Thinking like a winner.

ATMOS

ATMOS ENERGY CORPORATION 1998 ANNUAL REPORT

Financial Highlights

	Year ended September 30,		
	1998	1997	% change
	(Dollars in thousands, except per share amounts)		
Operating revenues	$ 848,208	$ 906,835	-6.5%
Gross profit	$ 331,836	$ 329,654	0.7%
Utility net income	$ 42,147	$ 16,991	148.1%
Non-utility net income	$ 13,118	$ 6,847	91.6%
Total net income	$ 55,265	$ 23,838	131.8%
Total assets	$1,141,390	$1,088,311	4.9%
Total capitalization	$ 769,706	$ 630,241	22.1%
Net income per share – diluted	$ 1.84	$ .81	127.2%
Cash dividends per share	$ 1.06	$ 1.01	5.0%
Book value per share at end of year	$ 12.21	$ 11.04	10.6%
Total throughput (MMcf)	215,597	213,008	1.2%
Heating degree days	3,799	3,909	-2.8%
Degree days as a % of normal	95%	98%	-3.1%
Meters in service at end of year	1,004,532	985,448	1.9%
Return on average shareholders' equity	15.8%	7.3%	116.4%
Shareholders' equity as a % of total capitalization at end of year	41.5%	40.3%	3.0%
Shareholders of record	36,949	29,867	23.7%
Average shares outstanding – diluted (000's)	30,031	29,422	2.1%

Table of Contents

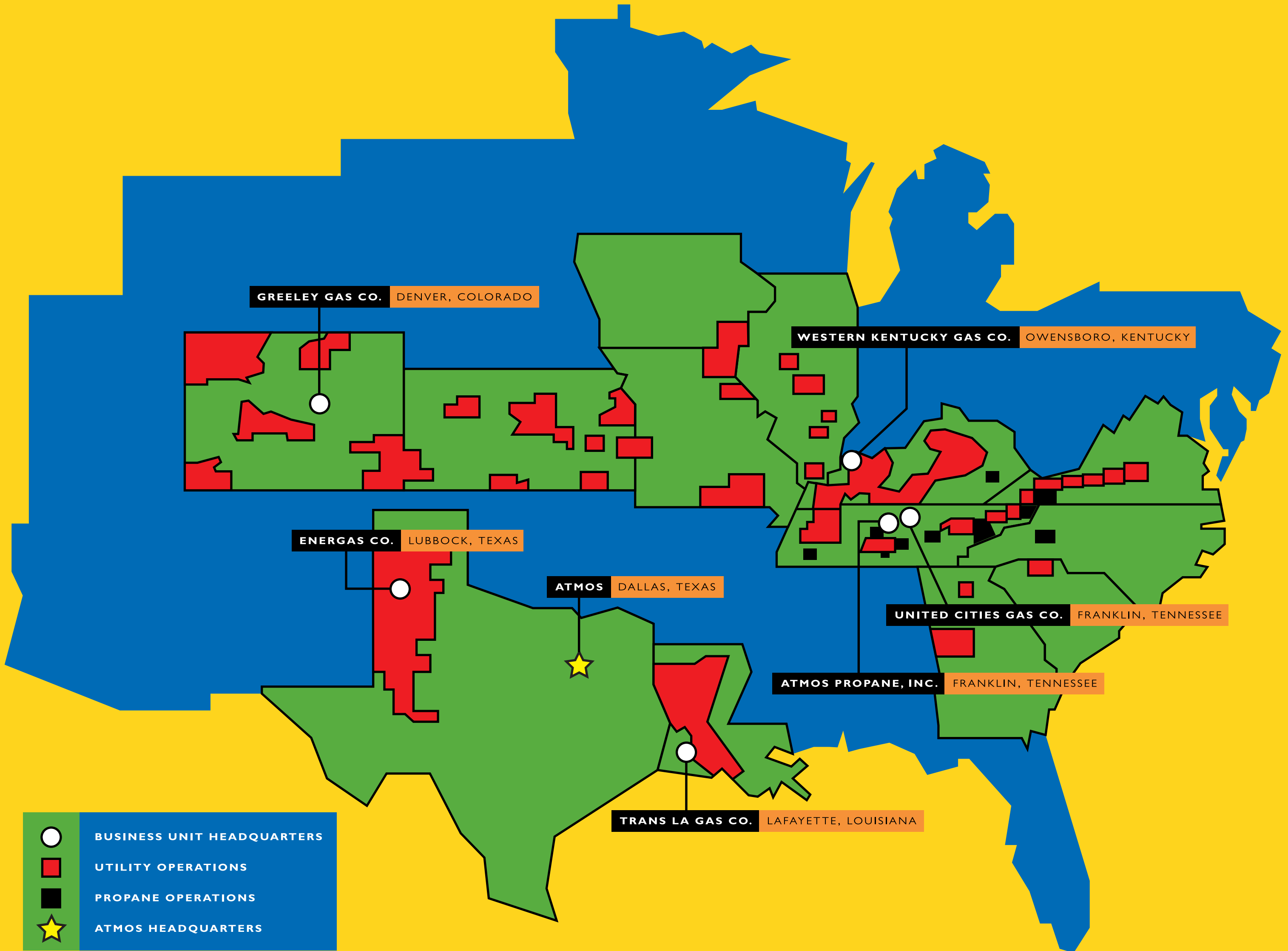
Letter to Shareholders 2
Chief Executive Q&A 5
Utility Operations 8
Energas Company Information 10
Greeley Gas Company Information 12
Trans Louisiana Gas Company Information 14
United Cities Gas Company Information 16
Western Kentucky Gas Company Information 18
Non-Utility Operations 20
Shared Services 22
Financial Information 23
Board of Directors 56
Corporate Information 57

Atmos has a tradition of delivering safe, reliable, economical and environmentally friendly natural gas to customers, doing so with a focus on exceptional customer service. Even though our industry is changing, our commitment to customers is not. This report outlines our successes in 1998 and highlights ways we are delivering on our commitment to be counted among the best in the industry. We also feature some outstanding citizens from the communities served by our company who display a winning attitude. They passionately pursue excellence, dare to reach for the summit, utilize their unique talents to make a difference, translate dreams into realities, help others to succeed and perform their best with precision, stamina and heart. By "thinking like a winner," they have become winners indeed.

Atmos at a Glance

	Year ended September 30,		
	1998	1997	1996
Utility Meters In Service [1]			
Residential	889,074	870,747	860,229
Commercial	94,302	92,703	91,960
Industrial (including agricultural)	16,322	17,217	19,403
Public authority	4,834	4,781	4,716
Total natural gas meters	1,004,532	985,448	976,308
Propane customers	37,400	29,097	26,108
Total	1,041,932	1,014,545	1,002,416
Heating Degree Days			
Actual (weighted average)	3,799	3,909	4,043
Percent of normal	95%	98%	101%
Sales Volumes (MMcf)			
Residential	73,472	75,215	77,001
Commercial	36,083	37,382	38,247
Industrial (including agricultural)	44,881	46,416	57,863
Public authority	4,937	5,195	5,182
Total	159,373	164,208	178,293
Transportation Volumes (MMcf)	56,224	48,800	44,146
Total Throughput (MMcf)	215,597	213,008	222,439
Propane – Gallons (000's)	33,676	32,975	40,723
Operating Revenues (000's)			
Gas Revenues			
Residential	$ 410,538	$ 452,864	$ 409,039
Commercial	184,046	193,302	186,032
Industrial (including agricultural)	161,382	168,386	187,693
Public authority	20,504	23,898	21,738
Total	776,470	838,450	804,502
Transportation revenues	23,971	19,885	18,872
Other gas revenue	8,121	6,385	13,751
Total gas revenues	808,562	864,720	837,125
Propane revenues	29,091	33,194	38,372
Other revenues	10,555	8,921	11,194
Total Operating Revenues (000's)	$ 848,208	$ 906,835	$ 886,691
Other Statistics			
Gross plant (000's)[1]	$1,446,420	$1,332,672	$1,219,774
Net plant (000's)[1]	$ 917,860	$ 849,127	$ 770,211
Miles of pipe [1]	30,108	30,902	30,163
Employees [1]	2,193	2,679	2,863

[1] Balances as of September 30, 1998

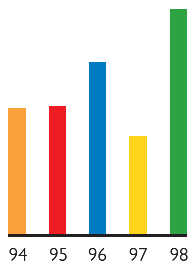


Based in Dallas, Texas, Atmos Energy Corporation distributes natural gas and propane to more than one million customers in Colorado, Georgia, Illinois, Iowa, Kansas, Kentucky, Louisiana, Missouri, North Carolina, South Carolina, Tennessee, Texas and Virginia through its operating divisions – Energas Company, Greeley Gas Company, Trans Louisiana Gas Company, United Cities Gas Company, Western Kentucky Gas Company and Atmos Propane, Inc.

Dear fellow share-holders:

company's accomplishments can be gauged in a variety of ways, but the ultimate measure of a company's performance is its total return to shareholders. For fiscal 1998, Atmos' total return to shareholders (simple price appreciation plus reinvestment of dividends) was 19.2 percent during a period when U.S. equity markets experienced dramatic volatility. The total return to Atmos shareholders for the fiscal year exceeded the return of the Dow Jones Industrial Average, the S&P 500 and was among the best of our peer group of mid-cap local distribution companies for the same 12-month period. For the past three-, five-, and 10-year periods, the total return to shareholders was 18.2 percent, 11.7 percent and 16.2 percent, respectively. We believe our returns to shareholders reflect the Company's underlying financial and operational successes. We would like to highlight the 1998 achievements.

Atmos achieved record earnings. Net income for 1998 was $1.84 per share on a fully diluted basis, compared with $.81 per share the previous year on a fully diluted basis. Winter weather in 1998 was 5 percent warmer than normal and 3 percent warmer than last year. However, the negative effect of weather was offset by a significant reduction in operations and maintenance expenses resulting from the restructuring of our organization and the successful integration of United Cities Gas Company, acquired through the merger completed in 1997. In addition, gas sales to Texas farmers for powering irrigation pumps were higher in fiscal 1998 compared to 1997 due to the hot, dry summer weather. Irrigation volumes increased 34 percent in 1998 compared with last year, providing more revenue during late spring, summer and early fall when natural gas sales are typically low because there are generally no sales or transportation of natural gas for space heating.



Earnings Per Share (fully diluted)

- **94** *$1.05*
- **95** *$1.06*
- **96** *$1.42*
- **97** *$0.81*
- **98** *$1.84*

The dividend was increased for the 11th consecutive year. In November 1998, the Company increased its quarterly dividend by 3.8 percent to $.275 per share, or $1.10 annually. With the payment of the quarterly dividend on December 10, 1998, to shareholders of record on November 25, 1998, the Company will have paid a quarterly dividend for 60 consecutive quarters.

United Cities was successfully integrated into Atmos' utility operations. During 1998, United Cities' integration into Atmos' operations was substantially completed. United Cities' operations were restructured to match Atmos' highly efficient utility business unit model and to gain the advantages of Atmos' "shared services"

approach to administrative and support functions. The benefits of the United Cities restructuring along with others throughout the Atmos utility operations are reflected in lower operation and maintenance expenses for fiscal 1998 compared to 1997. Net income in 1998 also included a one-time gain totaling $2.2 million, or $.07 per diluted share, from the sale of certain real estate and equipment owned by the United Cities Division that were no longer essential to Atmos' operations or those of the United Cities Division.

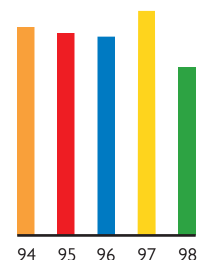
Atmos has completed four major acquisitions since 1986, nearly tripling the number of meters served to over one million in 12 states. Closing a merger or acquisition is an achievement in itself, but deriving value from the transaction is an even greater accomplishment. Atmos has demonstrated the abilities to integrate companies quickly and without unnecessary expense. Atmos retains the acquired company's name, capitalizes on its local identity and reputation with customers, but utilizes its business unit and shared services structure to achieve economies of scale without replicating administrative and support functions in each business unit.

We continued to enhance utility customer service and operating efficiency. The Company is showing the benefits of a restructuring of its customer service operations begun in 1997 for all of our utility business units, including United Cities. We enhanced service and convenience for our customers by employing technology to improve our already efficient operations. Our Customer Support Center is now providing 24-hour a day, seven days a week customer call support to utility customers of all five utility divisions. The Customer Support Center and a new state-of-the-art customer information system currently being developed will further improve our responsiveness to our customers.

Atmos strives to be among the best of its peers in terms of efficiency in utility operations. One measure of this is operating and maintenance expense per meter. Atmos' 1998 operating and maintenance expense of $136 per meter achieved our goal of being among the best, if not the best, of our peers. This is the result of a dedicated, focused employee team that serves on average 475 meters per employee, again a measure that puts Atmos among the best, if not the best, of our peers.

We continued to add meters in our current service areas. Atmos added more than 19,000 new utility meters in 1998, with the largest number of additions in the United Cities and Greeley Divisions. We are focusing on untapped market potential in our existing service areas, particularly in residential gas fireplaces, water heating and gas lighting. We are initiating programs to pursue these opportunities and target areas where we can increase market penetration.

Non-utility contributions to consolidated net income increased. Atmos' non-utility operations include a propane operation, a leasing and rental operation, and an energy services operation that includes storage, gas marketing, irrigation, and energy services. In 1998, about 24 percent of the Company's reported net income was from non-utility operations, primarily from irrigation, gains on asset sales and Woodward Marketing, LLC. Excluding the one-time gain on asset sales, non-utility operations contributed 20 percent to 1998 consolidated net income compared to 17 percent in 1997. The 1997 contribution to consolidated net income excludes the one-time charge for reserve for integration and management reorganization. The contributions to net income from each non-utility operation are described elsewhere in this report.



Operating and Maintenance Expense Per Customer

- **94** $169
- **95** $163
- **96** $160
- **97** $183
- **98** $136

Atmos will be **working** to make **shareholders,** customers, **communities** and employees **winners,** too.

Established compensation more closely aligned with financial performance. We instituted a new total rewards program in October 1998 that more directly aligns the interests of our Board of Directors, officers and employees with those of our shareholders by basing compensation on the Company's financial performance. Starting at the very top of our organization, our Board of Directors has elected to replace the directors' retirement plan with a plan providing for deferred payment of annual compensation and meeting fees in the form of cash or company stock. Directors may also receive annual current compensation and meeting fees in the form of company stock. The total rewards program establishes share ownership guidelines for Atmos executives at a minimum of one and one-half to five times their annual salary, and a new officer incentive plan will base stock option grants on the achievement of financial performance measures. A variable pay program will give all employees the opportunity to share in the success of the Company based on the attainment of certain financial targets. Nearly all our employees are shareholders, and together the board, officers and employees currently hold more than 12 percent of Atmos stock. Certain of our compensation plans will require a vote of the shareholders at the February 1999 shareholders meeting.

Thinking ahead. Atmos has been a successful company. Our challenge is to build on that success, and to be as successful in the future as we have been in the past. Our successful past sets a high standard for future performance.

We devoted much of 1998 to assessing every aspect of our business, defining our organizational structure, governance policies and strategies that will position the Company for what we believe will be a successful future. I would like to recognize our employees for their openness to change, their unwavering dedication to exceptional customer service even in times of change, and their commitment to excellence. I also want to thank our Board of Directors for their counsel and ongoing support of the Company's vision and strategies for growth.

Now, all our focus and energies are dedicated to executing our plans. We intend to be a winner and measured among the best. And we know that while our accomplishments can be described in a variety of ways, in the final analysis, the measure of our accomplishments will be the total return to you, our shareholder. By thinking like a winner in everything we do, Atmos will be working to make shareholders, customers, employees and communities winners, too.

Robert W. Best

Chairman of the Board, President and Chief Executive Officer

Robert W. Best

Robert W. Best

Chairman, President and Chief Executive Officer

Thinking like a winner.

A Conversation with Bob Best

Describe Atmos' vision for the future and its underlying operating philosophy.

Best: Since joining the Company in March 1997, we have reconfirmed the vision for the future with four major strategies for achieving the vision. We intend to be as successful in the future as we have been in the past by running our utility operations exceptionally well; growing the market share of the non-utility operations (propane and gas marketing); developing retail energy services; and growing through acquisitions.

We have worked to define our organizational structure and governance policies. Our business units have established brand names and are closest to our customers, giving them greater ability to determine customer expectations. Our shared services approach to administration and support avoids duplication of functions in our business units and allows us to quickly integrate acquisitions. We are committed to providing the highest level of service to our customers, and investing in technology to remain competitive and efficient in our operations. We intend to grow our net income every year. Our new total rewards compensation and benefits strategy supports our values and aligns the interests of our Board of Directors, officers and employees with those of our shareholders.

I have visited every business unit communicating to our employees our values and how we will live out those values in the workplace. We've invested considerable time this year in team-building and visiting with all employees about their role in achieving our vision and strategy.

The Company has pursued an aggressive corporate development strategy. Will that strategy continue in the future?

With our vision and strategy confirmed, our top priorities are execution of our plans and acquisition strategy. We will not be satisfied as a "maintenance" utility just managing, although very well, our current operations. To achieve our objective, we must continue the acquisition strategy that has successfully brought Atmos to this point. We also believe that larger scale operations will have an even greater competitive advantage with the unbundling of energy services and an increasingly competitive marketplace.

We continually evaluate opportunities. However, the decision is not solely in our hands. Potential partners have to share our vision and see the benefits and synergies of a larger company. We have been successful in acquiring companies, integrating them quickly and efficiently, retaining the local company's brand identity, and adding value to the shareholders of both companies. Our track record makes us an attractive partner for a company looking for a partner that is focused on a combination that is "seamless" to the customer and value creating for shareholders.

How do you intend to grow your non-utility business?

Our non-utility operations contributed about 24 percent of our consolidated net income in 1998. If you exclude the one-time gain from asset sales, our non-utility business contributed 20 percent of 1998 consolidated net income. Our objective is for continued growth in both our utility and non-utility businesses, and for our non-utility operations to continue to contribute about 20 percent to net income each year.

Gross Profit

- **94** *$297,020*
- **95** *$300,158*
- **96** *$324,412*
- **97** *$329,654*
- **98** *$331,836*

Q A

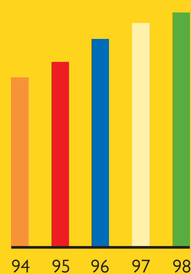
A Conversation with Bob Best *(continued)*

The Company is committed to improving the profitability of its propane operations through internal growth and through acquisitions. Currently, Atmos Propane, Inc. is the 33rd largest propane company in the United States. Our non-utility operations also include a 45 percent interest in Woodward Marketing, LLC, a natural gas services firm. Woodward's strategy for continued growth is to increase gas usage by existing customers and to add new customers. We also may seek an electric partner to become a member of Woodward Marketing, LLC, and create the opportunity to market electricity to Woodward customers.

How does Atmos plan to offer retail services to its customers?

The cornerstone of our retail services strategy is to position the Company to sell the gas commodity to customers behind the meter through partnerships with commodity providers. We are limited in our ability to implement this part of our retail strategy until the states in which we operate permit us to offer these services. Until unbundling occurs, we are focusing on three key areas. First, we are preparing to sell other products and services to our customers by establishing partnerships with third parties that have mass marketing expertise. Our focus is on products and services that have recurring monthly revenues. A second key area is restructuring our non-regulated agricultural and industrial businesses to separate them from the utility so that we can clearly focus on the needs and expectations of these customers. The third key area is identifying technological opportunities that can increase our cash flow, earnings and gas throughput, such as introducing natural gas-fired electric generator units for irrigation.

We believe our approach to retail services offers many advantages, including minimal investment or operating expenses with limited risk. Our retail strategy also positions the Company for unbundling when it does occur.



Total Assets

94	*$ 829,385*
95	*$ 900,948*
96	*$1,010,610*
97	*$1,088,311*
98	*$1,141,390*

What competitive advantages does Atmos have in providing services in an unbundled environment?

Tomorrow's customers will insist on competitive rates, a choice of providers, superior customer service that exceeds expectations, and enhanced product and service offerings beyond the core business. We believe unbundling will occur in the long-term, although it may be slower and less comprehensive than some have predicted. The states we serve are taking a very measured, cautious approach to make sure that customers receive real benefits. We have developed a consistent set of guiding principles for unbundling across all regulatory jurisdictions in the areas we serve, and are participating in the proceedings in those jurisdictions to ensure rules being developed provide for a level playing field. As unbundling occurs, we believe that the incumbent utility or one of its affiliates will have an advantage, both as a seller of the natural gas commodity and as the seller of other products and services. We have an organization that is efficient and responsive to customers, and our desire is to make it convenient for customers to do business with us.

How is Atmos using technology to support its vision for growth?

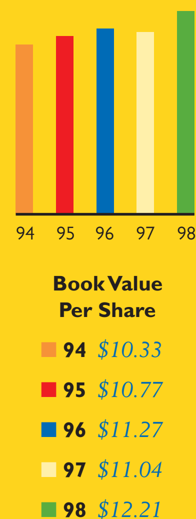
We are using technology to gain efficiencies in our current operations and to enhance the services and convenience provided to our customers. We plan to eventually allow customers the opportunity to receive their bills on line and remit payment electronically,

for example. We also are investing in information technology to respond to future customer growth that occurs through acquisitions and to prepare for unbundling. Unbundling will require the capability to bill in many different ways, and will make our financial systems more complex. We are automating many functions of our billing and financial systems to give us flexibility in the wake of unbundling and allow us to integrate acquisitions in months instead of a year or more. We are implementing an enterprise resource planning system that will get more timely financial and human resources information to the desktop, and also addresses Year 2000 (Y2K) issues. We are automating the way we handle customer service requests through our new customer information system, and our next step is to implement an automated workforce management system to handle construction, cathodic protection of our pipe and facilities management. We're also planning the development of a comprehensive gas supply and capacity management system.

I'm often asked about our Year 2000 readiness. Our goal is to make the Year 2000 a non-event for our customers and the Company. We formed a Y2K team in October 1996 to inventory all internal and external systems and to address related issues throughout Atmos and with our external business partners. We are working with our vendors, particularly our gas suppliers, to ensure that they are Y2K compliant and that we have gas flowing into our distribution system. Our new customer information system is being implemented to allow us more capabilities and flexibility, but has the upside of taking care of most customer issues related to Y2K.

What are the strengths that will make the Company continue to be a winner in the future?

Our strategy of growth by acquisition and the diversity we have created through that strategy are tremendous strengths that set us apart from other companies. We operate in 13 states with great variety in economic climates, regulatory environments, markets and weather patterns – Atmos' breadth of operations is unmatched in the industry. Our agricultural market in Texas and Colorado is an example of a unique market niche, providing spring and summer sales of natural gas for powering irrigation pumps. Our non-regulated operations, particularly propane distribution and our interest in Woodward Marketing, also complement our utility operations and promote real earnings growth opportunities.



Let's look at some of the intangibles that set us apart. I believe that we have an excellent team that is diverse in thinking and open to pursuing best practices. The way we think and work matches the diversity of our operations and our physical assets. We have a vision and strategy we believe in, and we expect to be successful. We have passionate, well-trained employees who take great pride in our Company and their work, and they want to be the best. We have a new total rewards strategy that supports our vision and rewards employees for achieving our financial goals. Our Board of Directors supports our vision and is fully committed to the growth of this Company.

I feel good about where our Company is positioned. I am confident about our Company's prospects for growth. We are a company with a bright and exciting future.

Running the Utility Operations Extremely Well

Our strong local presence provides us with a distinct competitive advantage.

Atmos' five utility business units – Energas Company, Greeley Gas Company, Trans Louisiana Gas Company, Western Kentucky Gas Company and United Cities Gas Company – serve over one million natural gas meters in 12 states. Utility operations produced revenues of $744.6 million in 1998, or about 88 percent of Atmos' total revenues. Utility revenues were about 8 percent lower than in 1997, generally the result of lower gas cost and winter weather that was 5 percent warmer than normal and 3 percent warmer than last year. However, utility net income for 1998 was $42 million, or about 76 percent of Atmos' consolidated net income, and up from 1997 utility net income of $17 million.

Our utility operations are the core of Atmos' business, and we are intensely focused on running our utility operations exceptionally well. We measure our utility performance in terms of superior customer satisfaction ratings; operating efficiency; earning our allowed rate of return each year in each jurisdiction; and growing utility earnings annually.

Customer Service Enhancements

In 1998, the Company's utility division continued to invest in developing and implementing its program of customer service enhancements. By investing in the technology of a new Customer Support Center and customer information system, Atmos is positioning itself to provide more convenience and extended service hours to its customers while continuing to enhance the efficiency of its field operations.

In early 1998, Atmos opened a central Customer Support Center in Amarillo, Texas, that provides customer call support 24 hours a day, seven days a week for all of its utility customers. The Company also is in the process of installing a state-of-the-art customer information system that is expected to be in service by the end of fiscal 1999. The new customer information system will provide more information than ever before on customer bills regarding energy usage and will provide customer service representatives more readily available information to handle customer inquiries. The system supports new technology that makes our customer service more responsive and efficient, such as automatic dispatching of service orders to in-truck terminals and computerized meter reading units that improve accuracy and reduce the time for reading meters.

The Company also established a network of payment centers in convenient locations such as banks and grocery stores, many of which offer extended business hours. With the payment centers and Customer Support Center in place, Atmos was able to consolidate its field offices.

Internal Growth

The Company added over 19,000 new utility meters in its current service areas in fiscal 1998. The largest number of additions occurred in the United Cities and Greeley Divisions. The Company participates in economic development efforts in the communities it serves. For example, Energas actively supported initiatives that helped Amarillo, Texas, attract a new helicopter assembly plant that will create 1,200 jobs, and the location of five call centers to the area that will create new jobs. Western Kentucky Gas was a leader in the effort to build a new airpark in Owensboro, Kentucky, that initially attracted five new businesses to the Western Kentucky area. These new businesses will create nearly 1,500 jobs.

The Company undertook an extensive assessment of its utility marketing initiatives in 1998. The results of the re-evaluation were to focus on untapped market potential in our existing service areas, particularly in residential gas fireplaces, water heating and gas lighting. We are initiating programs to pursue these opportunities and target areas where we can increase market penetration. Responsibility for marketing strategy and program development is in each business unit, giving each business unit the opportunity to promote greater market segmentation and customization of programs for local market conditions. A companywide marketing council was established to share expertise and successful marketing ideas across the utility business units.

The true measure of success of our service enhancement efforts will be in achieving superior customer satisfaction ratings. We are planning to regularly survey our customers to ensure they are totally satisfied with our service and that we are truly meeting their expectations. We will continually evaluate and modify our programs and practices to be responsive to what our customers are telling us. We want to go beyond just satisfied customers – we want happy, satisfied and loyal customers.

Earning our allowed rates of return

In 1998, none of our utility business units filed any general rate cases. During the year, we evaluated the financial performance in each jurisdiction under each current rate case, and no rate cases were filed in 1998. The Company will continue to carefully monitor performance under the current rate cases and make the filings when necessary to ensure the Company is achieving adequate returns on its utility investments and the capital employed in its utility operations.

In June, Western Kentucky Gas received approval for a three-year, performance-based gas cost incentive plan in Kentucky. Under the plan, Western Kentucky Gas shares equally with customers any savings in gas costs it achieves, as measured against certain predetermined industry benchmarks. United Cities Gas has a similar performance-based gas cost incentive plan in effect in Georgia, and a plan is under review in Tennessee.

Local identity

Our five utility business units are committed to being good citizens in the communities they serve. We believe in the importance of supporting and improving the well-being of those who are in need or less fortunate. Our interests include such areas as community development, education systems, and health and welfare agencies. Our employees are active in civic and community organizations – several of our employees serve in public office.

Part of our strategy includes using established brand identity. Each acquired company continues to operate under its name, ensuring the trust and respect that was developed decades ago with our customers continues to grow. We believe that our strong local presence provides us with a distinct competitive advantage in an increasingly competitive marketplace.

Being a winner

demands the

passionate pursuit

of excellence seven days

a week.

Between daily practice sessions and weekend travel to competitions, seven-year-old Tyler Burns of Amarillo, Texas, devotes seven days a week to his passion for Motocross racing. “He started asking for a motorcycle at age three. I told him he’d have to wait until he could ride his bicycle without training wheels. He’s been riding in Motocross events since he was five,” says Energas employee, Michael Burns, Tyler’s dad and coach. For Atmos, providing convenient customer call support is a seven-day per week passion.

Amarillo, Texas will be the home of the world's first tiltrotor assembly plant. Amarillo's Economic Development Corporation prepared an aggressive proposal to attract Bell Helicopter, creating 1,200 new jobs.

ENERGAS CO.

The company serves a unique non-utility agricultural market in Texas that provides revenues during the summer when heating sales are low. Farmers use natural gas to power irrigation pumps.

Energas Company is headquartered in Lubbock, Texas. Energas serves more than 300,000 customers in 92 West Texas towns and communities, including Amarillo, Lubbock, and Midland/Odessa. Energas has 401 employees. Operating revenues in 1998 were $220.7 million.

Winners dream

big

and dare to

reach

the top.

Greg Bardin and Chip White started a home-sewing operation making funky athletic headwear for skiers and for college students in Colorado. Today, their Durango-based company, Bula Inc., is a world-class manufacturer of headwear, and is a sponsor of the U.S. Olympic ski team and many athletes, including Gold Medalist Tommy Moe. "Bula is the Fijian greeting meaning life, health and happiness. That's the Bula attitude: Punch it. Go BIG. No matter how much we grow, we'll keep our attitude," said President Chip White. Atmos dares to dream big, measuring itself against the best in this and other industries.

Neosho Gardens in Council Grove, Kansas, depends on natural gas to keep plants warm and growing when the temperature is below 65 degrees, and has been assisted by Greeley Gas as the greenhouse operations have expanded.

GREELEY GAS CO. **Service technicians receive customer service orders automatically from our state-of-the-art customer information system through in-truck computers, increasing their responsiveness to customer requests for service.**

Greeley Gas Company is headquartered in Denver, Colorado, and serves more than 115,000 customers in 123 communities in Colorado, Kansas and Missouri. Towns served include Greeley, Steamboat Springs, Durango and Cañon City, Colorado, and Bonner Springs, and Johnson County, Kansas. Greeley Gas has 193 employees. Operating revenues in 1998 were $85.0 million.

Winners use unique talents to play in the big leagues.

Stanley Dural Jr. played organ, fronting his own R&B band. He was not initially interested in the traditional music he grew up with in Carencro, Louisiana. Then he rediscovered his Creole roots, picked up the accordion and 20 years ago this year became Buckwheat Zydeco. Fifteen acclaimed albums later, nominated for four Grammy awards, Buckwheat Zydeco says, "Don't criticize what you don't understand, or you'll be the loser." Atmos is taking what it understands and employing a strategy to play in the big leagues.

Stuller Settings, a customer in Lafayette, Louisiana, has grown from a small jewelry operation to become one of the world's largest distributors of jewelry-related products, and a major employer. Stuller's accomplishments have been recognized with the U.S. Senate Productivity Award and numerous state awards.

TRANS LA GAS CO. New trenching technology allows installation of new pipe without tearing up the customer's lawn and landscaping.

Trans Louisiana Gas Company is headquartered in Lafayette, Louisiana, and serves more than 81,000 customers in 41 communities in Louisiana, including Monroe, Natchitoches, Pineville and Lafayette. Trans La has 134 employees. Operating revenues in 1998 were $41.9 million.

Winners are not

limited by

what they see...

they are driven by what

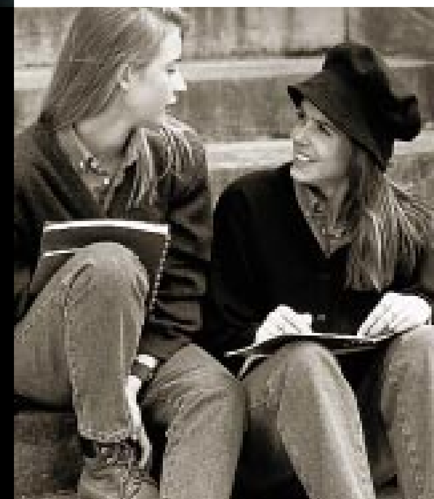
can be.

Developer Calvin LeHew has created remarkable transformations in downtown Franklin, Tennessee, rehabilitating abandoned industrial buildings into tourist attractions. "I don't see broken bricks and walls when I walk through these old buildings — I see people attending concerts, and visiting art galleries and restaurants," he says. Atmos' vision is to be among the top competitors in the industry in customer service and financial performance.

Four educational institutions in Tennessee are using new natural gas cooling technology, which provide a year-round gas load for the Company. The Company offers technical assistance to large users to help them improve their energy efficiency.

UNITED CITIES GAS CO. **Our marketing study pinpointed untapped market potential in residential gas lighting and fireplaces.**

United Cities Gas Company is headquartered in Franklin, Tennessee, and serves more than 316,000 customers in 383 communities in Illinois, Tennessee, Iowa, Virginia, Georgia, South Carolina, Kansas and Missouri. Towns served include Franklin and Johnson City, Tennessee, and Columbus, Georgia. United Cities has 621 employees. Operating revenues in 1998 were $337.4 million.



Reward for a winner is helping others succeed.

A gospel singer and Owensboro, Kentucky, city employee who served three terms on the city commission of her hometown of Beaver Dam, Alma Randolph heads a charitable foundation that provides new back-to-school clothes and supplies for more than 500 disadvantaged children each year. "I've never forgotten my family's struggle through poverty after my father died when I was a child, and I wanted to use my talent to help children traveling the same road I once traveled," she said. Atmos has built its success on helping its customers succeed by providing reliable, affordable and environmentally friendly natural gas service.

Biosource Technologies, Inc. is developing pharmaceutical uses of tobacco at its Owensboro, Kentucky facility. The company is one of five companies attracted to the city's MidAmerica AirPark creating 1,500 new jobs for the area. Western Kentucky Gas assisted in the development of the airpark and recruiting of the companies, as well as providing natural gas services.

WESTERN KENTUCKY GAS CO. **Our service technicians use computerized meter reading devices that improve accuracy and reduce paperwork.**

Western Kentucky Gas Company is headquartered in Owensboro, Kentucky, and serves more than 176,000 customers in 163 communities in Kentucky, including Owensboro, Paducah, Danville and Bowling Green. Western Kentucky Gas has 267 employees. Operating revenues in 1998 were $123.6 million.

Winners combine precision, stamina and heart.

Our growing propane operations include service to new upscale developments that have hidden, underground propane tanks like this subdivision near Franklin, Tennessee.

ATMOS PROPANE, INC. Atmos Propane, Inc. distributes propane to 37,400 customers in 240 communities in Tennessee, Kentucky, Virginia and North Carolina. The propane division has 186 employees. Operating revenues from propane were $29.1 million in 1998.

Rolling Stone is a nine-year-old stallion named 1998 World Grand Champion in the show pleasure class at the National Walking Horse Celebration in Shelbyville, Tennessee, trained by David Landrum Stables. Landrum's stables in Franklin, Tennessee, breed and train winning Tennessee Walking Horses. "These horses were developed through 150 years of selective breeding to implant stamina, style and spirit, mild manners and an easy-going ride," said Landrum. For Atmos, customer service is a combination of precise performance and the personal touch in caring for our customers' needs.

Growing the Market Share of the Non-Utility Operations

Non-utility operations contributed about 24 percent of reported net income in 1998, including the sale of certain United Cities' assets. Atmos' non-utility operations include propane distribution, gas storage and energy services, and leasing and rental operations.

Atmos Propane, Inc.

Atmos currently is the 33rd largest propane distributor in the country according to the 1998 survey published by *LP Gas Magazine*. Our goal is to increase the size of our propane operation with the objective of creating value through the economies of scope and scale that we think can be achieved by consolidation in the currently very fragmented industry. The propane operations serve more than 37,000 customers in Tennessee, Kentucky, Virginia and North Carolina. During 1998, the Company completed five propane acquisitions that added 8,500 new customers in Tennessee. The Company's primary competitors are independent operators and co-ops.

The Company's propane operations reported a loss of $66,000 for fiscal 1998 compared to a loss of $90,000 for fiscal 1997. In each of these years, propane operations were significantly impacted by warmer weather and lower margins due to increased competition. The Company is committed to profitability in its current propane operations as well as growth of the propane business. To that end, the propane operation is changing its strategic direction to focus on retail and wholesale propane distribution, and will be exiting less profitable segments of the business including transportation, propane cylinder exchange and propane appliance sales and service. To increase margins, the Company is continuing its strategy of pre-buying propane in the off-season to lock in its supply so that it avoids price spikes in the winter months. The Company has targeted its Southeast service area to increase market penetration, and is also evaluating marketing incentive programs to increase market share.

Gas Storage and Energy Services

The Company's gas storage and energy services segment includes wholesale gas services through Woodward Marketing, irrigation, natural gas storage, and retail services.

Woodward Marketing, LLC Woodward Marketing, LLC, a natural gas services firm, contributed $3.9 million pre-tax earnings in 1998 compared with $3.3 million in 1997, due to an increase in gas volumes sold in 1998 compared to 1997 as well as a modest average margin improvement. Atmos owns a 45 percent interest in Woodward, which is based in Houston, Texas. Woodward provides natural gas services to the Company, industrial customers, municipalities and natural gas utilities in the Southeast, Midwest and California. Woodward's management services include contract negotiation and administration, load forecasting, nominations and scheduling, storage management, capacity utilization and risk management. Atmos expects Woodward's growth to continue through increased gas usage by existing customers and by adding new customers. Atmos continues to consider opportunities for electricity marketing as an added service through Woodward Marketing, LLC.

Irrigation Atmos serves a unique agricultural market in West Texas, selling natural gas to farmers who use natural gas-fired engines that pump water for irrigation. Due to hotter and drier weather in 1998, irrigation sales volumes increased 34 percent and revenues increased to $52.0 million compared to $40.8 million in 1997.

Natural Gas Storage Atmos has underground storage facilities in Kansas and Kentucky that allow the Company to purchase natural gas during the summer when prices are lower and store it for the Company's use or to sell it to others during the winter months when natural gas prices are higher. Storage contributed $1.8 million in net income in 1998, compared to $.7 million in 1997.

Retail Energy Services Our retail energy services strategy is to develop partnerships to sell the natural gas commodity, and eventually the electric commodity, to customers behind the meter when unbundling occurs in the states where we operate. Until then, we are focusing on three retail initiatives through Atmos Energy Services: selling other products and services to our customers by developing partnerships with experienced mass marketers; restructuring our non-regulated agricultural and industrial businesses to separate them from our utility businesses; and identifying technological opportunities that can increase our cash flow, earnings and gas throughput. We believe our approach to retail services limits our investment and operating expenses, minimizes risk, and positions the Company for unbundling when it does occur.

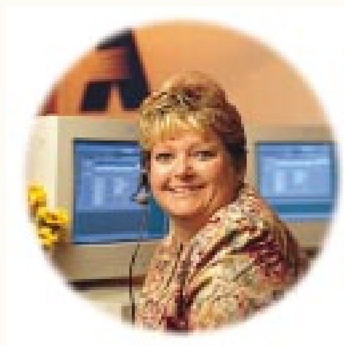
Leasing and Rental

The Company leases and rents appliances, real estate, equipment and vehicles to the United Cities Division. Net income from leasing and rental increased to $3.3 million in 1998, compared with $1.1 million in 1997, due to the sale of certain assets.

Shared Services

Shared services offers significant economies of scale and efficiency.

Atmos provides call support 24 hours a day, seven days a week to its utility customers from a central Customer Support Center and is implementing a state-of-the-art information system. The Company achieves significant economies of scale and efficiency by having one unit performing support functions rather than duplicating them in each business unit.



Atmos continues to achieve efficiencies in its day-to-day operations by providing administrative and support services to its business units through a central group called "shared services." The Company gains significant economies of scale, efficiency and consistency in work practices by having one unit performing support functions rather than duplicating them in each business unit. This structure also enables the Company to integrate the operations of acquired companies quickly and efficiently.

Atmos' shared services include accounting, customer billing, bill payment processing, treasury, purchasing, legal, human resources, information technology, investor relations and corporate communications, gas supply, and internal audit.

Atmos added an important new function to shared services during 1998: the Customer Support Center. The Company opened the central Customer Support Center in Amarillo, Texas, to provide response to customer calls 24 hours a day, seven days a week. Previously, the Company had staffed business offices in locations throughout its service areas to handle customer inquiries and requests for service. The Atmos Customer Support Center demonstrates the Company's shared services philosophy: providing service to the business units from a central location that is responsive, efficient, economical and expandable to serve new customers added by internal growth and through acquisitions.

Atmos has been a pioneer in operating with a shared services structure. The Company regularly reviews its support functions to ensure that they are located where it makes the most sense for efficiency, customer service or strategic reasons.

Shared Services Officers

David L. Bickerstaff
Vice President, Controller

Donald P. Burman
Treasurer

Lee A. Everett
Vice President, Price Policy and Administration

Cleaburne H. Fritz
Vice President, Information Technology

Tom S. Hawkins, Jr.
Vice President, Budget and Planning

Lynn L. Hord
Vice President, Investor Relations and Corporate Communications

J. Patrick Reddy
Vice President, Corporate Development

Gordon J. Roy
Vice President, Gas Supply

Mark G. Thessin
Vice President, Regulatory Affairs

Financial Review

Consolidated Balance Sheets	24
Consolidated Statements of Income	25
Consolidated Statements of Shareholders' Equity	26
Consolidated Statements of Cash Flows	27
Notes to Consolidated Financial Statements	28
Management's Responsibility for Financial Statements	42
Report of Independent Auditors	42
Management's Discussion and Analysis of Financial Condition and Results of Operations	43
Selected Quarterly Financial Data (unaudited)	53
Market Price of Common Stock and Related Matters	54
Selected Financial Data	54
Consolidated Five-Year Financial and Statistical Summary	55
Board of Directors	56
Corporate Information	Inside Back Cover

Senior Management Team

Robert W. Best
Chairman of the Board, President and Chief Executive Officer

Glen A. Blanscet
Vice President, General Counsel and Corporate Secretary

Larry J. Dagley
Executive Vice President and Chief Financial Officer

J. Charles Goodman
Executive Vice President, Utility Operations

Wynn D. McGregor
Vice President, Human Resources

Business Units

Thomas R. Blose, Jr.
President, United Cities Gas Company

Eugene A. Ehler
President, Energas Company (retiring January 1, 1999)

R. Earl Fischer
President, Energas Company (effective January 1, 1999)

Conrad E. Gruber
President, Western Kentucky Gas Company (effective January 1, 1999)

B.J. Hackler
President, Trans Louisiana Gas Company

Robert E. Mattingly
Vice President, New Business Ventures – Retail Services

Ron W. McDowell
Vice President, New Business Ventures

Gary L. Schlessman
President, Greeley Gas Company

Anthony W. Slayden
Vice President and General Manager, Atmos Propane, Inc.

Consolidated Balance Sheets

	September 30, 1998	September 30, 1997
	(In thousands, except share data)	
Assets		
Property, plant and equipment	$1,333,556	$1,301,004
Construction in progress	112,864	31,668
	1,446,420	1,332,672
Less accumulated depreciation and amortization	528,560	483,545
Net property, plant and equipment	917,860	849,127
Current assets		
Cash and cash equivalents	4,735	6,016
Accounts receivable, less allowance for doubtful accounts of $1,969 in 1998 and $2,188 in 1997	34,887	71,217
Inventories	15,219	12,333
Gas in storage	48,909	48,122
Prepayments	3,630	6,017
Total current assets	107,380	143,705
Deferred charges and other assets	116,150	95,479
	$1,141,390	$1,088,311
Capitalization and Liabilities		
Shareholders' equity		
Common stock, no par value (stated at $.005 per share); 75,000,000 shares authorized; issued and outstanding 1998 – 30,398,319 shares, 1997 – 29,642,437 shares	$ 152	$ 148
Additional paid-in capital	271,637	251,174
Retained earnings	99,369	75,938
Total shareholders' equity	371,158	327,260
Long-term debt	398,548	302,981
Total capitalization	769,706	630,241
Current liabilities		
Current maturities of long-term debt	57,783	15,201
Notes payable to banks	66,400	167,300
Accounts payable	44,742	62,626
Taxes payable	12,736	416
Customers' deposits	12,029	15,098
Other current liabilities	30,369	52,582
Total current liabilities	224,059	313,223
Deferred income taxes	80,213	87,828
Deferred credits and other liabilities	67,412	57,019
	$1,141,390	$1,088,311

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income

	Year ended September 30,		
	1998	1997	1996
	(In thousands, except per share data)		
Operating revenues	$ 848,208	$ 906,835	$ 886,691
Purchased gas cost	516,372	577,181	562,279
Gross profit	331,836	329,654	324,412
Operating expenses			
Operation	131,336	173,683	148,196
Maintenance	10,278	11,974	11,719
Depreciation and amortization	47,555	45,257	41,666
Taxes, other than income	29,788	32,131	30,254
Income taxes	31,806	14,298	23,316
Total operating expenses	250,763	277,343	255,151
Operating income	81,073	52,311	69,261
Other income (expense)			
Interest and investment income	5,430	5,410	3,867
Other, net	4,341	(288)	(300)
Total other income	9,771	5,122	3,567
Interest charges	35,579	33,595	31,677
Net income	$ 55,265	$ 23,838	$ 41,151
Basic net income per share	$ 1.85	$ .81	$ 1.42
Diluted net income per share	$ 1.84	$ .81	$ 1.42
Cash dividends per share	$ 1.06	$ 1.01	$ .98
Weighted average shares outstanding			
Basic	29,822	29,409	28,978
Diluted	30,031	29,422	28,994

See accompanying notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

	Common stock			
	Number of shares	Stated value	Additional paid-in capital	Retained earnings
	(In thousands, except share data)			
Balance, September 30, 1995	28,246,392	$141	$230,630	$73,578
Net income	-	-	-	41,151
Cash dividends ($.98 per share)	-	-	-	(28,478)
Common stock issued:				
Restricted stock grant plan	41,700	1	733	-
Direct stock purchase plans	251,224	1	4,322	-
ESOP	161,477	1	3,641	-
Long-term stock plan for United Cities Division	16,900	-	241	-
Outside directors stock-for-fee plan	3,389	-	76	-
Monarch Gas Co. acquisition	207,366	1	1,499	933
Oceana Heights acquisition	313,411	1	304	594
Other	-	-	212	-
Balance, September 30, 1996	29,241,859	146	241,658	87,778
Net income	-	-	-	23,838
Cash dividends ($1.01 per share)	-	-	-	(26,415)
Common stock issued:				
Restricted stock grant plan	100,000	1	2,443	-
Direct stock purchase plans	85,243	-	1,888	-
Outside directors stock-for-fee plan	3,008	-	72	-
ESOP/401(k) plans	212,327	1	5,113	-
Less: UCGC net income for the quarter ended December 31, 1996	-	-	-	(9,263)
Balance, September 30, 1997	29,642,437	148	251,174	75,938
Net income	-	-	-	55,265
Cash dividends ($1.06 per share)	-	-	-	(31,834)
Common stock issued:				
Restricted stock grant plan	114,250	1	2,898	-
Direct stock purchase plan	531,353	3	14,482	-
ESOP/401(k) plans	52,473	-	1,485	-
Long-term stock plan for United Cities Division	55,500	-	1,533	-
Outside directors stock-for-fee plan	2,306	-	65	-
Balance, September 30, 1998	30,398,319	$152	$271,637	$99,369

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

	Year ended September 30,		
	1998	1997	1996
		(In thousands)	
Cash flows from operating activities			
Net income	$ 55,265	$ 14,575	$ 41,151
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization:			
Charged to depreciation and amortization	47,555	39,970	41,666
Charged to other accounts	5,861	2,237	3,580
Deferred income taxes	(3,968)	5,807	7,585
Gain on sales of non-utility assets	(3,335)	-	-
Other	-	-	(1,866)
Changes in assets and liabilities:			
(Increase) decrease in accounts receivable	36,330	32,198	(12,697)
(Increase) decrease in inventories	(2,886)	1,562	(1,238)
Increase in gas in storage	(787)	(4,772)	(15,949)
(Increase) decrease in prepayments	2,387	(3,208)	1,966
Increase in deferred charges and other assets	(20,671)	(29,683)	(4,623)
Increase (decrease) in accounts payable	(17,884)	(17,695)	23,796
Increase (decrease) in taxes payable	8,673	(837)	7,099
Increase (decrease) in customers' deposits	(3,069)	(1,714)	592
Increase (decrease) in other current liabilities	(22,213)	28,716	(4,165)
Increase in deferred credits and other liabilities	10,393	1,593	4,836
Net cash provided by operating activities	91,651	68,749	91,733
Cash flows from investing activities			
Capital expenditures	(134,989)	(122,312)	(117,589)
Retirements of property, plant and equipment, net	178	1,189	5,708
Proceeds from sales of assets	15,997	-	-
Net cash used in investing activities	(118,814)	(121,123)	(111,881)
Cash flows from financing activities			
Net increase (decrease) in notes payable	(100,900)	38,812	62,675
Proceeds from issuance of long-term debt	154,445	40,000	-
Repayment of long-term debt	(16,296)	(14,659)	(20,734)
Cash dividends paid	(31,834)	(26,415)	(28,478)
Issuance of common stock	20,467	9,518	8,523
Net cash provided by financing activities	25,882	47,256	21,986
Net increase (decrease) in cash and cash equivalents	(1,281)	(5,118)	1,838
Cash and cash equivalents at beginning of year	6,016	11,134	9,296
Cash and cash equivalents at end of year	$ 4,735	$ 6,016	$ 11,134

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Contents of Notes to Consolidated Financial Statements

1 Summary of significant accounting policies 28
2 Business combinations 30
3 Rates 31
4 Income taxes 32
5 Contingencies 33
6 Leases 35
7 Long-term debt and notes payable 35
8 Statement of cash flows supplemental disclosures 36
9 Common stock and stock options 36
10 Employee retirement and stock ownership plans 38
11 Other postretirement benefits 39
12 Earnings per share 41
13 Related party transactions 41

1 Summary of significant accounting policies

Forward-Looking Statements These notes to consolidated financial statements, particularly notes 2, 5, 9, and 11 may contain "forward-looking statements" as discussed herein in Management's Discussion and Analysis of Financial Condition and Results of Operations under the heading, "Cautionary Statement for the Purposes of the Safe Harbor under the Private Securities Litigation Reform Act of 1995" and should be read in conjunction with such discussion.

Description of Business Atmos Energy Corporation and its subsidiaries ("Atmos" or the "Company") are engaged primarily in the natural gas utility business as well as certain non-utility businesses. The Company distributes through sales and transportation arrangements natural gas to approximately 1.0 million residential, commercial, industrial and agricultural customers through its five regulated utility divisions: Energas Company ("Energas Division") in Texas; Trans Louisiana Gas Company ("Trans La Division") in Louisiana; Western Kentucky Gas Company ("Western Kentucky Division") in Kentucky; Greeley Gas Company ("Greeley Division") in Colorado and Kansas; and United Cities Gas Company ("United Cities Division") in Illinois, Tennessee, Iowa, Virginia, Georgia, South Carolina, Kansas and Missouri. Such business is subject to federal and state regulation and/or regulation by local authorities in each of the twelve states in which the utility divisions operate.

Through United Cities Gas Storage Company ("Storage"), a non-regulated utility business, the Company also owns and operates natural gas storage fields in Kentucky and Kansas to supplement natural gas used by regulated customers in Tennessee, Kansas and Illinois and to provide storage services to other customers that may be in other states.

Through Atmos Propane, Inc. ("Propane"), a non-regulated utility business and a wholly-owned subsidiary of UCG Energy Corporation ("UCG Energy"), which is a wholly-owned subsidiary of Atmos, the Company is engaged in the retail distribution of propane (LP) gas, the wholesale supply and the transportation of LP gas, the transportation of certain products for other companies and the direct merchandising and repair of propane gas appliances. Propane currently has operation and storage centers and store front offices located in Tennessee, Kentucky, and North Carolina with a total company storage capacity of approximately 2.3 million gallons. As of September 30, 1998, Propane served approximately 37,400 customers.

Through UCG Energy's 45% interest in Woodward Marketing, L.L.C. ("WMLLC"), a limited liability company formed in Delaware and headquartered in Houston, Texas, the Company is engaged in gas marketing and energy management services. WMLLC provides gas marketing services to industrial customers, municipalities and local distribution companies, including the United Cities, Energas, Greeley, and Trans La Divisions. The Company utilizes equity accounting for its investment in WMLLC.

Finally, the Company, through UCG Energy, leases and rents appliances, real estate, equipment, and vehicles to the United Cities Division and others, and owns a small interest in a partnership engaged in exploration and production activities.

Principles of Consolidation The accompanying consolidated financial statements include the accounts of Atmos Energy Corporation and its subsidiaries. Each subsidiary is wholly owned and all material intercompany transactions have been eliminated.

Accounting for Unconsolidated Investments The Company accounts for its 45% interest in WMLLC, using the equity method of accounting for investments. Equity in pre-tax earnings of WMLLC included in the interest and investment income caption in the consolidated statement of income were $3.9 million, $3.3 million and $2.0 million in 1998, 1997 and 1996, respectively.

Restatement for Pooling of Interests The consolidated financial statements for all periods prior to July 31, 1997 have been restated for the pooling of interests of the Company with United Cities Gas Company. Certain changes in account classifications have been made to conform United Cities Gas Company's classifications to Atmos' presentation.

Regulation The Company's utility operations are subject to regulation with respect to rates, service, maintenance of accounting records and various other matters by the respective regulatory authorities in the states in which it operates. Atmos' accounting policies recognize the financial effects of the ratemaking and

accounting practices and policies of the various regulatory commissions. Regulated utility operations are accounted for in accordance with Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation." This statement requires cost-based rate regulated entities that meet certain criteria to reflect the authorized recovery of costs due to regulatory decisions in their financial statements.

The Company records regulatory assets which represent assets which are being recovered through customer rates or are probable of being recovered through customer rates. Significant regulatory assets as of September 30, 1998 included the following: unamortized debt expense of $5.6 million, merger and integration costs of $59.8 million, environmental costs of $4.0 million, and deferred cost of purchased gas proceeding of $1.1 million. Regulatory liabilities represent probable future reductions in revenues associated with amounts that are to be credited to customers through the ratemaking process. As of September 30, 1998, the Company had recorded a regulatory liability of $2.2 million for deferred income taxes.

Revenue Recognition Sales of natural gas are billed on a monthly cycle basis; however, the billing cycle periods for certain classes of customers do not necessarily coincide with accounting periods used for financial reporting purposes. The Company follows the revenue accrual method of accounting for natural gas revenues whereby revenues applicable to gas delivered to customers but not yet billed under the cycle billing method are estimated and accrued and the related costs are charged to expense. Estimated losses due to credit risk are reserved at the time revenue is recognized.

Utility Property, Plant and Equipment Utility property, plant and equipment is stated at original cost net of contributions in aid of construction. The cost of additions includes direct construction costs, payroll related costs (taxes, pensions and other fringe benefits), administrative and general costs, and the estimated cost of an allowance for funds used during construction (See AFUDC below). Major renewals and betterments are capitalized, while the costs of maintenance and repairs are charged to expense as incurred. The costs of large projects are accumulated in construction in progress until the project is completed. When the project is completed, tested and placed in service, the balance is transferred to the utility plant in service account, included in rate base and depreciation begins. As of September 30, 1998, the Company has invested approximately $80 million in its Customer Service Initiative ("CSI"). The CSI investment is currently recorded in construction in progress. CSI is a group of projects that are reorganizing processes throughout the Company to leverage technology and implement industry best practices. It is expected to be fully placed in service in 1999. Property, plant and equipment is depreciated at various rates on a straight-line basis over the estimated useful lives of the assets. The composite rates were 4.0% and 3.9% for the years ended September 30, 1998 and 1997, respectively. At the time property, plant and equipment is retired, the cost, plus removal expenses and less salvage, is charged to accumulated depreciation.

Allowance for Funds Used During Utility Construction ("AFUDC") AFUDC represents the estimated cost of funds used to finance the construction of major projects. Under regulatory practices, the costs are capitalized and included in rate base for ratemaking purposes when the completed projects are placed in service. Interest expense of $4.1 million, $1.2 million and $.4 million was capitalized in 1998, 1997 and 1996, respectively. The increased amounts in 1998 and 1997 were related to CSI.

Non-Utility Property, Plant and Equipment Balances are stated at cost and depreciation is computed generally on the straight-line method for financial reporting purposes.

Inventories Inventories consist primarily of materials and supplies and merchandise held for resale. These inventories are stated at the lower of average cost or market. Inventories also include propane inventories of $979,000 and $722,000 at September 30, 1998 and 1997, respectively. Propane is priced at average cost.

Gas in Storage Net additions of inventory gas to storage and withdrawals of inventory gas from storage are priced using the average cost method for all Atmos utility divisions, except for the United Cities Division, where it is priced on the first-in first-out method. Gas stored underground and owned by Storage is priced on the last-in first-out ("LIFO") method. In accordance with the United Cities Division's purchased gas adjustment ("PGA") clause, the liquidation of a LIFO layer would be reflected in subsequent gas adjustments in customer rates and does not affect the results of operations. Noncurrent gas in storage is classified as property, plant and equipment and is priced at cost.

Income Taxes The Company provides deferred income taxes for significant temporary differences in the recognition of revenues and expenses for tax and financial reporting purposes.

Cash and Cash Equivalents The Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Deferred Charges and Other Assets Deferred charges and other assets at September 30, 1998 and 1997 include merger and integration costs of $59.8 million and $49.0 million in 1998 and 1997, respectively; the related reserve for merger and integration costs of $20.3 million in both 1998 and 1997; and the investment in WMLLC of $11.9 million and $10.0 million in 1998 and 1997, respectively. Also included in deferred charges and other assets

are assets of the Company's qualified defined benefit retirement plans in excess of the plans' obligations, Company assets related to the nonqualified retirement plans, unamortized debt expense, and deferred compensation expense related to non-vested restricted stock grants.

Deferred Credits and Other Liabilities Deferred credits and other liabilities include customer advances for construction, obligations under capital leases, obligations under other postretirement benefits, and obligations under the Company's nonqualified retirement plans.

Earnings Per Share The calculation of basic earnings per share is based on income available to common stockholders divided by weighted average common shares outstanding. The calculation of diluted earnings per share is based on net income available to common stockholders divided by weighted average shares outstanding plus the dilutive shares related to the United Cities Division's Long-term Stock Plan and Atmos' Restricted Stock Grant Plan.

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

Recently Issued Accounting Standards Not Yet Adopted The Company has not yet adopted Statement of Financial Accounting Standards No. 130 "Reporting Comprehensive Income." The Statement will be effective for the Company's 1999 fiscal year. It establishes standards for reporting and display of comprehensive income and its components (revenues, expenses, gains, and losses) in a full set of general-purpose financial statements. Reclassification of financial statements for earlier periods provided for comparative purposes is required.

The Company has not yet adopted Statement of Financial Accounting Standards No. 131 "Disclosures about Segments of an Enterprise and Related Information." The Statement will be effective for the Company's 1999 fiscal year. It establishes standards for the way that public business enterprises report information about operating segments in annual financial statements and requires that those enterprises report selected information about operating segments in interim financial reports issued to shareholders. In the initial year of application, comparative information for earlier years is to be restated.

In addition, the Company has not yet adopted Statement of Financial Accounting Standards No. 133 "Accounting for Derivative Instruments and Hedging Activities." The Statement will be effective for the Company's fiscal year 2000. It establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. This Statement does not allow retroactive application to financial statements of prior periods.

The Company believes that adoption of these Statements will not have a material impact on its reported financial condition, results of operations, or cash flows.

2 Business combinations

On July 31, 1997, Atmos acquired by means of a merger all of the assets and liabilities of United Cities Gas Company ("UCGC") in accordance with the terms and provisions of an Agreement and Plan of Reorganization dated July 19, 1996 and amended October 3, 1996. A total of 13,320,221 shares of Atmos common stock were issued in a one-for-one exchange for all outstanding shares of UCGC common stock. UCGC was a natural gas utility company engaged in the distribution and sale of natural gas. At the time of the merger, UCGC served approximately 306,000 utility customers in Georgia, Illinois, Iowa, Kansas, Missouri, South Carolina, Tennessee, and Virginia, and approximately 29,000 propane customers in Kentucky, North Carolina, Tennessee, and Virginia. Its assets consisted of the property, plant and equipment used in its natural gas and propane sales and distribution businesses.

UCGC was merged with and into Atmos by means of a tax-free reorganization. The transaction was accounted for as a pooling of interests; therefore, historical financial statements for periods prior to the merger have been restated. UCGC prepared its financial statements on a December 31 fiscal year-end. UCGC's fiscal year has been changed to September 30 to conform to the Company's year end. The restated consolidated statements of income and cash flows for the year ended September 30, 1996 include Atmos operations for the year then ended and UCGC operations for the year ended December 31, 1996. The consolidated statement of income for the year ended September 30, 1997 includes Atmos and UCGC operations for the twelve months then ended. As a result, UCGC's operations for the three months ended December 31, 1996 (operating revenues of approximately $123.0 million and net income of $9.3 million) are included in both the 1997 and 1996 consolidated statements of income, and the UCGC net income for this period has been deducted in calculating the shareholders' equity balances at September 30, 1997 and cash flows for the year then ended. Certain account reclassifications were made to conform UCGC 's classifications to Atmos' presentation.

Following the merger, UCGC's business began operating as United Cities Gas Company, a division of Atmos ("United Cities Division") and integration of the companies began. The United Cities Division is structured like other divisions of Atmos. To achieve this structure, approximately 560 utility positions in the

United Cities Division were eliminated by September 1998. An additional 75 Atmos positions were eliminated as part of the integration, resulting in approximately 635 total position reductions in the combined Company by September 1998. Atmos also has initiated plans to enhance its customer service in Texas, Louisiana, Kentucky, Colorado, Kansas and Missouri through business process changes which resulted in a net reduction of approximately 240 positions. These changes include restructuring business office operations, establishing a network of payment centers and creating a customer support center, all part of the CSI project.

The Company has recorded as regulatory assets through September 30, 1998 the costs of the merger and integration of the United Cities Division, which amounted to $59.8 million. The Company believes there are substantial long term benefits to its customers and shareholders from the merger of the two companies, which are expected to result in operating cost savings over the next 10 years totaling approximately $375 million. The Company believes a significant amount of the costs to achieve these benefits will be recovered through rates and future operating efficiencies of the combined operations. Therefore, the merger and integration costs will be charged to operations concurrent with the benefits received. However, in the fourth quarter of fiscal 1997 the Company established a general reserve of approximately $20.3 million ($12.6 million after-tax), to account for costs that may not be recovered through rates.

The statements above concerning anticipated cost savings in the future constitute "forward-looking statements," as defined in the Private Securities Litigation Reform Act of 1995. Such forward-looking statements should be read in conjunction with the Company's disclosures under the heading "Cautionary Statement for the Purposes of the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995" at the beginning of Management's Discussion and Analysis.

Results of operations and net income for the previously separate companies for the periods prior to the merger are as follows:

	10 Months ended July 31, 1997 *(Unaudited)*	Year ended September 30, 1996
	(In thousands)	
Operating revenues:		
Atmos	$474,069	$483,744
UCGC	356,325	402,947
	$830,394	$886,691
Net income:		
Atmos	$ 23,079	$ 23,949
UCGC	19,434	17,202
	$ 42,513	$ 41,151
Dividends per share:		
Atmos	$ .75	$ .96
UCGC	$ .76	$ 1.02

3 Rates

As of September 30, 1998, the Company did not have any general rate cases currently pending. The Trans La Division does have a hearing scheduled before the Louisiana Public Service Commission in April 1999 for the Louisiana Commission to consider the Trans La Division rate of return. Rate proceedings completed during the three years ended September 30, 1998 are summarized as follows.

In September 1998, the Company and the staff of the Virginia State Corporation Commission presented a Stipulation and Settlement of issues to the Virginia State Corporation Commission. It was adopted effective October 1, 1998. The Stipulation and Settlement provided for a reduction of approximately $249,000 in annual gross revenues of the United Cities Division. This represents approximately a .2% reduction in the gross profit of the United Cities Division and less than .08% reduction in the consolidated gross profit of the Company.

In fiscal 1997, the Colorado Office of Consumer Counsel filed a complaint with the Colorado Public Utilities Commission ("Colorado Commission") requesting a $3.5 million reduction in the annual revenues in Colorado of the Greeley Division. On December 17, 1997, a hearing was held at the Colorado Commission presenting a Stipulation and Agreement reached by the Greeley Division and the Colorado Office of Consumer Counsel. It settled the Consumer Counsel's complaint against the Greeley Division for a $1.6 million reduction in annual revenues. The Stipulation and Agreement became effective in January 1998. The reduction decreased the annual gross profit of the Greeley Division by approximately 4% and the gross profit of the Company by approximately .5%.

On June 9, 1998, the Kentucky Public Service Commission issued an Order approving an Experimental Performance-Based Ratemaking ("PBR") mechanism related to gas procurement and gas transportation activities filed by the Western Kentucky Division. The PBR mechanism is incorporated into the Western Kentucky Division's Gas Cost Adjustment Clause.

The Georgia Public Service Commission and the Tennessee Regulatory Authority have approved Weather Normalization Adjustments ("WNA"). The WNAs, effective October through May each year in Georgia, and November through April each year in Tennessee, allow the United Cities Division to increase the base rate portion of customers' bills when weather is warmer than normal and decrease the base rate when weather is colder than normal. The net effect of the WNA was an increase/(decrease) in revenues of $.7 million, $2.6 million and $(2.6) million in 1998, 1997 and 1996, respectively.

In May 1996, the Company filed to increase revenues by approximately $7.7 million for a portion of its Energas Division service area, which includes approximately 200,000 customers inside the city limits of 67 cities in West Texas. All cities either approved, or took no action to reject, a settlement allowing a $5.3 million increase in annual revenues to be effective for bills rendered on or after November 1, 1996. In October 1996, the Company filed a rate request with the Railroad Commission of Texas to increase revenues by approximately $.5 million for the remaining 22,000 rural customers in West Texas. The rate request was approved and became effective in April 1997.

4 INCOME TAXES

The components of income tax expense for 1998, 1997 and 1996 are as follows:

	1998	1997	1996
	(In thousands)		
Current			
Federal	$31,694	$ 7,917	$13,641
State	4,503	1,000	2,515
Deferred			
Federal	(3,352)	4,807	7,024
State	(616)	1,000	561
Investment tax credits	(423)	(426)	(425)
	$31,806	$14,298	$23,316

Deferred income taxes reflect the tax effect of differences between the basis of assets and liabilities for book and tax purposes. The tax effect of temporary differences that give rise to significant components of the deferred tax liabilities and deferred tax assets at September 30, 1998 and 1997 are presented below:

	1998	1997
	(In thousands)	
Deferred tax assets:		
Costs expensed for book purposes and capitalized for tax purposes	$ 1,049	$ 641
Accruals not currently deductible for tax purposes	7,189	12,398
Customer advances	3,730	3,160
Nonqualified benefit plans	11,297	9,118
Postretirement benefits	10,093	5,757
Unamortized investment tax credit	1,427	1,723
Regulatory liabilities	3,175	3,117
Other, net	2,838	3,758
Total deferred tax assets	40,798	39,672
Deferred tax liabilities:		
Difference in net book value and net tax value of assets	(114,229)	(102,038)
Pension funding	(4,120)	(4,190)
Gas cost adjustment	8,943	(6,568)
Regulatory assets	(4,941)	(8,673)
Other, net	(6,664)	(6,031)
Total deferred tax liabilities	(121,011)	(127,500)
Net deferred tax liabilities	$ (80,213)	$ (87,828)
SFAS No. 109 deferred accounts for rate regulated entities (included in other deferred credits)	$ 13,475	$ 15,072

Reconciliations of the provisions for income taxes computed at the statutory rate to the reported provisions for income taxes for 1998, 1997 and 1996 are set forth below:

	1998	1997	1996
		(In thousands)	
Tax at statutory rate of 35%	$30,474	$13,348	$22,564
Common stock dividends deductible for tax reporting	(695)	(706)	(684)
State taxes	2,526	1,300	2,000
Other, net	(499)	356	(564)
Provision for income taxes	$31,806	$14,298	$23,316

5 CONTINGENCIES

Litigation

Trans La Division In November 1997, a jury in Plaquemine, Louisiana awarded Brian L. Heard General Contractor, Inc., ("Heard") a total of $177,929 in actual damages and $15 million in punitive damages resulting from a lawsuit by Heard against the Trans La Division, the successor in interest to Oceana Heights Gas Company, which the Company acquired in November 1995. The trial judge also awarded interest on the total judgment amount. The claims are for events that occurred prior to the time Atmos acquired Oceana Heights Gas Company. Heard claimed damages associated with delays he allegedly incurred in constructing a sewer system in Iberville Parish, Louisiana. Heard filed the suit against the Trans La Division and two other defendants, alleging that gas leaks had caused delays in Heard's completion of a sewer project, resulting in lost business opportunities for the contractor during 1994.

The jury awarded punitive damages under a prior Louisiana statute that allowed punitive damages to be awarded in cases involving hazardous substances, which, as defined in the statute, included natural gas. Although not retroactive, the Louisiana legislature repealed the statute in 1996. The Company has appealed the verdict and intends to aggressively pursue obtaining reversal of the judgment. However, the Company cannot assess, at this time, the likelihood of the judgment being reversed on appeal. The Company is in the process of reviewing its insurance coverage with respect to this case. To date, the insurance companies have denied coverage and one company has filed a declaratory action to determine its obligations under the policy. The Company does not expect the final outcome of this case to have a material adverse effect on the financial condition, the results of operations or the cash flows of the Company because in the Company's opinion, it is more likely than not that the amount of punitive damages ultimately awarded will be substantially reduced.

On March 15, 1991, suit was filed in the 15th Judicial District Court of Lafayette Parish, Louisiana, by the "Lafayette Daily Advertiser" and others against Trans Louisiana Gas Company ("Trans La Division"), Trans Louisiana Industrial Gas Company, Inc., a wholly owned subsidiary of the Company, and Louisiana Intrastate Gas Corporation and certain of its affiliates ("LIG"). LIG is the Company's primary supplier of natural gas in Louisiana and is not otherwise affiliated with the Company.

The plaintiffs purported to represent a class consisting of all residential and commercial gas customers in the Trans La Division's service area. Among other things, the lawsuit alleged that the defendants violated antitrust laws of the state of Louisiana by manipulating the cost-of-gas component of the Trans La Division's gas rate to the purported customer class, thereby causing such purported class members to pay a higher rate. The plaintiffs made no specific allegation of an amount of damages. The case was concluded on December 15, 1997 when the Court entered its final approval of the settlement whereby LIG made a payment of $10.3 million to the Trans La Division for the benefit of its customers in the form of credits to customers' bills during the period November 1997 through March 1998. The suit was dismissed with prejudice at the same fairness hearing on December 15, 1997.

Greeley Division In Colorado, the Greeley Division is a defendant in several lawsuits filed as a result of a fire in a building in Steamboat Springs, Colorado on February 3, 1994. The plaintiffs claim that the fire resulted from a leak in a severed gas service line owned by the Greeley Division. On January 12, 1996, the jury awarded the plaintiffs approximately $2.5 million in compensatory damages and approximately $2.5 million in punitive damages. The jury assessed the Company with liability for all of the damages awarded. The Company appealed the judgment to the Colorado Court of Appeals. On June 11, 1998, the Colorado Court of Appeals reversed the trial court verdict and ordered a new trial. The plaintiffs have appealed the case to the Colorado Supreme Court. The Company does not expect the final outcome of this case to have a material adverse effect on the financial condition, the results of operations or the cash flows of the Company because the Company believes it has adequate insurance and reserves to cover any damages that may ultimately be awarded.

Western Kentucky Division In March 1997, Western Kentucky Gas Company ("Western Kentucky Division") was named as a defendant in a lawsuit in the District Court in Danville, Kentucky, as a result of an explosion and fire at a residence in Danville, Kentucky on March 4, 1997. The plaintiffs, Lisa Benedict, et al, who were leasing the residence, suffered serious burns in the accident and alleged that the Western Kentucky Division was negligent in installing and servicing gas lines at the residence. In September 1998, the Company and the plaintiffs entered into a confidential settlement of all claims in this case and the case was dismissed. The majority of the settlement was paid by the Company's insurance carriers and the remainder borne by the Company and charged to the reserve for litigation losses.

From time to time, other claims are made and lawsuits are filed against the Company arising out of the ordinary business of the

Company. In the opinion of the Company's management, liabilities, if any, arising from these other claims and lawsuits are either covered by insurance, adequately reserved for by the Company or would not have a material adverse effect on the financial condition, results of operations, or cash flows of the Company.

Guarantees

The Company's wholly-owned subsidiary, UCG Energy, and Woodward Marketing, Inc. ("WMI"), sole members of WMLLC, act as guarantors of up to $12.5 million of balances outstanding under a $30 million bank credit facility for WMLLC. UCG Energy guarantees the payment of up to $5.6 million of borrowings under this facility. No balance was outstanding under this credit facility at September 30, 1998. UCG Energy and WMI also act as joint and several guarantors on certain accounts payable for gas purchases. UCG Energy has agreed to guarantee payables of WMLLC up to $40.0 million of natural gas purchases and transportation services from suppliers. WMLLC payable balances outstanding that were subject to these guarantees amounted to $8.5 million at September 30, 1998.

Environmental Matters

Atmos is the owner or previous owner of manufactured gas plant sites which were used to supply gas prior to availability of natural gas. The gas manufacturing process resulted in certain by-products and residual materials including coal tar. It was an acceptable and satisfactory process at the time such operations were being conducted. Under current environmental protection laws and regulations, the Company may be responsible for response actions with respect to such materials, if response actions are necessary.

The United Cities Division owns or owned former manufactured gas plant sites in Johnson City and Bristol, Tennessee, Hannibal, Missouri and Americus, Georgia. UCGC and the Tennessee Department of Environment and Conservation entered into a consent order effective January 23, 1997, for the purpose of facilitating the investigation, removal and remediation of the Johnson City site. UCGC began the implementation of the consent order in the first quarter of 1997.

The Company is unaware of any information which suggests that the Bristol site gives rise to a present health or environmental risk as a result of the manufactured gas process or that any response action will be necessary. The Tennessee Regulatory Authority granted UCGC permission to defer, until its next rate case, all costs incurred in Tennessee in connection with state and federally mandated environmental control requirements.

On July 22, 1998, Atmos entered into an Abatement Order on Consent with the Missouri Department of Natural Resources addressing the former manufactured gas plant located in Hannibal, Missouri. Atmos, through its United Cities Division, agreed in the order to perform a removal action, a subsequent site evaluation and to reimburse the response costs incurred by the state of Missouri in connection with the property. The removal action was conducted and completed in August 1998 and the site evaluation will be completed in 1999. The Company has requested an Accounting Authority Order from the Missouri Public Service Commission ("MSPC") that would authorize it to defer its response costs related to the Hannibal site. On July 7, 1998, the MPSC Staff recommended that the MPSC approve the application.

As of September 30, 1998, the Company had incurred and deferred for recovery $1.1 million including $258,000 related to an insurance recoverability study, and accrued and deferred for recovery an additional $750,000 associated with the preliminary survey and invasive study of the Johnson City, Hannibal and Bristol sites.

On December 16, 1997, the Company, through its United Cities Division, entered into a Settlement Agreement with two other responsible parties at the Americus, Georgia former manufactured gas plant site. UCGC was a former owner of the property. In the Settlement Agreement, the Company agreed to pay $250,000 to resolve its liability for response costs and property damages associated with the site. The Company has paid the $250,000. The agreement contains a covenant not to sue, an indemnification provision from the other parties and gives the other parties all responsibility for investigation and response actions at the site. On October 20, 1998, the Company filed a proposal with the Georgia Public Service Commission for recovery of this amount through a rate rider. In November 1998, the Commission approved recovery through the rate rider which will take affect December 1, 1998.

Atmos is currently conducting an investigation pursuant to a Consent Order between the Kansas Department of Health and Environment and UCGC. The Order provides for the investigation, and a possible response action, for mercury contamination at gas pipeline sites which utilize or formerly utilized mercury meter equipment in Kansas. As of September 30, 1998, the Company had identified approximately 720 sites where mercury may have been used and had incurred and deferred for recovery $100,000. In addition, based upon available current information, the Company accrued and deferred for recovery an additional $280,000 for the investigation of these sites. The Kansas Corporation Commission has authorized the Company to defer these costs and seek recovery in a future rate case.

The Company addresses other environmental matters from time to time in the regular and ordinary course of its business. Management expects that future expenditures related to response action at any site will be recovered through rates or insurance, or

shared among other potentially responsible parties. Therefore, the costs of responding to these sites are not expected to materially affect the results of operations, financial condition or cash flows of the Company.

6 Leases

The Company has entered into noncancelable operating leases for office and warehouse space used in its operations. The remaining lease terms range from one to 20 years and generally provide for the payment of taxes, insurance and maintenance by the lessee. The Company has also entered into capital leases for division offices and operating facilities. Net property, plant and equipment included amounts for capital leases of $3.2 million and $2.3 million at September 30, 1998 and 1997, respectively.

The related future minimum lease payments at September 30, 1998 were as follows:

	Capital leases	Operating leases
	(In thousands)	
1999	$ 735	$ 9,633
2000	735	9,199
2001	735	8,810
2002	735	8,679
2003	735	8,172
Thereafter	4,119	52,564
Total minimum lease payments	7,794	$97,057
Less amount representing interest	(4,215)	
Present value of net minimum lease payments	$3,579	

Consolidated lease and rental expense amounted to $9.2 million, $10.5 million and $9.7 million for fiscal 1998, 1997 and 1996, respectively. Rents for the regulated business are expensed and the Company receives rate treatment as a cost of service on a pay-as-you-go basis.

7 Long-term debt and notes payable

Long-term debt at September 30, 1998 and 1997 consisted of the following:

	1998	1997
	(In thousands)	
Unsecured 7.95% Senior Notes, due 2006, payable in annual installments of $1,000	$ 8,000	$ 9,000
Unsecured 9.57% Senior Notes, due 2006, payable in annual installments of $2,000	16,000	18,000
Unsecured 9.76% Senior Notes, due 2004, payable in annual installments of $3,000	21,000	24,000
Unsecured 11.2% Senior Notes, due 2002, payable in annual installments of $2,000	10,000	12,000
Unsecured 10% Notes, due 2011	2,303	2,303
Unsecured 6.09% Note, due November 1998	40,000	40,000
Unsecured 8.07% Senior Notes, due 2006, payable in annual installments of $4,000 beginning 2002	20,000	20,000
Unsecured 8.26% Senior Notes, due 2014, payable in annual installments of $1,818 beginning 2004	20,000	20,000
Unsecured 6.75% Debentures, due 2028	150,000	–
First Mortgage Bonds		
Series J, 9.40% due 2021	17,000	17,000
Series N, 8.69% due 2000	3,000	5,000
Series P, 10.43% due 2017	25,000	25,000
Series Q, 9.75% due 2020	20,000	20,000
Series R, 11.32% due 2004	12,860	15,000
Series T, 9.32% due 2021	18,000	18,000
Series U, 8.77% due 2022	20,000	20,000
Series V, 7.50% due 2007	10,000	10,000
Medium term notes		
Series A, 1995-1, 6.67%, due 2025	10,000	10,000
Series A, 1995-2, 6.27%, due 2010	10,000	10,000
Series A, 1995-3, 6.20%, due 2000	2,000	2,000
Rental property, propane and other term notes due in installments through 2013	21,168	20,879
Total long-term debt	456,331	318,182
Less current maturities	(57,783)	(15,201)
	$398,548	$302,981

In July 1998, the Company issued $150 million of 30-year 6.75% debentures. The proceeds were used to refinance short-term borrowings.

Most of the Senior Notes and First Mortgage Bonds contain provisions that allow the Company to prepay the outstanding balance in whole at any time, subject to a prepayment premium. The Senior Note agreements and First Mortgage Bond indentures

provide for certain cash flow requirements and restrictions on additional indebtedness, sale of assets and payment of dividends. Under the most restrictive of such covenants, cumulative cash dividends paid after December 31, 1988 may not exceed the sum of accumulated net income for periods after December 31, 1988 plus $15.0 million. At September 30, 1998, approximately $60.9 million of retained earnings was unrestricted.

As of September 30, 1998, all of the Greeley Division utility plant assets with a net book value of approximately $88.3 million are subject to a lien under the 9.4% Series J First Mortgage Bonds assumed by the Company in the acquisition of Greeley Gas Company. Also, substantially all of the United Cities Division utility plant assets, totaling approximately $324.7 million, are subject to a lien under the Indenture of Mortgage of the Series N through V First Mortgage Bonds.

Based on the borrowing rates currently available to the Company for debt with similar terms and remaining average maturities, the fair value of long-term debt at September 30, 1998 and 1997 is estimated, using discounted cash flow analysis, to be $489.0 million and $348.3 million, respectively. It is not currently advantageous for the Company to refinance its long-term debt because of costs of prepayment required in the various debt agreements.

Maturities of long-term debt at September 30, 1998 are as follows (in thousands):

1999	$ 57,783
2000	16,389
2001	17,934
2002	15,823
2003	22,745
Thereafter	325,657
	$ 456,331

Short-term debt

Committed Credit Facilities The Company has two short-term committed credit facilities. The committed lines are renewed or renegotiated at least annually. One short-term, unsecured credit facility from a group of eight banks is for $250 million. This facility expires in August 1999. No balance was outstanding under it at September 30, 1998. This facility requires a commitment fee of .06% on the unused portion. A second facility is for $12 million with a single bank. This facility expires March 31, 1999. It requires a commitment fee of .075% on the unused portion.

Uncommitted Credit Facilities The Company also has unsecured short-term uncommitted credit lines from three banks totaling $80 million, of which $25.6 million was unused as of September 30, 1998. These uncommitted lines expire at various dates from May through August 1999, and are renewed or renegotiated at least annually. The uncommitted lines have varying terms and the Company pays no fee for the availability of the lines. Borrowings under these lines are made on a when and as-available basis at the discretion of the banks. The weighted average interest rate on short-term borrowings outstanding was 6.2% and 6.1% at September 30, 1998 and 1997, respectively.

Commercial Paper Program The Company implemented a $250 million commercial paper program in October 1998. It is supported by the $250 million committed line of credit described above. The Company's commercial paper was rated A-2 by Standard and Poor's and P-2 by Moody's.

8 Statement of cash flows supplemental disclosures

Supplemental disclosures of cash flow information for 1998, 1997 and 1996 are presented below.

	1998	1997	1996
		(In thousands)	
Cash paid for			
Interest	$29,980	$25,216	$32,778
Income taxes	$25,598	$ 9,736	$14,562

9 Common stock and stock options

Shareholders' Rights Plan On November 12, 1997, the Board of Directors approved a new Rights Agreement to become effective upon the expiration of the then existing Rights Agreement on May 10, 1998. Under the Rights Agreement, each right ("Right") will entitle the holder thereof, until May 10, 2008 or the date of redemption the Rights, to buy two additional shares of Common Stock of the Company at the exercise price of $80.00, subject to adjustment. At no time will the Rights have any voting rights. The exercise price payable and the number of shares of Common Stock or other securities or property issuable upon exercise of the Rights are subject to adjustment from time to time to prevent dilution. At the date upon which the rights become separate from the Company's Common Stock (the "Distribution Date"), the Company will issue one right with each share of Common Stock that becomes outstanding so that all shares of Common Stock will have attached Rights. After the Distribution Date, the Company may issue Rights when it issues Common Stock if the Board deems such issuance to be necessary or appropriate.

The Rights will separate from the Common Stock and a Distribution Date will occur upon the occurrence of certain events specified in the Agreement, including but not limited to, the acquisition by certain persons of at least 10% of the beneficial ownership of the Company's Common Stock. The Rights have

certain anti-takeover effects and may cause substantial dilution to a person or entity that attempts to acquire the Company on terms not approved by the Board of Directors except pursuant to an offer conditioned upon a substantial number of Rights being acquired. The Rights should not interfere with any merger or other business combination approved by the Board of Directors because, prior to the time that the Rights become exercisable or transferable, the Rights may be redeemed by the Company at $.01 per Right.

Shares Issued Under Various Plans The following table presents the number of shares issued under various plans in 1998 and 1997, as well as the number of shares available for future issuance at September 30, 1998.

	Shares issued 1998	Shares issued 1997	Shares available for issuance at September 30, 1998
Restricted Stock Grant Plan	114,250	100,000	788,250
Employee Stock Ownership Plan	52,473	212,327	460,398
Direct Stock Purchase Plan	531,353	85,243	968,217
Outside Directors Stock-For-Fee Plan	2,306	3,008	42,379
United Cities Long-term Stock Plan	55,500	–	194,500

Restricted Stock Grant Plan The Company's Restricted Stock Grant Plan ("Plan") for management and key employees of the Company, which became effective October 1, 1987 and was amended and restated in November 1997, provides for awards of common stock that are subject to certain restrictions. The Plan is administered by the Board of Directors. The members of the Board who are not employees of the Company make the final determinations regarding participation in the Plan, awards under the Plan, and restrictions on the restricted stock awarded. The restricted stock may consist of previously issued shares purchased on the open market or shares issued directly from the Company. During 1998 the Company increased the number of shares of its common stock that may be issued under the plan by 650,000 shares. Compensation expense of $1,238,000, $437,000 and $795,000 was recognized in 1998, 1997 and 1996, respectively, in connection with the issuance of shares under the Plan.

Employee Stock Ownership Plan Atmos has an Employee Stock Ownership Plan ("ESOP") and the United Cities Division has a 401(k) savings plan, as discussed in Note 10. The ESOP will be amended effective January 1, 1999, as is more fully discussed in Note 10.

Direct Stock Purchase Plan The Company also has a Direct Stock Purchase Plan ("DSPP"). Participants in the DSPP may have all or part of their dividends reinvested at a 3% discount from market prices. DSPP participants may purchase additional shares of Company common stock as often as weekly with voluntary cash payments of at least $25, up to an annual maximum of $100,000.

Outside Directors Stock-For-Fee Plan In November 1994, the Board adopted the Outside Directors Stock-for-Fee Plan, which was approved by the shareholders of the Company in February 1995 and was amended and restated in November 1997. The plan permits non-employee directors to receive all or part of their annual retainer and meeting fees in stock rather than in cash.

United Cities Long-Term Stock Plan Prior to the UCGC merger, certain officers and key employees of UCGC were covered under UCGC's Long-term Stock Plan implemented in 1989. At the time of the UCGC merger on July 31, 1997, Atmos adopted this plan by registering a total of 250,000 shares of Atmos stock to be issued under the Long-term Stock Plan for the United Cities Division. Under this plan, incentive stock options, nonqualified stock options, stock appreciation rights, restricted stock or any combination thereof may be granted to officers and key employees of the United Cities Division. During 1998, 55,500 options and rights were exercised under the plan. At September 30, 1998, there were 26,500 options outstanding. No incentive stock options, nonqualified stock options, stock appreciation rights, or restricted stock have been granted under the plan since 1996.

In October 1995, the FASB issued Statement No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation." This statement establishes a fair-value-based method of accounting for employee stock options or similar equity instruments and encourages, but does not require, all companies to adopt that method of accounting for all of their employee stock compensation plans. SFAS 123 allows companies to continue to measure compensation cost for employee stock options or similar equity instruments using the intrinsic value method of accounting described in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." The Company has elected to continue using this method. Because of the limited nature of the Company's stock-based compensation plans, the effect of adoption of SFAS 123 would not materially impact reported earnings per share.

Long-Term Incentive Plan On August 12, 1998, the Board of Directors approved and adopted the 1998 Long-Term Incentive Plan (the "LTIP"), which became effective October 1, 1998, subject to the approval of the shareholders of the Company at the Annual Meeting of Shareholders on February 10, 1999. The LTIP represents a part of the Company's total rewards strategy, which the Company developed as a result of a study it conducted of all

employee, executive and non-employee director compensation and benefits. The LTIP is a comprehensive, long-term incentive compensation plan, providing for discretionary awards of incentive stock options, non-qualified stock options, stock appreciation rights, bonus stock, restricted stock and performance-based stock to help attract, retain, and reward employees and non-employee directors of the Company and its subsidiaries. The maximum aggregate number of shares that may by issued under the LTIP shall not exceed 1,500,000 shares of common stock.

10 EMPLOYEE RETIREMENT AND STOCK OWNERSHIP PLANS

In fiscal 1998, the Company adopted SFAS No. 132, "Employers Disclosures about Pensions and Other Postretirement Benefits." The Statement revises employers' disclosures about pension and other postretirement benefit plans. It does not change the measurement or recognition of those plans. Disclosures for earlier periods have been restated as required by SFAS No. 132.

Defined Benefit Plans As of September 30, 1998, the Company had four defined benefit pension plans, covering the Western Kentucky Division employees, the Greeley Division employees, the United Cities Division employees, and the fourth covering all other Atmos employees. The plans provide similar benefits to all employees. Prior to January 1, 1999, the benefits are based upon years of service and the highest paid five consecutive calendar years of compensation within the last 10 years of employment.

Effective January 1, 1999, the plans will be merged into the Western Kentucky Gas plan, and will be known as the Pension Account Plan which will cover all employees of the Company. Participants will have an opening account balance established for them as of January 1, 1999 equal to the present value of their respective accrued benefits under the pension plans as of December 31, 1998. The Pension Account Plan will credit an allocation to each participant's account at the end of each year according to a formula based on his age, service and total pay (excluding incentive pay).

The Pension Account Plan provides for an additional annual allocation based upon a participant's age as of January 1, 1999 for those participants who were participants in the prior pension plans. The plan will credit this additional allocation each year through December 31, 2008. In addition, at the end of each year, a participant's account will be credited with interest on the employee's prior year account balance. A special grandfather benefit also applies through December 31, 2008, for participants who will be at least age 50 as of January 1, 1999, and who were participants in one of the prior plans on December 31, 1998. Participants are fully vested in their account balances after five years of service and may choose to receive their account balances as a lump sum or an annuity. The obligations shown as of September 30, 1998 anticipate the changes which will be effective January 1, 1999.

The Company's funding policy is to contribute annually an amount in accordance with the requirements of the Employee Retirement Income Security Act of 1974. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

Supplemental Executive Benefits Plan The Company has a non-qualified Supplemental Executive Benefits Plan ("Supplemental Plan") which provides additional pension, disability and death benefits to the officers and certain other employees of the Company. The supplemental plan was amended and restated in November 1997. In addition, in August 1998, the Company adopted the Performance-Based Supplemental Executive Benefits Plan, which will cover all employees who become officers or business unit presidents after August 12, 1998.

The following table sets forth the combined total for the four defined benefit pension plans and the Supplemental Plan's funded status for 1998 and 1997:

	1998	1997
Change in benefit obligation:		
Benefit obligation at beginning of year	$247,948	$235,943
Service cost	5,761	6,124
Interest cost	17,901	16,054
Curtailments/Special termination benefits	(2,645)	4,557
Plan amendments	(14,041)	2,314
Actuarial (gain)/loss	15,028	(6,561)
Benefits paid	(14,937)	(10,483)
Benefit obligation at end of year	255,015	247,948
Change in plan assets:		
Fair value of plan assets at beginning of year	259,852	224,699
Actual return on plan assets	40,062	42,416
Employer contribution	1,731	3,219
Benefits paid	(14,937)	(10,482)
Fair value of plan assets at end of year	286,708	259,852
Funded status	31,693	11,904
Unrecognized transition asset	(294)	(414)
Unrecognized prior service cost	(524)	13,490
Unrecognized net (gain)/loss	(38,844)	(35,681)
Accrued pension cost (net amount recognized)	$ (7,969)	$ (10,701)

	1998	1997
Weighted average assumptions for end of year disclosure:		
Discount rate	7.0%	7.5%
Rate of compensation increase	4.0%	4.0%
Expected return on plan assets	9.0%	9.0%

The plan assets consist primarily of investments in common stocks, interest bearing securities and interests in commingled pension trust funds.

The projected benefit obligation, accumulated benefit obligation, and fair value of plan assets for the pension plan with accumulated benefit obligations in excess of plan assets were $36.8 million, $31.4 million, and none, respectively, as of September 30, 1998, and $30.8 million, $26.0 million, and none, respectively, as of September 30, 1997.

Net periodic pension cost for the combined pension benefit plans for 1998, 1997 and 1996 included the following components:

	1998	1997	1996
		(In thousands)	
Components of net periodic pension cost:			
Service cost	$ 5,761	$ 6,903	$ 6,786
Interest cost	17,901	17,234	16,288
Expected return on assets	(23,249)	(19,730)	(18,695)
Amortization of:			
Transition obligation/(asset)	(146)	(335)	(354)
Prior service cost	1,660	1,731	1,048
Actuarial (gain)/loss	(1,091)	390	279
Net periodic pension cost	836	6,193	5,352
Curtailment (gain)/loss and special termination benefits	(1,840)	4,758	56
Total pension cost accruals	$ (1,004)	$ 10,951	$ 5,408

Employee Stock Ownership Plan Atmos sponsors an ESOP for employees other than those in the United Cities Division. Full-time employees who have completed one year of service, as defined in the plan, are eligible to participate. Each participant enters into a salary reduction agreement with the Company pursuant to which the participant's salary is reduced by an amount not less than 2% nor more than 10%. Taxes on the amount by which the participant's salary is reduced are deferred pursuant to Section 401(k) of the Internal Revenue Code. The amount of the salary reduction is contributed by the Company to the ESOP for the account of the participant. The Company may make a matching contribution for the account of the participant in an amount determined each year by the Board of Directors, which amount must be at least equal to 25% of all or a portion of the participant's salary reduction. For the 1998 plan year, the Board of Directors elected to match 100% of each participant's salary reduction contribution up to 4% of the participant's salary. Matching contributions to the ESOP amounted to $1.8 million, $2.1 million, and $1.9 million for 1998, 1997 and 1996, respectively. The directors may also approve discretionary contributions, subject to the provisions of the Internal Revenue Code of 1986 and applicable regulations of the Internal Revenue Service. The Company recorded a charge of $1.5 million for a discretionary contribution in the year ended September 30, 1996. No discretionary contributions were made for 1997 and 1998. Company contributions to the plan are expensed as incurred. The Company's ESOP has been amended effective January 1, 1999 to provide for deferral of a portion of a participant's salary of up to 21%. In addition, among other changes to the ESOP as of January 1, 1999, participants will be provided with automatic matching contributions of 100% of each participant's salary reduction up to 4% of the participant's salary, and will be provided the option of taking out loans against their ESOP accounts, subject to certain restrictions.

401(k) savings plan The Company sponsors a 401(k) savings plan for the United Cities Division employees. The plan allows participants to make contributions toward retirement savings. Each participant may contribute up to 15% of qualified compensation. For employee contributions up to 6% of the participant's qualified compensation, the Company will contribute 30% of the employee's contribution. The Company may also contribute up to an additional 20% of the employee's contribution based on certain criteria specified in the plan. Effective January 1, 1995, any additional contribution made by the Company will be through the issuance of the Company's common stock. The Company contributed $648,000 for the year ended September 30, 1998, $694,000 for the nine months ended September 30, 1997, and $826,000 for the year ended December 31, 1996. This 401(k) savings plan will be merged into the ESOP effective January 1, 1999, and the United Cities Division employees will receive the same benefits as other Atmos employees.

11 Other postretirement benefits

Atmos sponsors two postretirement plans other than pensions. Each provides health care benefits to retired employees. One provides benefits to the United Cities Division retirees and the other provides medical benefits to all other retired Atmos employees.

Substantially all of the Company's employees become eligible

for these benefits if they reach retirement age while working for the Company and attain certain specified years of service. Although specific terms of the two plans are different, participant contributions are required under these plans.

Effective January 1, 1999, the United Cities plan will provide benefits to future retirees that are essentially the same as provided to other Atmos employees. The obligations as of September 30, 1998 anticipate this plan change.

The following table sets forth the combined total for the two postretirement plans other than pensions:

	1998	1997
	(In thousands)	
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 53,295	$ 46,801
Service cost	1,659	1,734
Interest cost	3,809	3,208
Plan participants' contributions	382	275
Curtailments/Special termination benefits	2,125	2,292
Plan amendments	1,888	2,427
Actuarial (gain)/loss	6,210	135
Benefits paid	(4,874)	(3,577)
Benefit obligation at end of year	64,494	53,295
Change in plan assets:		
Fair value of plan assets at beginning of year	5,614	4,642
Actual return on plan assets	295	249
Employer contribution	4,963	4,024
Plan participants' contribution	382	276
Benefits paid	(4,874)	(3,577)
Fair value of plan assets at end of year	6,380	5,614
Funded status	(58,114)	(47,681)
Unrecognized transition obligation	23,243	30,131
Unrecognized prior service cost	3,614	2,125
Unrecognized net loss	8,571	996
Accrued pension cost (net amount recognized)	$(22,686)	$(14,429)

	1998	1997
Weighted average assumptions for end of year disclosure:		
Discount rate	7.0%	7.5%
Rate of compensation increase	4.0%	4.0%
Expected return on plan assets	5.3%	5.3%
Initial trend rate	9.0%	7.5%
Ultimate trend rate	4.5%	5.0%
Number of years from initial to ultimate trend	6	3

Net periodic pension cost for the combined postretirement benefit plans for 1998, 1997 and 1996 included the following components:

	1998	1997	1996
		(In thousands)	
Components of net periodic pension cost:			
Service cost	$ 1,659	$ 1,772	$ 1,622
Interest cost	3,810	3,467	3,260
Expected return on assets	(235)	(225)	(196)
Amortization of:			
Transition obligation/(asset)	1,862	1,994	1,994
Prior service cost	269	202	–
Actuarial (gain)/loss	(58)	4	98
Net periodic pension cost	7,307	7,214	6,778
Curtailment (gain)/ loss and special termination benefits	5,915	3,043	–
Total pension cost accruals	$13,222	$10,257	$ 6,778

Assumed health care cost trend rates have a significant effect on the amounts reported for the plans. A one-percentage point change in assumed health care cost trend rates would have the following effects on the latest actuarial calculations:

	1 – Percentage Point Increase	1 – Percentage Point Decrease
	(In thousands)	
Effect on total of service and interest cost components	$ 504	$ (495)
Effect on postretirement benefit obligation	$6,890	$(5,828)

The Company is currently recovering other postretirement benefits ("OPEB") costs through its regulated rates under SFAS No. 106 accrual accounting in Colorado, Kansas, the majority of its Texas service area and in Kentucky (effective November 1, 1995). It receives rate treatment as a cost of service item for OPEB costs on the pay-as-you-go basis in Louisiana. OPEB costs have been specifically addressed in rate orders in each jurisdiction served by the United Cities Division or have been included in a rate case and not disallowed. However, the Company was required to recover the portion of the UCGC transition obligation applicable to Virginia operations over 40 years, rather than 20 years, as in other states. Management believes that accrual accounting in accordance with SFAS No. 106 is appropriate and will continue to seek rate recovery of accrual-based expenses in its ratemaking jurisdictions that have not yet approved the recovery of these expenses.

12 Earnings per share

In 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 128, Earnings per Share. Statement 128 replaced the previously reported primary and fully diluted earnings per share with basic and diluted earnings per share. Unlike primary earnings per share, basic earnings per share excludes any dilutive effects of options, warrants and convertible securities. Diluted earnings per share is very similar to the previously reported fully diluted earnings per share. Earnings per share amounts for all historical periods presented have been restated to conform to the Statement 128 requirements. Adoption of Statement 128 did not change the fully diluted earnings per share amounts for the years ended September 30, 1997 and 1996. Reconciliations of the numerators and denominators of the basic and diluted per-share computations for net income for 1998 are as follows:

	Income *(Numerator)*	Shares *(Denominator)*	Per-Share *Amount*
	(In thousands, except per share amounts)		
Basic EPS:			
Income available to common stockholders	$55,265	29,822	$ 1.85
Effect of dilutive securities:			
Restricted stock	–	199	
Stock options	–	10	
Diluted EPS:			
Income available to common stockholders and assumed conversions	$55,265	30,031	$ 1.84

13 Related party transactions

Included in purchased gas cost were purchases from WMLLC of $124.7 million, $103.0 million and $46.9 million in 1998, 1997, and 1996, respectively. Volumes purchased were 53.4 billion cubic feet ("Bcf"), 38.6 Bcf and 21.7 Bcf in 1998, 1997 and 1996, respectively. These purchases were made in a competitive open bidding process and reflect market prices. Average prices per thousand cubic feet ("Mcf") for gas purchased from WMLLC were $2.33, $2.67 and $2.17 in 1998, 1997 and 1996, respectively.

Management's Responsibility for Financial Statements

Management is responsible for the preparation, presentation and integrity of the financial statements and other financial information in this report. The accompanying financial statements have been prepared in accordance with generally accepted accounting principles, and include estimates and judgments made by management that were necessary to prepare the statements in accordance with such accounting principles.

The Company maintains a system of internal accounting controls designed to provide reasonable assurance that assets are safeguarded from loss and that transactions are executed and recorded in accordance with established procedures. The concept of reasonable assurance is based on the recognition that the cost of maintaining a system of internal accounting controls should not exceed related benefits. The system of internal accounting controls is supported by written policies and guidelines, internal auditing and the careful selection and training of qualified personnel.

The financial statements have been audited by the Company's independent auditors. Their audit was made in accordance with generally accepted auditing standards, as indicated in the Report of Independent Auditors, and included a review of the system of internal accounting controls and tests of transactions to the extent they considered necessary to carry out their responsibilities for the audit.

Management has considered the internal auditors' and the independent auditors' recommendations concerning the Company's system of internal control and has taken actions that are believed to be cost-effective in the circumstances to respond appropriately to these recommendations. The Audit Committee of the Board of Directors meets periodically with the internal auditors and the independent auditors to discuss the Company's internal accounting controls, auditing and financial reporting matters.

Report of Ernst & Young LLP, Independent Auditors

Board of Directors
Atmos Energy Corporation

We have audited the accompanying consolidated balance sheets of Atmos Energy Corporation at September 30, 1998 and 1997, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended September 30, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of United Cities Gas Company, wholly owned by Atmos Energy Corporation (see Note 2), which statements reflect total revenues of $402,947,000 for the year ended December 31, 1996. Those statements were audited by other auditors whose report has been furnished to us and our opinion, insofar as it relates to data included for United Cities Gas Company is based solely on the report of the other auditors.

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

In our opinion, based on our audits and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Atmos Energy Corporation at September 30, 1998 and 1997, and its consolidated results of operations and its cash flows for each of the three years in the period ended September 30, 1998 in conformity with generally accepted accounting principles.

Ernst & Young LLP

Dallas, Texas
November 10, 1998

Introduction This section provides management's discussion of Atmos Energy Corporation's ("the Company" or "Atmos") financial condition, cash flows and results of operations with specific information on liquidity, capital resources and results of operations. It includes management's interpretation of such financial results, the factors affecting these results, the major factors expected to affect future operating results, and future investment and financing plans. This discussion should be read in conjunction with the Company's consolidated financial statements and notes thereto.

Cautionary Statement for the Purposes of the Safe Harbor Under the Private Securities Litigation Reform Act of 1995

The matters discussed or incorporated by reference in this Annual Report may contain "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical facts included in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the notes to consolidated financial statements, regarding the Company's financial position, business strategy and plans and objectives of management of the Company for future operations, are forward-looking statements made in good faith by the Company and are intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. When used in this Report or in any of the Company's other documents or oral presentations, the words "anticipate," "expect," "estimate," "plans," "believes," "objective," "forecast," "goal" or similar words are intended to identify forward-looking statements. Such forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those expressed or implied in the statements relating to the Company's operations, markets, services, rates, recovery of costs, availability of gas supply, and other factors. These risks and uncertainties include, but are not limited to, national, regional and local economic and competitive conditions, regulatory and business trends and decisions, technological developments, Year 2000 issues, inflation rates, weather conditions, and other uncertainties, all of which are difficult to predict and many of which are beyond the control of the Company.

Accordingly, while the Company believes that the expectations reflected in the forward-looking statements are reasonable, there can be no assurance that such expectations will be realized or will approximate actual results.

Organization The Company distributes and sells natural gas through 1,004,532 meters in service areas located in Texas, Louisiana, Kentucky, Colorado, Kansas, Illinois, Tennessee, Iowa, Virginia, Georgia, South Carolina and Missouri. The Company also transports gas for others through parts of its distribution system. Its non-utility operations include a propane operation; a leasing and rental operation; and an energy services operation that includes storage, gas marketing, irrigation and energy services.

The Company's primary source of revenues, net income and cash flows is its utility business which is composed of five local distribution companies that are operated as divisions of Atmos. For additional information about these businesses, please see the "Description of Business" section of Note 1 in the accompanying notes to consolidated financial statements.

Each segment's contribution to net income is reflected in the table below:

	Year ended September 30,		
	1998	1997	1996
Utility	76.3 %	71.3 %	77.5%
Propane	(0.1)%	(.4)%	3.1%
Leasing / Rental	5.9 %	4.7 %	3.0%
Storage and Energy Services	17.9 %	24.4 %	16.4%
Total	100.0 %	100.0 %	100.0%

Acquisitions and Mergers The Company has expanded its customer base and sought to diversify the regulatory climates, weather patterns and local economic conditions to which it is subject through acquisitions in fiscal years 1997, 1994, 1987, and 1986. The Company plans to continue its acquisition strategy to add new customers and service areas for both natural gas and propane. It has an excellent track record of acquiring local distribution company ("LDC") operations and achieving synergies and benefits quickly, while preserving brand equity.

In addition to growing through acquisitions, the Company's strategy includes running the utility operations exceptionally well, increasing the size and market share of non-utility operations (gas marketing, related storage and energy services and propane) and developing plans to participate in retail services behind the meter.

Ratemaking Procedures The Company's five utility divisions are regulated by various state or local public utility authorities. The method of determining regulated rates varies among the 12 states in which the Company has utility operations. It is the responsibility of the regulators to determine that utilities under their jurisdiction operate in the best interests of customers while providing the utilities the opportunity to earn a reasonable return on investment.

In a general rate case, the applicable regulatory authority, which is typically the state public utility commission, establishes a base margin, which is the amount of revenue authorized to be collected from customers to recover authorized operating expense (other than the cost of gas), depreciation, interest, taxes

and return on rate base. The utility divisions perform annual deficiency studies for each rate jurisdiction to determine when to file rate cases, which are typically filed every two to five years.

Substantially all of the sales rates charged by the Company to its customers fluctuate with the cost of gas purchased by the Company. Rates established by regulatory authorities are adjusted for increases and decreases in the Company's purchased gas cost through automatic purchased gas adjustment mechanisms. Therefore, while the Company's operating revenues may fluctuate, gross profit (which is defined as operating revenues less purchased gas cost) is generally not eroded or enhanced because of gas cost increases or decreases.

The Georgia Commission and Tennessee Regulatory Authority have approved Weather Normalization Adjustments as discussed below under "Weather and Seasonality."

The Company received rate reductions of $1.8 million in 1998, and rate increases totaling $9.4 million in 1997, and $6.8 million in 1996. For further information regarding rate activity please see Note 3, "Rates," in notes to consolidated financial statements.

Weather and Seasonality The Company's natural gas and propane distribution businesses and irrigation sales business are seasonal due to weather conditions in the Company's service areas. Natural gas sales to residential, commercial, and public customers and propane sales are affected by winter heating season requirements. Sales to industrial customers are much less weather sensitive. Sales to agricultural customers (who use natural gas to power irrigation pumps) during the period from April through September are affected by rainfall amounts. These factors generally result in higher operating revenues and net income during the period from October through March of each year and lower operating revenues, and either net losses or lower net income during the period from April through September of each year. Degree day information is shown below. For further information regarding the impact of weather and seasonality on operating results, see the Supplementary Quarterly Financial Data following the notes to consolidated financial statements herein.

	Year ended September 30,		
	1998	1997	1996
Sales volumes – Bcf	159.4	164.2	178.3
Transportation volumes – Bcf	56.2	48.8	44.1
Total	215.6	213.0	222.4
Degree days:			
Actual	3,799	3,909	4,043
Normal	3,989	3,990	3,990
% of normal	95%	98%	101%

The Georgia Public Service Commission and the Tennessee Regulatory Authority have approved Weather Normalization Adjustments ("WNA"). The WNA, effective October through May each year in Georgia and November through April each year in Tennessee, allow the United Cities Division to increase the base rate portion of customers' bills when weather is warmer than normal and decrease the base rate when weather is colder than normal. The net effect of the WNA was an increase/(decrease) in revenues of $.7 million, $2.6 million and $(2.6) million in 1998, 1997 and 1996, respectively. Approximately 170,000 of the Company's customers are located in Georgia and Tennessee.

The Company has not sought weather normalization clauses in its other rate jurisdictions because of the effect of its geographical diversification strategy and the potential for increased profits in unusually cold years.

Year 2000 Issues

The Year 2000 issues arose because many computer systems and software applications as well as embedded computer chips in plant and equipment currently in use were constructed using an abbreviated date field that eliminates the first two digits of the year. On January 1, 2000, these systems, applications and embedded computer chips may incorrectly recognize the date as January 1, 1900. Accordingly, many computer systems and software applications, as well as embedded chips, may incorrectly process financial and operating information or fail to process such information completely. The Company recognized this problem and is addressing its potential effects on its computer systems, software applications and plant and equipment.

State of Readiness In October 1996, the Company established its Year 2000 Project Team with the mission of ensuring that all critical systems, facilities and processes are identified, analyzed for Year 2000 compliance, corrected if necessary, and tested if changes are necessary. The Year 2000 Project Team is headed by an officer of the Company and consists of representatives from all business units and shared services units of the Company. The Company, including all of its departments and business units, has a Year 2000 strategy in place and has begun the implementation of the Year 2000 plan to manage and minimize risks associated with the Year 2000 issues.

The Company has also obtained an assessment from an independent consulting firm, who specializes in such matters, of the risks posed for the Company and its business units by the Year 2000 issues, including an assessment of its risks in every area involving the use of computer technology and an assessment of the business and legal risks created for the Company by the Year 2000 issues. Such assessment also includes the risks associated with the Company's embedded technologies such as micro-con-

trollers or microchips embedded in non-information technology-related equipment.

With respect to information technology ("IT") systems, the Company has conducted an inventory of and is evaluating and reviewing its application software on all platforms such as the mainframe, local area network and personal computers. Concerning non-IT systems, including embedded technology, the Company has conducted an inventory of and is reviewing and evaluating all of its telecommunications, security access and building control systems, forms, reports and other business processes and activities as well as the equipment and facilities utilized in the Company's gas distribution and storage systems. In addition, several members of the Year 2000 Project Team have completed training on an American Gas Association-sponsored database relating to testing of embedded technology. This database will help expedite the review and compliance efforts related to embedded technology.

The Company's Year 2000 plan includes specific timetables for the following categories of tasks for each of its shared services units and business units with respect to both IT systems and embedded technology as follows:

- Identification of Year 2000 issues – substantially completed;
- Prioritization of Year 2000 issues – substantially completed;
- Estimation of total Year 2000-related costs – in process and to be completed by December 31, 1998;
- Implementation of Year 2000 solutions – in process and to be completed by May 31, 1999;
- Testing of Year 2000 solutions – in process and to be completed by September 30, 1999;
- Certification of Year 2000 compliance by third party vendors and suppliers – in process and to be completed by September 30, 1999;
- Monitoring of all systems for changes in current systems that would require changes in Year 2000 plan – in process and to be completed by September 30, 1999;
- Development of Year 2000 contingency plans – in process and to be completed by March 31, 1999; and
- Final Year 2000 tests – to be conducted starting September 30, 1999.

The Company is also currently in the process of conducting an inventory and review of computer systems provided by outside vendors. The Year 2000 Project Team is contacting all vendors to coordinate their Year 2000 compliance schedules with those of the Company. The Company is requiring vendors who provide mission critical goods or services to submit to the Company their compliance plans and to certify compliance in order to continue to do business with the Company. As discussed, the Company is also in the process of testing vendor products that provide mission critical goods or services to ensure their Year 2000 compliance. In addition, the Company has identified its key suppliers, including gas suppliers, and is communicating with them for the purpose of evaluating the status of their solutions to their respective Year 2000 issues. The expected date of completion of these procedures is September 30, 1999.

Costs to Address Year 2000 Issues As of September 30, 1998, the Company had incurred a total of less than $300,000 in fees and expenses in connection with its Year 2000 efforts. The Company currently expects to spend no more than $1.0 million directly on its Year 2000 efforts by December 31, 1999. As part of its normal systems upgrade in the ordinary course of business, the Company is in the process of replacing its customer information system, accounting and financial reporting system, and human resources system with systems that happen to be Year 2000 compliant. However, the installation of these systems was not accelerated in an attempt to deal with the Year 2000 issues.

Risks of Year 2000 Issues and Contingency Plans The Company has identified what it believes are its most significant worst case Year 2000 scenarios. These scenarios are (i) interference with the Company's ability to receive and deliver gas to customers; (ii) interference with the Company's ability to communicate with customers; and (iii) the temporary inability to send invoices to and receive payments from customers.

The most likely primary business risk associated with the Year 2000 issues is the Company's ability to continue to transport and distribute gas to its customers without interruption. In the event the Company and/or its suppliers and vendors are unable to remediate the Year 2000 issues prior to January 1, 2000, operations of the Company could be significantly impacted. In order to mitigate this risk, the Company is developing a contingency plan to continue operations through manual intervention and other procedures should it become necessary to do so. Such procedures are expected to include back-up power supply for its critical distribution and storage operations and, if necessary, curtailment of supply. The Company's storage capacity could be used to supplement system supply in the event its suppliers can not make deliveries. The Company expects to complete its operational contingency plan by March 31, 1999.

With respect to the communications with customers, which is heavily reliant on services provided by third parties, the Company is in the process of evaluating Year 2000 compliance by such third parties and will be developing contingency plans to address any worst case scenarios that may be determined after such evaluations are complete. Concerning the billing and payment systems, as previously discussed, the Company is in the process of replacing

its customer information system, accounting and financial reporting system, and human resources system with systems that are Year 2000 compliant, which should substantially diminish the risk of Year 2000 issues. Nevertheless, the Company will be developing contingency plans by March 31, 1999 in case the billing and payment systems prove not to be Year 2000 compliant.

Despite the Company's efforts, there can be no assurance that all material risks associated with Year 2000 issues relating to systems within its control will have been adequately identified and corrected before the end of 1999. However, as the result of its Year 2000 plan and the replacement of the customer information system, accounting and financial reporting system, and human resources system in 1999, the Company does not believe that in the aggregate, Year 2000 issues with respect to both its own IT and non-IT systems will be material to its business, operations or financial condition. On the other hand, while the Company is in the process of researching the Year 2000 readiness of its suppliers and vendors, the Company can make no representation regarding the Year 2000 compliance status of systems or parties outside its control, and currently cannot assess the effect on it of any non-compliance by such systems or parties.

All statements concerning Year 2000 issues other than historical statements, including, without limitation, estimated costs and the projected timetable of Year 2000 compliance, constitute "forward-looking statements," as defined in the Private Securities Litigation Reform Act of 1995. Such forward-looking statements should be read in conjunction with the Company's disclosures under the heading "Cautionary Statement for the Purposes of the Safe Harbor under the Private Securities Litigation Reform Act of 1995" at the beginning of Management's Discussion and Analysis.

Environmental Matters The Company is involved in certain environmental matters as discussed in Note 5 "Contingencies" of notes to consolidated financial statements.

Results of Operations

Year ended September 30, 1998 compared with year ended September 30, 1997

To assist in management's discussion of results of operations, the following table presents the effects of certain non-recurring charges and weather on reported consolidated net income. Earnings per share amounts presented in this discussion are on a diluted basis.

	Year ended September 30,					
	1998		1997		1996	
	Amount	Per Share	Amount	Per Share	Amount	Per Share
	(In thousands, except per share data)					
Net income as reported	$55,265	$1.84	$23,838	$ .81	$41,151	$1.42
Non-recurring charges:						
Management reorganization	–	–	2,800	.10	–	–
Reserve for integration costs	–	–	12,630	.43	–	–
Sale of assets	(2,244)	(.07)	–	–	–	–
Normalized net income except for effects of weather	53,021	1.77	39,268	1.34	41,151	1.42
Effects of weather	3,485	.11	3,571	.12	(1,838)	(.06)
Normalized net income	$56,506	$1.88	$42,839	$1.46	$39,313	$1.36

Net Income as Reported For the fiscal year ended September 30, 1998, the Company reported net income of $55.3 million, or $1.84 per diluted share, on operating revenues of $848.2 million. The 1998 net income includes one-time gains totaling $2.2 million or $.07 per diluted share, from the sales of real estate and equipment owned by UCG Energy. Although revenues for 1998 were lower as a result of winter weather that was 5% warmer than normal, as well as warmer than last year, earnings improved due to gains on asset sales, lower operation and maintenance expenses and increased irrigation sales. Operations and maintenance expenses were lower for 1998 due to a company-wide restructuring of the organization and Atmos' integration of United Cities Gas Company. Sales of gas in Texas to farmers for fueling irrigation pumps increased due to hot and dry summer weather in 1998. Irrigation volumes increased 34% in 1998 compared with 1997. Utility operations contributed about 76% of 1998 net income, with non-utility operations generating about 24%.

For the fiscal year ended September 30, 1997, the Company reported net income of $23.8 million, or $.81 per share, on operating revenues of $906.8 million. The 1997 net income included the effects of non-recurring after-tax charges related to management

reorganization ($2.8 million or $.10 per share) and reserves related to the UCGC merger and integration ($12.6 million or $.43 per share). Excluding the effect of these charges, the Company's net income would have been $39.3 million or $1.34 per share in 1997, compared with $41.2 million, or $1.42 per share for 1996. The 1997 results include UCGC, which merged with Atmos effective July 31, 1997, and operating results for years prior to the merger have been restated to reflect the pooling of interests accounting which was used for the merger.

Non-Recurring Charges In 1998 the Company sold the office building in which UCGC had headquartered its operation in Brentwood, Tennessee; two office buildings and a piece of land in Franklin, Tennessee UCGC had held for investment; and an airplane. The Company realized a pre-tax gain on the sale of assets totaling $3.3 million or $2.2 million after-tax.

In 1997 the Company completed a management reorganization and recorded a charge of $4.4 million ($2.8 million after-tax) in related costs.

In connection with the UCGC merger and integration in 1997, the Company recorded approximately $17 million of transaction costs and $42.8 million for separation and other costs. There are substantial longer term benefits to the Company's customers and shareholders from the merger of the two companies, which the Company expects to result in cost savings over the next 10 years totaling about $375 million. The Company believes a significant amount of the costs to achieve these benefits will be recovered through rates and future operating efficiencies of the combined operations. Therefore, the Company recorded as regulatory assets the costs of the merger and integration of UCGC. However, the Company established a reserve of $20.3 million ($12.6 million after-tax), to account for costs that may not be recovered. For further information regarding the merger please see Note 2 of notes to consolidated financial statements.

The statements in the preceding paragraph relating to the anticipated cost savings over the next 10 years constitute "forward-looking statements." Such forward-looking statements should be read in conjunction with the Company's disclosures under the heading "Cautionary Statement for the Purposes of the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995" at the beginning of Management's Discussion and Analysis.

Net Income by Segment As previously discussed, the Company currently has four business segments: utility operations, propane operations, leasing/rental operations, and storage and energy services including the Company's 45% interest in WMLLC.

The following table sets forth the net income (loss) of each of these business operations for the years 1998, 1997 and 1996.

	Year ended September 30,		
	1998	1997	1996
	(In thousands)		
Utility	$42,147	$16,991	$31,905
Propane	(66)	(90)	1,276
Leasing/Rental	3,272	1,117	1,237
Storage and Energy Services	9,912	5,820	6,733
Reported net income	$55,265	$23,838	$41,151

Results of Utility Operations Key financial and operating data for the Company's utility operations are highlighted in the following table.

	Year ended September 30,		
	1998	1997	1996
	(Dollars in thousands)		
Financial			
Operating revenues	$744,652	$811,537	$778,208
Purchased gas cost	444,288	510,943	488,575
Gross profit	300,364	300,594	289,633
Operating expenses	225,933	253,997	229,158
Other income	901	846	429
Interest charges	33,185	30,452	28,999
Net income	$ 42,147	$ 16,991	$ 31,905
Operating			
Sales volumes (MMcf):			
Residential	73,472	75,215	77,001
Commercial	36,083	37,382	38,247
Public authority and other	4,937	5,195	5,182
Industrial and irrigation	24,057	29,452	34,898
Total	138,549	147,244	155,328
Transportation (MMcf)	56,224	48,800	44,146
Total volumes (MMcf)	194,773	196,044	199,474
Meters in service, end of year	1,004,532	985,448	976,308
Average gas sales price/Mcf	$ 5.37	$ 5.51	$ 5.01
Average cost of gas/Mcf	$ 3.21	$ 3.47	$ 3.15
Average transportation revenue/Mcf	$ .43	$ .41	$ .43

Year ended September 30, 1998 compared with year ended September 30, 1997

Utility operating revenues decreased 8% to $744.7 million for 1998 from $811.5 million for 1997 due to lower total volumes delivered and a lower average sales price per Mcf. The lower total volumes delivered resulted from weather that was 3% warmer than 1997 and 5% warmer than 30-year normals. Sales volumes and revenues were also reduced by certain industrial customers switching

from sales service to transportation service. Gross profits are not significantly affected by such switching. Gross profit was basically unchanged at $300.4 million for 1998 as compared with 1997.

Operating expenses, excluding income taxes, decreased $42.0 million for 1998 as compared with 1997 due to a $20.3 million reserve for integration included in 1997, and a $21.7 million reduction in 1998 operating expenses due to the company-wide reorganization related to the Customer Service Initiative ("CSI") and UCGC integration. CSI is composed of a combination of enhancements including a customer call center, a new customer information system on client server architecture, mobile data terminals, ITRON electronic meter reading technology, a network of third party payment centers, and implementation of industry best practices. Interest charges increased 9% to $33.2 million due to an increased level of debt in 1998 as compared with 1997.

Year ended September 30, 1997 compared with year ended September 30, 1996

Operating revenues increased approximately 4% to $811.5 million in 1997 from $778.2 million in 1996 due to an increase of 10% in the average sales price per thousand cubic feet ("Mcf") of gas sold, which more than offset a 5% decrease in total volumes delivered. The increase in sales price reflects an increase in the commodity cost of gas which is passed through to end users and rate increases implemented in 1996 and 1997. Average gas sales revenues per Mcf increased by $.50 to $5.51 in 1997, while the average cost of gas per Mcf sold increased $.32 to $3.47 in 1997. Sales to weather sensitive residential, commercial and public authority customers decreased approximately 2.6 billion cubic feet ("Bcf") in 1997 while sales and transportation volumes delivered to industrial and agricultural customers decreased approximately 0.8 Bcf. Total sales and transportation volumes delivered decreased 2% to 196.0 Bcf in 1997, as compared with 199.5 Bcf in 1996. The decrease was primarily due to lower demand as a result of 3% warmer weather in 1997 than in 1996.

Gross profit increased by approximately 4% to $300.6 million in 1997 from $289.6 million in 1996. The primary factor contributing to the higher gross profit was annual rate increases totaling approximately $16.2 million implemented in fiscal 1997 and 1996 in Texas, Kentucky, Tennessee, Iowa, Missouri, Georgia, and Illinois. This was partially offset by a decrease in sales volumes of 8.1 Bcf or 5% due to the effect of warmer than normal weather and switching of certain industrial customers from sales service to transportation service. Operating expenses increased $24.9 million or 11% to $254.0 million in 1997. The increase in operating expenses was due primarily to the non-recurring $20.3 million reserve for merger and integration costs, and the $4.4 million charge for management reorganization. The $3.3 million increase in depreciation was due to utility plant additions placed in service in 1996 and 1997.

Effects of Weather Annual sales volumes and revenues vary in relation to winter heating degree days and summer irrigation demand. The Company has weather normalization adjustments in its rates in Georgia and Tennessee, but not in the other 10 states in which it has natural gas distribution operations. The estimated effect on net income of weather different from 30-year normals is included in the normalized income statement presented at the beginning of Management's Discussion and Analysis. The decline in net income, excluding the charges and reserves, was the result of the effects of warmer than normal weather during the winter months, which negatively impacted gas throughput and sales. Normal weather conditions would have added $.11 per share to net income in 1998 and $.12 per share to net income in 1997.

Rates The Company received rate increases totaling $9.4 million and $6.8 million in fiscal 1997 and 1996, respectively, in jurisdictions in Texas, Kentucky, Illinois, Georgia, Iowa, Tennessee, Missouri and Virginia. Weather normalization adjustments in Georgia and Tennessee contributed approximately $.7 million to gross profit in 1998, $2.6 million in 1997, and a reduction of $2.6 million in 1996. The Company received rate reductions totaling approximately $1.8 million in Colorado and Virginia in fiscal 1998.

Results of Propane Operations Key financial and operating data for the propane operations are presented in the following table.

	Year ended September 30, 1998	1997	1996
	(Dollars in thousands)		
Financial Data:			
Operating revenues	$29,091	$33,194	$38,372
Purchased gas cost	17,709	21,193	24,858
Gross profit	11,382	12,001	13,514
Operating expenses	10,725	11,508	11,766
Other income	72	159	223
Interest charges	795	742	695
Net income (loss)	$ (66)	$ (90)	$ 1,276
Operating Data:			
Propane heating degree days:			
Actual	3,799	3,847	4,258
% of normal	94%	96%	108%
Sales volumes (000 gallons):			
Retail	17,229	17,145	19,724
Wholesale	16,447	15,830	20,999
Total	33,676	32,975	40,723
Average selling price/gallon:			
Retail	$ 1.02	$ 1.12	$ 1.09
Wholesale	$ .51	$ .65	$ .63
Average cost of propane/gallon	$ .53	$ .65	$ .61
Customers, end of year	37,400	29,097	26,108

Year ended September 30, 1998, compared with year ended September 30, 1997

Revenues from propane operations decreased from $33.2 million in 1997 to $29.1 million in 1998 primarily due to the decreased selling price per gallon to retail and wholesale customers. This decreased selling price was the result of the lower demand because of warmer weather and increased competition for customers as compared to the prior year. Partially offsetting this decrease was an increase in total gallon sales. The increase in volumes sold resulted from the acquisitions of Ingas, Inc. in May 1998, Harris Propane Gas Co., Inc. in July 1998, Massey Propane Gas Company and E-con Gas, Inc. in August 1998 and Shaw LP Gas, Inc. in September 1998.

Purchased gas cost decreased from $21.2 million in 1997 to $17.7 million in 1998 primarily due to the decreased market cost of propane to the Company amounting to approximately $.12 per gallon. Partially offsetting this decrease was increased retail and wholesale gallon sales in 1998 as compared to 1997.

Operating expenses decreased from $11.5 million in 1997 to $10.7 million in 1998 primarily due to decreased administrative and general expenses due to control of operating expenses during 1998. Partially offsetting this decrease was an increase in depreciation and amortization expense from $2.1 million in 1997 to $2.3 million in 1998 due to the acquisitions in 1997 and in 1998, and depreciation on additional plant placed in service.

Interest expense increased from $.74 million in 1997 to $.80 million in 1998 due to increased short-term borrowings and long-term interest payments associated with the acquisitions in 1998, as well as increased short-term borrowings to cover cash flow deficits from decreased sales.

Net loss from propane operations decreased from $90,000 in 1997 to $66,000 in 1998, due primarily to the favorable operating expense variances discussed above. The Company is committed to substantially improving the profitability of its propane operations. To that end, the Company plans to exit the less profitable propane transportation, cylinder exchange, and appliance sales and service segments in 1999.

Year ended September 30, 1997 compared with year ended September 30, 1996

Propane revenues decreased $5.2 million from $38.4 million in 1996 to $33.2 million in 1997 primarily due to decreased retail and wholesale volumes sold as a result of warmer than normal weather. The weather in 1997 was 4% warmer than normal, compared to 8% colder than normal in 1996. Partially offsetting the decrease in volumes sold was an increase in the average selling price per gallon in 1997.

Purchased gas cost decreased $3.7 million from $24.9 million in 1996 to $21.2 million 1997 due primarily to decreased propane volumes sold as a result of warmer than normal weather. This decrease was partially offset by an increase in wholesale cost per gallon of $.04 per gallon from $.61 per gallon in 1996 to $.65 per gallon in 1997.

Operating expenses decreased $.3 million from $11.8 million in 1996 to $11.5 million in 1997 due primarily to a decrease in income tax expense of $.9 million, which was partially offset by increased administrative and general expenses due to the acquisitions of Harlan LP Gas, Inc. and Propane Sales and Services, Inc. in 1997. Additionally, depreciation and amortization expense increased from $1.9 million in 1996 to $2.1 million in 1997. This increase was due primarily to the acquisitions, and increased depreciation expense on additional plant and equipment placed in service.

Interest expense increased from $.7 million in 1996 to $.74 million in 1997 due to increased short-term borrowings and long-term interest payments associated with the acquisitions in 1997, as well as increased short-term borrowings to cover cash flow deficits from decreased sales.

Net income from propane operations decreased from $1.3 million in 1996 to a net loss of $90,000 in 1997, due primarily to warmer than normal weather. The decrease in gross profit of $1.5 million more than offset the decrease in operating expenses of $.3 million, resulting in 1997 being less profitable when compared to 1996.

Effects of Weather Like the utility operations, annual sales volumes and revenues of the propane operation vary in relation to winter heating degree days. The table above presents data for propane heating degree days, propane volumes delivered and profitability of the propane business for 1998, 1997 and 1996.

Gas Storage and Energy Services This segment is currently composed of four parts: United Cities Gas Storage Company, which owns underground storage fields in Kansas and Kentucky and provides storage services to the United Cities Division and other non-regulated customers; EnerMart, Inc. and EGASCO, which market gas to industrial and irrigation customers in West Texas; Atmos Energy Services, which is developing plans for marketing various non-regulated services and products; and the Company's 45% investment in WMLLC, a gas marketing and energy management services business.

Key financial data for the storage and energy services segment are set forth below.

	Year ended September 30,		
	1998	1997	1996
		(In thousands)	
Operating revenues	$70,488	$58,099	$65,907
Purchased gas cost	54,375	45,045	48,846
Gross profit	16,113	13,054	17,061
Operating expense	10,357	9,230	11,509
Other income	1,418	358	432
Equity in WMLLC	3,920	3,254	1,997
Interest charges	1,182	1,616	1,248
Net income	$ 9,912	$ 5,820	$ 6,733

Year ended September 30, 1998 compared with year ended September 30, 1997

Operating revenues increased 21% from $58.1 million for 1997 to $70.5 million for 1998 due to increases of $10.7 million in non-regulated West Texas irrigation and industrial revenues, and $1.7 million for gas storage operations. The increase in irrigation and industrial revenues was primarily due to hotter and drier than normal weather in West Texas. The increase in storage revenues was due to increased volumes withdrawn from underground storage in 1998 as compared with 1997. Like the utility and propane operations, gas storage volumes and revenues vary in relation to winter heating degree days.

Operating expenses increased $1.1 million in 1998 as compared with 1997 due primarily to the increased volumes delivered to West Texas irrigation customers and storage customers in Kansas and Tennessee.

Other income increased to $1.4 million for 1998 as compared with $.4 million for 1997. The increase was primarily due to gas brokering and utilization of storage capacity in excess of that dedicated to regulated markets to serve certain non-regulated markets.

Interest charges decreased $.4 million in 1998 as compared with 1997 due primarily to reduced debt balances in EnerMart Inc., the Company's wholly-owned subsidiary that conducts non-regulated utility operations in West Texas.

Net income for 1998 increased by $4.1 million from 1997 primarily due to increased West Texas irrigation revenues, favorable returns from its 45% investment in WMLLC, increased other income from non-regulated storage services and gas brokering, and a reduction in interest expense.

Year ended September 30, 1997 compared with year ended September 30, 1996

Operating revenues decreased 12% from $65.9 million in 1996 to $58.1 million in 1997 due primarily to decreased West Texas non-regulated irrigation and industrial revenues. The decrease in irrigation revenues was due to increased rainfall and cooler summer temperatures in West Texas. Storage revenues also decreased due to decreased volumes withdrawn from underground storage as a result of warmer than normal winter weather in Kansas and Tennessee.

Operating expenses decreased $2.3 million due primarily to decreased irrigation volumes in West Texas and storage withdrawals in Kansas and Tennessee.

Interest charges increased $.4 million due primarily to increased short-term debt due to lower cash flows and revenues from irrigation and storage operations in 1997 as compared with 1996.

Net income decreased to $5.8 million in 1997 as compared with $6.7 million in 1996. The primary factor causing the decreased net income was a $7.1 million decrease in West Texas irrigation revenues in 1997 as discussed above.

Equity in Earnings of WMLLC The Company accounts for its 45% investment in WMLLC through UCG Energy using the equity method of accounting. Against the 45% of the net income before tax recorded in the WMLLC financial statements, the Company records the amortization of the excess of the purchase price over the value of the net tangible assets, amounting to approximately $5.4 million which was allocated to intangible assets consisting of customer contracts and goodwill, and are being amortized over ten and twenty years, respectively, as well as the provision for income taxes.

The following table presents the WMLLC financial results recorded by Atmos for the years ended September 30, 1998, 1997 and 1996. WMLLC has a calendar year for financial reporting purposes.

	Year ended September 30,		
	1998	1997	1996
		(In thousands)	
WMLLC net income	$8,711	$7,231	$4,438
Atmos share @ 45%	3,920	3,254	1,997
Less:			
Amortization of excess purchase price	400	359	352
Provision for taxes	1,337	1,100	625
Atmos equity in WMLLC earnings	$2,183	$1,795	$1,020

The net income of WMLLC increased from $4.4 million for 1996, to $7.2 million for 1997, to $8.7 million for 1998, due to growth in number of customers and gas marketing revenues each year. Gross brokerage profit increased approximately 48% in 1998

as compared with 1997 due to increases in both sales volumes and margins, due primarily to customer growth. The Company's equity investment in WMLLC has grown from $5.8 million in 1995 to $11.9 million at September 30, 1998.

Leasing and Rental Operations Key financial and operating data for the leasing and rental operations are presented in the following table.

	Year ended September 30, 1998	1997	1996
	(In thousands)		
Operating revenues	$3,977	$4,005	$4,204
Operating expenses	3,748	2,609	2,718
Operating income	229	1,396	1,486
Other income	3,460	505	486
Interest charges	417	784	735
Net income	$3,272	$1,117	$1,237

This segment leases buildings, vehicles, and other equipment to the Company and other non-related customers.

Year ended September 30, 1998 compared with year ended September 30, 1997

Operating revenues remained consistent due to the stable nature of the leasing business (the leasing and rental segment leases buildings and equipment to the United Cities Division and other third parties).

Operating expenses increased $1.1 million from $2.6 million in 1997 to $3.7 million in 1998 primarily due to the tax effect of gains on sales of real estate and equipment.

Other income increased $3.0 million from $.5 million in 1997 to $3.5 million in 1998 primarily due to gains on the sale of real estate and equipment.

Interest expense decreased $.4 million from $.8 million in 1997 to $.4 million in 1998 due to decreased debt, which was retired using the proceeds from the sales of real estate and equipment.

Year ended September 30, 1997 compared with year ended September 30, 1996

Operating revenues, operating expenses, other income, and interest charges remained relatively consistent between 1997 and 1996 due to the stable nature of the business. No buildings or equipment were purchased or sold during 1997.

Capital Resources and Liquidity

(See "Consolidated Statements of Cash Flows")

Because of the pooling of interests of Atmos, which has a September 30 fiscal year end, with UCGC, which had a December 31 year end, as required by generally accepted accounting principles, the activities of UCGC for the quarter ended December 31, 1996 are included in the restated 1996 consolidated statement of cash flows instead of the 1997 consolidated statement of cash flows. As a result, amounts in the 1997 consolidated statement of cash flows as reported are different than they would have been, had they included a full 12 month's activity for UCGC.

The following pro forma condensed consolidated statement of cash flows reflects activities of both Atmos and UCGC for the full 12 months ended September 30, 1997.

	(In thousands)
Cash flows from operating activities:	
Net income	$ 23,838
Depreciation	47,494
Other	(11,054)
Net cash provided by operating activities	60,278
Net cash used in investing activities	(131,286)
Cash flows from financing activities:	
Increase in notes payable, net	63,600
Issuance of long-term debt	40,000
Repayment of long-term debt	(16,037)
Issuance of common stock	10,482
Cash dividends paid	(29,778)
Net cash provided by financing activities	68,267
Decrease in cash	(2,741)
Cash at beginning of year	8,757
Cash at end of year	$ 6,016

Cash Flows From Operating Activities Cash flows from operating activities as reported in the consolidated statement of cash flows totaled $91.7 million for 1998 compared with $68.7 million for 1997 and $91.7 million for 1996. The decline in net cash provided by operating activities from 1996 to 1997 was primarily the result of only including nine months of UCGC activity in the 1997 statement of cash flows. Likewise, the increase in net cash provided from 1997 to 1998 was the result of the full 12 months activity for 1998 for the combined companies. Using 1997 beginning balances for UCGC as of December 31, 1996 resulted in large swings in certain seasonal asset and liability accounts like accounts receivable and accounts payable. Gas in storage increased in 1996 because of higher gas cost, but was lower in 1997 and 1998 because of substantially lower gas prices during the summers of 1997 and 1998

when the storage reservoirs were being refilled. The changes in deferred charges and other assets and other current liabilities in 1997 and 1998 were related to merger and integration costs accrued and the related regulatory assets recorded in the fourth quarter of 1997. See "Consolidated Statements of Cash Flows" for other changes in assets and liabilities.

Cash Flows From Investing Activities A substantial portion of the Company's cash resources is used to fund its ongoing construction program in order to provide natural gas services to a growing customer base and CSI which will upgrade processes and systems companywide. Net cash used in investing activities totaled $118.8 million in 1998 compared with $121.1 million in 1997 and $111.9 million in 1996. In 1998, the Company received $16.0 million from the sale of office buildings and an airplane. Capital expenditures in fiscal 1998 amounted to $135.0 million compared with $122.3 million in 1997 and $117.6 million in 1996. Currently budgeted capital expenditures for 1999 total $86.8 million and include funds for completing the CSI project and implementing new financial systems, as well as funds for additional mains, services, meters, and vehicles. The CSI project includes application software, related technology infrastructure and business process changes. Capital expenditures on the CSI project to date include approximately $26 million in 1997 and $54 million in 1998. Benefits related to the CSI project include enabling the Company's ability to achieve its vision by positioning for future growth, using industry best practices, timely integration of new acquisitions and resolution of Year 2000 issues. Capital expenditures for fiscal 1999 are planned to be financed from internally generated funds and financing activities, as discussed below.

The following table reflects the Company's capitalization, including short-term debt except for the portion related to current storage gas.

	September 30, 1998		September 30, 1997	
	(In thousands)			
Working capital				
Short-term debt[1]	$ 48,909		$ 48,122	
Short-term debt	$ 17,491	2.1%	$119,178	15.6%
Long-term debt	456,331	54.0%	318,182	41.6%
Shareholders' equity	371,158	43.9%	327,260	42.8%
Total capitalization	$844,980	100.0%	$764,620	100.0%

[1] *Includes short-term borrowings associated with working gas inventories.*

As of the end of fiscal 1998, the debt to capitalization ratio had decreased to 56.1% from 57.2% for 1997 which was an increase from 53.4% for 1996. The improvement in 1998 reflects the benefits of 1998 net income in excess of dividend requirements and the issuance of equity under the Direct Stock Purchase Plan ("DSPP"). The increase in 1997 was primarily due to increased cash requirements related to merger and integration costs and CSI investments, as well as the effects of the nonrecurring charges and reserves previously discussed. The Company plans to decrease the debt to capitalization ratio to nearer its target range of 50-52% over the next two years through cash flow generated from operations, issuance of new common stock under its DSPP and ESOP, recovery of CSI and merger/integration costs and from the possible sale of certain remaining real estate assets.

Future Capital Requirements Short-term borrowings are expected to continue to increase somewhat in fiscal 1999 due to budgeted capital expenditures discussed above and scheduled maturities of long-term debt of $57.8 million. The Company has access to $262.0 million under its committed lines of credit and $80.0 million under its uncommitted lines. A committed line of credit of $250.0 million is used to support the Company's $250.0 million commercial paper program which was begun in October 1998.

Forward-looking cash requirements beyond fiscal 1999 include capital expenditures and possible contingencies and environmental matters as discussed in the notes to consolidated financial statements. The Company plans to fund future requirements through internally generated cash flows, credit facilities and its access to the public debt and equity capital markets.

Cash Flows From Financing Activities Net cash provided by financing activities totaled $25.9 million for 1998 compared with $47.3 million for 1997 and $22.0 million for 1996. Financing activities during these periods included issuance of common stock, dividend payments, short-term borrowings from banks under the Company's credit lines, and issuance and repayments of long-term debt.

Cash Dividends Paid The Company paid $31.8 million in cash dividends during 1998 compared with $26.4 million in 1997 (excluding dividends of $3.4 million paid by UCGC in the quarter ended December 31, 1996) and $28.5 million in 1996. Prior to the UCGC merger in July 1997, Atmos increased its actual annual dividend rate by $.04 in each of the years presented. It also raised the dividend rate $.04 for 1998 and 1999. Including fiscal 1999, the Company has increased its dividend rate for 11 consecutive years.

Short-Term Financing Activities At September 30, 1998, the Company had committed lines of credit totaling $262.0 million, $250.0 million of which was unused, in order to provide for short-term cash requirements. These credit facilities are negotiated at least annually. At September 30, 1998, the Company also had uncommitted short-term credit lines of $80.0 million, of which $25.6 million was unused. Subsequent to September 30, 1998, the Company began a commercial paper program under which it is authorized to issue up to $250.0 million. The commercial paper

program is supported by the $250.0 million committed line of credit. During 1998, notes payable decreased $100.9 million, after the application of a portion of the $150.0 million proceeds from the issuance of 6.75% debentures to reduce notes payable, compared with an increase of $38.8 million during 1997 and an increase of $62.7 million in 1996.

Long-term Financing Activities In July 1998, the Company issued $150.0 million of 30-year 6.75% debentures. The debentures are rated A3 by Moody's and A- by Standard & Poor's. In November 1996, the Company issued $40.0 million of 6.09% unsecured notes due in November 1998 to a bank. The proceeds were used to refinance short-term debt. Long-term debt payments totaled $16.3 million, $14.7 million, and $20.7 million for the years ended September 30, 1998, 1997 and 1996, respectively. The amount for 1997 excludes repayments of $1.4 million by UCGC in the quarter ended December 31, 1996. Payments of long-term debt in 1998, 1997 and 1996 consisted of annual installments under the various loan documents. No long-term debt was issued in fiscal 1996.

The loan agreements pursuant to which the Company's Senior Notes and First Mortgage Bonds have been issued contain covenants by the Company with respect to the maintenance of certain debt-to-equity ratios and cash flows, and restrictions on the payment of dividends. Also see Note 7 of the accompanying notes to consolidated financial statements.

UCG Energy and Woodward Marketing, Inc. ("WMI"), sole members of WMLLC, act as guarantors of up to $12.5 million of balances outstanding under a $30 million bank facility for WMLLC. UCG Energy guarantees the payment of up to $5.6 million of borrowings under this facility. No balance was outstanding on this credit facility at September 30, 1998. UCG Energy and WMI also act as joint and several guarantors on certain purchases of natural gas and transportation services from suppliers by WMLLC. UCG Energy has agreed to guarantee such payables up to $40.0 million. These outstanding obligations amounted to $8.5 million at September 30, 1998.

Issuance of Common Stock The Company issued 755,882, 400,578 and 995,467 shares of common stock in 1998, 1997 and 1996, respectively, for its Direct Stock Purchase Plan, Employee Stock Ownership Plans, Long-term Stock Plan for United Cities Division, Restricted Stock Grant Plan, Outside Directors Stock-for-Fee Plan, and acquisitions of Oceana Heights and Monarch Gas Company in 1996. See the Consolidated Statements of Shareholders' Equity for the number of shares issued under each of the plans and for other transactions. Please see Note 9 of the accompanying notes to consolidated financial statements for the number of shares registered and available for future issuance under each of the Company's plans.

In November 1995, the Company exchanged 313,411 shares of its common stock valued at approximately $6.4 million in exchange for privately held Oceana Heights Gas Company of Thibodaux, Louisiana.

In June 1996, in connection with the acquisition of Monarch Gas Company ("Monarch"), 207,366 shares of UCGC's common stock were exchanged for the common stock of Monarch. The merger added approximately 2,900 natural gas customers in the Vandalia, Illinois area.

The Company believes that internally generated funds, its credit facilities, commercial paper program and access to the public debt and equity capital markets will provide necessary working capital and liquidity for capital expenditures and other cash needs for 1999.

Inflation The Company believes that inflation has caused and will continue to cause increases in certain operating expenses and has required and will continue to require assets to be replaced at higher costs. The Company continually reviews the adequacy of its gas rates in relation to the increasing cost of providing service and the inherent regulatory lag in adjusting those gas rates.

Selected Quarterly Financial Data (Unaudited)

Summarized unaudited quarterly financial data are presented below. The sum of net income per share by quarter may not equal the net income per share for the year due to variations in the weighted average shares outstanding used in computing such amounts. The Company's natural gas and propane distribution businesses are seasonal due to weather conditions in the Company's service areas. For further information on its effects on quarterly results, please see the "Seasonality" discussion included in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section herein.

	Fiscal year 1998 Quarter ended			
	December 31,	March 31,	June 30,	September 30,
	(In thousands, except per share data)			
Operating revenues	$295,331	$288,550	$137,311	$127,016
Gross profit	99,601	123,971	57,366	50,898
Operating income	28,668	44,493	6,931	981
Net income (loss)	20,122	37,398	1,676	(3,931)
Net income (loss) per share	.68	1.25	.06	(.13)

	Fiscal year 1997 Quarter ended			
	December 31,	March 31,	June 30,	September 30,
	(In thousands, except per share data)			
Operating revenues	$280,624	$362,636	$143,714	$119,861
Gross profit	97,269	124,249	59,546	48,590
Operating income (loss)	25,968	37,075	4,599	(15,331)
Net income (loss)	18,155	30,625	(3,018)	(21,924)
Net income (loss) per share	.62	1.04	(.10)	(.74)

Market Price of Common Stock and Related Matters

The Company's stock trades on the New York Stock Exchange under the trading symbol "ATO". The high and low sale prices and dividends paid per share of the Company's common stock for fiscal 1998 and 1997 are listed below. Dividends paid for 1997 have been restated to reflect the merger of Atmos and UCGC accounted for as a pooling of interests. The high and low prices listed are the actual closing NYSE quotes for Atmos shares.

	Fiscal year 1998		
	High	Low	Dividends Paid
Quarter ended:			
December 31	$30 1/2	$24 5/16	$.265
March 31	30 5/16	26 1/16	.265
June 30	31 3/16	28 3/16	.265
September 30	30 15/16	24 3/4	.265
			$1.06

	Fiscal year 1997		
	High	Low	Dividends Paid
Quarter ended:			
December 31	$24 3/4	$22 5/8	$.251
March 31	26 1/4	22 1/8	.252
June 30	25 1/2	22 1/2	.252
September 30	27 7/8	24 1/2	.255
			$1.01

See Note 7 of notes to consolidated financial statements for restriction on payment of dividends. The number of record holders of the Company's common stock on September 30, 1998 was 36,949.

Selected Financial Data

The following table sets forth selected financial data of the Company and should be read in conjunction with the consolidated financial statements included herein. Amounts for 1998 and 1997 reflect the pooled operations of Atmos and the United Cities Division. Prior year amounts have been restated for the pooling.

	Year ended September 30,				
	1998	1997	1996	1995	1994
	(In thousands, except per share data)				
Operating revenues	$ 848,208	$ 906,835	$ 886,691	$ 749,555	$ 826,302
Net income	$ 55,265	$ 23,838	$ 41,151	$ 28,808	$ 26,772
Net income per share	$ 1.84	$ .81	$ 1.42	$ 1.06	$ 1.05
Cash dividends per share	$ 1.06	$ 1.01	$ .98	$ .96	$ .91
Total assets at end of year	$ 1,141,390	$ 1,088,311	$ 1,010,610	$ 900,948	$ 829,385
Long-term debt at end of year	$ 398,548	$ 302,981	$ 276,162	$ 294,463	$ 282,647

Consolidated Five-Year Financial and Statistical Summary[1]

	Year ended September 30,				
	1998	1997	1996	1995	1994
Balance Sheet Data at September 30	*(In thousands)*				
Capital expenditures	$ 134,989	$ 122,312	$ 117,589	$103,904	$ 85,471
Net property, plant and equipment	917,860	849,127	770,211	697,287	638,787
Total assets	1,141,390	1,088,311	1,010,610	900,948	829,385
Shareholders' equity	371,158	327,260	329,582	304,349	267,584
Long-term debt, excluding current maturities	398,548	302,981	276,162	294,463	282,647
Total capitalization	769,706	630,241	605,744	598,812	550,231
Income Statement Data	*(In thousands, except per share data)*				
Operating revenues	$ 848,208	$ 906,835	$ 886,691	$749,555	$826,302
Gross profit	331,836	329,654	324,412	300,158	297,020
Net income	55,265	23,838	41,151	28,808	26,772
Net income per share - diluted	1.84	.81	1.42	1.06	1.05
Common Stock Data					
Shares outstanding (in thousands)					
End of year	30,398	29,642	29,242	28,246	25,911
Average	30,031	29,422	28,994	27,208	25,604
Cash dividends per share	$ 1.06	$ 1.01	$ .98	$ .96	$ .91
Shareholders of record	36,949	29,867	36,472	31,782	27,005
Market price - High	$ 31 3/16	$ 27 7/8	$ 31	$ 20 5/8	$ 21 1/8
Low	$ 24 5/16	$ 22 1/8	$ 18	$ 15 7/8	$ 16 3/8
End of year	$ 28 9/16	$ 24 7/8	$ 23 3/8	$ 19 3/8	$ 17 3/4
Book value per share at end of year	$ 12.21	$ 11.04	$ 11.27	$ 10.77	$ 10.33
Price/Earnings ratio at end of year	15.52	30.71	16.46	18.28	16.90
Market/Book ratio at end of year	2.34	2.25	2.07	1.80	1.72
Annualized dividend yield at end of year	3.7%	4.1%	4.2%	5.0%	5.1%
Customers and Volumes (as metered)					
Gas sales volumes (MMcf)	159,373	164,208	178,293	166,656	170,691
Gas transportation volumes (MMcf)	56,224	48,800	44,146	47,647	47,882
Total throughput (MMcf)	215,597	213,008	222,439	214,303	218,573
Meters in service at end of year	1,004,532	985,448	976,308	949,213	943,728
Total meters and propane customers	1,041,932	1,014,545	1,002,416	972,572	965,421
Heating degree days (weighted average)	3,799	3,909	4,043	3,706	3,855
Degree days as % of normal	95%	98%	101%	93%	97%
Average gas sales price per Mcf sold	$ 4.87	$ 5.11	$ 4.51	$ 4.07	$ 4.41
Average purchased gas cost per Mcf sold	$ 3.24	$ 3.51	$ 3.15	$ 2.70	$ 3.10
Average transportation fee per Mcf	$ .43	$ .41	$ .43	$ .42	$ .45
Statistics					
Return on average shareholders' equity	15.8%	7.3%	13.0%	10.1%	10.3%
Number of employees	2,193	2,679	2,863	2,944	3,052
Net plant per meter	$ 914	$ 862	$ 789	$ 735	$ 677
Operating, maintenance and administrative expense per customer	$ 136	$ 183	$ 160	$ 163	$ 169
Meters/customers per employee	475	379	350	330	316
Times interest earned before income taxes	3.09	2.04	3.00	2.44	2.45

[1] Amounts have been restated for poolings of interests with United Cities in July 1997 and Greeley Gas Company in December 1993, and share data have been adjusted for a 3-for-2 stock split in May 1994.

Board of Directors

Top:
Front, from left
Dan Busbee, Lee Schlessman (Honorary Director)
Rear, from left
Richard Cardin, Phillip Nichol, Richard Ware, Carl Quinn, Robert Best

Bottom:
Front
Vincent Lewis
Rear, from left
Thomas Meredith, Gene Koonce, Travis Bain, Thomas Garland, Charles Vaughan

Travis W. Bain II
President, Bain Enterprises, Inc.
Plano, Texas
Board member since 1988
Committees: Work Session/Annual Meeting (Chairman), Audit, Human Resources

Robert W. Best
Chairman of the Board, President and Chief Executive Officer
Atmos Energy Corporation,
Dallas, Texas
Board member since 1997
Committee: Executive

Dan Busbee
Of Counsel with Gibson Dunn & Crutcher
Dallas,Texas
Board Member since 1998
Committees: Audit (Chairman), Human Resources

Richard W. Cardin
Consultant and retired partner of Arthur Andersen LLP
Nashville, Tennessee
Board Member since 1997
Committees: Audit, Nominating

Thomas J. Garland
Chairman of the Tusculum Institute for Public Leadership and Policy
Greeneville, Tennessee
Board Member since 1997
Committees: Human Resources, Work Session/Annual Meeting

Gene C. Koonce
Formerly Chairman of the Board, President and Chief Executive Officer
United Cities Gas Company
Brentwood, Tennessee
Board member since 1997
Committees: Executive, Nominating, Work Session/Annual Meeting

Honorary Director
Lee E. Schlessman
President, Dolo Investment Company
Denver, Colorado
Retired from Board in 1998

Vincent J. Lewis
Senior Vice President
Legg Mason Wood Walker Inc.
Rutherford, New Jersey
Board member since 1997
Committees: Audit, Nominating

Dr. Thomas C. Meredith
Chancellor of the University of Alabama System
Tuscaloosa, Alabama
Board member since 1995
Committees: Audit, Nominating

Phillip E. Nichol
Senior Vice President and Divisional Hiring Officer for Central Division
PaineWebber Incorporated
Fort Worth, Texas
Board member since 1985
Committees: Nominating (Chairman), Human Resources, Work Session/Annual Meeting

Carl S. Quinn
General Partner, Quinn Oil Company, Ltd.
East Hampton, New York
Board member since 1994
Committees: Human Resources (Chairman), Executive

Charles K. Vaughan
Formerly Chairman of the Board
Atmos Energy Corporation
Dallas, Texas
Board member since 1983
Committees: Executive (Chairman)

Richard Ware II
President, Amarillo National Bank
Amarillo, Texas
Board member since 1994
Committees: Audit, Work Session/Annual Meeting

Gene C. Koonce retired from active service with United Cities Gas Company in December, 1997 with 20 years of service. He remains a member of our Board of Directors, and his counsel and industry expertise will continue to be of great value to Atmos.

Corporate Information Page

Common Stock Listing

New York Stock Exchange

Trading Symbol

ATO

Stock Transfer Agent and Registrar

Shareholder inquiries on stock transfers may be directed to Boston EquiServe, L.P., Mail Stop 45-02-64, P.O. Box 644, Boston, MA 02102-0644. You may call the Interactive Voice Response System 24 hours a day at 1-800-543-3038, or to speak to a customer service representative, call between 9 a.m. and 6 p.m. EST, Monday through Friday.

Independent Auditors

Ernst & Young LLP
2121 San Jacinto, Suite 1500
Dallas, Texas 75201
(214) 969-8000

Form 10-K

The Atmos Energy Corporation Annual Report on Form 10-K is available upon request from Investor Relations, Atmos Energy Corporation, P.O. Box 650205, Dallas, Texas 75265-0205, or by calling 1-800-38-ATMOS (382-8667) 7:30 a.m. – 4:30 p.m. CST. Form 10-K may also be viewed on Atmos' website: http://www.atmosenergy.com.

Annual Meeting of Shareholders

The Annual Meeting of Shareholders will be held at The Westin Hermitage, 231 Sixth Ave. North, Nashville, Tennessee, at 11 a.m. CST on Feb. 10, 1999.

Direct Stock Purchase Plan

Atmos Energy Corporation has a Direct Stock Purchase Plan that is available to all investors.

For an initial Investment Form or Enrollment Authorization Form and a Plan Prospectus, please call Atmos Shareholder Relations at 1-800-38-ATMOS (382-8667) 7:30 a.m. – 4:30 p.m. CST; or Boston EquiServe, L.P., at 1-800-543-3038. The Prospectus is also available on the Internet at http://www.atmosenergy.com. You may also obtain information by writing to Shareholder Relations, Atmos Energy Corporation, P.O. Box 650205, Dallas, Texas 75265-0205.

This is not an offer to sell nor a solicitation to buy any securities of Atmos. Shares of Atmos common stock purchased through the Direct Stock Purchase Plan will be offered only by Prospectus.

Atmos Information by Phone

Atmos Energy Corporation shareholder information is available by phone seven days a week, 24 hours a day through Boston EquiServe, L.P.'s interactive voice response system. To perform stock transfers, listen to current company information and access daily stock quotes without the assistance of a customer service representative, call 1-800-543-3038 and have your Atmos Energy shareholder account number and Social Security or taxpayer ID number ready.

Atmos on the Internet

Information about Atmos and its business units may be accessed over the Internet. The Atmos home page, located at http://www.atmosenergy.com, includes current and historical financial reports and other investor information, management biographies, employment opportunities and information about the company's operations and service areas. Each business unit has its own home page, with details about products and services. You can reach the business units directly at the following web addresses:

http://www.energas.com

http://www.greeleygas.com

http://www.transla.com

http://www.westernkentuckygas.com

http://www.unitedcitiesgas.com

http://www.atmospropane.com

Please visit us on the worldwide web.

Atmos Energy Corporation Contacts:

Shareholder and Direct Stock Purchase Plan Information:
1-800-38-ATMOS (382-8667), 7:30 a.m. – 4:30 p.m. CST

Financial Information for Securities Analysts,
Investment Managers and General Information:
Lynn Hord
Vice President of Investor Relations
and Corporate Communications
(972) 855-3729

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