

Just a flick  
of a switch...



2010 Annual Report  
Memphis Light, Gas and Water Division

...Instantly transports our customers from darkness, to a vibrant, new world where everyday tasks of yesteryear become infinitely easier. Effortless, instant access to energy frees their time to fashion a brilliant collage of their lives - composed of work, a little play and a measure of making our community a better place.



## About MLGW

Memphis Light, Gas and Water Division is the nation's largest three-service municipal utility. Since 1939, MLGW has met the needs of Memphis and Shelby County residents by delivering reliable and affordable electric, natural gas and water services. Electricity is supplied to MLGW by the Tennessee Valley Authority (TVA), while natural gas is purchased from a variety of suppliers and transported by three pipeline companies, Texas Gas Transmission Corporation, Trunkline Gas Company and ANR Pipeline Company. Memphis receives its water from one of the largest artesian water systems in the world. MLGW is led by a President and a five-member Board of Commissioners who are appointed by the Mayor of Memphis and approved by the Memphis City Council.





# Letter from the President

*MLGW President and CEO Jerry R. Collins Jr.*

As I reflect on 2010, I recall several milestones that indicate we're moving in a positive direction. From the very beginning of the New Year, we were greeted with extreme weather that tested our system's reliability, tried our patience and put many of our customers at risk from frigid temperatures. But out of this experience came good as we witnessed the resilience of our utility system and felt the spirit of compassion take over in an outpouring of giving to those in need.

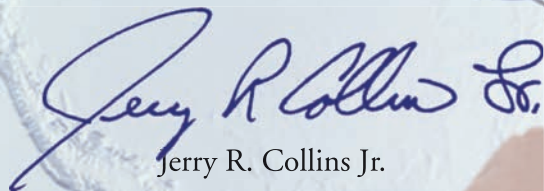
Then we had the fortunate opportunity to save a significant amount of money for the Division through the refinancing of our Electric Division prepay bonds. On the heels of this event, Fitch upgraded our electric system revenue bonds twice within the year, elevating the bonds to the highest AAA status.

We had the exciting opportunity to be at the forefront of technological innovation by launching the Smart Grid Demonstration project followed by the installation of Smart Meters in the homes of volunteers.

Last, but not least, we saw some upward movement in the J.D. Power and Associates' Residential Electric Survey as our score rose 36 points, earning us the distinction of being among the top 10 most improved utilities in the survey.

These occurrences would not have happened if we weren't moving on the right course. I am proud of the hard work of every employee for helping to make this happen. I encourage everyone to keep up the momentum as I am confident that we face even greater achievements ahead. I am delighted by all that we achieved in 2010 and I look forward to what the future holds in 2011.

Sincerely,



Jerry R. Collins Jr.



# Table of Contents

President's Letter .....	1
MLGW Leadership .....	3
Just a Flick of a Switch .....	4
Letter of Transmittal.....	L-1

## **FINANCIAL SECTION**

Independent Auditor's Report .....	A-1
Management's Discussion and Analysis .....	M-1

## **FINANCIAL STATEMENTS**

Balance Sheets .....	F-1
Statements of Revenues, Expenses and Changes in Net Assets .....	F-3
Statements of Cash Flows .....	F-4
Notes to Financial Statements .....	N-1
Supplementary Information .....	S-1
Independent Auditor's 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 .....	Z-1
Independent Auditor's Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 .....	Z-3
Schedule of Expenditures of Federal Awards .....	Z-5
Schedule of Findings and Questioned Costs .....	Z-6

## MLGW Board of Commissioners

### **Darrell T. Cobbins, Chair**

Mr. Cobbins established Universal Commercial Real Estate, LLC in 2007, as Memphis' first black-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. He currently chairs MLGW's Pension Board.

### **Dedrick Brittenum Jr., Vice Chair**

Mr. Brittenum Jr. 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 owner of V. Lynn Evans, CPA, a certified public accounting and consulting firm. 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**

Mr. 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 for six years and as the Executive Director of the Shelby Farms Park Conservancy. He is a Board member of Triumph Bank and chairs the MLGW Human Resources committee.

### **Steven Wishnia**

As president and managing director of Highland Capital Management Corporation, Mr. Wishnia directs the company's management of 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

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

**Nicholas Newman**  
Vice President of Construction and Maintenance

**Cheryl W. Patterson**  
Vice President and General Counsel

**Linda K. Peppers**  
Vice President and Chief Technology Officer

**Alonzo Weaver III**  
Vice President of Engineering and Operations

**Gale Jones Carson**  
Director of Corporate Communications

**Clifford M. DeBerry**  
Director of Analysis, Strategy and Performance

**Dana Jeanes**  
Controller

**Lesia J. Walton**  
Director of Internal Audit

**Anderson D. Williams**  
Executive Analyst



## Our actions revolve around our customers...

As MLGW customers ourselves, and neighbors to fellow residents who use our services, we want to keep the utilities running smoothly to minimize any potential inconvenience or hardship. Our customers expect and deserve nothing less than safe, affordable and reliable power from friendly, helpful utility employees.

The J.D. Power & Associates 2010 Electric Utility Residential Customer Satisfaction Study ranked MLGW among the top 10 most improved scores from 2009. The survey measures customer satisfaction by examining six key factors: power quality and reliability; price; billing and payment; corporate citizenship; communications and customer service.

MLGW's efforts have also aided in moving the bar further up the gauge in J.D. Power and Associates' residential gas survey. The results, released on September 22, showed that MLGW scored 589, up 56 points from the 2009 score of 533. Of the 75 utilities included in the survey, MLGW showed the strongest improvement and was ranked among the top utilities in corporate citizenship awareness.

In 2010, MLGW was identified as one of the Top 10 Utilities in Economic Development in the nation, according to Site Selection magazine. MLGW also made their Top 10 list in 2000 and 2001. Site Selection's designation was based on a utility's 2009 performance in capital investment and job creation.

## Customer-centered Focus

Like the air we breathe, MLGW's utility services are essential to sustaining modern life to residents within our operational sector of the globe. When our customers are cold, hungry or thirsty, they want the assurance that their natural gas, electricity and water services are available to meet their needs.



# Distinctive Service in our sphere of operation

The power behind these extraordinary achievements is Memphis Light, Gas and Water's (MLGW) 2,700-person workforce. Like the people we serve, MLGW is continuously moving...steadily working to improve the quality of life for utility customers in our sphere of operation. The numerous outreach



efforts we undertook in 2010 showcased our commitment to community service.

MLGW had the opportunity to prove its loyalty last January when prolonged, frigid temperatures sparked an urgent need to sustain heat in the homes of its customers. MLGW answered the call, engaging in a historic collaboration with the city of Memphis and Shelby County in a reconnect initiative that restored utilities to hundreds of customers' homes.

The brutal winter's effect on the community inspired MLGW to partner with the Metropolitan Inter-faith Association (MIFA) to donate space heaters to customers in need. MLGW's annual winter moratorium provided yet another barrier to the cold for registered seniors and disabled customers who were spared from having services disconnected from December through February regardless of their utility account status.

The weather proved as challenging in the summer as it had been in the winter. When summer heat reached dangerous levels, MLGW responded by relaxing certain reinstatement fees and lowering limits for participation in payment plans. As an added safety measure, MLGW field personnel knocked on doors and checked on customers to make sure they weren't suffering from heat-related illnesses. MLGW also partnered with the Metropolitan Inter-faith Association (MIFA) and Community Services Agency (CSA) last summer to distribute free box fans and window air conditioner units to Memphians during the stifling heat wave.





...and gravitate toward fulfilling our community's many needs.

MLGW's generosity extends to charitable causes as well. MLGW employees raised hundreds of thousands of dollars for United Way during MLGW's "emPowered to meet the need" employee campaign last fall. As a testament to MLGW's giving spirit, all of these donations were employee donations – no corporate funds were used.

A significant amount of money was also raised for the American Heart Association during its Annual Heart Walk campaign. Jerry Collins Jr., President and CEO of MLGW, served as Chair of the 2010 Mid-South Heart Walk.

In the months leading up to the citywide walk, MLGW organized its own monthly "Energize your Heart" walks at its various facilities to get in shape for the final walk and to get in the spirit and boost pledges for the campaign.

MLGW employees even created a new cause last year by launching the first annual "Kruisin' for Kids" motorcycle ride event to benefit Le Bonheur Children's Hospital.

In addition to providing critical services, MLGW employees generously donated blood in 2010 and catapulted MLGW to the position of Lifeblood's top corporate blood

donor.

MLGW employees also help foster education every year by assisting with local science and engineering fairs and art contests involving Memphis and Shelby County area students. Last year they judged more than 300 projects from 32 Shelby County Schools at the Shelby County Elementary STEMulating Science Fair.

Other organizations receiving MLGW employee donations and support included the following:

- Junior Achievement's annual "Bowling on the River" event
- MLGW/Special Olympics Sportsfest
- March of Dimes "March for Babies" walk
- The National Kidney Foundation's Annual Kidney Walk
- "Operation Feed" campaign for the Memphis Food Bank
- The American Diabetes Association's "Step Out Walk to Fight Diabetes" event
- The Salvation Army's 2010 Angel Tree Program
- The Salvation Army's 2010 Christmas Kettle Campaign.

It doesn't take a crisis for MLGW to try to make life easier for our customers. In 2010, dozens of MLGW employees selflessly volunteered to perform repair work at five of MLGW's Project Max home improvement events resulting in 18 wheelchair ramps being built, 21 homes being weatherized, 10 homes receiving plumbing work, and 350 energy kits being distributed. The Project Max initiative began 26 years ago to help the less fortunate in our community, including the elderly and disabled.



## Bolstering Power Reliability, Today and Tomorrow

When it comes to securing the electric infrastructure, MLGW leads the way. Situated near the New Madrid seismic zone, MLGW's infrastructure faces a uniquely critical risk that elevates the importance of seismic mitigation. For more than two decades, MLGW has taken protective measures to strengthen its utility structures and facilities against damage from seismic activity. Such ardent efforts have positioned MLGW as a leader in its industry in

earthquake preparedness. MLGW's electric system has undergone vital, earthquake-resistant measures including anchoring transformers and other critical substation equipment. High-voltage transformers were retrofitted thanks to a FEMA grant that MLGW received in 2008 resulting from its successful FEMA Hazard Mitigation Grant submission crafted with the help of Howe and Associates.

The system's reliability won the first round against brutally cold weather when a New Year's cold snap produced peak electric usage in the region, according to TVA. Undeterred, MLGW's electric system delivered. By January 29, another round of frigid temperatures

brought ice and sleet, resulting in downed power lines and poles, as well as limbs and trees. More than 35,000 customers lost power. After working vigorously around the clock, MLGW crews restored power to all customers within a couple of days.

The reliability of MLGW's electric system continued to be tested in 2010. On May 1, severe weather roared through the community in a series of storms, which produced major flooding and high winds, leaving thousands without power. Customer Care Service Advisors fielded calls late into the night, emergency dispatchers and trouble-shooters assessed damage and crews performed repairs around the clock.

MLGW's ability to restore power quickly and to enhance the system's reliability has been duly acknowledged by numerous groups. A North American Electric Reliability Corporation (NERC) audit of MLGW last year exceeded the federal regulators' expectations. In addition, Sharp Electronics Corporation awarded MLGW a plaque in 2010 in honor of its rigorous efforts to restore power to Sharp's manufacturing plants following a series of devastating thunderstorms in February 2008.



We stand as a strong and steady force, ever evolving through innovation,

- We reduced the number of customers experiencing more than three interruptions in a year from 20 percent in 2002 to less than 10 percent in 2010.
- We spent millions to replace faulty underground cable in the last year and to make system improvements that serve critical facilities.

Efforts are also being made to strengthen electric services to water pumping stations, water treatment facilities and other critical customers to minimize the resulting community hardship when these services are disrupted.

In areas of long electric circuits, MLGW has installed additional lines to reduce line exposure and the risk of outages. We have reduced the average number of outages customers experienced by more than 40 percent during the past 15 years.

## MLGW Begins Smart Grid Era

Last year, MLGW received a matching grant of \$5 million from the U.S. Department of Energy, resulting in a \$10 million project for digital Smart Grid upgrades to the electric network serving the medical center and downtown areas. A high-speed data communication and control system will be created that will enhance power quality in those

areas, reduce maintenance costs and serve as a platform for future electric-system enhancements.

With expectations of increasing power reliability and cost-effectiveness, MLGW joined the ranks of numerous utilities across the country in upgrading its communications, monitoring and metering systems with Smart Grid technology. The project was rolled out in phases beginning with 1,000 residential customer volunteers receiving digital electric smart meters as part of MLGW's three-year Smart Grid Demonstration initiative. These Smart Grid pioneers will test the effectiveness of smart meters and in-home energy monitoring devices in helping customers to strategically reduce their electricity consumption—resulting in a smaller bill every month. Following this phase, several new features were added to MLGW's My Account Web service, allowing Smart Grid participants to view time-stamped electricity usage data. Smart Grid technology also offers increased power reliability since outages are detected automatically and MLGW's response is quicker since the meters communicate directly with MLGW.



These weather events could have proven to be far more perilous had it not been for MLGW's proactive efforts to improve system reliability through the ongoing replacement of old equipment and underground cables and many other measures including the following:

- We monitor the performance of our electric system and troubleshoot areas with frequent outages.
- We conduct root cause analysis to determine the best way to solve a problem. Examples of improvements include animal mitigation, tree trimming, or even redesigning the system.
- We target customers who have more than three outages per year or who experience outages lasting 10 hours or more. We reduced the number of customers experiencing interruptions over 10 hours in duration from nearly 20,000 in 2002 to 7,500 in 2010.





## Keeping Safety at the Forefront

MLGW is dedicated to maintaining and promoting utility safety awareness in the community. Since unsafe digging practices are the cause of most pipeline leaks, MLGW frequently communicates the importance of calling Tennessee One Call's "811" number to locate underground utilities prior to excavation projects.

Our efforts aren't limited to educating residential customers. In October, MLGW hosted a meeting for local and state public officials to learn about the importance of natural gas pipeline safety.

With a fierce dedication to ensuring the safety of our natural gas pipeline network, MLGW routinely checks the system for weaknesses and is in the process of replacing cast iron pipe with PVC pipe.

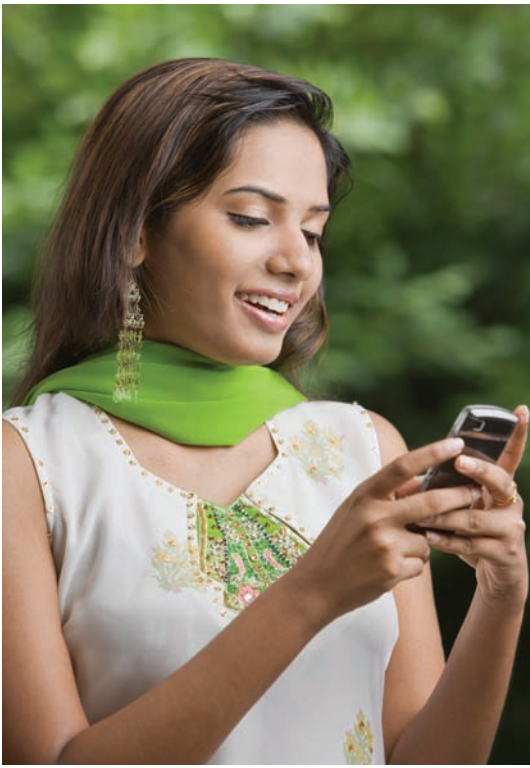
## Bold Leadership and Financial Strength

MLGW prides itself on having leaders with financial wisdom and restraint. During these tough economic times, MLGW's sound fiscal policies and decisions have been of tremendous benefit. Our financial health has ensured the success of our core business and the security of our workforce which has

been spared from layoffs suffered by so many companies in our nation. Our activities in 2010 further bolstered our financial standing.

MLGW refinanced some of its electric division prepay bonds, yielding significant savings in interest expense over the next eight years. The savings will help meet MLGW's operating budget needs, offsetting some of the impact the weak economy has had on residential and business energy use.

MLGW capitalized on the electric prepay deal it created with TVA eight years ago and the secure credit ratings of the utility's outstanding electric system revenue bonds that were upgraded to an "AA+" rating by Fitch and Moody's Investors Service prior to the bond transaction. Within six months, Fitch issued a second upgrade elevating MLGW's bond rating to "AAA" status. MLGW is one of only a handful of electric utilities to hold an "AAA" rating from Fitch, which rates 200 U.S. public power systems. MLGW's high credit rating is aided by the electric prepay of 2003 and manageable debt levels.



...and succeeding at making life more vibrant and habitable within our domain.

ing ways to satisfy our customers' needs and keep them informed.

MLGW provides a large variety of bill payment options, and the selection increased in 2010 when MLGW gave customers the option to pay their utility bills using Visa, MasterCard and Discover, and when MLGW partnered with TIO Networks, enabling MLGW customers to pay their utility bills using TIO Networks' touch-screen kiosks located in participating local Walgreens stores.

Last year, MLGW also introduced mobile alerts to notify customers of bill due dates and impending cutoffs. Now reminders, delivered right to customers' cell phones, will help prevent the costly and inconvenient dilemma of late payments and disconnected services.

In an effort to stay in tune with customers' needs, MLGW has increased outreach to the community through social media. Our social media tools have grown to encompass Twitter, Facebook, YouTube and our Bird on a Wire Blog. These tools have proven invaluable for gauging customer opinion and keeping our customers abreast of important MLGW information.

## Outstanding Rates

A survey of approximately 50 similar-sized, three-service utilities conducted by MLGW last summer ranked MLGW first overall in rates across the combined residential services. Our low comparative utility bills revealed in this survey were due in part to continuing competitive natural gas prices from suppliers, as well as continued low electric rates provided by the Tennessee Valley Authority (TVA). The fact that our utility services are consistently among the most affordable in the nation is an incentive to industries considering relocating to Memphis.

In addition, a Jacksonville Energy Authority (JEA) survey last year of 55 public and private utilities revealed that MLGW's residential electric rates are the fifth lowest in the nation.

Our pristine water derived from the Memphis Sands Aquifer also ranked Number 1 for affordability according to last October's rate comparison study conducted by MLGW. The study compared the published water rates of approximately 50 similar-sized utilities, and MLGW was found to offer the lowest average residential water bills.

## Broadening Customer Options

MLGW recognizes that its customers want more than just quality utility services; they want options that correspond to their needs, and open, honest and frequent communication. As a utility that is dedicated to achieving customer service excellence, we continuously seek and expand our offerings to enable our customers to spend less time worrying about their utility-related issues and more time achieving their pathways to success. From new payment options to new communication vehicles, MLGW offers ever-increas-





## Commitment to Energy Conservation

MLGW values the environment and frequently advocates that customers conserve energy to preserve the environment and to reduce utility costs.

In 2010, the availability of several federally sponsored programs served as a springboard for MLGW to intensify its calls to conserve.

- The Department of Energy's (DOE) Home Energy Efficiency Grant (HEEG) program offered rebates to customers for the purchase of energy-efficient heating and cooling systems.
- The DOE's Energy Efficiency and Conservation Block Grant (EECBG) program awarded the city of Memphis with a block grant – a portion of which funded a renewable power generation project at the M.C. Stiles Wastewater Treatment Plant. The remaining amount was distributed through MLGW to help fund home energy efficiency improvements for qualifying homeowners.
- MLGW and TVA partnered in the In-Home Energy Evaluation (IHEE) program initiative to offer rebates to residential customers for home energy improvements made by a member of the TVA Quality Contractor Network.

MLGW also hosted a series of community conservation events in 2010 and helped launch "The Smallest User" contest, a year-long competition between the residents of Cooper-Young Development Corporation and Evergreen

Historic Neighborhood Association to challenge residents to reduce their energy consumption.

## A clear and purposeful future

With solid leadership, financial stability and exceptional services, MLGW is poised to experience greater success. Innovative technologies such as Smart Grid and Smart Meters will pave the way by helping us to work more efficiently and reduce losses in time and revenue. As our customers learn more about the benefits of this technology, we will expand its use. We will also continue to seek ways to further enhance the reliability of our power systems, and ensure that we remain in a position to respond to the evolving needs of our community on the horizon.

# 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, 2010, 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 the findings for internal controls and compliance are herein presented.

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

MLGW's financial statements have been audited by Thompson Dunavant, PLC 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, 2010 are free of material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation.

The independent auditors concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that MLGW's financial statements for the fiscal year ended December 31, 2010, are fairly presented in conformity with generally accepted accounting principles. The independent 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 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 monthly among the divisions. A 1981 amendment to the City Charter permits the establishment of additional divisions to provide other energy services.

MLGW controls the administration of its activities and business affairs. It operates independently, manages its own finances and is responsible for obligations incurred in such operations, including indebtedness payable from operations of the Division. MLGW must have the approval of the 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 19th largest city with a population of 676,640. The MLGW service area comprises all of Shelby County, which in 2010 reported a population of 904,703. The eight-county Memphis Metro area provides a diverse range of employers, which contributes to the overall stability of the area. Memphis' central location, which is traversed by seven federal and two interstate highways, and is 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 air cargo airport since 1991, and boasting the third largest rail center and the fourth largest inland port in the United States. Home to major hubs for FedEx and UPS, world headquarters for Federal Express and a major thoroughfare for the trucking industry, Memphis is a vital epicenter of commerce. MLGW works diligently to maintain reliable power for these operations to ensure they run smoothly.

**National Economy** – Throughout 2010, experts' opinions varied regarding the degree to which the country was recovering from the economic recession that began in the last quarter of 2008. This was partly due to varying methods among the GAO, Congress and a number of economic experts and institutions for calculating signs of an economic rebound. This lack of clarity, combined with a national debt numbering in the trillions, civil unrest unfolding in Middle-Eastern oil-producing countries and anxiety over the impact of existing or future federal regulations, perpetuated economic uncertainty. Overall for 2010, real GDP rose 2.8 percent in contrast to a decline of 2.6 percent in 2009, according to the Bureau of Economic Analysis. The slight boost in 2010 growth mainly reflected upturns in exports, nonresidential fixed investment (notably equipment and software), consumer spending, and inventory investment. Despite this small upswing, a sustained high unemployment rate created a cautious environment relative to spending and a further economic burden for many of our customers.


In 2009, as part of the American Recovery and Reinvestment Act, the federal government developed a plan to distribute more than \$3.3 billion in "Smart Grid" technology development grants and an additional \$615 million for Smart Grid storage, monitoring and technology viability. In other words, the federal government was willing to help utilities pay for huge upgrades to their systems. The basic concept of Smart Grid is to add monitoring, analysis, control, and communication capabilities to the national electrical delivery system to maximize its capabilities while reducing energy consumption. MLGW received a \$5 million award that will improve the resiliency, power quality, and reliability of the electric grid which serves downtown Memphis and the medical district, significantly reducing most electric problems in those key districts of our service area. The total cost of these upgrades is \$10.5 million, and the remaining \$5.5 million was approved in MLGW's 2010 budget. These upgrades were implemented in 2010, along with the installation of automated meters in 1,000 homes of volunteer customers funded by a \$1 million pilot project that was approved in the MLGW 2010 budget by the Memphis City Council.


**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 5-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 5-year capital plans are updated periodically during the year in order to provide the most current possible cash flow projections.

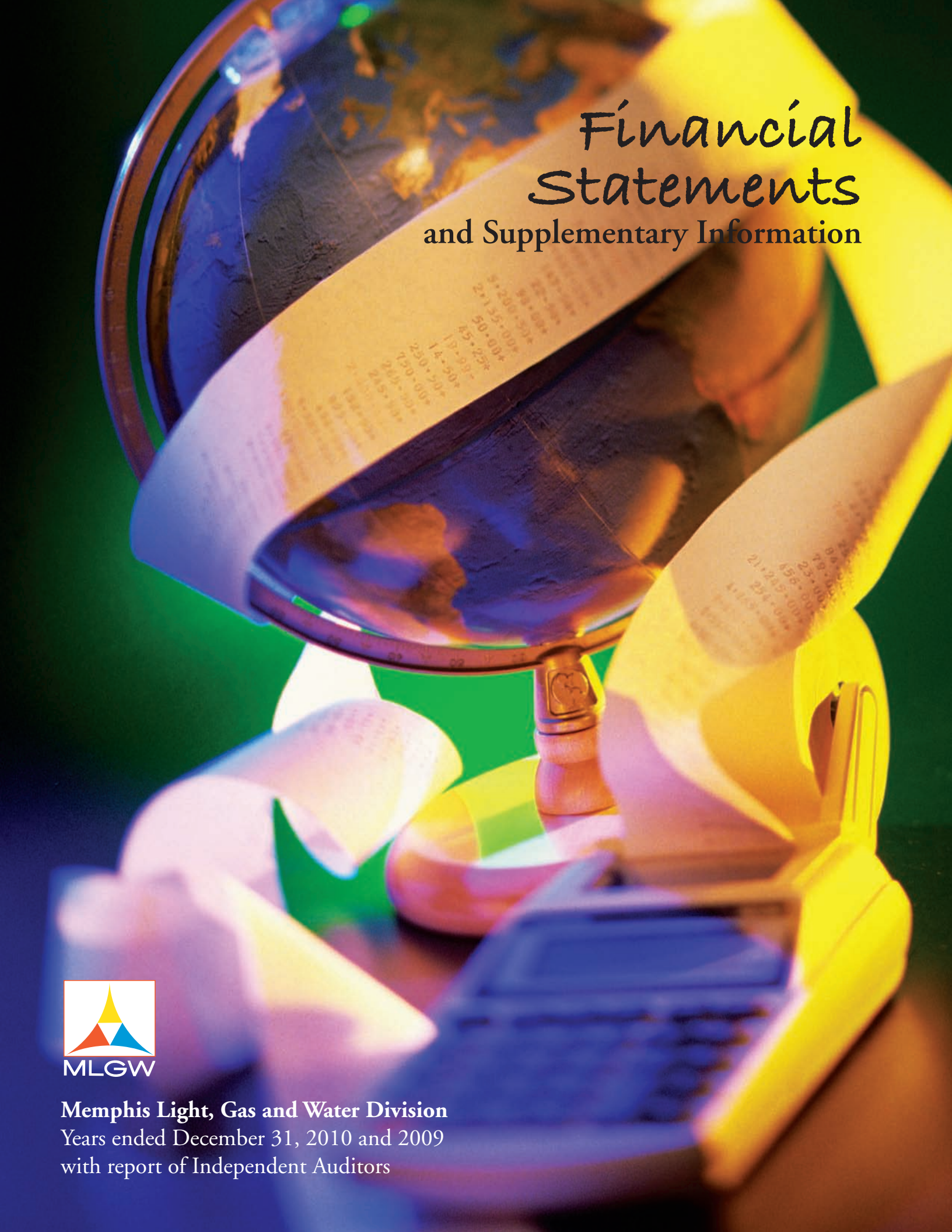
Among the three divisions, MLGW averages around \$100 million in capital expenditures throughout the year. Major electric projects planned within the next five years include installation of a substation in Collierville, rebuilding of a substation, and a mainframe system replacement. Gas division plans include continued investment in our cast iron replacement system project, purchase of meters for replacement and growth, and the purchase of transportation equipment. 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. In 2010, MLGW refinanced nearly \$500 million in electric division prepay bonds, yielding \$18.8 million in interest expense savings over the next eight years.

**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 Thompson Dunavant, PLC 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**  
Acting Vice President, CFO and Secretary-Treasurer

A magnifying glass is positioned over a laptop keyboard and several financial documents. The documents contain various numerical values, some with asterisks, such as 21,200,000, 2,135,000, 50,000, 85,250, 19,000, 14,500, 230,500, 240,000, 245,000, 90,000, 25,000, 21,245,000, 231,000, 1,125,000, 90,000, 25,000, 455,000, and 231,000. The background is a dark green gradient.

# Financial Statements and Supplementary Information



**Memphis Light, Gas and Water Division**  
Years ended December 31, 2010 and 2009  
with report of Independent Auditors

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 years ended December 31, 2010 and 2009, 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.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our 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, 2010 and 2009, and the changes in its financial position, or, where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Electric, Gas and Water Divisions of Memphis Light, Gas and Water Division as of December 31, 2010 and 2009, and the changes in financial position and cash flows thereof for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Governmental Auditing Standards*, we have also issued our report dated May 19, 2011, 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.

Accounting principles generally accepted in the United States of America require that management's discussion and analysis; schedule of funding progress for OPEB; schedule of employer contributions; 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 auditing standards generally accepted in the United States of America, 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 auditing standards generally accepted in the United States of America. 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.

A handwritten signature in black ink that reads "Thompson Duvarand LLC". The signature is written in a cursive, flowing style.

Memphis, Tennessee  
May 19, 2011



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 March 2010, MLGW refunded the entire portion of the callable 2003A Electric System Revenue bonds. During this process, MLGW received credit upgrades from Fitch Ratings (“Fitch”). Fitch raised its credit ratings on all MLGW outstanding debt which included the 2002, 2003A and 2008 series bonds from AA to AA+. Subsequently in April 2010, MLGW was recalibrated to an AAA rating by Fitch. Moody’s Investor Service (“Moody’s”) and Standard & Poor’s (“S&P”) reaffirmed their respective ratings on all outstanding electric system revenue bonds. The Water Division continues to hold the highest possible bond ratings which are Aaa from Moody’s and AAA from S&P. The Gas Division currently has no debt that is credit rated. When issuing bond ratings, agencies typically look at financial operations, management practices, rates, and debt ratios. Higher ratings result in the ability to issue and refinance debt at favorable rates compared to companies with lower ratings.



The following tables show MLGW bond ratings and debt administration for the Electric and Water Divisions in 2010:

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

MLGW Bond Ratings				Debt Administration		
	S&P	Moody's	Fitch		Outstanding Balance	Coverage
<b>Electric</b>				<b>Electric</b>	\$848,305	1.91
2002	AA+	Aa2	AAA			
2003A	AA+	Aa2	AAA			
2008	AA+	Aa2	AAA			
2010	AA+	Aa2	AAA			
<b>Water</b>	AAA	Aaa		<b>Water</b>	\$ 1,625	8.24

### 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:

	2010	2009	FY10 - FY09 Percentage Change	2008	FY09 - FY08 Percentage Change
		As Restated		As Restated	
Current assets (excluding restricted funds)	\$ 478,012	\$ 444,587	7.5%	\$ 468,684	-5.1%
Restricted assets	53,878	53,670	0.4%	56,149	-4.4%
Other assets	7,566	8,945	-15.4%	11,552	-22.6%
Prepaid power costs - long-term	785,243	886,968	-11.5%	982,550	-9.7%
Utility plant	929,401	908,976	2.2%	890,805	2.0%
<b>Total assets</b>	<b>2,254,100</b>	<b>2,303,146</b>	<b>-2.1%</b>	<b>2,409,740</b>	<b>-4.4%</b>
Current liabilities payable from current assets	288,514	271,898	6.1%	295,185	-7.9%
Current liabilities payable from restricted assets	28,301	28,732	-1.5%	32,846	-12.5%
Long-term debt	807,287	909,690	-11.3%	1,014,310	-10.3%
Non-current liabilities	36,294	38,395	-5.5%	42,432	-9.5%
<b>Total liabilities</b>	<b>1,160,396</b>	<b>1,248,715</b>	<b>-7.1%</b>	<b>1,384,773</b>	<b>-9.8%</b>
<b>Net assets:</b>					
Invested in utility plant, net of related debt	929,401	903,133	2.9%	879,348	2.7%
Restricted	15,748	15,295	3.0%	14,830	3.1%
Unrestricted	148,555	136,003	9.2%	130,789	4.0%
<b>Total net assets</b>	<b>\$ 1,093,704</b>	<b>\$1,054,431</b>	<b>3.7%</b>	<b>\$ 1,024,967</b>	<b>2.9%</b>



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### *Assets*

As of December 31, 2010, total assets were \$2.25 billion, a decrease of \$49.0 million (-2.1%) compared to December 31, 2009. This decrease is 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 amortization of debt expenses. These decreases are 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.

Total assets were \$2.30 billion for fiscal year 2009, a decrease of \$106.6 million (-4.4%) compared to fiscal year 2008. This decrease is mainly due to a \$95.6 million decrease in long-term prepaid power cost due to amortization (See Note 10). Current assets decreased by \$24.1 million due, in part, to a decrease in accounts receivable that can be attributed to Tennessee Valley Authority's ("TVA") fuel cost adjustment rate decreases. Restricted assets decreased by \$2.5 million due, in part, to the discontinuance of renewal and replacement funding. Other assets decreased by \$2.6 million partly due to the pay off of the Naval Support Activity long-term notes receivable. These decreases were partially offset by an \$18.2 million dollar increase in utility plant as a result of additions to electric plant in service.

### *Capital Assets and Construction Activities*

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 \$1.6 million, or 2.7%, 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 equipment (\$2.2 million).

The Electric Division had approximately \$909.0 million in utility plant assets, net of accumulated depreciation, as of December 31, 2009, an increase of 2.0% over fiscal year 2008. Beginning accumulated depreciation for 2008 was reduced by \$9.4 million and accumulated depreciation for 2009 and 2008 were each reduced by \$0.4 million as a result of the implementation of GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. In accordance with GASB 51, accumulated amortization related to intangible assets with indefinite lives should be restated to reflect that these assets are not to be amortized. During 2009, the Electric Division expended \$59.6 million on capital equipment purchases and construction activities, a decrease of \$7.3 million (-11.0%) compared to fiscal year 2008. Major Electric Division construction expenditures included substation and transmission projects (\$16.5 million), extensions to serve new customers (\$7.5 million), and distribution transformers (\$5.8 million). Other significant Electric Division capital expenditures included street lighting and leased outdoor lighting installations (\$6.2 million), meters and equipment (\$1.7 million), mainframe system replacement project (\$1.6 million), and communications network equipment (\$1.5 million).

### *Liabilities*

Total liabilities were \$1.16 billion as of December 31, 2010, a decrease of \$88.3 million (-7.1%) as compared to \$1.25 billion as of December 31, 2009. This decrease is primarily the result of a \$102.4 million (-11.3%) decrease in long-term debt due to principal payments and the refunding of the callable portion of the Series 2003A Revenue bonds (see Note 8). This decrease was partially offset by a \$16.6 million (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.

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009  
(Continued)**



As of December 31, 2009, total liabilities were \$1.25 billion representing a \$136.1 million (-9.8%) decrease compared to \$1.38 billion as of December 31, 2008. This decrease is mainly the result of a \$104.6 million decrease in long-term debt and a \$23.3 million decrease in current liabilities payable from current assets primarily due to a decrease in fuel cost adjustment rates from TVA. Current liabilities payable from restricted assets decreased by \$4.1 million as a result of a decrease in accrued medical benefits and the discontinuance of the renewal and replacement fund. Non-current liabilities decreased by \$4.0 million, in part, as a result of a reduction in customer advances for construction.

***Net Assets***

As of December 31, 2010, the Electric Division's total net assets (total assets less total liabilities) were \$1.09 billion, an increase of \$39.3 million, or 3.7%, as compared to December 31, 2009. Eighty-five percent of the net assets were related to utility plant, net of related debt, which accounts for \$26.3 million of the increase and unrestricted net assets contributed \$12.6 million to the overall increase in total net assets. For fiscal year 2009, total net assets were \$1.05 billion, a \$29.5 million, or 2.9%, increase over fiscal year 2008. This increase is mainly attributed to an increase in invested in utility plant, net of related debt, which accounts for \$23.8 million of the increase; unrestricted net assets added another \$5.2 million to the overall increase in total net assets.

In 2010, a prior period restatement was made to the Electric Division's net assets balance for 2008. The adjustment, an increase in net assets in the amount of \$9.8 million, was due to the reduction of the original accumulated depreciation associated with intangible assets. The adjustment was due to the implementation of GASB Statement No. 51.



**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:

	<u>2010</u>	<u>2009</u> As Restated	<u>FY10 - FY09</u> <u>Percentage</u> <u>Change</u>	<u>2008</u> As Restated	<u>FY09 - FY08</u> <u>Percentage</u> <u>Change</u>
Revenues:					
Operating revenues	\$ 1,281,485	\$ 1,208,856	6.0%	\$ 1,214,046	-0.4%
Non-operating revenues	66,861	76,007	-12.0%	82,712	-8.1%
Total revenues	<u>1,348,346</u>	<u>1,284,863</u>	<u>4.9%</u>	<u>1,296,758</u>	<u>-0.9%</u>
Expenses:					
Depreciation expense	42,100	41,043	2.6%	39,618	3.6%
Purchased power	1,032,960	969,309	6.6%	991,866	-2.3%
Other operating expense	160,657	165,512	-2.9%	152,270	8.7%
Non-operating expense	34,948	41,536	-15.9%	45,843	-9.4%
Total expenses	<u>1,270,665</u>	<u>1,217,400</u>	<u>4.4%</u>	<u>1,229,597</u>	<u>-1.0%</u>
Income (loss) before contributions in aid of construction and transfers	77,681	67,463	15.1%	67,161	0.4%
Contributions in aid of construction	7,827	10,532	-25.7%	11,675	-9.8%
Reduction of plant costs recovered through contributions in aid of construction	(7,827)	(10,532)	25.7%	(11,675)	9.8%
Transfers to City	<u>(38,408)</u>	<u>(37,999)</u>	<u>1.1%</u>	<u>(34,263)</u>	<u>10.9%</u>
Change in net assets	<u>39,273</u>	<u>29,464</u>	<u>33.3%</u>	<u>32,898</u>	<u>-10.4%</u>
Beginning net assets, as previously reported	<u>1,054,431</u>	<u>1,024,967</u>	<u>2.9%</u>	<u>978,174</u>	<u>4.8%</u>
Prior period adjustment	-	-	0.0%	13,895	-100.0%
Beginning net assets as adjusted	<u>1,054,431</u>	<u>1,024,967</u>	<u>2.9%</u>	<u>992,069</u>	<u>3.3%</u>
Ending net assets	<u>\$ 1,093,704</u>	<u>\$ 1,054,431</u>	<u>3.7%</u>	<u>\$ 1,024,967</u>	<u>2.9%</u>

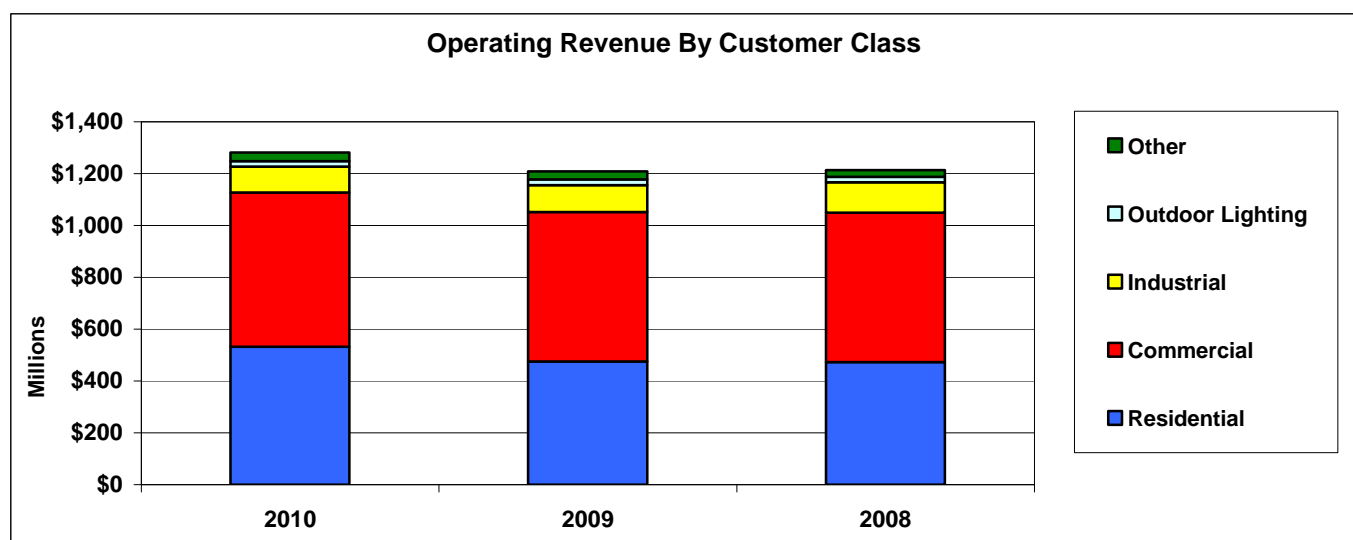
As of December 31, 2010, the change in net assets was \$39.3 million representing a \$9.8 million (33.3%) increase. This increase is mainly due to an increase in operating margin (operating revenues less purchased power cost) of \$9.0 million created by increased sales. The change in net assets for fiscal year 2009 was \$29.5 million, a decrease of \$3.4 million (-10.4%). This decrease is mainly due to a \$3.7 million increase in transfers to the City as a result of an increase in net plant and the tax and equalization rates.



Total revenues were \$1.35 billion for fiscal year 2010, 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 is mainly due to a \$6.2 million decrease in other income prepay credit, related to the Electric Prepay Bonds.

For fiscal year 2009, total revenues were \$1.28 billion, a decrease of \$11.9 million (-0.9%) from fiscal year 2008. TVA wholesale rate adjustments passed through to retail customers, combined with a decrease in electricity sales of 6.8% from 2008, decreased sales and service revenues by \$5.2 million. There was a corresponding decrease in purchased power cost of \$22.6 million. Miscellaneous operating revenues decreased by \$1.0 million in 2009 primarily from a \$0.9 million decrease in other operating revenues and a \$0.4 million decrease in forfeited discounts. Non-operating revenues decreased by 8.1% in 2009 as a result of a decrease in investment income.

**Figure 2: Electric Division's Operating Revenue**



For fiscal year 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. The decrease in non-operating expense was due, in part, to lower interest costs as a result of refunding the callable portion of the Series 2003A bonds.

As of December 31, 2009, total expenses were \$1.22 billion, a decrease of \$12.2 million (-1.0%) compared to December 31, 2008. This decrease was mainly the result of a \$22.6 million decrease in purchased power as a result of a TVA wholesale rate adjustment and decreased consumption and a \$4.3 million decrease in non-operating expenses that resulted from the continuing decline in interest expense on long-term debt from Electric Prepay Bonds. These decreases were offset by increases in other operating expenses of \$13.2 million as a result of concentrating resources on operations and maintenance work as a result of a major storm and a decline in capital construction activity. Depreciation expense increased by 3.6% in 2009 due to plant additions.

MANAGEMENT'S DISCUSSION AND ANALYSIS  
 FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009  
 (Continued)



Contributions in aid of construction ("CIAC") were \$7.8 million for fiscal year 2010, a decrease of \$2.7 million (-25.7%) from fiscal year 2009. CIAC decreased by \$3.0 million due to a decrease in reimbursements from the Federal Emergency Management Agency ("FEMA") for natural disasters. A reduction in cancelled contracts over 2009 caused a decrease of \$1.9 million. These decreases were offset by an increase of \$1.3 million due to a 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. For fiscal year 2009, CIAC was \$10.5 million, a decrease of \$1.1 million (-9.8%) from fiscal year 2008 as a result of less construction activity by developers.

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, 2010, transfers to the City were \$38.4 million. This represents a \$0.4 million increase compared to fiscal year 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. For the year ended December 31, 2009, transfers to the City were \$38.0 million. This represents a \$3.7 million increase from 2008; \$2.4 million is attributed to an increase in net plant and \$1.3 million is attributed to a tax and equalization rate increase.

**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:

	<u>2010</u>	<u>2009</u> As Restated	FY10 - FY09 Percentage Change	<u>2008</u> As Restated	FY09 - FY08 Percentage Change
Current assets (excluding restricted funds)	\$ 241,893	\$ 221,444	9.2%	\$ 199,617	10.9%
Restricted assets	14,801	21,298	-30.5%	35,639	-40.2%
Other assets	6,530	7,798	-16.3%	8,579	-9.1%
Utility plant	299,687	295,496	1.4%	294,643	0.3%
<b>Total assets</b>	<u>562,911</u>	<u>546,036</u>	<u>3.1%</u>	<u>538,478</u>	<u>1.4%</u>
Current liabilities payable from current assets	97,172	100,159	-3.0%	108,728	-7.9%
Current liabilities payable from restricted assets	5,989	7,287	-17.8%	7,980	-8.7%
Non-current liabilities	8,567	8,322	2.9%	10,940	-23.9%
<b>Total liabilities</b>	<u>111,728</u>	<u>115,768</u>	<u>-3.5%</u>	<u>127,648</u>	<u>-9.3%</u>
<b>Net assets</b>					
Invested in utility plant, net of related debt	299,687	295,496	1.4%	294,643	0.3%
Restricted	5,950	9,957	-40.2%	24,150	-58.8%
Unrestricted	145,546	124,815	16.6%	92,037	35.6%
<b>Total net assets</b>	<u>\$ 451,183</u>	<u>\$ 430,268</u>	<u>4.9%</u>	<u>\$ 410,830</u>	<u>4.7%</u>



### *Assets*

As of December 31, 2010, total assets were \$562.9 million, an increase of \$16.9 million, or 3.1%, as compared to December 31, 2009. The increase in total assets is mainly due to an increase in current assets. Collateral held in trust for securities on loan increased by \$9.4 million, inventories increased by \$2.6 million, cash and investments increased by \$7.1 million, and accounts receivable increased by \$6.8 million. Utility plant in service increased by \$4.2 million. Partially offsetting these increases were a decrease in unbilled revenue of \$7.4 million and decreases in restricted assets and other assets of \$6.5 million and \$1.3 million, respectively. Restricted assets decreased due to discontinuance of the renewal and replacement funding. Other assets decreased in accordance with the amortization of the Valero pipeline lease (See Note 3).

Total assets were \$546.0 million as of December 31, 2009, an increase of \$7.6 million over December 31, 2008. Current assets increased by \$21.8 million for fiscal year 2009 due to increases in cash and investments, offset, in part, by changes in the value of gas swaps and options and a decrease in unbilled revenue. Restricted assets decreased by \$14.3 million for fiscal year 2009 due to discontinuance of funding for renewal and replacement. Other assets decreased by \$0.8 million due to the normal amortization activity associated with the Valero pipeline lease.

### *Capital Assets and Construction Activities*

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, or 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).

The Gas Division had approximately \$295.5 million in utility plant assets, net of accumulated depreciation, as of December 31, 2009, an increase of \$0.8 million, or 0.3%, from December 31, 2008. During 2009, the Gas Division expended \$16.5 million on capital equipment purchases and construction activities, resulting in an increase of \$2.1 million, or 14.4%, in comparison to fiscal year 2008. The Gas Division's major construction expenditures included retrofit cast iron system and steel taps (\$5.5 million), extensions to serve customers (\$1.4 million), pipeline integrity management (\$1.2 million), and relocation of facilities to accommodate road improvements (\$0.5 million). A substantial portion of the Gas Division's expenditures was also attributed to meters and equipment (\$3.5 million) transportation and power operated equipment (\$1.5 million), and buildings and structures upgrades (\$1.0 million).

### *Liabilities*

For fiscal year 2010, total liabilities were \$111.7 million, a decrease of \$4.0 million (-3.5%) from \$115.8 million as of December 31, 2009. Current liabilities payable from current assets decreased by \$3.0 million (-3.0%) due, in part, to the payment of \$15 million on notes payable associated with the gas purchases for storage and a \$3.1 million decrease in accounts payable for purchased gas. Partially offsetting this decrease is an increase of \$9.4 million for collateral subject to return to borrowers as well as an increase of \$6.4 million in other deferred credits. Current liabilities payable from restricted assets decreased by \$1.3 million. The \$1.3 million decrease in current liabilities payable from restricted assets is due to a \$0.7 million reduction in customer deposits and a \$0.6 million decrease in customer advances for construction.

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009  
(Continued)**



As of December 31, 2009, total liabilities were \$115.8 million as compared to \$127.6 million as of December 31, 2008, a decrease of 9.3%. Current liabilities payable from current assets decreased by 7.9% as a result of the decline in notes payable balance associated with gas purchases for storage. Decreased financial liabilities for the pollution remediation obligation contributed to the decrease in non-current liabilities of 23.9%.

***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.

Total net assets for fiscal year 2009 increased by \$19.4 million, or 4.7%, over fiscal year 2008. Restricted net assets decreased by \$14.2 million (-58.8%), due, in part, to the discontinuance of funding for renewal and replacement. Unrestricted net assets increased by \$32.8 million, or 35.6%, in part, due to the discontinuance of funding for renewal and replacement and the change in net assets.

In 2010, a prior period restatement was made to the Gas Division's current assets and current liabilities payable from current assets for 2009 and 2008. The adjustment, an increase in unbilled revenue in the amount of \$6.2 million in 2009 and \$6.3 million in 2008, was due to a correction in the calculation of the purchase gas adjustment. A correlating increase to other deferred credits was also made in the amounts of \$6.2 million in 2009 and \$6.3 million in 2008.



**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, 2010, 2009 and 2008 (In Thousands)					
	<u>2010</u>	<u>2009</u>	FY10 - FY09 Percentage <u>Change</u>	<u>2008</u>	FY09 - FY08 Percentage <u>Change</u>
Revenues:					
Sales, service and other operating revenues	\$ 334,548	\$ 356,024	-6.0%	\$ 518,780	-31.4%
Transported gas revenue	4,887	3,657	33.6%	4,537	-19.4%
Non-operating revenues	1,915	1,590	20.4%	3,785	-58.0%
Total revenues	<u>341,350</u>	<u>361,271</u>	<u>-5.5%</u>	<u>527,102</u>	<u>-31.5%</u>
Expenses:					
Depreciation expense	12,266	12,458	-1.5%	12,377	0.7%
Purchased gas	213,538	240,518	-11.2%	394,023	-39.0%
Other operating expense	78,943	73,695	7.1%	76,570	-3.8%
Non-operating expense	48	463	-89.6%	1,149	-59.7%
Total expenses	<u>304,795</u>	<u>327,134</u>	<u>-6.8%</u>	<u>484,119</u>	<u>-32.4%</u>
Income (loss) before contributions in aid of construction and transfers	36,555	34,137	7.1%	42,983	-20.6%
Contributions in aid of construction	16	796	-98.0%	1,568	-49.2%
Reduction of plant costs recovered through contributions in aid of construction	(16)	(796)	98.0%	(1,568)	49.2%
Transfers to City	<u>(15,640)</u>	<u>(14,699)</u>	<u>6.4%</u>	<u>(12,827)</u>	<u>-14.6%</u>
Change in net assets	<u>20,915</u>	<u>19,438</u>	<u>7.6%</u>	<u>30,156</u>	<u>-35.5%</u>
Beginning net assets	<u>\$ 430,268</u>	<u>\$ 410,830</u>	<u>4.7%</u>	<u>\$ 380,674</u>	<u>7.9%</u>
Ending net assets	<u>\$ 451,183</u>	<u>\$ 430,268</u>	<u>4.9%</u>	<u>\$ 410,830</u>	<u>4.7%</u>

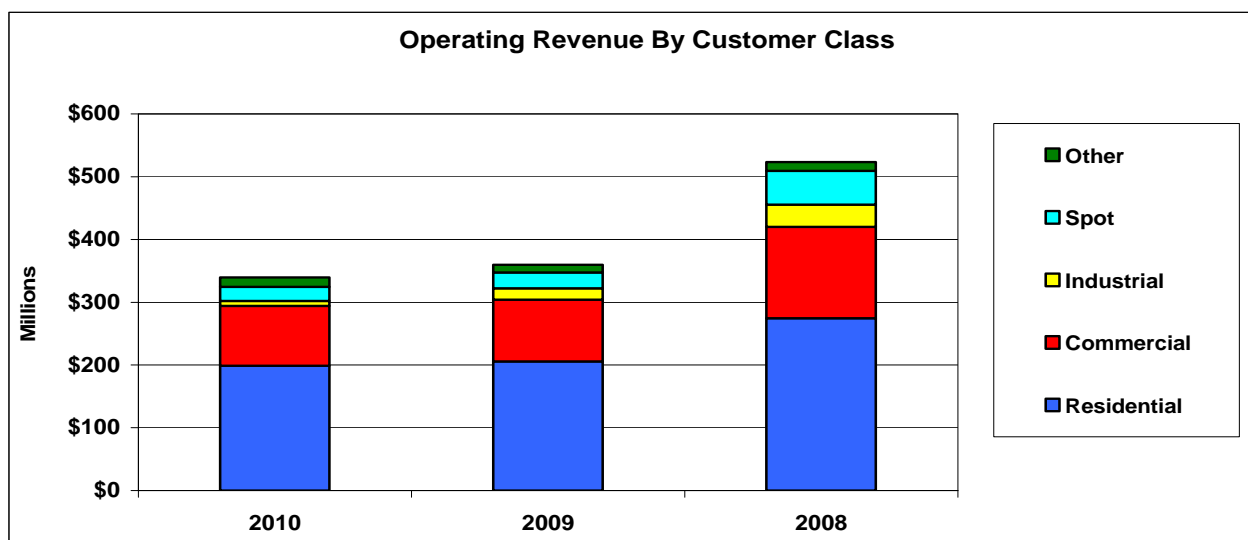
As of December 31, 2010, the change in net assets was \$20.9 million. This represents a \$1.5 million, or 7.6%, increase as compared to \$19.4 million as of December 31, 2009. This increase is mainly the result of higher operating margin of \$6.7 million generated from increased sales, offset, in part, by higher operations and maintenance expenses. The change in net assets decreased by \$10.7 million (-35.5%) to \$19.4 million as of December 31, 2009 from \$30.2 million as of December 31, 2008. This decrease is primarily the result of a decrease in sales, service and other operating revenues as a consequence of a decrease in sales volume and lower wholesale gas prices.



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.

Total revenues were \$361.3 million for fiscal year 2009, a decrease of 31.5% from fiscal year 2008. There was a 31.4% decrease in sales, service and other operating revenues in 2009, which can be attributed to an 8.1% decrease in sales volume and lower wholesale gas prices. A corresponding 39.0% decrease in purchased gas cost occurred. Transported gas revenue decreased by 19.4% in 2009 resulting from a 9.2% decrease in volumes transported. The 59.7% decrease in 2009 non-operating revenues is attributed to a decrease in investment income.

**Figure 3: Gas Division's Operating Revenue**



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 mainly due 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.

Total expenses decreased by \$157.0 million to \$327.1 million as of December 31, 2009. This decrease is mainly due to a \$153.5 million decrease in purchased gas as a result of a decrease in sales volume and lower wholesale gas costs. There was a decrease in other operating expense due to a reduction in operation and maintenance expenses. Non-operating expenses decreased as a result of a decline in interest expense.

For fiscal year 2010, CIAC decreased by \$0.8 million from fiscal year 2009 as a result of fewer construction projects from developers and other agencies. Of this amount, \$0.5 million was a reallocation from CIAC to operating and maintenance expense. A decrease of \$0.2 million was the result of a reduction in cancelled contracts in 2010 as compared to 2009. CIAC decreased to \$0.8 million in 2009, representing a decrease of \$0.8 million (-49.2%) from 2008. This decrease was due to a reduction in construction activity during 2009.

MANAGEMENT'S DISCUSSION AND ANALYSIS  
 FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009  
 (Continued)



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 2010, transfers to the City were \$15.6 million. 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.

The Gas Division's transfers to the City (in lieu of tax payments) were \$14.7 million in 2009. This amount represents an increase of \$1.9 million compared to 2008. This increase can be attributed to an increase in tax and equalization rates.

**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)*

	<u>2010</u>	<u>2009</u> As Restated	<u>FY10 - FY09</u> <u>Percentage</u> <u>Change</u>	<u>2008</u> As Restated	<u>FY09 - FY08</u> <u>Percentage</u> <u>Change</u>
Current assets (excluding restricted assets)	\$ 43,066	\$ 33,108	30.1%	\$ 33,882	-2.3%
Restricted assets	13,669	22,658	-39.7%	26,529	-14.6%
Other assets	1,849	2,653	-30.3%	2,501	6.1%
Utility plant	254,329	253,741	0.2%	251,315	1.0%
<b>Total assets</b>	<u>312,913</u>	<u>312,160</u>	<u>0.2%</u>	<u>314,227</u>	<u>-0.7%</u>
Current liabilities payable from current assets	19,042	14,092	35.1%	12,202	15.5%
Current liabilities payable from restricted assets	3,412	5,264	-35.2%	8,992	-41.5%
Long-term debt	1,612	3,127	-48.4%	4,546	-31.2%
Non-current liabilities	7,887	7,996	-1.4%	6,990	14.4%
<b>Total liabilities</b>	<u>31,953</u>	<u>30,479</u>	<u>4.8%</u>	<u>32,730</u>	<u>-6.9%</u>
<b>Net assets</b>					
Invested in utility plant, net of related debt	252,716	250,613	0.8%	243,534	2.9%
Restricted	9,624	16,776	-42.6%	20,227	-17.1%
Unrestricted	18,620	14,292	30.3%	17,736	-19.4%
<b>Total net assets</b>	<u>\$ 280,960</u>	<u>\$ 281,681</u>	<u>-0.3%</u>	<u>\$ 281,497</u>	<u>0.1%</u>



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### *Assets*

As of December 31, 2010, total assets were \$312.9 million, an increase of \$0.8 million as compared to December 31, 2009. This increase is due, in part, to an increase in current assets of \$10.0 million which was due mainly to an increase 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 offset by a decrease of \$9.0 million in restricted assets attributable to a decline in the master bond reserve fund.

Total assets for fiscal year 2009 decreased by \$2.1 million (-0.7%) to \$312.2 million compared to \$314.2 million for fiscal year 2008. The decrease in total assets was mainly due to a \$3.9 million reduction in restricted assets which was the result of a reduction in funds held in reserve for bonds and debt service, medical benefits and insurance reserves – injuries and damages. Total assets were further reduced by a \$0.8 million decrease in current assets due to a decline in cash and cash equivalents, investments, unbilled revenue and collateral held in trust for securities on loan. These decreases were offset by an increase in other assets by \$0.2 million on account of an increase in notes receivable and other prepayments and a \$2.4 million increase in utility plant resulting from capital equipment purchases and construction activity.

### *Capital Assets and Construction Activities*

The Water Division had approximately \$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).

The Water Division had approximately \$253.7 million in utility plant assets, net of accumulated depreciation, as of December 31, 2009, an increase of 1.0%. During 2009, the Water Division expended \$13.7 million on capital equipment purchases and construction activities, which was an increase of \$1.8 million, or 15.2%, in comparison to fiscal year 2008. The Water Division's major construction expenditures included extensions to new customers (\$2.2 million), relocation of facilities to accommodate road improvements (\$1.7 million), upgrades to McCord Pumping Station (\$1.0 million), upgrades to Allen Pumping Station (\$0.4 million), and upgrades to Shaw Pumping Station (\$0.3 million). The Water Division's major equipment purchases included data processing equipment (\$2.5 million), meters (\$1.3 million), and transportation and power operated equipment (\$0.2 million).

### *Liabilities*

As of December 31, 2010, total liabilities were \$32.0 million, representing an increase of \$1.5 million (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.



As of December 31, 2009, total liabilities were \$30.5 million, representing a decrease of \$2.3 million (-6.9%) as compared to December 31, 2008. Total liabilities decreased due to a decrease in current liabilities payable from restricted assets as a result of a \$3.2 million decline in bonds payable and a \$0.6 million decline in medical benefit accrual. These decreases were offset by an increase in current liabilities payable from current assets as a result of an increase in other accounts payable, accrued expenses and deferrals. There were also increases in customer deposits and other non-current liabilities.

### *Net Assets*

Total net assets decreased by \$0.7 million (-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).

Total net assets increased by \$0.2 million, or 0.1%, to \$281.7 million as of December 31, 2009, from \$281.5 million as of December 31, 2008. The increase in total net assets can be attributed, in part, to an increase in utility plant, net of related debt, by \$7.1 million. This increase was reduced by a decrease of \$3.5 million in restricted net assets mainly due to a reduction in reserves for medical benefits and debt service. There was also a \$3.4 million decrease in unrestricted net assets.

For fiscal years 2009 and 2008, restatements were made to current liabilities payable from current assets, non-current liabilities and unrestricted net assets. The adjustments made were related to a misallocation of accrued employee benefits.



**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:

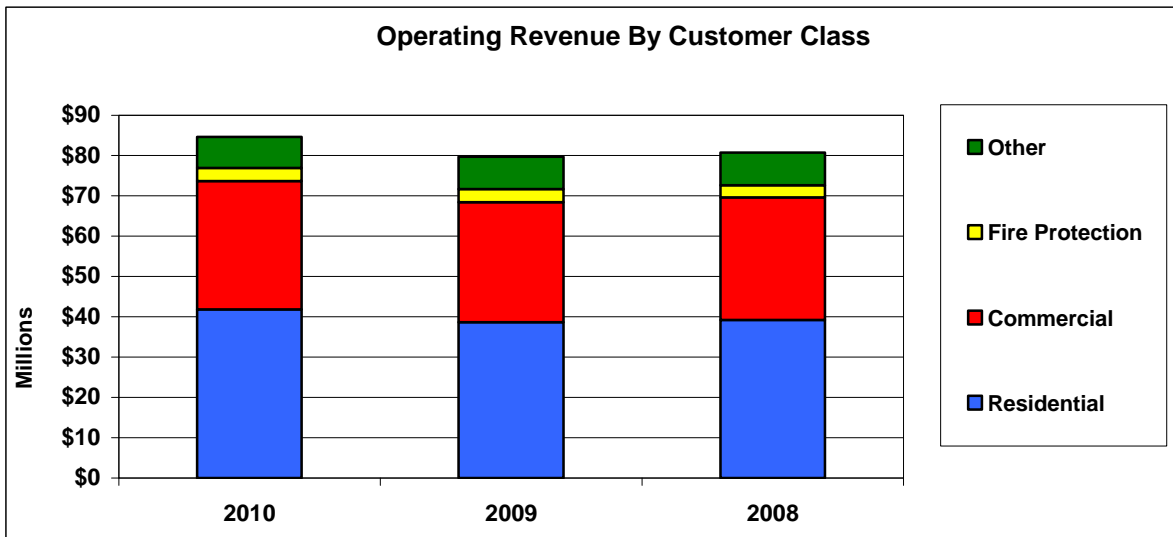
	<u>2010</u>	<u>2009</u> As Restated	FY10 - FY09 Percentage <u>Change</u>	<u>2008</u> As Restated	FY09 - FY08 Percentage <u>Change</u>
Revenues:					
Operating revenues	\$ 84,593	\$ 79,657	6.2%	\$ 80,741	-1.3%
Non-operating revenues	364	638	-42.9%	1,692	-62.3%
Total Revenues	<u>84,957</u>	<u>80,295</u>	<u>5.8%</u>	<u>82,433</u>	<u>-2.6%</u>
Expenses:					
Depreciation expense	11,079	10,932	1.3%	10,493	4.2%
Other operating expense	71,908	66,382	8.3%	66,433	-0.1%
Non-operating expense	191	297	-35.7%	420	-29.3%
Total Expenses	<u>83,178</u>	<u>77,611</u>	<u>7.2%</u>	<u>77,346</u>	<u>0.3%</u>
Income (loss) before contributions in aid of construction and transfers	1,779	2,684	-33.7%	5,087	-47.2%
Contributions in aid of construction	720	3,152	-77.2%	4,589	-31.3%
Reduction of plant costs recovered through contributions in aid of construction	(720)	(3,152)	77.2%	(4,589)	31.3%
Transfers to City	(2,500)	(2,500)	0.0%	(2,500)	0.0%
Change in net assets	<u>(721)</u>	<u>184</u>	<u>-491.8%</u>	<u>2,587</u>	<u>-92.9%</u>
Beginning net assets	<u>281,681</u>	<u>281,497</u>	<u>0.1%</u>	<u>278,910</u>	<u>0.9%</u>
Ending net assets	<u>\$ 280,960</u>	<u>\$ 281,681</u>	<u>-0.3%</u>	<u>\$ 281,497</u>	<u>0.1%</u>

As of December 31, 2010, the change in net assets was \$-0.7 million, a decrease of \$0.9 million (-491.8%). This decrease is due primarily to increased operation and maintenance cost, partially offset by an increase in operating revenue. The change in net assets was \$0.2 million as of December 31, 2009. This is a decrease of \$2.4 million (-92.9%) compared to December 31, 2008. This decline is a result of the continued growth of expenses relative to revenue.



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. Total revenues were \$80.3 million for fiscal year 2009, a decrease of 2.6% from fiscal year 2008. Operating revenues decreased by 1.3% in 2009 and is attributed to a 1.4% decrease in sales and service revenue. Non-operating revenues decreased by 62.3% in 2009, which can be attributed to decreases in investment and interest income.

**Figure 4: Water Division's Operating Revenue**



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

As of December 31, 2009, total expenses were \$77.6 million representing a 0.3% increase compared to December 31, 2008. Non-operating expenses decreased by 29.3% as a result of the continuing decline in interest expense related to long-term debt. Other operating expenses decreased by 0.1%.

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. CIAC decreased to \$3.2 million in 2009, representing a decrease of \$1.4 million (-31.3%) from 2008. This decrease was due to a reduction in developers' construction activity during 2009.

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.



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### **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, 2010 AND 2009**  
(Dollars in Thousands)



	Electric Division		Gas Division		Water Division	
	2010	2009	2010	2009	2010	2009
	As Restated		As Restated		As Restated	
<b>Assets</b>						
Current assets:						
Cash and cash equivalents	\$ 84,374	\$ 108,592	\$ 71,621	\$ 81,576	\$ 9,872	\$ 8,831
Investments	63,112	45,505	50,083	33,026	7,439	3,714
Derivative financial instruments	-	40	-	2,351	-	-
Restricted funds - current	28,301	28,738	7,318	12,676	4,337	5,264
Accounts receivable, less allowance for doubtful accounts	110,083	80,213	53,731	46,891	15,748	11,547
Unbilled revenues	62,806	67,562	19,426	26,863	2,445	2,375
Prepaid power cost	100,504	95,582	-	-	-	-
Unrecovered purchased gas cost	-	-	432	1,585	-	-
Inventories	18,313	22,191	17,170	14,525	1,910	2,142
Collateral held in trust for securities on loan	36,890	21,419	22,152	12,755	5,428	2,832
Other current assets	1,930	3,483	7,278	1,872	224	1,667
Total current assets	506,313	473,325	249,211	234,120	47,403	38,372
Non-current assets:						
Restricted funds:						
Futures margin deposits	-	6	1,329	4,880	-	-
Construction	-	-	-	1,108	1,100	1,630
Insurance reserves - injuries and damages	6,729	6,163	2,511	2,314	1,560	1,850
Insurance reserves - casualties and general	15,748	15,289	4,621	4,569	6,692	6,491
Medical benefits	4,296	4,691	1,916	2,092	1,272	1,389
Customer deposits	16,113	15,808	4,424	6,335	1,038	1,012
Bond reserve and debt service	10,992	11,713	-	-	2,007	10,286
Total restricted funds	53,878	53,670	14,801	21,298	13,669	22,658
Less restricted funds – current	(28,301)	(28,738)	(7,318)	(12,676)	(4,337)	(5,264)
Restricted funds – non-current	25,577	24,932	7,483	8,622	9,332	17,394
Other assets:						
Prepaid power cost – long term	785,243	886,968	-	-	-	-
Prepayments In Lieu of Taxes	1,904	1,426	44	414	-	-
Unamortized debt expense	4,333	6,099	-	-	-	-
Notes receivable	-	-	5,887	6,734	1,452	2,223
Other prepayments	1,329	1,420	599	650	397	430
Total other assets	792,809	895,913	6,530	7,798	1,849	2,653
Utility plant	1,501,609	1,450,893	554,010	539,873	440,254	432,985
Less accumulated depreciation	(572,208)	(541,917)	(254,323)	(244,377)	(185,925)	(179,244)
Utility plant, net	929,401	908,976	299,687	295,496	254,329	253,741
Total non-current assets	1,747,787	1,829,821	313,700	311,916	265,510	273,788
Total assets	\$ 2,254,100	\$ 2,303,146	\$ 562,911	\$ 546,036	\$ 312,913	\$ 312,160

See accompanying notes.

**BALANCE SHEETS**  
**DECEMBER 31, 2010 AND 2009**  
(Dollars in Thousands)  
(Continued)



	Electric Division		Gas Division		Water Division	
	2010	2009	2010	2009	2010	2009
	As Restated		As Restated		As Restated	
<b>Liabilities</b>						
Current liabilities:						
Accounts payable - purchased power and gas	\$ 121,946	\$ 113,330	\$ 37,900	\$ 40,974	\$ -	\$ -
Other accounts payable, accrued expenses, and deferrals	46,795	50,992	35,137	31,409	13,614	11,249
Derivative financial instruments	-	-	1,983	-	-	-
Bonds and notes payable	82,883	86,082	-	15,000	-	-
Collateral subject to return to borrowers	36,890	21,494	22,152	12,776	5,428	2,843
Total current liabilities payable from current assets	288,514	271,898	97,172	100,159	19,042	14,092
Current liabilities payable from restricted assets:						
Construction	-	-	-	600	175	1,630
Customer deposits	6,284	6,165	1,562	2,281	405	395
Medical benefits	4,296	4,691	1,916	2,092	1,272	1,389
Insurance reserves - injuries and damages	6,729	6,163	2,511	2,314	1,560	1,850
Bonds payable – accrued interest	3,455	3,947	-	-	-	-
Bonds payable – principal	7,537	7,766	-	-	-	-
Total current liabilities payable from restricted assets	28,301	28,732	5,989	7,287	3,412	5,264
Total current liabilities	316,815	300,630	103,161	107,446	22,454	19,356
Non-current liabilities:						
Customer advances for construction	8,017	7,556	1,003	1,015	-	-
Customer deposits	9,829	9,643	2,862	4,053	633	617
Other	18,448	21,196	4,702	3,254	7,254	7,379
Bonds payable	807,287	909,690	-	-	1,612	3,127
Total non-current liabilities	843,581	948,085	8,567	8,322	9,499	11,123
Total liabilities	1,160,396	1,248,715	111,728	115,768	31,953	30,479
<b>Net assets</b>						
Invested in capital assets, net of related debt	929,401	903,133	299,687	295,496	252,717	250,613
Restricted	15,748	15,295	5,950	9,957	9,624	16,776
Unrestricted	148,555	136,003	145,546	124,815	18,619	14,292
Total net assets	1,093,704	1,054,431	451,183	430,268	280,960	281,681
Total liabilities and net assets	\$ 2,254,100	\$ 2,303,146	\$ 562,911	\$ 546,036	\$ 312,913	\$ 312,160

See accompanying notes.

**STATEMENTS OF REVENUES, EXPENSES  
AND CHANGES IN NET ASSETS  
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009  
(Dollars in Thousands)**



	Electric Division		Gas Division		Water Division	
	2010	2009	2010	2009	2010	2009
	As Restated				As Restated	
Operating revenues:						
Sales and service revenues	\$ 1,249,216	\$ 1,179,260	\$ 322,418	\$ 343,842	\$ 76,029	\$ 70,837
Transported gas revenue	-	-	4,887	3,657	-	-
Other revenues	32,269	29,596	12,130	12,182	8,564	8,820
Total operating revenues	1,281,485	1,208,856	339,435	359,681	84,593	79,657
Operating expenses:						
Purchased power and gas for resale	1,032,960	969,309	213,538	240,518	-	-
Production	-	-	-	-	17,050	16,215
Operation	115,243	116,680	70,103	64,651	44,821	41,645
Maintenance	44,830	48,243	8,764	8,810	10,037	8,522
Depreciation	42,100	41,043	12,266	12,458	11,079	10,932
Payments in lieu of taxes	584	589	76	234	-	-
	1,235,717	1,175,864	304,747	326,671	82,987	77,314
Operating income	45,768	32,992	34,688	33,010	1,606	2,343
Non-operating revenues (expenses):						
Contributions in aid of construction	7,827	10,532	16	796	720	3,152
Reduction of plant costs recovered through contributions in aid of construction	(7,827)	(10,532)	(16)	(796)	(720)	(3,152)
Transmission credits	28,066	27,895	-	-	-	-
Investment and other income	4,186	7,274	1,915	1,590	364	638
Prepay credit	34,609	40,838	-	-	-	-
Interest expense	(34,948)	(41,536)	(48)	(463)	(191)	(297)
Total non-operating revenues (expenses)	31,913	34,471	1,867	1,127	173	341
Income before transfers	77,681	67,463	36,555	34,137	1,779	2,684
Transfers out	(38,408)	(37,999)	(15,640)	(14,699)	(2,500)	(2,500)
Change in net assets	\$ 39,273	\$ 29,464	\$ 20,915	\$ 19,438	\$ (721)	\$ 184
Net assets, beginning of year, as previously reported	\$ 1,054,431	\$ 1,015,123	\$ 430,268	\$ 410,830	\$ 281,681	\$ 282,460
Adjustments to beginning net assets	-	9,844	-	-	-	(963)
Net assets, beginning of year as adjusted	1,054,431	1,024,967	430,268	410,830	281,681	281,497
Change in net assets	39,273	29,464	20,915	19,438	(721)	184
Net assets, end of year	\$ 1,093,704	\$ 1,054,431	\$ 451,183	\$ 430,268	\$ 280,960	\$ 281,681

See accompanying notes.

**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**  
(Dollars in Thousands)



	Electric Division		Gas Division		Water Division	
	2010	2009	2010	2009	2010	2009
	As Restated		As Restated		As Restated	
Cash flows from operating activities:						
Receipts from customers and users	\$ 1,267,061	\$ 1,207,244	\$ 339,463	\$ 391,749	\$ 79,861	\$ 72,978
Payments to suppliers	(919,070)	(890,061)	(234,485)	(225,673)	(27,662)	(20,432)
Payments to/on behalf of employees	(115,460)	(103,922)	(56,168)	(51,618)	(42,742)	(38,813)
Payments from (to) other Division funds	(519)	(41)	(1,430)	(1,517)	1,606	1,519
Payments for taxes	(426)	(791)	897	(186)	-	-
Net cash provided by operating activities	<b>231,586</b>	212,429	<b>48,277</b>	112,755	<b>11,063</b>	15,252
Cash flows from noncapital financing activities:						
Transfers to City of Memphis	(38,408)	(37,999)	(15,640)	(14,699)	(2,500)	(2,500)
Proceeds from issuance of long-term debt	471,305	-	-	-	-	-
Principal payments on long-term debt	(558,055)	(82,210)	-	-	-	-
Interest expense on bonds	(45,019)	(50,735)	-	-	-	-
Proceeds from issuance of notes payable	-	-	-	15,000	-	-
Principal payment on notes payable	-	-	(15,000)	(35,000)	-	-
Interest payments on notes payable	-	-	(126)	(674)	-	-
Net cash used in noncapital financing activities	<b>(170,177)</b>	(170,944)	<b>(30,766)</b>	(35,373)	<b>(2,500)</b>	(2,500)
Cash flows from capital and related financing activities:						
Purchase and construction of utility plant	(70,511)	(72,726)	(18,988)	(17,136)	(12,740)	(17,155)
Contributions in aid of construction	7,827	10,532	16	796	720	3,152
Principal payments on long-term debt	(7,354)	(7,156)	-	-	(1,540)	(4,700)
Interest payments on debt	(350)	(695)	-	-	(166)	(433)
Net cash used in capital and related financing activities	<b>(70,388)</b>	(70,045)	<b>(18,972)</b>	(16,340)	<b>(13,726)</b>	(19,136)
Cash flows from investing activities:						
Sales and maturities of investments	25,661	29,413	21,825	5,044	5,883	3,142
Purchases of investments	(46,648)	(16,811)	(39,601)	(21,786)	(10,687)	(1,801)
Payments received on notes receivable	1,139	1,708	1,712	1,712	-	-
Issuance of notes receivable	-	-	-	-	772	(94)
Investment income earned on investments	1,509	2,048	374	193	180	248
Net cash provided by (used in) investing activities	<b>(18,339)</b>	16,358	<b>(15,690)</b>	(14,837)	<b>(3,852)</b>	1,495
Increase (decrease) in cash and cash equivalents	<b>(27,318)</b>	(12,202)	<b>(17,151)</b>	46,205	<b>(9,015)</b>	(4,889)
Cash and cash equivalents, beginning of year	<b>155,911</b>	168,113	<b>100,508</b>	54,303	<b>28,537</b>	33,426
Cash and cash equivalents, end of year	<b>\$ 128,593</b>	\$ 155,911	<b>\$ 83,357</b>	\$ 100,508	<b>\$ 19,522</b>	\$ 28,537

See accompanying notes.

**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**  
(Dollars in Thousands)  
(Continued)



	Electric Division		Gas Division		Water Division	
	2010	2009	2010	2009	2010	2009
	As Restated		As Restated		As Restated	
Reconciliation of operating income to net cash provided by operating activities:						
Operating income	\$ 45,768	\$ 32,992	\$ 34,688	\$ 33,010	\$ 1,606	\$ 2,343
Adjustments to reconcile operating income to net cash provided by operating activities:						
Depreciation of utility plant	42,259	44,024	14,780	15,487	11,433	11,577
Transmission credits	28,066	27,895	-	-	-	-
Prepay power credits	34,609	40,838	-	-	-	-
Other income	2,645	5,074	568	341	184	382
(Increase) decrease in assets:						
Accounts receivable	(29,779)	12,511	(6,841)	11,056	(4,201)	(866)
Unbilled revenues	4,756	(8,649)	7,437	11,097	(70)	643
Prepaid power cost	96,803	92,155	-	-	-	-
Prepayments – In Lieu of Taxes	(479)	18	370	49	-	-
Unrecovered purchased gas cost	-	-	1,154	(1,311)	-	-
Inventories	3,877	1,566	(2,644)	16,965	232	249
Other assets	485	630	(2,897)	18,549	1,475	(1,726)
Increase (decrease) in liabilities:						
Accounts payable - purchased power and gas	8,617	(33,012)	(3,073)	(3,983)	-	-
Other accounts payable and accrued expenses	(4,228)	4,557	3,206	15,845	489	1,947
Customer deposits	304	1,920	(1,911)	873	26	118
Insurance reserves	566	(806)	196	290	(290)	(158)
Medical benefit accrual	(395)	(2,065)	(175)	(920)	(117)	(611)
Other	(2,288)	(7,219)	3,419	(4,593)	296	1,354
Total adjustments	185,818	179,437	13,589	79,745	9,457	12,909
Net cash provided by operating activities	\$ 231,586	\$ 212,429	\$ 48,277	\$ 112,755	\$ 11,063	\$ 15,252
Reconciliation of cash and cash equivalents per statements of cash flows to the balance sheets:						
Restricted funds	\$ 53,878	\$ 53,670	\$ 14,801	\$ 21,298	\$ 13,669	\$ 22,658
Less investments included in restricted funds	(9,659)	(6,351)	(3,065)	(2,366)	(4,019)	(2,952)
Cash and cash equivalents included in restricted funds	44,219	47,319	11,736	18,932	9,650	19,706
Current assets - cash and cash equivalents	84,374	108,592	71,621	81,576	9,872	8,831
Total cash and cash equivalents	\$ 128,593	\$ 155,911	\$ 83,357	\$ 100,508	\$ 19,522	\$ 28,537

See accompanying notes.



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## 1. Summary of Significant Accounting Policies

### Organization

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

### Basis of Presentation

The financial statements present only the Electric, Gas and Water Divisions of MLGW in conformity with accounting principles generally accepted in the United States that are applicable to a proprietary fund of a government unit. The accompanying financial statements present the separate financial positions, results of operations, and 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.

MLGW’s accounting policies are in conformity with accounting principles generally accepted in the United States. Where applicable, the Federal Energy Regulatory Commission’s (FERC) (Electric and Gas Divisions) and the National Association of Regulatory Utility Commissioners’ (NARUC) (Water Division) Uniform Systems of Accounts are used. MLGW is not subject to the jurisdiction of federal or state regulatory commissions.



## 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.

### Recent Accounting Standards

In June 2010, GASB issued Statement No. 59, *Financial Instruments Omnibus*. The objective of this standard is to update and improve existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools. This statement is effective for periods beginning after June 15, 2010. MLGW has not completed the process of evaluating the impact of this statement on its financial statements, and has not elected early implementation.

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.

### Regulatory Accounting

MLGW prepares its financial statements in accordance with the provisions of *FASB Accounting Standards Codification (“ASC”) 980, Regulated Operations* (formerly Statement of Financial Accounting Standards No. 71, *Accounting for the Effects of Certain Types of Regulation*.) In general, ASC 980 recognizes that accounting for rate regulated enterprises should reflect the relationship of costs and revenues introduced by rate regulation.



**1. Summary of Significant Accounting Policies (continued)**

**Regulatory Accounting (continued)**

As a result, a regulated utility may defer recognition of a cost (a regulatory asset) or recognize an obligation (a regulatory liability) if it is probable that through the rate making process, there will be a corresponding increase or decrease in future revenues. Accordingly, MLGW has recognized certain regulatory assets and regulatory liabilities in the accompanying balance sheets.

In the event operations are no longer subject to the provisions of 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 and expenses. The following are the regulatory assets and liabilities included in the balance sheets:

		2010	2009
<b>Assets</b>			
Electric Division	Deferred asset pollution remediation	\$ 1,712	\$ 1,535
Gas Division	Unrecovered purchased gas cost	432	1,585
Gas Division	Deferred asset pollution remediation	2,504	-
Water Division	Deferred asset pollution remediation	224	1,667
<b>Liabilities</b>			
Gas Division	Deferred Credits - PGA	\$ 18,990	\$ 12,550
Gas Division	Deferred liability pollution remediation	-	1,195

**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 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**

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.



**1. Summary of Significant Accounting Policies (continued)**

**Fair Value of Financial Instruments (continued)**

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, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Electric Division	\$ 935,439	\$ 1,048,553
Water Division	1,700	3,383

**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, 2010 and 2009, accounts receivable and allowances for doubtful accounts were as follows:

	<u>Electric Division</u>		<u>Gas Division</u>		<u>Water Division</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Accounts receivable	\$ 117,174	\$ 88,507	\$ 55,554	\$ 49,143	\$ 16,825	\$ 12,633
Allowance for doubtful accounts	(7,091)	(8,294)	(1,824)	(2,252)	(1,077)	(1,086)
TOTAL A/R, net of allowance	<u>\$ 110,083</u>	<u>\$ 80,213</u>	<u>\$ 53,730</u>	<u>\$ 46,891</u>	<u>\$ 15,748</u>	<u>\$ 11,547</u>

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:

	<u>2010</u>	<u>2009</u>
Electric	\$ 8,939	\$ 6,914
Gas	2,463	3,726
Water	1,338	1,271



## 1. Summary of Significant Accounting Policies (continued)

### 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. Customers' financial condition and credit worthiness are evaluated regularly.

Management of MLGW does not believe that it has a significant credit risk on its derivative instruments. MLGW's derivatives transactions are mostly conducted directly or indirectly with the New York 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 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 (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.

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## 1. Summary of Significant Accounting Policies (continued)

### Utility Plant (continued)

An allowance for borrowed funds used during construction is computed at actual interest rates to the extent that major projects are financed by specific long-term debt. In 2010 and 2009, no construction projects were financed with specific long-term debt. Interest on other debt is not capitalized, as it is recovered through current revenues.

Depreciation is computed 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, 2.8% 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.

### Reserves and Related Restricted Funds

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

The Electric and Gas Divisions maintain cash margin accounts with its futures clearing member. 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.

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## 1. Summary of Significant Accounting Policies (continued)

### Reserves and Related Restricted Funds (continued)

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

MLGW adopted GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* for the years ending December 31, 2010 and 2009. GASB 53 is intended to improve how state and local governments report information about derivative instruments to manage specific risks. The Statement addresses hedge accounting requirements and requires governments to measure most derivative instruments at fair value in their financial statements.

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.



**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, 2010 and 2009.

<u>Type</u>	<u>December 31, 2010</u>		<u>December 31, 2009</u>	
	<u>Market Value</u>	<u>Notional Amount</u>	<u>Market Value</u>	<u>Notional Amount</u>
Futures	(\$432)	\$4,714	\$54	\$9,362
Swaps	(\$1,551)	\$8,250	\$2,188	\$28,132
Options	\$0	\$0	\$109	\$8,193
Total	<u>(\$1,983)</u>	<u>\$12,964</u>	<u>\$2,351</u>	<u>\$45,687</u>

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

<u>Type</u>	<u>December 31, 2010</u>	<u>December 31, 2009</u>
	<u>Deferred Gains (Losses)</u>	<u>Deferred Gains (Losses)</u>
Futures	(\$432)	\$54
Swaps	(\$1,551)	\$2,188
Options	\$0	\$109
Total	<u>(\$1,983)</u>	<u>\$2,351</u>

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

<u>Type</u>	<u>December 31, 2010</u>	<u>December 31, 2009</u>
	<u>Deferred Gains (Losses)</u>	<u>Deferred Gains (Losses)</u>
Futures	(\$585)	\$162
Swaps	(\$238)	\$850
Total	<u>(\$823)</u>	<u>\$1,012</u>

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, 2010 and 2009, were \$6,491 and \$7,934, 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.

Swap contracts as of December 31, 2010 and 2009 are reported at market values of \$0 and \$40. The market values of these derivative positions are reported on the balance sheet as derivative financial instruments. The notional amounts of the open swaps as of December 31, 2010 and 2009 were \$0 and \$122.

Deferred gains (losses) at year end associated with recording derivative positions at fair market value were \$0 and \$40 for the years ending 2010 and 2009. The deferred gains at year end for these derivative positions are reported on the balance sheet as other liability deferrals. Gains and losses associated with derivative positions on fuel are transferred monthly to MLGW's transportation costs.

The fuel margin account balance with MLGW's New York Mercantile Exchange clearing member as of December 31, 2010 and 2009 were \$621 and \$212, 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.”



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## 1. Summary of Significant Accounting Policies (continued)

### Revenues and Expenses

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

### Statements of Cash Flows

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

### Related Parties

MLGW conducts business with its related parties as "arm's length" transactions. Major related party entities include the City of Memphis government. Generally, MLGW provides utility and related services to these parties and receives payments in the same manner as other customers. For the years ending 2010 and 2009, receivables from related parties for utility construction, pole rentals and utility related services excluding utility bills were \$4,118 and \$3,230. 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 \$2,272 and \$2,316 for 2010 and 2009, respectively.

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## 1. Summary of Significant Accounting Policies (continued)

### Prior Period Restatements

In 2010, MLGW implemented GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. In accordance with GASB 51 guidance, accumulated amortization related to intangible assets with indefinite lives should be restated to reflect that these assets are not to be amortized. As a result of the implementation of this provision, MLGW increased Electric Division beginning net assets for 2009 by \$9,844. The 2009 Statement of Revenues, Expenses and Changes in Net Assets was restated to reflect a decrease in depreciation expense related to land rights of \$401. The 2009 Balance Sheet was restated to reflect the cumulative decrease in accumulated depreciation of \$10,245.

An analysis of Gas Division unbilled revenue and the related PGA amounts included in the unbilled revenue calculations as of December 31, 2010 revealed monthly PGA amounts for 2008 through 2010 had been incorrectly calculated, resulting in the understatement of unbilled revenue (asset) and deferred credits – PGA (liability). The understatements to unbilled revenue and deferred credits – PGA totaled \$6,440 in 2010, \$6,200 in 2009, and \$6,350 in 2008. Correction of the understatements increased unbilled revenue and deferred credits – PGA by \$18,990 and \$12,550 as of December 31, 2010 and 2009, respectively. The correction had no effect on Gas Division net assets. The additional PGA recovery of \$18,990 will be refunded to customers in 2011.

The Water Division also had a restatement related to employee benefit accruals. In 2009, a new method of allocating employee benefit accruals between the Electric, Gas and Water Divisions was adopted. In 2010, a correction was made to the allocation. As a result, the Water Division beginning 2009 net asset balance was reduced by \$963 and the 2009 operation expenses increased by \$706. The 2009 Balance Sheet reflects an increase of \$1,669 in current and non-current liabilities.

### Events occurring after reporting date

Management has evaluated events and transactions that have occurred between December 31, 2010 and May 19, 2011, 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 2009 financial statements have been reclassified to conform to the 2010 presentation.

## 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, 2010, MLGW deposits with financial institutions were \$3,611, gas margin deposits were \$6,491, and electric margin deposits were \$621. Deposits of \$3,611 were maintained in collateralized accounts or covered by federal depository insurance, and were not exposed to custodial credit risk. The margin deposits of \$6,491 and \$621 were exposed to custodial credit risk as they were uninsured and uncollateralized.

#### *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; 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 leveraged notes, or notes linked to lagging indices or to long-term indices.



**2. Deposits and Investments (continued)**

*Investments (continued)*

The following table presents the investments and maturities of MLGW's investment portfolio as of December 31, 2010:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Remaining Maturities (in Years)</u>	
		<u>Maturities &lt; 1 year</u>	<u>Maturities 1 to 5 years</u>
U.S. Treasuries	\$ 18,108	\$ 2,527	\$ 15,581
Federal Agency (Fixed Rate)	15,731	6,074	9,657
Corporate Bonds/Notes (medium term)	11,933	3,485	8,448
Asset - Backed Securities	28,785	105	28,680
Money Market Mutual Funds	92,703	92,703	-
Commercial Paper (Rated AA or higher)	127,382	127,382	-
Securities held by Brokers-Dealers under Securities Loans for Cash Collateral:			
U.S. Treasuries	50,331	-	50,331
Federal Agency (Fixed Rate)	8,440	1,014	7,426
Corporate Bonds/Notes (medium term)	4,050	1,318	2,732
<b>Total Investments</b>	<b>\$ 357,463</b>	<b>\$ 234,608</b>	<b>\$ 122,855</b>

*Custodial credit risk* for investments is the risk that, in the event of failure of the counterparty to a transaction, MLGW will not be able to recover the value of its investment or collateral securities that are in the possession of another party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government, and are held by either the counterparty, or the counterparty's trust department or agent but not in the name of MLGW. Investments in external investment pools and in open-end mutual funds are not exposed to custodial credit risks because their existence is not evidenced by securities that exist in physical or book entry form. The underlying securities for securities on loan are not subject to custodial credit risk because the collateral for those loans is reported 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 as of December 31, 2010 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.



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## 2. Deposits and Investments (continued)

### Interest Rate Risk (continued)

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, 2010, 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 and government mortgage-backed securities are most sensitive to changes in interest rates as their repayments can vary significantly with interest rate changes. These securities represent 8.1% of the total investment portfolio with a fair market value of \$28,948 as of December 31, 2010.

### 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 \$172,150, or 48.2% of total investments. Of this amount, \$132,290 has a remaining maturity of one year or less.



2. Deposits and Investments (continued)

Credit Risk (continued)

MLGW's ratings and policy limits as of December 31, 2010 are as follows:

Investment Type	Fair Value	S&P Rating	Moody Rating
Corporate Bonds/Notes	\$ 2,024	AAA	Aaa
Corporate Bonds/Notes	795	AA+	Aaa
Corporate Bonds/Notes	757	AA+	Aa1
Corporate Bonds/Notes	5,129	AA+	Aa2
Corporate Bonds/Notes	1,018	A+	Aa2
Corporate Bonds/Notes	2,245	AA	Aa1
Corporate Bonds/Notes	1,486	AA	Aa2
Corporate Bonds/Notes	1,008	AA	Aa3
Corporate Bonds/Notes	509	AA-	Aa1
Corporate Bonds/Notes	512	AA-	Aa3
Corporate Bonds/Notes	500	AA-	A1
Asset-Backed Securities	19,116	AAA	Aaa
Asset-Backed Securities	4,183	AAA	NA
Asset-Backed Securities	5,486	NA	Aaa
Commercial Paper	20,898	AAA	Aaa
Commercial Paper	18,098	AA+	Aa2
Commercial Paper	35,097	AA	Aa1
Commercial Paper	18,692	AA	Aa2
Commercial Paper	9,499	AA-	Aa1
Commercial Paper	25,098	AA-	Aa3
<b>Total credit risk debt securities</b>	172,150		
U.S. Treasuries	58,699	AAA	Aaa
U.S. Treasuries	12,999 <sup>1</sup>	AAA	Aaa
U.S. Treasuries (explicitly guaranteed)	9,740	AAA	Aaa
Federal Agency (Fixed Rate)	24,008	AAA	Aaa
Federal Agency (Fixed Rate)	79,704 <sup>2</sup>	AAA	Aaa
Federal Agency (Fixed Rate - implicitly guaranteed)	163	AAA	Aaa
<b>U.S. Government and Agencies</b>	185,313		
<b>Total debt securities investments</b>	<b>\$ 357,463</b>		

Non-Rating Description	
NA	Not Available

<sup>1</sup> Money Market Treasury Fund primarily consists of U.S. Treasury securities.

<sup>2</sup> Government/Agency Money Market Fund primarily consists of U.S. government/agencies securities.



**2. Deposits and Investments (continued)**

**Concentration of Credit Risk**

*Concentration of credit risk* is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Investments in any one issuer that represent five percent or more of total investments must be disclosed by amount and issuer. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement.

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, 2010, the investments in any one issuer of commercial paper and corporate bonds that represents 5% or more of MLGW's investments are as follows:

<b>Issuer</b>	<b>Reported Amount</b>	<b>Percentage of Portfolio</b>
United Parcel Service	\$ 22,598	6.3%
General Electric	22,226	6.2%
Toyota Motor Credit	20,697	5.8%
Chevron Corporation	19,420	5.4%
<b>Total</b>	<b>\$ 84,941</b>	



## 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, 2010, 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.

As of December 31, 2010, MLGW had no credit risk exposure to borrowers because the amounts MLGW owed the borrowers exceeded the amounts the borrowers owed MLGW. The borrower is required to deliver additional collateral when necessary so that the total collateral held by the Agent for all loans to the borrower will at least equal the market value of the securities without a borrower default. MLGW does not have the ability to pledge or sell collateral securities without a borrower default. 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.

During fiscal year 2008, losses in the financial market affected the securities lending collateral pool held by The Northern Trust Company. The securities lending collateral pool has relatively high levels of overnight liquid and high-quality assets, but the unprecedented market events drove the markets into a highly illiquid condition. The impact of the highly illiquid market caused a decline in the market value of the securities lending collateral pool, resulting in a collateral deficiency declared on September 19, 2008. As of December 31, 2009, MLGW had an outstanding collateral deficiency liability of \$107.



## 2. Deposits and Investments (continued)

### Securities Lending (continued)

On March 18, 2010, Northern Trust reversed the MLGW collateral deficiency liability of \$107, due to the improved market conditions in the securities lending collateral pool. MLGW had no collateral deficiency liability at year-end.

As of December 31, 2010, MLGW investments held by broker-dealers under securities loans consist of the following:

Securities on Loan	Market Value of Securities on Loan				Cash Collateral Received			
	Electric Division	Gas Division	Water Division	Total	Electric Division	Gas Division	Water Division	Total
U.S. Agencies	\$ 4,829	\$ 2,900	\$ 711	\$ 8,440	\$ 5,004	\$ 3,006	\$ 736	\$ 8,746
U.S. Corporate Fixed	2,317	1,392	341	4,050	2,439	1,464	359	4,262
U.S. Government Fixed	28,799	17,294	4,238	50,331	29,447	17,682	4,333	51,462
<b>Total</b>	<b>\$ 35,945</b>	<b>\$ 21,586</b>	<b>\$ 5,290</b>	<b>\$ 62,821</b>	<b>\$ 36,890</b>	<b>\$ 22,152</b>	<b>\$ 5,428</b>	<b>\$ 64,470</b>

### Restricted and Unrestricted Funds

Restricted funds, cash and cash equivalents, and investments consisted of the following as of December 31, 2010 and 2009:

	Electric Division		Gas Division		Water Division	
	2010	2009	2010	2009	2010	2009
Restricted funds:						
Cash and cash equivalents	\$ 44,219	\$ 47,319	\$ 11,736	\$ 18,932	\$ 9,650	\$ 19,706
Investments	9,659	6,351	3,065	2,366	4,019	2,952
Total restricted funds	<b>\$ 53,878</b>	<b>\$ 53,670</b>	<b>\$ 14,801</b>	<b>\$ 21,298</b>	<b>\$ 13,669</b>	<b>\$ 22,658</b>
Unrestricted funds:						
Cash and cash equivalents	\$ 84,374	\$ 108,592	\$ 71,621	\$ 81,576	\$ 9,872	\$ 8,831
Investments	63,112	45,505	50,083	33,026	7,439	3,714
Total unrestricted funds	<b>\$ 147,486</b>	<b>\$ 154,097</b>	<b>\$ 121,704</b>	<b>\$ 114,602</b>	<b>\$ 17,311</b>	<b>\$ 12,545</b>



### 3. Long-Term Receivables

The Electric Division had an unsecured note receivable from a government agency, which totaled \$1,106 as of December 31, 2009. Interest was earned at a fixed rate of 7.723% per annum. The note provided for monthly payments of principal and interest and matured August 1, 2010. The note receivable secured an Electric Division note payable (see Note 8). This note was paid in full in August 2010.

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

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

2011	\$ 1,712
2012	1,712
2013	1,712
2014	1,712
2015	1,712
Thereafter	1,140
	<u>\$ 9,700</u>

The Valero lease receivable is included in notes receivable in the accompanying 2010 Gas Division’s balance sheet, except for the current portion of \$1,712, which is included in other current assets.



#### 4. Utility Plant

Utility plant activity for the years ended December 31, 2010 and 2009 is as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
<b>Year ended December 31, 2010</b>				
<b>Electric Division</b>				
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:				
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	1,339,183	59,543	(10,533)	1,388,193
Less accumulated depreciation	(541,917)	(46,099)	15,808	(572,208)
Total capital assets being depreciated, net	797,266	13,444	5,275	815,985
Total capital assets, net	\$ 908,976	\$ 75,051	\$ (54,626)	\$ 929,401
<b>Gas Division</b>				
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:				
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	522,933	15,509	(5,041)	533,401
Less accumulated depreciation	(244,377)	(15,252)	5,306	(254,323)
Total capital assets being depreciated, net	278,556	257	265	279,078
Total capital assets, net	\$ 295,496	\$ 19,435	\$ (15,244)	\$ 299,687



**4. Utility Plant (continued)**

	Beginning Balance	Increases	Decreases	Ending Balance
<b>Year ended December 31, 2010</b>				
<b>Water Division</b>				
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	<u>18,201</u>	<u>11,822</u>	<u>(15,084)</u>	<u>14,939</u>
Capital assets being depreciated:				
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	<u>423,936</u>	<u>15,084</u>	<u>(5,517)</u>	<u>433,503</u>
Less accumulated depreciation	(179,244)	(12,563)	5,882	(185,925)
Less acquisition adjustment	(9,152)	964	-	(8,188)
Total capital assets being depreciated, net	<u>235,540</u>	<u>3,485</u>	<u>365</u>	<u>239,390</u>
Total capital assets, net	<u>\$ 253,741</u>	<u>\$ 15,307</u>	<u>\$ (14,719)</u>	<u>\$ 254,329</u>
<b>Year ended December 31, 2009 (Restated)</b>				
<b>Electric Division</b>				
Capital assets not being depreciated:				
Land	\$ 28,887	\$ 667	\$ -	\$ 29,554
Land – Non-utility	15,345	-	-	15,345
Construction in progress	59,775	59,556	(52,520)	66,811
Total capital assets not being depreciated	<u>104,007</u>	<u>60,223</u>	<u>(52,520)</u>	<u>111,710</u>
Capital assets being depreciated:				
Structures and improvements	54,801	490	(33)	55,258
Transmission and distribution plant equipment	1,102,250	47,005	(10,760)	1,138,495
General plant equipment	144,527	4,358	(3,455)	145,430
Total capital assets being depreciated	<u>1,301,578</u>	<u>51,853</u>	<u>(14,248)</u>	<u>1,339,183</u>
Less accumulated depreciation	(514,780)	(47,334)	20,197	(541,917)
Total capital assets being depreciated, net	<u>786,798</u>	<u>4,519</u>	<u>5,949</u>	<u>797,266</u>
Total capital assets, net	<u>\$ 890,805</u>	<u>\$ 64,742</u>	<u>\$ (46,571)</u>	<u>\$ 908,976</u>



4. Utility Plant (continued)

	Beginning Balance	Increases	Decreases	Ending Balance
<b>Year ended December 31, 2009</b>				
<b>Gas Division</b>				
Capital assets not being depreciated:				
Land	\$ 7,302	\$ 200	\$ -	\$ 7,502
Land – Non-utility	66	-	-	66
Construction in progress	10,920	16,512	(18,272)	9,160
Plant held for future use	212	-	-	212
Total capital assets not being depreciated	18,500	16,712	(18,272)	16,940
Capital assets being depreciated:				
Structures and improvements	54,016	1,810	(895)	54,931
Processing and distribution plant equipment	399,563	13,294	(8,914)	403,943
General plant equipment	63,080	2,968	(2,189)	63,859
Non-utility plant equipment	200	-	-	200
Total capital assets being depreciated	516,859	18,072	(11,998)	522,933
Less accumulated depreciation	(240,716)	(15,959)	12,298	(244,377)
Total capital assets being depreciated, net	276,143	2,113	300	278,556
Total capital assets, net	\$ 294,643	\$ 18,825	\$ (17,972)	\$ 295,496
<b>Water Division</b>				
Capital assets not being depreciated:				
Land	\$ 3,269	\$ 35	\$ -	\$ 3,304
Construction in progress	15,870	13,732	(14,705)	14,897
Total capital assets not being depreciated	19,139	13,767	(14,705)	18,201
Capital assets being depreciated:				
Structures and improvements	47,272	592	(45)	47,819
Pumping, transmission and distribution plant equipment	298,623	11,051	(972)	308,702
General plant equipment	66,065	3,027	(1,677)	67,415
Total capital assets being depreciated	411,960	14,670	(2,694)	423,936
Less accumulated depreciation	(169,668)	(12,789)	3,213	(179,244)
Less acquisition adjustment	(10,116)	964	-	(9,152)
Total capital assets being depreciated, net	232,176	2,845	519	235,540
Total capital assets, net	\$ 251,315	\$ 16,612	\$ (14,186)	\$ 253,741



#### 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 2011 are estimated as follows (unaudited):

Electric Division	\$ 81,173
Gas Division	23,747
Water Division	19,010

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.



**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, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Retirees and beneficiaries receiving benefits	2,495	2,478
Terminated plan members entitled to but not yet receiving benefits	41	47
Active members fully vested	1,153	1,143
Active members not vested	<u>1,447</u>	<u>1,478</u>
Total	<u><u>5,136</u></u>	<u><u>5,146</u></u>

**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 2010, MLGW contributed 17.8% of the annual covered payroll.



**5. Employee Retirement System (continued)**

**Annual Pension Cost and Net Pension Obligation**

MLGW's annual pension cost ("APC") and net pension asset for the MLGW Pension Plan consisted of the following for fiscal year 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Annual required contribution ("ARC")	\$ 27,381	\$ 22,401
Interest on net pension asset	(1,248)	(1,368)
Adjustment to annual required contribution	<u>1,814</u>	<u>1,951</u>
Annual pension cost	27,947	22,984
Contributions made	<u>(27,385)</u>	<u>(21,388)</u>
Change in net pension asset	562	1,596
Net pension asset at beginning of fiscal year	(16,641)	(18,237)
Net pension asset at end of fiscal year	<u><u>\$ (16,079)</u></u>	<u><u>\$ (16,641)</u></u>

**Three-Year Trend Information**

<u>Fiscal Year Ending</u>	<u>Annual Pension Cost</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation (Asset)</u>
December 31, 2010	\$ 27,947	98.0%	\$ (16,079)
December 31, 2009	22,984	93.1%	(16,641)
December 31, 2008	10,913	169.2%	(18,237)

**Funded Status and Funding Progress**

As of January 1, 2011, the most recent actuarial valuation date, the MLGW Pension Plan was 88.5% funded. The actuarial accrued liability ("AAL") for benefits was \$1,324,410, and the actuarial value of assets was \$1,171,384, resulting in an unfunded actuarial accrued liability ("UAAL") of \$153,027. The covered payroll (annual payroll of active employees covered by the pension plan) was \$153,509, and the ratio of the UAAL to the covered payroll was 99.7%.



**5. Employee Retirement System (continued)**

**Funded Status and Funding Progress (continued)**

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

**Actuarial Methods and Assumptions**

The annual required contribution for the current year was determined as part of the January 1, 2011 actuarial valuation using the entry age normal cost method. Actuarial methods and significant assumptions were as follows:

<b>Valuation Date</b>	January 1, 2011
<b>Actuarial Cost Method</b>	Entry Age Normal Cost Method
<b>Amortization Method</b>	Level percentage of pay
<b>Remaining Amortization Period</b>	30 years as of January 1, 2011, closed
<b>Asset Valuation Method</b>	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.
<b>Actuarial Assumptions:</b>	
<b>Investment Rate of Return</b>	7.50%
<b>Inflation Rate</b>	3.25%
<b>Projected Salary Increases</b>	Inflation plus merit increases that vary by age and service
<b>Cost of Living Adjustments</b>	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 health care, life insurance, accident/death and dismemberment (AD&D), medical and prescription drug benefits 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 paid 100% by the retiree.

Employees retired under the MLGW Pension Plan, or disabled with five years of service at any age, or disabled in the line of duty at any age with no years of service restriction are eligible for OPEB benefits. Health care benefits are also offered to qualifying survivors of active employees who are eligible to retire at the time of death. Currently, 4,068 retirees and beneficiaries are receiving postemployment benefits.



**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 2010, employer contributions were \$43,476 to the Plan. Plan members receiving benefits contributed \$4,763 through their required contribution of \$43.77 to \$431.29 (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 2011, 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, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Annual required contribution	\$ 43,693	\$ 55,340
Interest on net OPEB asset	(188)	-
Adjustment to annual required contribution	<u>146</u>	<u>-</u>
Annual OPEB cost	43,651	55,340
Contributions made	<u>(43,476)</u>	<u>(55,688)</u>
Change in net OPEB asset	175	(348)
Net OPEB asset at beginning of fiscal year	<u>(2,500)</u>	<u>(2,152)</u>
Net OPEB asset at end of fiscal year	<u>\$ (2,325)</u>	<u>\$ (2,500)</u>



**7. Other Postemployment Benefits (continued)**

MLGW's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for fiscal year 2010 and the two preceding years were as follows:

<b>Fiscal Year Ended</b>	<b>Annual OPEB Cost</b>	<b>Percentage of Annual OPEB Cost Contributed</b>	<b>Net OPEB Obligation (Asset)</b>
December 31, 2010	\$ 43,651	99.6%	\$ (2,325)
December 31, 2009	55,340	100.6%	(2,500)
December 31, 2008	57,991	115.3%	(2,152)

**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 304.54%.

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



**7. Other Postemployment Benefits (continued)**

**Actuarial Methods and Assumptions**

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

<b>Valuation Date</b>	December 31, 2009
<b>Actuarial Cost Method</b>	Entry Age Normal
<b>Amortization Method</b>	Level percent of pay, 30 years
<b>Remaining Amortization Period</b>	27 years as of December 31, 2009
<b>Asset Valuation Method</b>	Market value
<b>Actuarial Assumptions:</b>	
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



## 8. Debt

Long-term debt as of December 31, 2010 and 2009 consists of the following:

	<b>Interest Rates</b>	<b>2010</b>	<b>2009</b>
Electric Division:			
Electric System Revenue Bonds:			
Series 2002, due serially 2009-2010	4.00-5.00%	\$ -	\$ 5,855
Series 2003A, due serially 2009-2018	3.00-5.00%	<b>291,325</b>	849,380
Series 2008, due serially 2009-2018	4.00-5.00%	<b>96,930</b>	96,930
Series 2010, due serially 2014-2018	2.50-5.00%	<b>460,050</b>	
Premium on revenue bonds		<b>70,961</b>	49,930
Unamortized deferred cost on bond refunding		<b>(21,559)</b>	(56)
Total		<b>897,707</b>	1,002,039
Note payable with bank, due serially through 2010	7.58%	-	1,499
		<b>897,707</b>	1,003,538
Less: current portion of bonds and notes payable		<b>(90,420)</b>	(93,848)
		<b>\$ 807,287</b>	\$ 909,690
Water Division:			
Revenue Refunding Bonds:			
Series 1998, due serially 2009-2012	4.15-5.25%	\$ 1,625	\$ 3,165
Premium on revenue bonds		2	7
Unamortized deferred cost on bond refunding		<b>(15)</b>	(45)
		<b>1,612</b>	3,127
Less: current portion of bonds and notes payable		-	-
		<b>\$ 1,612</b>	\$ 3,127

Principal payments on bonds are due annually on January 1 or December 1. Debt service requirements, including notes payable, as of December 31, 2010, are as follows:

	<b>Electric Division</b>		<b>Water Division</b>	
	<b>Principal</b>	<b>Interest</b>	<b>Principal</b>	<b>Interest</b>
2011	90,420	41,462	-	43
2012	95,190	37,027	1,625	43
2013	99,700	32,290	-	-
2014	102,765	27,431	-	-
2015	107,775	22,417	-	-
2016-2018	352,455	34,483	-	-
Total	<b>\$ 848,305</b>	<b>\$ 195,110</b>	<b>\$ 1,625</b>	<b>\$ 86</b>

MLGW, at its option, may redeem bonds prior to maturity at premiums and prices specified in the indentures. The Series 2003A and Series 2008 bonds are subject to mandatory redemption upon early termination of the Supplement to the Power Contract ("Supplement") with TVA as discussed in Note 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. 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, and bore interest for 35-day auction periods. The Series 2003B revenue bonds were refunded in 2008, as discussed above.

During 2002, the Electric Division issued \$41,625 in revenue bonds to refund \$41,905 of Series 1993 revenue bonds. The refunding was undertaken to reduce total future debt service payments. The reacquisition price exceeded the net carrying value of the old debt by \$462. This amount is netted against the carrying value of the new debt and is being amortized over the life of the new debt, which was shorter than the life of the refunded debt.

MLGW's Electric Division bond covenants require that for Series 2002 Bonds, the ratio of net revenues available for debt service to the maximum amount of principal and interest for any fiscal year ("electric coverage") must not be less than 1.20. For Series 2003A, 2008, 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, 2010, was 1.91.

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, 2010, was 8.24.

MLGW buys and stores natural gas during the off-season (summer) to use in the upcoming winter months. In July 2009, the Gas Division issued a revenue anticipation note in the amount of \$15,000 with a yield rate of 1.25% to provide funds for the purchase of gas and related storage. The note was repaid in full on March 31, 2010.



**8. Debt (continued)**

Long-term debt activity for the years ended December 31, 2010 and 2009 was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
<b>Year ended December 31, 2010:</b>				
<b>Electric Division</b>				
Bonds and notes 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 notes payable	<u>\$ 1,003,538</u>	<u>\$ 505,217</u>	<u>\$ (611,048)</u>	<u>\$ 897,707</u>
<b>Water Division</b>				
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	<u>\$ 3,127</u>	<u>\$ -</u>	<u>\$ (1,515)</u>	<u>\$ 1,612</u>
<b>Year ended December 31, 2009:</b>				
<b>Electric Division</b>				
Bonds and notes payable:				
Revenue bonds	\$ 1,040,010	\$ -	\$ (87,845)	\$ 952,165
Premium on revenue bonds	60,800	-	(10,870)	49,930
Note payable	3,020	-	(1,521)	1,499
Less deferred amounts:				
For issuance discounts and on refunding	(154)	-	98	(56)
Total bonds and notes payable	<u>\$ 1,103,676</u>	<u>\$ -</u>	<u>\$ (100,138)</u>	<u>\$ 1,003,538</u>
<b>Water Division</b>				
Bonds payable:				
Revenue bonds	\$ 7,865	\$ -	\$ (4,700)	\$ 3,165
Premium on revenue bonds	5	2	-	7
Less deferred amounts:				
For issuance discounts and on refunding	(89)	-	44	(45)
Total bonds payable	<u>\$ 7,781</u>	<u>\$ 2</u>	<u>\$ (4,656)</u>	<u>\$ 3,127</u>



## 9. Insurance Reserves for Medical Benefits and Injuries and Damages

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

The changes in the self-insurance reserves for medical benefits and injuries and damages for the years ended December 31, 2010 and 2009 are as follows:

	<u>Medical Benefits</u>			<u>Injuries and Damages</u>		
	<u>Electric Division</u>	<u>Gas Division</u>	<u>Water Division</u>	<u>Electric Division</u>	<u>Gas Division</u>	<u>Water Division</u>
Balance – December 31, 2008	\$ 6,594	\$ 3,110	\$ 1,859	\$ 6,969	\$ 2,024	\$ 2,008
Payments	(25,487)	(11,368)	( 7,549)	(2,045)	(944)	(972)
Incurred claims expense	23,393	10,433	6,928	1,239	1,234	814
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	<u>\$ 4,296</u>	<u>\$ 1,916</u>	<u>\$ 1,272</u>	<u>\$ 6,729</u>	<u>\$ 2,511</u>	<u>\$ 1,560</u>

## 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 (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 June 2006, Public Energy Authority of Kentucky, Inc. (“PEAK”) and MLGW entered into a 5 year gas purchase contract with 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 rate adjustment effective with the October 2009 revenue month, increasing the cost of wholesale power purchased by MLGW by approximately 9.0%. MLGW implemented changes to its retail rate schedules effective with meters read on or after September 30, 2009, 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 7.2% for residential, 7.7% for commercial customers and 8.6% 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 who are not on interruptible rate schedules. The FCA was a quarterly adjustment until the October 2009 revenue month, when TVA changed to a monthly adjustment.

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

In 2010, the Council approved a water rate increase effective with meters read on or after January 3, 2011. The retail impact is 5%.

## 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 actions arising on or after July 1, 2007, for personal injuries are \$300 per person and \$700 for two or more persons per accident. Property damages are limited to \$100 per accident.

## 14. Commitments and Contingencies

The Electric and Gas Divisions have 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 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.



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## 15. Federal Grant Contributions

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, including a \$319 addition to plant for capital asset replacement and \$279 in Electric Division operating and maintenance expenses. 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). Of this \$538, \$287 was accounted for as a contribution in aid of construction in the Electric Division and \$251 as other income. In December 2010, the Electric Division received a payment of \$20 from FEMA leaving a balance of \$518. The Gas Division incurred total costs of \$5 to remove and replace a gas main damaged due to flooding. These costs include \$4 for addition to Gas Division plant for capital asset replacement and \$1 in Gas Division operating and maintenance expenses. MLGW Gas Division has been approved to receive \$5 (or 90%) reimbursement of eligible expenses from FEMA. Of this \$5, \$3 was accounted for as a contribution in aid of construction in the Gas Division and \$2 as other income. In December 2010, a payment of \$4 was received from FEMA leaving a remaining balance of \$1.

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 result of the storms were \$8,505, which includes a \$4,973 addition to plant for capital asset replacement and \$3,532 in Electric Division operating and maintenance expenses. Insurance proceeds in the amount of \$100 for these expenditures are accounted for as a contribution in aid of construction for the Electric Division. MLGW was approved to receive reimbursement from FEMA (Contract 34101-0000001983) totaling \$5,932 (or 75%) of eligible expenses. Of this \$5,932, \$3,331 was accounted for as a contribution in aid of construction in the Electric Division and \$2,601 as other income. In March 2010, a partial payment of \$4,453 was received from FEMA, leaving a balance as of December 31, 2010 of \$1,479. In January 2011, FEMA closed out the contract with an immaterial adjustment.

During February 2008, severe storms and tornadoes caused damage to transmission towers, one substation and portions of MLGW's electric distribution system. Also, as a result of the storms, additional expenses were incurred for the operation of the water pumping stations during the period of the electrical power outage. MLGW was approved to receive reimbursement from FEMA (Contract 34101-0000000525) totaling \$2,389 (or 75%) of eligible expenses for the Electric Division and \$25 (or 75%) of eligible expenses for the Water Division. In November 2008, the Electric Division received reimbursement from FEMA for \$2,318, leaving a balance as of December 31, 2009 of \$71. Final payment was received by the Electric Division in March 2010. In August 2008, the Water Division received a partial payment of \$19 leaving a balance as of December 31, 2009 of \$6. Final payment was received by the Water Division in March 2010.



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## 15. Federal Grant Contributions (continued)

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 2010 expenditures totaled \$522 with \$392 (or 75%) eligible for federal reimbursement. Fiscal year 2009 expenditures totaled \$548, with \$411 (or 75%) eligible for federal reimbursement. Fiscal year 2008 expenditures totaled \$19, with \$14 (or 75%) eligible for federal reimbursement. As of December 31, 2009, receivables of \$411 were included in accounts receivable. A reimbursement of \$429 was received in April 2010. As of December 31, 2010, the total receivable balance for the High Voltage Transformer Seismic Retrofit Project is \$388.

In September 2009, MLGW determined that the Sheahan Water Plant Seismic Retrofit Project (Contract GR-07-20788-000), approved under the Pre-Disaster Mitigation Competitive Program in 2006, was no longer cost effective and should be discontinued. MLGW informed the Tennessee Emergency Management Agency (“TEMA”) of its decision and requested final payment along with formal closeout notification. As of December 31, 2009, the total eligible project expenditures incurred were \$297, of which \$223 (or 75%) qualified for federal reimbursement. Federal share payments received as of December 2009 totaled \$110, leaving the remaining receivable balance of \$113. The final payment of \$113 was received March 2010.

In 2009, MLGW applied for the Smart Grid Investment Grant (Contract DE-OE0000281) under the American Recovery and Reinvestment 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. As of December 31, 2010, expenditures totaled \$711, of which \$341 (or 48%) qualified for federal reimbursement. Federal share payments received as of December 2010 total \$164, leaving the remaining receivable balance of \$177.

In 2009, the City of Memphis, in conjunction with MLGW, applied for a grant under the 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. Planning began, but no funds were expended in 2009. As of December 31, 2010, MLGW had expended \$966 with \$966 reimbursed and receivables totaling \$0.



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## 16. Pollution Remediation Obligation

Accounting and financial standards for pollution remediation obligations are in accordance with the provisions of GASB Statement No. 49, *Pollution Remediation Obligations*.

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 U.S. Environmental Protection Agency for violations of Section 6(e) of TSCA, 15 U.S.C. § 2605. The liability for PCB's also includes removal and disposal of other transformers and equipment that meet the criteria for pollution remediation. These costs are based on past experience and assume no expected change orders.

In July 2009, MLGW was notified by the Tennessee Department of Environmental 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 the TDEC agency. After approval of the plan, MLGW obtained an estimate from a licensed contractor to perform the necessary activities.

As provided by GASB 49, MLGW annually reevaluates its liability to measure the scope of current conditions, evaluate remediation plan changes and adhere to changes in legal or regulatory requirements. Regulatory accounts are used to capture the net effect of the changes in estimates for each Division. See Note 1, Regulatory Accounting.



**16. Pollution Remediation Obligation (continued)**

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

	<u>12/31/2010</u>	<u>12/31/2009</u>
Electric		
PCB	\$ 2,327	\$ 4,613
Asbestos	1,440	1,127
Lead	9,979	9,666
Storm Water	900	998
<b>Total Electric</b>	<b>14,646</b>	<b>16,404</b>
Gas		
Asbestos	183	246
Lead	2,495	1,450
Storm Water	345	363
<b>Total Gas</b>	<b>3,023</b>	<b>2,059</b>
Water		
Mold	-	80
Asbestos	1,304	1,250
Lead	4,153	4,310
Storm Water	255	327
<b>Total Water</b>	<b>5,712</b>	<b>5,967</b>
<b>Total Liability</b>	<b>\$ 23,381</b>	<b>\$ 24,430</b>
Total PCB	\$ 2,327	\$ 4,613
Total Mold	-	80
Total Asbestos	2,927	2,623
Total Lead	16,627	15,426
Total Storm Water	1,500	1,688
<b>Total Liability</b>	<b>\$ 23,381</b>	<b>\$ 24,430</b>

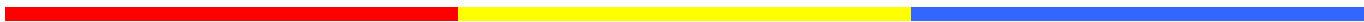


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**17. Subsequent Event (April 2011 Storms and May 2011 Flooding)**

On several occasions in April of 2011, storm systems passed through the service area causing damage and outages to the electric transmission and distribution systems of MLGW. In addition, near record high levels of the Mississippi River in May 2011 caused localized flood damage. A preliminary estimate of the financial cost of these storms and flooding is approximately \$9,000. It is estimated that 75% of this cost will be recovered through FEMA reimbursement.

**SCHEDULE OF ADDITIONS AND  
RETIREMENTS TO UTILITY PLANT  
DECEMBER 31, 2010  
(Dollars in Thousands)**



	<u>Electric Division</u>	<u>Gas Division</u>	<u>Water Division</u>
Utility plant in service, December 31, 2009	\$ 1,368,737	\$ 530,235	\$ 418,088
Additions- Construction	59,901	15,509	15,084
Additions – Acquisition Adjustment			964
Retirements	<u>(10,533)</u>	<u>(5,041)</u>	<u>(5,517)</u>
<b>Utility plant in service, December 31, 2010</b>	<b><u>\$ 1,418,105</u></b>	<b><u>\$ 540,703</u></b>	<b><u>\$ 428,619</u></b>

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

**SCHEDULE OF DEPOSITS AND INVESTMENTS**  
**DECEMBER 31, 2010**  
(Dollars in Thousands)



	<u>ACCRUAL YIELD</u>	<u>MATURITY DATE</u>	<u>FAIR VALUE</u>
<b>COMMERCIAL PAPER</b>			
Chevron Funding Corp.	0.150	01/03/2011	\$ 5,499
Chevron Funding Corp.	0.170	01/03/2011	4,099
Exxon Mobile	0.120	01/03/2011	4,999
Exxon Mobile	0.120	01/03/2011	7,299
Exxon Mobile	0.100	01/03/2011	2,599
Gen Elec Cap Corp.	0.120	01/03/2011	1,000
Gen Elec Cap Corp.	0.150	01/03/2011	2,400
Gen Elec Cap Corp.	0.120	01/03/2011	1,600
Toyota Motor Credit	0.130	01/03/2011	2,700
Toyota Motor Credit	0.100	01/03/2011	3,000
Toyota Motor Credit	0.130	01/03/2011	3,999
Toyota Motor Credit	0.130	01/03/2011	2,200
United Parcel Service	0.100	01/03/2011	12,199
United Parcel Service	0.100	01/03/2011	5,999
United Parcel Service	0.100	01/03/2011	1,900
Gen Elec Cap Corp.	0.120	01/07/2011	4,700
Gen Elec Cap Corp.	0.120	01/07/2011	1,100
United Parcel Service	0.010	01/07/2011	2,500
KFW	0.140	01/18/2011	4,999
Royal Bank of Canada	0.130	01/18/2011	9,499
Exxon Mobile	0.130	01/20/2011	1,000
Gen Elec Cap Corp.	0.150	01/20/2011	2,000
Nestle Capital	0.070	01/20/2011	10,899
Procter & Gamble	0.150	01/20/2011	2,500
Toyota Motor Credit	0.130	01/20/2011	3,000
Toyota Motor Credit	0.100	01/20/2011	1,400
Gen Elec Cap Corp.	0.100	01/21/2011	3,500
Nestle Capital	0.030	01/21/2011	5,500
Chevron Funding Corp.	0.140	01/25/2011	5,299
Chevron Funding Corp.	0.120	01/25/2011	3,800
Gen Elec Cap Corp.	0.130	01/25/2011	1,800
Toyota Motor Credit	0.100	01/25/2011	2,396
			<u>\$ 127,384</u>
Fair Market Value			(2)
Total Commercial Paper			<u>\$ 127,382</u>
<b>MONEY MARKET MUTUAL FUNDS</b>			
Northern Institutional Government Select Funds			\$ 79,704
Federated Treasury Obligations FD 398			<u>12,999</u>
Total Money Market Mutual Funds			<u>\$ 92,703</u>

**SCHEDULE OF DEPOSITS AND INVESTMENTS**  
**DECEMBER 31, 2010**  
(Dollars in Thousands)  
(Continued)



	<b>ACCRUAL YIELD</b>	<b>MATURITY DATE</b>	<b>FAIR VALUE</b>
<b>CASH</b>			
Bank Deposits			\$ 10,723
Total Cash			\$ 10,723
<b>ACCRUED INTEREST</b>			\$ 662
<b>TOTAL CASH AND CASH EQUIVALENTS</b>			\$ 231,470
<b>TREASURY NOTE</b>			
Fair Market Value	(0.079)	5/31/2012	\$ 501
Total Treasury Note			\$ 502
<b>U.S. GOVERNMENT BONDS</b>			
	4.750	01/31/2012	\$ 560
	3.375	11/30/2012	554
	2.375	08/31/2014	8,288
	1.750	07/31/2015	4,246
	0.625	07/31/2012	3,510
	0.500	11/30/2012	1,997
	1.000	04/30/2012	1,008
	1.000	07/31/2011	502
	2.375	02/28/2015	3,484
	2.500	04/30/2015	1,370
	4.625	07/31/2012	426
	0.375	08/31/2012	749
	1.250	08/31/2015	4,863
	3.375	07/31/2013	187
	3.125	04/30/2013	792
	2.500	03/31/2015	2,070
	2.250	01/31/2015	3,080
	0.750	05/31/2012	25,119
	1.750	11/15/2011	2,025
	2.375	09/30/2014	3,107
Total U.S. Government Bonds			\$ 67,937

**SCHEDULE OF DEPOSITS AND INVESTMENTS**  
**DECEMBER 31, 2010**  
**(Dollars in Thousands)**  
**(Continued)**



	<b>ACCRUAL YIELD</b>	<b>MATURITY DATE</b>	<b>FAIR VALUE</b>
<b>U.S. GOVERNMENT AGENCIES</b>	4.875	11/18/2011	\$ 1,559
	5.000	09/14/2012	279
	3.625	09/16/2011	1,023
	4.875	11/15/2011	104
	5.000	03/25/2011	505
	2.125	03/23/2012	3,060
	6.135	02/15/2011	201
	4.750	01/18/2011	751
	5.125	07/15/2012	2,673
	5.500	08/20/2012	2,159
	1.750	06/15/2012	1,018
	6.410	11/13/2012	1,104
	6.125	03/15/2012	1,601
	4.750	11/19/2012	2,152
	5.125	04/15/2011	1,521
	4.125	02/17/2011	502
	1.125	07/30/2012	2,017
	5.500	03/15/2011	758
	1.900	10/19/2012	1,021
Total U.S. Government Agencies			\$ 24,008

**SCHEDULE OF DEPOSITS AND INVESTMENTS**  
**DECEMBER 31, 2010**  
**(Dollars in Thousands)**  
**(Continued)**



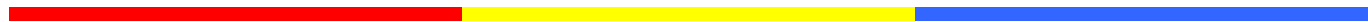
	<b>ACCRUAL YIELD</b>	<b>MATURITY DATE</b>	<b>FAIR VALUE</b>
<b>CORPORATE BONDS</b>			
Westpac Bkg Corp.	2.250	11/19/2012	\$ 512
PVTPL Dexia Cr Loc Societe	2.375	09/23/2011	757
Bank Montreal	2.125	06/28/2013	1,018
Bank N S Halifax	2.250	01/22/2013	509
Shell Intl Fin	1.300	09/22/2011	503
Shell Intl Fin	1.875	03/25/2013	508
Arden Rlty Ltd Partnership	5.200	09/01/2011	1,029
Berkshire Hathaway Fin Corp.	0.414	01/13/2012	1,001
Chevron Corp.	3.450	03/03/2012	722
Gen Elec Cap Corp.	4.800	05/01/2013	1,390
Gen Elec Cap Corp.	0.409	04/10/2012	1,198
Gen Elect Cap Corp.	2.800	01/08/2013	511
Merck & Co Inc.	1.875	06/30/2011	1,008
Met Life Global	2.875	09/17/2012	512
Private Expt Fdg Corp.	3.550	04/15/2013	795
Walmart Stores	0.750	10/25/2013	1,486
Wells Fargo & Co.	4.875	01/12/2011	500
Total Corporate Bonds			\$ 13,959
<b>ASSET-BACKED SECURITIES</b>			
Ally Auto	1.110	10/15/2014	\$ 2,495
BMW Veh Lease	1.180	04/15/2013	998
BMW Veh Lease	2.910	03/15/2012	581
CAP 1 Multi-Asset	4.850	02/18/2014	2,815
Carmax Auto Owner	1.410	02/16/2015	1,007
Chase Issuance Tr	1.810	04/15/2014	1,017
Chrysler Finl Auto	0.910	08/08/2013	1,999
Citibank Cr Card	2.250	12/23/2014	2,045
Daimler Chrysler	4.710	09/08/2012	227
Discover Card	5.100	10/15/2013	2,533
Ford Cr Auto Owner	1.210	01/15/2012	40
Ford Cr Floor Plan	1.500	09/15/2015	992
Harley-Davidson	2.620	03/15/2014	517
Harley-Davidson	2.000	07/15/2012	22
Honda Auto	0.700	04/21/2014	2,490
Hyundai Auto	2.030	08/15/2013	1,011
Hyundai Auto	1.110	02/15/2012	166
John Deere Owner	2.590	10/15/2013	826
Nissan Auto Lease	1.120	12/15/2013	1,997
Nissan Auto Lease	1.220	09/15/2011	105

**SCHEDULE OF DEPOSITS AND INVESTMENTS**  
**DECEMBER 31, 2010**  
**(Dollars in Thousands)**  
**(Continued)**



	<b>ACCRUAL YIELD</b>	<b>MATURITY DATE</b>	<b>FAIR VALUE</b>
<b>ASSET-BACKED SECURITIES</b>			
<b>(continued)</b>			
Nissan Auto	4.460	04/16/2012	261
Toyota Auto	0.750	05/15/2012	1,001
Toyota Auto	1.040	02/18/2014	1,004
Volkswagen Auto	0.990	11/20/2013	2,495
Volkswagen Auto Ln	4.500	07/20/2012	<u>141</u>
Total Asset-Backed Securities			\$ 28,785
<b>GOVERNMENT MORTGAGE- BACKED SECURITIES</b>			
Federal Home LN	4.000	06/01/2011	<u>\$ 163</u>
Total Government Mortgage-Backed Securities			\$ 163
<b>GUARANTEED FIXED INCOME</b>			
Citibank N A FDIC	1.375	08/10/2011	1,006
GMAC Inc. FDIC	1.750	10/30/2012	<u>1,018</u>
Total Guaranteed Fixed Income			<u>\$ 2,024</u>
<b>TOTAL INVESTMENTS</b>			<u>\$ 137,378</u>
<b>TOTAL CASH AND INVESTMENTS</b>			<u><u>\$ 368,849</u></u>

**SCHEDULE OF LONG TERM DEBT,  
PRINCIPAL AND INTEREST REQUIREMENTS  
DECEMBER 31, 2010  
(Dollars in Thousands)**



	<b>Series 2003A</b>		<b>Series 2008</b>		<b>Series 2010</b>	
	<b>Principal</b>	<b>Interest</b>	<b>Principal</b>	<b>Interest</b>	<b>Principal</b>	<b>Interest</b>
Electric Division:						
2011	\$ 90,420	\$ 14,270	\$ -	\$ 4,564	\$ -	\$ 22,628
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	12,418
2017	2,220	169	31,625	4,564	83,350	6,821
2018	1,950	80	65,305	3,043	55,070	2,654
<b>Total</b>	<b>\$ 291,325</b>	<b>\$ 30,101</b>	<b>\$ 96,930</b>	<b>\$ 34,991</b>	<b>\$ 460,050</b>	<b>\$ 130,019</b>

	<b>Series 1998</b>	
	<b>Principal</b>	<b>Interest</b>
Water Division:		
2011	\$ -	\$ 43
2012	1,625	43
<b>Total</b>	<b>\$ 1,625</b>	<b>\$ 86</b>

**SCHEDULE OF CURRENT UTILITY RATES  
DECEMBER 31, 2010**



<b>Electric Division Rate Class</b>	<b>Base Charge</b>	<b>Customers</b>
<u>Residential – Schedule RS</u>	Effective meters read on or after September 30, 2009.	357,856
Customer charge:	\$11.20 per month, less hydro allocation credit: \$1.71	
Energy charge:	First 2,000 kWh per month at 8.076 cents per kWh; Additional kWh per month at 8.930 cents per kWh The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>General Service – Schedule GSA</u>	Effective meters read on or after September 30, 2009. If (a) the higher of (i) the customer’s currently effective contract demand, if any, or (ii) its highest billing demand during the latest twelve-month period is not more than 50 kW, and (b) customer’s monthly energy taking for any month during such period does not exceed 15,000 kWh:	43,644
Customer charge:	\$15.52 per delivery point per month	
Energy charge:	9.291 cents per kWh  If (a) the higher of (i) the customer’s currently effective contract demand or (ii) its highest billing demand during the latest twelve-month period is greater than 50kW but not more than 1,000 kW, or (b) if the customer’s billing demand is less than 50kW and its energy takings for any month during such period exceed 15,000 kWh.	
Customer charge:	\$53.42 per delivery point per month	
Demand charge:	First 50kW of billing demand per month, no demand charge Excess over 50kW of billing demand per month, at \$13.84 per kW	
Energy charge:	First 15,000 kWh per month at 9.875 cents per kWh Additional kWh per month at 4.729 cents per kWh  If the higher of the customer’s currently effective contract demand or its highest billing demand during the latest twelve-month period is greater than 1.000 kW.	
Customer charge:	\$191.84 per delivery point per month	

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
**(Continued)**



<b>Electric Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
Demand charge:	First 1,000 kW of billing demand per month, at \$13.47 per kW Excess over 1,000 kW of billing demand per month, at \$15.47 per kW, plus an additional \$15.47 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds the higher of 2,500 kW or its contract demand	
Energy charge:	5.030 cents per kWh per month The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>General Service – Schedule GSB</u>	Effective meters read on or after September 30, 2009.	1
Customer charge:	\$1,500 per delivery point per month	
Demand charge:	\$15.85 per kW of billing demand per month, plus an additional \$15.85 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds its contract demand	
Energy charge:	First 620 hours use of metered demand per month at 4.259 cents per kWh Additional kWh per month at 3.477 cents per kWh The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>General Service – Schedule GSC</u>	Effective meters read on or after September 30, 2009.	0
Customer charge:	\$1,500 per delivery point per month	
Demand charge:	\$15.32 per kW of billing demand per month, plus an additional \$15.32 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds its contract demand	
Energy charge:	First 620 hours use of metered demand per month at 4.259 cents per kWh Additional kWh per month at 3.477 cents per kWh The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>General Service – Schedule GSD</u>	Effective meters read on or after September 30, 2009.	0
Customer charge:	\$1,500 per delivery point per month	

**SCHEDULE OF CURRENT UTILITY RATES  
DECEMBER 31, 2010  
(Continued)**



<b>Electric Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
Demand charge:	\$18.53 per kW of billing demand per month, plus an additional \$18.53 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds its contract demand	
Energy charge:	3.349 cents per kWh per month The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>Manufacturing – Schedule MSB</u>	Effective meters read on or after September 30, 2009.  If the customer's metered demand for the month is not more than 5,000 kW:	1
Customer charge:	\$1,500 per delivery point per month	
Demand charge:	\$13.61 per kW of billing demand per month, plus an additional \$13.61 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds its contract demand	
Energy charge:	First 620 hours use of metered demand per month at 3.611 cents per kWh Additional kWh per month at 2.947 cents per kWh  If the customer's metered demand for the month is greater than 5,000 kW:	
Customer charge:	\$1,500.00 per delivery point per month	
Demand charge:	\$12.93 per kW billing demand per month, plus an additional \$12.93 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds its contract demand	
Energy charge:	First 620 hours use of metered demand per month at 3.431 cents per kWh Additional kWh per month at 2.803 cents per kWh The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>Manufacturing – Schedule MSC</u>	Effective meters read on or after September 30, 2009.	0
Customer charge:	\$1,500 per delivery point per month	
Demand charge:	\$12.40 per kW of billing demand per month, plus an additional \$12.40 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds its contract demand	

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
**(Continued)**



<b>Electric Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
Energy charge:	First 620 hours use of metered demand per month at 3.431 cents per kWh Additional kWh per month at 2.803 cents per kWh The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>Manufacturing – Schedule MSD</u>	Effective meters read on or after September 30, 2009.	0
Customer charge:	\$1,500 per delivery point per month	
Demand charge:	\$14.95 per kW of billing demand per month, plus an additional \$14.95 per kW per month for each kW, if any, of the amount by which the customer’s billing demand exceeds its contract demand	
Energy charge:	2.708 cents per kWh per month The above rates are subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>Time-Of-Day – Schedule TGSA</u>	Effective meters read on or after September 30, 2009.	1
	If the higher of (1) the higher of the customer’s currently effective onpeak or offpeak contract demand or (2) its highest onpeak or offpeak billing demand during the latest 12 month period is not more than 50 kW:	
Customer charge:	\$198.95 per delivery point per month.	
Energy charge:	16.014 cents per kWh per month for all onpeak kWh 5.137 cents per kWh per month for all offpeak kWh  If the higher of (1) the higher of the customer’s currently effective onpeak or offpeak contract demand or (2) the customer’s highest onpeak or offpeak billing demand during the latest 12-month period is greater than 50 kW but no more than 1,000 kW.	
Customer charge:	\$198.95 per delivery point per month.	
Demand charge:	\$14.20 per kW of the customer’s onpeak billing demand, plus \$4.16 per month for each kW, if any, of the amount by which the customer’s offpeak billing demand exceeds its onpeak billing demand.	
Energy charge:	6.636 cents per kWh per month for all onpeak kWh 4.217 cents per kWh per month for all offpeak kWh  If the higher of (1) the higher of the customer’s currently effective onpeak or offpeak contract demand or (2) the customer’s highest onpeak or offpeak billing demand during the latest 12-month period is greater than 1,000 kW:	

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
**(Continued)**



<b>Electric Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
Customer charge:	\$198.95 per delivery point per month	
Demand charge:	\$15.05 per kW per month of the customer's onpeak billing demand, plus \$3.01 per month for each kW, if any, of the amount by which the customer's offpeak billing demand exceeds its onpeak billing demand, plus an additional \$15.05 per kW per month for each kW, if any, of the amount by which (1) the customer's onpeak billing demand exceeds the higher of 2,500 kW or its onpeak contract demand or (2) the customer's offpeak billing demand exceeds the higher of 2,500 kW or its offpeak contract demand, whichever is higher,	
Energy charge:	6.459 cents per kWh per month for all onpeak kWh 4.024 cents per kWh per month for all offpeak kWh The above rates are subject to adjustment under the Provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>Time-Of-Day – Schedule TGSC</u>	Effective meters read on or after September 30, 2009.	1
Customer charge:	\$1,500 per delivery point per month.	
Demand charge:	\$15.23 per kW per month of the customer's onpeak billing demand, plus \$1.81 per month for each kW, if any, of the amount by which the customer's offpeak billing demand exceeds its onpeak billing demand, plus an additional \$15.23 per kW per month for each kW, if any, of the amount by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
Energy charge:	5.699 cents per kWh per month for all onpeak kWh 3.364 cents per kWh per month for all offpeak kWh The above rates are subject to adjustment under the Provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>Time-Of-Day – Schedule TMSB</u>	Effective meters read on or after September 30, 2009.	0
	If the higher of the customer's onpeak metered demand or offpeak metered demand for the month is not more than 5,000 kW:	
Customer charge:	\$1,500 per delivery point per month.	
Demand charge:	\$14.48 per kW per month of the customer's onpeak billing demand, plus \$2.23 per kW per month for each kW, if any, of the amount by which the customer's offpeak billing demand exceeds its onpeak billing demand, plus an additional \$14.48	

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
**(Continued)**



<b>Electric Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
Demand charge:	per kW per month for each kW, if any, of the amount by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
Energy charge:	5.191 cents per kWh per month for all onpeak kWh 3.065 cents per kWh per month for all offpeak kWh  If the higher of the customer's onpeak metered demand or offpeak metered demand for the month is greater than 5,000kW:	
Customer charge:	\$1,500 per delivery point per month.	
Demand charge:	\$12.94 per kW per month of the customer's onpeak billing demand, plus \$2.02 per month for each kW, if any, of the amount by which the customer's offpeak billing demand exceeds its onpeak billing demand, plus an additional \$12.94 per kW per month for each kW, if any, of the amount by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
Energy charge:	4.620 cents per kWh per month for all onpeak kWh 2.727 cents per kWh per month for all offpeak kWh The above rates are subject to adjustment under the Provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
<u>Time-Of-Day – Schedule TMSC</u>	Effective meters read on or after September 30, 2009.	0
Customer charge:	\$1,500 per delivery point per month.	
Demand charge:	\$12.44 per kW per month of the customer's onpeak billing demand, plus \$1.54 per month for each kW, if any, of the amount by which the customer's offpeak billing demand exceeds its onpeak billing demand, plus an additional \$12.44 per kW per month for each kW, if any, of the amount by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
Energy charge:	4.620 cents per kWh per month for all onpeak kWh 2.727 cents per kWh per month for all offpeak kWh The above rates are subject to adjustment under the Provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
**(Continued)**



<b>Electric Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
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<u>Outdoor Lighting- Schedule LS</u>	Effective meters read on or after September 30, 2009.	17,053
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Part A – Charges for street and park lighting systems, traffic signal systems, and athletic field lighting installations.

Energy charge:	6.109 cents per kWh per month This rate is subject to adjustment under the provisions of the TVA Fuel Cost and Purchased Power Adjustment Rider.	
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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.	
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Traffic signal systems and athletic field lighting installations shall be provided, owned, and maintained by and at the expense of 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 of any such system or installation and shall require payment by the customer of a facility charge sufficient to cover all of Division’s costs (except reimbursed costs), including appropriate overheads, of providing, owning, and maintaining such system or installation; provided that, for athletic field lighting installations, such facility charge shall in no case be less than 12% per year of such costs. Said facility charge will be in addition to the annual facility charge on the facilities necessary to provide service to such system or installation as provided for in the preceding paragraph.

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
(Continued)



<b>Electric Division Rate Class (cont.)</b>	<b>Base Charge</b>			<b>Customers</b>
	Part B – Charges for outdoor lighting for individual customers – charges per fixture per month			
<b>(a) Type of fixture</b>	<b>Watts</b>	<b>Lamp Size (Lumens)</b>	<b>Rated (kWh)</b>	<b>Charge</b>
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>Gas Division Rate Class</b>	<b>Base Charge</b>	<b>Customers</b>
<u>Residential G-1 &amp; G-3</u>	Effective meters read on or after December 26, 2007 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.	290,179
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	
<u>Small General Service G-7</u>	Effective meters read on or after December 26, 2007 This rate schedule is available for gas service to all gas customers except residential.	22,044

**SCHEDULE OF CURRENT UTILITY RATES  
DECEMBER 31, 2010  
(Continued)**



<b>Gas Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
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.	
<u>Large General Service Firm on-peak G-8 and G-9</u>	Effective meters on or after December 26, 2007  This rate schedule is available for gas service to all customers contracting for not less than 100 Ccf of maximum daily demand.	467
Demand charge:	\$0.251 Ccf per month of contract demand or maximum daily demand during the twelve (12) months ending with the billing month, whichever is higher, plus	
Commodity Charge:	First 200,000 Ccf per month @ \$0.978 ccf  Excess over 200,000 Ccf per month @ \$0.864 ccf, plus the above rates are subject to adjustment under the provisions of the Purchased Gas Adjustment Rider.	
Minimum bill:	The minimum bill shall be \$0.904 for Ccf of the higher of: (1) the maximum Daily Demand during the twelve (12) months ending with the billing month, or (2) the Daily Contract Demand.	
<u>Large General Service Interruptible Off- peak G-10 and G-12</u>	Effective December 26, 2007  This rate schedule is available for gas service to all customers contracting for not less than 1,500 Ccf of maximum daily demand and providing oil or other alternate fuel facilities approved by the Division as being adequate in design and capacity.	25

**SCHEDULE OF CURRENT UTILITY RATES  
DECEMBER 31, 2010  
(Continued)**



<b>Gas Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
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 of the higher of (1) the maximum daily demand during the twelve months ending with the billing month, or (2) the daily contract demand, but in no event less than \$500.00.	

<b>Water Division Rate Class</b>	<b>Base Charge</b>	<b>Customers</b>										
<u>Residential – Inside City Rate</u>	Effective meters read on or after June 26, 2008 For water furnished to premises entirely within the corporate limits of the City of Memphis	185,241										
Commodity charge:	All water consumed: \$1.31 per Ccf per month											
Minimum bill:	The minimum monthly bill shall be determined by the size of the meter installed, as follows:  <table style="margin-left: 40px;"> <tr><td>5/8" meter</td><td>\$ 5.54</td></tr> <tr><td>3/4" meter</td><td>7.99</td></tr> <tr><td>1" meter</td><td>14.18</td></tr> <tr><td>1-1/2" meter</td><td>31.91</td></tr> <tr><td>2" meter</td><td>56.72</td></tr> </table>	5/8" meter	\$ 5.54	3/4" meter	7.99	1" meter	14.18	1-1/2" meter	31.91	2" meter	56.72	
5/8" meter	\$ 5.54											
3/4" meter	7.99											
1" meter	14.18											
1-1/2" meter	31.91											
2" meter	56.72											
<u>Residential – Outside City Rate</u>	Effective meters read on or after June 26, 2008 For water furnished to premises outside the corporate limits of the City of Memphis	22,443										
Commodity charge:	All water consumed: \$2.04 per Ccf per month											
Minimum bill:	The minimum monthly bill shall be determined by the size of the meter installed, as follows:  <table style="margin-left: 40px;"> <tr><td>5/8" meter</td><td>\$ 7.71</td></tr> <tr><td>3/4" meter</td><td>11.09</td></tr> <tr><td>1" meter</td><td>19.74</td></tr> <tr><td>1-1/2" meter</td><td>44.39</td></tr> <tr><td>2" meter</td><td>78.91</td></tr> </table>	5/8" meter	\$ 7.71	3/4" meter	11.09	1" meter	19.74	1-1/2" meter	44.39	2" meter	78.91	
5/8" meter	\$ 7.71											
3/4" meter	11.09											
1" meter	19.74											
1-1/2" meter	44.39											
2" meter	78.91											

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
**(Continued)**



<b>Water Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>																														
<u>General Service – Inside City Rate</u>	Effective meters read on or after June 26, 2008 For water service to all customers within the corporate limits of the City of Memphis, except residential customers	18,939																														
Commodity charge:	Water consumed per month: <table style="margin-left: 20px;"> <tr><td>First 30 Ccf</td><td>\$1.67 per Ccf</td></tr> <tr><td>Next 70 Ccf</td><td>\$1.42 per Ccf</td></tr> <tr><td>Next 100 Ccf</td><td>\$1.08 per Ccf</td></tr> <tr><td>Next 400 Ccf</td><td>\$0.90 per Ccf</td></tr> <tr><td>Next 5,400 Ccf</td><td>\$0.70 per Ccf</td></tr> <tr><td>Excess over 6,000 Ccf</td><td>\$0.73 per Ccf</td></tr> </table>	First 30 Ccf	\$1.67 per Ccf	Next 70 Ccf	\$1.42 per Ccf	Next 100 Ccf	\$1.08 per Ccf	Next 400 Ccf	\$0.90 per Ccf	Next 5,400 Ccf	\$0.70 per Ccf	Excess over 6,000 Ccf	\$0.73 per Ccf																			
First 30 Ccf	\$1.67 per Ccf																															
Next 70 Ccf	\$1.42 per Ccf																															
Next 100 Ccf	\$1.08 per Ccf																															
Next 400 Ccf	\$0.90 per Ccf																															
Next 5,400 Ccf	\$0.70 per Ccf																															
Excess over 6,000 Ccf	\$0.73 per Ccf																															
Minimum bill:	The minimum monthly bill shall be determined by the size of the meter installed, as follows: <table style="margin-left: 20px;"> <tr><td>5/8" meter</td><td>\$ 10.62</td></tr> <tr><td>3/4" meter</td><td>12.37</td></tr> <tr><td>1" meter</td><td>21.21</td></tr> <tr><td>1-1/2" meter</td><td>42.44</td></tr> <tr><td>2" meter</td><td>88.45</td></tr> <tr><td>3" meter</td><td>176.84</td></tr> <tr><td>4" meter</td><td>264.45</td></tr> <tr><td>6" meter</td><td>334.53</td></tr> <tr><td>8" meter</td><td>404.63</td></tr> <tr><td>10" meter</td><td>838.18</td></tr> <tr><td>12" meter</td><td>1,169.54</td></tr> <tr><td>14" meter</td><td>1,608.13</td></tr> <tr><td colspan="2"> </td></tr> <tr><td>Battery of 2-2" meters</td><td>176.84</td></tr> <tr><td>Battery of 3-2" meters</td><td>264.45</td></tr> </table>	5/8" meter	\$ 10.62	3/4" meter	12.37	1" meter	21.21	1-1/2" meter	42.44	2" meter	88.45	3" meter	176.84	4" meter	264.45	6" meter	334.53	8" meter	404.63	10" meter	838.18	12" meter	1,169.54	14" meter	1,608.13			Battery of 2-2" meters	176.84	Battery of 3-2" meters	264.45	
5/8" meter	\$ 10.62																															
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1-1/2" meter	42.44																															
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3" meter	176.84																															
4" meter	264.45																															
6" meter	334.53																															
8" meter	404.63																															
10" meter	838.18																															
12" meter	1,169.54																															
14" meter	1,608.13																															
Battery of 2-2" meters	176.84																															
Battery of 3-2" meters	264.45																															
<u>General Service – Outside City Rate</u>	Effective meters read on or after June 26, 2008 For water service to all customers outside the corporate limits of the City of Memphis, except residential customers	803																														
Commodity charge:	Water consumed per month: <table style="margin-left: 20px;"> <tr><td>First 30 Ccf</td><td>\$2.51 per Ccf</td></tr> <tr><td>Next 70 Ccf</td><td>\$2.11 per Ccf</td></tr> <tr><td>Next 100 Ccf</td><td>\$1.61 per Ccf</td></tr> <tr><td>Next 400 Ccf</td><td>\$1.35 per Ccf</td></tr> <tr><td>Next 5,400 Ccf</td><td>\$1.06 per Ccf</td></tr> <tr><td>Excess over 6,000 Ccf</td><td>\$1.10 per Ccf</td></tr> </table>	First 30 Ccf	\$2.51 per Ccf	Next 70 Ccf	\$2.11 per Ccf	Next 100 Ccf	\$1.61 per Ccf	Next 400 Ccf	\$1.35 per Ccf	Next 5,400 Ccf	\$1.06 per Ccf	Excess over 6,000 Ccf	\$1.10 per Ccf																			
First 30 Ccf	\$2.51 per Ccf																															
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Next 100 Ccf	\$1.61 per Ccf																															
Next 400 Ccf	\$1.35 per Ccf																															
Next 5,400 Ccf	\$1.06 per Ccf																															
Excess over 6,000 Ccf	\$1.10 per Ccf																															

**SCHEDULE OF CURRENT UTILITY RATES  
DECEMBER 31, 2010  
(Continued)**



<b>Water Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
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Minimum bill: The minimum monthly bill shall be determined by the size of the meter installed, as follows:

5/8" meter	\$ 16.22
3/4" meter	18.93
1" meter	32.45
1-1/2" meter	64.88
2" meter	135.18
3" meter	270.39
4" meter	404.09
6" meter	511.20
8" meter	618.30
10" meter	1,280.82
12" meter	1,787.17
14" meter	2,455.69
Battery of 2-2" meters	270.39
Battery of 3-2" meters	404.09

<u>Residential – Shelby County Water Distribution System</u>	Effective meters read on or after June 26, 2008	20,807
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For water service within the area served by the Shelby County Water Distribution System at the time of its acquisition on June 30, 1999, for domestic uses to residential customers in individual private residences or other individual dwelling places.

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

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

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

Residential customers shall be served through a single meter not larger than 2" in size.

**SCHEDULE OF CURRENT UTILITY RATES**  
**DECEMBER 31, 2010**  
**(Continued)**



<b>Water Division Rate Class (cont.)</b>	<b>Base Charge</b>	<b>Customers</b>
<u>Commercial - Industrial – Shelby County</u> <u>Water Distribution System</u>	Effective meters read on or after June 26, 2008	601

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.

Monthly rate:

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

Minimum bill:

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

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

**SCHEDULE OF INSURANCE**  
**DECEMBER 31, 2010**  
**(Dollars in Thousands)**



<u>Type of Coverage</u>	<u>Amount of Coverage</u>
Property	\$ 500,000
Crime	1,000
Travel Accident	1,000

**REQUIRED SCHEDULE OF FUNDING PROGRESS FOR OPEB  
DECEMBER 31, 2010  
(Dollars in Thousands)**



<b>Actuarial Valuation Date</b>	<b>Actuarial Value of Assets ( a )</b>	<b>Actuarial Accrued Liability (AAL) ( b )</b>	<b>Unfunded AAL (UAAL) ( b - a )</b>	<b>Funded Ratio ( a / b )</b>	<b>Covered Payroll ( c )</b>	<b>UAAL as a Percentage of Covered Payroll ( ( b - a ) / c )</b>
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*	0	743,484	743,484	0.0%	148,219 **	501.6%

\* Projected from 12/31/05 valuation.

\*\* Projected from 2006 payroll.

**REQUIRED SCHEDULE OF EMPLOYER CONTRIBUTIONS**  
**DECEMBER 31, 2010**  
**(Dollars in Thousands)**



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<b>Fiscal Year Ended</b>	<b>Annual OPEB Cost</b>	<b>Employer Contributions</b>	<b>Percentage of Annual OPEB Cost Contributed</b>
December 31, 2010	\$ 43,651	\$ 43,476	99.6%
December 31, 2009	55,340	55,688	100.6%
December 31, 2008	57,991	66,881	115.3%

**REQUIRED SCHEDULE OF FUNDING PROGRESS FOR PENSION PLAN  
DECEMBER 31, 2010  
(Dollars in Thousands)**



<b>Actuarial Valuation Date</b>	<b>Actuarial Value of Assets (a)</b>	<b>Actuarial Accrued Liability (AAL)* (b)</b>	<b>Unfunded/ (Overfunded) AAL (UAAL) (b - a)</b>	<b>Funded Ratio (a / b)</b>	<b>Covered Payroll (c)</b>	<b>UAAL as a Percentage of Covered Payroll** ((b - a) / c)</b>
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%
January 1, 2009	1,176,590	1,243,630	67,040	94.6%	150,253	44.6%

\* Based on Entry Age Normal Cost Method

\*\* Not less than zero

**SCHEDULE OF UNACCOUNTED FOR WATER  
FOR THE YEAR ENDED DECEMBER 31, 2010  
(Amounts in Gallons or Dollars)**



<b>A</b>	<b>Water Treated and Purchased:</b>		
B	Water Pumped (potable)	54,018,318,900	
C	Water Purchased	-	
<b>D</b>	<b>Total Water Treated and Purchased</b>		<b>54,018,318,900</b>
<b>E</b>	<b>Accounted for Water:</b>		
F	Water Sold (includes free water for City of Memphis, bulk sales, and water bill adjustments)	44,718,139,150	
G	Metered for Consumption (in house usage)	354,000,000	
H	* Fire Department Usage	25,141,470	
I	Flushing	47,255,095	
J	Tank Cleaning/Filling	-	
K	Street Cleaning	442,680	
L	Bulk Sales	-	
M	Water Bill Adjustments	-	
N	Other (explain)	-	
<b>O</b>	<b>Total Accounted for Water</b>		<b>45,144,978,395</b>
P	Unaccounted for Water		8,873,340,505
Q	Percent Unaccounted for Water		16.4%
R	Cost per 1,000 gallons	\$	0.248
S	Cost of Unaccounted for Water	\$	2,201,607.37

Explained  
Other:

\* Fire Department usage is estimated using the amount from 2009 per agreement with the Memphis Fire Department.

**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, 2010 and have issued our report thereon dated May 19, 2011. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our 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 2010-1 and 2010-2 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 its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing 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 an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and questioned costs as item 2010-3.

We noted certain matters that we reported to management of the Divisions in a separate letter dated May 19, 2011.

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.

A handwritten signature in black ink that reads "Thompson Dunavant PC". The signature is written in a cursive, flowing style.

Memphis, Tennessee  
May 19, 2011

**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, 2010. 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 auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audits to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Divisions' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions. Our audits do not provide a legal determination on the Divisions' compliance with those requirements.

As described in item 2010-3 in the accompanying schedule of findings and questioned costs, the Electric Division did not comply with requirements regarding reporting that are applicable to its American Recovery and Reinvestment Act Electricity Delivery and Energy Reliability, Research, Development and Analysis program. Compliance with such requirements is necessary, in our opinion, for the Electric Division to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, 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, 2010.

## 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.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph 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. However, as discussed below, we identified a certain deficiency in internal control over compliance that we consider to be a significant deficiency.

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. We did not consider the deficiency described in the accompanying schedule of findings and questioned costs related to internal control over compliance to be a material weakness.

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiency in internal control described in the accompanying schedule of findings and questioned costs as item 2010-3 to be a significant deficiency.

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.



Memphis, Tennessee  
May 19, 2011

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED DECEMBER 31, 2010  
(Dollars in Thousands)**



Federal Grantor/Pass-Through Grantor	CFDA Number	Contract Number	Beginning (Accrued) Deferred	Cash Receipts	Expenditures	Ending (Accrued) Deferred
Federal Awards U.S. Department of Homeland Security/ Tennessee Emergency Management Agency	97.036	34101-0000001983	\$ (5,932)	\$ 4,453	\$ -	\$ (1,479)
U.S. Department of Homeland Security/ Tennessee Emergency Management Agency	97.036	34101-0000000525*	(77)	77	-	-
U.S. Department of Homeland Security/ Tennessee Emergency Management Agency	97.036	34101-0000005751	-	24	543	(519)
<b>Total Program 97.036</b>			<b>\$ (6,009)</b>	<b>\$ 4,554</b>	<b>\$ 543</b>	<b>\$ (1,998)</b>
U.S. Department of Homeland Security/ Tennessee Emergency Management Agency	97.047	Edison #E-18001	(425)	429	392	(388)
U.S. Department of Homeland Security/ Tennessee Emergency Management Agency	97.047	GR-07-20788-00	(113)	113	-	-
<b>Total Program 97.047</b>			<b>(538)</b>	<b>542</b>	<b>392</b>	<b>(388)</b>
ARRA - U.S. Department of Energy/ Smart Grid Investment Grant	81.122	DE-OE0000281	-	164	341	(177)
<b>Total Program 81.122</b>			<b>-</b>	<b>164</b>	<b>341</b>	<b>(177)</b>
<b>Total Federal Awards</b>			<b>\$ (6,547)</b>	<b>\$ 5,260</b>	<b>\$ 1,276</b>	<b>\$ (2,563)</b>

\* Contracts Z-08-212844-00 and Z-08-212844-01, in the 2008 and 2009 SEFA, were later combined as contract 34101-000000525 in 2010.

**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, 2010. 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.

## MEMPHIS LIGHT, GAS AND WATER DIVISION

Schedule of Findings and Questioned Costs  
For the Year Ended December 31, 2010

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### 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. Two 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. One instance of noncompliance material to the financial statements of the Divisions, which would be required to be reported in accordance with *Government Auditing Standards*, was disclosed during the audits.
4. One significant deficiency 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 its major federal programs, except for the noncompliance with requirements regarding reporting that are applicable to the Electric Division's American Recovery and Reinvestment Act Electricity Delivery and Energy Reliability, Research, Development and Analysis program.
6. There was one audit finding related to major programs that is 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
97.047	Pre-Disaster Mitigation
8. The threshold for distinguishing Type A and B programs was \$300,000.
9. The Divisions were determined to be a low risk auditee.

## MEMPHIS LIGHT, GAS AND WATER DIVISION

### Schedule of Findings and Questioned Costs (Continued) For the Year Ended December 31, 2010

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#### B. Financial Statement Findings Section

##### Significant Deficiencies

###### 2010 -1 Vacation and sick leave accrual

Condition: During its 2010 review process, Management discovered an error in the calculation of its allocation of vacation and sick accrual liabilities related to 2009.

Criteria: Neither information systems nor management accounting followed its normal review procedures prior to recording the 2009 adjustment.

Effect: Management posted a prior period adjustment to the accounts of the Water division.

Recommendation: We recommend that both information systems and accounting personnel apply appropriate review procedures to data obtained to verify its accuracy and relevance to the intended purpose of the report.

Response: Management has implemented improvements in the reporting and review process which values accuracy over speed. An additional review is required for all entries. For entries or reports generated outside of General Accounting, an additional level of review is required to approve the accuracy of the information.

###### 2010 -2 Gas Division unbilled revenue and Purchased Gas Adjustment (PGA)

Condition: The Gas Division unbilled revenue balance as of December 31, 2010 was unusually low compared to its expected value. In addition, the billed sales revenue for 2010 was high when compared to the expected revenue based on actual gas costs for 2010. An analysis of this situation by Division personnel revealed a problem with the monthly calculations of the PGA for 2008 through 2009. The PGA is a variable in the unbilled revenue calculation and the incorrect PGA calculation had the effect of understating both unbilled revenue (asset) and deferred credits – PGA (liability) by approximately \$19 million as of December 31, 2010.

Criteria: Timely review of non-system generated calculations and the comparison of calculation results to expected results are essential for strong internal control over such calculations.

Effect: Because the monthly PGA calculations did not include all the gas costs included in the related rates charged to customers, the PGA liability to customers was understated by \$18.99 million and the proper PGA amounts were not reflected on customers' utility bills for 2008 through the present date. Net assets of the Gas Division were not misstated as the result of this situation.

## MEMPHIS LIGHT, GAS AND WATER DIVISION

Schedule of Findings and Questioned Costs (Continued)  
For the Year Ended December 31, 2010

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### B. Financial Statement Findings Section (continued)

#### Significant Deficiencies (continued)

2010 -2 Gas Division unbilled revenue and Purchased Gas Adjustment (PGA) (continued)

Recommendation: We recommend that all unbilled revenue and PGA calculations be reviewed and questioned as to propriety on a monthly basis. Comparison of calculated amounts to expected results should be performed to determine the reasonableness of the calculated amounts.

Response: Management has implemented additional verifications and analytical tests for accuracy.

### C. Major Federal Awards Findings and Questioned Cost Section

#### Significant Deficiencies

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.

Criteria: Quarterly reports must be submitted within 30 days after the end of the reporting period.

Effect: Inaccurate and untimely reports are considered a reporting compliance finding and may hinder eligibility for future federal funding.

Recommendation: We recommend that management strongly enforce the compliance requirements outlined in the grant agreement.

Response: Due to the ARRA (Smart Grid) grant having characteristics somewhat different from other grants sponsored by the DOE and a continuous change with Technical Project Officers (TPO), there was a deficiency in the communication and clarity between the DOE and MLGW. MLGW has met all other compliance reporting and invoicing requirements. MLGW submitted the 2011 January – March Form SF-425 on April 29, 2011, within the required time period.

**MEMPHIS LIGHT, GAS AND WATER DIVISION**

Schedule of Prior Year Audit Findings  
December 31, 2010

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**Prior Year Findings**

There were no prior year audit findings.



