



BOULT ■ CUMMINGS®  
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August 31, 2007

Eddie Roberson, Chairman  
Tennessee Regulatory Authority  
460 James Robertson Parkway  
Nashville, TN 37243-0505

filed electronically in docket office on 08/31/07

**Re: Request for an Investigation of the Business Partnership Between Memphis  
Light, Gas & Water and Memphis Networx, LLC  
Docket No. 07-00183**

Dear Chairman Roberson:

Please find attached supplemental responses to Data Request Number 13. The 2006 financials will be filed with the Authority when they become available.

Please do not hesitate to contact me with any questions about these responses.

Very truly yours,

BOULT, CUMMINGS, CONNERS & BERRY, PLC

By:

  
Henry Walker

HW/djc

**MEMPHIS NETWORKX, LLC**

**FINANCIAL STATEMENTS**

December 31, 2005 and 2004

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Watkins Uiberall, PLLC  
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## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Members  
Memphis Networkx, LLC  
Memphis, Tennessee

We have audited the accompanying balance sheets of Memphis Networkx, LLC, as of December 31, 2005 and 2004, and the related statements of operations, changes in members' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Memphis Networkx, LLC as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*Watkins Uiberall, PLLC*

Memphis, Tennessee  
January 30, 2006, except for Note 10,  
as to which the date is June 28, 2006

# MEMPHIS NETWORKX, LLC

## BALANCE SHEETS

December 31, 2005 and 2004

	<u>Assets</u>	
	<u>2005</u>	<u>2004</u>
Current Assets		
Cash and cash equivalents	\$ 11,062	\$ 58,659
Trade accounts receivables	283,997	758,966
Prepaid expenses	195,418	38,060
Costs and estimated earnings in excess of billings on uncompleted contracts	640,000	-
Deposits	133,000	33,000
Total current assets	<u>1,263,477</u>	<u>888,685</u>
Property and Equipment		
Plant equipment	7,522,339	6,813,208
Computer software	2,457,848	2,452,017
Broadband equipment	4,577,819	4,160,718
Furniture and office equipment	375,483	358,102
Leasehold improvements	1,654,710	954,896
	<u>16,588,199</u>	<u>14,738,941</u>
Less: accumulated depreciation	<u>(6,330,497)</u>	<u>(4,776,980)</u>
Net property and equipment	<u>10,257,702</u>	<u>9,961,961</u>
Deposits	<u>507,636</u>	<u>542,428</u>
Total assets	<u>\$ 12,028,815</u>	<u>\$ 11,393,074</u>
	<u>Liabilities and Members' Equity</u>	
Current Liabilities		
Checks issued in excess of deposits	\$ 166,979	\$ -
Accounts payable	1,073,504	1,502,980
Accrued expenses	742,777	298,391
Unearned revenue - current	16,800	-
Note payable - related party	-	85,000
Current maturities of long-term debt	640,686	-
Note payable - line of credit	1,935,150	-
Total current liabilities	<u>4,575,896</u>	<u>1,886,371</u>
Other Liabilities		
Long-term debt, less current maturities	1,565,652	-
Unearned revenue, non-current	167,737	91,764
Total liabilities	<u>6,309,285</u>	<u>1,978,135</u>
Members' Equity	<u>5,719,530</u>	<u>9,414,939</u>
Total liabilities and members' equity	<u>\$ 12,028,815</u>	<u>\$ 11,393,074</u>

The accompanying notes are an integral part of these financial statements.

**MEMPHIS NETWORKX, LLC****STATEMENTS OF OPERATIONS**

For the Years Ended December 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Revenue	\$ 4,045,611	\$ 3,569,094
Cost of sales	<u>2,418,294</u>	<u>2,354,128</u>
Gross profit	1,627,317	1,214,966
Operating Expenses		
Consulting fees	11,127	23,203
Professional fees	24,227	42,522
General and administrative	3,094,612	3,180,926
Compensation and payroll taxes	<u>2,071,860</u>	<u>1,857,132</u>
Total operating expenses	<u>5,201,826</u>	<u>5,103,783</u>
Loss from operations	(3,574,509)	(3,888,817)
Other Income (Expense)		
Interest income	3,129	3,034
Interest expense	<u>(124,029)</u>	<u>(313)</u>
Total other income (expense)	<u>(120,900)</u>	<u>2,721</u>
Net loss	<u>\$ (3,695,409)</u>	<u>\$ (3,886,096)</u>

The accompanying notes are an integral part of these financial statements.

**MEMPHIS NETWORKX, LLC**

**STATEMENTS OF CHANGES IN MEMBERS' EQUITY**

For the Years Ended December 31, 2005 and 2004

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	<u>Members'</u> <u>Contributions</u>	<u>Accumulated</u> <u>Deficit</u>	<u>Total</u>
Balance at January 1, 2004	\$ 30,585,731	\$ (20,816,696)	\$ 9,769,035
Contributions	3,532,000	-	3,532,000
Net loss	<u>-</u>	<u>(3,886,096)</u>	<u>(3,886,096)</u>
Balance at December 31, 2004	34,117,731	(24,702,792)	9,414,939
Net loss	<u>-</u>	<u>(3,695,409)</u>	<u>(3,695,409)</u>
Balance at December 31, 2005	<u>\$ 34,117,731</u>	<u>\$ (28,398,201)</u>	<u>\$ 5,719,530</u>

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The accompanying notes are an integral part of these financial statements.

# MEMPHIS NETWORKX, LLC

## STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2005 and 2004

	2005	2004
Cash Flows From (Used For) Operating Activities:		
Net loss	\$ (3,695,409)	\$ (3,886,096)
Adjustments to Reconcile Net Loss to Net Cash Used For Operating Activities:		
Depreciation	1,553,517	1,972,167
Changes in Operating Assets and Liabilities:		
Increase (decrease) in cash and cash equivalents:		
Accounts receivable	474,969	(661,774)
Prepaid expenses	(157,358)	16,046
Costs and estimated earnings in excess of billings on uncompleted contracts	(640,000)	-
Deposits	(65,208)	(7,379)
Accounts payable	(429,476)	864,524
Accrued expenses	444,386	109,532
Unearned revenue	92,773	25,866
Total adjustments	1,273,603	2,318,982
Net cash used for operating activities	(2,421,806)	(1,567,114)
Cash Flows Used For Investing Activities:		
Purchases of property and equipment	(1,849,258)	(2,137,379)
Cash Flows From Financing Activities:		
Checks issued in excess of deposits	166,979	-
Proceeds from issuance of note payable to a related party	-	85,000
Principal payments on notes payable to a related party	(85,000)	-
Net increase in note payable - line of credit	1,935,150	-
Proceeds from issuance of long-term debt	2,274,262	-
Principal payments on long-term debt	(67,924)	-
Member contributions	-	3,532,000
Net cash from financing activities	4,223,467	3,617,000
Net decrease in cash and cash equivalents	(47,597)	(87,493)
Cash and cash equivalents - beginning of year	58,659	146,152
Cash and cash equivalents - end of year	\$ 11,062	\$ 58,659

The accompanying notes are an integral part of these financial statements.



**MEMPHIS NETWORKX, LLC**

**STATEMENTS OF CASH FLOWS (CONTINUED)**

For the Years Ended December 31, 2005 and 2004

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	<u>2005</u>	<u>2004</u>
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for interest	<u>\$ 124,029</u>	<u>\$ -</u>

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The accompanying notes are an integral part of these financial statements.

## MEMPHIS NETWORKX, LLC

### NOTES TO FINANCIAL STATEMENTS

December 31, 2005 and 2004

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#### NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

##### Organization and Nature of Operations

Memphis Networkx, LLC (the Company) was organized under the Tennessee Limited Liability Act on November 8, 1999, to provide telecommunications services through the installation of broadband fiber optic cable in the Memphis, Tennessee, area. The Company is a joint venture between the Electric Division of Memphis Light, Gas & Water Divisions (MLGW, a component unit of the City of Memphis), and Memphis Broadband, LLC, a Delaware limited liability company. On August 9, 2001, the TRA issued a final order approving the Company's amended and restated operating agreement and granted a certificate of public convenience and necessity for the State of Tennessee.

Under the terms of the Company's Operating Agreement, capital contributions and cost incurred by the Company prior to its formation and through the date of Tennessee Regulatory Authority (TRA) approval are to be shared equally by the members. Subsequent to TRA approval, MLGW continued to provide periodic investments of capital as requested by the Company. The Company shall continue until it is wound up and liquidated, as stated in the Operating Agreement.

Effective April 1, 2002, MLGW entered into a capital contribution agreement with Memphis Broadband, LLC. The agreement established planned monthly capital contributions through 2004 for both members. The agreement also amended the operating agreement to allow one member to contribute the required capital on behalf of the other member. If a member makes such a disproportionate contribution, the agreement allows the contributing member to charge the other member interest on the disproportionate contribution or increase its ownership percentage. Each member has a voting interest in the Company equal to their current sharing ratio as defined in the Operating Agreement. On the contribution date, the sharing ratio of net operating income or loss and distributions is adjusted to reflect the increased capital contribution. For the years ended December 31, 2005 and 2004, MLGW contributed \$0 and \$3,532,000, respectively, which was equal to both members' required capital contributions.

On June 21, 2005, the Members entered into a capital contribution allowance agreement. The agreement stipulates that guarantees of debt shall be treated as capital contributions. Certain individuals have personally guaranteed debt on behalf of the Company and as such the sharing ratios have been adjusted. Allocations of net operating income or loss and distributions are as follows: 56.14% for MLGW and 43.86% for Memphis Broadband, LLC. See Note 8 for additional information.

The Company's members have limited liability under the Operating Agreement such that a member of the Company has no personal obligation and is not otherwise personally liable for the acts, debts, liabilities, or obligations of the Company or the acts or omissions of any other member, economic interest owner (as defined in the Operating Agreement), manager, director, employee, or agent of the Company except as explicitly described in the previous paragraph.

### Method of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

### Use of Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and 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.

### Concentrations

The Company's credit risks relate to cash and cash equivalents and accounts receivable. The Company maintains cash at a bank. Those accounts are insured by the Federal Deposit Insurance Corporation up to an aggregate of \$100,000.

For the year ended December 31, 2005, three customers comprised 34.18% of total sales. For the year ended December 31, 2004, two customers comprised 43.68% of total sales.

At December 31, 2005, three customers comprised 43.16% of total accounts receivable. At December 31, 2004, one customer comprised 66.29% of total accounts receivable.

### Cash and Cash Equivalents

For purposes of the statement of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

### Accounts Receivable

Accounts receivable consists primarily of amounts due from customers in the Memphis area. The Company performs continual credit evaluations of its customers and does not consider an allowance for doubtful accounts necessary.

### Property and Equipment

Property and equipment is stated at cost. Depreciation of plant and equipment, broadband equipment, leasehold improvements, furniture, office equipment and computer software is computed using the straight-line method over the estimated useful lives of 3 to 25 years.

### Revenue Recognition

The Company generates revenues from selling network capacity and related services to other communications service providers. The Company recognizes revenues when earned as services are provided throughout the life of each contract with a customer. The majority of the Company's revenues

are generated on a monthly recurring basis under contracts of various lengths, ranging from twelve months to twenty years. Revenue is recognized over the service contract period for all general services. Unearned revenues consist primarily of payments received in advance of revenue being earned under contracts for indefeasible rights to use.

Revenue from fixed-price construction contracts are recognized on the percentage-of-completion method, measured by the percentage of costs incurred to date to estimated total costs for each contract. This method is used because management considers expended costs to be the best available measure of progress on these contracts. Because of inherent uncertainties in estimating costs, it is at least reasonably possible that estimates used will change within the near term.

The asset "costs and estimated earnings in excess of billings on uncompleted contracts" represents revenues recognized in excess of amounts billed.

#### Contract Costs

Contract costs include all direct material and labor costs and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs, and insurance. Indirect construction costs and general and administrative costs are charge to expense as incurred. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined.

#### Income Taxes

A limited liability company is treated as a partnership for federal income tax purposes and is not subject to federal income taxes. The taxable income or loss of the Company is included in the individual income tax returns of its members based upon their percentage of ownership. Consequently, no provision for federal income taxes is required in the accompanying financial statements. The Company, however, is subject to state income taxes.

Deferred state income taxes have been determined using the asset and liability method of accounting for state income taxes. Under this method, state deferred tax assets and liabilities are determine based on the difference between the financial statement carrying amounts and tax bases of assets and liabilities using enacted state tax rates in effect for the years in which the differences are expected to reverse. This method also allows for the recognition for deferred tax assets in the current period for the future benefit of net operating loss carryforwards and items for which expenses have been recognized for financial statement purposes, but will be deductible in future periods for income tax purposes. The temporary differences in these financial statements relate primarily to depreciation, amortization, and net operating loss carryforwards. A valuation allowance is provided for net state deferred tax assets as it is uncertain as to the future realization of these benefits.

#### Advertising

All advertising costs are expensed as incurred. Advertising costs for the years ended December 31, 2005 and 2004 were \$26,531 and \$31,958, respectively.

### Long-Lived Assets and Impairments

The Company evaluates the recoverability of long-lived assets on an annual basis. When it is determined that the long-lived asset cannot be recovered through future operations, it is reduced to its estimated fair value by an impairment charge to operations.

### **NOTE 2 - LEASES**

The Company leases office space, automobiles, and other pieces of equipment under operating leases. Total rent expense for the years ended December 31, 2005 and 2004 was \$1,094,923 and \$995,164, respectively. Future commitments under these leases for the years ending December 31 are as follows:

2006	\$ 769,484
2007	391,314
2008	147,000
2009	130,527
2010	130,527
Thereafter	118,696
	<u>\$ 1,687,548</u>

As a part of a building operating lease, the Company obtained a letter of credit in the amount of \$160,000 at December 31, 2002. The required amount is reduced by \$40,000 per year over the lease term. At December 31, 2005 and 2004, the remaining balance was \$40,000 and \$80,000, respectively. The Company has a certificate of deposit that serves as collateral for the letter of credit and is shown on the balance sheet in deposits.

### **NOTE 3 - PROFIT SHARING PLAN**

The Company sponsors a profit sharing plan under the provisions of Section 401(k) of the Internal Revenue Code covering substantially all full-time employees. Eligibility requirements are at least one month of employment and attainment of age 21. Employees become fully vested after six years in the plan. The Company's contributions to the plan are voluntary and the Company elected not to make a contribution for the years ended December 31, 2005 and 2004.

### **NOTE 4 - STATE INCOME TAXES**

The tax effects of temporary differences that give rise to the significant portions of deferred tax assets and deferred tax liabilities at December 31, are as follows:

	<u>2005</u>	<u>2004</u>
Deferred Tax Assets		
Due to benefit of state net operating loss carryforwards	\$ 1,931,472	\$ 1,524,775
Due to benefit of amortization of start up costs	186,654	318,411

Deferred Tax Liabilities		
Due to depreciation	<u>(279,022)</u>	<u>(243,860)</u>
Net deferred tax asset	1,839,104	1,599,326
Valuation allowance	<u>(1,839,104)</u>	<u>(1,599,326)</u>
	<u>\$ -</u>	<u>\$ -</u>

At December 31, 2005, the Company had state tax loss carryforwards of approximately \$29,714,947 expiring through 2020, which are available to reduce future state taxable income.

#### NOTE 5 – RELATED PARTY TRANSACTIONS

At December 31, 2005 and 2004, the Company owed a member \$199,869 and \$37,940, respectively, for pole attachment and conduit fees. As of December 31, 2005 and 2004, the Company had two deposits with a member totaling \$200,790 for both years.

For the years ended December 31, 2005 and 2004, the Company paid a member \$34,728 and \$141,885, respectively, for pole attachment and conduit fees. For the years ended December 31, 2005 and 2004, the Company paid \$139,929 and \$84,632, respectively, for utilities.

At December 31, 2005 and 2004, the Company had receivables from a member totaling \$46,112 in both years for fiber installation services.

At December 31, 2005 and 2004, the Company had a deposit with the City of Memphis totaling \$100,000.

At December 31, 2005 and 2004, the Company had accrued franchise fees to the City of Memphis of \$152,332 and \$69,758, respectively.

For the year ended December 31, 2004, the Company had revenues from a member totaling \$84,152 for fiber installation, collocation services, and internet services.

For the years ended December 31, 2005 and 2004, the Company had revenues from the City of Memphis of approximately \$777,330 and \$1,009,000, respectively, for fiber installation services.

At December 31, 2005 and 2004, the Company had receivables from the City of Memphis of approximately \$16,321 and \$503,000, respectively, for fiber installation services.

At December 31, 2004, the Company had an uncollateralized bridge loan outstanding of \$85,000 payable to a company owned by the Chief Executive Officer of Memphis Networkx, LLC. The note bore interest at 2%. At December 31, 2005, there is no outstanding loan balance.

## NOTE 6 – FRANCHISE AGREEMENTS

The Company has entered into various franchise agreements with certain municipalities in Shelby County. The agreements are for periods of between five and twenty years. These agreements authorize the Company to use these municipalities' streets to operate, or lease and maintain a telecommunication system within the municipalities' city limits. As part of these agreements, some of the municipalities require deposits and fees equal to 5% of the gross revenues charged for services provided in the municipality. The following is a list of deposits and fees accrued to the various municipalities at December 31:

	2005		2004	
	Deposit	Accrued Franchise Fees	Deposit	Accrued Franchise Fees
City of Memphis	\$ 100,000	\$ 152,332	\$ 100,000	\$ 69,758
City of Germantown	50,000	8,932	50,000	670
City of Collierville	50,000	12,829	50,000	-
City of Bartlett	-	-	-	-
	<u>\$ 200,000</u>	<u>\$ 174,093</u>	<u>\$ 200,000</u>	<u>\$ 70,428</u>

The deposits are shown on the balance sheet under deposits and the franchise fees are shown on the balance sheet under accrued expenses.

## NOTE 7 – LONG-TERM CONTRACTS

The Company has entered into certain non-cancelable long-term contracts to provide services to its customers. Estimated future service and construction revenue under contracts longer than one year in effect at December 31, 2005 is as follows:

2006	\$ 3,500,792
2007	2,540,451
2008	1,659,807
2009	393,844
	<u>\$ 8,094,894</u>

## NOTE 8 – NOTES PAYABLE AND SHORT-TERM DEBT

On June 15, 2005 the Company obtained financing through a bank. The financing agreement provides for a line-of-credit of \$2,000,000 and a term loan of \$5,000,000. The line-of-credit expires May 15, 2007 and bears interest at the thirty day LIBOR rate plus 1.45%. At December 31, 2005, the outstanding balance on the line of credit was \$1,935,150. The term loan is to be funded in two phases. The first phase provides funds up to \$2,915,643 and is collateralized by personal property of the Company and is guaranteed by certain private equity owners of the Company. The second phase will fund the remaining balance of \$2,084,357 and is contingent upon obtaining additional guarantees from certain other private

equity owners of the Company. The term loan bears interest at the U.S. Treasury rate of a similar maturity period in effect at the close of each term note drawn plus 1.7%.

The Company's long term debt as of December 31, 2005 and 2004 is as follows:

	<u>2005</u>	<u>2004</u>
Uncollateralized note payable to a related party, due on demand, interest payable in monthly installments at 2%.	\$ -	\$ 85,000
Notes payable to a bank, collateralized by property and equipment and personal guarantees of certain owners, payable in monthly installments through 2011 at fixed interest rates ranging from 5.25% to 6.24%.	2,206,338	-
	<u>2,206,338</u>	<u>85,000</u>
Less current maturities	640,686	85,000
	<u>\$ 1,565,652</u>	<u>\$ -</u>

Future maturities of long-term debt are as follows:

2006	\$ 640,686
2007	673,875
2008	488,617
2009	217,282
2010	166,755
Thereafter	19,123
	<u>\$ 2,206,338</u>

The Company's bank debt agreements contain various covenants including timely filing of financial reports and maintaining a minimum net worth of \$5,500,000. At December 31, 2005, the Company was in compliance with all covenants.



## NOTE 9 – COSTS AND ESTIMATED EARNINGS ON UNCOMPLETED CONTRACTS

Costs, estimated earnings, and billings on uncompleted contracts are summarized as follows:

	<u>2005</u>	<u>2004</u>
Costs incurred on uncompleted contracts	\$ 438,330	\$ -
Estimated earnings	<u>201,670</u>	<u>-</u>
	640,000	-
Less billings to date	-	-
	<u>\$ 640,000</u>	<u>\$ -</u>

Amounts are included in the accompanying balance sheet under the following caption:

	<u>2005</u>	<u>2004</u>
Costs and estimated earnings in excess of billings on uncompleted contracts	<u>\$ 640,000</u>	<u>\$ -</u>

## NOTE 10 – SUBSEQUENT EVENT

On May 30, 2006, the bank loan agreement discussed in Note 8 was modified. The Company received approval for up to \$998,184 in additional financing for a total term loan of \$6 million. The loan bears interest at the U.S. Treasury rate of a similar maturity period in effect at the close of each term note drawn plus 1.7%. The term loan is guaranteed by certain private equity owners of the Company. As part of the modification agreement, the covenant to maintain minimum equity of \$5,500,000 has been reduced to \$3,500,000.

AUDITED FINANCIAL STATEMENTS

**Memphis Networx, LLC**

*For the years ended December 31, 2002 and 2001,  
with Report of Independent Auditors*

Memphis Networx, LLC  
Audited Financial Statements

For the years ended December 31, 2002 and 2001

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## Report of Independent Auditors

The Board of Directors and Members  
Memphis Networx, LLC

We have audited the accompanying balance sheets of Memphis Networx, LLC as of December 31, 2002 and 2001, and the related statements of operations, changes in members' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in 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 opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Memphis Networx, LLC at December 31, 2002 and 2001, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.

*Ernst & Young LLP*

March 20, 2003

# Memphis Networkx, LLC

## Balance Sheets

	December 31	
	2002	2001
<b>Assets</b>		
Current assets:		
Cash	\$ 195,185	\$ 219,686
Trade accounts receivable	49,441	-
Prepaid expenses	109,884	74,833
Total current assets	354,510	294,519
Property and equipment:		
Plant and equipment	4,917,313	-
Computer software	2,292,827	72,352
Broadband equipment	1,827,199	-
Furniture and office equipment	317,100	226,056
Leasehold improvements	903,995	107,724
Construction materials	-	2,758,252
	10,258,434	3,164,384
Accumulated depreciation	(1,143,379)	(81,302)
	9,115,055	3,083,082
Other assets:		
Deposits	598,266	544,919
Total assets	\$ 10,067,831	\$ 3,922,520
<b>Liabilities and members' equity</b>		
Current liabilities:		
Accounts payable	\$ 311,014	\$ 415,238
Accrued expenses	130,516	78,478
Total current liabilities	441,530	493,716
Unearned revenues	72,972	-
Members' equity:		
Contributed equity	24,845,731	13,645,731
Accumulated deficit	(15,292,402)	(10,216,927)
Total members' equity	9,553,329	3,428,804
Total liabilities and members' equity	\$ 10,067,831	\$ 3,922,520

See accompanying notes.

Memphis Networkx, LLC

Statements of Operations

	Year ended December 31	
	2002	2001
Revenues	\$ 122,464	\$ -
Cost of sales	706,053	-
	(583,589)	-
Operating expenses:		
Consulting fees	131,309	1,317,985
Professional fees	216,579	637,504
General and administrative	1,895,503	793,602
Compensation and payroll taxes	2,251,773	789,010
Total operating expenses	4,495,164	3,538,101
Loss from operations	(5,078,753)	(3,538,101)
Other income	3,278	1,128
Net loss	<u>\$(5,075,475)</u>	<u>\$(3,536,973)</u>

*See accompanying notes.*

# Memphis Network, LLC

## Statements of Changes in Members' Equity

	<b>Members'</b>	<b>Accumulated</b>	
	<b>Contributions</b>	<b>Deficit</b>	<b>Total</b>
Balance at December 31, 2000	\$ 7,908,731	\$ (6,679,954)	\$ 1,228,777
Contributions	5,737,000	-	5,737,000
Net loss	-	(3,536,973)	(3,536,973)
Balance at December 31, 2001	13,645,731	(10,216,927)	3,428,804
Contributions	11,200,000	-	11,200,000
Net loss	-	(5,075,475)	(5,075,475)
Balance at December 31, 2002	<b>\$24,845,731</b>	<b>\$(15,292,402)</b>	<b>\$ 9,553,329</b>

*See accompanying notes.*

# Memphis Networx, LLC

## Statements of Cash Flows

	Year ended December 31	
	2002	2001
<b>Operating activities</b>		
Net loss	\$ (5,075,475)	\$ (3,536,973)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	1,065,436	41,924
Loss on disposal of equipment and software	2,663	2,054
Changes in operating assets and liabilities:		
Accounts receivable	(49,441)	—
Prepaid expenses	(35,051)	(74,833)
Deposits	(53,347)	(526,325)
Accounts payable	(104,224)	(313,445)
Accrued expenses	52,038	(172,891)
Unearned revenues	72,972	—
Net cash used in operating activities	(4,124,429)	(4,580,489)
<b>Investing activities</b>		
Purchases of property and equipment	(7,100,072)	(952,477)
<b>Financing activities</b>		
Proceeds from members' contributions	11,200,000	5,737,000
Net increase (decrease) in cash	(24,501)	204,034
Cash at beginning of year	219,686	15,652
Cash at end of year	<u>\$ 195,185</u>	<u>\$ 219,686</u>

*See accompanying notes.*



# Memphis Networkx, LLC

## Notes to Financial Statements

December 31, 2002

### 1. Description of Business

Memphis Networkx, LLC (the Company) was organized under the Tennessee Limited Liability Act on November 8, 1999, to provide telecommunications services through the installation of broadband fiber optic cable in the Memphis, Tennessee, area. The Company is a joint venture, the founding members of which were Memphis Light, Gas & Water Division (MLGW), a division of the City of Memphis, Tennessee, and A&L Networks Tennessee, LLC (A&L), a Kansas limited liability company. Effective November 29, 2000, A&L transferred its membership interest to Memphis Broadband, LLC, a Delaware limited liability company, pursuant to the terms of a Membership Interest Purchase Agreement, and the Company amended and restated its operating agreement.

Under the terms of the Company's operating agreement, capital contributions and costs incurred by the Company prior to its formation and through the date of Tennessee Regulatory Authority (TRA) approval are to be shared equally by the members. Subsequent to TRA approval, each of the members shall contribute capital to the Company such that contributed members' equity equals 53% for MLGW and 47% for Memphis Broadband LLC. As of December 31, 2002, member contributions required by the operating agreement to make contributed members' equity equal to 53% for MLGW and 47% for Memphis Broadband had not occurred. Each member has a 50% voting interest in the Company. Future allocations of net operating income or loss and distributions are based on cumulative members' contributions, accumulated members' equity, and the ratio of contributed members' equity. The Company shall continue until it is wound up and liquidated, as stated in the Operating Agreement.

The Company's members have limited liability under the Operating Agreement such that a member of the Company has no personal obligation and is not otherwise personally liable for the acts, debts, liabilities, or obligations of the Company or the acts or omissions of any other member, economic interest owner (as defined in the Operating Agreement), manager, director, employee, or agent of the Company.

MLGW's Board of Commissioners has approved investment in the Company of up to \$32 million, of which approximately \$19.3 million has been funded as of December 31, 2002. MLGW's continued funding is subject to the approval of the Memphis City Council, which approves MLGW's annual budget. The 2003 annual budget has been approved by the Memphis City Council. The obligations of MLGW under the operating agreement are limited to the extent required by applicable state and federal law and by its contract with the Tennessee Valley Authority.

## Memphis Networx, LLC

### Notes to Financial Statements (continued)

#### **1. Description of Business (continued)**

On August 9, 2001, the TRA issued a final order approving the Company's amended and restated operating agreement and granting a certificate of public convenience and necessity for the State of Tennessee.

During the last quarter of 2002, the Company began earning revenues from its principal operations. Accordingly, the Company is no longer considered to be in the development stage. The Company's activities in prior years primarily consisted of establishing its facilities, recruiting personnel, developing business and financial planning, obtaining regulatory approvals, raising capital, and the installation of broadband fiber optic cable.

#### **2. Significant Accounting Policies**

##### **Use of Estimates**

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

##### **Cash and Cash Equivalents**

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

##### **Property and Equipment**

Property and equipment is stated at cost. Depreciation of plant and equipment, broadband equipment, leasehold improvements, furniture, office equipment and computer software is computed using the straight-line method over the estimated useful lives of 3 to 25 years.

##### **Long-lived Assets and Impairments**

The Company evaluates the recoverability of long-lived assets on an annual basis. When it is determined that the long-lived asset cannot be recovered through future operations, it is reduced to its estimated fair value by an impairment charge to operations.

## Memphis Networx, LLC

### Notes to Financial Statements (continued)

#### 2. Significant Accounting Policies (continued)

##### Revenue Recognition

The Company generates revenues from selling network capacity and related services to other communications service providers. The Company recognizes revenues when earned as services are provided throughout the life of each contract with a customer. The majority of the Company's revenues are generated on a monthly recurring basis under contracts of various lengths, ranging from twelve months to twenty years. Revenue is recognized over the service contract period for all general services. Unearned revenues consist primarily of payments received in advance of revenue being earned under contracts for indefeasible rights to use.

Revenues are derived from two general types of services:

**Transport services** - The Company's transport services include the offering of broadband circuits on its metropolitan transport network. Over the Company's metropolitan transport network, it can provision circuits from one of its carrier point facilities to another carrier point facility or to an on-net building via an interconnection in that building.

**Collocation services** - The Company's collocation services include providing customers with the ability to locate their communications and networking equipment at its carrier point facilities in a secure technical operating environment. The Company also can provide its customers with collocation services in the central equipment rooms of certain of its on-net buildings.

The Company evaluates the collectibility of its accounts receivable monthly and records an allowance for doubtful accounts in the period that an account is determined to be uncollectible. The Company grants trade credit to its customers without collateral.

##### Income Taxes

The Company operates under Subchapter K of the Internal Revenue Code and, consequently, is not subject to federal income tax. Income of the Company will flow to the members and they will be responsible for any corresponding tax liability.

##### Reclassifications

Certain amounts in the 2001 financial statements have been reclassified to conform to the 2002 presentation.

## Memphis Networkx, LLC

### Notes to Financial Statements (continued)

#### 2. Significant Accounting Policies (continued)

##### Advertising Costs

The Company expenses the costs of advertising and promoting its services as incurred.

##### Accounting Pronouncements

Effective January 1, 2002, the Company adopted the provisions of Statements of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. SFAS 144 supersedes SFAS 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*, and provides a single accounting method for the disposal of long-lived assets from continuing and discontinued operations. The adoption of this statement had no effect on the Company's financial position or results of operations.

#### 3. Leases

Total rental expense for operating leases was approximately \$239,000 and \$119,000 for the years ended December 31, 2002 and 2001, respectively.

The following summarizes approximate minimum future rental payments required under noncancelable operating leases that have initial or remaining lease terms in excess of one year as of December 31, 2002:

2003	\$ 155,000
2004	142,000
2005	129,000
2006	127,000
2007	131,000
Thereafter	510,000
	<u>\$1,194,000</u>

As part of a vehicle operating lease, one of the Company's members obtained a letter of credit on behalf of the Company in the amount of \$57,000 that expired on February 3, 2003.

As part of a building operating lease, the Company obtained a letter of credit in the amount of \$160,000 at December 31, 2002. The required amount is reduced by \$40,000 per year over the lease term.

**MEMPHIS NETWORKX, LLC**

**FINANCIAL STATEMENTS**

December 31, 2004 and 2003

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## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Members  
Memphis Networkx, LLC  
Memphis, Tennessee

We have audited the accompanying balance sheets of Memphis Networkx, LLC, as of December 31, 2004 and 2003, and the related statements of operations, changes in members' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Memphis Networkx, LLC as of December 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*Watkins Uiberall, PLLC*

Memphis, Tennessee

February 26, 2005, except for Note 8, as to which the date is July 6, 2005

# MEMPHIS NETWORKX, LLC

## BALANCE SHEETS

December 31, 2004 and 2003

	<u>Assets</u>	
	2004	2003
<b>Current Assets</b>		
Cash and cash equivalents	\$ 58,659	\$ 146,152
Trade accounts receivables	758,966	97,192
Prepaid expenses	38,060	54,106
Deposits	33,000	33,000
Total current assets	888,685	330,450
<b>Property and Equipment</b>		
Plant equipment	6,813,208	5,917,594
Computer software	2,452,017	2,443,285
Broadband equipment	4,160,718	2,997,890
Furniture and office equipment	358,102	338,796
Leasehold improvements	954,896	903,995
	14,738,941	12,601,560
Less: accumulated depreciation	(4,776,980)	(2,804,811)
Net property and equipment	9,961,961	9,796,749
<b>Deposits</b>	542,428	535,049
<b>Total assets</b>	<u>\$ 11,393,074</u>	<u>\$ 10,662,248</u>
	<u>Liabilities and Members' Equity</u>	
<b>Current Liabilities</b>		
Accounts payable	\$ 1,502,980	\$ 638,456
Accrued expenses	298,391	188,859
Note payable - related party	85,000	-
Total current liabilities	1,886,371	827,315
Unearned revenues	91,764	65,898
<b>Total liabilities</b>	1,978,135	893,213
<b>Members' Equity</b>		
Contributed equity	34,117,731	30,585,731
Accumulated deficit	(24,702,792)	(20,816,696)
<b>Total members' equity</b>	9,414,939	9,769,035
<b>Total liabilities and members' equity</b>	<u>\$ 11,393,074</u>	<u>\$ 10,662,248</u>

The accompanying notes are an integral part of these financial statements.



# MEMPHIS NETWORKX, LLC

## STATEMENTS OF OPERATIONS

For the Years Ended December 31, 2004 and 2003

	2004	2003
Revenue	\$ 3,569,094	\$ 675,477
Cost of sales	2,354,128	1,208,607
Gross profit (loss)	1,214,966	(533,130)
Operating expenses		
Consulting fees	23,203	131,469
Professional fees	42,522	85,171
General and administrative	3,180,926	2,807,144
Compensation and payroll taxes	1,857,132	1,969,823
Total operating expenses	5,103,783	4,993,607
Loss from operations	(3,888,817)	(5,526,737)
Other Income (Expense)		
Interest income	3,034	3,822
Loss on disposal of equipment and software	-	(1,379)
Loan Interest Expense	(313)	-
Total other income (expense)	2,721	2,443
Net loss	\$ (3,886,096)	\$ (5,524,294)

The accompanying notes are an integral part of these financial statements.

**MEMPHIS NETWORKX, LLC**

**STATEMENTS OF CHANGES IN MEMBERS' EQUITY**

For the Years Ended December 31, 2004 and 2003

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	<u>Members'</u> <u>Contributions</u>	<u>Accumulated</u> <u>Deficit</u>	<u>Total</u>
Balance at December 31, 2002	\$ 24,845,731	\$ (15,292,402)	\$ 9,553,329
Contributions	5,740,000	-	5,740,000
Net loss	<u>-</u>	<u>(5,524,294)</u>	<u>(5,524,294)</u>
Balance at December 31, 2003	30,585,731	(20,816,696)	9,769,035
Contributions	3,532,000	-	3,532,000
Net loss	<u>-</u>	<u>(3,886,096)</u>	<u>(3,886,096)</u>
Balance at December 31, 2004	<u>\$ 34,117,731</u>	<u>\$ (24,702,792)</u>	<u>\$ 9,414,939</u>

---

The accompanying notes are an integral part of these financial statements.

**MEMPHIS NETWORKX, LLC****STATEMENTS OF CASH FLOWS**

For the Years Ended December 31, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Cash Flows From (Used For) Operating Activities:		
Net loss	\$ (3,886,096)	\$ (5,524,294)
Adjustments to Reconcile Net Loss to Net Cash Used For Operating Activities:		
Depreciation	1,972,167	1,662,521
Loss on disposal of equipment and software	-	1,379
Changes in Operating Assets and Liabilities:		
Increase (decrease) in cash and cash equivalents:		
Accounts receivable	(661,774)	(47,751)
Prepaid expenses	16,046	55,778
Deposits	(7,379)	30,217
Accounts payable	864,524	327,442
Accrued expenses	109,532	58,343
Unearned revenues	25,866	(7,074)
Total adjustments	<u>2,318,982</u>	<u>2,080,855</u>
Net cash used for operating activities	(1,567,114)	(3,443,439)
Cash Flows Used For Investing Activities:		
Purchases of property and equipment	(2,137,379)	(2,345,594)
Cash Flows From Financing Activities:		
Proceeds from issuance of note payable to a related party	85,000	-
Member contributions	<u>3,532,000</u>	<u>5,740,000</u>
Net cash from financing activities	<u>3,617,000</u>	<u>5,740,000</u>
Net decrease in cash and cash equivalents	(87,493)	(49,033)
Cash and cash equivalents - beginning of year	<u>146,152</u>	<u>195,185</u>
Cash and cash equivalents - end of year	<u>\$ 58,659</u>	<u>\$ 146,152</u>

The accompanying notes are an integral part of these financial statements.

# MEMPHIS NETWORK, LLC

## NOTES TO FINANCIAL STATEMENTS

December 31, 2004 and 2003

---

### NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Organization and Nature of Operations

Memphis Network, LLC (the Company) was organized under the Tennessee Limited Liability Act on November 8, 1999, to provide telecommunications services through the installation of broadband fiber optic cable in the Memphis, Tennessee, area. The Company is a joint venture between the Electric Division of Memphis Light, Gas & Water Divisions (MLGW, a component unit of the City of Memphis), and Memphis Broadband, LLC, a Delaware limited liability company. On August 9, 2001, the TRA issued a final order approving the Company's amended and restated operating agreement and granted a certificate of public convenience and necessity for the State of Tennessee.

Under the terms of the Company's Operating Agreement, capital contributions and cost incurred by the Company prior to its formation and through the date of Tennessee Regulatory Authority (TRA) approval are to be shared equally by the members. Subsequent to TRA approval, MLGW has continued to provide periodic investments of capital as requested by the Company. At December 31, 2004 and 2003, MLGW's share of capital contributions was approximately 84% and 82%, respectively. Allocations of net operating income or loss and distributions are based on cumulative members' contributions, accumulated members' equity (loss), and the ratio of contributed members' equity. The Company shall continue until it is wound up and liquidated, as stated in the Operating Agreement.

Effective April 1, 2002, MLGW entered into a capital contribution agreement with Memphis Broadband, LLC. The agreement established planned monthly capital contributions through 2004 for both members. The agreement also amended the operating agreement to allow one member to contribute the required capital on behalf of the other member. If a member makes such a disproportionate contribution, the agreement allows the contributing member to charge the other member interest on the disproportionate contribution or increase its ownership percentage. Each member has a voting interest in the Company equal to their current sharing ratio as defined in the Operating Agreement. On the contribution date, the sharing ratio of net operating income or loss and distributions is adjusted to reflect the increased capital contribution. For the years ended December 31, 2004 and 2003, MLGW contributed \$3,532,000 and \$5,740,000, respectively, which was equal to both members' required capital contributions.

The Company's members have limited liability under the Operating Agreement such that a member of the Company has no personal obligation and is not otherwise personally liable for the acts, debts, liabilities, or obligations of the Company or the acts or omissions of any other member, economic interest owner (as defined in the Operating Agreement), manager, director, employee, or agent of the Company.

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#### Method of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

### Use of Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and 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.

### Concentrations

The Company's credit risks relate to cash and cash equivalents and accounts receivable. The Company maintains cash at a bank. Those accounts are insured by the Federal Deposit Insurance Corporation up to an aggregate of \$100,000.

For the year ending December 31, 2004, two customers comprised 43.68% of total sales. For the year ending December 31, 2003, five customers comprised 74.4% of total sales.

As of December 31, 2004, one customer comprised 66.29% of total accounts receivable.

### Cash and Cash Equivalents

For purposes of the statement of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

### Accounts Receivable

Accounts receivable consists primarily of amounts due from customers in the Memphis area. The Company performs continual credit evaluations of its customers and does not consider an allowance for doubtful accounts necessary.

### Property and Equipment

Property and equipment is stated at cost. Depreciation of plant and equipment, broadband equipment, leasehold improvements, furniture, office equipment and computer software is computed using the straight-line method over the estimated useful lives of 3 to 25 years.

### Revenue Recognition

The Company generates revenues from selling network capacity and related services to other communications service providers. The Company recognizes revenues when earned as services are provided throughout the life of each contract with a customer. The majority of the Company's revenues are generated on a monthly recurring basis under contracts of various lengths, ranging from twelve months to twenty years. Revenue is recognized over the service contract period for all general services. Unearned revenues consist primarily of payments received in advance of revenue being earned under contracts for indefeasible rights to use.

### Income Taxes

A limited liability company is treated as a partnership for federal income tax purposes and is not subject to federal income taxes. The taxable income or loss of the Company is included in the individual income tax returns of its members based upon their percentage of ownership. Consequently, no provision for federal income taxes is required in the accompanying financial statements. The Company, however, is subject to state income taxes.

Deferred state income taxes have been determined using the asset and liability method of accounting for state income taxes. Under this method, state deferred tax assets and liabilities are determined based on the difference between the financial statement carrying amounts and tax bases of assets and liabilities using enacted state tax rates in effect for the years in which the differences are expected to reverse. This method also allows for the recognition for deferred tax assets in the current period for the future benefit of net operating loss carryforwards and items for which expenses have been recognized for financial statement purposes, but will be deductible in future periods for income tax purposes. The temporary differences in these financial statements relate primarily to depreciation, amortization and net operating loss carryforwards. A valuation allowance is provided for net state deferred tax assets as it is uncertain as to the future realization of these benefits.

### Advertising

All advertising costs are expensed as incurred. Advertising costs for the years ended December 31, 2004 and 2003 were \$31,958 and \$0, respectively.

### Long-Lived Assets and Impairments

The Company evaluates the recoverability of long-lived assets on an annual basis. When it is determined that the long-lived asset cannot be recovered through future operations, it is reduced to its estimated fair value by an impairment charge to operations.

## **NOTE 2 - LEASES**

The Company leases office space, automobiles, and other pieces of equipment under operating leases. Total rent expense for the years ended December 31, 2004 and 2003 was \$995,164 and \$523,871, respectively. Future commitments under these leases for the years ending December 31 are as follows:

2005	\$ 717,490
2006	703,592
2007	325,422
2008	130,527
2009	130,527
Thereafter	249,223
	<u>\$ 2,256,781</u>

As a part of a building operating lease, the Company obtained a letter of credit in the amount of \$160,000 at December 31, 2002. The required amount is reduced by \$40,000 per year over the lease term.

At December 31, 2004 and 2003, the remaining balance was \$80,000 and \$120,000, respectively. The Company has a certificate of deposit that serves as collateral for the letter of credit and is shown on the balance sheet in deposits.

### NOTE 3 – PROFIT SHARING PLAN

The Company sponsors a profit sharing plan under the provisions of Section 401(k) of the Internal Revenue Code covering substantially all full-time employees. Eligibility requirements are at least one month of employment and attainment of age 21. Employees become fully vested after six years in the plan. The Company's contributions to the plan are voluntary and the Company elected not to make a contribution for the years ended December 31, 2004 and 2003.

### NOTE 4 – STATE INCOME TAXES

The tax effects of temporary differences that give rise to the significant portions of deferred tax assets and deferred tax liabilities at December 31, are as follows:

	2004	2003
Deferred Tax Assets		
Due to benefit of state net operating loss carryforwards	\$ 1,524,775	\$ 1,066,125
Due to benefit of amortization of start up costs	318,411	450,167
Deferred Tax Liabilities		
Due to depreciation	(243,860)	(168,912)
Net deferred tax asset	1,599,326	1,347,380
Valuation allowance	(1,599,326)	(1,347,380)
	\$ -	\$ -

At December 31, 2004, the Company had state tax loss carryforwards of approximately \$23,455,000 expiring through 2019, which are available to reduce future state taxable income.

### NOTE 5 – RELATED PARTY TRANSACTIONS

As of December 31, 2004 and 2003, the Company owed a member \$37,940 and \$34,471, respectively for pole attachment and conduit fees. As of December 31, 2004 and 2003, the Company had two deposits with a member totaling \$200,790.

For the years ended December 31, 2004 and 2003, the Company paid a member \$141,885 and \$135,657, respectively for pole attachment and conduit fees. For the years ended December 31, 2004 and 2003, the Company paid \$84,632 and \$30,983, respectively for utilities.

As of December 31, 2004 and 2003, the Company had receivables from a member totaling \$46,112 and \$0, respectively for fiber installation services.

For the years ended December 31, 2004 and 2003, the Company had revenues from a member totaling \$84,152 and \$0, respectively for fiber installation, collocation services, and internet services.

For the years ended December 31, 2004 and 2003, the Company had revenues from the City of Memphis of approximately \$1,009,000 and \$0, respectively for fiber installation services.

At December 31, 2004 and 2003, the Company had receivables from the City of Memphis of approximately \$503,000 and \$0, respectively for fiber installation services.

As of December 31, 2004, the Company has an uncollateralized bridge loan outstanding of \$85,000 payable to a company owned by the Chief Executive Officer of Memphis Networkx, LLC. The note bears interest at 2% and interest is payable monthly.

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

#### NOTE 6 – FRANCHISE AGREEMENTS

The Company has entered into various franchise agreements with certain municipalities in Shelby County. The agreements are for periods of between five and twenty years. These agreements authorize the Company to use these municipalities' streets to operate, or lease and maintain a telecommunication system within the municipalities' city limits. As part of these agreements, some of the municipalities require deposits and fees equal to 5% of the gross revenues charged for services provided in the municipality. The following is a list of deposits and fees accrued to the various municipalities at December 31:

	2004		2003	
	Deposit	Accrued Franchise Fees	Deposit	Accrued Franchise Fees
City of Memphis	\$ 100,000	\$ 69,758	\$ 100,000	\$ 39,897
City of Germantown	50,000	670	-	-
City of Collierville	50,000	-	-	-
City of Bartlett	-	-	-	-
	<u>\$ 200,000</u>	<u>\$ 70,428</u>	<u>\$ 100,000</u>	<u>\$ 39,897</u>

The deposits are shown on the balance sheet under deposits and the franchise fees are shown on the balance sheet under accrued expenses.



## NOTE 7 – LONG-TERM CONTRACTS

The Company has entered into certain non-cancelable long-term contracts to provide services to its customers. Estimated future service and construction revenue under contracts longer than one year in effect at December 31, 2005 is as follows:

2005	\$ 2,750,024
2006	2,267,648
2007	1,350,730
2008	844,965
2009	317,816
	<u>\$ 7,531,183</u>

## NOTE 8 – SUBSEQUENT EVENTS

On April 7, 2005, MLGW agreed to provide an additional ninety-day bridge loan of up to \$750,000 to the Company. The loan will bear interest at 8% per annum.

On June 15, 2005 the Company obtained financing through a bank. The financing agreement provides for a line-of-credit of \$2,000,000 and a term loan of \$5,000,000. The line-of-credit expires May 15, 2007 and bears interest at the thirty day Libor rate plus 1.45%. The term loan is to be funded in two phases. The first phase shall provide funds of \$2,915,643 and is guaranteed by certain private equity owners of the Company. The second phase shall fund the remaining balance of \$2,084,357 and is contingent upon obtaining additional guarantees from certain other private equity owners of the Company. The term loan shall bear interest at the U.S. Treasury rate, in effect at the close of the agreement, plus 1.7%. The bridge loans referred to in Note 5 and Note 8 were subsequently paid off on June 23, 2005 using the line of credit mentioned in this footnote.