 1.8%.

As of December 31, 2010, total expenses for the Water Division were $83.2 million, an increase of $5.6 million, or 7.2%, over fiscal year 2009 resulting from an 8.3% increase in other operating expense due to increases in production and maintenance costs. Non-operating expenses decreased by 35.7% in 2010, which is attributed to lower interest expense on long-term debt.

CIAC increased to $1.7 million in 2011, representing an increase of $1.0 million as compared to 2010. These increases were partially offset by reductions of a $0.2 million for the cancellation of an economic development grant and $0.8 million for reduction in developers' and other governmental agency construction activity.

CIAC decreased to $0.7 million in 2010, representing a decrease of $2.4 million from 2009. Of this decrease, $1.3 million was due to the transfer of the GIS project to the Electric Division, $0.7 million is the result of an addition to plant for several capital projects that were previously charged to the Town of Arlington and $0.4 million was due to less reimbursable construction activity by developers and other governmental agencies.

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
DECEMBER 31, 2011 AND 2010
(Dollars in Thousands)

MLGW

	Electric Division		Gas Division		Water Division	
	2011	**2010**	**2011**	**2010**	**2011**	**2010**
Assets						
Current assets:						
Cash and cash equivalents	**$ 89,780**	$ 84,374	**$ 62,551**	$ 71,621	**$ 7,105**	$ 9,872
Investments	**75,288**	63,112	**50,797**	50,083	**5,966**	7,439
Restricted funds - current	**28,703**	28,301	**6,111**	7,318	**8,152**	4,337
Accounts receivable, less allowance for doubtful accounts	**93,494**	110,083	**49,318**	53,731	**14,740**	15,748
Unbilled revenues	**67,979**	62,806	**25,935**	41,869	**3,734**	2,445
Prepaid power cost	**104,350**	100,504	**-**	-	**-**	-
Unrecovered purchased gas cost	**-**	-	**-**	432	**-**	-
Inventories	**17,814**	18,313	**15,889**	17,170	**2,055**	1,910
Collateral held in trust for securities on loan	**37,677**	36,890	**23,474**	22,152	**5,404**	5,428
Other current assets	**414**	1,930	**8,065**	7,278	**1,039**	224
Total current assets	**515,499**	506,313	**242,140**	271,654	**48,195**	47,403
Non-current assets:						
Restricted funds:						
Futures margin deposits	**-**	-	**950**	1,329	**-**	-
Construction	**-**	-	**-**	-	**3,251**	1,100
Insurance reserves - injuries and damages	**6,399**	6,729	**1,646**	2,511	**1,377**	1,560
Insurance reserves - casualties and general	**16,206**	15,748	**4,673**	4,621	**6,894**	6,692
Medical benefits	**4,890**	4,296	**2,181**	1,916	**1,448**	1,272
Customer deposits	**16,397**	16,113	**3,871**	4,424	**1,046**	1,038
Bond reserve and debt service	**11,019**	10,992	**-**	-	**3,675**	2,007
Total restricted funds	**54,911**	53,878	**13,321**	14,801	**17,691**	13,669
Less restricted funds - current	**(28,703)**	(28,301)	**(6,111)**	(7,318)	**(8,152)**	(4,337)
Restricted funds - non-current	**26,208**	25,577	**7,210**	7,483	**9,539**	9,332
Other assets:						
Prepaid power cost - long term	**680,894**	785,243	**-**	-	**-**	-
Prepayment - In Lieu of Taxes	**1,872**	1,904	**43**	44	**-**	-
Unamortized debt expense	**3,192**	4,333	**-**	-	**-**	-
Notes receivable	**-**	-	**4,917**	5,887	**1,470**	1,452
Other prepayments	**717**	1,329	**320**	599	**212**	397
Total other assets	**686,675**	792,809	**5,280**	6,530	**1,682**	1,849
Utility plant	**1,550,338**	1,501,609	**570,333**	554,010	**451,680**	440,254
Less accumulated depreciation	**(602,179)**	(572,208)	**(264,078)**	(254,323)	**(196,469)**	(185,925)
Utility plant, net	**948,159**	929,401	**306,255**	299,687	**255,211**	254,329
Total non-current assets	**1,661,042**	1,747,787	**318,745**	313,700	**266,432**	265,510
Total assets	**$ 2,176,541**	$ 2,254,100	**$ 560,885**	$ 585,354	**$ 314,627**	$ 312,913

See accompanying notes.

BALANCE SHEETS
DECEMBER 31, 2011 AND 2010
(Dollars in Thousands)
(Continued)

	Electric Division		Gas Division		Water Division	
	2011	**2010**	**2011**	**2010**	**2011**	**2010**
Liabilities						
Current liabilities:						
Accounts payable - purchased power and gas	**$ 120,816**	$ 121,946	**$ 22,271**	$ 37,900	**$ -**	$ -
Other accounts payable, accrued expenses, and deferrals	**48,415**	46,795	**39,338**	57,580	**13,327**	13,614
Derivative financial instruments	**-**	-	**2,366**	1,983	**-**	-
Bonds Payable	**87,257**	82,883	**-**	-	**-**	-
Collateral subject to return to borrowers	**37,677**	36,890	**23,474**	22,152	**5,404**	5,428
Total current liabilities payable from current assets	**294,165**	288,514	**87,449**	119,615	**18,731**	19,042
Current liabilities payable from restricted assets:						
Construction	**-**	-	**-**	-	**1,489**	175
Customer deposits	**6,395**	6,284	**1,335**	1,562	**408**	405
Medical benefits	**4,890**	4,296	**2,181**	1,916	**1,448**	1,272
Insurance reserves - injuries and damages	**6,399**	6,729	**1,646**	2,511	**1,377**	1,560
Bonds payable - accrued interest	**3,086**	3,455	**-**	-	**43**	-
Bonds payable - principal	**7,933**	7,537	**-**	-	**1,625**	-
Total current liabilities payable from restricted assets	**28,703**	28,301	**5,162**	5,989	**6,390**	3,412
Total current liabilities	**322,868**	316,815	**92,611**	125,604	**25,121**	22,454
Non-current liabilities:						
Customer advances for construction	**8,535**	8,017	**1,094**	1,003	**-**	-
Customer deposits	**10,002**	9,829	**2,536**	2,862	**638**	633
Other	**16,675**	18,448	**4,436**	4,702	**6,922**	7,254
Bonds payable	**701,531**	807,287	**-**	-	**-**	1,612
Total non-current liabilities	**736,743**	843,581	**8,066**	8,567	**7,560**	9,499
Total liabilities	**1,059,611**	1,160,396	**100,677**	134,171	**32,681**	31,953
Net assets						
Invested in capital assets, net of related debt	**948,159**	929,401	**306,255**	299,687	**253,585**	252,717
Restricted	**16,206**	15,748	**5,623**	5,950	**10,663**	9,624
Unrestricted	**152,565**	148,555	**148,330**	145,546	**17,698**	18,619
Total net assets	**1,116,930**	1,093,704	**460,208**	451,183	**281,946**	280,960
Total liabilities and net assets	**$ 2,176,541**	$ 2,254,100	**$ 560,885**	$ 585,354	**$ 314,627**	$ 312,913

See accompanying notes.

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010 (Dollars in Thousands)

	Electric Division		Gas Division		Water Division	
	2011	**2010**	**2011**	**2010**	**2011**	**2010**
Operating revenues:						
Sales and service revenues	**$ 1,286,291**	$ 1,249,216	**$ 269,299**	$ 322,418	**$ 78,078**	$ 76,029
Transported gas revenues	**-**	-	**5,710**	4,887	**-**	-
Other revenues	**32,739**	32,269	**11,825**	12,130	**8,304**	8,564
Total operating revenues	**1,319,030**	1,281,485	**286,834**	339,435	**86,382**	84,593
Operating expenses:						
Purchased power and gas for resale	**1,073,538**	1,032,960	**168,189**	213,538	**-**	-
Production	**-**	-	**-**	-	**16,791**	17,050
Operation	**127,604**	115,243	**69,399**	70,103	**46,585**	44,821
Maintenance	**45,708**	44,830	**13,017**	8,764	**8,653**	10,037
Depreciation	**43,833**	42,100	**12,709**	12,266	**11,274**	11,079
Payments in lieu of taxes	**680**	584	**207**	76	**-**	-
	1,291,363	1,235,717	**263,521**	304,747	**83,303**	82,987
Operating income	**27,667**	45,768	**23,313**	34,688	**3,079**	1,606
Non-operating revenues (expenses):						
Contributions in aid of construction	**10,817**	7,827	**406**	16	**1,736**	720
Reduction of plant costs recovered through contributions in aid of construction	**(10,817)**	(7,827)	**(406)**	(16)	**(1,736)**	(720)
Transmission credits	**28,400**	28,066	**-**	-	**-**	-
Investment and other income	**6,599**	4,186	**1,575**	1,915	**505**	364
Prepay credit	**31,404**	34,609	**-**	-	**-**	-
Interest expense	**(31,405)**	(34,948)	**(197)**	(48)	**(98)**	(191)
Total non-operating revenues (expenses)	**34,998**	31,913	**1,378**	1,867	**407**	173
Income before transfers	**62,665**	77,681	**24,691**	36,555	**3,486**	1,779
Transfers out	**(39,439)**	(38,408)	**(15,666)**	(15,640)	**(2,500)**	(2,500)
Change in net assets	**$ 23,226**	$ 39,273	**$ 9,025**	$ 20,915	**$ 986**	$ (721)
Net assets, beginning of year	**$ 1,093,704**	$ 1,054,431	**$ 451,183**	$ 430,268	**$ 280,960**	$ 281,681
Change in net assets	**23,226**	39,273	**9,025**	20,915	**986**	(721)
Net assets, end of year	**$ 1,116,930**	$ 1,093,704	**$ 460,208**	$ 451,183	**$ 281,946**	$ 280,960

See accompanying notes.

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010
(Dollars in Thousands)

	Electric Division		Gas Division		Water Division	
	2011	**2010**	**2011**	**2010**	**2011**	**2010**
Cash flows from operating activities:						
Receipts from customers and users	**$ 1,317,033**	$ 1,267,061	**$ 286,350**	$ 339,463	**$ 79,666**	$ 79,861
Payments to suppliers	**(945,393)**	(919,070)	**(205,284)**	(234,485)	**(23,045)**	(27,662)
Payments to/on behalf of employees	**(119,696)**	(115,460)	**(59,915)**	(56,168)	**(43,626)**	(42,742)
Payments from (to) other Division funds	**(86)**	(519)	**3,132**	(1,430)	**1,465**	1,606
Payments for taxes	**(987)**	(426)	**(809)**	897	**-**	-
Net cash provided by operating activities	**250,871**	231,586	**23,474**	48,277	**14,460**	11,063
Cash flows from noncapital financing activities:						
Transfers to City of Memphis	**(39,439)**	(38,408)	**(15,666)**	(15,640)	**(2,500)**	(2,500)
Proceeds from issuance of long-term debt	**-**	471,305	**-**	-	**-**	-
Principal payments on long-term debt	**(90,420)**	(558,055)	**-**	-	**-**	-
Interest expense on bonds	**(41,199)**	(45,019)	**-**	-	**-**	-
Principal payment on notes payable	**-**	-	**-**	(15,000)	**-**	-
Interest payment on notes payable	**-**	-	**(197)**	(126)	**-**	-
Net cash used in noncapital financing activities	**(171,058)**	(170,177)	**(15,863)**	(30,766)	**(2,500)**	(2,500)
Cash flows from capital and related financing activities:						
Purchase and construction of utility plant	**(73,511)**	(70,511)	**(20,173)**	(18,988)	**(14,045)**	(12,740)
Contributions in aid of construction	**10,817**	7,827	**406**	16	**1,736**	720
Principal payments on long-term debt	**-**	(7,354)	**-**	-	**-**	(1,540)
Interest payments on debt	**-**	(350)	**-**	-	**(43)**	(166)
Net cash used in capital and related financing activities	**(62,694)**	(70,388)	**(19,767)**	(18,972)	**(12,352)**	(13,726)
Cash flows from investing activities:						
Sales and maturities of investments	**83,602**	25,661	**3,478**	21,825	**1,984**	5,883
Purchases of investments	**(96,437)**	(46,648)	**(4,013)**	(39,601)	**(1,751)**	(10,687)
Payments received on notes receivable	**-**	1,139	**1,712**	1,712	**-**	-
Issuance of notes receivable	**-**	-	**-**	-	**(18)**	772
Investment income earned on investments	**1,496**	1,509	**610**	374	**191**	180
Net cash provided by (used in) investing activities	**(11,339)**	(18,339)	**1,787**	(15,690)	**406**	(3,852)
Increase (decrease) in cash and cash equivalents	**5,780**	(27,318)	**(10,369)**	(17,151)	**14**	(9,015)
Cash and cash equivalents, beginning of year	**128,593**	155,911	**83,357**	100,508	**19,522**	28,537
Cash and cash equivalents, end of year	**$ 134,373**	$ 128,593	**$ 72,988**	$ 83,357	**$ 19,536**	$ 19,522

See accompanying notes.

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010
(Dollars in Thousands)
(Continued)

	Electric Division		Gas Division		Water Division	
	2011	**2010**	**2011**	**2010**	**2011**	**2010**
Reconciliation of operating income to net cash provided by operating activities:						
Operating income (loss)	**$ 27,667**	$ 45,768	**$ 23,313**	$ 34,688	**$ 3,079**	$ 1,606
Adjustments to reconcile operating income to net cash provided by operating activities:						
Depreciation of utility plant	**43,936**	42,259	**13,199**	14,780	**11,427**	11,433
Transmission credits	**28,400**	28,066	**-**	-	**-**	-
Prepay power credits	**31,404**	34,609	**-**	-	**-**	-
Other income	**5,103**	2,645	**100**	568	**314**	184
(Increase) decrease in assets:						
Accounts receivable	**17,200**	(29,779)	**4,412**	(6,841)	**1,008**	(4,201)
Unbilled revenues	**(5,173)**	4,756	**15,934**	7,437	**(1,289)**	(70)
Prepaid power cost	**100,504**	96,803	**-**	-	**-**	-
Prepayments - In Lieu of Taxes	**33**	(479)	**1**	370	**-**	-
Unrecovered purchased gas cost	**-**	-	**433**	1,154	**-**	-
Inventories	**500**	3,877	**1,281**	(2,644)	**(145)**	232
Other assets	**1,515**	485	**(384)**	(2,897)	**(631)**	1,475
Increase (decrease) in liabilities:						
Accounts payable - purchased power and gas	**(1,130)**	8,617	**(15,628)**	(3,073)	**-**	-
Other accounts payable and accrued expenses	**1,620**	(4,228)	**(18,242)**	3,206	**608**	489
Customer deposits	**284**	304	**(553)**	(1,911)	**8**	26
Insurance reserves	**(330)**	566	**(865)**	196	**(183)**	(290)
Medical benefit accrual	**594**	(395)	**266**	(175)	**176**	(117)
Other	**(1,256)**	(2,288)	**207**	3,419	**88**	296
Total adjustments	**223,204**	185,818	**161**	13,589	**11,381**	9,457
Net cash provided (used) by operating activities	**$ 250,871**	$ 231,586	**$ 23,474**	$ 48,277	**$ 14,460**	$ 11,063
Reconciliation of cash and cash equivalents per statements of cash flows to the balance sheets:						
Restricted funds	**$ 54,911**	$ 53,878	**$ 13,321**	$ 14,801	**$ 17,691**	$ 13,669
Less investments included in restricted funds	**(10,318)**	(9,659)	**(2,884)**	(3,065)	**(5,260)**	(4,019)
Cash and cash equivalents included in restricted funds	**44,593**	44,219	**10,437**	11,736	**12,431**	9,650
Current assets - cash and cash equivalents	**89,780**	84,374	**62,551**	71,621	**7,105**	9,872
Total cash and cash equivalents	**$ 134,373**	$ 128,593	**$ 72,988**	$ 83,357	**$ 19,536**	$ 19,522

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 U.S. generally accepted accounting principles that are applicable to a proprietary fund of a government unit. The accompanying financial statements present the separate financial positions, results of operations, and 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, or cash flows of MLGW, a division 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 or 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 or 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.

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.

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(Dollars in Thousands)

1. Summary of Significant Accounting Policies (continued)

Basis of Accounting (continued)

Under Governmental Accounting Standards Board ("GASB") Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting,* MLGW has elected to apply all Financial Accounting Standards Board ("FASB") statements and interpretations and Accounting Standards Updates issued after November 30, 1989, except for those that conflict with or contradict GASB pronouncements, to MLGW's accounting and financial reporting.

Regulatory Accounting

MLGW prepares its financial statements in accordance with the provisions of *FASB Accounting Standards Codification* ("ASC") 980, *Regulated Operations*. In general, ASC 980 recognizes that accounting for rate regulated enterprises should reflect the relationship of costs and revenues introduced by rate regulation.

Regulatory accounting allows a regulated utility to defer 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 ASC 980 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, expenses and changes in net assets. The following are the regulatory assets and liabilities included in the balance sheets:

		2011	2010
Assets			
Electric Division	Deferred asset pollution remediation	**$ 230**	$ 1,712
Gas Division	Unrecovered purchased gas cost	**-**	432
Gas Division	Deferred asset pollution remediation	**1,501**	2,504
Water Division	Deferred asset pollution remediation	**1,039**	224
Liabilities			
Gas Division	Deferred Credits – PGA	**$ 23,202**	$ 41,434

Use of Estimates

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, 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 date of

(Dollars in Thousands)

1. Summary of Significant Accounting Policies (continued)

Use of Estimates (continued)

the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Fair Value of Financial Instruments

Fair value is the price that would be received in the sale of an asset or extinguishment of a liability between market participants at the measurement date. 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, 2011 and 2010:

	2011	2010
Electric Division	**$ 863,605**	$ 935,439
Water Division	**1,625**	1,700

Investments

Investments are carried at 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, 2011 and 2010, accounts receivable and allowances for doubtful accounts were as follows:

	Electric Division		Gas Division		Water Division	
	2011	2010	2011	2010	2011	2010
Accounts Receivable	**$ 102,241**	$ 117,174	**$ 50,774**	$ 55,555	**$ 15,670**	$ 16,825
Allowance for doubtful accounts	**(8,747)**	(7,091)	**(1,457)**	(1,824)	**(930)**	(1,077)
Total A/R, net of allowance	**$ 93,494**	$ 110,083	**$ 49,318**	$ 53,731	**$ 14,740**	$ 15,748

(Dollars in Thousands)

1. Summary of Significant Accounting Policies (continued)

Accounts Receivables (continued)

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 150 days of non-payment. The bad debt expense amounts netted against operating revenues are as follows:

	2011	2010
Electric	**$ 9,729**	$ 8,939
Gas	**2,243**	2,463
Water	**1,208**	1,338

Unbilled Revenue

MLGW divides billing for its customers into twenty-one billing cycles. Revenue is reported on a calendar month basis. Unbilled revenue represents the estimate of revenue for power, gas or water delivered to customers during a month but not yet billed by month end.

Concentration of Credit Risk

MLGW's financial instruments that are potentially exposed to concentrations of credit risk primarily consist of trade receivables and derivative instruments. Trade receivables result from 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.

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 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. 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

1. Summary of Significant Accounting Policies (continued)

Prepaid Power Cost (continued)

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. See Note 8 (Long-Term Debt) and Note 10 (Energy Supplies) for further disclosure of the revenue bonds and subsequent refinancing.

Inventories

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

Utility Plant

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. Costs 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.

Depreciation is computed using the straight-line method based on estimated service lives of various classes of property at rates equivalent to annual composite rates of approximately 3.1% for the electric division, 2.4% for the gas division and 2.9% 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.

Bond Premiums, Discounts and Issuance Costs

Bond premiums and discounts, as well as issuance costs, are deferred and amortized using 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.

Restricted Funds and Related Reserves

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

1. Summary of Significant Accounting Policies (continued)

Restricted Funds and Related Reserves (continued)

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 Electric Division had a cash margin account in 2010. The clearing member requires that a minimum cash margin be maintained based on the value of the Divisions' 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 generally maintained for the purpose of paying certain repairs and capital additions and improvements. The respective bond resolutions of the Electric, Gas and Water Divisions allow 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.

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 in providing medical benefits to employees and retirees which are not insured by third party providers.

Since MLGW is self-insured for insurance and medical benefit 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.

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 as cash flow hedges to manage the risk of volatility in the market price of natural gas on anticipated purchase transactions. The market values of the open derivative positions are reported on the balance sheet as derivative financial instruments.

(Dollars in Thousands)

1. Summary of Significant Accounting Policies (continued)

Futures, Options and Swap Contracts (continued)

Gas Division:

The schedule below shows the market values and notional amounts of the open futures, swaps, and options on futures contracts as of December 31, 2011 and 2010.

Type	December 31, 2011 Market Value	December 31, 2011 Notional Amount	December 31, 2010 Market Value	December 31, 2010 Notional Amount
Futures	**($1,206)**	**$9,626**	($432)	$4,714
Swaps	**($1,160)**	**$5,488**	($1,551)	$8,250
Options	**$0**	**$0**	$0	$0
Total	**($2,366)**	**$15,114**	($1,983)	$12,964

The schedule below reflects the deferred gains (losses) at year end associated with recording open derivative positions.

Type	December 31, 2011 Deferred Gains (Losses)	December 31, 2010 Deferred Gains (Losses)
Futures	**($1,206)**	($432)
Swaps	**($1,160)**	($1,551)
Options	**$0**	$0
Total	**($2,366)**	($1,983)

Deferred costs at year end associated with gains (losses) on closed derivative positions are shown below.

Type	December 31, 2011 Deferred Gains (Losses)	December 31, 2010 Deferred Gains (Losses)
Futures	**($761)**	($585)
Swaps	**($1,400)**	($238)
Total	**($2,161)**	($823)

The deferred gains (losses) at year end for the open and closed derivative positions are reported on the balance sheet as other current assets and other liability deferrals. The gains or losses are included in deferred purchased gas costs until they are charged to gas costs through the purchased gas adjustment.

Natural gas margin account balances with MLGW's New York Mercantile Exchange clearing member as of December 31, 2011 and 2010, were $3,009 and $6,491, respectively.

1. Summary of Significant Accounting Policies (continued)

Futures, Options and Swap Contracts (continued)

Electric Division:

The Electric Division enters into swap contracts to manage the risk of volatility in the market price of unleaded and diesel fuel on anticipated purchase transactions. No trades were made during 2011 or 2010.

The fuel margin account balances with MLGW's New York Mercantile Exchange clearing member as of December 31, 2011 and 2010 were $0 and $621, respectively.

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 external constraints placed on net asset use 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 which generally occurs when power, gas, or water is delivered to the customer. 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 each month.

MLGW distinguishes between operating and non-operating revenues and expenses. 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

1. Summary of Significant Accounting Policies (continued)

Revenues and Expenses (continued)

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.

Customer Deposits

Customers that do not have adequate credit history are required to make utility deposits before services are provided. Deposits are refunded or applied toward a 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.

Cash and Cash Equivalents

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 2011 and 2010, receivables from related parties for utility construction, pole rentals and utility related services excluding utility bills were $2,302 and $4,118, respectively. 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 $2,109 and $2,272 for 2011 and 2010, respectively.

Events occurring after reporting date

Management has evaluated events and transactions that have occurred between December 31, 2011 and May 17, 2012, which is the date that the financial statements were available to be issued, for possible recognition or disclosure in the financial statements.

Reclassifications

Certain amounts in the 2010 financial statements have been reclassified to conform to the 2011 presentation.

1. Summary of Significant Accounting Policies (continued)

Recent Accounting Standards

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.* The objective of this Statement is to incorporate into the GASB's authoritative literature certain FASB and American Institute of Certified Public Accountants' ("AICPA") accounting and financial reporting guidance issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements.

GASB Statement No. 62 also supersedes Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting,* thereby eliminating the election provided in that Statement for enterprise funds and business-type activities to apply post-November 30, 1989 FASB Statements and Interpretations that do not conflict with or contradict GASB pronouncements. However, those entities can continue to apply, as other accounting literature, post-November 30, 1989 FASB pronouncements that do not conflict with or contradict GASB pronouncements, including this Statement.

The requirements of GASB Statement No. 62 are effective for financial statements for periods beginning after December 15, 2011. The provisions of this Statement generally are required to be applied retroactively for all periods presented. MLGW has not elected early implementation of this standard and has not completed the process of evaluating the impact of this statement on its financial statements.

In June 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.* This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. This Statement amends the net asset reporting requirements in Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2011. MLGW has not elected early implementation of this standard and has not completed the process of evaluating the impact of this statement on its financial statements.

In June 2011, GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions—an Amendment of GASB Statement No. 53.* This statement addresses interest rate and commodity swap agreements in which a swap counterparty, or the swap counterparty's credit support provider, commits or experiences either an act of default or a termination event as both are described in the swap agreement. When these swap agreements have been reported as hedging instruments, Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* requires a government to cease hedge accounting upon the termination of the hedging derivative instrument, resulting in the immediate recognition of the deferred outflows of resources or deferred inflows of resources as a component of investment income. The objective of this Statement is to clarify whether an effective hedging relationship continues after the replacement of a swap counterparty or a swap

1. Summary of Significant Accounting Policies (continued)

Recent Accounting Standards (continued)

counterparty's credit support provider. This Statement sets forth criteria that establish when the effective hedging relationship continues and hedge accounting should continue to be applied. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2011. MLGW has not elected early implementation of this standard and has not completed the process of evaluating the impact of this statement on its financial statements.

2. Deposits and Investments

The MLGW Statement of Investment Policy has been adopted and approved by the MLGW Board of Commissioners. This policy sets 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 futures margin deposits. The 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, 2011, MLGW deposits with financial institutions were $14,296 and gas margin deposits were $3,009. Deposits of $14,296 were maintained in collateralized accounts or covered by federal depository insurance, and were not exposed to custodial credit risk. The margin deposits of $3,009 were exposed to custodial credit risk as they were uninsured and uncollateralized.

(Dollars in Thousands)

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 to invest in the following investments as authorized by state law and as it deems proper: U.S. Treasuries; U.S. government obligations; repurchase agreements; commercial paper with specified ratings; bankers' acceptances with specified ratings; domestic and international 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; investments 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, 2011:

		Remaining Maturities (in Years)	
Investment Type	**Fair Value**	**Maturities < 1 year**	**Maturities 1 to 5 years**
U.S. Treasuries	$ 23,014	$ 7,321	$ 15,693
Federal Agency (Fixed Rate)	19,348	15,570	3,778
Municipal Obligations	1,218	-	1,218
Corporate Bonds/Notes (medium term)	11,405	3,155	8,250
Asset - Backed Securities	30,129	-	30,129
Money Market Mutual Funds	113,001	113,001	-
Commercial Paper (Rated AA or higher)	96,056	96,056	-
Securities held by Brokers-Dealers under Securities Loans for Cash Collateral:			
U.S. Treasuries	57,063	-	57,063
Federal Agency (Fixed Rate)	6,125	1,026	5,099
Corporate Bonds/Notes (medium term)	2,209	390	1,819
Total Investments	**$ 359,568**	**$ 236,519**	**$ 123,049**

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

2. Deposits and Investments (continued)

Investments (continued)

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 in the balance sheets. To limit its exposure, MLGW's investment policy requires that all securities purchased by MLGW shall be held in safekeeping by a third-party custodial bank or financial institutions. None of MLGW's investments at December 31, 2011 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. As of December 31, 2011, MLGW had purchased no investments in debt securities that were outside of the policy guidelines. MLGW uses the segmented time distribution method of disclosure, as shown above, to identify this risk.

Some investments can be highly sensitive to changes in interest rates due to their terms or characteristics. In MLGW's investment portfolio, asset-backed securities are most sensitive to changes in interest rates as their repayments can vary significantly with interest rate changes. These securities represent 8.4% of the total investment portfolio with a fair market value of $30,129 at year-end 2011.

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. MLGW debt securities that were subject to credit risk were $141,017, or 39.2% of total investments. Of this amount, $99,601 has a remaining maturity of one year or less.

(Dollars in Thousands)

2. Deposits and Investments (continued)

Credit Risk (continued)

MLGW's ratings and policy limits as of December 31, 2011 are as follows:

Investment Type	Fair Value		S&P Rating	Moody Rating
Municipal Obligations	$ 1,117		AA	Aa2
Municipal Obligations	101		AA-	Aa2
Corporate Bonds/Notes	1,015		AAA	Aaa
Corporate Bonds/Notes	1,013		AA+	Aaa
Corporate Bonds/Notes	4,269		AA+	Aa2
Corporate Bonds/Notes	509		AA	Aa1
Corporate Bonds/Notes	1,507		AA	Aa2
Corporate Bonds/Notes	507		AA-	Aa1
Corporate Bonds/Notes	1,533		AA-	Aa2
Corporate Bonds/Notes	507		AA-	Aa3
Corporate Bonds/Notes	2,005		A+	Aa2
Corporate Bonds/Notes	749		NA	Aaa
Asset-Backed Securities	15,816		AAA	Aaa
Asset-Backed Securities	4,311		AAA (sf)	NA
Asset-Backed Securities	10,002		NA	Aaa (sf)
Commercial Paper	17,699		AAA	Aaa
Commercial Paper	18,060		AA+	Aa2
Commercial Paper	1,100		AA	Aaa
Commercial Paper	28,099		AA	Aa1
Commercial Paper	15,199		AA-	Aa1
Commercial Paper	15,899		AA-	Aa3
Total credit risk debt securities	141,017			
U.S. Treasuries	501		AA +u	Aaa
U.S. Treasuries	14,693	1	AAAm	Aaa-mf
U.S. Treasuries (explicitly guaranteed)	79,576		AA +u	Aaa
Federal Agency (Fixed Rate)	25,473		AA+	Aaa
Federal Agency (Fixed Rate)	98,308	2	AAAm	Aaa-mf
U.S. Government and Agencies	218,551			
Total debt securities investments	**$ 359,568**			

Non-Rating Description	
NA	Not Available

[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.

(Dollars in Thousands)

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.

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 up to 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

As of December 31, 2011, the investments in any one issuer of corporate bonds, asset-backed securities and commercial paper that represents 5% or more of MLGW's investments are as follows:

Issuer	Reported Amount	Percentage of Portfolio
General Electric	$ 23,825	6.6%
Total	**$ 23,825**	

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, 2011, 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, 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, 2011, MLGW had no credit risk exposure to borrowers because the amounts MLGW owed the borrowers exceeded the amounts the borrowers owed MLGW. The maturities of the investments made with cash collateral do not necessarily match the maturities of the securities on loan. There are no restrictions on the amount of securities that can be lent at one time or to one borrower. 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. The Agent shall issue a safekeeping receipt to MLGW listing the specific instrument, rate, maturity and other pertinent information. On a monthly basis, the Agent will also provide reports which list all securities held for MLGW, the book value of holdings and the market value as of month-end. Appropriate MLGW officials and representatives of the Agent responsible for, or in any manner involved with, the safekeeping and custody process of MLGW shall be bonded in such a fashion as to protect MLGW from losses from malfeasance and misfeasance. In addition, MLGW will not deposit funds through third parties or money brokers.

Under the terms of the lending agreement, MLGW is indemnified against any losses, damages, costs and expenses should the Agent be unable to recover borrowed securities and distributions due to 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.

(Dollars in Thousands)

2. Deposits and Investments (continued)

Securities Lending (continued)

As of December 31, 2011, MLGW investments held by broker-dealers under securities loans consist of the following:

	Market Value of Securities on Loan *				Cash Collateral Received			
Securities on Loan	Electric Division	Gas Division	Water Division	Total	Electric Division	Gas Division	Water Division	Total
U.S. Agencies	$ 3,467	$ 2,161	$ 497	$ 6,125	$ 3,562	$ 2,220	$ 511	$ 6,293
U.S. Government Fixed	32,303	20,126	4,634	57,063	32,828	20,453	4,709	57,990
Corporate Bonds	1,251	779	179	2,209	1,287	801	184	2,272
Total	**$ 37,021**	**$ 23,066**	**$ 5,310**	**$ 65,397**	**$ 37,677**	**$ 23,474**	**$ 5,404**	**$ 66,555**

* Market value of securities on loan includes accrued interest.

Restricted and Unrestricted Funds

Restricted funds, cash and cash equivalents, and investments consisted of the following as of December 31, 2011 and 2010:

	Electric Division		Gas Division		Water Division	
	2011	**2010**	**2011**	**2010**	**2011**	**2010**
Restricted funds:						
Cash and cash equivalents	**$ 44,593**	$ 44,219	**$ 10,437**	$ 11,736	**$ 12,432**	$ 9,650
Investments	**10,318**	9,659	**2,884**	3,065	**5,259**	4,019
Total restricted funds	**$ 54,911**	$ 53,878	**$ 13,321**	$ 14,801	**$ 17,691**	$ 13,669
Unrestricted funds:						
Cash and cash equivalents	**$ 89,780**	$ 84,374	**$ 62,551**	$ 71,621	**$ 7,105**	$ 9,872
Investments	**75,288**	63,112	**50,797**	50,083	**5,966**	7,439
Total unrestricted funds	**$ 165,068**	$ 147,486	**$ 113,348**	$ 121,704	**$ 13,071**	$ 17,311

(Dollars in Thousands)

3. Long-Term Receivables

In 2002, MLGW and the Valero Refining Group ("Valero") 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 receivable payments are as follows for the years ending December 31:

2012	$ 1,712
2013	1,712
2014	1,712
2015	1,712
2016	1,139
	$ 7,987

The Valero lease receivable is included in notes receivable in the accompanying 2011 Gas Division's balance sheet, except for the current portion of $1,712, which is included in other current assets.

(Dollars in Thousands)

4. Utility Plant

Utility plant activity for the years ended December 31, 2011 and 2010 is as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Year ended December 31, 2011				
Electric Division				
Capital assets not being depreciated:				
Land	$ 29,912	$ (11)	$ -	$ 29,901
Land - Non-utility	15,345	-	-	15,345
Construction in progress	68,159	60,877	(55,249)	73,787
Total capital assets not being depreciated	113,416	60,866	(55,249)	119,033
Capital assets being depreciated or amortized:				
Structures and improvements	57,007	252	(101)	57,158
Transmission and distribution plant equipment	1,180,172	46,535	(10,009)	1,216,698
General plant equipment	151,014	8,473	(2,038)	157,449
Total capital assets being depreciated or amortized	1,388,193	55,260	(12,148)	1,431,305
Less accumulated depreciation and amortization	(572,208)	(48,212)	18,241	(602,179)
Total capital assets being depreciated or amortized, net	815,985	7,048	6,093	829,126
Total capital assets, net	$ 929,401	$ 67,914	$ (49,156)	$ 948,159
Gas Division				
Capital assets not being depreciated:				
Land	$ 7,502	$ -	$ -	$ 7,502
Land - Non-utility	66	-	-	66
Construction in progress	12,829	20,076	(22,706)	10,199
Plant held for future use	212	-	-	212
Total capital assets not being depreciated	20,609	20,076	(22,706)	17,979
Capital assets being depreciated or amortized:				
Structures and improvements	55,687	1,628	(11)	57,304
Processing and distribution plant equipment	414,702	17,211	(484)	431,429
General plant equipment	62,812	3,867	(3,258)	63,421
Non-utility plant equipment	200	-	-	200
Total capital assets being depreciated or amortized	533,401	22,706	(3,753)	552,354
Less accumulated depreciation and amortization	(254,323)	(13,856)	4,101	(264,078)
Total capital assets being depreciated or amortized, net	279,078	8,850	348	288,276
Total capital assets, net	$ 299,687	$ 28,926	$ (22,358)	$ 306,255

(Dollars in Thousands)

4. Utility Plant (continued)

	Beginning Balance	Increases	Decreases	Ending Balance
Year ended December 31, 2011				
Water Division				
Capital assets not being depreciated:				
Land	**$ 3,304**	**$ 24**	**$ -**	**$ 3,328**
Construction in progress	**11,635**	**12,028**	**(8,071)**	**15,592**
Total capital assets not being depreciated	**14,939**	**12,052**	**(8,071)**	**18,920**
Capital assets being depreciated or amortized:				
Structures and improvements	**48,585**	**78**	**-**	**48,663**
Pumping, transmission and distribution plant equipment	**319,979**	**5,295**	**(905)**	**324,369**
General plant equipment	**64,939**	**2,674**	**(661)**	**66,952**
Total capital assets being depreciated or amortized	**433,503**	**8,047**	**(1,566)**	**439,984**
Less accumulated depreciation and amortization	**(185,925)**	**(12,513)**	**1,969**	**(196,469)**
Less acquisition adjustment	**(8,188)**	**964**	**-**	**(7,224)**
Total capital assets being depreciated or amortized, net	**239,390**	**(3,502)**	**403**	**236,291**
Total capital assets, net	**$ 254,329**	**$ 8,550**	**$ (7,668)**	**$ 255,211**

	Beginning Balance	Increases	Decreases	Ending Balance
Year ended December 31, 2010				
Electric Division				
Capital assets not being depreciated:				
Land	$ 29,554	$ 358	$ -	$ 29,912
Land - Non-utility	15,345	-	-	15,345
Construction in progress	66,811	61,249	(59,901)	68,159
Total capital assets not being depreciated	111,710	61,607	(59,901)	113,416
Capital assets being depreciated or amortized:				
Structures and improvements	55,258	1,765	(16)	57,007
Transmission and distribution plant equipment	1,138,495	48,546	(6,869)	1,180,172
General plant equipment	145,430	9,232	(3,648)	151,014
Total capital assets being depreciated or amortized	1,339,183	59,543	(10,533)	1,388,193
Less accumulated depreciation and amortization	(541,917)	(46,099)	15,808	(572,208)
Total capital assets being depreciated or amortized, net	797,266	13,444	5,275	815,985
Total capital assets, net	$ 908,976	$ 75,051	$ (54,626)	$ 929,401

(Dollars in Thousands)

4. Utility Plant (continued)

	Beginning Balance	Increases	Decreases	Ending Balance
Year ended December 31, 2010				
Gas Division				
Capital assets not being depreciated:				
Land	$ 7,502	$ -	$ -	$ 7,502
Land - Non-utility	66	-	-	66
Construction in progress	9,160	19,178	(15,509)	12,829
Plant held for future use	212	-	-	212
Total capital assets not being depreciated	16,940	19,178	(15,509)	20,609
Capital assets being depreciated or amortized:				
Structures and improvements	54,931	1,096	(340)	55,687
Processing and distribution plant equipment	403,943	12,104	(1,345)	414,702
General plant equipment	63,859	2,309	(3,356)	62,812
Non-utility plant equipment	200	-	-	200
Total capital assets being depreciated or amortized	522,933	15,509	(5,041)	533,401
Less accumulated depreciation and amortization	(244,377)	(15,252)	5,306	(254,323)
Total capital assets being depreciated or amortized, net	278,556	257	265	279,078
Total capital assets, net	$ 295,496	$ 19,435	$ (15,244)	$ 299,687

	Beginning Balance	Increases	Decreases	Ending Balance
Water Division				
Capital assets not being depreciated:				
Land	$ 3,304	$ -	$ -	$ 3,304
Construction in progress	14,897	11,822	(15,084)	11,635
Total capital assets not being depreciated	18,201	11,822	(15,084)	14,939
Capital assets being depreciated or amortized:				
Structures and improvements	47,819	807	(41)	48,585
Pumping, transmission and distribution plant equipment	308,702	11,889	(612)	319,979
General plant equipment	67,415	2,388	(4,864)	64,939
Total capital assets being depreciated or amortized, net	423,936	15,084	(5,517)	433,503
Less accumulated depreciation and amortization	(179,244)	(12,563)	5,882	(185,925)
Less acquisition adjustment	(9,152)	964	-	(8,188)
Total capital assets being depreciated or amortized, net	235,540	3,485	365	239,390
Total capital assets, net	$ 253,741	$ 15,307	$ (14,719)	$ 254,329

(Dollars in Thousands)

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 2012 are estimated as follows (unaudited):

Electric Division	$ 102,916
Gas Division	27,707
Water Division	18,883

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 expand the acquired water system.

5. Employee Retirement System

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.

(Dollars in Thousands)

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, 2011 and 2010:

	2011	2010
Retirees and beneficiaries receiving benefits	**2,532**	2,495
Terminated plan members entitled to but not yet receiving benefits	**35**	41
Active members fully vested	**1,150**	1,153
Active members not vested	**1,434**	1,447
Total	**5,151**	5,136

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. 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. MLGW also funds the 8% pension plan member's contribution on behalf of the president and vice presidents. For 2011, MLGW contributed 17% of the annual covered payroll.

(Dollars in Thousands)

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 2011 and 2010:

	2011	2010
Annual required contribution ("ARC")	**$ 26,208**	$ 27,381
Interest on net pension asset	**(1,206)**	(1,248)
Adjustment to annual required contribution	**942**	1,814
Annual pension cost	**25,944**	27,947
Contributions made	**(26,213)**	(27,385)
Change in net pension asset	**(269)**	562
Net pension asset at beginning of fiscal year	**(16,079)**	(16,641)
Net pension asset at end of fiscal year	**$ (16,348)**	$ (16,079)

Three-Year Trend Information

Fiscal Year Ending	Annual Pension Cost	Percentage of APC Contributed	Net Pension Obligation (Asset)
December 31, 2011	$ 25,944	101.0%	$ (16,348)
December 31, 2010	27,947	98.0%	(16,079)
December 31, 2009	22,984	93.1%	(16,641)

Funded Status and Funding Progress

As of January 1, 2012, the most recent actuarial valuation date, the MLGW Pension Plan was 84.2% funded. The actuarial accrued liability ("AAL") for benefits was $1,350,812, and the actuarial value of assets was $1,137,615, resulting in an unfunded actuarial accrued liability ("UAAL") of $213,197. The covered payroll (annual payroll of active employees covered by the pension plan) was $154,036, and the ratio of the UAAL to the covered payroll was 138.4%.

(Dollars in Thousands)

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, 2012 actuarial valuation using the entry age normal cost method. Actuarial methods and significant assumptions were as follows:

Valuation Date	January 1, 2012
Actuarial Cost Method	Entry Age Normal Cost Method
Amortization Method	Level percent of payroll
Remaining Amortization Period	29 years remaining as of January 1, 2012
Asset Valuation Method	Market value of assets less unrecognized returns in each of the last five years. Unrecognized return is equal to the difference between the actual market return and the expected return on the market value, and is recognized over a five-year period, further adjusted, if necessary, to be within 30% of the market value.
Actuarial Assumptions:	
Investment Rate of Return	7.50%
Inflation Rate	3.25%
Projected Salary Increases	Inflation plus merit increases that vary by age and service
Cost of Living Adjustments	0.98% for ages 56 - 58 1.95% for ages 59 - 61 2.44% for ages 62 and older, and all disabled participants

6. Deferred Compensation Plan

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

The 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 in MLGW's balance sheets.

7. Other Postemployment Benefits

The Memphis Light, Gas and Water Division OPEB Trust ("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. The OPEB Trust is administered by the MLGW OPEB Committee.

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 dependents. 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.

The Plan provides postemployment coverage for 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. Current year 4,182 retirees and spouses are receiving postemployment benefits.

(Dollars in Thousands)

7. Other Postemployment Benefits (continued)

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 No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. 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 2011, employer contributions were $43,554 to the Plan. Plan members receiving benefits contributed $5,718 through their required contribution of $62.70 to $566.18 (dollars) per month depending on the coverage (employee only, employee and spouse, or family) and the health plan selected.

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, 2009. During 2012, an updated actuarial valuation was performed. The actuarial valuation of MLGW's postemployment welfare benefit program as of December 31, 2009 was updated based on the revised valuation. 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, 2011 and 2010:

	2011	2010
Annual required contribution	**$ 44,666**	$ 43,693
Interest on net OPEB obligation	**(174)**	(188)
Adjustment to annual required contribution	**138**	146
Annual OPEB cost	**44,630**	43,651
Contributions made	**(43,554)**	(43,476)
Change in net OPEB asset	**1,076**	175
Net OPEB asset at beginning of fiscal year	**(2,325)**	(2,500)
Net OPEB asset at end of fiscal year	**$ (1,249)**	$ (2,325)

(Dollars in Thousands)

7. Other Postemployment Benefits (continued)

Annual OPEB Cost and Net OPEB Obligation (continued)

MLGW's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for fiscal year 2011 and the two preceding years were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation (Asset)
December 31, 2011	$ 44,630	97.6%	$ (1,249)
December 31, 2010	43,651	99.6%	(2,325)
December 31, 2009	55,340	100.6%	(2,500)

Funded Status and Funding Progress

As of December 31, 2009, the most recent actuarial valuation date, the plan was 21.2% funded. The actuarial accrued liability (AAL) for benefits was $591,528 and the actuarial value of assets was $125,234, resulting in an unfunded actuarial accrued liability (UAAL) of $466,294. The covered payroll (annual payroll of active employees covered by the Plan) was $153,117, and the ratio of the UAAL to the covered payroll was 304.5%.

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.

(Dollars in Thousands)

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:

Valuation Date	December 31, 2009
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level percent of pay, 30 years
Remaining Amortization Period	27 years as of December 31, 2009
Asset Valuation Method	Market value
Actuarial Assumptions:	
Investment Rate of Return	7.50%
Inflation Rate	3.25%
Projected Salary Increases	Ultimately, 7.60% at age 24 graded to 3.25% at age 60 and older
Medical Cost Trend Rate for PPO, POS and HMO (starting 1/1/2010)	9.25% graded to 5.00% over 9 years
Medical Cost Trend Rate for POS and HMO	9.00% graded to 5.00% over 8 years
Drug Cost Trend Rate	8.50% graded to 5.00% over 7 years

(Dollars in Thousands)

8. Long-Term Debt

Long-term debt as of December 31, 2011 and 2010 consists of the following:

	Interest Rates	2011	2010
Electric Division:			
Electric System Revenue Bonds:			
Series 2003A, due serially 2010-2018	3.00-5.00%	**$ 200,905**	$ 291,325
Series 2008, due serially 2017-2018	4.00-5.00%	**96,930**	96,930
Series 2010, due serially 2014-2018	2.50-5.00%	**460,050**	460,050
Premium on revenue bonds		**56,588**	70,961
Unamortized deferred cost on bond refunding		**(17,752)**	(21,559)
Total		**796,721**	897,707
Less: current portion of bonds		**(95,190)**	(90,420)
		$ 701,531	$ 807,287
Water Division:			
Revenue Refunding Bonds:			
Series 1998, due serially 2010-2012	5.25%	**$ 1,625**	$ 1,625
Premium on revenue bonds		**-**	2
Unamortized deferred cost on bond refunding		**-**	(15)
		1,625	1,612
Less: current portion of bonds		**-**	-
		$ 1,625	$ 1,612

Principal payments on bonds are due annually on January 1 or December 1. Debt service requirements as of December 31, 2011, are as follows:

	Electric Division		Water Division	
	Principal	Interest	Principal	Interest
2012	$ 95,190	$ 37,028	$ 1,625	$ 43
2013	99,700	32,291	-	-
2014	102,765	27,431	-	-
2015	107,775	22,417	-	-
2016	112,935	17,150	-	-
2017-2018	239,520	17,331	-	-
Total	$ 757,885	$ 153,648	$ 1,625	$ 43

MLGW, at its option, may redeem bonds prior to maturity at premiums and prices specified in the indentures. The Series 2003A, Series 2008, and Series 2010 bonds are subject to mandatory redemption upon early termination of the Supplement to the Power Contract ("Supplement") with TVA as discussed in Note 10.

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. Long-Term Debt (continued)

During 2010, the Electric Division issued $460,050 of Series 2010 bonds to advance refund a portion of the outstanding Electric System Subordinate Revenue Bonds, Series 2003A, and to pay certain costs of issuance of the Series 2010 Bonds. The refunding was undertaken to reduce total future debt service payments. The 2010 Series Bonds have a net present value benefit of $16,541, with a cash savings of $18,809 over the life of the bonds. The first principal payment is to be made December 1, 2014, and thereafter annually with a final maturity date of December 1, 2018. The Series 2010 Bonds bear interest at annual fixed rates ranging from 2.50% to 5.00%. The Series 2010 Bonds are not subject to optional redemption, but will be subject to extraordinary redemption prior to maturity. See Note 10.

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 10. 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, bore interest for 35-day auction periods. The Series 2003B revenue bonds were refunded in 2008, as discussed above.

MLGW's Electric Division bond covenants require that for Series 2003A, 2008 Bonds, and 2010 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, 2011, was 1.81.

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, 2011, was 8.69.

(Dollars in Thousands)

8. Long-Term Debt (continued)

Long-term debt activity for the years ended December 31, 2011 and 2010 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Year ended December 31, 2011:				
Electric Division				
Bonds payable:				
Revenue bonds	$ 848,305	$ -	$ (90,420)	$ 757,885
Premium on revenue bonds	70,961	-	(14,373)	56,588
Less deferred amounts:				
For issuance discounts and on refunding	(21,559)	-	3,807	(17,752)
Total bonds payable	$ 897,707	$ -	$ (100,986)	$ 796,721
Water Division				
Bonds payable:				
Revenue bonds	$ 1,625	$ -	$ -	$ 1,625
Premium on revenue bonds	2	-	(2)	-
Less deferred amounts:				
For issuance discounts and on refunding	(15)	-	15	-
Total bonds payable	$ 1,612	$ -	$ 13	$ 1,625
Year ended December 31, 2010:				
Electric Division				
Bonds and note payable:				
Revenue bonds	$ 952,165	$ 460,050	$ (563,910)	$ 848,305
Premium on revenue bonds	49,930	69,740	(48,709)	70,961
Notes payable	1,499	-	(1,499)	-
Less deferred amounts:				
For issuance discounts and on refunding	(56)	(24,573)	3,070	(21,559)
Total bonds and note payable	$ 1,003,538	$ 505,217	$ (611,048)	$ 897,707
Water Division				
Bonds payable:				
Revenue bonds	$ 3,165	$ -	$ (1,540)	$ 1,625
Premium on revenue bonds	7	-	(5)	2
Less deferred amounts:				
For issuance discounts and on refunding	(45)	-	30	(15)
Total bonds payable	$ 3,127	$ -	$ (1,515)	$ 1,612

(Dollars in Thousands)

9. Self-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, 2011 and 2010 are as follows:

	Medical Benefits			Injuries and Damages		
	Electric Division	Gas Division	Water Division	Electric Division	Gas Division	Water Division
Balance -- December 31, 2009	$ 4,500	$ 2,175	$ 1,238	$ 6,163	$ 2,314	$ 1,850
Payments	(27,473)	(12,253)	(8,136)	(1,334)	(583)	(890)
Incurred claims expense	27,269	11,993	8,170	1,900	780	600
Balance -- December 31, 2010	4,296	1,916	1,272	6,729	2,511	1,560
Payments	**(30,221)**	**(13,479)**	**(8,950)**	**(4,230)**	**(1,645)**	**(783)**
Incurred claims expense	**30,815**	**13,744**	**9,126**	**3,900**	**780**	**600**
Balance -- December 31, 2011	**$ 4,890**	**$ 2,181**	**$ 1,448**	**$ 6,399**	**$ 1,646**	**$ 1,377**

10. Energy Supplies

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 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 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. Subsequently, MLGW has refinanced portions of the bonds originally issued for the prepayment. In 2008, the Series 2003B bonds were refunded by the Series 2008 bonds. In 2010, the callable portion of the 2003A Series bonds were refunded by the Series 2010 bonds. See also Note 1 (Prepaid Power Cost) and Note 8 (Long-Term 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.

10. Energy Supplies (continued)

MLGW purchases natural gas from multiple suppliers on multiple pipelines in order to minimize operational and performance risk. MLGW has 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 gas purchase contract beginning January 1, 2007 with volume commitments for the term. In November 2006, Public Energy Authority of Kentucky, Inc. ("PEAK") and MLGW entered into a 5 year gas purchase contract with volume commitments for the term. In October 2011, PEAK and MLGW renewed, for a second term, a 5 year gas purchase contract with volume commitments for the term. MLGW and the Public Energy Authority of Kentucky, Inc. (PEAK) are negotiating a new, 7 1/2 year gas purchase contract with declining volume commitments for the term. 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.

11. Rates

Electric, gas and water rates are established by MLGW and rate changes are subject to approval by the Council. The 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.

TVA implemented a wholesale rate change effective with the April 2011 revenue month, moving from end-use rates to a wholesale rate structure where the cost of power varies based on when electricity is used. The new wholesale rate structure was designed to be revenue neutral for TVA. MLGW implemented changes to its retail rate schedules effective with meters read on or after March 31, 2011. New retail rates had minimal impacts to customers' bills, but rates now change seasonally. The retail effects varied by customer class, with the approximate annual changes being reduced 0.6% for residential, reduced 0.7% for small and medium commercial customers reduced 0.2% for large commercial customers and increased 3.1% for industrial customers.

TVA implemented a rate adjustment effective with the October 2011 revenue month, increasing the cost of wholesale power (excluding fuel and purchased power) purchased by MLGW by approximately 3.08%. MLGW implemented changes to its retail rate schedules effective with meters read on or after September 30, 2011, 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 1.8% for residential, 1.8% for commercial customers and 1.9% for industrial customers.

MLGW retail electric rates are adjusted for TVA's Fuel Cost Adjustor ("FCA"). The FCA is a variable wholesale energy rate that can fluctuate each month 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.

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.

11. Rates (continued)

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.

MLGW implemented a water rate increase effective with meters read on or after January 3, 2011. This rate increase was required due to increased general operating expenses. The retail impact was 5% to all customer classes.

12. Transfers to City

The Electric, Gas and Water Divisions make transfers to the City.

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, transfers a payment in the amount of $2,500 per year. The agreement is effective through the year 2028.

13. Self-Insurance

MLGW is self-insured for health and medical benefits, and for injuries and damages, including workers compensation and general liability claims. 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 personal injuries are $300 per person and $700 for two or more persons per accident. Property damages are limited to $100 per accident.

14. Commitments and Contingencies

The Gas Division has derivative contracts and agreements from which risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in prices. The exposure to credit loss in the event of nonperformance by the other party is represented by the fair values of the open derivative contracts. However, there is no counterparty financial risk for contracts transacted through the New York Mercantile Exchange (“NYMEX”) or the Intercontinental Exchange (“ICE”).

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

14. Commitments and Contingencies (continued)

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 10 for discussions of MLGW's power contract with TVA and gas purchase commitments.

15. Federal Grant Contributions

On three separate occasions during April 2011 severe storm systems produced heavy winds and thunderstorms that hit the service area causing damage to MLGW's electric distribution system. The April 4th storm expenditures totaled $3,289. Of that amount, the Electric Division has been approved to receive $2,467 (or 75%) reimbursement of eligible expenses from the Federal Emergency Management Agency ("FEMA") (Contract 34101-0000008735.)

The April 19th storm also caused damage to MLGW's electric distribution system in the amount of $3,142. Of that amount, the Electric Division has been approved to receive $2,357 (or 75%) reimbursement of eligible expenses from FEMA (Contract 34101-0000009241.)

The April 26th storm, with the accompanying flooding, caused damage to the electric, gas and water distribution systems. The flood qualified as a 500-year flood for the Mississippi River in the Memphis area. Total expenditures for this storm and flood during April and May totaled $2,612; of which $2,274 was for the Electric Division for damage to the electric distribution system, $315 for the Gas Division for costs to remove and replace gas mains and $23 for the Water Division to remove and replace water mains. The Electric Division has been approved to receive $1,706 (or 75%) reimbursement of eligible expenses from FEMA (Contract 34101-0000009498.) The Gas Division has been approved to receive $236 (or 75%) reimbursement; and the Water Division has been approved to be reimbursed for $17 (or 75%).

During May 2010, severe storms caused damage to MLGW's electric and gas distribution systems. Total expenditures for all divisions related to the storm and subsequent flood were $603. Of these costs, $598 was in the Electric Division and $5 was in the Gas Division. The MLGW Electric Division has been approved to receive $538 (or 90%) reimbursement of eligible expenses from the Federal Emergency Management Agency ("FEMA") (Contract 34101-0000005751); and the Gas Division has been approved to receive a reimbursement of $5 (or 90%) of eligible expenses. In December 2010, FEMA paid $20 to the Electric Division and $4 to the Gas Division. In January 2011, FEMA paid the Electric Division an additional $383, leaving a $135 balance for the Electric Division and $1 balance for the Gas Division.

During June 2009, straight-line winds and two tornadoes caused damage to Substation 67 and MLGW's electric distribution system. As of December 31, 2009 the total expenditures for the Electric Division as a

15. Federal Grant Contributions (continued)

result of the storms was $8,505. The Electric Division received insurance proceeds in the amount of $100 for these expenditures. MLGW has been approved to receive reimbursement from FEMA (Contract 34101-0000001983) totaling $5,932 (or 75%) of eligible expenses. In March 2010, a partial payment of $4,453 was received from FEMA leaving a balance of $1,479. The Electric Division received payment of $919 in August 2011 leaving a $560 balance as of December 31, 2011. Final payment was received in March 2012.

In October 2008, FEMA announced approval of the High Voltage Transformer Seismic Retrofit Project (Contract Edison #E-18001) under the Pre-Disaster Mitigation Competitive Program. The award was approximately $2,700, of which $2,025 is being federally funded. Fiscal year 2008 expenditures totaled $19, with $14 (or 75%) eligible for federal reimbursement. Fiscal year 2009 expenditures totaled $548, with $411 (or 75%) eligible for federal reimbursement. As of December 31, 2008 and 2009, receivable balances were $14 and $425, respectively. Fiscal year 2010 expenditures totaled $522 with $392 (or 75%) eligible for federal reimbursement. A reimbursement of $429 was received in April 2010 leaving a receivable balance of $388. Reimbursements in the amount of $568 were received during 2011. Fiscal year 2011 expenditures totaled $240. As of December 31, 2011, the total receivable balance for the High Voltage Transformer Seismic Retrofit Project is $60.

In 2009, MLGW applied for the Smart Grid Investment Grant (Contract# DE-OE0000281) under the American Recovery and Investment Act ("ARRA") for the Department of Energy's Electricity Delivery and Energy Reliability, Research, Development, and Analysis Program. The grant was awarded in 2010. The grant will allow MLGW to install a communications system that will enable the observation and control of its network electric grid. The total grant was for $13,112 with $5,063 being federally funded. Fiscal year 2010 expenditures totaled $711, of which $341 (or 48%) qualified for federal reimbursement. Federal share payments received as of December 2010 totaled $164, leaving the remaining receivable balance of $177. Reimbursements in the amount of $753 were received during fiscal year 2011. Fiscal year 2011 expenditures totaled $841. As of December 31, 2011, the total receivables balance for the Smart Grid Investment Grant is $265.

In 2009, The City of Memphis, in conjunction with MLGW, applied for a grant under the American Recovery and Investment Act ("ARRA") for the Department of Energy's Energy Efficiency and Conservation Block Program. The grant was awarded in September 2009. The total grant was for $6,767, with $5,000 allocated to MLGW for direct investment in energy efficiency improvements to customer homes and businesses. As of December 31, 2009, planning began with no funds expended in 2009. As of December 31, 2011, MLGW had expended $3,680 with $3,680 reimbursed and receivables totaling $0.

In 2010, MLGW applied for the Network System Transformer Seismic Retrofit Grant (Contract# E-29504). The grant was awarded in 2011 under the Pre-Disaster Mitigation Competitive Program. The grant will allow MLGW to retrofit 482 network system transformers. The grant was awarded in the amount of $603 of which $453 (or 75%) will be federally funded. As of December 31, 2011, MLGW had not incurred any expenditure under this grant.

15. Federal Grant Contributions (continued)

As recipients of federal grant contributions, the Divisions are subject to examination by various federal and state authorities and the results of such examinations could result in changes to the reported grant contributions. During early 2012, the Office of Inspector General (OIG) began an examination of certain Federal Emergency Management Agency (FEMA) grants received in 2008 and 2009. The examination is still in process and the Divisions have not received the final results of such examination. During the examination process, the OIG indicated that they plan to question certain costs that were incurred without competitive bids. The Divisions believe that the competitive bidding process was not feasible for these costs because of the public exigency or emergency nature of these expenditures. Resolution of this matter may not be known for several months. If the Divisions receive an unfavorable determination from FEMA concerning such 2008 and 2009 costs, the grant contributions reported for 2008 and 2009 could be reduced with a portion refunded to FEMA and the grant contributions reported in 2010 and 2011 could also be adversely effected. Management believes that reductions in the 2008 and 2009 grants, if any, will not be material to the Divisions' financial statements.

16. Pollution Remediation Obligation

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. These estimates assume no expected change orders.

MLGW is under a Consent Agreement and Final Order from the United States Environmental Protection Agency ("EPA") to perform a Supplemental Environmental Project ("SEP") over three years beginning November, 2008. 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 EPA for violations of Section 6(e) of TSCA, 15 U.S.C. § 2605. The liability for PCBs includes removal and disposal of substation equipment that meets the criteria for pollution remediation.

In July 2009, MLGW was notified by the Tennessee Department of Environment and Conservation, Division of Water Pollution Control ("TDEC") of a violation of the Water Quality Control Act (TCA 69-3-114 (a)). In response to this violation, MLGW presented a remediation action plan to TDEC agency. After approval of the plan, MLGW obtained an estimate from a licensed contractor to perform the necessary activities. This project was completed in 2011.

MLGW annually evaluates current conditions, remediation plan updates and changes in legal or regulatory requirements to revise MLGW's estimated liability. Regulatory accounts are used to capture the net effect of the changes in estimates for each Division. See Note 1 (Regulatory Accounting).

(Dollars in Thousands)

16. Pollution Remediation Obligation (continued)

The schedule below shows the balances as of December 31, 2011 and 2010 for each pollution liability by Division:

		2011	2010
Electric			
	PCB	**$ 1,424**	$ 2,327
	Asbestos	**1,341**	1,440
	Lead	**9,355**	9,979
	Storm Water	**255**	900
Total Electric		**12,375**	14,646
Gas			
	Asbestos	**183**	183
	Lead	**3,076**	2,495
	Storm Water	**46**	345
Total Gas		**3,305**	3,023
Water			
	Asbestos	**1,304**	1,304
	Lead	**4,863**	4,153
	Storm Water	**34**	255
Total Water		**6,201**	5,712
Total Liability		**$ 21,881**	$ 23,381
Total PCB		**$ 1,424**	$ 2,327
Total Asbestos		**2,828**	2,927
Total Lead		**17,294**	16,627
Total Storm Water		**335**	1,500
Total Liability		**$ 21,881**	$ 23,381

REQUIRED SCHEDULE OF FUNDING PROGRESS FOR PENSION PLAN
DECEMBER 31, 2011
(Dollars in Thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded/ (Overfunded) AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll* ((b - a) / c)
January 1, 2012	$ 1,137,615	$ 1,350,812	$ 213,197	84.2%	$ 154,036	138.4%
January 1, 2011	1,171,384	1,324,410	153,026	88.5%	153,509	99.7%
January 1, 2010	1,191,027	1,292,791	101,764	92.1%	154,057	66.1%

* Not less than zero

REQUIRED SCHEDULE OF FUNDING PROGRESS FOR OPEB
DECEMBER 31, 2011
(Dollars in Thousands)

MLGW

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll (c)		UAAL as a Percentage of Covered Payroll ((b - a) / c)
December 31, 2009	$ 125,234	$ 591,528	$ 466,294	21.2%	$ 153,117		304.5%
December 31, 2007	15,097	674,002	658,905	2.2%	144,756		455.2%
December 31, 2006*	-	743,484	743,484	0.0%	148,219	**	501.6%

* Projected from 12/31/05 valuation.
** Projected from 2006 payroll.

(Dollars in Thousands)

Fiscal Year Ended	Annual OPEB Cost	Employer Contributions	Percentage of Annual OPEB Cost Contributed
December 31, 2011	$ 44,630	$ 43,554	97.6%
December 31, 2010	43,651	43,476	99.6%
December 31, 2009	55,340	55,688	100.6%

SCHEDULE OF LONG-TERM DEBT,
PRINCIPAL AND INTEREST REQUIREMENTS
DECEMBER 31, 2011
(Dollars in Thousands)

	Series 2003A		Series 2008		Series 2010	
	Principal	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**
Electric Division:						
2012	$ 95,190	$ 9,836	$ -	$ 4,564	$ -	$ 22,628
2013	99,700	5,099	-	4,564	-	22,628
2014	-	239	-	4,564	102,765	22,628
2015	1,845	239	-	4,564	105,930	17,614
2016	-	169	-	4,564	112,935	12,417
2017	2,220	169	31,625	4,564	83,350	6,821
2018	1,950	81	65,305	3,043	55,070	2,653
Total	$ 200,905	$ 15,832	$ 96,930	$ 30,427	$ 460,050	$ 107,389

	Series 1998	
	Principal	**Interest**
Water Division:		
2012	$ 1,625	$ 43
Total	$ 1,625	$ 43

Electric Division Rate Class	Base Charge	Customers

All Electric Rate Schedules Are Subject To Adjustment Under The Provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.

Residential - Schedule RS 357,273

Effective meters read on or after September 30, 2011.

Customer Charge: $11.20 per month, less Hydro Allocation Credit: $1.60

Energy Charge:	Summer	Winter	Transition
First 2,000 kWh per month:	$0.06257	$0.06244	$0.06179
Additional kWh per month:	$0.07111	$0.07098	$0.07033

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

General Service - Schedule GSA 43,450

Effective meters read on or after September 30, 2011.

If (a) the higher of (i) the customer's currently effective contract demand, if any, or (ii) its highest billing demand during the latest 12 month period is not more than 50 kW, and (b) customer's monthly energy takings for any month during such period do not exceed 15,000 kWh:

Customer Charge: $15.52 per delivery point per month

Energy Charge:	Summer	Winter	Transition
	$0.07491	$0.07480	$0.07414

If (a) the higher of (i) the customer's currently effective contract demand or (ii) its highest billing demand during the latest 12 month period is greater than 50 kW but not more than 1,000 kW, or (b) if the customer's billing demand is less than 50 kW and its energy takings for any month during such period exceed 15,000 kWh:

Electric Division Rate Class (cont.)	Base Charge			Customers
General Service - Schedule GSA (cont.)				
Customer Charge:	$53.42 per delivery point per month			
Demand Charge:	Summer	Winter	Transition	
First 50 kW of billing demand per month:	$0.00	$0.00	$0.00	
Excess over 50 kW of billing demand per month:	$12.42	$11.59	$11.59	
Energy Charge:				
First 15,000 kWh per month:	$0.08075	$0.08064	$0.07998	
Additional kWh per month:	$0.03350	$0.03350	$0.03350	
	If the higher of the customer's currently effective contract demand or its highest billing demand during the latest 12 month period is greater than 1,000 kW:			
Customer Charge:	$191.84 per delivery point per month			
Demand Charge:	Summer	Winter	Transition	
First 1,000 kW of billing demand per month:	$11.42	$10.60	$10.60	
Excess over 1,000 kW of billing demand per month:	$11.26	$10.44	$10.44	
Excess of billing demand over the higher of 2,500 kW or the customer's contract demand per month:	$11.26	$10.44	$10.44	
Energy Charge:				
All kWh per month:	$0.03843	$0.03843	$0.03843	
Time-Of-Day General Power Rate - Part A (Schedule TGSA)	Effective October 1, 2011			1
	Summer	Non-Summer		
Customer Charge:	$198.95	$198.95		
On-peak per kW of billing demand charges per month:	$11.95	$11.10		

Electric Division Rate Class (cont.)	Base Charge	Customers

Time-Of-Day General Power Rate - Part A (Schedule TGSA) (cont.)

	Summer	Non-Summer
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$1.66	$1.66
Per kW charge 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:	$11.95	$11.10
On-peak per kWh energy charge:	$0.03855	$0.03855
Off-peak per kWh energy charge:	$0.03782	$0.03782

General Power Rate - TDGSA 0

Effective October 1, 2011

Customer Charge: $1,500.00 per delivery point per month
TVA Administrative Charge: $350.00 per delivery point per month

	Summer	Winter	Transition
On-peak per kW of billing demand charges per month:	$16.89	$9.79	$0.00
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$4.45	$4.45	$4.45
Excess per kW charge per month by which billing demand exceeds contract demand:	$16.89	$9.79	$4.45
On-peak per kWh energy charge:	$0.07387	$0.04321	$0.00000
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.03919	$0.03919	$0.03919
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.02053	$0.02053	$0.02053
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.00469	$0.00469	$0.00469

Electric Division Rate Class (cont.)	Base Charge	Customers

Manufacturing Power Rate - TDMSA — Customers: 2

Effective October 1, 2011

Customer Charge: $1,500.00 per delivery point per month
TVA Administrative Charge: $350.00 per delivery point per month

	Summer	Winter	Transition
On-peak per kW of billing demand charges per month:	$16.78	$9.68	$0.00
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$4.34	$4.34	$4.34
Excess per kW charge per month by which billing demand exceeds contract demand:	$16.78	$9.68	$4.34
On-peak per kWh energy charge:	$0.05833	$0.02830	$0.00000
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.02403	$0.02403	$0.02403
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.00537	$0.00537	$0.00537
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	-$0.01047	-$0.01047	-$0.01047

General Power Rate - Part B (Schedule GSB) — Customers: 0

Effective October 1, 2011

Customer Charge: $1,500.00 per delivery point per month
TVA Administrative Charge: $350.00 per delivery point per month

	Summer	Winter	Transition
On-peak per kW of billing demand charges per month:	$16.89	$9.79	$0.00
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$4.45	$4.45	$4.45

Electric Division Rate Class (cont.)	**Base Charge**			**Customers**
General Power Rate - Part B (Schedule GSB) (cont.)				
	Summer	Winter	Transition	
Excess per kW charge per month by which billing demand exceeds contract demand:	$16.89	$9.79	$4.45	
On-peak per kWh energy charge:	$0.07387	$0.04321	$0.00000	
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.03919	$0.03919	$0.03919	
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.02053	$0.02053	$0.02053	
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.00469	$0.00469	$0.00469	
General Power Rate - Part C (Schedule GSC)				1
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
On-peak per kW of billing demand charges per month:	$16.36	$9.26	$0.00	
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$3.92	$3.92	$3.92	
Excess per kW charge per month by which billing demand exceeds contract demand:	$16.36	$9.26	$3.92	
On-peak per kWh energy charge:	$0.07027	$0.04036	$0.00000	
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.03657	$0.03657	$0.03657	
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.01789	$0.01789	$0.01789	
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.00205	$0.00205	$0.00205	

Electric Division Rate Class (cont.)	Base Charge			Customers
General Power Rate - Part D (Schedule GSD)				0
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
On-peak per kW of billing demand charges per month:	$16.11	$9.01	$0.00	
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$3.67	$3.67	$3.67	
Excess per kW charge per month by which billing demand exceeds contract demand:	$16.11	$9.01	$3.67	
On-peak per kWh energy charge:	$0.06783	$0.03705	$0.00000	
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.03307	$0.03307	$0.03307	
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.01441	$0.01441	$0.01441	
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	-$0.00144	-$0.00144	-$0.00144	
Manufacturing Power Rate - Part B (Schedule MSB)				3
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
On-peak per kW of billing demand charges per month:	$16.78	$9.68	$0.00	
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$4.34	$4.34	$4.34	
Excess per kW charge per month by which billing demand exceeds contract demand:	$16.78	$9.68	$4.34	

Electric Division Rate Class (cont.)	Base Charge			Customers
Manufacturing Power Rate - Part B (Schedule MSB) (cont.)				3
	Summer	Winter	Transition	
On-peak per kWh energy charge:	$0.05833	$0.02830	$0.00000	
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.02403	$0.02403	$0.02403	
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.00537	$0.00537	$0.00537	
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	-$0.01047	-$0.01047	-$0.01047	
Manufacturing Power Rate - Part C (Schedule MSC)	Effective October 1, 2011			0
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
On-peak per kW of billing demand charges per month:	$16.25	$9.15	$0.00	
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$3.81	$3.81	$3.81	
Excess per kW charge per month by which billing demand exceeds contract demand:	$16.25	$9.15	$3.81	
On-peak per kWh energy charge:	$0.05916	$0.02844	$0.00000	
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.02390	$0.02390	$0.02390	
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.00524	$0.00524	$0.00524	
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	-$0.01061	-$0.01061	-$0.01061	

Electric Division Rate Class (cont.)	Base Charge	Customers

Manufacturing Power Rate - Part D (Schedule MSD) — Customers: 1

Effective October 1, 2011

Customer Charge: $1,500.00 per delivery point per month
TVA Administrative Charge: $350.00 per delivery point per month

	Summer	Winter	Transition
On-peak per kW of billing demand charges per month:	$15.99	$8.89	$0.00
Per kW charge per month for each kW, if any, by which offpeak billing demand exceeds onpeak billing demand:	$3.55	$3.55	$3.55
Excess per kW charge per month by which billing demand exceeds contract demand:	$15.99	$8.89	$3.55
On-peak per kWh energy charge:	$0.05686	$0.02599	$0.00000
First 425 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.02164	$0.02164	$0.02164
Next 195 hours use of maximum metered demand multiplied by the ratio of offpeak energy to total energy rate per kWh:	$0.00298	$0.00298	$0.00298
Hours use of maximum metered demand in excess of 620 hours multiplied by the ratio of offpeak energy to total energy rate per kWh:	-$0.01286	-$0.01286	-$0.01286

Seasonal Demand And Energy Power Rate - Part B (Schedule SGSB) — Customers: 8

Effective October 1, 2011

Customer Charge: $1,500.00 per delivery point per month
TVA Administrative Charge: $350.00 per delivery point per month

	Summer	Winter	Transition
Per kW billing demand charge per month:	$22.08	$15.76	$11.00
Excess per kW charge per month by which billing demand exceeds contract demand:	$22.08	$15.76	$11.00
Energy charge per kWh:	$0.02676	$0.02265	$0.02175

Electric Division Rate Class (cont.)	Base Charge			Customers
Seasonal Demand And Energy Power Rate - Part C (Schedule SGSC)				0
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
Per kW billing demand charge per month:	$21.55	$15.23	$10.47	
Excess per kW charge per month by which billing demand exceeds contract demand:	$21.55	$15.23	$10.47	
Energy charge per kWh:	$0.02689	$0.02269	$0.02182	
Seasonal Demand And Energy Power Rate - Part D (Schedule SGSD)				0
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
Per kW billing demand charge per month:	$24.87	$18.53	$13.79	
Excess per kW charge per month by which billing demand exceeds contract demand:	$24.87	$18.53	$13.79	
Energy charge per kWh:	$0.01890	$0.01524	$0.01444	
Manufacturing Seasonal Demand And Energy Power Rate - Part B (Schedule SMSB)				11
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
Per kW billing demand charge per month:	$19.08	$12.75	$7.99	
Excess per kW charge per month by which billing demand exceeds contract demand:	$19.08	$12.75	$7.99	
Energy charge per kWh:	$0.01873	$0.01408	$0.01300	

Electric Division Rate Class (cont.)	Base Charge			Customers
Manufacturing Seasonal Demand And Energy Power Rate - Part C (Schedule SMSC)				2
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
Per kW billing demand charge per month:	$18.55	$12.22	$7.46	
Excess per kW charge per month by which billing demand exceeds contract demand:	$18.55	$12.22	$7.46	
Energy charge per kWh:	$0.01843	$0.01407	$0.01302	
Manufacturing Seasonal Demand And Energy Power Rate - Part D (Schedule SMSD)				2
	Effective October 1, 2011			
Customer Charge:	$1,500.00 per delivery point per month			
TVA Administrative Charge:	$350.00 per delivery point per month			
	Summer	Winter	Transition	
Per kW billing demand charge per month:	$21.18	$14.86	$10.10	
Excess per kW charge per month by which billing demand exceeds contract demand:	$21.18	$14.86	$10.10	
Energy charge per kWh:	$0.01068	$0.00720	$0.00637	
Drainage Pumping Station Rate (Schedule DPS)				13
	Effective September 30, 2011			
Customer Charge:	$15.52 per delivery point per month			
Energy Charge:	Summer	Winter	Transition	
All kWh per month:	$0.03175	$0.03164	$0.03098	
Outdoor Lighting Rate (Schedule LS)				16,924
	Effective September 30, 2011			
	Part A - Charges for street and park lighting systems, traffic signal systems and athletic field lighting installations.			
Energy Charge:	Summer	Winter	Transition	
All kWh per month:	$0.04222	$0.04211	$0.04145	

Electric Division Rate Class (cont.)	Base Charge	Customers

Outdoor Lighting Rate (Schedule LS) (cont.)

Outdoor Lighting Facilities Charge:	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. 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. 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	

Electric Division Rate Class (cont.)	Base Charge	Customers

Outdoor Lighting Rate (Schedule LS) (cont.)

of any such system or installation and shall require payment by the customer of 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 shall 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 paragraphs.

Part B - Charges for outdoor lighting for individual customers - charges per fixture per month:

(a) Type of fixture	Lamp Size		Rated	
	(Watts)	(Lumens)	(kWh)	Charge
Mercury Vapor or Incandescent	175	7,650	70	$2.95
	250	10,400	98	3.49
	400	19,100	155	4.42
	700	33,600	266	5.96
	1,000	47,500	378	7.59
Metal Halide	175	8,300	70	$2.95
	250	14,000	98	3.49
	400	22,600	155	4.42
	1,000	88,000	378	7.59
High Pressure Sodium	50	3,285	22	$4.19
	100	8,550	42	4.48
	150	14,400	63	4.61
	200	18,900	82	5.01
	250	23,000	105	5.30
	400	45,000	165	6.29
	1,000	126,000	385	10.05

(b) Energy Charge: For each lamp size under (a) above per rated kWh per month:

	Summer	Winter	Transition
All rated kWh per month:	$0.04222	$0.04211	$0.04145

Gas Division Rate Class	Base Charge	Customers
Residential G-1 & G-3	Effective meters read on or after December 26, 2007	288,985
	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.	
Service charge:	$10.00 per month, plus	
Commodity charge:	First 100 ccf per month @ $1.081 per ccf	
	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.	
Minimum bill:	$10.00 per meter per month	
Small General Service G-7	Effective meters read on or after December 26, 2007 This rate schedule is available for gas service to all gas customers except residential.	21,844
Service charge:	For 0 to 250 ccf meter, $25.00 Over 250 to 1,000 ccf meter, $50.00 Over 1,000 ccf meter, $100.00 per month, plus	
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.	

Gas Division Rate Class (cont.)	Base Charge	Customers
Large General Service Firm on-peak G-8 and G-9	Effective meters on or after December 26, 2007	453
	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 per 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	23
	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.	
Service charge:	$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	
	The above rates are subject to adjustment under the provisions of the Purchased Gas Adjustment Rider.	
Minimum bill:	The minimum monthly bill shall be $0.350 for each Ccf 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	Base Charge	Customers
Residential – Inside City Rate	Effective meters read on or after January 3, 2011 For water furnished to premises entirely within the corporate limits of the City of Memphis	184,243
Commodity charge:	All water consumed: $1.376 per Ccf per month	
Minimum bill:	The minimum monthly bill shall be determined by the size the meter installed, as follows: 5/8" meter $ 5.82 3/4" meter 8.39 1" meter 14.89 1-1/2" meter 33.51 2" meter 59.56	
Residential – Outside City Rate	Effective meters read on or after January 3, 2011 For water furnished to premises outside the corporate limits of the City of Memphis	22,596
Commodity charge:	All water consumed: $2.142 per Ccf per month	
Minimum bill:	The minimum monthly bill shall be determined by the size the meter installed, as follows: 5/8" meter $ 8.10 3/4" meter 11.64 1" meter 20.73 1-1/2" meter 46.61 2" meter 82.86	
General Service – Inside City Rate	Effective meters read on or after January 3, 2011 For water service to all customers within the corporate limits of the City of Memphis, except residential customers	18,735
Commodity charge:	Water consumed per month: First 30 Ccf $1.754 per Ccf Next 70 Ccf $1.491 per Ccf Next 100 Ccf $1.134 per Ccf	

Water Division Rate Class (cont.)	Base Charge		Customers
General Service – Inside City Rate (cont.)			
Commodity charge (cont.):	Water consumed per month:		
	Next 400 Ccf	$0.945 per Ccf	
	Next 5,400 Ccf	$0.735 per Ccf	
	Excess over 6,000 Ccf	$0.767 per Ccf	
Minimum bill:	The minimum monthly bill shall be determined by the size of the meter installed, as follow:		
	5/8" meter	$ 11.15	
	3/4" meter	12.99	
	1" meter	22.27	
	1-1/2" meter	44.56	
	2" meter	92.87	
	3" meter	185.68	
	4" meter	277.67	
	6" meter	351.26	
	8" meter	424.86	
	10" meter	880.09	
	12" meter	1,228.02	
	14" meter	1,688.54	
	Battery of 2-2" meters	185.68	
	Battery of 3-2" meters	277.67	
General Service – Outside City Rate	Effective meters read on or after January 3, 2011 For water service to all customers outside the corporate limits of the City of Memphis, except residential customers		808
Commodity charge:	Water consumed per month:		
	First 30 Ccf	$2.636 per Ccf	
	Next 70 Ccf	$2.216 per Ccf	
	Next 100 Ccf	$1.691 per Ccf	
	Next 400 Ccf	$1.418 per Ccf	
	Next 5,400 Ccf	$1.113 per Ccf	
	Excess over 6,000 Ccf	$1.155 per Ccf	

Water Division Rate Class (cont.)	Base Charge		Customers
General Service – Outside City Rate (cont.)			
Minimum bill:	The minimum monthly bill shall be determined by the size the meter installed, as follows:		
	5/8" meter	$ 17.03	
	3/4" meter	19.88	
	1" meter	34.07	
	1-1/2" meter	68.12	
	2" meter	141.94	
	3" meter	283.91	
	4" meter	424.29	
	6" meter	536.76	
	8" meter	649.22	
	10" meter	1,344.86	
	12" meter	1,876.53	
	14" meter	2,578.47	
	Battery of 2-2" meters	283.91	
	Battery of 3-2" meters	424.29	
Residential – Shelby County Water Distribution System	Effective meters read on or after January 3, 2011		20,764
	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 $2.142 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	$ 8.10	
	3/4" meter	11.64	
	1" meter	20.73	
	1-1/2" meter	46.61	
	2" meter	82.86	
	Residential customers shall be served through a single meter not larger than 2" in size.		

Water Division Rate Class (cont.)	Base Charge	Customers
Commercial - Industrial – Shelby County Water Distribution System	Effective meters read on or after June 26, 2008 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 all customers except residential customers using service exclusive for domestic use.	604
Monthly rate:	Water consumed per month:	

First 30 Ccf	$2.636 per Ccf
Next 70 Ccf	$2.216 per Ccf
Next 100 Ccf	$1.691 per Ccf
Next 400 Ccf	$1.418 per Ccf
Next 5,400 Ccf	$1.113 per Ccf
Excess over 6000 Ccf	$1.155 per Ccf

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

5/8" meter	$ 17.03
3/4" meter	19.88
1" meter	34.07
1-1/2" meter	68.12
2" meter	141.94
3" meter	283.91
4" meter	424.29
6" meter	536.76
8" meter	649.22
10" meter	1,344.86
12" meter	1,876.53
14" meter	2,578.47

MLGW

A	**Water Treated and Purchased:**		
B	Water Pumped (potable)	51,758,925,801	
C	Water Purchased	-	
D	**Total Water Treated and Purchased (Sum Lines B and C)**		51,758,925,801
E	**Accounted for Water:**		
F	Water Sold *	41,937,519,412	
G	Metered for Consumption (in house usage)	424,650,000	
H	Fire Department Usage	22,500,000	
I	Flushing	50,370,427	
J	Tank Cleaning/Filling	6,230,114	
K	Street Cleaning	388,720	
L	Bulk Sales	-	
M	Water Bill Adjustments	-	
N	**Total Accounted for Water (Sum Lines F thru M)**		42,441,658,672
O	**Unaccounted for Water (Lines D minus Line N)**		9,317,267,129
P	**Percent Unaccounted for Water (Lines O divided by Line D times 100)**		18.0%
Q	**Other (explain)**	See Below	

Explained Other:

* Water Sold includes free water for City of Memphis.

All amounts included in this schedule are supported by documentation on file at the water system.
If no support is on file for a line item or if the line item is not applicable, a "-" is shown.

(Dollars in Thousands)

		ACCRUAL YIELD	MATURITY DATE	FAIR VALUE
COMMERCIAL PAPER				
	Chevron Corp	0.050	01/03/2012	$ 11,799
	General Electric Capital Corp	0.030	01/03/2012	5,999
	General Electric Capital Corp	0.030	01/03/2012	3,299
	KFW	0.070	01/03/2012	3,199
	KFW	0.070	01/03/2012	6,500
	KFW	0.070	01/03/2012	8,000
	Toyota Motor Credit	0.050	01/03/2012	5,000
	Chevron Corp	0.030	01/06/2012	4,500
	General Electric Capital Corp	0.030	01/17/2012	2,000
	Nestle Finance International	0.040	01/17/2012	3,300
	Toyota Motor Credit	0.070	01/17/2012	3,000
	Bank of Nova Scotia	0.040	01/20/2012	7,200
	Rabo Bank USA	0.070	01/20/2012	1,100
	Toyota Motor Credit	0.050	01/20/2012	1,200
	Toyota Motor Credit	0.040	01/20/2012	6,700
	Nestle Capital Corp	0.030	01/23/2012	8,500
	Bank of Nova Scotia	0.050	01/25/2012	8,000
	General Electric Capital Corp	0.020	01/25/2012	2,500
	General Electric Capital Corp	0.020	01/25/2012	4,260
				$ 96,056
	Fair Market Value			(10)
	Total Commercial Paper			$ 96,046

(Dollars in Thousands)

	ACCRUAL YIELD	MATURITY DATE	FAIR VALUE
MONEY MARKET MUTUAL FUNDS			
Northern Institutional Government Select Funds			$ 98,308
Federated Treas Obligations FD 398			14,693
Total Money Market Mutual Funds			$ 113,001
CASH			
Bank Deposits			$ 17,305
Total Cash			$ 17,305
ACCRUED INTEREST			$ 546
TOTAL CASH AND CASH EQUIVALENTS			$ 226,898
U.S. TREASURIES:			
TREASURY NOTE			
	(0.079)	5/31/2012	$ 501
Fair Market Value			1
Subtotal Treasury Note			$ 502

(Dollars in Thousands)

	ACCRUAL YIELD	MATURITY DATE	FAIR VALUE
U. S. GOVERNMENT BONDS			
	0.125	09/30/2013	$ 3,992
	0.250	12/15/2014	1,993
	0.625	02/28/2013	2,010
	3.375	11/30/2012	541
	2.375	08/31/2014	8,428
	1.750	07/31/2015	4,446
	0.625	07/31/2012	3,511
	0.625	12/31/2012	4,270
	0.500	11/30/2012	1,354
	0.375	06/30/2013	5,012
	1.000	04/30/2012	1,003
	2.375	02/28/2015	3,586
	2.500	04/30/2015	1,414
	4.625	07/31/2012	410
	1.250	08/31/2015	5,133
	3.375	07/31/2013	184
	3.125	04/30/2013	779
	0.250	10/31/2013	20,003
	0.375	07/31/2013	2,005
	2.500	03/31/2015	2,133
	2.250	01/31/2015	3,169
	1.500	06/30/2016	1,034
	2.375	09/30/2014	3,165
Subtotal U.S. Government Bonds			$ 79,575
Total U.S. Treasuries			$ 80,077

(Dollars in Thousands)

MLGW

		ACCRUAL YIELD	MATURITY DATE	FAIR VALUE
U. S. GOVERNMENT AGENCIES				
		0.380	10/07/2014	$ 2,998
		5.000	09/14/2012	268
		1.375	05/28/2014	5,099
		2.125	03/23/2012	3,013
		5.125	07/15/2012	2,567
		5.500	08/20/2012	2,067
		1.750	06/15/2012	1,007
		6.410	11/13/2012	1,052
		6.125	03/15/2012	1,518
		4.750	11/19/2012	2,079
		1.125	07/30/2012	2,011
		3.550	04/15/2013	780
		1.900	10/19/2012	1,014
	U.S. Government Agencies			$ 25,473
MUNICIPAL OBLIGATIONS				
	Baltimore MD	1.600	10/15/2014	100
	Connecticut ST	1.430	05/15/2014	1,011
	New York NY City	2.050	05/01/2013	107
	Total Muncipal Obligations			$ 1,218

(Dollars in Thousands)

		ACCRUAL YIELD	MATURITY DATE	FAIR VALUE
CORPORATE BONDS:				
CORPORATE BONDS				
	Westpac Bkg Corp	2.250	11/19/2012	$ 505
	Bank Montreal	2.125	06/28/2013	1,016
	Bank N S Halifax	2.250	01/22/2013	507
	PVTPL Bk Montreal	1.300	10/31/2014	749
	Shell Intl Fin BV	1.875	03/25/2013	509
	Berkshire Hathaway Fin Corp	0.523	01/13/2012	1,000
	Gen Elec Cap Corp	0.693	03/20/2014	1,398
	Gen Elec Cap Corp	2.800	01/08/2013	510
	Gen Elec Cap Corp	4.800	05/01/2013	1,361
	Google Inc	1.250	05/19/2014	507
	Johnson & Johnson	1.200	05/15/2014	1,015
	Mellon Fdg Corp	0.607	05/15/2014	989
	Met Life Global Fdg	2.875	09/17/2012	507
	Walmart Stores	0.750	10/25/2013	1,507
	3M Co Medium Term	4.650	12/15/2012	520
	Subtotal Corporate Bonds			$ 12,600
GUARANTEED FIXED INCOME				
	GMAC Inc FDIC	1.750	10/30/2012	$ 1,013
	Subtotal Guaranteed Fixed Income			$ 1,013
	Total Corporate Bonds:			$ 13,613

(Dollars in Thousands)

		ACCRUAL YIELD	MATURITY DATE	FAIR VALUE
ASSET BACKED SECURITIES				
	Ally Auto	1.110	10/15/2014	$ 2,507
	BMW Veh Lease	0.820	04/15/2013	999
	CAP 1 Multi-Asset	4.700	06/15/2015	2,765
	Carmax Auto Owner	1.410	02/16/2015	910
	Chase Issuance Tr	1.828	04/15/2014	1,004
	Chrysler Finl Auto	0.910	08/08/2013	2,001
	Citibank Cr Card	2.250	12/23/2014	2,030
	Ford Cr Auto Owner	1.050	10/15/2014	999
	Ford Cr Floor Plan Master	1.828	09/15/2014	1,008
	Ford Cr Floor Plan	1.500	09/15/2015	1,002
	GE Dealer Floor Plan Master	0.885	07/20/2016	2,497
	Harley-Davidson	0.710	05/15/2015	999
	Harley-Davidson	2.620	03/15/2014	119
	Honda Auto	0.700	04/21/2014	2,500
	Hyundai Auto	2.030	08/15/2013	401
	Hyundai Auto	1.160	04/15/2015	1,003
	Hyundai Auto	1.500	10/15/2014	933
	John Deere Owner	2.590	10/15/2013	48
	Nissan Auto Lease	1.120	12/15/2013	2,005
	PVTPL Mercedes Benz Auto	1.180	11/15/2013	1,003
	Toyota Auto	1.040	02/18/2014	892
	Volkswagen Auto	0.990	11/20/2013	2,504
	Total Asset Backed Securities			$ 30,129
TOTAL INVESTMENTS				$ 150,510
TOTAL CASH AND INVESTMENTS				**$ 377,408**

Type of Coverage	Amount of Coverage
Property	$ 600,000
Crime	2,500
Travel Accident	1,000

SCHEDULE OF ADDITIONS AND RETIREMENTS TO UTILITY PLANT
DECEMBER 31, 2011
(Dollars in Thousands)

	Electric Division	Gas Division	Water Division
Utility plant in service, December 31, 2010	$ 1,418,105	$ 540,703	$ 428,619
Additions - Construction	55,249	22,706	8,071
Additions - Acquisition Adjustment			964
Retirements	(12,148)	(3,753)	(1,566)
Utility plant in service, December 31, 2011	**$ 1,461,206**	**$ 559,656**	**$ 436,088**

Note: Utility plant in service balances exclude amounts for construction work in process, non-utility property and land held for future use.

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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, 2011 and have issued our report thereon dated May 17, 2012. We conducted our audits in accordance with U.S. generally accepted auditing standards 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 audits, we considered the Divisions' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing opinions on the effectiveness of the Divisions' internal control over financial reporting. Accordingly, we do not express opinions on the effectiveness of the Divisions' internal control over financial reporting.

A deficiency in internal control 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 and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Divisions' financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs, that we consider to be significant deficiencies in internal control over financial reporting. We consider deficiencies 2011-1, 2011-2 and 2011-3 to be significant deficiencies. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Divisions' financial statements are free of material misstatements, we performed tests of the Divisions' 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 opinions on compliance with those provisions was not an objective of our audits, and accordingly, we do not express such opinions. 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 17, 2012.

The Divisions' responses to the findings identified in our audits are described in the accompanying schedule of findings and questioned costs. We did not audit the Divisions' responses and, accordingly, we express no opinion on them.

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.

Mayer Hoffman McCann P.C.

Memphis, Tennessee
May 17, 2012

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Independent Auditor's Report on Compliance with Requirements That Could Have a Direct and Material Effect on 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 could have a direct and material effect on each of the Divisions' major federal programs for the year ended December 31, 2011. The Divisions' major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Divisions' management. Our responsibility is to express an opinion on the Divisions' compliance based on our audits.

We conducted our audits of compliance in accordance with U.S. generally accepted auditing standards; 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 audits to obtain reasonable assurance about whether noncompliance occurred under the types of compliance requirements referred to above that could have a direct and material effect on a major federal program. An audit includes examining, on a test basis, evidence about the Divisions' compliance with those requirements and performing such other procedures as we consider necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions. Our audits do not provide a legal determination on the Divisions' compliance with those requirements.

In our opinion, the Divisions complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2011.

Internal Control Over Compliance

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 audits, we considered the Divisions' internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine the auditing procedures for the purpose of expressing our opinions on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing opinions on the effectiveness of internal control over compliance. Accordingly, we do not express opinions on the effectiveness of the Divisions' internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. We did not identify any deficiencies in internal control over compliance that we consider to 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.

Mayer Hoffman McCann P.C.

Memphis, Tennessee
May 17, 2012

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2011
(Dollars in Thousands)

Federal Grantor/Pass-Through Grantor Federal Awards	CFDA Number	Contract Number	Beginning (Accrued) Deferred	Cash Receipts	Expenditures	Ending (Accrued) Deferred
U.S. Department of Homeland Security/ Tennessee Emergency Management	97.036	34101-0000008735	$ -	$ -	$ 2,467	$ (2,467)
U.S. Department of Homeland Security/ Tennessee Emergency Management	97.036	34101-0000009241	-	-	2,357	(2,357)
U.S. Department of Homeland Security/ Tennessee Emergency Management	97.036	34101-0000009498	-	-	1,959	(1,959)
U.S. Department of Homeland Security/ Tennessee Emergency Management	97.036	34101-0000005751	(519)	383	-	(136)
U.S. Department of Homeland Security/ Tennessee Emergency Management	97.036	34101-0000001983	(1,479)	919	-	(560)
Total Program 97.036			(1,998)	1,302	6,783	(7,479)
U.S. Department of Homeland Security/ Tennessee Emergency Management	97.047	Edison #E-18001	(388)	568	240	(60)
U.S. Department of Homeland Security/ Tennessee Emergency Management	97.047	E-29504	-	-	-	-
Total Program 97.047			(388)	568	240	(60)
ARRA - U.S. Department of Energy/ Smart Grid Investment Grant	81.122	DE-OE0000281	(177)	753	841	(265)
Total Program 81.122			(177)	753	841	(265)
Total Federal Awards			**$ (2,563)**	**$ 2,623**	**$ 7,864**	**$ (7,804)**

BASIS OF PRESENTATION

The accompanying 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, a division of the City of Memphis, Tennessee, for the year ended December 31, 2011. 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.* Each of the divisions of Memphis Light, Gas and Water Division generally follows the Federal Energy Regulatory Commission's Uniform System of Accounts prescribed for Public Utilities.

FEDERAL GRANT CONTRIBUTIONS

As recipients of federal grant contributions, the Divisions are subject to examination by various federal and state authorities and the results of such examinations could result in changes to the reported grant contributions. During early 2012, the Office of Inspector General (OIG) began an examination of certain Federal Emergency Management Agency (FEMA) grants received in 2008 and 2009. The examination is still in process and the Divisions have not received the final results of such examination. During the examination process, the OIG indicated that they plan to question certain costs that were incurred without competitive bids. The Divisions believe that the competitive bidding process was not feasible for these costs because of the public exigency or emergency nature of these expenditures. Resolution of this matter may not be known for several months. If the Divisions receive an unfavorable determination from FEMA concerning such 2008 and 2009 costs, the grant contributions reported for 2008 and 2009 could be reduced with a portion refunded to FEMA and the grant contributions reported in 2010 and 2011 could also be adversely effected. Management believes that reductions in the 2008 and 2009 grants, if any, will not be material to the Divisions' financial statements.

MEMPHIS LIGHT, GAS AND WATER DIVISION

Schedule of Findings and Questioned Costs
For the Year Ended December 31, 2011

A. Summary of Audit Results

1. The auditor's report expresses unqualified opinions on the financial statements of the Electric, Gas, and Water Divisions (the "Divisions") of Memphis Light, Gas and Water Division.

2. Three significant deficiencies relating to the audits of the financial statements are reported in the 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.*

3. No instances of noncompliance material to the financial statements of the Divisions, which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audits.

4. No deficiencies relating to the audits of the major federal award programs are reported in the Independent Auditor's Report on Compliance with Requirements That Could Have a Direct and Material Effect to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133.

5. The auditor's report on compliance for the major federal award programs for the Divisions expresses unqualified opinions on all major federal programs.

6. There were no audit findings related to major programs that were required to be reported under OMB Circular A-133.

7. The programs tested as major programs included:

81.122	ARRA - Electricity Delivery and Energy Reliability, Research, Development and Analysis
97.036	Disaster Grants - Public Assistance (Presidentially Declared Disasters)

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

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

B. Financial Statement Findings Section

Significant Deficiencies

2011 -1 Unbilled revenue

Condition: The Electric Division calculated unbilled revenue amount did not agree with the general ledger as of December 31, 2011. In the Gas Division, the calculated unbilled revenue was net of the PGA amount due to customers for differences in gas prices.

Criteria: The normal review procedures for Electric division unbilled revenue were not followed.

Effect: Management posted an adjustment to Electric division unbilled revenue to adjust the general ledger. An entry was recorded in the Gas division to properly state assets and liabilities

Recommendation: We recommend that all unbilled revenue accounts be reviewed for reasonableness after all calculations and adjustments are made to ensure that they are properly stated in the financial statements.

Response: *Management has identified additional testing for validation purposes. This testing will be implemented by June 2012.*

2011 -2 Injuries and damages reserve

Condition: The IDI reserve was not adjusted as of December 31 to include all outstanding claims. MLGW was provided an incorrect report from its third-party administrator for injury and disability claims. The report received only displayed the estimated liability for claims with current month activity, as opposed to all claims.

Criteria: Obtaining complete and accurate information is essential in preparing financial statements.

Effect: Because management did not ensure the report used to record the reserve was complete, the reserve balances and the related restricted funds were understated.

B. Financial Statement Findings Section (continued)

Significant Deficiencies (continued)

2011 -2 Injuries and damages reserve (continued)

Recommendation: We recommend that management coordinate with service providers to obtain complete and appropriate information to record account activity.

Response: *Management will verify with service providers that reports are complete and accurate.*

2011 -3 Cashiering process

Condition: MLGW's bank reconciliations contain certain reconciling items related to cashier keying or recording errors that have been carried as reconciling items for over six months.

Criteria: Unidentified payments and reconciling items should be investigated and posted timely to ensure accuracy and timeliness of bank reconciliations.

Effect: These keying errors caused large credit balances relative to the customer's account balance, which would be inappropriately refunded to customers in the event of termination of service.

Recommendation: We recommend modifications be implemented to the cash reconciliation process to more easily identify and correct errors on a timely basis.

Response: *Additional resources will be applied to reconcile items in a more timely manner. This should also accelerate the bank reconciliation process.*

C. Major Federal Awards Findings and Questioned Cost Section

None.

MEMPHIS LIGHT, GAS AND WATER DIVISION

Schedule of Prior Year Audit Findings
December 31, 2011

Prior Year Findings

2010-3 *CFDA 81.122 ARRA Electricity Delivery and Energy Reliability, Research, Development and Analysis*
Department of Energy
Grant Award: DE-OE0000281

Condition: Form SF-425 was not submitted quarterly as required by the granting agency.

Current status: Implemented. All required reports were submitted in accordance with the grant requirements.

MLGW