CSG SYSTEMS INTERNATIONAL INC
Form 10-K
February 28, 2008
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2007

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number 0-27512

CSG SYSTEMS INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Delaware	**47-0783182**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

9555 Maroon Circle

Englewood, Colorado 80112

(Address of principal executive offices, including zip code)

(303) 200-2000

(Registrant s telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, Par Value $0.01 Per Share	**Nasdaq Stock Market LLC**

Securities Registered Pursuant to Section 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to the Form 10-K. ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of large accelerated filer, accelerated file and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ¨ No x

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, computed by reference to the last sales price of such stock, as of the close of trading on June 29, 2007 was **$1,110,309,714**.

Shares of common stock outstanding at February 25, 2008: **34,922,179**

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s Proxy Statement for its 2008 Annual Meeting of Stockholders to be filed on or prior to April 29, 2008, are incorporated by reference into Part III of the Form 10-K.

Table of Contents

CSG SYSTEMS INTERNATIONAL, INC.

2007 FORM 10-K

TABLE OF CONTENTS

		Page
PART I		
Item 1.	Business	3
Item 1A.	Risk Factors	10
Item 1B.	Unresolved Staff Comments	14
Item 2.	Properties	14
Item 3.	Legal Proceedings	14
Item 4.	Submission of Matters to a Vote of Security Holders	14
PART II		
Item 5.	Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	19
Item 6.	Selected Financial Data	22
Item 7.	Management s Discussion and Analysis of Financial Condition and Results of Operation	24
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	43
Item 8.	Financial Statements and Supplementary Data	44
Item 9.	Changes in and Disagreements With Accountants on Accounting and Financial Disclosure	82
Item 9A.	Controls and Procedures	82
Item 9B.	Other Information	82
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	82
Item 11.	Executive Compensation	82
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	82
Item 13.	Certain Relationships and Related Transactions, and Director Independence	83
Item 14.	Principal Accounting Fees and Services	83
PART IV		
Item 15.	Exhibits, Financial Statement Schedules	83
Signatures		84

Table of Contents

PART I

Item 1. Business
Overview

CSG Systems International, Inc. (the Company , CSG , or forms of the pronoun we) was formed in October 1994 and acquired all of the outstanding stock of CSG Systems, Inc. (formerly Cable Services Group, Inc.) from First Data Corporation (FDC) in November 1994. CSG Systems, Inc. had been a subsidiary or division of FDC from 1982 until this acquisition.

We are a leading provider of outsourced solutions that facilitate customer interaction management on the behalf of our clients, generating approximately 95% of our 2007 revenues from the North American cable and Direct Broadcast satellite (DBS) communications markets. Our solutions also support an increasing number of other industries such as financial services, utilities, telecommunications, and home security.

Our solutions manage key customer interactions such as set-up and activation of customer accounts, sales support and marketing, order processing, invoice calculation (i.e., customer billing), production and mailing of monthly customer invoices, management reporting, electronic presentment and payment of invoices, automated and interactive messaging, and deployment and management of the client s field technicians to the customer s home. Our unique combination of solutions, services, and expertise ensure that our clients can rapidly launch new service offerings, improve operational efficiencies, and deliver a high-quality customer experience in a competitive and ever-changing marketplace.

Our principal executive offices are located at 9555 Maroon Circle, Englewood, Colorado 80112, and the telephone number at that address is (303) 200-2000. Our common stock is listed on the NASDAQ Stock Market, Inc. under the symbol CSGS . We are an S&P Midcap 400 company.

General Development of Business

Comcast Business Relationship. In September 1997, we entered into a 15-year exclusive contract (the Master Subscriber Agreement) with Tele-Communications, Inc. (TCI) to consolidate all TCI customers onto our customer care and billing systems. This transaction allowed our company to substantially increase the number of customers processed on our systems, and at the time, was one of the catalysts to the growth of our domestic broadband business.

In 1999 and 2000, respectively, AT&T completed its mergers with TCI and MediaOne Group, Inc. (MediaOne), and consolidated the merged operations into AT&T Broadband (AT&T), and we continued to service the merged operations under the terms of the Master Subscriber Agreement. On November 18, 2002, Comcast Corporation (Comcast) completed its merger with AT&T, and assumed the Master Subscriber Agreement. Comcast is our largest client, making up approximately 27% of our total revenues in 2007.

During 2002 and 2003, we were involved in various legal proceedings with Comcast, consisting principally of arbitration proceedings related to the Master Subscriber Agreement. In October 2003, we received an unfavorable ruling in the arbitration proceedings. The Comcast arbitration ruling included an award of $119.6 million to be paid by us to Comcast. The award was based on the arbitrator s determination that we had violated the most favored nations (MFN) clause of the Master Subscriber Agreement. We recorded the full impact from the arbitration ruling in the third quarter of 2003 as a charge to revenues. In addition, the arbitration ruling also required that we invoice Comcast for lower fees under the MFN clause of the Master Subscriber Agreement beginning in October 2003. This had the effect of reducing quarterly revenues from Comcast by approximately $13-14 million ($52-56 million annually), when compared to amounts prior to the arbitration ruling. In March 2004, we signed a new contract with Comcast (the Comcast Contract) that runs through December 31, 2008. The Comcast Contract superseded the former Master Subscriber Agreement that was set to expire at the end of

2012. The pricing inherent in the Comcast Contract was consistent with that of the arbitration ruling in October 2003. See Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) for additional discussion of our business relationship with Comcast.

Discontinued Operations. In February 2002, we acquired the billing and customer care assets of Lucent Technologies (Lucent). Lucent s billing and customer care business consisted primarily of: (i) software products and related consulting services acquired by Lucent when it purchased Kenan Systems Corporation in February 1999; (ii) BILLDATS Data Manager mediation software; and (iii) elements of Lucent s client support, product support, and sales and marketing organizations (collectively, the Kenan Business). This acquisition allowed us to expand our customer care and billing product and service offerings into international markets. On December 9, 2005, we sold our Global Software Services (GSS) business (GSS Business), which consisted principally of the acquired Kenan Business, to Comverse, Inc., a division of Comverse Technology, Inc. (Comverse). As a result of our sale of the GSS Business, we no longer provide customer care and billing products or services outside of North America. The decision to sell the GSS Business allowed us intensify our focus on our core competencies in the cable and DBS markets utilizing our Advanced Convergent Platform (ACP) product and related services. See Note 2 to our Consolidated Financial Statements and MD&A for additional discussion of the sale of the GSS Business.

In addition to the sale of the GSS Business noted above, we also sold our plaNet Consulting business to a group of private investors led by the plaNet management team on December 30, 2005. As a result of these sales, the results of operations for the GSS and plaNet businesses have been reflected as discontinued operations for all periods presented in the accompanying Consolidated Statements of Income. The remainder of the Business section of this Form 10-K is focused on our continuing operations. See Notes 2 and 5 to our Consolidated Financial Statements and MD&A for additional discussion of our reporting of discontinued operations, and the impact these sales had on our reporting of segment and related information.

Industry Overview

Background. We provide our customer interaction management solutions primarily to the North American cable and DBS communications markets. Our client base includes some of the world s largest and most innovative service providers of bundled multi-channel video, Internet, voice and IP-based services. Our solutions coordinate and manage the many aspects of the customers interactions with a service provider, from the initial set-up and activation of customer accounts, to the support of various service activities, through the presentment of customer invoices and accounts receivable management.

Market Conditions of Communications Industry. The North American communications industry has experienced significant consolidation and increased competition among service providers, and there is the possibility of further consolidation. Market consolidation results in a fewer number of service providers who have massive scale and can deliver a total communications package. The significant plant upgrades and network rationalizations that have taken place have allowed service providers to focus their attention on new revenue and growth opportunities. In addition, new competitors, new technologies, and unique partnerships are forcing service providers to be more creative in their approaches for rolling out new products and services and enhancing their customers experiences. These factors drive the demand for scalable, flexible, and cost efficient customer interaction management solutions, which we believe will provide us with revenue opportunities.

However, another facet of this market consolidation poses certain risks to our company. The consolidation of service providers decreases the potential number of buyers for our products and services, and carries the inherent risk that the consolidators may choose to move their purchased customers to a competitor s solution. Should this consolidation result in a concentration of customer accounts being owned by companies with whom we do not have a relationship, or with whom competitors are entrenched, it could negatively affect our ability to maintain or expand our market share, thereby having a material adverse effect to our results of operations. In addition, service providers at times have chosen to use their size and scale to exert more pressure on pricing negotiations.

Table of Contents

In addition, it is widely anticipated that traditional wireline and wireless telephone service providers will continue their aggressive pursuit of providing convergent services. These providers have recently entered the residential video market, a market which has historically been dominated by our clients. Should these traditional telephone service providers be successful in their video strategy, it could threaten our clients market share, and thus our revenues as, generally speaking, traditional wireline and wireless telephone providers do not currently use our products and services.

Business Strategy

Our business strategy is designed to achieve growth of revenues and profitability. The key elements of our business strategy include:

Expand Our Core Customer Information Processing and Output Solutions. Most of our revenues are generated from our core customer information processing and output solutions. We provide a fully outsourced processing solution that combines the reliability and high-volume transaction processing capabilities of an enterprise server platform with the flexibility of client/server architecture. As of December 31, 2007, we had approximately 45 million customer accounts on our processing systems. In addition, we provide a full suite of output solutions that include statement design, printing, marketing services, electronic bill presentment, inserting and mailing on a variety of high-speed equipment. We provide our output solutions primarily to those clients that utilize our information processing services, but also provide such services to clients that do not utilize our outsourced customer information processing services. As of December 31, 2007, our average production volume for our output solutions was approximately 60 million customer statements per month.

Our customer information processing and output solutions provide highly predictable, recurring revenues through multi-year contracts with a client base that includes leading cable and DBS providers. We will continue to leverage our investment in and expertise in providing enhanced customer interaction management solutions as we look to expand these core elements of our business. Our customer information processing solutions are currently designed to focus on the North American cable and DBS markets. While our output solution clients are primarily those that utilize our customer information processing solutions, we look to continue to expand this solution set to other markets that demand high-quality, recurring monthly output solutions, such as financial services, utilities, telecommunications, and home security.

Increase the Penetration of Ancillary Products/Services. We provide a complete suite of fully-integrated customer interaction management products and services that complement our customer information processing and output solutions platforms. While our primary value proposition to our clients is the breadth and depth of this integrated offering, we are evolving our product solutions to allow clients to utilize certain of our products as point solutions.

Our ancillary products and services enable and automate various aspects of a service provider s customer interactions, ranging from the call center, to the field technicians, to the end customer. As our clients businesses have consolidated and become much more complex with an increasingly diverse portfolio of service offerings, we have seen an increase in demand for our ancillary products and services, as our products are designed to help our clients solve their ever-changing customer interaction business needs as they arise.

Evolve Our Products and Services to Meet the Changing Needs of Our Clients. In 1995, we offered our solutions solely to providers of analog cable video. Since then, our solutions have evolved and expanded to accommodate DBS, digital video, high-speed Internet (HSI) and digital voice. Our clients continue to look to add more services to their product bundle, including advanced IP and wireless services, as well as services to commercial customers. Our continued investment in our solution set is designed to expand our customer interaction management capabilities to enable our clients to grow their product offerings, control costs, and provide better customer service.

Enhance Growth Through Focused Acquisitions. We follow a disciplined approach in acquiring assets and businesses which provide the technology and technical personnel to expedite our product development efforts, provide complementary products and services, increase market share, and/or provide access to new markets and clients.

Continue Technology Leadership. We believe that our product technology and integrated suite of software solutions gives communications service providers a competitive advantage. Our continuing investment in research and development (R&D) is designed to position us to meet the growing and evolving needs of existing and potential clients. Over the last five years, we have invested approximately $200 million, or approximately 11% of our total revenues, into R&D.

In summary, our R&D and recent acquisition efforts, discussed below, have better positioned us to assist our clients and enable both of us to grow through maximizing every customer interaction. We have continually shown our commitment to deliver solutions and services to our clients with the highest level of performance and functionality, and with our continued investment in R&D and acquisition activities, we believe we will continue to find ways to solve our clients business challenges and provide them with a competitive advantage. While we continue to strive to provide superior solutions and services to our existing clients, we will continue to focus on growing and diversifying our business and finding new ways to expand our footprint in some of the new vertical markets we have entered with our recent acquisitions**.**

Description of Business

Clients. We work with the leading cable and DBS providers located in the U.S. and Canada. A partial list of those service providers as of December 31, 2007 is included below:

Charter Communications (Charter)	DISH Network Corporation (DISH), formerly EchoStar Communications Corporation
Comcast Corporation (Comcast)	Mediacom Communications
Cox Communications	Time Warner Inc. (Time Warner)

The North American communications industry has experienced significant consolidation over the last few years, resulting in a large percentage of the market being served by a limited number of service providers with greater size and scale. Consistent with this market concentration, a large percentage of our historical revenues have been generated from a limited number of clients, with approximately 70% of our revenues being generated from our four largest clients, which include Comcast, DISH, Time Warner, and Charter. Revenues from these clients represented the following percentages of our total revenues for 2007 and 2006:

	2007	2006
Comcast	27%	24%
DISH	20%	19%
Time Warner	13%	12%
Charter	9%	11%

Research and Development. Our clients are facing more competition than ever before from new entrants, and at the same time, are deploying new services at a faster pace than ever before, dramatically increasing the complexity of their business operations. Therefore, we continue to invest heavily in R&D to ensure that we stay ahead of our clients needs and advance our clients business as well as our own. We recognize these challenges and believe our value proposition is to provide solutions that help our clients ensure that each interaction they have with their customers is an opportunity to create value and deepen the business relationship. As a result of our R&D efforts, we have broadened our footprint within our client base with many innovative product offerings.

Our total R&D expenses were $58.3 million and $46.2 million, respectively, for 2007 and 2006, or approximately 14% and 12% of total revenues. In the near term, we expect that the percentage of our total revenues to be spent on R&D to be relatively consistent with that of 2007, with the level of our R&D spend highly dependent upon the opportunities that we see in our markets.

There are certain inherent risks associated with significant technological innovations. Some of these risks are described in this report in our Risk Factors section below.

Products and Services. Our primary product offerings include our core outsourced processing product, Advanced Convergent Platform (ACP), and related services and software products, to include our output solutions. A background in high-volume transaction processing and statement production, complemented with world-class applications software, allows us to offer one of the most comprehensive, pre-integrated products and services solutions to the cable and DBS market. We believe this pre-integrated approach and outsourced delivery model allows our clients to get new product offerings to market quickly and provide high-quality customer service in a cost effective manner.

We license certain software products (e.g., ACSR, Workforce Express, etc.) and provide our professional services principally to our existing base of processing clients to enhance the core functionality of ACP, increase the efficiency and productivity of the clients operations, and allow clients to effectively roll out new products and services to new and existing markets, such as HSI and telephony to residential and commercial customers.

Historically, a substantial percentage of our total revenues have been generated from ACP processing and output services and related software products. These products and services are expected to provide a substantial percentage of our total revenues in the foreseeable future as well.

ACP Architectural Upgrade and Migration. During 2004, we completed a significant architectural upgrade to our primary product, then called CCS, and related services and software products. This enhancement, called ACP, has increased our ability to support convergent broadband services including cross-service bundling, convergent order entry and advanced service provisioning capabilities for multiple products to one end customer, such as video, HSI, and Voice over Internet Protocol (VoIP). This advanced convergent solution for broadband service providers facilitates our clients offering of combinations of video, voice and data services (commonly referred to in the industry as the triple-play service offering). We have successfully migrated all of the cable customer accounts processed on our systems to our ACP platform, giving our clients the full benefit of our technology to support the advanced marketing and rollout of new services.

Continued Evolution of ACP. We continue to evolve ACP, both functionally and architecturally, in response to market demands that our products have certain functional features and capabilities, as well as architectural flexibilities (such as service oriented architecture, or SOA). This product evolution will result in the modularization of certain product functionality that historically has been tightly integrated with the ACP platform, which will allow us to respond more quickly to required changes to our products and provide greater interoperability with other computer systems. Although our primary value proposition to our clients will continue to be the breadth and depth of our fully pre-integrated solution, these R&D efforts will also allow us to separate certain software components so as to allow such components to be marketed on a stand-alone basis where a specific client requirement and/or business need dictates, including the use of certain products across non-CSG customer care and billing systems.

Telution Acquisition. As part of this product evolution strategy, we acquired Telution, Inc. (Telution) in March of 2006 to further expand these capabilities around our ACP platform. Our recent R&D efforts include the integration of these acquired technologies into our solution set. In particular, the acquired software assets are an integral part of the new functionality that has been added to our ACP platform since the acquisition, including a robust product catalog, offer and order management functions, and product capabilities to support commercial customers.

Table of Contents

ComTec Acquisition. In July of 2007 we acquired ComTec, Inc. (ComTec), to expand our output solutions footprint and capabilities. With this acquisition, we added enhanced statement production and electronic statement presentation hardware and software technologies, as well as additional plant capacities. These technologies, which include extensive highlight color and cut-sheet printing capabilities, will accelerate our ability to offer enhanced output functionality to existing and prospective customers. In addition, the acquisition increased our presence in our core cable television and DBS markets, while also providing an established customer base in new industry verticals such as telecommunications, home security, healthcare, financial services, and utilities.

Prairie Acquisition. In August of 2007 we acquired Prairie Voice Services, Inc. This business, which was renamed Prairie Interactive Messaging, Inc. (Prairie), extends our suite of products and solutions that help our clients maximize the value of their interactions with their customers. Prairie provides inbound and outbound automated voice, text/SMS, email, and fax messaging services to manage workforce communications, collections, lead generation, automated order capture, service outage notifications, and other key business functions. We acquired Prairie to extend our customer interaction management capabilities within our core cable television and DBS markets, while also providing an established customer base in new industry verticals such as financial services and telecommunications.

FDC Data Processing Facility. We outsource to FDC the data processing and related computer services required for the operation of our processing services. Our ACP proprietary software and other software applications are run in FDC s facility to obtain the necessary enterprise server computer capacity and other computer support services without us having to make the substantial capital and infrastructure investments that would be necessary for us to provide these services internally. Our clients are connected to the FDC facility through a combination of private and commercially-provided networks. Our service agreement with FDC expires June 30, 2010, and is cancelable only for cause, as defined in the agreement. We believe we could obtain mainframe data processing services from alternative sources, if necessary. We have a business continuity plan as part of our agreement with FDC should the FDC data processing center suffer an extended business interruption or outage. This plan is tested on an annual basis.

Client and Product Support. Our clients typically rely on us for ongoing support and training needs related to our products. We have a multi-level support environment for our clients, which includes dedicated account management teams to support the business, operational, and functional requirements of each client. These account teams help clients resolve strategic and business issues and are supported by our Product Support Center (PSC), which operates 24 hours a day, seven days a week. Clients call an 800 number, and through an automated voice response unit, have their calls directed to the appropriate PSC personnel to answer their questions. We have a full-time training staff and conduct ongoing training sessions both in the field and at our training facilities.

Sales and Marketing. We organize our sales efforts to existing clients primarily within our dedicated account teams, with senior level account managers who are responsible for new revenues and renewal of existing contracts within a client account. The account teams are supported by sales support personnel who are experienced in the various products and services that we provide. In addition, we have dedicated staff engaged in selling our products and services to prospective clients.

Competition. The market for customer interaction management products and services in the converging communications industry in North America, as well as in other industries we serve, is highly competitive. We compete with both independent outsourced providers and in-house developers of customer management systems. We believe that our most significant competitors in our primary markets are Amdocs Limited, Convergys Corporation, Oracle Corporation, and in-house systems. Some of our actual and potential competitors have substantially greater financial, marketing, and technological resources than us.

We believe service providers in our industry use the following criteria when selecting a vendor to provide customer care and billing products and services: (i) functionality, scalability, flexibility, interoperability, and architecture of the software assets; (ii) the breadth and depth of pre-integrated product solutions; (iii) product quality, client service, and support; (iv) quality of R&D efforts; and (v) price. We believe that our products and services allow us to compete effectively in these areas.

Proprietary Rights and Licenses

We rely on a combination of trade secret and copyright laws, nondisclosure agreements, and other contractual and technical measures to protect our proprietary rights in our products. While we hold a limited number of patents on some of our newer products, we do not rely upon patents as a primary means of protecting our rights in our intellectual property. There can be no assurance that these provisions will be adequate to protect our proprietary rights. Although we believe that our intellectual property rights do not infringe upon the proprietary rights of third parties, there can be no assurance that third parties will not assert infringement claims against us or our clients.

We continually assess whether there is any risk to our intellectual property rights. Should these risks be improperly assessed, or if for any reason should our right to develop, produce and distribute our products be successfully challenged or be significantly curtailed, it could have a material adverse impact on our financial condition and results of operations.

Employees

As of December 31, 2007, we had a total of 1,877 employees, an increase of 192, or 11%, from December 31, 2006. The increase in number of employees is due to (i) the addition of employees from the ComTec and Prairie acquisitions, and (ii) an increase in our R&D and support function personnel to support the development and roll out of new products. Our success is dependent upon our ability to attract and retain qualified employees. None of our employees are subject to a collective bargaining agreement. We believe that our relations with our employees are good.

Available Information

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy materials, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act are available free of charge on our website at www.csgsystems.com. Additionally, these reports are available at the SEC s Public Reference Room at 100 F Street, NE., Washington, D.C. 20549 or on the SEC s website at www.sec.gov. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

Code of Business Conduct and Ethics

A copy of our Code of Business Conduct and Ethics (the Code of Conduct) is maintained on our website. Any future amendment to the Code of Conduct, or any future waiver of a provision of our Code of Conduct, will be timely posted to our website upon their occurrence. Historically, we have had minimal changes to our Code of Conduct, and have had no waivers of a provision of our Code of Conduct.

Item 1A. Risk Factors

We or our representatives from time-to-time may make or may have made certain forward-looking statements, whether orally or in writing, including without limitation, any such statements made or to be made in MD&A contained in our various SEC filings or orally in conferences or teleconferences. We wish to ensure that such statements are accompanied by meaningful cautionary statements, so as to ensure, to the fullest extent possible, the protections of the safe harbor established in the Private Securities Litigation Reform Act of 1995.

Accordingly, the forward-looking statements are qualified in their entirety by reference to and are accompanied by the following meaningful cautionary statements identifying certain important risk factors that could cause actual results to differ materially from those in such forward-looking statements. This list of risk factors is likely not exhaustive. We operate in a rapidly changing and evolving market involving the North American communications industry (e.g., bundled multi-channel video, Internet, voice and IP-based services), and new risk factors will likely emerge. Management cannot predict all of the important risk factors, nor can it assess the impact, if any, of such risk factors on our business or the extent to which any risk factor, or combination of risk factors, may cause actual results to differ materially from those in any forward-looking statements. Accordingly, there can be no assurance that forward-looking statements will be accurate indicators of future actual results, and it is likely that actual results will differ from results projected in forward-looking statements and that such differences may be material.

We Derive a Significant Portion of Our Revenues From a Limited Number of Clients, and the Loss of the Business of a Significant Client Would Materially Adversely Affect Our Financial Condition and Results of Operations. The North American communications industry has experienced significant consolidation over the last few years, resulting in a large percentage of the market being served by a limited number of service providers with greater size and scale. Consistent with this market concentration, a large percentage of our revenues are generated from a limited number of clients, with approximately 70% of our revenues being generated from our four largest clients, which are (in order of size) Comcast, DISH, Time Warner, and Charter. See the Significant Client Relationships section of MD&A for key renewal dates and a brief summary of our business relationship with these clients.

There are inherent risks whenever a large percentage of total revenues are concentrated with a limited number of clients. One such risk is that, should a significant client: (i) terminate or fail to renew their contracts with us, in whole or in part for any reason; (ii) significantly reduce the number of customer accounts processed on our systems, the price paid for our services, or the scope of services that we provide; or (iii) experience significant financial or operating difficulties, it could have a material adverse effect on our financial condition and results of operations.

Our industry is highly competitive, and the possibility that a major client may move all or a portion of its customers to a competitor has increased. While our clients may incur some costs in switching to our competitors, they may do so for a variety of reasons, including: (i) if we do not maintain favorable relationships; (ii) if we do not provide satisfactory services and products; or (iii) for reasons associated with price.

A Reduction in Demand for Our Key Customer Care and Billing Products and Services Could Have a Material Adverse Effect on Our Financial Condition and Results of Operations. Historically, a substantial percentage of our total revenues have been generated from our core outsourced processing product, ACP, and related services. These products and services are expected to continue to provide a large percentage of our total revenues in the foreseeable future. Any significant reduction in demand for ACP and related services could have a material adverse effect on our financial condition and results of operations.

We May Not Be Able to Respond to the Rapid Technological Changes in Our Industry. The market for customer care and billing systems is characterized by rapid changes in technology and is highly competitive with respect to the need for timely product innovations and new product introductions. As a result, we believe that our

future success in sustaining and growing our revenues depends upon the continued market acceptance of our products, especially ACP, and our ability to continuously adapt, modify, maintain, and operate our products to address the increasingly complex and evolving needs of our clients, without sacrificing the reliability or quality of the products. In addition, the market is demanding that our products have greater architectural flexibility and interoperability with other computer systems, and that we are able to meet the demands for technological advancements to our products and services at a greater pace. Attempts to meet these demands subjects our R&D efforts to greater risks.

As a result, substantial R&D will be required to maintain the competitiveness of our products and services in the market. Technical problems may arise in developing, maintaining and operating our products and services as the complexities are increased. Development projects can be lengthy and costly, and may be subject to changing requirements, programming difficulties, a shortage of qualified personnel, and/or unforeseen factors which can result in delays. In addition, we may be responsible for the implementation of new products and/or the migration of clients to new products, and depending upon the specific product, we may also be responsible for operations of the product.

There is an inherent risk in the successful development, implementation, migration, and operations of our products and services as the technological complexities, and the pace at which we must deliver these products and services to market, continue to increase. The risk of making an error that causes significant operational disruption to a client increases proportionately with the frequency and complexity of changes to our products and services. There can be no assurance: (i) of continued market acceptance of our products and services; (ii) that we will be successful in the development of product enhancements or new products that respond to technological advances or changing client needs at the pace the market demands; or (iii) that we will be successful in supporting the implementation, migration and/or operations of product enhancements or new products.

Our Business is Dependent on the North American Cable and DBS Industries. We have historically generated a significant portion of our revenues by providing products and services to clients in the North American cable and DBS industries. A decrease in the number of customers served by our clients, an adverse change in the economic condition of these industries, and/or changing consumer demand for services could have a material adverse effect on our results of operations. Additionally, a significant portion of our historical growth has come from our support of clients expansion into new lines of business, such as HSI and VoIP. There can be no assurance that our current and potential clients will be successful in expanding into new segments of the converging communications industry. Even if major forays into new markets by our current or potential clients are successful, we may be unable to meet the special billing and customer interaction management needs of those markets.

Our clients operate in a highly competitive environment. It is widely anticipated that traditional wireline and wireless telephone service providers, and others, will continue their aggressive pursuit of providing convergent services, including residential video, a market historically dominated by our clients. Should these alternative service providers be successful in their video strategies, it could threaten our clients market share, and thus our source of revenues, as generally speaking these companies do not use our core products and services and there can be no assurance that new entrants will become our clients.

The Consolidation of the North American Cable and DBS Industry May Have a Material Adverse Effect on Our Results of Operations. The North American cable and DBS industry may continue to be subject to significant ownership changes. One facet of these changes is that consolidation by and among our core client base, the cable and DBS providers, as well as new entrants such as the traditional wireline and wireless carriers, will decrease the potential number of buyers for our products and services. Should these consolidations result in a concentration of customer accounts being owned by companies with whom we do not have a relationship, or with whom competitors are entrenched, we could be subject to the inherent risk that subscribers will be moved off of us and onto a competitor s system, thereby having a material adverse effect on our results of operations.

Furthermore, movement of our clients customers from our systems to a competitor s system as a result of regionalization strategies by our clients could have a material adverse affect on our operations. Finally, as the result of the consolidations, our current and potential clients may choose to use their size and scale to exercise more severe pressure on pricing negotiations.

We Face Significant Competition in Our Industry. The market for our products and services is highly competitive. We directly compete with both independent providers of products and services and in-house systems developed by existing and potential clients. In addition, some independent providers are entering into strategic alliances with other independent providers, resulting in either new competitors, or competitors with greater resources. Many of our current and potential competitors have significantly greater financial, marketing, technical, and other competitive resources than our company, many with significant and well-established domestic and international operations. There can be no assurance that we will be able to compete successfully with our existing competitors or with new competitors.

Client Bankruptcies Could Adversely Affect Our Business, and Any Accounting Reserves We Have Established May Not Be Sufficient. In the past, certain of our clients have filed for bankruptcy protection. Companies involved in bankruptcy proceedings pose greater financial risks to us, consisting principally of possible claims of preferential payments for certain amounts paid to us prior to the bankruptcy filing date, as well as increased collectibility risk for accounts receivable, particularly those accounts receivable that relate to periods prior to the bankruptcy filing date. We consider such risks in assessing our revenue recognition and the collectibility of accounts receivable related to our clients that have filed for bankruptcy protection, and for those clients that are seriously threatened with a possible bankruptcy filing. We establish accounting reserves for our estimated exposure on these items. However, there can be no assurance that our accounting reserves related to this exposure will be adequate. Should any of the factors considered in determining the adequacy of the overall reserves change adversely, an adjustment to the accounting reserves may be necessary. Because of the potential significance of this exposure, such an adjustment could be material.

We May Incur Additional Material Restructuring Charges in the Future. Since the third quarter of 2002, we have recorded restructuring charges related to involuntary employee terminations, various facility abandonments, and various other restructuring activities. The accounting for facility abandonments requires highly subjective judgments in determining the proper accounting treatment for such matters. We continually evaluate our assumptions, and adjust the related restructuring reserves based on the revised assumptions at that time. Moreover, we continually evaluate ways to reduce our operating expenses through new restructuring opportunities, including more effective utilization of our assets, workforce and operating facilities. As a result, there is a reasonable likelihood that we may incur additional material restructuring charges in the future.

Failure to Attract and Retain Our Key Management and Other Highly Skilled Personnel Could Have a Material Adverse Effect on Our Business. Our future success depends in large part on the continued service of our key management, sales, product development, and operational personnel. We believe that our future success also depends on our ability to attract and retain highly skilled technical, managerial, operational, and marketing personnel, including, in particular, personnel in the areas of R&D and technical support. Competition for qualified personnel at times can be intense, particularly in the areas of R&D, conversions, software implementations, and technical support, especially now that market conditions are improved and the demand for such talent has increased. For these reasons, we may not be successful in attracting and retaining the personnel we require, which could have a material adverse effect on our ability to meet our commitments and new product delivery objectives.

We May Not Be Successful in the Integration of Our Acquisitions. As part of our growth strategy, we seek to acquire assets, technology, and businesses which will provide the technology and technical personnel to expedite our product development efforts, provide complementary products or services, or provide access to new markets and clients.

Acquisitions involve a number of risks and difficulties, including: (i) expansion into new markets and business ventures; (ii) the requirement to understand local business practices; (iii) the diversion of management s attention to the assimilation of acquired operations and personnel; and (iv) potential adverse effects on a company s operating results for various reasons, including, but not limited to, the following items: (a) the inability to achieve revenue targets; (b) the inability to achieve certain operating synergies; (c) charges related to purchased in-process R&D projects; (d) costs incurred to exit current or acquired contracts or activities; (e) costs incurred to service any acquisition debt; and (f) the amortization or impairment of intangible assets.

Due to the multiple risks and difficulties associated with any acquisition, there can be no assurance that we will be successful in achieving our expected strategic, operating, and financial goals for any such acquisition.

Failure to Protect Our Proprietary Intellectual Property Rights Could Have a Material Adverse Effect on Our Financial Condition and Results of Operations. We rely on a combination of trade secret and copyright laws, nondisclosure agreements, and other contractual and technical measures to protect our proprietary rights in our products. We also hold a limited number of patents on some of our newer products, but do not rely upon patents as a primary means of protecting our rights in our intellectual property. There can be no assurance that these provisions will be adequate to protect our proprietary rights. Although we believe that our intellectual property rights do not infringe upon the proprietary rights of third parties, there can be no assurance that third parties will not assert infringement claims against us or our clients.

We continually assess whether there are any risks to our intellectual property rights. Should these risks be improperly assessed or if for any reason should our right to develop, produce and distribute our products be successfully challenged or be significantly curtailed, it could have a material adverse effect on our financial condition and results of operations.

The Delivery of Our Products and Services is Dependent on a Variety of Computing Environments and Communications Networks, Which May Not Be Available or May Be Subject to Security Attacks. Our products and services are generally delivered through a variety of computing environments operated by us, which we will collectively refer to herein as Systems. We provide such computing environments through both outsourced arrangements, such as our data processing arrangement with FDC, as well as internally operating numerous distributed servers in geographically dispersed environments. The end users are connected to our Systems through a variety of public and private communications networks, which we will collectively refer to herein as Networks. Our products and services are generally considered to be mission critical customer management systems by our clients. As a result, our clients are highly dependent upon the continuous availability and uncompromised security of our Networks and Systems to conduct their business operations.

Our Networks and Systems are subject to the risk of an extended interruption or outage due to many factors such as: (i) planned changes to our Systems and Networks for such things as scheduled maintenance and technology upgrades, or migrations to other technologies, service providers, or physical location of hardware; (ii) human and machine error; (iii) acts of nature; and (iv) intentional, unauthorized attacks from computer hackers. In addition, we continue to expand our use of the Internet with our product offerings thereby permitting, for example, our clients customers to use the Internet to review account balances, order services or execute similar account management functions. Allowing access to our Networks and Systems via the Internet increases their vulnerability to unauthorized access and corruption, as well as increasing the dependency of our Systems reliability on the availability and performance of the Internet s infrastructure.

As a means to mitigate certain risks in this area of our business, we have done the following: (i) established policies and procedures related to planned changes to our Systems and Networks; (ii) implemented a business continuity plan, to include testing certain aspects of this plan on a periodic basis; and (iii) implemented a security and data privacy program (utilizing ISO 17799 as a guideline) designed to mitigate the risk of an unauthorized access to the Networks and Systems primarily through the use of network firewalls, procedural controls, intrusion detection systems and antivirus applications. In addition, we undergo periodic security reviews of certain aspects of our Networks and Systems by independent parties.

Table of Contents

The method, manner, cause and timing of an extended interruption or outage in our Networks or Systems are impossible to predict. As a result, there can be no assurances that our Networks and Systems will not fail, or that our business continuity plans will adequately mitigate all damages incurred as a consequence. Should our Networks or Systems: (i) experience an extended interruption or outage, (ii) have their security breached, or (iii) have their data lost, corrupted or otherwise compromised, it would impede our ability to meet product and service delivery obligations, and likely have an immediate impact to the business operations of our clients. This would most likely result in an immediate loss to us of revenue or increase in expense, as well as damaging our reputation. Any of these events could have both an immediate, negative impact upon our financial condition and our short-term revenue and profit expectations, as well as our long-term ability to attract and retain new clients.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

As of December 31, 2007, we were operating from eight leased sites in the U.S., representing approximately 535,000 square feet. This amount excludes approximately 84,000 square feet of leased space that we have abandoned.

We lease office facilities totaling approximately 100,000 square feet in Englewood, Colorado and surrounding communities. We utilize these office facilities primarily for: (i) corporate headquarters; (ii) sales and marketing activities; (iii) product and operations support; and (iv) R&D activities. The leases for these office facilities expire in the years 2013 through 2015.

We lease office facilities totaling approximately 225,000 square feet in Omaha, Nebraska. We utilize these facilities primarily for (i) client services, training and product support; (ii) systems and programming activities; (iii) R&D activities; and (iv) general and administrative functions. The leases for these facilities expire in the years 2009 through 2012.

We lease an office facility totaling approximately 16,000 square feet in Chicago, Illinois. We utilize this facility primarily for: (i) R&D activities; (ii) client services; and (iii) professional services staff. The lease for this office facility expires in 2008.

We lease statement production and mailing facilities totaling approximately 194,000 square feet in Omaha, Nebraska, Wakulla County, Florida, and Fairfield, New Jersey. The leases for these facilities expire in the years 2011 through 2013.

We believe that our facilities are adequate for our current needs and that additional suitable space will be available as required. We also believe that we will be able to extend the leases as they terminate at comparable rates. See Note 11 to our Consolidated Financial Statements for information regarding our obligations under our facility leases.

Item 3. Legal Proceedings

From time-to-time, we are involved in litigation relating to claims arising out of our operations in the normal course of business. In the opinion of our management, we are not presently a party to any material pending or threatened legal proceedings.

Item 4. Submission of Matters to a Vote of Security Holders

None.

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Table of Contents

Executive Officers of the Registrant

As of December 31, 2007, our executive officers were Peter E. Kalan (Chief Executive Officer and President), Randy R. Wiese (Executive Vice President and Chief Financial Officer), Robert M. (Mike) Scott (Executive Vice President and Chief Operating Officer), and Joseph T. Ruble (Executive Vice President, General Counsel, Corporate Secretary and Chief Administrative Officer). We have employment agreements with each of the executive officers.

Peter E. Kalan

Chief Executive Officer and President

Mr. Kalan, 48, joined CSG in January 1997 and was named Chief Financial Officer in October 2000. In April 2006, he was named Executive Vice President of Business and Corporate Development. In December 2007, Mr. Kalan was named Chief Executive Officer and President, and elected to the Board. Prior to joining CSG, he was Chief Financial Officer at Bank One, Chicago, and he also held various other financial management positions with Bank One in Texas and Illinois from 1985 through 1996. Mr. Kalan holds a BA degree in Business Administration from the University of Texas at Arlington.

Randy R. Wiese

Executive Vice President and Chief Financial Officer

Mr. Wiese, 48, joined CSG in 1995 as Controller and later served as Chief Accounting Officer. He was named Executive Vice President and Chief Financial Officer in April 2006. Prior to joining CSG, he was manager of audit and business advisory services and held other accounting-related positions at Arthur Andersen & Co. Mr. Wiese is a member of the AICPA and the Nebraska Society of Certified Public Accountants. He holds a BS degree in Accounting from the University of Nebraska-Omaha.

Robert M. Scott

Executive Vice President and Chief Operating Officer

Mr. Scott, 57, joined CSG in September 1999 as Vice President of the Broadband Services Division and served as Senior Vice President of that division from 2001 to 2004. In December 2004, Mr. Scott was named Executive Vice President, and became the head of the Broadband Services Division in March 2005. In July 2006, he was named Chief Operating Officer. Prior to joining CSG, he served for 21 years in a variety of management positions, both domestically and internationally, with First Data Corporation. Mr. Scott holds a BA degree in Social Studies from Florida Atlantic University.

Joseph T. Ruble

Executive Vice President, General Counsel, Corporate Secretary and Chief Administrative Officer

Mr. Ruble, 47, joined CSG in 1997 as Vice President and General Counsel. In November 2000 he was appointed Senior Vice President of Corporate Development, General Counsel & Corporate Secretary. In February 2007, he was named Executive Vice President. Prior to joining CSG, Mr. Ruble served from 1991 to 1997 as Vice President, General Counsel & Corporate Secretary for Intersolv, Inc., and as counsel to Pansophic Systems, Inc. for its international operations from 1988 to 1991. Prior to that, he represented the software industry in Washington, D.C. on legislative matters. Mr. Ruble holds a JD from Catholic University of America and a BS degree from Ohio University.

Board of Directors of the Registrant

Effective November 14, 2007, our Board of Directors increased the number of directors of our company from eight to nine by adding a Class III director and approved Mr. Kalan to fill the vacancy created by the increase in the number of Class III directors.

Table of Contents

Information related to our Board of Directors is provided below.

Bernard W. Reznicek

Consultant

The Premier Group

Mr. Reznicek, 71, was elected to the Board in January 1997 and presently serves as the Company s non-executive Chairman of the Board. He currently provides consulting services through Premier Enterprises. Mr. Reznicek previously was an Executive with Central States Indemnity Company of Omaha, a Berkshire Hathaway company, from 1997 to 2003. He has 40 years of experience in the electric utility industry, having served as Chairman, President and Chief Executive Officer of Boston Edison Company and President and Chief Executive Officer of Omaha Public Power District. Mr. Reznicek currently is a director of Pulte Homes, Inc. (NYSE) and infoUSA Inc. (NASDAQ).

Peter E. Kalan

Chief Executive Officer and President

CSG Systems International, Inc.

Mr. Kalan s biographical information in included in Executive Officers of the Registrant section shown directly above.

Ronald Cooper

Former President and Chief Operating Officer

Adelphia Communications

Mr. Cooper, 50, was elected to the Board in November 2006. He has spent nearly 25 years in the cable and telecommunications industry, most recently at Adelphia Communications where he served as President and Chief Operating Officer from 2003 to 2006. Prior to Adelphia, Mr. Cooper held a series of executive positions at AT&T Broadband, RELERA Data Centers & Solutions, and MediaOne and its predecessor Continental Cablevision, Inc. He has held various board and committee seats with the National Cable Television Association, California Cable & Telecommunications Association, Cable Television Association for Marketing and the New England Cable Television Association. In addition, Mr. Cooper is a trustee at the Denver Art Museum and a director for Colorado Public Radio.

Edward C. Nafus

Former Chief Executive Officer and President

CSG Systems International, Inc.

Mr. Nafus, 67, was elected to the Board in March 2005. Mr. Nafus joined CSG in August 1998 as Executive Vice President and became the President of our Convergent Services and Solutions Division in January 2002. In April 2005, Mr. Nafus assumed the position of Chief Executive Officer and President of CSG and held that position until his retirement in December 2007. Prior to joining CSG, Mr. Nafus held numerous management positions within FDC from 1978 to 1998. From 1992 to 1998, he served as Executive Vice President of FDC; from 1989 to 1992, he served as President of First Data International; and Executive Vice President of First Data Resources from 1984 to 1989. From 1971 to 1978, Mr. Nafus worked in sales management, training and sales for Xerox Corporation. From 1966 to 1971, Mr. Nafus was a pilot and division officer in the United States Navy. Mr. Nafus holds a BS degree from Jamestown College.

Table of Contents

Janice I. Obuchowski

President

Freedom Technologies, Inc.

Ms. Obuchowski, 56, was elected to the Board in November 1997. She has been President of Freedom Technologies, Inc., a public policy and corporate strategy consulting firm specializing in telecommunications, since 1992. In 2003, Ms. Obuchowski was appointed by President George W. Bush to serve as Ambassador and Head of the U.S. Delegation to the World Radio Communication Conference. She has served as Assistant Secretary for Communications and Information at the Department of Commerce and as Administrator for the National Telecommunications and Information Administration. Ms. Obuchowski currently is a director of Orbital Sciences Corporation and Stratos Global Corporation.

Donald B. Reed

Former Chief Executive Officer

Cable & Wireless Global

Mr. Reed, 63, was elected to the Board in May 2005. He currently is retired, having served as Chief Executive Officer of Cable & Wireless Global from May 2000 to January 2003. Cable & Wireless Global, Cable & Wireless plc s wholly owned operations in the United States, United Kingdom, Europe and Japan, is a provider of internet protocol (IP) and data services to business customers. From June 1998 until May 2000, Mr. Reed served Cable & Wireless in various other executive positions. Mr. Reed s career includes 30 years at NYNEX Corporation (now part of Verizon), a regional telephone operating company. From 1995 to 1997 Mr. Reed served NYNEX Corporation as President and Group Executive with responsibility for directing the company s regional, national and international government affairs, public policy initiatives, legislative and regulatory matters, and public relations. Mr. Reed currently is a director of Intervoice, Inc., Idearc Media (formerly Verizon Yellow Pages) (NYSE) and Aggregate Industries in London, England, a wholly owned subsidiary of Holcim Group located in Switzerland.

Frank V. Sica

Managing Partner

Tailwind Capital

Mr. Sica, 57, has served as a director of the Company since its formation in 1994. He is currently a Managing Partner of Tailwind Capital. From 2004 to 2005, Mr. Sica was a Senior Advisor to Soros Private Funds Management. From 2000 until 2003, he was President of Soros Private Funds Management which oversaw the direct real estate and private equity investment activities of Soros. In 1998, he joined Soros Fund Management where he was a Managing Director responsible for Soros private equity investments. From 1988 to 1998, Mr. Sica was a Managing Director at Morgan Stanley and its private equity affiliate, Morgan Stanley Capital Partners. Prior to 1988, Mr. Sica was a Managing Director in Morgan Stanley s mergers and acquisitions department. From 1974 to 1977, Mr. Sica was an officer in the U.S. Air Force. Mr. Sica currently is a director of JetBlue Airways, Kohl s Corporation, and NorthStar Realty Finance Corporation.

Donald V. Smith

Senior Managing Director

Houlihan Lokey Howard & Zukin, Inc.

Mr. Smith, 65, was elected to the Board in January 2002. He presently serves as Senior Managing Director of Houlihan Lokey Howard & Zukin, Inc., an international investment banking firm with whom he has been associated since 1988. Mr. Smith currently is in charge of the firm s New York office and serves on the board of directors of the firm. From 1978 to 1988, he was employed by Morgan Stanley & Co. Incorporated, where he headed the valuation and reorganization services within that firm s corporate finance group. Mr. Smith is director of the Princeton (NJ) Health Care Foundation and of Business Executives for National Security.

Table of Contents

James A. Unruh

Managing Principal

Alerion Capital Group

Mr. Unruh, 67, was elected to the Board in June 2005. He became a founding principal of Alerion Capital Group, LLC (a private equity investment company) in 1998 and currently holds such position. Mr. Unruh was an executive with Unisys Corporation from 1987 to 1997 and served as its Chairman and Chief Executive Officer from 1990 to 1997. From 1982 to 1987, Mr. Unruh held various executive positions, including Senior Vice President, Finance, with Burroughs Corporation, a predecessor of Unisys Corporation. Mr. Unruh currently is a director of Prudential Financial, Inc., Tenet Healthcare Corporation, and Qwest Communications International Inc.

18

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is listed on the Nasdaq Stock Market LLC (NASDAQ/NMS) under the symbol CSGS . The following table sets forth, for the fiscal quarters indicated, the high and low sale prices of our common stock as reported by NASDAQ/NMS.

	High	Low
2007		
First quarter	$ 26.97	$ 24.02
Second quarter	28.22	24.45
Third quarter	27.26	19.64
Fourth quarter	21.97	14.52

	High	Low
2006		
First quarter	$ 23.29	$ 20.82
Second quarter	26.21	22.87
Third quarter	27.48	23.18
Fourth quarter	28.45	26.11

On February 25, 2008, the last sale price of our common stock as reported by NASDAQ/NMS was $11.79 per share. On January 31, 2008, the number of holders of record of common stock was 235.

Dividends

We have not declared or paid cash dividends on our common stock since our incorporation. We did, however, complete a two-for-one stock split, effected in the form of a stock dividend, in March 1999. We intend to retain any earnings to finance the growth and development of our business, and at this time, we do not plan to pay cash dividends in the foreseeable future.

Our revolving credit facility contains certain restrictions on the payment of dividends. In addition, the payment of dividends has certain impacts to our Convertible Debt Securities. See Note 7 to our Consolidated Financial Statements for additional discussion of our revolving credit facility and Convertible Debt Securities, and the impact the payment of dividends may have on these items.

Table of Contents

Stock Price Performance

The following graph compares the cumulative total stockholder return on our common stock, the S&P 500 Index, and our Standard Industrial Classification (SIC) Code Index: Computer Processing and Data Preparation and Processing Services during the indicated five-year period. The graph assumes that $100 was invested on December 31, 2002, in our common stock and in each of the two indexes and that all dividends, if any, were reinvested.

	12/31/02	12/31/03	12/31/04	12/31/05	12/31/06	12/31/07
CSG Systems International, Inc.	100.00	91.50	137.00	**Supplemental Cash Flow Disclosures:**		
Cash paid for interest, net of amounts capitalized		**$**	**55**	$ 308		
Cash paid (refunds received) for income taxes		**$**	**25**	$ (20)		
Cash paid for reorganization items		**$**	**57**	$		
Business Acquisitions:						
Fair value of assets acquired		**$**	**21**	$ 61		
Less cash paid			**21**	61		
Liabilities assumed		**$**		$		

The accompanying notes are an integral part of these condensed consolidated statements.

8

MIRANT CORPORATION AND SUBSIDIARIES
(Debtor-in-Possession)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2004 and 2003

A. Description of Business and Chapter 11 Proceedings

Overview

Mirant Corporation (formerly Southern Energy, Inc.) and its subsidiaries (collectively, "Mirant" or the "Company") is an international energy company incorporated in Delaware on April 20, 1993. Prior to April 2, 2001, Mirant was a subsidiary of Southern Company ("Southern"). The Company's revenues are primarily generated through the production of electricity in the U.S., the Philippines and the Caribbean. As of June 30, 2004, Mirant owned or leased more than 17,000 MW of electric generating capacity.

Mirant manages its business through two principal operating segments. The Company's North America segment consists of power generation and trading and marketing operations. In North America, the Company trades and markets energy commodities to manage the financial performance of its power generation business and to enter into other energy trading positions, primarily in regions where it owns generating facilities or other physical assets. The International segment includes power generation businesses in the Philippines, Curacao and Trinidad and Tobago, and integrated utilities in the Bahamas and Jamaica. In the Philippines, over 80% of Mirant's generation output is sold under long-term contracts. The Company's operations in the Caribbean include fully integrated electric utilities, which generate, distribute and sell power to residential, commercial and industrial customers.

Proceedings under Chapter 11 of the Bankruptcy Code

On July 14, 2003 and July 15, 2003 ("Petition Date"), Mirant and 74 of its wholly-owned subsidiaries in the United States (collectively, the "Original Debtors") filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Northern District of Texas, Fort Worth Division ("Bankruptcy Court"). On August 18, 2003, October 3, 2003 and November 18, 2003, four additional wholly-owned subsidiaries and four affiliates of Mirant commenced Chapter 11 cases under the Bankruptcy Code (together with the Original Debtors, the "Mirant Debtors"). The Chapter 11 cases of the Mirant Debtors are being jointly administered for procedural purposes only under case caption In re Mirant Corporation *et al*., Case No. 03-46590 (DML).

Additionally, on the Petition Date, certain of Mirant's Canadian subsidiaries, Mirant Canada Energy Marketing, Ltd. and Mirant Canada Marketing Investments, Inc., filed an application for creditor protection under the Companies Creditors' Arrangement Act in Canada ("CCAA"), which, like Chapter 11, allows for reorganization under the protection of the court system. These Canadian subsidiaries emerged from creditor protection on May 21, 2004. The accounting for their emergence is reflected in the financial results for the three months ended June 30, 2004 and did not have a material impact on the Company's operating results.

Mirant's businesses in the Philippines and the Caribbean were not included in the Chapter 11 filings.

The Mirant Debtors are continuing to operate their businesses as debtors-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code, the Federal Rules of Bankruptcy Procedure, applicable court orders, as well as other applicable laws and rules. In general, as debtors-in-possession, each of the Mirant Debtors is authorized under the Bankruptcy Code to continue to operate as an ongoing business, but may not engage in

transactions outside the ordinary course of business without the prior approval of the Bankruptcy Court.

The Office of the United States Trustee has established a committee of unsecured creditors for Mirant Corporation and a committee of unsecured creditors for Mirant Americas Generation (collectively, the "Creditor Committees"). The Office of the United States Trustee has also established a committee of equity securities holders of Mirant Corporation (the "Equity Committee," and collectively with the Creditor Committees, the "Statutory Committees"). Pursuant to an order of the Bankruptcy Court, the Office of the United States Trustee appointed an examiner (the "Examiner") in these cases to analyze certain potential causes of action and act as a mediator with respect to certain disputes that arise among the Mirant Debtors, the Statutory Committees, or other parties in interest.

Subject to certain exceptions in the Bankruptcy Code, the Chapter 11 filings automatically stayed the initiation or continuation of most actions against the Mirant Debtors, including most actions to collect pre-petition indebtedness or to exercise control over the property of the bankruptcy estates. As a result, absent an order of the Bankruptcy Court, creditors are precluded from collecting pre-petition debts and substantially all pre-petition liabilities are subject to compromise under a plan or plans of reorganization to be developed by the Mirant Debtors later in the bankruptcy proceedings. One exception to this stay of litigation is actions or proceedings by a governmental agency to enforce its police or regulatory power.

Under the Bankruptcy Code, the Mirant Debtors also have the right to assume, assign or reject certain executory contracts and unexpired leases, subject to the approval of the Bankruptcy Court and certain other conditions. The Mirant Debtors continue to evaluate their executory contracts in order to determine which contracts will be assumed, assigned or rejected. For those contracts with an effective rejection date or amendment during the six months ended June 30, 2004, the Company recorded estimated damage claims of $79 million as a component of reorganization expense in its unaudited condensed consolidated statement of operations and a liability subject to compromise on its unaudited condensed consolidated balance sheet.

At this time, it is not possible to accurately predict the effect of the Chapter 11 reorganization process on the business of the Mirant Debtors, or if and when, some or all of the Mirant Debtors may emerge from Chapter 11. The prospects for the future results depend on the timely and successful development, confirmation and implementation of a plan of reorganization. There can be no assurance that a successful plan or plans of reorganization will be proposed by the Mirant Debtors, supported by Mirant Debtors' creditors or security holders or confirmed by the Bankruptcy Court, or that any such plan or plans will be consummated. The rights and claims of various creditors and security holders will be determined by the applicable plans as well. Under the priority scheme established by the Bankruptcy Code, certain post-petition and pre-petition liabilities need to be satisfied before equity security holders are entitled to any distributions. The ultimate recovery to creditors and equity security holders, if any, will not be determined until confirmation of a plan or plans of reorganization. No assurance can be given as to what values, if any, will be ascribed in the bankruptcy proceedings to the interests of each of these constituencies, and it is possible that the equity interests in Mirant and the other Mirant Debtors, or other securities will be restructured in a manner that will reduce substantially or eliminate any remaining value. Whether or not a plan or plans of reorganization are approved, it is possible that the assets of any one or more of the Mirant Debtors may be liquidated.

B. Accounting and Reporting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements (unaudited) of Mirant and its wholly-owned subsidiaries have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions for Form 10-Q and

Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Form 10-K for the year ended December 31, 2003.

The financial statements include the accounts of Mirant and its wholly-owned, and controlled majority-owned subsidiaries, as well as variable interest entities in which Mirant has an interest and is the primary beneficiary, and have been prepared from records maintained by Mirant and its subsidiaries in their respective countries of operation. All significant intercompany accounts and transactions have been eliminated in consolidation. Investments in minority-owned companies in which Mirant exercises significant influence over operating and financial policies are accounted for using the equity method of accounting. Majority or jointly owned affiliates, which Mirant does not control, as well as interests in variable interest entities in which Mirant is not the primary beneficiary, are also accounted for using the equity method of accounting.

Certain prior period amounts have been reclassified to conform to the current year financial statement presentation. The results of operations for the three and six months ended June 30, 2004 are not necessarily indicative of the results to be expected for the full year. All amounts are presented in US dollars unless otherwise noted.

Accounting for Reorganization

The accompanying unaudited condensed consolidated financial statements of Mirant have been prepared in accordance with Statement of Position 90-7, "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code"and on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. However, as a result of the bankruptcy filings, such realization of assets and satisfaction of liabilities are subject to a significant number of uncertainties. Mirant's unaudited condensed consolidated financial statements do not reflect adjustments that might be required if Mirant (or each of the Mirant Debtors) is unable to continue as a going concern.

Mirant Debtors include all entities that filed for protection from creditors in 2003. Non-debtors include the Company's businesses in the Caribbean and Philippines that are generally not affected by the bankruptcy filings. Non-debtors also includes certain non wholly-owned subsidiaries and Canada which emerged from creditor protection in May 2004. Unaudited condensed combined financial statements of the Mirant Debtors and Non-Debtors are set forth below.

Unaudited Condensed Combined Statement of Operations Data
For the Three Months ended June 30, 2004
(in millions)

	Debtors	Non-Debtors	Consolidation/ Elimination Entries	Consolidated
Operating revenues	$ 1,007	$ 257	$	$ 1,264
Cost of fuel, electricity and other products	697	71		768
Operating expenses	240	142		382
Operating income	70	44		114
Other income (expense), net	14	(23)	20	11
Reorganization items, net	70	3*		73
(Benefit) provision for income taxes	(18)	31		13
Minority interest		7		7
Net income (loss)	$ 32	$ (20)	$ 20	$ 32

*

Represents corporate reorganization expenses allocated to international subsidiaries

Unaudited Condensed Combined Statement of Operations Data
For the Six Months ended June 30, 2004
(in millions)

	Debtors	Non-Debtors	Consolidation/ Elimination Entries	Consolidated
Operating revenues	$ 1,941	$ 507	$	$ 2,448
Cost of fuel, electricity and other products	1,363	138		1,501
Operating expenses	451	244		695
Operating income	127	125		252
Other income (expense), net	25	(40)	(1)	(16)
Reorganization items, net	126	4*		130
(Benefit) provision for income taxes	(36)	68		32
Minority interest		12		12
Net income (loss)	$ 62	$ 1	$ (1)	$ 62

*

Represents corporate reorganization expenses allocated to international subsidiaries

Unaudited Condensed Combined Balance Sheet Data
June 30, 2004
(in millions)

	Debtors	Non-Debtors	Consolidation/ Elimination Entries	Consolidated
Current assets	$ 2,361	$ 1,244	$ (219)	$ 3,386
Intercompany receivables	700	602	(1,302)	
Property, plant and equipment, net	4,286	2,281		6,567
Intangible assets, net	266	596		862
Investments	2,312	226	(2,293)	245
Other	232	363		595
Total assets	$ 10,157	$ 5,312	$ (3,814)	$ 11,655
Liabilities not subject to compromise:				
Current liabilities	$ 885	$ 464	$ (4)	$ 1,345
Intercompany payables	366	703	(1,069)	
Other noncurrent liabilities	429	393	(1)	821
Long-term debt	187	1,074		1,261
Liabilities subject to compromise	9,137	125	(446)	8,816
Minority interest		165		165
Stockholders' (deficit) equity	(847)	2,388	(2,294)	(753)
Total liabilities and stockholders' (deficit) equity	$ 10,157	$ 5,312	$ (3,814)	$ 11,655

Unaudited Condensed Combined Statement of Cash Flows Data
For Six Months Ended June 30, 2004
(in millions)

	Debtors	Non-Debtors	Consolidation/ Elimination Entries	Consolidated
Net cash (used in) provided by:				
Operating activities	$ (464)	$ 259	$ (46)	$ (251)
Investing activities	(89)	12	(12)	(89)
Financing activities	218	(251)	58	25
Net (decrease) increase in cash and cash equivalents	(335)	20		(315)
Cash and cash equivalents, beginning of period	1,074	515		1,589
Cash and cash equivalents, end of period	$ 739	$ 535	$	$ 1,274
Cash paid for reorganization items	$ 57	$	$	$ 57

Classification of Liabilities as "Liabilities Not Subject to Compromise" Versus "Liabilities Subject to Compromise."

Liabilities subject to compromise refer to liabilities incurred prior to the Petition Date as specified above. The amounts of the various categories of liabilities that are subject to compromise are set forth below. These amounts represent the Company's estimates of known or potential pre-petition date claims against Mirant Debtors that are likely to be resolved in connection with the bankruptcy filings. Such claims remain subject to future adjustments. Adjustments may result from negotiations, actions of the Bankruptcy Court, rejection of executory contracts and unexpired leases, and the determination as to the value of any collateral securing claims, proofs of claim, or other events. The fair value of a Mirant Debtor's assets may be lower than its liabilities. This could result in liabilities being settled at less than 100% of their face value and the equity of Mirant's stockholders being diluted or eliminated entirely.

Liabilities not subject to compromise include: (1) liabilities of Non-Debtor entities; (2) liabilities incurred after the Petition Date; (3) liabilities incurred prior to the Petition Date that the Mirant Debtors expect to pay in full, even though certain of these amounts may not be paid until a plan of reorganization is approved; (4) liabilities related to pre-petition contracts that have not been rejected; and (5) liabilities incurred prior to the Petition Date that have been approved for payment by the Court and that the Mirant Debtors expect to pay (in advance of a plan of reorganization) in the ordinary course of business, including certain employee related items (salaries, vacation and medical benefits).

The classification of liabilities "not subject to compromise" versus liabilities "subject to compromise" is based on currently available information and analysis. As the bankruptcy cases proceed and additional information and analysis is completed or, as the Bankruptcy Court rules on relevant matters, the classification of amounts between these two categories may change. The amount of any such changes could be significant.

The amounts subject to compromise at June 30, 2004, consisted of the following items (in millions):

Items, absent the bankruptcy filings, that would have been considered current at June 30, 2004:		
Accounts payable and accrued liabilities	$	1,009
Current portion of long-term debt		2,543
Price risk management liabilities		83
Items, absent the bankruptcy filings, that would have been considered noncurrent at June 30, 2004:		
Long-term debt		4,328
Price risk management liabilities		478
Note payable to Mirant Trust I		356
Other noncurrent liabilities		19
Total	$	8,816

The price risk management liabilities included in liabilities subject to compromise relate to power purchase agreements. The $147 million decrease in these liabilities from December 31, 2003 to June 30, 2004 relates to purchases made under the power purchase agreements during the six months ended June 30, 2004 and to changes in the fair value of the remaining obligation as of June 30, 2004 due to changes in power prices.

Accounts payable and accrued liabilities above are net of approximately $131 million of pre-petition accounts receivable due from counterparties with which the Mirant Debtors have netting agreements.

During the first quarter of 2003, Mirant paid $51 million to purchase $83 million in aggregate principal amount of TIERS Fixed Rate Certificates (the "TIERS Certificates"). The TIERS Certificates were issued by a third party trust (the "Trust") and were secured by $400 million aggregate principal amount of Mirant's 2.5% convertible senior debentures due 2021 (the "Mirant Debentures"). On June 15, 2004, the Trust was terminated in accordance with the terms of the Trust agreement and the Mirant Debentures were distributed to the TIERS Certificate holders. The Company received $83 million of the Mirant Debentures upon liquidation of the Trust. The acquisition of the Mirant Debentures was accounted for as an extinguishment of $83 million of debt. Mirant recognized a $38 million gain on the extinguishment of debt for the three and six months ended June 30, 2004, which is reflected in other income (expense), net in the unaudited condensed consolidated statements of operations.

Interest Expense

The Mirant Debtors have discontinued recording interest on liabilities subject to compromise. Contractual interest on liabilities subject to compromise in excess of reported interest was approximately $134 million and $257 million for the three and six months ended June 30, 2004 respectively. Contractual interest on liabilities subject to compromise in excess of reported interest for the period from the Petition Date through June 30, 2004 is approximately $492 million.

Reorganization Items

Reorganization items, net represents expense or income amounts that were recorded in the financial statements as a result of the bankruptcy proceedings. For the three months and six months ended June 30, 2004, the following were the significant items within this category (in millions):

	Three Months Ended June 30, 2004	Six Months Ended June 30, 2004
Estimated damage claims	$ 33	$ 79
Professional fees and administrative expense	25	47
Losses on contract amendments, net	33	22
Other gains, net	(18)	(18)
Total	$ 73	$ 130

Estimated damage claims of $33 million and $79 million relate to gas transportation and electric transmission contracts rejected in the three and six months ended June 30, 2004, respectively.

Professional fees and administrative expense relate to legal, accounting and other professional costs directly associated with the reorganization process. Approximately $9 million and $16 million of the professional fees and administrative expense for the three and six months ended June 30, 2004, respectively, relates to advisors of the Statutory Committees.

For the three and six months ended June 30, 2004, losses on contract amendments, net were approximately $33 million and $22 million, respectively. Included in this amount for the three months ended June 30, 2004 is $33 million of forfeited prepayments and impairments of certain purchased intangible assets related to the previous long-term service agreements ("LTSAs") for certain combustion turbine generation facilities. Additionally, included in the amount for the six months ended June 30, 2004 is an $11 million gain on the lease amendment to the corporate headquarters lease.

Other gains, net for the three and six months ended June 30, 2004 include a $7 million gain on settlements of accounts payable upon emergence of the Mirant Canadian subsidiaries from creditor protection and $11 million of gains on other contract settlements.

Cumulative Effect of Changes in Accounting Principles

In October 2002, the Emerging Issues Task Force ("EITF") reached a consensus on EITF Issue 02-03, "Issues Related to Accounting for Contracts Involved in Energy Trading and Risk Management Activities," to rescind EITF Issue 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities." Accordingly, energy-related contracts that are not accounted for pursuant to SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," ("SFAS No. 133") such as transportation contracts, storage contracts and tolling agreements, are required to be accounted for as executory contracts using the accrual method of accounting and not fair value. Energy-related contracts that meet the definition of a derivative pursuant to SFAS No. 133 continue to be carried at fair value. In addition, the Task Force observed that accounting for energy-related inventory at fair value by analogy to the consensus on EITF Issue 98-10 is not appropriate and that such inventory is not to be recognized at fair value. As a result of the consensus on EITF Issue 02-03, all non-derivative energy trading contracts on the consolidated balance sheet as of January 1, 2003 that existed on October 25, 2002 and energy-related inventories that were recorded at fair value have been adjusted to historical cost resulting in a cumulative effect adjustment of $25 million, net of tax, which was recorded in the first quarter of 2003.

The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 143 "Accounting for Asset Retirement Obligations" ("SFAS No. 143") effective January 1, 2003, relating to costs associated with legal obligations to retire tangible, long-lived assets, referred to as asset retirement obligations. Asset retirement obligations are recorded at fair value in the period in which they are incurred by increasing the carrying amount of the related long-lived asset. In each subsequent period, the liability is accreted to its fair value and the capitalized costs are depreciated over the useful life of the related asset. In the first quarter of 2003, the Company recorded a charge as a cumulative effect of change in accounting principle of approximately $3 million, net of tax, related to the adoption of this accounting standard.

New Accounting Standards

In December 2003, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin (ARB) No. 51* ("FIN 46R"). FIN 46R addresses the consolidation by business enterprises of variable interest entities ("VIEs"), as defined in the Interpretation. FIN 46R expands existing accounting guidance regarding when a company should consolidate in its financial statements the assets, liabilities and activities in another entity. The consolidation requirements applied immediately to Special Purpose Entities ("SPEs") in 2003 and for all other VIEs no later than the end of the first reporting period ending after March 15, 2004. At December 31, 2003, the Company deconsolidated Mirant Trust I, an SPE, and began accounting for its interest in Mirant Trust I on the equity method of accounting pursuant to FIN 46R.

As of March 31, 2004, the Company applied the consolidation requirements of FIN 46R to all interests it has in non-SPE VIEs. The effect of the Company's adoption of FIN 46R with respect to these VIEs was not material to the Company's consolidated results of operations, cash flows or financial position.

The Company has held a minority equity interest in a non-consolidated VIE since July 2000. The non-consolidated VIE primarily holds an interest in a generation facility and has total assets of approximately $98 million at June 30, 2004. The Company believes that its maximum exposure to loss

associated with its interest in the non-consolidated VIE is the Company's carrying value of its investment in the VIE at June 30, 2004 of approximately $52 million.

Stock-Based Compensation

Mirant accounts for its stock-based employee compensation plans under the intrinsic-value method of accounting for recognition, but discloses pro forma fair value information. Under the intrinsic-value method, compensation expense for employee stock options is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. The following table illustrates the effect on net income or loss if the fair value based method had been applied to all outstanding and unvested awards in each period (in millions, except per share data).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Net income (loss), as reported	$ 32	$ (2,202)	$ 62	$ (2,230)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(2)	(8)	(6)	(12)
Pro forma net (loss)	$ 30	$ (2,210)	$ 56	$ (2,242)
Income (loss) per share:				
Basic as reported	$ 0.08	$ (5.44)	$ 0.15	$ (5.51)
Basic pro forma	$ 0.07	$ (5.46)	$ 0.14	$ (5.54)
Diluted as reported	$ 0.08	$ (5.44)	$ 0.15	$ (5.51)
Diluted pro forma	$ 0.07	$ (5.46)	$ 0.14	$ (5.54)

C. Price Risk Management Assets and Liabilities

The fair values of Mirant's price risk management assets and liabilities, net of credit reserves, as of June 30, 2004 are included in the following table (in millions).

	Assets		Liabilities	
	Current	Noncurrent	Current	Noncurrent
Electricity	$ 57	$ 102	$ 188	$ 99
Natural gas	55	27	53	23
Crude oil	35	2	5	1
Other	3	1	2	
Total	$ 150	$ 132	$ 248	$ 123

The volumetric weighted average maturity, or weighted average tenor, of the price risk management portfolio at June 30, 2004, was approximately 1 year. The net notional amount of the price risk management assets and liabilities at June 30, 2004, was a net short position of approximately 24 million equivalent MWh.

The following table represents the net fair value (liability) of Mirant's price risk management assets and liabilities by portfolio, net of credit reserves, as of June 30, 2004 (in millions).

Optimization	$	18
Asset management		(91)
Legacy portfolio		(16)
Total	$	(89)

D. Dispositions and Acquisitions

The following developments occurred during the six months ended June 30, 2004.

Sual Project

The Sual project shareholder agreement grants minority shareholders put option rights such that they can require Mirant Asia-Pacific Limited and /or certain of its subsidiaries to purchase the minority shareholders' interests in the project. In February 2004, a minority shareholder of the Sual project served notice to exercise its put option pursuant to the Sual project shareholder agreement. In March 2004, our Philippines business paid approximately $21 million to acquire this additional 2.94% ownership interest in the Sual project. The remaining minority interest subject to the Sual put agreement, which expires in December 2005, is 5.15%.

Mirant Canada Operations

In March 2004, Mirant closed on agreements to dispose of its Canadian natural gas transportation contracts and certain natural gas marketing contracts. As part of the sale agreements, Mirant paid approximately $12 million to have a third party assume these contracts which released $28 million in liabilities related to such contracts. The resulting $16 million gain is reflected in gain on sales of assets in the accompanying unaudited condensed consolidated statement of operations.

E. Goodwill and Other Intangible Assets

Goodwill

The Company's goodwill balance at June 30, 2004 relates to its International operating segment. There were no changes in goodwill for the six months ended June 30, 2004.

As a result of two credit rating downgrades, public opposition to Mirant's restructuring proposals, material unfavorable variances to its prior business plan through the second quarter of 2003 and a lawsuit filed against its restructuring proposal by Mirant Americas Generation bondholders, Mirant reassessed its goodwill for impairment at June 30, 2003 related to its North America reporting unit. The results of the analysis indicated that a goodwill impairment existed at June 30, 2003. A detailed impairment analysis indicated that all of the North America goodwill was impaired and accordingly, Mirant recorded an impairment charge of $2.1 billion, which is reflected as an impairment loss in the unaudited condensed consolidated statements of operations for the three and six months ended June 30, 2003.

Other Intangible Assets

Following is a summary of intangible assets as of June 30, 2004 and December 31, 2003 (in millions):

	Weighted Average Amortization Lives	June 30, 2004		December 31, 2003	
		Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Trading rights	26 years	$ 27	$ (1)	$ 27	$ (-)
Development rights	38 years	119	(10)	119	(7)
Emission allowances	32 years	131	(13)	131	(12)
Other intangibles	18 years	24	(2)	41	(6)
Total other intangible assets		$ 301	$ (26)	$ 318	$ (25)

F. Impairment Losses and Restructuring Charges

Components of the restructuring charges and impairment losses for the three and six months ending June 30, 2004 and 2003 are as follows (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Impairment losses	$ 48	$ 2,071	$ 48	$ 2,076
Restructuring charges:				
Costs to cancel equipment orders and service agreements per contract terms		2		4
Severance of employees and other employee termination-related charges	5	3	7	8
Total restructuring charges	5	5	7	12
Total impairment losses and restructuring charges	$ 53	$ 2,076	$ 55	$ 2,088

Mirant evaluates its long-lived assets (property, plant and equipment) and definite-lived intangibles for impairment whenever events or changes in circumstances indicate that the Company may not be able to recover the carrying amount of the asset. An asset impairment charge is recognized when the sum of the undiscounted expected future cash flows from a long-lived asset or definite-lived intangible is less than the carrying value of that asset. The amount of the impairment charge is calculated as the excess of the carrying value of the asset over its fair value. Fair value is estimated based on the discounted future cash flows from that asset or determined by other valuation techniques. In the case of assets that Mirant expects to sell, the impairment charge is based on the estimated fair value less the costs to sell. In the second quarter of 2004, the Company began pursuing the sale of one of its combined cycle generation facilities in North America. This decision to pursue the sale represented a triggering event that required the Company to perform an impairment analysis on that generation facility. As a result of the analysis, Mirant recorded an impairment charge of $48 million in the three and six months ended June 30, 2004.

Following is a summary of the liability for accrued restructuring charges as of June 30, 2004 and 2003:

	Six Months Ended June 30,	
	2004	2003
Balance, beginning of period	$ 19	$ 9
Provision	7	16
Reversal		(4)
Cash payments	(22)	(20)
Balance, end of period	$ 4	$ 1

During the six months ended June 30, 2004, Mirant terminated approximately 346 employees as part of its restructuring activities and paid $22 million related to restructuring charges. Approximately 270 of the employees terminated were part of Mirant's international operations. Restructuring charges related to these terminations were recognized in December 2003.

During the six months ended June 30, 2003, Mirant terminated approximately 191 employees as part of its restructuring activities and paid $20 million related to restructuring charges.

G. Debt

Debtor-in-Possession Financing

On November 5, 2003 certain of the Mirant Debtors (the "DIP Borrowers") entered into a two-year debtor-in-possession credit facility ("DIP Facility") providing for borrowings or the issuance of letters of credit in an amount not to exceed the lesser of $500 million or the then existing "borrowing base." The borrowing base is the aggregate value assigned to specified power generation assets of the DIP Borrowers that serve as collateral for the DIP Facility. The initial borrowing base was $777 million. However, upon the occurrence of certain triggering events, including an event that has a material adverse effect on the business, operations or value of a power generation facility, the borrowing base may be revalued or reserves against the borrowing base may be imposed, thus lowering the borrowing base amount. The orders entered by the Bankruptcy Court approving the DIP Facility permit up to $300 million of borrowings, which amount may be increased to $500 million upon written approval of each of the Statutory Committees or further order of the Bankruptcy Court. The DIP Facility also contains an option, exercisable by Mirant or Mirant Americas Generation, to remove Mirant Americas Generation and its subsidiaries as borrowers and obligors under the DIP Facility and reduce the DIP Facility commitment to a maximum of $200 million of borrowings. Borrowings under the DIP Facility are secured by substantially all of the assets of the DIP Borrowers.

Pursuant to the DIP Facility, the DIP Borrowers are subject to a number of affirmative and restrictive covenants, reporting requirements, and, subject to usage, financial covenants. The Company was in compliance with the DIP Facility covenants, or had received affirmative waivers of compliance where compliance was not attained, as of June 30, 2004. On June 1, 2004, the DIP Borrowers and the required lenders under the DIP Facility replaced the Value at Risk ("VaR") covenant therein with a $10 million VaR limit on optimization activities only, restrictions on transactions with respect to the legacy portfolio and additional reporting requirements with respect to the Company's optimization and legacy activities.

Jamaica Public Service Company Credit Facilities

In February 2004, Jamaica Public Service Company Limited, in which Mirant has an 80% ownership interest, entered into a $30 million, 7-year amortizing credit facility ("2004 RBTT credit facility") with RBTT Merchant Bank Limited. The proceeds from this facility were used to replace the construction financing of the Bogue construction project completed in 2003. The loans are non-recourse to Mirant Corporation. The loan agreements contain a number of covenants, including (i) restrictions on change of control; (ii) restrictions on the issuance or purchase of borrower's shares; (iii) limitations on transactions with affiliates; (iv) limitations on the incurrence of new debt; and (v) limitations on dividends.

Jamaica Public Service Company Limited is also party to a separate $30 million, 7-year amortizing credit facility with RBTT Merchant Bank Limited entered into in 2003 ("2003 RBTT credit facility") and a $45 million, 12-year amortizing credit facility with International Finance Corporation ("IFC credit facility"). In connection with the 2004 RBTT, 2003 RBTT and IFC credit facilities, Jamaica Public Service Company Limited was required to obtain and register a title related to property on which the 120MW facility at Bogue is situated to facilitate registration of the lenders' mortgages. At December 31, 2003, Jamaica Public Service Company Limited had secured title and was actively working with the lender's local attorneys to register the mortgages, but had not finalized the registration at that time, which represented a breach of the IFC credit facility and a potential breach of the 2004 RBTT and 2003 RBTT credit facilities. As a result, the Company included amounts outstanding under the 2003 RBTT and IFC credit facilities in the current portion of long-term debt on its condensed consolidated balance sheets at December 31, 2003. In June 2004, the registration of the mortgage was finalized and the amounts outstanding under the 2004 RBTT, 2003 RBTT and IFC credit facilities were reclassified to long-term debt on its condensed consolidated balance sheets at June 30, 2004.

H. Litigation and Other Contingencies

The Company is involved in a number of significant legal proceedings. In certain cases, plaintiffs seek to recover large and sometimes unspecified damages, and some matters may be unresolved for several years. The Company cannot currently determine the outcome of the proceedings described below or the ultimate amount of potential losses and therefore has not made any provision for such matters unless specifically noted below. Pursuant to SFAS No. 5, "Accounting for Contingencies," management provides for estimated losses to the extent information becomes available indicating that losses are probable and that the amounts are reasonably estimable. Additional losses could have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

Effect of Chapter 11 Filings

On the Petition Date, August 18, 2003, October 3, 2003, and November 18, 2003, the Mirant Debtors filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code. Additionally, certain of Mirant's Canadian subsidiaries have filed an application for creditor protection under the CCAA in Canada, which, like Chapter 11, allows for reorganization. These Canadian subsidiaries emerged from creditor protection on May 21, 2004. The accounting for their emergence is reflected in the financial results for the three months ended June 30, 2004 and did not have a material impact on the Company's operating results. The subsidiaries of Mirant that operate in the Philippines and the Caribbean were not included in the Chapter 11 filings.

As debtors-in-possession, the Mirant Debtors are authorized under Chapter 11 to continue to operate as an ongoing business, but may not engage in transactions outside the ordinary course of business without the prior approval of the Bankruptcy Court. As of the Petition Date, most pending

litigation (including some of the actions described below) is stayed, and absent further order of the Bankruptcy Court, no party, subject to certain exceptions, may take any action, again subject to certain exceptions, to recover on pre-petition claims against the Mirant Debtors. One exception to this stay of litigation is actions or proceedings by a governmental agency to enforce its police or regulatory power. The claims asserted in litigation and proceedings to which the stay applies may be fully and finally resolved in connection with the administration of the bankruptcy proceedings and, to the extent not resolved, will need to be addressed in the context of any plan or plans of reorganization. On November 19, 2003, the Bankruptcy Court entered an order staying most litigation pending against current or former officers, directors and managers of the Mirant Debtors arising out of the performance of their duties and against certain potential indemnities of the Mirant Debtors. The Bankruptcy Court took that action to avoid the risk that the continuation of such litigation would impede the Mirant Debtors' ability to reorganize or would have a negative impact upon the assets of the Mirant Debtors. At this time, it is not possible to predict the outcome of the Chapter 11 filings or their effect on the business of the Mirant Debtors or outstanding legal proceedings.

California and Western Power Markets

The Company is subject to litigation related to its activities in California and the western power markets and the high prices for wholesale electricity experienced in the western markets during 2000 and 2001. Various lawsuits and complaints have been filed by the California Attorney General, the California Public Utility Commission ("CPUC"), the California Electricity Oversight Board ("EOB") and various states' rate payers in state and federal courts and with the Federal Energy Regulatory Commission ("FERC"). Most of the plaintiffs in the rate payer suits seek to represent a state-wide class of retail rate payers. In addition, civil and criminal investigations have been initiated by the United States Department of Justice ("DOJ"), the General Accounting Office, the FERC and various states' attorneys general. These matters involve claims that the Company engaged in unlawful business practices and generally seek unspecified amounts of restitution and penalties, although the damages alleged to have been incurred in some of the suits are in the billions of dollars. One of the suits brought by the California Attorney General seeks an order requiring the Company to divest its California plants. In addition, the Company is subject to the proceedings described below in *California Receivables, FERC Show Cause Proceeding Relating to Trading Practices, FERC Investigation Relating to Bidding,* and *DWR Power Purchases* relating to its operations in California and the western power markets. The Company made a provision of approximately $319 million for losses related to the Company's operations in California and the western power markets during 2000 and 2001. Resolution of these matters is subject to resolution of the ongoing litigation for the matters pending in courts and for those matters pending at the FERC to the issuance of final decisions by the FERC.

On July 6, 2004, the United States Court of Appeals for the Ninth Circuit upheld the dismissal by the United States District Court for the Northern District of California of the civil suit filed on March 11, 2002 by the California Attorney General against Mirant and several of its wholly-owned subsidiaries. The lawsuit alleged that between 1998 and 2001 the companies effectively double-sold their capacity by selling both ancillary services and energy from the same generating units, such that if called upon, the companies would have been unable to perform their contingent obligations under the ancillary services contracts. The court of appeals ruled that the California Attorney General's claims under California's Unfair Competition Act are barred by the doctrine of preemption and the filed rate doctrine, finding that the remedies sought would interfere with the FERC's exclusive authority to set wholesale electric rates under the Federal Power Act.

California Receivables: In 2001, Southern California Edison ("SCE") and Pacific Gas and Electric ("PG&E") suspended payments to the California Power Exchange Corporation ("PX") and California Independent System Operator ("CAISO") for certain power purchases, including purchases from Mirant. Both the PX and PG&E filed for bankruptcy protection in 2001. As of June 30, 2004, the

Company has outstanding receivables for power sales made in 2000 and 2001 in California totaling $342 million. The Company does not expect any significant payments to be received for these sales until the FERC issues final rulings regarding the related matters discussed in the next paragraph.

In July 2001, the FERC issued an order requiring hearings to determine the amount of any refunds and amounts owed for sales made to the CAISO or the PX from October 2, 2000 through June 20, 2001. Various parties have appealed these FERC orders to the United States Court of Appeals for the Ninth Circuit seeking review of a number of issues, including changing the potential refund date to include periods prior to October 2, 2000 and expanding the sales of electricity subject to potential refund to include sales made to the California Department of Water Resources ("DWR"). On December 12, 2002, an administrative law judge ("ALJ") determined the preliminary amounts currently owed to each supplier in the proceeding. Based on that determination the initial amounts owed to Mirant total approximately $122 million, which is net of refunds owed by Mirant to the CAISO and the PX. The ALJ decision indicated that these amounts do not reflect the final mitigated market clearing prices, interest that would be applied under the FERC's regulations, offsets for emission costs or the effect of certain findings made by the ALJ in the initial decision. A December 2002 errata issued by the ALJ to his initial decision indicated that the amounts identified by the initial decision as being owed to Mirant and other sellers by the PX failed to reflect an adjustment for January 2001 that the ALJ concluded elsewhere in his initial decision should be applied. If that adjustment is applied, the net amount owed Mirant after taking into account the proposed refunds would increase by approximately $37 million.

On March 3, 2003, the California Attorney General, the EOB, the CPUC, PG&E and SCE (the "California Parties") filed submittals with the FERC in the California refund proceeding alleging that owners of generating facilities in California and energy marketers, including Mirant entities, had engaged in extensive manipulation of the California wholesale electricity market during 2000 and 2001. The California Parties argued that the FERC should expand the transactions subject to the refund proceeding to include short-term and long-term bilateral transactions entered into by the DWR that were not conducted through the CAISO and PX and should begin the refund period as of January 1, 2000 rather than October 2, 2000. Expansion of the scope of the transactions subject to refund in the manner sought by the California Parties could materially affect the amount of any refunds that Mirant might be determined to owe, and any such additional refunds could negatively impact the Company's consolidated financial position, results of operations or cash flows. On March 20, 2003, the Company filed reply comments denying that it had engaged in any conduct that violated the Federal Power Act or any tariff provision applicable to its transactions in California. The Company stated that the purported evidence presented by the California Parties did not support the allegations that it had engaged in market manipulation, had violated the Federal Power Act or had not complied with any applicable tariff or order of the FERC.

On March 26, 2003, the FERC largely adopted the findings of the ALJ made in his December 12, 2002 order with the exception that the FERC concluded that the price of gas used in calculating the mitigated market prices used to determine refunds should not be based on published price indices. Instead, the FERC ruled that the price of gas should be based upon the price at the producing area plus transportation costs. This adjustment by the FERC to the refund methodology is expected to reduce the net amount that would remain owed to Mirant after taking into account any refunds. Based solely on the FERC staff's formula, the amount of the reduction could be as much as approximately $110 million, which would reduce the net amount owed to Mirant to approximately $49 million. The FERC indicated that it would allow any generator that can demonstrate it actually paid a higher price for gas to recover the differential between that higher price and the proxy price for gas adopted by the FERC. Mirant's actual cost of gas used to make spot sales of electricity was higher than the amounts calculated under the staff's formula, which differential, if accepted by the FERC, would decrease significantly the $110 million and increase the resulting net amount owed to Mirant, although the

amount of such potential decrease that will be accepted by the FERC and the resulting net amount owed to Mirant cannot at this time be determined. On October 16, 2003, the FERC issued an order addressing motions for rehearing filed with respect to its March 26, 2003 order, and in that October 16, 2003 order the FERC changed how certain power sales made to the CAISO were to be treated. Mirant estimates that the effect of the October 16, 2003 order will be to increase the net amounts owed to Mirant, by $27 million. On May 12, 2004, the FERC issued an order on rehearing of the October 16, 2003 order that further modified how certain power sales made to the CAISO are to be treated and that may reduce significantly the potential benefit to Mirant of the October 16, 2003 order. In another order issued May 12, 2004, the FERC also further refined the methodology to be used to determine the costs of gas that a generator can recover where it can demonstrate that it paid a higher price for gas than the proxy price for gas previously adopted by the FERC in its March 23, 2003 order, and those changes may have the effect of reducing the costs that Mirant is able to recover. Mirant is unable at this time to quantify further the impact of the May 12, 2004 orders.

In its March 26, 2003 order, the FERC also ruled that any future findings of market manipulation resulting from its ongoing review of conduct in the California market in 2000 and 2001 discussed below in *FERC Show Cause Proceeding Relating to Trading Practices* and *FERC Investigation Related to Bidding* would not result in a resetting of the refund effective date or the mitigated market prices developed for the refund period. Instead, the remedy for any such market manipulation that is found to have occurred will be disgorgement of profits and other appropriate remedies and such remedies could apply to conduct both prior to and during the refund period. The amount owed to Mirant from sales made to either the CAISO or the PX, the amount of any refund that Mirant might be determined to owe, and whether Mirant may have any refund obligation with respect to sales made to the DWR may be affected materially by the ultimate resolution of the issues described above related to which gas indices should be used in calculating the mitigated market clearing prices, allegations of market manipulation, whether the refund period should include periods prior to October 2, 2000, and whether the sales of electricity potentially subject to refund should include sales made to the DWR.

In the July 2001 order, the FERC also ordered that a preliminary evidentiary proceeding be held to develop a factual record on whether there were unjust and unreasonable charges for spot market bilateral sales in the Pacific Northwest from December 25, 2000 through June 20, 2001. In that proceeding, the California parties (consisting of the California Attorney General, the CPUC and the EOB) filed to recover certain refunds from parties, including Mirant Americas Energy Marketing, for bilateral sales of electricity to the DWR at the California/Oregon border, claiming that such sales took place in the Pacific Northwest. The refunds sought from Mirant Americas Energy Marketing totaled approximately $90 million. If Mirant Americas Energy Marketing were required to refund such amounts, other subsidiaries of the Company, including subsidiaries of Mirant Americas Generation, could be required to refund amounts previously received pursuant to sales made on their behalf by Mirant Americas Energy Marketing during the refund periods. In addition, the Company's subsidiaries would be owed amounts for purchases made on their behalf from other sellers in the Pacific Northwest. In an order issued June 25, 2003, the FERC ruled that no refunds were owed and terminated the proceeding. On November 10, 2003, the FERC denied requests for rehearing filed by various parties. Various parties have appealed the FERC's decision to the United States Court of Appeals for the Ninth Circuit.

FERC Show Cause Proceeding Relating to Trading Practices: On June 25, 2003, the FERC issued a show cause order (the "Trading Practices Order") to more than fifty parties, including Mirant entities, that the FERC Staff report issued on March 26, 2003 indicated may have engaged in one or more trading strategies of the type employed by Enron Corporation and its affiliates ("Enron") that were portrayed in the Enron memos released by the FERC in May 2002. The Trading Practices Order identified certain specific trading practices that the FERC indicated could constitute gaming or anomalous market behavior in violation of the CAISO and PX tariffs. The order required the CAISO

to identify those transactions engaged in by the parties that are the subject of the order between January 1, 2000 and June 20, 2001 that potentially fall within the specified practices. Those parties, including the Mirant entities, then had to demonstrate why those transactions were not violations of the PX and CAISO tariffs. On September 30, 2003, the Company filed with the FERC a settlement agreement, dated September 25, 2003, entered into between the Company and the FERC Trial Staff, under which Mirant would pay $332,411 to settle the show cause proceeding, except for the issue related to selling of ancillary services, which is discussed below. In a November 14, 2003 order in a different proceeding, the FERC ruled that certain allegations of improper trading conduct with respect to the selling of ancillary services during 2000 should be resolved in the show cause proceeding. The proposed settlement entered into by the Company and the FERC Trial Staff did not resolve the allegations made against Mirant with respect to that particular practice. On December 19, 2003, Mirant filed with the FERC for its approval an amendment to the settlement agreement reached with the FERC Trial Staff under which the FERC would have an allowed claim in Mirant Americas Energy Marketing's bankruptcy proceeding for $3.67 million in settlement of the allegations with respect to the sale of ancillary services. That settlement is subject to the approval of the FERC and the Bankruptcy Court. On March 11, 2004, an ALJ recommended that the FERC approve the settlement, finding that the settlement amounts were reasonable. The ALJ, however, suggested that approval of the settlement be conditioned on the settlement amount associated with claims of improper selling of ancillary services being treated as an administrative claim or a setoff rather than as an allowed pre-petition claim.

FERC Investigation Relating to Bidding: The FERC on June 25, 2003 issued an order (the "Bidding Order") initiating an investigation by its staff into bidding practices in the PX and CAISO markets between May 1, 2000 and October 1, 2000 of more than fifty parties, including Mirant entities. These entities were previously identified in the report issued by the FERC Staff on March 26, 2003 as having bid generation resources to the PX and CAISO at prices unrelated to costs. The Bidding Order requires those entities, including the Mirant entities, to demonstrate why bids in the PX and CAISO markets from May 1, 2000 through October 1, 2000 that were in excess of $250 per megawatt hour did not constitute a violation of the CAISO and PX tariffs. If the FERC finds that the Mirant entities engaged in bidding practices that violated the PX or CAISO tariffs between May 1, 2000 through October 1, 2000, the FERC could require the disgorgement of profits made as a result of those bids and could impose other non-monetary penalties. While the Company believes its bidding practices were legitimate and that it did not violate the appropriate tariffs, the standards by which the FERC will ultimately judge the Company's bidding practices are unclear. Depending on the standards applied by the FERC and if Mirant entities are found by the FERC to have violated the PX or CAISO tariffs, the amount of any disgorgement of profits required or other remedy imposed by the FERC could have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

DWR Power Purchases: On May 22, 2001, Mirant entered into a 19-month agreement with the DWR to provide the State of California with approximately 500 MW of electricity during peak hours through December 31, 2002. On February 25, 2002, the CPUC and the EOB filed separate complaints at the FERC against Mirant and other sellers of energy under long-term agreements with the DWR, alleging that the terms of these contracts are unjust and unreasonable and that the contracts should be abrogated or the prices under the contracts should be reduced. The complaints allege that the prices the DWR was forced to pay pursuant to these long-term contracts were unreasonable due to dysfunctions in the California market and the alleged market power of the sellers. On June 26, 2003, the FERC issued an order dismissing the complaints filed by the CPUC and the EOB against Mirant. On November 10, 2003, the FERC denied motions for rehearing filed by the CPUC and the EOB. The CPUC and EOB have appealed the FERC's decision to the United States Court of Appeals for the Ninth Circuit.

"Reliability-Must-Run" Agreements: Certain of the Company's generating facilities acquired from PG&E are operated subject to reliability-must-run ("RMR") agreements. These agreements allow the CAISO to require the Company, under certain conditions, to operate these facilities to support the California electric transmission system. Mirant assumed these agreements from PG&E subject to the outcome of a 1997 FERC proceeding to determine the amount of the charges to be paid by the CAISO under the agreements with respect to those plants out of which Mirant could also receive additional revenues from market sales. For those plants that are subject to the RMR agreements and from which Mirant has exercised its right to also make market sales, Mirant has been collecting from the CAISO since April 1999 an amount equal to 50% of the annual fixed revenue requirement of those plants. The amounts the Company collects from the CAISO are subject to refund pending final review and approval by the FERC. In June 2000, an ALJ issued a decision finding that the amount the Company should be allowed to charge the CAISO for such plants was approximately 3 1/2%, on average, of the annual fixed revenue requirement. In July 2000, Mirant sought review by the FERC of the ALJ decision, and a decision is pending at the FERC.

The Company recognizes revenue related to these agreements based on the rates ruled to be reasonable by the ALJ. If the Company is unsuccessful in its appeal of the ALJ's decision, it will be required to refund amounts collected in excess of those rates for the period from June 1, 1999. For the Potrero plant and Pittsburg Units 1 through 4 the period for which such refunds would be owed would run through December 31, 2001, for Mirant's other California plants except Pittsburg Unit 5 the refund period would run through December 31, 2002, and for Pittsburg Unit 5 the refund period would run through December 31, 2003. Amounts collected in excess of those rates and other significantly smaller amounts collected under the RMR tariffs that are also subject to refund due to other issues pending at the FERC totaled $293 million, of which $288 million is included in liabilities subject to compromise and $5 million is deferred and included in revenues subject to refund in the accompanying consolidated balance sheet as of June 30, 2004 and December 31, 2003. In addition, the Company records accrued interest on such amounts, which amounted to $42 million and is included in liabilities subject to compromise in the accompanying consolidated balance sheets as of June 30, 2004 and December 31, 2003, respectively. If resolution of the proceeding results in refunds of that magnitude and the Company were unable to arrange to make the refunds over a multi-year period, it may result in the Company's subsidiaries that are subject to the RMR agreements disposing of one or more of the generating facilities owned by such subsidiaries.

Shareholder Litigation

Twenty lawsuits have been filed since May 2002 against Mirant and four of its officers alleging, among other things, that defendants violated federal securities laws by making material misrepresentations and omissions to the investing public regarding Mirant's business operations and future prospects during the period from January 19, 2001 through May 6, 2002 due to potential liabilities arising out of its activities in California during 2000 and 2001. The complaints seek unspecified damages, including compensatory damages and the recovery of reasonable attorneys' fees and costs. These suits have been consolidated into a single action.

In November 2002, the plaintiffs filed an amended complaint that added as defendants Southern Company, the directors of Mirant immediately prior to its initial public offering of stock, and various firms that were underwriters for the initial public offering by the Company. In addition to the claims set out in the original complaint, the amended complaint asserts claims under the Securities Act of 1933, alleging that the registration statement and prospectus for the initial public offering of Mirant's stock misrepresented and omitted material facts. On July 14, 2003, the district court dismissed the claims asserted by the plaintiffs based on the Company's California business activities but allowed the case to proceed on the plaintiffs' other claims. This action is stayed as to Mirant by the filing of its Chapter 11 proceeding. On November 19, 2003, the Bankruptcy Court entered an order staying this

action also with respect to the other defendants to avoid the suit impeding the ability of Mirant to reorganize or having a negative effect upon Mirant's assets. The Bankruptcy Court has modified the stay to allow the plaintiffs to proceed with discovery of documentary materials from Mirant and the other defendants.

Under a master separation agreement between Mirant and Southern Company, Southern Company is entitled to be indemnified by Mirant for any losses arising out of any acts or omissions by Mirant and its subsidiaries in the conduct of the business of Mirant and its subsidiaries. The underwriting agreements between Mirant and the various firms added as defendants that were underwriters for the initial public offering by the Company also provide for Mirant to indemnify such firms against any losses arising out of any acts or omissions by Mirant and its subsidiaries.

Shareholder Derivative Litigation

Four purported shareholders' derivative suits have been filed against Mirant, its directors and certain officers of the Company. Two of those suits have been consolidated. These lawsuits allege the directors breached their fiduciary duty by allowing the Company to engage in alleged unlawful or improper practices in the California energy markets in 2000 and 2001. The Company practices alleged in these lawsuits largely mirror those alleged with respect to the Company's activities in California in the shareholder litigation discussed above. One suit also alleges that the defendant officers engaged in insider trading. The complaints seek unspecified damages on behalf of the Company, including attorneys' fees, costs and expenses and punitive damages. These actions are stayed as to Mirant by the filing of its Chapter 11 proceeding. On November 19, 2003, the Bankruptcy Court entered an order staying these actions also with respect to the individual defendants to avoid the suit impeding the ability of Mirant to reorganize or having a negative effect upon Mirant's assets. On December 8, 2003, the court in the Cichocki suit took notice of the Bankruptcy Court's Order dated November 19, 2003 staying the litigation and administratively closed the action.

ERISA Litigation

On April 17, 2003 and June 3, 2003, purported class action lawsuits alleging violations of ERISA were filed in the United States District Court for the Northern District of Georgia (the "ERISA Litigation"). The ERISA Litigation names as defendants Mirant Corporation, certain of its current and former officers and directors, and Southern Company. The plaintiffs, who seek to represent a putative class of participants and beneficiaries of Mirant's 401(k) plans (the "Plans"), allege that defendants breached their duties under ERISA by, among other things, (1) concealing information from the Plans' participants and beneficiaries; (2) failing to ensure that the Plans' assets were invested prudently; (3) failing to monitor the Plans' fiduciaries; and (4) failing to engage independent fiduciaries to make judgments about the Plans' investments. The plaintiffs seek unspecified damages, injunctive relief, attorneys' fees and costs. On September 2, 2003, the District Court issued an order consolidating the two suits. On September 23, 2003, the plaintiffs filed an amended and consolidated complaint. The amended and consolidated complaint asserted similar factual allegations as the previously filed lawsuits and added as defendants T. Rowe Price Trust Company and certain additional current and former officers of the Company. The consolidated action is stayed as to Mirant by the filing of its Chapter 11 proceeding. On November 19, 2003, the Bankruptcy Court entered an order staying this action also with respect to the other defendants to avoid the suit impeding the ability of Mirant to reorganize or having a negative effect upon Mirant's assets. By agreement, however, the suit has been allowed to proceed through the filing of, and ruling by the District Court upon, motions to dismiss. On January 9, 2004, T. Rowe Price Trust Company answered the amended and consolidated complaint. All other defendants filed motions on that date seeking dismissal of the plaintiffs' claims for failure to state a claim upon which relief can be granted. On February 19, 2004, the plaintiffs dismissed their claims against Southern Company without prejudice. On June 14, 2004, the plaintiffs filed a motion seeking to

amend their consolidated complaint to add as defendants Mirant Services, LLC and its board of managers. Mirant is opposing that request.

Mirant Americas Generation Bondholder Suit

On June 10, 2003, certain holders of senior notes of Mirant Americas Generation maturing after 2006 filed a complaint in the Court of Chancery of the State of Delaware*, California Public Employees' Retirement System, et al. v. Mirant Corporation, et. al.,* that named as defendants Mirant, Mirant Americas, Mirant Americas Generation, certain past and present Mirant directors, and certain past and present Mirant Americas Generation managers. Among other claims, the plaintiffs assert that a restructuring plan pursued by the Company prior to its filing a petition for reorganization under Chapter 11 of the Bankruptcy Code was in breach of fiduciary duties allegedly owed to them by Mirant, Mirant Americas, and Mirant Americas Generation's managers. In addition, plaintiffs challenge certain dividends and distributions made by Mirant Americas Generation. Plaintiffs seek damages in excess of one billion dollars. Mirant has removed this suit to the United States District Court for the District of Delaware. This action is stayed with respect to the Mirant entities that are defendants by the filing of the Chapter 11 proceedings of these entities. On November 19, 2003, the Bankruptcy Court entered an order staying this action also with respect to the individual defendants to avoid the suit impeding the ability of the Mirant Debtors to reorganize or having a negative effect upon the assets of the Mirant Debtors. The committee representing unsecured creditors of Mirant Americas Generation filed a motion in Mirant's bankruptcy proceedings seeking to pursue claims against Mirant, Mirant Americas, certain past and present Mirant directors, and certain past and present Mirant Americas Generation managers similar to those asserted in this suit. The Bankruptcy Court ruled that while the committee has standing to assert claims on behalf of the estate of Mirant Americas Generation, no such claims could be filed without the Bankruptcy Court's approval and no motions seeking such approval could be filed at least through April 2004. No such motion has been filed with the Bankruptcy Court since April 2004, and the Bankruptcy Court has not authorized any such litigation at this time.

Mirant Americas Generation Securities Class Action

On June 25, 2003, Mirant received notice that on June 11, 2003, a purported class action lawsuit alleging violations of Sections 11 and 15 of the Securities Act of 1933 was filed in the Superior Court of Fulton County, Georgia entitled *Wisniak v. Mirant Americas Generation, LLC, et al*. The lawsuit names as defendants Mirant Americas Generation and certain current and former officers and managers of Mirant Americas Generation. The plaintiff seeks to represent a putative class of all persons who purchased debt securities of Mirant Americas Generation pursuant to or traceable to an exchange offer completed by Mirant Americas Generation in May 2002 in which $750 million of bonds registered under the Securities Act were exchanged for $750 million of previously issued senior notes of Mirant Americas Generation. The plaintiff alleges, among other things, that Mirant Americas Generation's restatement in April 2003 of prior financial statements rendered the registration statement filed for the May 2002 exchange offer materially false. The complaint seeks damages, interest and attorneys' fees. The defendants have removed the suit to the United States District Court for the Northern District of Georgia. This action is stayed as to Mirant Americas Generation by the filing of its Chapter 11 proceeding. On November 19, 2003, the Bankruptcy Court entered an order staying this action also with respect to the individual defendants to avoid the suit impeding the ability of Mirant Americas Generation to reorganize or having a negative effect upon its assets. On December 8, 2003, the district court took notice of the Bankruptcy Court's Order dated November 19, 2003 staying the litigation and administratively closed the action. On December 16, 2003, the plaintiff dismissed Mirant Americas Generation as a defendant, without prejudice.

U.S. Government Inquiries

SEC Investigation: In August 2002, Mirant received a notice from the Division of Enforcement of the Securities and Exchange Commission ("SEC") that it was conducting an investigation of Mirant. The Division of Enforcement has asked for information and documents relating to various topics such as accounting issues (including the issues announced on July 30, 2002 and August 14, 2002), energy trading matters (including round trip trades), Mirant's accounting for transactions involving special purpose entities, and information related to shareholder litigation. In late June 2003, the Division of Enforcement advised Mirant that its investigation of Mirant had become a formal investigation in February 2003. Mirant intends to continue to cooperate fully with the SEC.

Department of Justice Inquiries: In 2002 the Company was contacted by the DOJ regarding the Company's disclosure of accounting issues, energy trading matters and allegations contained in the amended complaint discussed above in *Shareholder Litigation* that Mirant improperly destroyed certain electronic records related to its activities in California. The Company has been asked to provide copies of the same documents requested by the SEC in their inquiry, and the Company intends to continue to cooperate fully with the DOJ. The DOJ has advised Mirant that it does not intend to take further action with respect to the allegations of improper destruction of electronic records.

In November 2002, Mirant received a subpoena from the DOJ, acting through the United States Attorney's office for the Northern District of California, requesting information about its activities and those of its subsidiaries for the period since January 1, 1998. The subpoena requested information related to the California energy markets and other topics, including the reporting of inaccurate information to the trade press that publish natural gas or electricity spot price data. The subpoena was issued as part of a grand jury investigation. Mirant has continued to receive additional requests for information from the United States Attorney's office, and it intends to continue to cooperate fully with the United States Attorney's office in this investigation.

Commodity Futures Trading Commission Inquiries: In August 2002, the Commodity Futures Trading Commission ("CFTC") asked the Company for information about certain buy and sell transactions occurring during 2001. The Company provided information regarding such trades to the CFTC, none of which the Company considers to be wash trades. The CFTC subsequently requested additional information, including information about all trades conducted on the same day with the same counterparty that were potentially offsetting during the period from January 1, 1999 through June 17, 2002, which information the Company provided. In March 2003, the Company received a subpoena from the CFTC requesting a variety of documents and information related to the Company's trading of electricity and natural gas and its reporting of transactional information to energy industry publications that prepare price indices for electricity and natural gas for the period from January 1, 1999 through the date of the subpoena. Among the documents requested were any documents previously produced to the FERC, the SEC, the DOJ, any state's Attorney General, and any federal or state grand jury. The Company has continued to receive additional requests for information from the CFTC, and it intends to continue to cooperate fully with the CFTC. In a submission to the United States District Court for the Southern District of Texas on July 16, 2003 in a proceeding not involving the Company, the CFTC identified Mirant as one of nineteen parties being investigated for potential inaccurate gas price reporting in violation of the Commodity Exchange Act. The filing made by the CFTC indicated that it had uncovered evidence showing that eighteen of the nineteen companies may have inaccurately reported gas prices to the trade publications. Mirant understands that it is one of those eighteen companies. During reviews in connection with the CFTC investigation, Mirant has become aware that some of its employees reported information to energy industry publications that was inaccurate. Because this investigation is ongoing and the data is voluminous, Mirant cannot predict what the outcome will be.

Department of Labor Inquiries: On August 21, 2003, the Company received a notice from the Department of Labor (the "DOL") that it was commencing an investigation pursuant to which it was undertaking to review various documents and records relating to the Mirant Services Employee Savings Plan and the Mirant Services Bargaining Unit Employee Savings Plan. The DOL has interviewed Mirant personnel regarding those plans. The Company intends to continue to cooperate fully with the DOL.

PEPCO Back-to-Back Agreement

In connection with Mirant's acquisition of the Mirant Mid-Atlantic assets from Potomac Electric Power Company ("PEPCO") in 2000, PEPCO granted Mirant certain rights to purchase from PEPCO all power it received under long-term power purchase agreements with Ohio Edison Company and Panda-Brandywine L.P. ("Panda") that expire in 2005 and 2021, respectively. Mirant and PEPCO entered into a contractual arrangement (the "Back-to-Back Agreement") with respect to PEPCO's agreements with Panda and Ohio Edison under which (1) PEPCO agreed to resell to Mirant all "capacity, energy, ancillary services and other benefits" to which it is entitled under those agreements; and (2) Mirant agreed to pay PEPCO each month all amounts due from PEPCO to Panda or Ohio Edison for the immediately preceding month associated with such capacity, energy, ancillary services and other benefits. Under this agreement, Mirant is obligated to purchase power from PEPCO in the Pennsylvania-New Jersey-Maryland Interconnection LLC ("PJM") marketplace at prices that are significantly higher than existing market prices for power. On August 28, 2003, the Mirant Debtors filed a motion with the Bankruptcy Court to reject the Back-to-Back Agreement. The Mirant Debtors forecast that it would cost the Mirant Debtors in excess of $300 million during 2004 and 2005 if the Back-to-Back Agreement were to remain in effect. These anticipated losses, as compared to what could be obtained if market rates were applied, are even greater over the entire life of the agreement, which continues until 2021.

In their August 28, 2003 motion, the Mirant Debtors also requested that the Bankruptcy Court enjoin the FERC from compelling the Mirant Debtors to perform under the Back-to-Back Agreement. On August 28, 2003, the Bankruptcy Court entered a temporary restraining order ("TRO") against PEPCO and the FERC. On September 8, 2003, the Office of the People's Counsel for the District of Columbia filed a complaint with the FERC seeking an order holding that the terms of the Back-to-Back Agreement may not be modified or terminated without the approval of the FERC. Also on September 8, 2003, the Public Service Commission of Maryland and the Maryland Office of People's Counsel filed a petition with the FERC seeking an order declaring that Mirant must continue to perform pursuant to the Back-to-Back Agreement with PEPCO. These filings by the Office of the People's Counsel for the District of Columbia, the Public Service Commission of Maryland and the Maryland Office of People's Counsel were withdrawn in February 2004. On September 17, 2003, the Bankruptcy Court entered an order extending the TRO and enjoining the FERC from issuing the orders requested by such administrative petitions filed with the FERC. On September 25, 2003, the Bankruptcy Court converted the TRO to a preliminary injunction. On October 9, 2003, the United States District Court for the Northern District of Texas entered an order that had the effect of transferring to that court from the Bankruptcy Court the motion filed by the Mirant Debtors seeking to reject the Back-to-Back Agreement and the proceedings in which the Bankruptcy Court had issued the preliminary injunction against the FERC.

On December 23, 2003, the United States District Court for the Northern District of Texas denied the Mirant Debtors' motion seeking to reject the Back-to-Back Agreement. The District Court ruled that the Federal Power Act preempts the Bankruptcy Code and that a bankruptcy court cannot affect a matter within the FERC's jurisdiction under the Federal Power Act, including the rejection of a wholesale power purchase agreement regulated by the FERC. In its December 23, 2003 order, the District Court also vacated the injunction granted by the Bankruptcy Court that restrained the FERC

from acting with respect to the Back-to-Back Agreement. On August 4, 2004, the United States Court of Appeals for the Fifth Circuit reversed the District Court's December 23, 2003 decision dismissing the Mirant Debtor's motion to reject the Back-to-Back Agreement. The Court of Appeals ruled that the Bankruptcy Code does authorize the District Court to reject a contract for the sale of electricity that is subject to the FERC's regulation under the Federal Power Act as part of a bankruptcy proceeding and that the Federal Power Act does not preempt that authority. The Court of Appeals did not address the merits of the Mirant Debtor's motion to reject the Back-to-Back Agreement but remanded the proceeding to the District Court for further action on that motion. The Court of Appeals did indicate that on remand the District Court should consider applying a more rigorous standard than the business judgement standard typically applicable to contract rejection decisions by debtors in bankruptcy, which more rigorous standard would take into account the public interest in the transmission and sale of electricity. With respect to the injunctions issued by the Bankruptcy Court that were vacated by the District Court, the Court of Appeals ruled that the injunctive relief granted by the Bankruptcy Court exceeded its authority under the Bankruptcy Code. While the Court of Appeals found that the injunctive relief actually granted by the Bankruptcy Court was too broad, it did state that the concern expressed by the Bankruptcy Court, that the FERC could negate the Mirant Debtor's rejection of an executory contract by ordering the Mirant Debtors to continue to perform under the terms of the rejected contract, was a legitimate basis for injunctive relief.

At the time of the acquisition of the Mirant Mid-Atlantic assets from PEPCO, Mirant also entered into an agreement with PEPCO that, as subsequently modified, provided that the price paid by Mirant for its December 2000 acquisition of PEPCO assets would be adjusted if by March 19, 2005 a binding court order has been entered finding that the Back-to-Back Agreement violates PEPCO's power purchase agreement with Panda ("Panda PPA") as a prohibited assignment, transfer or delegation of the Panda PPA or because it effects a prohibited delegation or transfer of rights, duties or obligations under the Panda PPA that is not severable from the rest of the Back-to-Back Agreement. If a court order is entered that triggers the purchase price adjustment, the amount of the adjustment is to be negotiated in good faith by the parties or determined by binding arbitration so as to compensate PEPCO for the termination of the benefit of the Back-to-Back Agreement while also holding Mirant economically indifferent from such court order. Panda initiated legal proceedings in 2000 asserting that the Back-to-Back Agreement violated provisions in the Panda PPA prohibiting PEPCO from assigning the Panda PPA or delegating its duties under the Panda PPA to a third party without Panda's prior written consent. On June 10, 2003, the Maryland Court of Appeals, Maryland's highest court, ruled that the assignment of certain rights and delegation of certain duties by PEPCO to Mirant did violate the non-assignment provision of the Panda PPA and was unenforceable. The court, however, left open the issues whether the provisions found to violate the Panda PPA could be severed and the rest of the Back-to Back Agreement enforced and whether Panda's refusal to consent to the assignment of the Panda PPA by PEPCO to Mirant was unreasonable and violated the Panda PPA. If the June 10, 2003 decision by the Maryland Court of Appeals or a subsequent decision addressing the Back-to-Back Agreement is determined to have triggered the adjustment to the purchase price paid by Mirant to PEPCO, such adjustment would not be expected to have a material adverse effect on the Company's financial position or results of operations.

Enron Bankruptcy Proceedings

Since December 2, 2001, Enron and a number of its subsidiaries have filed for bankruptcy. As of June 30, 2004 and December 31, 2003, the total amount owed to Mirant by Enron was approximately $72 million. Mirant has filed formal claims in the Enron bankruptcy proceedings. Mirant has recorded a reserve for potential bad debts of $64 million as of December 31, 2003. The Company does not expect the outcome of Enron's bankruptcy proceeding to have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

Enron Canada Claim

In June 2000, Mirant provided a guarantee of the obligations of Mirant Americas Energy Marketing Canada, Ltd. ("Mirant Canada") to Enron Canada Corp. up to a maximum amount of $30 million (Canadian). In May 2002, Enron Canada filed a claim against Mirant Canada in the Court of Queen's Bench of Alberta seeking $45 million (Canadian) related to Mirant Canada's termination of transactions for the purchase and sale of natural gas with Enron Canada in December 2001. Enron Canada's claim against Mirant Canada was subject to Mirant Canada's reorganization proceeding under the CCAA in Canada. Mirant had recorded approximately $25 million (US) as liabilities subject to compromise on its consolidated balance sheets as of December 31, 2003 with respect to these claims. Recently, as part of the CCAA proceeding, Mirant Canada settled Enron Canada's claim for $31.9 million (Canadian). Further, as part of the CCAA proceeding, Enron Canada will receive 80% of the settled claim from Mirant Canada. Enron Canada will be permitted to assert a claim against Mirant under the guarantee for the remaining 20% of the settled claim (approximately $6.3 million (Canadian)).

Edison Mission Energy Litigation

In March 2002, two subsidiaries of Edison International (collectively "EME") filed suit alleging Mirant breached its agreement to purchase EME's 50% interest in EcoElectrica Holdings Ltd., the owner of a 540 MW cogeneration facility in Puerto Rico. On April 29, 2003, EME amended its complaint to assert additional claims for fraudulent misrepresentation and concealment, conspiracy to defraud, and negligent misrepresentation. EME seeks compensatory damages in excess of $50 million, punitive and exemplary damages of an unspecified amount, interest and attorneys' fees. The Company believes it did not breach its agreement with EME. At the same time Mirant and its subsidiaries entered into the contract with EME, they entered into a separate agreement with a subsidiary of Enron Corporation to purchase an additional 47.5% ownership interest in EcoElectrica. That purchase also was not completed, and the Enron subsidiary has filed claims against Mirant in its Chapter 11 proceeding asserting damages for breach of the purchase agreement with Enron. The EME suit is stayed by the filing of Mirant's Chapter 11 proceeding.

Environmental Liabilities

In 2000, the State of New York issued a notice of violation to Orange and Rockland Utilities, Inc., the previous owner of Mirant New York's Lovett facility, concerning the air permitting and air emission control implications under the Environmental Protection Agency's ("EPA") new source review regulations promulgated under the Clean Air Act ("NSR") of the operation of that plant prior to its acquisition by Mirant New York. On June 11, 2003, Mirant New York and the State of New York entered into, and filed for approval with the United States District Court for the Southern District of New York, a consent decree that released Mirant New York from all potential liability for matters addressed in the notice of violation previously issued by the State of New York to Orange and Rockland Utilities, Inc. and for any other potential violation of NSR or related New York air laws prior to and through the date of entry of the consent decree by the court. Under the decree, Mirant New York commits to install on Lovett's two coal-fired units by 2007 to 2008 emission control technology consisting of selective catalytic reduction technology to reduce nitrogen oxide emissions, alkaline in-duct injection technology to reduce sulfur dioxide emissions, and a baghouse. The cost of the emission controls prescribed by the consent decree could exceed $100 million over the approximately five year period covered by the consent decree. Such costs would generally be capitalized and amortized as a component of property, plant and equipment. The consent decree allows Mirant New York to shut down a unit rather than install the prescribed emission controls on the unit. For one of the units, Mirant New York also has the option to convert the unit to operate exclusively as a gas-fired boiler and limit the hours of operation rather than install the prescribed emission controls.

Mirant New York did not admit to any liability, and the consent decree does not impose any penalty on Mirant New York for alleged past violations. The District Court approved and entered the consent decree on October 9, 2003, and it was approved by the Bankruptcy Court on October 15, 2003. Under the consent decree, Mirant New York by August 1, 2004 was required to notify the State of New York whether it would convert Lovett Unit 5 to natural gas, install control technology on that unit, or discontinue the operation of that unit, and, if Mirant New York elected to install control technology on that unit, to award construction contracts for such control technology. The consent decree also required Mirant New York to notify the State of New York by August 1, 2004 whether it would install a baghouse on Lovett Unit 4 or Lovett Unit 5 to reduce particulate emissions. On July 30, 2004, Mirant New York and the State of New York agreed to modify the consent decree to delay such notification requirements until August 1, 2005.

In January 2001, the EPA issued a request for information to Mirant concerning the air permitting and air emission control implications under the New Source Review regulations promulgated by the EPA under the Clean Air Act of past repair and maintenance activities at the Company's Potomac River plant in Virginia and Chalk Point, Dickerson and Morgantown plants in Maryland. The requested information concerns the period of operations that predates the Company's ownership and lease of the plants. Mirant has responded fully to this request. If a violation is determined to have occurred at any of the plants, the Company may be responsible for the cost of purchasing and installing emission control equipment, the cost of which may be material. Under the sales agreement with PEPCO for those plants, PEPCO is responsible for fines and penalties arising from any violation associated with historical operations prior to the Company's acquisition of the plants. If a violation is determined to have occurred after Mirant acquired the plants or, if occurring prior to the acquisition, is determined to constitute a continuing violation, Mirant would be subject to fines and penalties by the state or federal government for the period subsequent to its acquisition of the plants, the cost of which may be material.

On September 10, 2003, the Virginia Department of Environmental Quality issued a Notice of Violation ("NOV") to Mirant Potomac River, LLC alleging that it violated its Virginia Stationary Source Permit to Operate by emitting nitrogen oxide in excess of the "cap" established by the permit for the 2003 summer ozone season. Mirant Potomac River has responded to the NOV, asserting that the cap is unenforceable, that it can comply through the purchase of emissions credits and raising other equitable defenses. Virginia's civil enforcement statute provides for injunctive relief and penalties, but no civil suit has as yet been filed. On January 22, 2004, the EPA issued a Notice of Violation to Mirant Potomac River alleging the same violation of its Virginia Stationary Source Permit to Operate as set out in the NOV issued by the Virginia Department of Environmental Quality.

New York Tax Proceedings

Mirant's subsidiaries that own generating plants in New York are the petitioners in forty-one proceedings ("Tax Certiorari Proceedings") initially brought in various New York state courts challenging the assessed value of those generating plants determined by their respective local taxing authorities. Mirant Bowline Energy, LLC ("Mirant Bowline") has challenged the assessed value of the Bowline generating facility and the resulting local tax assessments paid for tax years 1995 through 2003. Mirant Bowline succeeded to rights held by Orange & Rockland Utilities, Inc. for the tax years prior to its acquisition of the Bowline Plant in 1999 under its agreement with Orange & Rockland for the purchase of that plant. Mirant Lovett, LLC ("Mirant Lovett") has initiated proceedings challenging the assessed value of the Lovett facility for each of the years 2000 through 2003. Mirant NY-Gen, LLC ("Mirant NY-Gen" and collectively with Mirant Bowline and Mirant Lovett, the "New York Debtors") has proceedings pending with respect to the combustion turbine and hydroelectric facilities it owns for each of the years 2000 through 2003. If the Tax Certiorari Proceedings result in a reduction of the

assessed value of the generating facility at issue in each proceeding, the Mirant entity owning the facility would be entitled to a refund with interest of any excess taxes paid for those tax years.

On September 30, 2003, the Mirant Debtors filed a motion (the "Tax Determination Motion") with the Bankruptcy Court requesting that it determine what the property tax liability should have been for the Bowline generating facility in each of the years 1995 through 2003. The Tax Determination Motion similarly sought to have the Bankruptcy Court determine what the property tax liability should have been for (a) the generating facility acquired by Mirant Lovett concurrently with Mirant Bowline's acquisition of the Bowline facility in each of the years 2000 through 2003, and (b) certain generating facilities concurrently acquired by Mirant NY-Gen at the time Mirant Bowline acquired the Bowline facility in each of the years 2000 through 2003. The bases for the relief requested in the Tax Determination Motion on behalf of each of the New York Debtors were that the assessed values of generating facilities located in New York made by the relevant taxing authorities had no justifiable basis and were (and are) far in excess of their actual value. The local taxing authorities have opposed the Tax Determination Motion, arguing that the Bankruptcy Court either lacks jurisdiction over the matters addressed by the Tax Determination Motion or should abstain from addressing those issues so that they can be addressed by the state courts in which the Tax Certiorari Proceedings described in the preceding paragraph were originally filed. On December 10, 2003, the Bankruptcy Court ruled that it would retain joint jurisdiction with the New York state courts over the issues raised by the Tax Certiorari Proceedings and the Tax Determination Motion. The ruling further indicated that for any of the Tax Certiorari Proceedings in which a trial on the merits had not commenced in the New York state court before which that proceeding was pending by August 1, 2004, the Bankruptcy Court would stay that state court proceeding and address itself the tax matters at issue in that proceeding. That ruling was incorporated in an order issued by the Bankruptcy Court on January 8, 2004. Certain of the taxing authorities moved for leave to appeal the Bankruptcy Court's January 8, 2004 order on an interlocutory basis to the United States District Court for the Northern District of Texas. On April 30, 2004, the district court denied the motions seeking leave to appeal.

Collectively, the New York Debtors have not paid approximately $62 million assessed by local taxing authorities on the generating facilities for 2003 which fell due on September 30, 2003 and January 30, 2004 in order to preserve their respective rights to offset the overpayments of taxes made in earlier years against the sums payable on account of current taxes. The failure to pay the taxes due on September 30, 2003 and January 30, 2004 could subject the New York Debtors to additional penalties and interest. In the Tax Determination Motion, the Mirant Debtors requested that the Bankruptcy Court permit each of the New York Debtors to apply any previous tax overpayments made on account of their generating facilities as determined by the Bankruptcy Court as requested in the Tax Determination Motion to any post-petition tax liabilities owing to the relevant local taxing authority for current tax liabilities and be entitled to a refund of any remaining overpayments. The Tax Determination Motion also requests the Bankruptcy Court to rule that any interest or penalties that may otherwise be imposed on the New York Debtors by the relevant taxing authorities for failure to timely pay taxes be disallowed or determined to be zero. On February 11, 2004, the County of Rockland, New York, filed a motion with the Bankruptcy Court requesting that it order the New York Debtors to pay all unpaid ad valorem taxes for 2003 assessed by the taxing authorities located in Rockland County and all prospective ad valorem taxes. On March 10, 2004, the Bankruptcy Court denied that motion. The various taxing authorities may seek to lift the bankruptcy stay (which arises automatically upon the filing of a bankruptcy petition and prevents creditors exercising remedies against a debtor) such that they may seek to foreclose their liens against the various generating facilities due to the failure of the applicable entities to pay their current property taxes. In the event that the motion to lift the stay were granted, each of the New York Debtors has the option to pay the unpaid taxes it owes and avoid the result of facing foreclosure of tax liens against its generating facilities.

On July 7, 2004 and July 28, 2004, the New York Debtors entered into settlement agreements with certain of the taxing authorities resolving sixteen Tax Certiorari Proceedings related to the real property tax assessments for Mirant NY-Gen's Hillburn, Swinging Bridge, Mongaup, and Rio generating facilities for the years 2000 through 2003. The New York Debtors have not paid real property taxes on the New York generating facilities for 2003 totaling approximately $62 million. For 2003, these settlements reduce the equalized assessed value of the affected generating facilities significantly, resulting in a reduction in the amount of taxes owed by Mirant NY-Gen to the settling taxing authorities for those facilities from $2.9 million to $0.9 million. These reduced assessed values will also apply to tax years 2004, 2005, and 2006. The settlements also set reduced assessed values for the affected generating facilities for the years 2000 through 2002 that will result in refunds to Mirant NY-Gen totaling $2.4 million. The settlement agreements are subject to the approval of the Bankruptcy Court.

City of Alexandria Potential Zoning Action

On June 22, 2004, the City Council for the City of Alexandria, Virginia adopted a resolution initiating certain zoning ordinance amendments and referring consideration of the amendments to the City Planning Commission for public hearing and consideration. Those amendments, if adopted, could result in the zoning status of Mirant Potomac River's generating plant being changed in a way that could require termination of the operation of the plant within a number of years that would be specified as part of the amendment process. The City Council also authorized institution of enforcement actions that would seek to revoke special use permits applicable to the administrative office space at Mirant Potomac River's plant and the plant's transportation management plan. Revocation of such permits would not materially impact plant production but could impact Mirant Potomac River's ability to obtain new permits for construction activities at the plant. The proceedings before the City Council also referred to the possible institution by the City of Alexandria of a suit against Mirant Potomac River for violation of the Clean Air Act based on the allegations underlying the notices of violation issued by the Virginia Department of Environmental Quality on September 10, 2003 and the EPA on January 22, 2004. Any such suit, however, would require further approval of the City Council before being instituted. The City Council also authorized the City to file an objection to any plan of reorganization that the Mirant Debtors file in the pending Chapter 11 proceedings that includes the continued operation of the Mirant Potomac River plant. Any action by the City Council that results in the termination of operation of the Mirant Potomac River generating plant could have a material adverse effect upon the Company depending upon the timing of such termination.

Other Legal Matters

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position, results of operations or cash flows.

Tax Matters

The Company has contingent liabilities related to taxes arising in the ordinary course of business. The Company periodically assesses its contingent liabilities in connection with these matters based upon the latest information available. For those matters where it is probable that a loss has been incurred and the loss or range of loss can be reasonably estimated, a reserve is recorded on the consolidated financial statements. As additional information becomes available, the assessment and estimates of such liabilities are adjusted accordingly. With respect to other matters, which are considered reasonably possible, but not probable, no accrual has been made. At this time, the Company estimates the possible loss for these matters is up to $32 million, including interest.

I. Commitments and Contingencies

Mirant has made firm commitments to buy materials and services in connection with its ongoing operations and has provided financial guarantees related to some of its investments.

Cash Collateral and Letters of Credit

In order to sell power and purchase fuel in the forward markets and perform other energy trading and marketing activities, the Company is often required to provide trade credit support to its counterparties or make deposits with brokers. In addition, the Company is often required to provide trade credit support for access to the transmission grid, to participate in power pools and other operating activities. Trade credit support includes cash collateral, letters of credit, and financial guarantees. In the event of default by the Company, the counterparty can draw on the letter of credit or apply cash collateral to satisfy the existing amounts outstanding under an open contract. Letters of credit total $475 million as of June 30, 2004, of which $422 million were issued under the pre-petition credit facilities and the remaining $53 million were issued under the DIP facility. Upon expiration in 2004 and 2005, letters of credit may be renewed or replaced with another form of credit support to the counterparty, if required, or under certain circumstances the letters of credit could be drawn down by the counterparty.

Following is a summary of cash collateral posted with counterparties and brokers and letters of credit issued as of June 30, 2004 and December 31, 2003 (in millions):

	June 30, 2004	December 31, 2003
Cash collateral posted energy trading and marketing	$ 511	$ 347
Cash collateral posted other operating activities	35	10
Letters of credit energy trading and marketing	211	270
Letters of credit other operating activities	264	331
Total	$ 1,021	$ 958

Long-Term Service Agreements

As of June 30, 2004, the total estimated commitments for LTSAs associated with turbines installed or in storage were approximately $668 million. These commitments are payable over the term of the respective agreements, which range from ten to twenty years. These agreements have terms that allow for cancellation of the contract at the occurrence of several major events during the term of the contracts. If the Company were to cancel these contracts at mid-term, the estimated commitments for the remaining LTSAs would be reduced. Estimates for future commitments for the long-term service agreements are based on the stated payment terms in the contracts at the time of execution. These payments are subject to an annual inflationary adjustment.

As part of the Chapter 11 process, Mirant rejected its LTSAs and entered into new agreements on June 16, 2004 related to certain of its combustion turbine generation facilities. The new agreements provide more favorable terms, including reduced pricing and increased flexibility to modify terms based upon market conditions. Under the terms of the previous LTSAs, Mirant had prepaid future maintenance services at certain generating facilities. The Company recognized a $33 million charge in reorganization items, net in the unaudited condensed consolidated statement of operations during the three months ended June 30, 2004 for forfeited prepayments and impairments of certain purchased intangible assets related to the previous LTSAs.

Mirant Mid-Atlantic Operating Leases

Mirant Mid-Atlantic leases the Morgantown and Dickerson base load units and associated property through 2034 and 2029, respectively. As of June 30, 2004, the total notional minimum lease payments for the remaining life of the leases was approximately $2.5 billion. Rent expenses associated with the Morgantown and Dickerson operating leases totaled approximately $24 million and $48 million for each of the three and six months ended June 30, 2004 and 2003, respectively.

Mirant Mid-Atlantic continues to make required lease payments and is in the process of reviewing the leases and considering whether to assume, assume and assign, or reject the leases pursuant to Section 365 of the Bankruptcy Code or to otherwise seek a determination of the Bankruptcy Court that the leases should be characterized as indebtedness for the purposes of the bankruptcy. In the event of an assumption or assumption and assignment of the leases, Mirant Mid-Atlantic would need to cure any existing defaults, secure a waiver of any existing defaults from the requisite owner lessors and certificate holders or obtain relief from the Bankruptcy Court with respect to such defaults. In the event of a rejection of the leases, the owner lessors would be entitled to a return of the leased assets and a claim equal to the amount of any unmitigated damages, if any, arising from such rejection, subject to the limitation on allowed claims under Section 502(b)(6) of the Bankruptcy Code, which allowed claim, if any, would be subject to compromise in Mirant Mid-Atlantic's Chapter 11 Case. In the event the Bankruptcy Court characterized the leases as indebtedness for the purposes of the bankruptcy, the treatment of the resulting indebtedness would be addressed in a plan of reorganization of Mirant Mid-Atlantic. The impact of any of these events would be reflected in Mirant's financial statements if and when the events occur.

These leases are part of a leveraged lease transaction. Three series of certificates were issued and sold pursuant to a Rule 144A offering and, subsequently, exchanged for certificates issued pursuant to an exchange offer registered under the Securities Act of 1933 ("Securities Act"). These certificates are interests in pass through trusts that hold the lessor notes issued by the owner lessors. Mirant Mid-Atlantic pays rent to an indenture trustee, who in turn makes payments of principal and interest to the pass through trusts and any remaining balance to the lessors for the benefit of the owner participants. As of August 27, 2003, Mirant Mid-Atlantic has less than 300 holders of record. Therefore, Mirant Mid-Atlantic notified the Securities Exchange Commission that it would no longer be a voluntary reporting entity under the Securities Act of 1934 ("Exchange Act"). Under the terms of the leases, Mirant Mid-Atlantic is required to amend the rent schedule to the leases to reflect an increase in rental payments commensurate with the 0.5% increase in interest on the lessor notes that is payable by the lessors so long as Mirant Mid-Atlantic is not a reporting entity under the Exchange Act. However, the automatic stay of the bankruptcy proceedings prevents the lessors from imposing an increased rent schedule on Mirant Mid-Atlantic for such amounts. If Mirant Mid-Atlantic is ultimately liable for the increased rental payments, the additional rent expense would be approximately $59 million over the remaining terms of the leases. The respective landlords for the leased assets have filed a motion with the Bankruptcy Court seeking to compel Mirant Mid-Atlantic to pay the incremental rent, which motion is being opposed by the Debtors.

As a result of Mirant Mid-Atlantic's bankruptcy filing, a lease event of default has occurred under the leases. The leases provide that, upon a lease event of default, the owner lessors' remedies include terminating the leases and repossessing the leased assets, selling their interests in the leased assets, demanding payment by Mirant Mid-Atlantic of the excess, if any, of termination value over the fair market sales value of the leased assets or the discounted fair market rental value of the leased assets and demanding payment of the termination value mitigated by a sale of the leased assets for the account of Mirant Mid-Atlantic. The termination value for the leases was approximately $1.4 billion at June 30, 2004 and generally decreases over time. The ability of the owner lessors to exercise their remedies under the leases is currently stayed as a result of Mirant Mid-Atlantic's Chapter 11 filing.

J. Power Purchase Agreements, Transition Power Agreements and Other Obligations

As of June 30, 2004, the estimated commitments under the power purchase agreements ("PPAs") with PEPCO were $1.2 billion, based on the total remaining MW commitment at contractual prices. The PPAs are derivative instruments and are recorded on the unaudited condensed consolidated balance sheet in liabilities subject to compromise at fair value, with changes in fair value recorded currently in cost of fuel, electricity and other products. As of June 30, 2004, the fair value of the PPAs was $561 million, of which $83 million would have been classified as current. The Company recognized unrealized gains of $69 million and unrealized losses of $32 million during the three months ended June 30, 2004 and 2003, respectively, and unrealized gains of $147 million and $54 million during the six months ended June 30, 2004 and 2003, respectively, in connection with the PPAs. These gains and losses associated with the PPAs are recorded in cost of fuel, electricity and other products in the unaudited condensed consolidated statements of operations as of June 30, 2004 and 2003, respectively.

As of June 30, 2004, the remaining obligation related to the Company's transition power agreements ("TPAs") with PEPCO, recorded in transition power agreements and other obligations, totaled $121 million, all of which is classified as current. The TPA related to load in Maryland expired in June 2004, while the TPA related to load in the District of Columbia expires in January 2005. As actual MWhs are purchased or sold under these agreements, Mirant amortizes a ratable portion of the obligation as an increase in revenues. The Company recorded, as an adjustment of revenues, amortization of the TPA obligation of approximately $119 million and $92 million during the three months ended June 30, 2004 and 2003, respectively, and $233 million and $216 million during the six months ended June 30, 2004 and 2003, respectively, in generation revenue in the unaudited condensed consolidated statements of operations.

All other transition power agreements and other obligations approximated $12 million at June 30, 2004, of which $4 million is classified in current transition power agreements and other obligations in the unaudited condensed consolidated balance sheet. These obligations relate primarily to acquired out-of-market gas transportation and power sales agreements. During the six months ended June 30, 2004, these obligations were reduced by approximately $28 million due to the Company's sale of its Canadian natural gas transportation contracts and certain natural gas marketing contracts.

K. Earnings (Loss) Per Share

Mirant calculates basic earnings (loss) per share by dividing the income (loss) available to common shareholders by the weighted average number of common shares outstanding. Diluted earnings (loss) per share gives effect to dilutive potential common shares, including stock options convertible notes and debentures and convertible trust preferred securities. The following table shows the computation of

basic and diluted earnings (loss) per share for the three months ended June 30, 2004 and 2003 and for the six months ended June 30, 2004 and 2003 (in millions, except per share data).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Income (loss) from continuing operations	$ 32	$ (2,195)	$ 62	$ (2,180)
Discontinued operations, net of taxes		(7)		(22)
Cumulative effect of changes in accounting principles, net of taxes				(28)
Net income (loss)	$ 32	$ (2,202)	$ 62	$ (2,230)
Basic:				
Weighted average shares outstanding	405.5	405.0	405.5	404.5
Earnings (loss) per share from:				
Continuing operations	$ 0.08	$ (5.42)	$ 0.15	$ (5.39)
Discontinued operations		(0.02)		(0.05)
Cumulative effect of change in accounting principle				(0.07)
Net income (loss)	$ 0.08	$ (5.44)	$ 0.15	$ (5.51)
Diluted:				
Net income (loss)	$ 32	$ (2,202)	$ 62	$ (2,230)
Weighted average shares outstanding	405.5	405.0	405.5	404.5
Shares due to assumed exercise of stock options and equivalents				
Adjusted shares	405.5	405.0	405.5	404.5
Earnings (loss) per share from:				
Continuing operations	$ 0.08	$ (5.42)	$ 0.15	$ (5.39)
Discontinued operations		(0.02)		(0.05)
Cumulative effect of change in accounting principle				(0.07)
Net income (loss)	$ 0.08	$ (5.44)	$ 0.15	$ (5.51)

The following potential common shares were excluded from the earnings per share calculations (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Out-of-the-money options	17.6	16.9	19.1	18.4
Shares issuable upon conversion of convertible debt	58.7	59.8	58.7	59.8
Shares issuable upon conversion of convertible trust preferred securities	12.5	12.5	12.5	12.5
Total	88.8	89.2	90.3	90.7

	Three Months Ended June 30,		Six Months Ended June 30,	

39

L. Segment Reporting

The Company has two reportable segments: North America and International. The North America segment consists of the Company's interrelated power generation and commodity trading operations in the United States and Canada. The International segment includes power generation and distribution operations in the Philippines, power generation operations in Curacao and Trinidad and Tobago and generation, transmission and distribution operations in Jamaica and the Bahamas. The Company's reportable segments are strategic businesses that are geographically separated and managed separately.

In 2003, certain corporate costs were not allocated to a reporting segment. Beginning January 1, 2004, the Company changed its allocation methodology related to corporate overhead expenses to better reflect its operating structure. As a result, substantially all of the operating expenses are now allocated to the Company's North America and International segments. The new methodology allocates costs using several methods but is primarily based on gross margin, property, plant and equipment balances, and labor costs. Our allocation methodology may be subject to further change during the Chapter 11 reorganization process.

Financial Data by Segment
(In Millions)

Three Months Ended June 30, 2004:

	North America	International	Corporate and Eliminations	Consolidated
Operating Revenues by Product and Service:				
Generation	$ 1,004	$ 122	$	$ 1,126
Integrated utilities and distribution		136		136
Net trading revenue	2			2
Total operating revenues	1,006	258		1,264
Cost of fuel, electricity and other products	697	71		768
Gross Margin	309	187		496
Operating Expenses:				
Operations and maintenance	195	71	(15)	251
Depreciation and amortization	41	30	6	77
Impairment losses and restructuring charges	51	1	1	53
Loss on sales of assets, net	1			1
Total operating expenses	288	102	(8)	382
Operating Income	$ 21	$ 85	$ 8	114
Other income, net				11
Income From Continuing Operations Before Reorganization Items and Income Taxes and Minority Interest				125
Reorganization items, net				73
Provision for income taxes				13
Minority interest				7
Income from Continuing Operations				$ 32
Total assets at June 30, 2004	$ 9,033	$ 4,981	$ (2,359)	$ 11,655

	North America	International	Corporate and Eliminations	Consolidated

Six Months Ended June 30, 2004:

	North America	International	Corporate and Eliminations	Consolidated
Operating Revenues by Product and Service:				
Generation	$ 1,919	$ 239	$	$ 2,158
Integrated utilities and distribution		270		270
Net trading revenue	20			20
Total operating revenues	1,939	509		2,448
Cost of fuel, electricity and other products	1,364	137		1,501
Gross Margin	575	372		947
Operating Expenses:				
Operations and maintenance	386	141	(29)	498
Depreciation and amortization	85	61	11	157
Impairment losses and restructuring charges	52	1	2	55
Gain on sales of assets, net	(15)			(15)
Total operating expenses	508	203	(16)	695
Operating Income	$ 67	$ 169	$ 16	252
Other expense, net				(16)
Income From Continuing Operations Before Reorganization Items and Income Taxes and Minority Interest				236
Reorganization items, net				130
Provision for income taxes				32
Minority interest				12
Income from Continuing Operations				$ 62
Total assets at June 30, 2004	$ 9,033	$ 4,981	$ (2,359)	$ 11,655

41

Three Months Ended June 30, 2003:

	North America	International	Corporate and Eliminations	Consolidated
Operating Revenues by Product and Service:				
Generation	$ 1,002	$ 126	$	$ 1,128
Integrated utilities and distribution		127		127
Net trading revenue	(7)			(7)
Total operating revenues	995	253		1,248
Cost of fuel, electricity and other products	750	66		816
Gross Margin	245	187		432
Operating Expenses:				
Operations and maintenance	219	65	54	338
Depreciation and amortization	53	30	6	89
Impairment losses and restructuring charges	2,068	4	4	2,076
Gain on sales of assets, net	(24)	(1)		(25)
Total operating expenses	2,316	98	64	2,478
Operating (Loss) Income	$ (2,071)	$ 89	$ (64)	(2,046)
Other expense, net				(125)
Loss From Continuing Operations Before Income Taxes and Minority Interest				(2,171)
Provision for income taxes				11
Minority interest				13
Loss From Continuing Operations				$ (2,195)
Total assets at December 31, 2003	$ 9,185	$ 4,751	$ (1,663)	$ 12,273

Six Months Ended June 30, 2003:

	North America	International	Corporate and Eliminations	Consolidated
Operating Revenues by Product and Service:				
Generation	$ 2,197	$ 254	$	$ 2,451
Integrated utilities and distribution		256		256
Net trading revenue	39			39
Total operating revenues	2,236	510		2,746
Cost of fuel, electricity and other products	1,656	138		1,794
Gross Margin	580	372		952
Operating Expenses:				
Operations and maintenance	377	119	91	587
Depreciation and amortization	104	60	12	176
Impairment losses and restructuring charges	2,075	8	5	2,088
Gain on sales of assets, net	(25)	(1)		(26)
Total operating expenses	2,531	186	108	2,825
Operating (Loss) Income	$ (1,951)	$ 186	$ (108)	(1,873)
Other expense, net				(247)
Loss From Continuing Operations Before Income Taxes and Minority Interest				(2,120)
Provision for income taxes				32
Minority interest				28
Loss From Continuing Operations				$ (2,180)
Total assets at December 31, 2003	$ 9,185	$ 4,751	$ (1,663)	$ 12,273

43

Item 2. ***Management's Discussion and Analysis of Results of Operations and Financial Condition***

The following discussion should be read in conjunction with Mirant's unaudited condensed consolidated financial statements and the notes thereto, which are included elsewhere in this report.

Executive Summary

Mirant operates as a debtor-in-possession under the jurisdiction of the Bankruptcy Court in accordance with Chapter 11 of the Bankruptcy Code. We continue to believe that the U.S. electricity markets have excess generation capacity and that generation capacity is expected to exceed combined demand levels and reserve generation targets until the 2007 to 2010 time period for most major markets. This market situation has the potential to result in continued narrow fuel to electricity conversion spreads. In this environment, customers typically transact over shorter durations and rely more heavily on spot markets to meet their energy needs, thus making it more difficult to sell our power for longer-term durations and at prices that provide a reasonable return, most notably on our gas-fired units.

In the first six months of 2004, forward commodity prices increased in many U.S. markets. This increased the expected future value of our generation asset portfolio; however, this adversely impacted the fair value of forward power contracts that we use to economically hedge portions of our anticipated North America generation and fuel requirements for the remainder of 2004 and 2005. In addition to recognizing unrealized losses in 2004 related to these contracts, we posted approximately $189 million of cash collateral with counterparties and brokers to support these contracts. Included in this $189 million was $56 million related to pre-petition letters of credit drawn upon by counterparties. From July 1, 2004 to July 23, 2004, approximately $90 million of collateral was returned to us due to changes in energy prices and settlements.

These forward power contracts and other derivative instruments do not currently receive cash flow hedge accounting treatment in our financial statements. Instead, these contracts are reflected in our financial statements at fair value, resulting in volatility in our gross margin. Our unrealized gains and losses for each period reflect changes in fair value of commodity contracts not yet settled and the reversal of unrealized gains and losses recognized in previous periods that settled in the current reporting period.

For the three and six months ended June 30, 2004 and 2003, our gross margin included the following (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Unrealized gains (losses) on PPAs	$ 69	$ (32)	$ 147	$ 54
Net unrealized losses on asset management, optimization and legacy portfolios	(37)	(41)	(81)	(100)
Net unrealized gross margin	32	(73)	66	(46)
TPA amortization	119	92	233	216
Realized gross margin	345	413	648	782
Total gross margin	$ 496	$ 432	$ 947	$ 952

Our financial performance during the three and six months ended June 30, 2004 included the following:

Our gross margin increased by $64 million for the three months ended June 30, 2004 compared to the same period in 2003. This increase reflects $28 million of higher generation gross margin,

44

$9 million of higher net trading revenues and $27 million of higher non-cash revenue related to transition power agreement amortization for the three months ended June 30, 2004.

Our gross margin decreased by $5 million for the six months ended June 30, 2004 compared to the same period in 2003. This decrease reflects $3 million of lower generation gross margin, $19 million of lower net trading revenues and $17 million of higher non-cash revenue related to transition power agreement amortization for the six months ended June 30, 2004.

In March 2004, we completed the sale of our remaining Canadian natural gas transportation contracts and certain natural gas marketing agreements. As part of the sale agreements, we paid approximately $12 million to a third party to assume approximately $28 million of net liabilities. We recognized a gain of approximately $16 million in connection with the sale of these agreements.

In the second quarter of 2004, we began pursuing the sale of one of our generation facilities in North America. This decision to pursue the sale represented a triggering event that required the Company to perform an impairment analysis on that generation facility. As a result of the analysis, we recorded an impairment charge of $48 million for the three and six month periods ended June 30, 2004.

In June 2004, we reflected a gain of $38 million related to the extinguishment of $83 million of our 2.5% convertible debentures due 2021 that were included in liabilities subject to compromise. This gain is reflected in other income (expense), net in the unaudited condensed consolidated statements of operations.

Our interest expense decreased by $135 million and $245 million for the three and six months ended June 30, 2004, respectively, compared to the same periods in 2003. Effective with the Chapter 11 filings, accrual of interest expense associated with the debt of the Mirant Debtors, with the exception of West Georgia, was suspended. Therefore, subsequent to the Petition Date, no interest expense related to those obligations was recorded. Contractual interest on liabilities subject to compromise in excess of reported interest was approximately $134 million and $257 million for the three and six months ended June 30, 2004, respectively.

For the three and six months ended June 30, 2004, we recognized net expenses for reorganization items of $73 million and $130 million, respectively.

For the six months ended June 30, 2004, we used $251 million of cash in our operating activities. This use of cash reflects additional collateral posted to counterparties and brokers of $189 million. Included in this $189 million was $56 million related to pre-petition letters of credit drawn upon by counterparties. Additionally, we paid $57 million for reorganization items.

In March 2004, a minority shareholder of the Sual project exercised its put option. As a result, our Philippines business paid approximately $21 million to acquire an additional 2.94% ownership interest in the Sual project.

Results of Operations

The following discussion of our performance is organized by reportable operating segment, which is consistent with the way we manage our business. Beginning January 1, 2004, we have changed our allocation methodology related to our corporate overhead expenses. As a result, substantially all of our corporate operating expenses are allocated to our North America and International segments. The new methodology allocates costs using several methods but is primarily based on gross margin, property, plant and equipment balances and labor costs. Our allocation methodology may be subject to further change during the Chapter 11 process.

North America

Our North America segment consists primarily of power generation (approximately 14,000 MW of generating capacity) and energy trading and marketing activities managed as a combined business.

The following table summarizes the operations of our North America segment for the three and six months ended June 30, 2004 and 2003 (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
Operating revenues:				
Generation	$ 1,004	$ 1,002	$ 1,919	$ 2,197
Net trading revenues	2	(7)	20	39
Total operating revenue	1,006	995	1,939	2,236
Cost of fuel, electricity and other products	697	750	1,364	1,656
Gross margin	309	245	575	580
Operating expenses:				
Operations and maintenance	195	219	386	377
Depreciation and amortization	41	53	85	104
Impairment losses and restructuring charges	51	2,068	52	2,075
Loss (gain) on sales of assets, net	1	(24)	(15)	(25)
Total operating expenses	288	2,316	508	2,531
Operating income (loss)	$ 21	$ (2,071)	$ 67	$ (1,951)

The following table summarizes gross margin by region in total and as a percentage of total gross margin for our North America segment for the three and six months ended June 30, 2004 and 2003 (in millions):

	Three months ended June 30,				Six months ended June 30,			
	2004		**2003**		**2004**		**2003**	
Mirant Americas Generation:								
Northeast	$ 51	16%	$ 70	29%	$ 101	17%	$ 43	7%
Mid-Atlantic	68	22	86	35	188	33	184	32
West	52	17	49	20	86	15	92	16
Other North America generation	42	14	40	16	76	13	71	12
TPA amortization	119	38	92	38	233	40	216	37
Net trading revenue	2	1	(7)	(3)	20	4	39	7
Other, including TPA and PPA losses	(25)	(8)	(85)	(35)	(129)	(22)	(65)	(11)
Total	$ 309		$ 245		$ 575		$ 580	

Three Months ended June 30, 2004 versus 2003

Gross Margin. Our gross margin increased by $64 million in the three months ended June 30, 2004 compared to the same period for 2003 primarily due to the following:

Northeast operations gross margin decreased $19 million in the three months ended June 30, 2004 compared to the same period in prior year primarily due to unrealized gains and losses on energy derivative contracts being used to hedge future expected generation and fuel requirements. The three months ended June 30, 2003 reflects approximately $32 million in

unrealized gains compared to $7 million in unrealized gains for the three months ended June 30, 2004.

Mid-Atlantic operations gross margin decreased $18 million in the three months ended June 30, 2004 compared to the same period in 2003. This is primarily due to $37 million in unrealized losses on energy derivative contracts being used to economically hedge the future expected generation in the three months ended June 30, 2004. This decrease in fair value of these energy derivative contracts is due to an increase in forward power prices. This is partially offset by a 20% increase in generation volumes and higher power price levels in the three months ended June 30, 2004 compared to the same period in 2003. Finally, in the three months ended June 30, 2003, Mid-Atlantic recognized $9 million higher gross margin in 2003 from fixed prices received under an intercompany capacity and energy agreement with our Mirant Americas Energy Marketing subsidiary than it would have received based on market prices. As a result of the intercompany agreement, approximately $(9) million of Mid-Atlantic gross margin for the three months ended June 30, 2003 is included in other gross margin. This agreement ended on May 1, 2003.

West operations gross margin reflects an increase in generation volumes without a corresponding increase in gross margin because most of our generating units were under reliability-must-run contracts in both periods. Under these contracts, revenues are based on a fixed rate of return on the investment in the generating units and the costs of operating the units.

Non-cash revenue related to the amortization of transition power agreements was $119 million and $92 million for the three months ended June 30, 2004 and 2003, respectively. One of the two transition power agreements ended in June 2004. The second ends in January 2005.

Our net trading revenues increased by $9 million from $(7) million in the three months ended June 30, 2003 to $2 million in same period in 2004. In the three months ended June 30, 2003, we closed significant positions on energy contracts due to uncertainty related to our financial restructuring. Subsequent to our bankruptcy filing, we have concentrated on adjusting our optimization activities to current market conditions.

Other gross margin increased by $60 million. This increase reflects an increase of $101 million in unrealized gains on power purchase agreements. Additionally, $(9) million of gross margin in 2003 reflects power purchased at higher fixed prices under an intercompany capacity and energy agreement with Mirant Mid-Atlantic than was received from the market. As a result, approximately $(9) million of Mid-Atlantic gross margin for the three months ended June 30, 2003 is included in other gross margin. This agreement ended May 1, 2003. Other gross margin also includes our realized losses under the transition power agreements and the realized and unrealized gains and losses under the power purchase agreements with PEPCO.

Operating Expenses. Our operating expenses decreased by $2,028 million in the three months ended June 30, 2004 compared to the same period in 2003. The following factors were responsible for the changes in operating expenses:

Operations and maintenance expense decreased by $24 million in the three months ended June 30, 2004 compared to the same period in 2003. The three months ended June 30, 2003 included bad debt expense of approximately $32 million related to an energy marketing customer. This is offset by a $28 million increase in corporate overhead costs allocated to the segment in the three months ended June 30, 2004. Corporate expenses allocated to the North America segment were $48 million for the three months ended June 30, 2004 compared to $20 million for the same period in 2003. The remaining decrease is primarily related to reduced scope and scale of our energy marketing operations that resulted in a decrease of approximately $12 million in operations and maintenance expense.

Depreciation and amortization expense decreased by $12 million in the three months ended June 30, 2004 compared to the same period in 2003. This decrease was primarily due to lower depreciation expense related to our property, plant and equipment after our $1,566 million impairment of long-lived assets in the fourth quarter of 2003.

Impairment losses and restructuring charges of $51 million in the three months ended June 30, 2004 primarily relates to a charge of $48 million stemming from an impairment charge relating to one of our generation facilities in North America. In June 2003, we recorded an impairment charge of $2,067 million to recognize the full impairment of goodwill of our North America segment.

The gain on sale of assets of $24 million for three months ended June 30, 2003 primarily related to the sale of gas storage contracts in our Canadian trading operations.

Six Months ended June 30, 2004 versus 2003

Gross Margin. Our gross margin decreased by $5 million in the six months ended June 30, 2004 compared to the same period for 2003 primarily due to the following:

Northeast operations gross margin increased $58 million in the six months ended June 30, 2004 compared to the same period in prior year. The significant change is primarily due to 2003 events that did not recur in 2004. Forced outages, transmission line problems, and losses on derivative instruments in the six months ended June 30, 2003 all decreased our 2003 gross margin position. In addition, the six months ended June 30, 2003 reflects approximately $30 million in unrealized losses on derivative instruments compared to $2 million in unrealized gains for the six months ended June 30, 2004.

Mid-Atlantic operations gross margin increased $4 million in the six months ended June 30, 2004 compared to the same period in 2003. There was an increase in prices received from the market compared to the fixed prices received under an intercompany capacity and energy agreement with our Mirant Americas Energy Marketing subsidiary in 2003. As a result of the intercompany agreement, approximately $94 million of Mid-Atlantic gross margin for the six months ended June 30, 2003 is included in other gross margin. This agreement ended May 1, 2003. Excluding the impact of this agreement, Mid-Atlantic operations gross margin would have been lower in the six months ended June 30, 2004 compared to the same period in 2003. This is primarily due to approximately $66 million in unrealized losses in the six months ended June 30, 2004 on power contracts for future periods. These contracts were entered into to economically hedge a portion of the energy price risk faced by the Mid-Atlantic operations.

West operations gross margin reflects an increase in generation volumes without a corresponding increase in gross margin because most of our generating units were under reliability-must-run contracts in both periods. Under these contracts, revenues are based on a fixed rate of return on the investment in the generating units and the units' operating costs of operating the units.

Non-cash revenue related to the amortization of transition power agreements was $233 million and $216 million for the six months ended June 30, 2004 and 2003, respectively. One of the two transition power agreements ended in June 2004. The second ends January in 2005.

Our net trading revenues decreased by $19 million from $39 million in the six months ended June 30, 2003 to $20 million in same period in 2004. In the three months ended June 30, 2003, we closed significant positions on energy contracts due to uncertainty related to our financial restructuring. Subsequent to our bankruptcy filing, we have concentrated on adjusting our optimization activities to current market conditions.

Other gross margin decreased by $64 million. This decrease primarily resulted from $94 million of gross margin in 2003 received from the market for power at higher prices than the fixed prices paid under an intercompany capacity and energy agreement with Mirant Mid-Atlantic. As a result, approximately $94 million of Mid-Atlantic gross margin for the six months ended June 30, 2003 is included in other gross margin. This agreement ended May 1, 2003. Other gross margin also includes our realized losses under the transition power agreements and the realized and unrealized gains and losses under the power purchase agreements with PEPCO.

Operating Expenses. Our operating expenses decreased by $2,023 million in the six months ended June 30, 2004 compared to the same period in 2003. The following factors were responsible for the changes in operating expenses:

Operations and maintenance expense increased by $9 million in the six months ended June 30, 2004 compared to the same period in 2003. The six months ended June 30, 2003 includes bad debt of approximately $32 million related to an energy marketing customer. This is offset by a $55 million increase in corporate overhead costs allocated to the segment in the 2004 period. Corporate expenses allocated to the North America segment were $95 million for the six months ended June 30, 2004 compared to $40 million for the same period in 2003. The remaining decrease is primarily related to reduced scope and scale of our energy marketing operations that resulted in a decrease of approximately $19 million in operations and maintenance expense.

Depreciation and amortization expense decreased by $19 million in the six months ended June 30, 2004 compared to the same period in 2003. This decrease was primarily due to lower depreciation expense related to our property, plant and equipment after our $1,566 million impairment of long-lived assets in the fourth quarter of 2003.

Impairment losses and restructuring charges of $52 million in the six months ended June 30, 2004 primarily relates to a charge of $48 million stemming from an impairment charge relating to one of our generation facilities in North America. In June 2003, we recorded an impairment charge of $2,067 million to recognize the full impairment of goodwill of our North America segment.

Gain on sales of assets of $15 million for the six months ended June 30, 2004 resulted from the sale of the remaining Canadian natural gas transportation contracts and certain natural gas marketing contracts. The gain on sales of assets of $25 million for six months ended June 30, 2003 primarily related to the sale of gas storage contracts in our Canadian trading operations.

International

Our International segment consists of our ownership interest in power generating operations in the Phillippines, Curacao and Trinidad and Tobago and our ownership interest in integrated utilities in Jamaica and the Bahamas. The following table summarizes the operations of our International businesses for the three and six months ended June 30, 2004 and 2003 (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
Operating revenues:				
Generation	$ 122	$ 126	$ 239	$ 254
Integrated utility and distribution	136	127	270	256
Total operating revenues	258	253	509	510
Cost of fuel, electricity and other products	71	66	137	138
Gross Margin	187	187	372	372
Operating expenses:				
Operations and maintenance	71	65	141	119
Depreciation and amortization	30	30	61	60
Impairment losses and restructuring charges	1	4	1	8
Gain on sales of assets, net		(1)		(1)
Total operating expenses	102	98	203	186
Operating income	$ 85	$ 89	$ 169	$ 186

Three Months ended June 30, 2004 versus 2003

Operating Revenue: Our operating revenues increased by $5 million in the three months ended June 30, 2004 compared to the same period in 2003. This increase was primarily caused by higher energy sales, higher fuel prices and regulatory approved increases in non-fuel tariffs at our Jamaica integrated utility in 2004 compared to the same period in 2003. Offsetting this total was a reduction of $4 million related to assets that were no longer owned, operated or consolidated by the Company in 2004 that were included in 2003 results.

Cost of fuel, electricity and other products: The increase of $5 million is primarily driven by higher commodity fuel prices and sales at our Caribbean integrated utilities offset by a decrease in fuel costs related to assets that were no longer owned, operated or consolidated by the Company in 2004 that were included in 2003 results.

Operating Expenses. Our operating expenses increased by $4 million in the three months ended June 30, 2004 compared to the same period in 2003.

Operations and maintenance expense increased by $6 million in the three months ended June 30, 2004 compared to the same period in 2003, primarily as a result of a $9 million increase in corporate overhead costs allocated to the segment. Corporate expenses allocated to the International segment were $11 million for the three months ended June 30, 2004 compared to $2 million for the same period in 2003. Maintenance activity at our Jamaica operations also increased $2 million for the three months ended June 30, 2004 compared the same period in 2003. Offsetting these increases were $3 million related to assets that were no longer owned, operated or consolidated by the Company in 2004 that were included in the 2003 results.

Impairment losses and restructuring charges of $4 million in the three months ended June 30, 2003 was related to withholding tax on Pagbilao pre-acquisition earnings as a result of the exercise of the minority shareholders' put option in 2003.

Six Months ended June 30, 2004 versus 2003

Operating Revenue: Our operating revenues decreased by $1 million in the six months ended June 30, 2004 compared to the same period in 2003. Of this total, $3 million was due to lower nominated capacity from Pagbilao as a result of the implementation of the General Framework Agreement ("GFA"). Additionally, a reduction of $10 million was related to assets that were no longer owned, operated or consolidated by the Company in 2004 that were included in 2003 results. The revenue reductions were offset by higher energy sales, higher fuel prices and regulatory approved increases in non-fuel tariffs at our Jamaica integrated utility in 2004 compared to the same period in 2003.

Cost of fuel, electricity and other products: The decrease of $1 million is primarily driven by higher commodity fuel prices for the year at our Caribbean integrated utilities in 2004 compared to the same period in 2003 offset by a decrease in fuel costs related to assets that were no longer owned, operated or consolidated by the Company in 2004 that were included in 2003 results.

Operating Expenses. Our operating expenses increased by $17 million in the six months ended June 30, 2004 compared to the same period in 2003.

Operations and maintenance expense increased by $22 million in the six months ended June 30, 2004 compared to the same period in 2003, primarily as a result of an $18 million increase in corporate overhead costs allocated to the segment. Corporate expenses allocated to the International segment were $22 million for the six months ended June 30, 2004 compared to $4 million for the same period in 2003. Maintenance activity at our Jamaica operations also increased for 2004 compared to the same period in 2003. Offsetting these increases was $3 million related to assets that were no longer owned, operated, or consolidated by the Company in 2004 that were included in the 2003 results.

Impairment losses and restructuring charges of $8 million in the six months ended June 30, 2003 were related to the severance of employees and other employee termination-related charges combined with withholding tax on Pagbilao pre-acquisition earnings of $4 million as a result of the exercise of the minority shareholders' put option in 2003.

Corporate

The following table summarizes our corporate expenses for the three and six months ended June 30, 2004 and 2003 (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
Operating expenses:				
Operations and maintenance	$ (15)	$ 54	$ (29)	$ 91
Depreciation and amortization	6	6	11	12
Impairment losses and restructuring charges	1	4	2	5
Total operating expenses	$ (8)	$ 64	$ (16)	$ 108

The corporate operating expenses for the three and six months ended June 30, 2004 represent the amount of billings to subsidiaries in excess of costs incurred during this period. This is a result of two

factors. First, we use budgeted costs to determine cost allocations to the operating segments and a one-month lag in allocations to the segment. This represents a timing difference that will be resolved through adjustments to the cost allocation amount in the following period. Second, all cost allocations are reflected in operations and maintenance expense, regardless of the statement of operations classification of the expense incurred by the corporate segment. As a result, depreciation and amortization and other expense items are reflected as reductions of operations and maintenance expense when allocated. This contributes to the negative operations and maintenance expense for the corporate segment but has no impact on the consolidated statements of operations. Before allocations to operating segments, our corporate expenses are in total $35 million and $51 million lower for the three and six months ended, respectively. This decrease is due primarily to restructuring cost cutting efforts.

Other Significant Consolidated Statements of Operations Movements

The following table summarizes our consolidated other income and expenses for the three and six months ended June 30, 2004 and 2003 (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Other (Expense) Income, net:				
Interest expense	$ (33)	$ (168)	$ (66)	$ (311)
Equity in income of affiliates	7	8	13	15
Interest income	2	8	5	17
Other, net	35	27	32	32
Total other income (expense), net	$ 11	$ (125)	$ (16)	$ (247)
Reorganization items, net	$ 73	$	$ 130	$
Provision for income tax	$ 13	$ 11	$ 32	$ 32
Minority interest	$ 7	$ 13	$ 12	$ 28
Loss from discontinued operations, net of tax	$	$ (7)	$	$ (22)
Cumulative effect of changes in accounting principles, net of tax	$	$	$	$ (28)

Three Months ended June 30, 2004 versus 2003

Interest expense. Interest expense decreased by $135 million for the three month period ended June 30, 2004, compared to the same period in 2003. Effective with the Chapter 11 filings, accrual of interest expense associated with the debt of the Mirant Debtors, with the exception of West Georgia, was suspended. Therefore, subsequent to the Petition Date, no interest expense related to those obligations was recorded. Contractual interest on liabilities subject to compromise in excess of reported interest was approximately $134 million for the three months ended June 30, 2004.

Other, net. The unaudited condensed consolidated statements of operations for the three months ended June 30, 2004, reflect a gain of $38 million related to the extinguishment of $83 million of our 2.5% convertible debentures due 2021 that were included in liabilities subject to compromise. For the three months ended June 30, 2003, we had miscellaneous income of $27 million including $11 million related to the sale of certain energy marketing contracts and $11 million of foreign currency gains.

Reorganization items, net. As discussed in Note B to our unaudited condensed consolidated financial statements, reorganization items, net represents expense or income amounts that were recorded in the financial statements as a result of the bankruptcy proceedings. For the three months ended June 30, 2004, this amount includes $33 million related to estimated damage claims on rejected

or amended contracts, $25 million in professional and administrative fees, $33 million of losses on contract amendments for forfeited prepayments and impairments of certain purchased intangible assets related to the previous LTSAs offset by a $7 million gain related to the emergence of the Mirant Canadian subsidiaries from creditor protection and $11 million of gains in other contract settlements.

Provision for Income Taxes. The unaudited condensed consolidated statements of operations for the three months ended June 30, 2004, reflect an income tax provision of $13 million. We currently record a tax provision for foreign income taxes as appropriate but record no tax benefit for losses for federal and state income tax purposes.

Discontinued Operations. The $7 million loss from discontinued operations for the three months ended June 30, 2003 reflected the financial results of the following entities that were disposed of in 2003: Mirant Europe B.V., the Neenah generating facility in Wisconsin, the Tanguisson power plant in Guam and investments held by Mirant Americas Energy Capital, LP and Mirant Canada Energy Capital.

Six Months ended June 30, 2004 versus 2003

Interest expense. Interest expense decreased by $245 million for the six month period ended June 30, 2004, compared to the same period in 2003. Effective with the Chapter 11 filings, accrual of interest expense associated with the debt of the Mirant Debtors, with the exception of West Georgia, was suspended. Therefore, subsequent to the Petition Date, no interest expense related to those obligations was recorded. Contractual interest on liabilities subject to compromise in excess of reported interest was approximately $257 million for the six months ended June 30, 2004.

Reorganization items, net. As discussed in Note B to our unaudited condensed consolidated financial statements, reorganization items, net represents expense or income amounts that were recorded in the financial statements as a result of the bankruptcy proceedings. For the six months ended June 30, 2004, this amount includes $79 million related to estimated damage claims on rejected or amended contracts, $47 million in professional and administrative fees, $33 million of losses on contract amendments related to the prepaid balances and intangible assets on the previous LTSAs, offset by an $11 million gain on the amended corporate headquarters lease agreement and a $7 million gain related to the emergence of the Mirant Canadian subsidiaries from creditor protection.

Other, net. The unaudited condensed consolidated statements of operations for the six months ended June 30, 2004, reflect a gain of $38 million related to the extinguishment of $83 million of our 2.5% convertible debentures due 2021 that were included in liabilities subject to compromise. For the six months ended June 30, 2003, we had miscellaneous income of $32 million including $11 million related to the sale of certain energy marketing contracts and $9 million of foreign currency gains.

Provision for Income Taxes. The unaudited condensed consolidated statements of operations for the six months ended June 30, 2004, reflect an income tax provision of $32 million. We currently record a tax provision for foreign income taxes as appropriate but record no tax benefit for losses for federal and state income tax purposes.

Discontinued Operations. The $22 million loss from discontinued operations for the six months ended June 30, 2003 reflected the financial results of the following entities that were disposed of in 2003: Mirant Europe B.V., the Neenah generating facility in Wisconsin, the Tanguisson power plant in Guam and investments held by Mirant Americas Energy Capital, LP and Mirant Canada Energy Capital.

Cumulative Effect of Changes in Accounting Principles. As a result of the consensus on EITF Issue 02-03, all non-derivative energy trading contracts as of January 1, 2003 that existed on October 25, 2002 have been adjusted to historical cost resulting in a cumulative effect adjustment of $25 million, net of

tax, which was recorded in the first quarter of 2003. Certain of these contracts were reclassified from price risk management liabilities to transition power agreements and other obligations on our consolidated balance sheets. We also adopted SFAS No. 143 effective January 1, 2003 and recognized an after-tax charge of $3 million associated with its implementation.

Financial Condition

Liquidity and Capital Resources

The matters described in this section relate to future events or expectations and may be significantly affected by the Chapter 11 filings. The Chapter 11 filings will involve, or may result in, various restrictions on the Company's activities, limitations on financing, the need to obtain Bankruptcy Court approval for various matters, and uncertainty as to relationships with vendors, suppliers, customers and others with whom the Company may conduct or seek to conduct business.

During the pendency of the Chapter 11 proceedings, Mirant and certain of its subsidiaries, including Mirant Americas Generation and Mirant Mid-Atlantic, are participating in an intercompany cash management program approved by the Bankruptcy Court pursuant to which cash balances at Mirant and the participating subsidiaries are transferred to central concentration accounts and, if necessary, lent to Mirant or any participating subsidiary to fund working capital and other needs, subject to the intercompany borrowing limits approved by the Bankruptcy Court. All intercompany transfers by such Mirant entities are recorded as intercompany loans which are secured by liens (such liens are junior to the liens of the DIP lenders) on the assets of the relevant borrowing group. Upon entering into the debtor-in-possession credit facility, the cash balances of the participating Mirant Debtors became subject to security interests in favor of the debtor-in-possession lenders and, upon certain conditions, such cash balances are swept into concentration accounts controlled by the debtor-in-possession lenders.

Under the existing cash management program, Mirant Americas Energy Marketing has limited access to liquidity and capital. However, the activities of Mirant Americas Energy Marketing require access to substantial liquidity, due in part to commitments under the Back-to-Back Agreement, collateral and settlement requirements in connection with its legacy portfolio of transactions and asset management activities for the Company's generation assets, including the generation assets of Mirant Americas Generation and Mirant Mid-Atlantic. To the extent that they are out-of-the market at the time of payment or settlement, the commitments under the Back-to Back Agreement and the settlement of the legacy portfolio transactions represent permanent reductions to the liquidity of Mirant Americas Energy Marketing. Although Mirant Americas Energy Marketing charges Mirant Americas Generation and Mirant Mid-Atlantic a fee for collateral posted in connection with asset management activities for their benefit, cash held by Mirant Americas Generation and Mirant Mid-Atlantic is presently not fully available as a source of liquidity for Mirant Americas Energy Marketing. The primary sources of liquidity for Mirant Americas Energy Marketing are its existing cash balances, intercompany borrowings, repayments by Mirant Corporation of an existing intercompany loan, and borrowings under the DIP Facility. The Bankruptcy Court has limited intercompany borrowing by Mirant Americas Energy Marketing to $100 million and, with respect to borrowings from Mirant Americas Generation and Mirant Mid-Atlantic, to the balance of the intercompany loan from Mirant Americas Energy Marketing to Mirant Corporation and usage under the DIP Facility by Mirant Americas Energy Marketing and Mirant Corporation to $200 million. As of June 30, 2004, Mirant Americas Energy Marketing has available liquidity of approximately $315 million. For the six months ended June 30, 2004, the Company has posted $189 million of cash collateral with counterparties or deposits with brokers primarily to support asset management activities. Included in this $189 million was $56 million related to pre-petition letters of credit drawn upon by counterparties. In the event the Company determines it is appropriate, it will petition the Bankruptcy Court to amend the existing inter-company borrowing limits to permit Mirant Americas Energy Marketing to borrow from Mirant

Americas Generation and Mirant Mid-Atlantic to fund collateral posted by Mirant Americas Energy Marketing in connection with asset management activities for their benefit.

Cash Flows

We used $175 million less cash in our operating activities in the six months ended June 30, 2004 compared to the same period in 2003. During the six months ended June 30, 2004, working capital changes, which are reflected as changes in operating assets and liabilities, required $315 million in cash compared to $373 million of cash required by changes in working capital during the same period in 2003. This was primarily due to the following:

Posting additional cash collateral to counterparties and brokers of $189 million in the six months ended June 30, 2004 compared to posting $127 million in the same period 2003.

Return of $14 million of collateral from counterparties in the six months ended June 30, 2004, compared to the return of $125 million from counterparties in the same period in 2003.

Net cash provided by operating activities excluding the effects of working capital was $64 million in the six months ended June 30, 2004 compared to net cash used of $53 million in the same period in 2003.

Gross margin excluding unrealized gains and losses and the non-cash revenue related to the TPA amortization decreased $134 million for the six months ended June 30, 2004 to $648 million from $782 million in the same period of 2003.

Excluding a 2003 bad debt expense of $32 million, operating and maintenance expenses decreased by $57 million in the six months ended June 30, 2004 compared to the same period of 2003.

Cash paid for interest for the six months ended June 30, 2004 decreased to $55 million from $308 million for the same period in 2003 due to our Chapter 11 filings.

In the six months ended June 30, 2004 we paid $57 million for reorganization items associated with the Chapter 11 filings.

Net cash used in investing activities was $89 million for the six months ended June 30, 2004. This compares to $105 million of cash used in investing activities for the six months ended June 30, 2003. For the six months ended June 30, 2004, we had capital expenditures of $60 million compared to capital expenditures of $401 million in 2003, which includes $124 million related to the cancellation of turbine contracts in Europe offset by proceeds from the sale of assets of $288 million during the six months ended June 30, 2003. During the six months ended June 30, 2004, our Philippines business paid $21 million to acquire an additional interest in the Sual project after a minority shareholder exercised its put option. During the six months ended June 30, 2003, we paid $59 million to acquire additional interests in the Pagbilao project after minority shareholders exercised their put options. We also paid $12 million to a third party to exit our Canadian natural gas transportation agreements and certain natural gas marketing contracts during the six months ended June 30, 2004. During the six months ended June 30, 2003, we received $288 million in proceeds from the sale of our Neenah generating facility, Mirant Americas Energy Capital investments and the Tanguisson power plant in Guam.

Net cash provided by financing activities was $25 million during the six months ended June 30, 2004 compared to cash used in financing activities of $154 million during the same period of 2003. This change is primarily due to $101 million of letters of credit being drawn upon by counterparties during the six months ended June 30, 2004. As a result, this $101 million increase in cash provided by financing is offset by an increase in the cash used in operations for working capital purposes as a portion was used to settle accounts payable and the remainder represents an increase to amounts posted as collateral with counterparties and on deposit with brokers. Cash provided by financing activities in the six months ended June 30, 2004 reflects repayments of long-term debt of $101 million

primarily related to our Asia operations of $80 million and Jamaica operations of $17 million. In the six months ended June 30, 2003, we repaid debt of $200 million and purchased $51 million of TIERS certificates.

Total Cash, Cash Equivalents and Credit Facility Availability

The table below sets forth total cash, cash equivalents and availability under the DIP Facility of Mirant Corporation and its subsidiaries as of June 30, 2004, and December 31, 2003 (in millions):

	June 30, 2004	December 31, 2003
Cash and Cash Equivalents:		
Debtors:		
Mirant Corporation	$ 307	$ 467
Mirant Americas Generation(1)	101	115
Mirant Mid-Atlantic(1)	232	209
Mirant Americas Energy Marketing	41	161
Other subsidiaries	58	125
Total debtors cash and cash equivalents	739	1,077
Non-debtors	535	512
Total cash and cash equivalents	1,274	1,589
Less: Cash required for operating, working capital or other purposes or restricted by the subsidiaries' debt agreements(2)	288	354
Total available cash and cash equivalents	986	1,235
Available under DIP Facility	247	279
Total cash, cash equivalents and credit facilities availability	$ 1,233	$ 1,514

(1) Since filing for protection under Chapter 11, none of the debtors have made dividends or capital contributions. As discussed above, Mirant and certain of its subsidiaries, including Mirant Americas Generation and Mirant Mid-Atlantic, are participating in an intercompany cash management program approved by the Bankruptcy Court.

(2) Amounts designated as "Cash required for operating working capital or other purposes or restricted by the subsidiaries' debt agreements" are estimated amounts. In addition, as of December 31, 2003, such amounts include $92 million held by certain Canadian subsidiaries that are subject to protection under the CCAA in Canada.

Other Developments

In August 2003, we unilaterally implemented the "Terms and Conditions of Employment" that reflect a final proposed labor agreement at our Mirant Mid-Atlantic plants in Maryland and Virginia. We formally reinitiated negotiations with the IBEW Local 1900 which represents employees at our Mirant Mid-Atlantic plants in May 2004 in an effort to reach a ratified collective bargaining agreement. If we are unsuccessful in reaching a new labor agreement, there is a risk that there could be a strike or some other form of adverse collective action by the union. If a strike does occur, there is a risk that such action could disrupt the ability of the affected plants to produce and/or distribute energy.

We reached a new labor agreement with unions at our Trinidad plants in April 2004. The terms of the new agreement are effective from January 1, 2003 through December 31, 2005.

On April 1, 2004, Mirant Kendall, LLC ("Mirant Kendall") applied to the Independent System Operator of New England ("ISO New England") to deactivate, as of October 1, 2004, a combustion turbine and three steam generation units located in Cambridge Massachusetts due to Mirant Kendall's determination that the units do not produce sufficient revenues under current market conditions to justify their continued operation at this time. On June 10, 2004, Mirant Kendall made a similar filing to deactivate its Kendall Jet #1 and to retire Kendall Jet #2. On June 25, 2004, the ISO New England did not approve Mirant Kendall's application to deactivate the three steam generation units, stating that two of the three steam generation units are needed to mitigate risk to the Kendall Substation area load, and only one of the steam generation units may be deactivated on October 1, 2004. On July 13, 2004, ISO New England determined that the deactivation of the combustion turbine will not have a significant effect upon the reliability or operating characteristics of the ISO New England's transmission system and Mirant Kendall may continue with its plan to deactivate the combustion turbine on October 1, 2004. On July 27, 2004, the ISO New England did not approve Mirant Kendall's application to deactivate Jet #1 stating that such deactivation would have a significant adverse effect on the reliability of the New England Power Pool system or of the systems of one or more other participants; namely the Kendall Substation area load. As with the July 13, 2004 rejection of the deactivation of two of the three steam generation units, Mirant must negotiate in good faith with the ISO New England regarding an agreement to avoid any adverse effect resulting from the deactivation of Jet #1. On July 27, 2004, the ISO New England determined that the deactivation of Jet #2 will not have a significant effect upon the reliability or operating characteristics of the ISO New England's transmission system or on the system of any other participant and Mirant Kendall may continue with its plan to deactivate Jet #2 on October 1, 2004.

The Office of Utilities Regulation has approved a rate case to set rates for our Jamaica operations for the five years beginning June 2004 with interim adjustments indexed to inflation and foreign exchange rate movements. The new rates will result in an average increase of between 3% to 12% for customers, depending on their rate category.

Critical Accounting Policies and Estimates

The accounting policies described below are considered critical to obtaining an understanding of our consolidated financial statements because their application requires significant estimates and judgments by management in preparing our consolidated financial statements. Management's estimates and judgments are inherently uncertain and may differ significantly from actual results achieved. We believe that the following critical accounting policies and the underlying estimates and judgments involve a higher degree of complexity than others. We discussed the selection of and application of these accounting policies with the Audit Committee of the Board of Directors.

Accounting for Commodity Trading and Marketing Activities

Our North America businesses use derivatives and other contracts to manage our power generation assets and to engage in optimization trading activities. We use a variety of derivative contracts, such as futures, swaps and option contracts, in the management of our business. Such derivative contracts have varying terms and durations, or tenors, which range from a few days to a number of years, depending on the instrument.

We classify certain derivatives or energy contracts into the following categories asset management, optimization and legacy. All derivative instruments are reflected in our financial statements at fair value, with changes in fair value recognized currently in earnings, except for a limited number of transactions which qualify for use of accrual accounting. Also, certain derivative contracts are entered into under master netting agreements that provide us with legal right of offset in the event of default by the counterparty and are, therefore, reported net in our consolidated balance sheets.

The fair value amounts contained within our consolidated financial statements are estimates based largely on quoted market prices or, if no active market exists, quantitative pricing models. We estimate the fair value of certain derivative contracts using our pricing models based on contracts with similar terms and risks. Our modeling techniques assume market correlation and volatility, such as using the prices of one delivery point to calculate the price of the contract's delivery point. The nominal value of the transaction is also discounted using a London InterBank Offered Rate ("LIBOR") based forward interest rate curve. In addition, the fair value of our derivative contracts reflects the risk that the counterparties to these contracts may default on their obligations. The degree of complexity of our pricing models increases for longer duration contracts, contracts with multiple pricing features and off-hub delivery points. The amounts recorded as revenue change as estimates are revised to reflect actual results and changes in market conditions or other factors, many of which are beyond our control.

Non-derivative energy-related contracts such as transportation contracts, storage contracts and tolling agreements, are required to be accounted for as executory contracts using the accrual method of accounting and not fair value.

Because we use derivatives, our financial statements including gross margin, operating income, balance sheet ratios and cash flow are, at times, volatile and subject to fluctuations in value due to changes in commodity prices. These fluctuations include changes in fair value of derivative contracts and changes to working capital due to collateral requirements to support open derivative positions. The largest of our derivative instruments are the PEPCO PPAs. We expect continued changes in fair value over the terms of the contracts, the longest of which extends to 2021.

Bankruptcy Claims Assessment

Our unaudited condensed consolidated financial statements include, as liabilities subject to compromise, the pre-petition liabilities recorded on our consolidated balance sheet at the time of our bankruptcy filing with the exception of the settlements approved by the Bankruptcy Court prior to June 30, 2004. In addition, we also reflect as liabilities subject to compromise the probable claim amount relating to liabilities for rejected contracts, litigation, accounts payable and accrued liabilities, debt and other. The probable claims estimate included in our June 30, 2004 consolidated financial statements is approximately $175 million. These probable claims require management to estimate the likely claim amount that will be allowed by the Bankruptcy Court prior to the Bankruptcy Court's ruling on the individual claims. These estimates are based on assumptions of future commodity prices, reviews of claimants' supporting material and assessments by management and outside experts. We expect that our estimates, although based on the best available information, will change, as the claims are resolved in the Bankruptcy Court.

The following table summarizes the proofs of claim filed in our Chapter 11 case as of June 30, 2004:

	Total number of Claims	Total Claims Exposure (in millions)
Total claims filed	7,957	$ 242,991
Less:		
Redundant claims	5,874	227,144
Claims with basis for objection	38	1,643
Total claims	2,045	14,204
Additional scheduled liabilities		35
Total claims exposure		$ 14,239

The amount of the proofs of claim net of redundancies and amounts for which we have identified a basis for objection totals approximately $14 billion, as summarized above. This amount plus approximately $2 billion of estimated liabilities for which claims have not been filed represents the total estimate of current claims exposure against the Mirant Debtors as of June 30, 2004. Of the $16 billion we have approximately $9 billion recorded as liabilities subject to compromise on our unaudited condensed balance sheet as of June 30, 2004. The most significant components of the $7 billion difference between the net claims exposure and the amount recorded as liabilities subject to compromise relate to litigation and rejected contract claims.

Long-Lived Assets

We evaluate our long-lived assets (property, plant and equipment) and definite-lived intangibles for impairment whenever indicators of impairment exist or when we commit to sell the asset. The accounting standards require that if the sum of the undiscounted expected future cash flows from a long-lived asset or definite-lived intangible is less than the carrying value of that asset, an asset impairment charge must be recognized. The amount of the impairment charge is calculated as the excess of the asset's carrying value over its fair value, which generally represents the discounted future cash flows from that asset or in the case of assets we expect to sell, at fair value less costs to sell.

The accounting estimates related to determining the fair value of long-lived assets require management to make assumptions about future revenues, operating costs and forward commodity prices over the life of the assets. Our assumptions about future revenues, costs and forward prices require significant judgment because such factors have fluctuated in the past and will continue to do so in the future.

Goodwill and Indefinite-lived Intangible Assets

We evaluate our goodwill and indefinite-lived intangible assets for impairment at least annually and periodically if indicators of impairment are present. An impairment occurs when the fair value of a reporting unit is less than its carrying value including goodwill (Step I). For this test our reporting units are North America, Asia and Caribbean. The amount of the impairment charge, if impairment exists, is calculated as the difference between the implied fair value of the reporting unit goodwill and its carrying value (Step II). We perform our annual assessment of goodwill at October 31 and whenever contrary evidence exists as to the recoverability of goodwill.

The accounting estimates related to determining the fair value of goodwill require management to make assumptions about future revenues, operating costs and forward commodity prices over the life of the assets. Our assumptions about future revenues, costs and forward prices require significant judgment because such factors have fluctuated in the past and will continue to do so in the future.

Litigation

We are currently involved in certain legal proceedings. These legal proceedings are discussed in Part II, Item 1, "Legal Proceedings" and Note H to the unaudited condensed consolidated financial statements contained elsewhere in this report. We estimate the range of liability through discussions with applicable legal counsel and analysis of case law and legal precedents. We record our best estimate of a loss, if estimable, when the loss is considered probable, or the low end of our range if no estimate is better than another estimate within a range of estimates. As additional information becomes available, we reassess the potential liability related to our pending litigation and revise our estimates. Revisions in our estimates of the potential liability could materially impact our results of operations, and the ultimate resolution may be materially different from the estimates that we make.

Item 3. ***Quantitative and Qualitative Disclosures about Market Risk***

We are exposed to market risks associated with commodity prices, foreign currency exchange rates and interest rates. We are also exposed to counterparty credit risk. Prior to the Petition Date, the Mirant Debtors were also exposed to market risks associated with interest rates on debt that is now classified as liabilities subject to compromise.

Commodity Price Risk

In connection with our power generating business in North America, we are exposed to energy commodity price risk associated with the electricity we produce and sell, as well as the acquisition of fuel consumed to generate electricity. A portion of the electricity we produce is sold in the spot market and a portion of our fuel requirements are also purchased in the spot market. In addition, the open positions in our asset management, optimization and legacy portfolio activities also expose us to changes in energy commodity prices. As a result, our financial performance in North America varies depending on changes in the prices of commodities. See "Critical Accounting Policies and Estimates" for the accounting treatment for optimization trading and asset management activities.

The financial performance of our power generating business is influenced by the difference between the cost of converting source fuel, such as natural gas or coal, into electricity, and the revenue we receive from the sale of that electricity. The difference between the cost of a specific fuel used to generate one megawatt hour of electricity and the market value of the electricity generated is commonly referred to as the "spark spread." Absent the impacts of our asset management activities, the operating margins that we realize are equal to the difference between the spark spread and the cost of operating the plants that produce the electricity sold.

Spark spreads are dependent on a variety of factors that influence the cost of fuel and the sales price of the electricity generated over the longer-term, including additional plant capacity in the regions in which we operate, plant outages, weather and general economic conditions. As a result of these influences, the cost of fuel and electricity prices do not always change by the same magnitude or direction, which results in spark spreads widening or narrowing.

Through our asset management activities, we enter into a variety of exchange-traded and over the counter ("OTC") energy and energy-related derivative contracts, such as forward contracts, futures contracts, option contracts and financial swap agreements to manage our exposure to commodity price risk and changes in spark spreads. These derivatives have varying terms and durations, or tenors, which range from a few days to a number of years, depending on the instrument. Our optimization trading activities also utilize similar contracts in markets where we have a physical presence to attempt to generate incremental gross margin. In addition, our legacy portfolio consists of a variety of energy and energy-related derivative and non-derivative contracts that have been determined to be no longer consistent with our asset management or optimization trading strategies.

Energy contracts required to be reflected at fair value are presented as price risk management assets and liabilities in the accompanying consolidated balance sheets. The net changes in their market values are recognized in income in the period of change. The fair value of the PEPCO PPAs related to our power purchase contracts which we account for as derivatives are included in liabilities subject to compromise on the accompanying consolidated balance sheet as of June 30, 2004 and December 31, 2003 due to our attempts to reject the agreements which are currently the subject of litigation.

The volumetric weighted average maturity, or weighted average tenor, of the North American portfolio at June 30, 2004 was approximately 1 year. The net notional amount of the price risk management assets and liabilities at June 30, 2004 was a net short position of approximately 24 million equivalent MWhs.

The following table provides a summary of the factors impacting the change in net fair value of the price risk management asset and liability accounts during the three months ended June 30, 2004 (in millions).

	Optimization	Asset Management	Legacy	Total
Net fair value of portfolio at December 31, 2003	$ 30	$ 16	$ (54)	$ (8)
(Losses) gains recognized in the period, net	(3)	(122)	13	(112)
Contracts settled during the period, net	(11)	15	25	29
Other changes in fair value, net	2			2
Net fair value of portfolio at June 30, 2004	$ 18	$ (91)	$ (16)	$ (89)

The decrease in the net fair value of price risk management assets and liabilities related to our asset management activities relates primarily to 2004 and 2005 forward power contracts that, due to higher prices, resulted in unrealized losses for the three and six months ended June 30, 2004. These contracts are primarily being used to economically hedge the gross margin of our Mid-Atlantic operations.

The fair values of our price risk management assets and liabilities, net of credit reserves, as of June 30, 2004 are included in the following table (in millions).

	Net Price Risk Management Assets/(Liabilities)		
	Price Risk Management Assets Value at June 30, 2004	Price Risk Management Liabilities Value at June 30, 2004	Net Value at June 30, 2004
Electricity	$ 159	$ (287)	$ (128)
Natural gas	82	(76)	6
Crude oil	37	(6)	31
Other	4	(2)	2
Total	$ 282	$ (371)	$ (89)

The following table represents the net price risk management assets and liabilities by tenor (in millions):

	Net Price Risk Management Assets/(Liabilities) As of June 30, 2004
2004	$ (63)
2005	(73)
2006	11
2007	10
2008	9
Thereafter	17
Net liabilities	$ (89)

Value at Risk

We continue to use VaR to summarize in dollar terms the market price risk we have and the potential loss in value of portions of our optimization portfolio due to adverse market movement over a defined time horizon within a specified confidence interval. The average VaR related to our optimization activities, using various assumed holding periods and a 95% confidence interval, was $1.7 million for the six months ended June 30, 2004 and the VaR as of June 30, 2004 was $1.3 million.

61

Effective November 5, 2003, we amended our Risk Management Policy to prohibit the trading of certain products (e.g., natural gas liquids and pulp and paper) and to change or clarify limits related to our asset management and optimization trading. As part of this amendment, we established a new VaR limit with respect to our optimization trading activities of $7.5 million. There is now no VaR limit with respect to our asset management activities, as these activities are only allowable if they reduce the commodity price exposure of our generation assets. We manage the market risks associated with our asset management activities in conjunction with the physical generation assets that they are designed to hedge. As a result, commencing in 2004, our asset management portfolio is no longer included in our VaR calculation for purposes of compliance with our Risk Management Policy.

We manage the risk associated with asset management activities through a variety of methods. To ensure that hedge positions are risk reducing in nature, the Company measures the impact of each asset management transaction executed relative to the overall asset position, including previously executed hedge transactions, that it is designed to hedge. See "Critical Accounting Policies and Estimates" for accounting treatment for asset management and optimization trading activities.

Credit Risk

Credit risk represents the loss that we would incur if counterparty fails to perform under its contractual obligations. We monitor credit concentration risk on both an individual basis and a group counterparty basis. The table below summarizes credit exposures by rating category as of June 30, 2004 (in millions, except percentages).

Credit Rating	Exposure	Collateral Held	Net Exposure	% of Net Exposure
AA/Aa2	$ 16	$	$ 16	8%
A/A2	75		75	38
BBB/Baa2	100	26	74	38
BB/Ba2 or lower	50	21	29	15
Unrated	16	10	6	3
Less credit reserves			(4)	(2)
Total	$ 257	$ 57	$ 196	100%

62

Item 4. ***Controls and Procedures***

As disclosed in previous filings, during 2002, our independent auditors identified a material control weakness related primarily to our North America energy marketing operations. Additionally, since 2002, we have identified various reportable conditions related to our structure of internal control over financial reporting. In order to address the above noted material weakness and reportable conditions, the Company implemented various procedures to mitigate the possibility of material error affecting the financial reporting process.

We believe that all identified internal control deficiencies were mitigated in preparing this quarterly report.

As required by Exchange Act Rule 13a-15(b), the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including its Chief Executive Officer and its Chief Financial Officer, of the effectiveness of the design and operation of its disclosure controls and procedures (as defined by Rules 13a-15(e) and 15d-15(e) under the Exchange Act), as of the end of the period covered by this report. Appearing as exhibits to this quarterly report are the certifications of the Chief Executive Officer and the Chief Financial Officer required in accordance with Section 302 of the Sarbanes-Oxley Act of 2002. This Item 4 Controls and Procedures contains the information concerning the evaluation of the Company's disclosure controls and procedures referred to in paragraph 4(b) and (c) of the certifications and this information should be read in conjunction with the certifications for a more complete understanding of the topics presented. Based upon the evaluation, and subject to the limitations noted below, the Chief Executive Officer and the Chief Financial Officer have concluded that, as of the end of the period covered by this report, the design and operation of these disclosure controls and procedures were effective in timely alerting the Company's management to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic SEC filings.

The Company's management, including the Chief Executive Officer and Chief Financial Officer, does not expect that the Company's disclosure controls and procedures, or its internal control over financial reporting, will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. The Chief Executive Officer and Chief Financial Officer nevertheless have reasonable assurance as to the effectiveness of the Company's disclosure controls and procedures.

PART II

Item 1. *Legal Proceedings*

The descriptions below update and should be read in conjunction with the complete descriptions in the section titled "Legal Proceedings" in the Company's Form 10-K for the period ended December 31, 2003 and Form 10-Q for the quarter ended March 31, 2004.

California Attorney General Litigation: On July 6, 2004, the United States Court of Appeals for the Ninth Circuit upheld the dismissal by the United States District Court for the Northern District of California of the civil suit filed on March 11, 2002 by the California Attorney General against Mirant and several of its wholly-owned subsidiaries. The lawsuit alleged that between 1998 and 2001 the companies effectively double-sold their capacity by selling both ancillary services and energy from the same generating units, such that if called upon, the companies would have been unable to perform their contingent obligations under the ancillary services contracts. The court of appeals ruled that the California Attorney General's claims under California's Unfair Competition Act are barred by the doctrine of preemption and the filed rate doctrine, finding that the remedies sought would interfere with the FERC's exclusive authority to set wholesale electric rates under the Federal Power Act.

ERISA Litigation: On June 14, 2004, the plaintiffs filed a motion seeking to amend their consolidated complaint to add as defendants Mirant Services, LLC and its board of managers. Mirant is opposing that request.

PEPCO Back-to-Back Agreement: In connection with Mirant's acquisition of the Mirant Mid-Atlantic assets from Potomac Electric Power Company ("PEPCO") in 2000, PEPCO granted Mirant certain rights to purchase from PEPCO all power it received under long-term power purchase agreements with Ohio Edison Company and Panda-Brandywine L.P. ("Panda") that expire in 2005 and 2021, respectively. Mirant and PEPCO entered into a contractual arrangement (the "Back-to-Back Agreement") with respect to PEPCO's agreements with Panda and Ohio Edison under which (1) PEPCO agreed to resell to Mirant all "capacity, energy, ancillary services and other benefits" to which it is entitled under those agreements; and (2) Mirant agreed to pay PEPCO each month all amounts due from PEPCO to Panda or Ohio Edison for the immediately preceding month associated with such capacity, energy, ancillary services and other benefits. Under this agreement, Mirant is obligated to purchase power from PEPCO in the Pennsylvania-New Jersey-Maryland Interconnection LLC ("PJM") marketplace at prices that are significantly higher than existing market prices for power. On August 28, 2003, the Mirant Debtors filed a motion with the Bankruptcy Court to reject the Back-to-Back Agreement. The Mirant Debtors forecast that it would cost the Mirant Debtors in excess of $300 million during 2004 and 2005 if the Back-to-Back Agreement were to remain in effect. These anticipated losses, as compared to what could be obtained if market rates were applied, are even greater over the entire life of the agreement, which continues until 2021.

In their August 28, 2003 motion, the Mirant Debtors also requested that the Bankruptcy Court enjoin the FERC from compelling the Mirant Debtors to perform under the Back-to-Back Agreement. On August 28, 2003, the Bankruptcy Court entered a temporary restraining order ("TRO") against PEPCO and the FERC. On September 8, 2003, the Office of the People's Counsel for the District of Columbia filed a complaint with the FERC seeking an order holding that the terms of the Back-to-Back Agreement may not be modified or terminated without the approval of the FERC. Also on September 8, 2003, the Public Service Commission of Maryland and the Maryland Office of People's Counsel filed a petition with the FERC seeking an order declaring that Mirant must continue to perform pursuant to the Back-to-Back Agreement with PEPCO. These filings by the Office of the People's Counsel for the District of Columbia, the Public Service Commission of Maryland and the Maryland Office of People's Counsel were withdrawn in February 2004. On September 17, 2003, the Bankruptcy Court entered an order extending the TRO and enjoining the FERC from issuing the

orders requested by such administrative petitions filed with the FERC. On September 25, 2003, the Bankruptcy Court converted the TRO to a preliminary injunction. On October 9, 2003, the United States District Court for the Northern District of Texas entered an order that had the effect of transferring to that court from the Bankruptcy Court the motion filed by the Mirant Debtors seeking to reject the Back-to-Back Agreement and the proceedings in which the Bankruptcy Court had issued the preliminary injunction against the FERC.

On December 23, 2003, the United States District Court for the Northern District of Texas denied the Mirant Debtors' motion seeking to reject the Back-to-Back Agreement. The District Court ruled that the Federal Power Act preempts the Bankruptcy Code and that a bankruptcy court cannot affect a matter within the FERC's jurisdiction under the Federal Power Act, including the rejection of a wholesale power purchase agreement regulated by the FERC. In its December 23, 2003 order, the District Court also vacated the injunction granted by the Bankruptcy Court that restrained the FERC from acting with respect to the Back-to-Back Agreement. On August 4, 2004, the United States Court of Appeals for the Fifth Circuit reversed the District Court's December 23, 2003 decision dismissing the Mirant Debtor's motion to reject the Back-to-Back Agreement. The Court of Appeals ruled that the Bankruptcy Code does authorize the District Court to reject a contract for the sale of electricity that is subject to the FERC's regulation under the Federal Power Act as part of a bankruptcy proceeding and that the Federal Power Act does not preempt that authority. The Court of Appeals did not address the merits of the Mirant Debtor's motion to reject the Back-to-Back Agreement but remanded the proceeding to the District Court for further action on that motion. The Court of Appeals did indicate that on remand the District Court should consider applying a more rigorous standard than the business judgement standard typically applicable to contract rejection decisions by debtors in bankruptcy, which more rigorous standard would take into account the public interest in the transmission and sale of electricity. With respect to the injunctions issued by the Bankruptcy Court that were vacated by the District Court, the Court of Appeals ruled that the injunctive relief granted by the Bankruptcy Court exceeded its authority under the Bankruptcy Code. While the Court of Appeals found that the injunctive relief actually granted by the Bankruptcy Court was too broad, it did state that the concern expressed by the Bankruptcy Court, that the FERC could negate the Mirant Debtor's rejection of an executory contract by ordering the Mirant Debtors to continue to perform under the terms of the rejected contract, was a legitimate basis for injunctive relief.

New York Tax Proceedings: On July 7, 2004 and July 28, 2004, the New York Debtors entered into settlement agreements with certain of the taxing authorities resolving sixteen Tax Certiorari Proceedings related to the real property tax assessments for Mirant NY-Gen's Hillburn, Swinging Bridge, Mongaup, and Rio generating facilities for the years 2000 through 2003. The New York Debtors have not paid real property taxes on the New York generating facilities for 2003 totaling approximately $62 million. For 2003, these settlements reduce the equalized assessed value of the affected generating facilities significantly, resulting in a reduction in the amount of taxes owed by Mirant NY-Gen to the settling taxing authorities for those facilities from $2.9 million to $0.9 million. These reduced assessed values will also apply to tax years 2004, 2005, and 2006. The settlements also set reduced assessed values for the affected generating facilities for the years 2000 through 2002 that will result in refunds to Mirant NY-Gen totaling $2.4 million. The settlement agreements are subject to the approval of the Bankruptcy Court.

Environmental Liabilities: In 2000, the State of New York issued a notice of violation to Orange and Rockland Utilities, Inc., the previous owner of Mirant New York's Lovett facility, concerning the air permitting and air emission control implications under the Environmental Protection Agency's new source review regulations promulgated under the Clean Air Act ("NSR") of the operation of that plant prior to its acquisition by Mirant New York. On June 11, 2003, Mirant New York and the State of New York entered into, and filed for approval with the United States District Court for the Southern District of New York, a consent decree that released Mirant New York from all potential liability for

matters addressed in the notice of violation previously issued by the State of New York to Orange and Rockland Utilities, Inc. and for any other potential violation of NSR or related New York air laws prior to and through the date of entry of the consent decree by the court. Under the decree, Mirant New York commits to install on Lovett's two coal-fired units by 2007 to 2008 emission control technology consisting of selective catalytic reduction technology to reduce nitrogen oxide emissions, alkaline in-duct injection technology to reduce sulfur dioxide emissions, and a baghouse. The cost of the emission controls prescribed by the consent decree could exceed $100 million over the approximately five year period covered by the consent decree. Such costs would generally be capitalized and amortized as a component of property, plant and equipment. The consent decree allows Mirant New York to shut down a unit rather than install the prescribed emission controls on the unit. For one of the units, Mirant New York also has the option to convert the unit to operate exclusively as a gas-fired boiler and limit the hours of operation rather than install the prescribed emission controls. Mirant New York did not admit to any liability, and the consent decree does not impose any penalty on Mirant New York for alleged past violations. The District Court approved and entered the consent decree on October 9, 2003, and it was approved by the Bankruptcy Court on October 15, 2003. Under the consent decree, Mirant New York by August 1, 2004 was required to notify the State of New York whether it would convert Lovett Unit 5 to natural gas, install control technology on that unit, or discontinue the operation of that unit, and if Mirant New York elected to install control technology on that unit, to award construction contracts for such control technology. The consent decree also required Mirant New York to notify the State of New York by August 1, 2004 whether it would install a baghouse on Lovett Unit 4 or Lovett Unit 5 to reduce particulate emissions. On July 30, 2004, Mirant New York and the State of New York agreed to modify the consent decree to delay such notification requirements until August 1, 2005.

California Department of Toxic Substances Control Claim: On January 7, 2004, the California Department of Toxic Substances Control (the "Department") filed a proof of claim in the Mirant Debtors bankruptcy proceedings based on civil penalties for alleged non-compliance with state hazardous waste laws and regulations requiring proper documentation of financial assurance for the ultimate closure and post-closure costs, and third-party liability coverage related to Mirant's power plant in Pittsburg, California. The Department has calculated potential penalties to be approximately $400,000. The Department has not notified Mirant of the assessment of any penalties nor of the institution of any administrative action. At this time, Mirant cannot predict what the outcome of this claim will be.

City of Alexandria Potential Zoning Action: On June 22, 2004, the City Council for the City of Alexandria, Virginia adopted a resolution initiating certain zoning ordinance amendments and referring consideration of the amendments to the City Planning Commission for public hearing and consideration. Those amendments, if adopted, could result in the zoning status of Mirant Potomac River's generating plant being changed in a way that could require termination of the operation of the plant within a number of years that would be specified as part of the amendment process. The City Council also authorized institution of enforcement actions that would seek to revoke special use permits applicable to the administrative office space at Mirant Potomac River's plant and the plant's transportation management plan. Revocation of such permits would not materially impact plant production but could impact Mirant Potomac River's ability to obtain new permits for construction activities at the plant. The proceedings before the City Council also referred to the possible institution by the City of Alexandria of a suit against Mirant Potomac River for violation of the Clean Air Act based on the allegations underlying the notices of violation issued by the Virginia Department of Environmental Quality on September 10, 2003 and the EPA on January 22, 2004. Any such suit, however, would require further approval of the City Council before being instituted. The City Council also authorized the City to file an objection to any plan of reorganization that the Mirant Debtors file in the pending Chapter 11 proceedings that includes the continued operation of the Mirant Potomac River plant. Any action by the City Council that results in the termination of operation of the Mirant

Potomac River generating plant could have a material adverse effect upon the Company depending upon the timing of such termination.

The Company is not aware of any other material developments in legal proceedings involving the Company or its subsidiaries since its report in Mirant's Annual Report on Form 10-K for the year ended December 31, 2003 and Form 10-Q for the quarter ended March 31, 2004.

Item 6. ***Exhibits and Reports on Form 8-K***

(a) ***Exhibits.***

10.1	Employment Agreement with Michele Burns
10.2	Employment Agreement with Loyd (Aldie) Warnock
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

(b) ***Reports on Form 8-K***

During the six months ended June 30, 2004, the Company filed no Current Reports on Form 8-K.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on this 9th day of August, 2004.

MIRANT CORPORATION

By: /s/ DAN STREEK

Dan Streek
Vice President and Controller
(Principal Accounting Officer)

QuickLinks

TABLE OF CONTENTS
DEFINITIONS
CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION
MIRANT CORPORATION AND SUBSIDIARIES (Debtor-in-Possession) CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
MIRANT CORPORATION AND SUBSIDIARIES (Debtor-in-Possession) CONDENSED CONSOLIDATED BALANCE SHEETS
MIRANT CORPORATION AND SUBSIDIARIES (Debtor-in-Possession) CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' DEFICIT (UNAUDITED)
MIRANT CORPORATION AND SUBSIDIARIES (Debtor-in-Possession) CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)
MIRANT CORPORATION AND SUBSIDIARIES (Debtor-in-Possession) CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
Financial Data by Segment (In Millions)

Item 2. Management's Discussion and Analysis of Results of Operations and Financial Condition

Item 3. Quantitative and Qualitative Disclosures about Market Risk
Item 4. Controls and Procedures
PART II

Item 1. Legal Proceedings
Item 6. Exhibits and Reports on Form 8-K
SIGNATURES