MISSISSIPPI POWER COMPANY

2017 ANNUAL REPORT

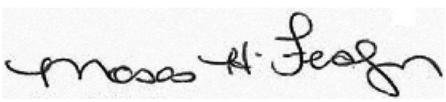
Mississippi Power

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
Mississippi Power Company 2017 Annual Report

The management of Mississippi Power Company (the Company) is responsible for establishing and maintaining an adequate system of internal control over financial reporting as required by the Sarbanes-Oxley Act of 2002 and as defined in Exchange Act Rule 13a-15(f). A control system can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

Under management's supervision, an evaluation of the design and effectiveness of the Company's internal control over financial reporting was conducted based on the framework in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2017.

Anthony L. Wilson
Chairman, President, and Chief Executive Officer



Moses H. Feagin
Vice President, Chief Financial Officer, and Treasurer

February 20, 2018

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the stockholders and the Board of Directors of Mississippi Power Company

Opinion on the Financial Statements

We have audited the accompanying balance sheets and statements of capitalization of Mississippi Power Company (the Company) (a wholly-owned subsidiary of The Southern Company) as of December 31, 2017 and 2016, the related statements of operations, comprehensive income (loss), common stockholder's equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements (pages 37 to 83) present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Deloitte & Touche LLP

Atlanta, Georgia
February 20, 2018

We have served as the Company's auditor since 2002.

DEFINITIONS

Term	Meaning
2012 MPSC CPCN Order	A detailed order issued by the Mississippi PSC in April 2012 confirming the CPCN originally approved by the Mississippi PSC in 2010 authorizing acquisition, construction, and operation of the Kemper County energy facility
AFUDC	Allowance for funds used during construction
Alabama Power	Alabama Power Company
ARO	Asset retirement obligation
ASC	Accounting Standards Codification
ASU	Accounting Standards Update
CCR	Coal combustion residuals
Clean Air Act	Clean Air Act Amendments of 1990
CO_2	Carbon dioxide
Cooperative Energy	Electric cooperative in Mississippi
CPCN	Certificate of public convenience and necessity
CWIP	Construction work in progress
DOE	U.S. Department of Energy
ECM	Energy cost management clause
ECO	Environmental compliance overview
EPA	U.S. Environmental Protection Agency
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
GAAP	U.S. generally accepted accounting principles
Georgia Power	Georgia Power Company
Gulf Power	Gulf Power Company
IGCC	Integrated coal gasification combined cycle, the technology originally approved for Mississippi Power's Kemper County energy facility (Plant Ratcliffe)
IRS	Internal Revenue Service
ITC	Investment tax credit
KWH	Kilowatt-hour
LIBOR	London Interbank Offered Rate
Mirror CWIP	A regulatory liability used by Mississippi Power to record financing costs associated with construction of the Kemper County energy facility, which were subsequently refunded to customers
mmBtu	Million British thermal units
Moody's	Moody's Investors Service, Inc.
MPUS	Mississippi Public Utilities Staff
MRA	Municipal and Rural Associations
MW	Megawatt
NO_X	Nitrogen oxide
OCI	Other comprehensive income
PEP	Performance evaluation plan
power pool	The operating arrangement whereby the integrated generating resources of the traditional electric operating companies and Southern Power (excluding subsidiaries) are subject to joint commitment and dispatch in order to serve their combined load obligations

DEFINITIONS
(continued)

Term	Meaning
PPA	Power purchase agreement
PSC	Public Service Commission
ROE	Return on equity
S&P	S&P Global Ratings, a division of S&P Global Inc.
scrubber	Flue gas desulfurization system
SCS	Southern Company Services, Inc. (the Southern Company system service company)
SEC	U.S. Securities and Exchange Commission
SO_2	Sulfur dioxide
Southern Company	The Southern Company
Southern Company Gas	Southern Company Gas and its subsidiaries
Southern Company system	Southern Company, the traditional electric operating companies, Southern Power, Southern Company Gas (as of July 1, 2016), Southern Electric Generating Company, Southern Nuclear, SCS, Southern Linc, PowerSecure, Inc. (as of May 9, 2016), and other subsidiaries
Southern Linc	Southern Communications Services, Inc.
Southern Nuclear	Southern Nuclear Operating Company, Inc.
Southern Power	Southern Power Company and its subsidiaries
SRR	System Restoration Rider, a tariff for retail property damage reserve
Tax Reform Legislation	The Tax Cuts and Jobs Act, which was signed into law on December 22, 2017 and became effective on January 1, 2018
traditional electric operating companies	Alabama Power, Georgia Power, Gulf Power, and Mississippi Power

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
Mississippi Power Company 2017 Annual Report

OVERVIEW

Business Activities

Mississippi Power Company (the Company) operates as a vertically integrated utility providing electric service to retail customers within its traditional service territory located within the State of Mississippi and to wholesale customers in the Southeast.

Many factors affect the opportunities, challenges, and risks of the Company's business of providing electric service. These factors include the Company's ability to maintain and grow energy sales and to operate in a constructive regulatory environment that provides timely recovery of prudently-incurred costs. These costs include those related to reliability, fuel, and stringent environmental standards, as well as ongoing capital and operations and maintenance expenditures and restoration following major storms. Appropriately balancing required costs and capital expenditures with customer prices will continue to challenge the Company for the foreseeable future.

The Kemper County energy facility was approved by the Mississippi PSC as an IGCC facility in the 2010 CPCN proceedings, subject to a construction cost cap of $2.88 billion, net of $245 million of grants awarded to the project by the DOE under the Clean Coal Power Initiative Round 2 (Initial DOE Grants) and excluding the cost of the lignite mine and equipment, the cost of the CO_2 pipeline facilities, AFUDC, and certain general exceptions (Cost Cap Exceptions). The combined cycle and associated common facilities portions of the Kemper County energy facility were placed in service in August 2014. In December 2015, the Mississippi PSC issued an order (In-Service Asset Rate Order), authorizing rates that provided for the recovery of approximately $126 million annually related to the assets previously placed in service.

On June 21, 2017, the Mississippi PSC stated its intent to issue an order (which occurred on July 6, 2017) directing the Company to pursue a settlement under which the Kemper County energy facility would be operated as a natural gas plant, rather than an IGCC plant, and address all issues associated with the Kemper County energy facility (Kemper Settlement Order). The Kemper Settlement Order established a new docket for the purposes of pursuing a global settlement of the related costs (Kemper Settlement Docket).

On June 28, 2017, the Company notified the Mississippi PSC that it would begin a process to suspend operations and start-up activities on the gasifier portion of the Kemper County energy facility, given the uncertainty as to its future. At the time of project suspension, the total cost estimate for the Kemper County energy facility was approximately $7.38 billion, including approximately $5.95 billion of costs subject to the construction cost cap, and was net of the $137 million in additional grants from the DOE received on April 8, 2016 (Additional DOE Grants). In the aggregate, the Company had incurred charges of $3.07 billion ($1.89 billion after tax) as a result of changes in the cost estimate above the cost cap for the Kemper IGCC through May 31, 2017. Given the Mississippi PSC's stated intent regarding no further rate increase for the Kemper County energy facility and the subsequent suspension, cost recovery of the gasifier portions became no longer probable; therefore, the Company recorded an additional charge to income in June 2017 of $2.8 billion ($2.0 billion after tax), which included estimated costs associated with the gasifier portions of the plant and lignite mine.

On February 6, 2018, the Mississippi PSC voted to approve a settlement agreement related to cost recovery for the Kemper County energy facility among the Company, the MPUS, and certain intervenors (Kemper Settlement Agreement). The Kemper Settlement Agreement provides for an annual revenue requirement of approximately $99.3 million for costs related to the Kemper County energy facility, which includes the impact of Tax Reform Legislation. The revenue requirement is based on (i) a fixed ROE for 2018 of 8.6%, excluding any performance adjustment, (ii) a ROE for 2019 calculated in accordance with PEP, excluding the performance adjustment, (iii) for future years, a performance-based ROE calculated pursuant to PEP, and (iv) amortization periods for the related regulatory assets and liabilities of eight years and six years, respectively. The revenue requirement also reflects a disallowance related to a portion of the Company's investment in the Kemper County energy facility requested for inclusion in rate base, which was recorded in the fourth quarter 2017 as an additional charge to income of approximately $78 million ($85 million net of accumulated depreciation of $7 million) pre-tax ($48 million after tax).

Under the Kemper Settlement Agreement, retail customer rates will reflect a reduction of approximately $26.8 million annually and include no recovery for costs associated with the gasifier portion of the Kemper County energy facility in 2018 or at any future date. On February 12, 2018, the Company made the required compliance filing with the Mississippi PSC. The Kemper Settlement Agreement also requires (i) the CPCN for the Kemper County energy facility to be modified to limit it to natural gas combined cycle operation and (ii) the Company to file a reserve margin plan with the Mississippi PSC by August 2018.

During the third and fourth quarters of 2017, the Company recorded charges to income of $242 million ($206 million after tax), including $164 million for ongoing project costs, estimated mine and gasifier-related costs, and certain termination costs during the suspension period prior to conclusion of the Kemper Settlement Docket, as well as the charge associated with the Kemper Settlement Agreement. Additional pre-tax cancellation costs, including mine and plant closure and contract termination costs, currently estimated at approximately $50 million to $100 million (excluding salvage), are expected to be incurred in 2018. The Company has begun efforts to dispose of or abandon the mine and gasifier-related assets.

Total pre-tax charges to income related to the Kemper County energy facility were $3.4 billion ($2.4 billion after tax) for the year ended December 31, 2017. In the aggregate, since the Kemper County energy facility project started, the Company has incurred charges of $6.2 billion ($4.1 billion after tax) through December 31, 2017.

As a result of the Mississippi PSC order on February 6, 2018, rate recovery for the Kemper County energy facility is resolved, subject to any future legal challenges.

For additional information, see FUTURE EARNINGS POTENTIAL – "Kemper County Energy Facility" and "Other Matters" herein.

The Company's financial statement presentation contemplates continuation of the Company as a going concern as a result of Southern Company's anticipated ongoing financial support of the Company. For additional information, see Note 6 to the financial statements under "Going Concern." In June 2017, Southern Company made equity contributions totaling $1.0 billion to the Company. The Company used a portion of the proceeds to (i) prepay $300 million of the outstanding principal amount under its $1.2 billion unsecured term loan; (ii) repay $591 million of the outstanding principal amount of promissory notes to Southern Company; and (iii) repay $10 million of the outstanding principal amount of bank loans.

As of December 31, 2017, the Company's current liabilities exceeded current assets by approximately $911 million primarily due to a $900 million unsecured term loan that matures on March 31, 2018. The Company expects to refinance the unsecured term loan with external security issuances and/or borrowings from financial institutions or Southern Company. To fund the Company's capital needs over the next 12 months, the Company intends to utilize operating cash flows, external security issuances, lines of credit, bank term loans, equity contributions from Southern Company, and, to the extent necessary, loans from Southern Company.

The Company continues to focus on several key performance indicators. In recognition that the Company's long-term financial success is dependent upon how well it satisfies its customers' needs, the Company's retail base rate mechanism, PEP, includes performance indicators that directly tie customer service indicators to the Company's allowed ROE. PEP measures the Company's performance on a 10-point scale as a weighted average of results in three areas: average customer price, as compared to prices of other regional utilities (weighted at 40%); service reliability, measured in percentage of time customers had electric service (40%); and customer satisfaction, measured in a survey of residential customers (20%). The Company also focuses on broader measures of customer satisfaction, plant availability, system reliability, and net income after dividends on preferred stock.

On January 16, 2018, the Mississippi PSC approved the 2018 retail fuel cost recovery factor, effective February 2018 through January 2019, which resulted in a $39 million increase in annual revenues. On February 7, 2018, the Company filed its 2018 PEP forecast, requesting an increase in annual base revenues of $26 million. On February 14, 2018, the Company submitted its 2018 ECO filing, requesting an increase in annual retail revenue of $17 million. The PEP and ECO filings include the effects of Tax Reform Legislation. Rulings from the Mississippi PSC on the PEP and ECO filings are expected in the first half of 2018. See FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters" herein and Note 3 to the financial statements under "Retail Regulatory Matters – Performance Evaluation Plan" for more information. The ultimate outcome of this matter cannot be determined at this time.

The Company's financial success is directly tied to customer satisfaction. Key elements of ensuring customer satisfaction include outstanding service, high reliability, and competitive prices. Management uses customer satisfaction surveys to evaluate the Company's results and generally targets top-quartile performance.

See RESULTS OF OPERATIONS herein for information on the Company's financial performance.

Earnings

The Company's net loss after dividends on preferred stock was $2.59 billion in 2017 compared to a $50 million net loss in 2016. The change in 2017 was primarily the result of higher pre-tax charges of $3.36 billion ($2.39 billion after tax) in 2017 compared to pre-tax charges of $428 million ($264 million after tax) in 2016 for estimated losses on the Kemper IGCC.

The Company's net loss after dividends on preferred stock was $50 million in 2016 compared to $8 million in 2015. The change in 2016 was primarily the result of higher pre-tax charges of $428 million ($264 million after tax) in 2016 compared to pre-tax charges of $365 million ($226 million after tax) in 2015 for estimated losses on the Kemper IGCC. The decrease in net income was partially offset by an increase in retail revenues due to the implementation of rates in September 2015 for certain Kemper

County energy facility in-service assets, partially offset by a decrease in wholesale revenues. The increase in revenues was partially offset by an increase in interest expense in 2016 compared to 2015 due to the termination of an asset purchase agreement between the Company and Cooperative Energy in 2015 and an increase in operations and maintenance expenses.

See Note 3 to the financial statements under "Kemper County Energy Facility" for additional information.

RESULTS OF OPERATIONS

A condensed statement of operations follows:

	Amount	Increase (Decrease) from Prior Year	
	2017	**2017**	2016
		(in millions)	
Operating revenues	**$ 1,187**	**$ 24**	$ 25
Fuel	**395**	**52**	(100)
Purchased power	**25**	**(9)**	22
Other operations and maintenance	**282**	**(30)**	38
Depreciation and amortization	**161**	**29**	9
Taxes other than income taxes	**104**	**(5)**	15
Estimated loss on Kemper IGCC	**3,362**	**2,934**	63
Total operating expenses	**4,329**	**2,971**	47
Operating loss	**(3,142)**	**(2,947)**	(22)
Allowance for equity funds used during construction	**72**	**(52)**	14
Interest expense, net of amounts capitalized	**42**	**(32)**	67
Other income (expense), net	**(8)**	**(1)**	1
Income taxes (benefit)	**(532)**	**(428)**	(32)
Net income (loss)	**(2,588)**	**(2,540)**	(42)
Dividends on preferred stock	**2**	**—**	—
Net loss after dividends on preferred stock	**$ (2,590)**	**$ (2,540)**	$ (42)

Operating Revenues

Operating revenues for 2017 were $1.2 billion, reflecting a $24 million increase from 2016. Details of operating revenues were as follows:

	Amount	
	2017	2016
	(in millions)	
Retail — prior year	**$ 859**	$ 776
Estimated change resulting from —		
Rates and pricing	**(7)**	96
Sales growth (decline)	**4**	(4)
Weather	**(15)**	8
Fuel and other cost recovery	**13**	(17)
Retail — current year	**854**	859
Wholesale revenues —		
Non-affiliates	**259**	261
Affiliates	**56**	26
Total wholesale revenues	**315**	287
Other operating revenues	**18**	17
Total operating revenues	**$ 1,187**	$ 1,163
Percent change	**2.1%**	2.2%

Total retail revenues for 2017 decreased $5 million, or 0.6%, compared to 2016 primarily due to a $15 million decrease as a result of milder weather in 2017 and the deferral of $17 million of revenue following the complete amortization of certain regulatory assets related to the Kemper County energy facility in July 2017. These decreases were partially offset by a $10 million net increase related to ECO plan rate changes in the third quarter 2016 and the second quarter 2017 and an increase of $13 million in fuel cost recovery. Total retail revenues for 2016 increased $83 million, or 10.7%, compared to 2015 primarily due to changes in rates and pricing of $96 million, partially offset by a net decrease in fuel and other cost recovery of $17 million.

See Note 3 to the financial statements under "Retail Regulatory Matters – Environmental Compliance Overview" and "Kemper County Energy Facility – Rate Recovery" for additional information. See "Energy Sales" below for a discussion of changes in the volume of energy sold, including changes related to sales and weather.

Electric rates for the Company include provisions to adjust billings for fluctuations in fuel costs, including the energy component of purchased power costs. Under these provisions, fuel revenues generally equal fuel expenses, including the energy component of purchased power costs, and do not affect net income. Recoverable fuel costs include fuel and purchased power expenses reduced by the fuel and emissions portion of wholesale revenues from energy sold to customers outside the Company's service territory. See FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Fuel Cost Recovery" herein for additional information.

Wholesale revenues from power sales to non-affiliated utilities, including FERC-regulated MRA sales as well as market-based sales, were as follows:

	2017	2016	2015
		(in millions)	
Capacity and other	**$ 154**	$ 157	$ 158
Energy	**105**	104	112
Total non-affiliated	**$ 259**	$ 261	$ 270

Wholesale revenues from sales to non-affiliates will vary depending on fuel prices, the market prices of wholesale energy compared to the cost of the Company's and the Southern Company system's generation, demand for energy within the Southern Company system's electric service territory, and the availability of the Southern Company system's generation. Increases and decreases in energy revenues that are driven by fuel prices are accompanied by an increase or decrease in fuel costs and do not have a significant impact on net income. In addition, the Company provides service under long-term contracts with rural electric cooperative associations and municipalities located in southeastern Mississippi under cost-based electric tariffs which are subject to regulation by the FERC. The contracts with these wholesale customers represented 19.3% of the Company's total operating revenues in 2017 and are largely subject to rolling 10-year cancellation notices. Historically, these wholesale customers have acted as a group and any changes in contractual relationships for one customer are likely to be followed by the other wholesale customers.

Short-term opportunity energy sales are also included in sales for resale to non-affiliates. These opportunity sales are made at market-based rates that generally provide a margin above the Company's variable cost to produce the energy.

Wholesale revenues from sales to affiliates will vary depending on demand and the availability and cost of generating resources at each company. These affiliate sales are made in accordance with the Intercompany Interchange Contract (IIC), as approved by the FERC. These transactions do not have a significant impact on earnings since this energy is generally sold at marginal cost.

Wholesale revenues from sales to affiliates increased $30 million, or 115.4%, in 2017 compared to 2016. The increase was primarily due to higher natural gas prices and higher KWH sales due to dispatch of the Company's lower cost generation resources to serve system territorial load. Wholesale revenues from sales to affiliates decreased $50 million, or 65.8%, in 2016 compared to 2015 primarily due to a $50 million decrease in energy revenues of which $4 million was associated with lower fuel prices and $46 million was associated with a decrease in KWH sales as a result of lower cost generation available in the Southern Company system.

Energy Sales

Changes in revenues are influenced heavily by the change in the volume of energy sold from year to year. KWH sales for 2017 and the percent change from the prior year were as follows:

	Total KWHs	Total KWH Percent Change		Weather-Adjusted Percent Change	
	2017	**2017**	2016	**2017**	2016
	(in millions)				
Residential	**1,944**	**(5.2)%**	1.3 %	**1.4 %**	(2.4)%
Commercial	**2,764**	**(2.7)**	1.3	**(0.1)**	(2.2)
Industrial	**4,841**	**(1.3)**	(1.0)	**(1.3)**	(1.6)
Other	**39**	**(1.6)**	(1.3)	**(1.6)**	(1.3)
Total retail	**9,588**	**(2.5)**	0.1	**(0.4)%**	(1.9)%
Wholesale					
Non-affiliated	**3,672**	**(6.3)**	1.7		
Affiliated	**2,024**	**82.7**	(60.5)		
Total wholesale	**5,696**	**14.0**	(24.5)		
Total energy sales	**15,284**	**2.8 %**	(9.8)%		

Changes in retail energy sales are generally the result of changes in electricity usage by customers, changes in weather, and changes in the number of customers. Retail energy sales decreased 2.5% in 2017 as compared to the prior year. This decrease was primarily the result of milder weather in 2017 as compared to 2016. Weather-adjusted residential KWH sales increased in 2017 primarily due to increased customer usage. Weather-adjusted commercial KWH sales decreased primarily due to decreased customer usage largely offset by customer growth. The decrease in industrial KWH energy sales was primarily due to Hurricane Nate, which impacted several large industrial customers.

Retail energy sales increased 0.1% in 2016 as compared to the prior year. This increase was primarily the result of warmer weather in the third quarter 2016 as compared to the corresponding period in 2015. Weather-adjusted residential and commercial KWH sales decreased primarily due to decreased customer usage partially offset by customer growth. The decrease in industrial KWH energy sales was primarily due to planned and unplanned outages by large industrial customers.

See "Operating Revenues" above for a discussion of significant changes in wholesale revenues to affiliated companies.

Fuel and Purchased Power Expenses

Fuel costs constitute one of the largest expenses for the Company. The mix of fuel sources for generation of electricity is determined primarily by demand, the unit cost of fuel consumed, and the availability of generating units. Additionally, the Company purchases a portion of its electricity needs from the wholesale market.

Details of the Company's generation and purchased power were as follows:

	2017	2016	2015
Total generation *(in millions of KWHs)*	**15,319**	14,514	17,014
Total purchased power *(in millions of KWHs)*	**1,314**	1,574	539
Sources of generation *(percent)* –			
Gas	**92**	91	83
Coal	**8**	9	17
Cost of fuel, generated *(in cents per net KWH)* –			
Gas	**2.69**	2.41	2.58
Coal	**3.64**	3.91	3.71
Average cost of fuel, generated *(in cents per net KWH)*	**2.77**	2.55	2.78
Average cost of purchased power *(in cents per net KWH)*	**3.50**	3.07	2.17

Fuel and purchased power expenses were $420 million in 2017, an increase of $43 million, or 11.4%, as compared to the prior year. The increase was primarily due to a $36 million increase in the average cost of generation and purchased power and a net increase of $7 million in KWHs generated from gas generation.

Fuel and purchased power expenses were $377 million in 2016, a decrease of $78 million, or 17.1%, as compared to the prior year. The decrease was primarily due to a decrease of $70 million in the volume of KWHs generated and purchased and an $8 million increase in the average cost of generation and purchased power.

Fuel and purchased power energy transactions do not have a significant impact on earnings, since energy expenses are generally offset by energy revenues through the Company's fuel cost recovery clauses. See FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Fuel Cost Recovery" herein and Note 1 to the financial statements under "Fuel Costs" for additional information.

Fuel

Fuel expense increased $52 million, or 15.2%, in 2017 compared to 2016 primarily due to an 11.6% higher cost of natural gas. Fuel expense decreased $100 million, or 22.6%, in 2016 compared to 2015 due to an 8.2% decrease in the average cost of fuel per KWH generated and a 15.5% decrease in the volume of KWHs generated.

Purchased Power

Purchased power expense decreased $9 million, or 26.5%, in 2017 compared to 2016. The decrease was primarily the result of a 16.5% decrease in the volume of KWHs purchased offset by a slight increase in the average cost per KWH purchased compared to 2016. Purchased power expense increased $22 million, or 183.3%, in 2016 compared to 2015. The increase in 2016 was primarily the result of a 192.1% increase in the volume of KWHs purchased due to the availability of lower cost energy as compared to the cost of self-generation.

Energy purchases will vary depending on the market prices of wholesale energy as compared to the cost of the Southern Company system's generation, demand for energy within the Southern Company system's service territory, and the availability of the Southern Company system's generation. These purchases are made in accordance with the IIC or other contractual agreements, as approved by the FERC.

Other Operations and Maintenance Expenses

Other operations and maintenance expenses decreased $30 million, or 9.6%, in 2017 compared to the prior year. The decrease was primarily due to a $10 million decrease in transmission and distribution expenses related to overhead line maintenance, an $8 million decrease in contractor services related to facilities, corporate advertising, and employee compensation and benefits, and an $8 million decrease related to the combined cycle and the associated common facilities portion of the Kemper County energy facility.

Other operations and maintenance expenses increased $38 million, or 13.9%, in 2016 compared to the prior year. The increase was primarily due to increases of $28 million related to the combined cycle and associated common facilities portion of the Kemper County energy facility and $10 million in amortization of prior expense deferrals, both following the In-Service Asset Rate Order in December 2015, as well as a $7 million increase in transmission and distribution expenses primarily related to overhead line maintenance and vegetation management expenses, partially offset by a $9 million decrease in planned generation outage costs.

Depreciation and Amortization

Depreciation and amortization increased $29 million, or 22.0%, in 2017 compared to 2016 primarily due to $13 million of amortization related to the ECO plan, $7 million of depreciation for additional plant in service, and $6 million in additional regulatory asset amortization associated with the Mercury and Air Toxics Standards (MATS) rule compliance.

Depreciation and amortization increased $9 million, or 7.3%, in 2016 compared to 2015 primarily due to $32 million of additional regulatory asset amortization related to the In-Service Asset Rate Order, ECO plan, and MATS rule compliance, $13 million associated with Kemper County energy facility deferrals primarily related to depreciation deferrals in 2015, and $9 million of depreciation for additional plant in service assets primarily associated with the Plant Daniel scrubbers. These increases were partially offset by $23 million of regulatory deferrals related to the In-Service Asset Rate Order and a $22 million deferral associated with the implementation of revised ECO plan rates with the first billing cycle for September 2016.

See Note 1 to the financial statements under "Depreciation and Amortization" and Note 3 to the financial statements under "FERC Matters" and "Retail Regulatory Matters – Environmental Compliance Overview Plan" for additional information.

Taxes Other Than Income Taxes

Taxes other than income taxes decreased $5 million, or 4.6%, in 2017 compared to 2016 primarily due to a decrease in franchise taxes of $4 million, as well as a decrease in ad valorem taxes of $1 million. Taxes other than income taxes increased $15 million, or 16.0%, in 2016 compared to 2015 primarily due to increases in ad valorem taxes of $10 million, related to an increase in the assessed value of property, as well as increases in franchise taxes of $5 million, related to increased operating revenue.

The retail portion of ad valorem taxes is recoverable under the Company's ad valorem tax cost recovery clause and, therefore, does not affect net income.

Estimated Loss on Kemper IGCC

In 2017, 2016, and 2015, estimated probable losses on the Kemper IGCC of $3.36 billion, $428 million, and $365 million, respectively, were recorded. On June 28, 2017, the Company suspended the gasifier portion of the project and recorded a charge to earnings for the remaining $2.8 billion book value of the gasifier portion of the project. Prior to the suspension, the Company recorded losses for revisions of estimated costs expected to be incurred on construction of the Kemper IGCC in excess of the $2.88 billion cost cap established by the Mississippi PSC, net of $245 million of the Initial DOE Grants and excluding the Cost Cap Exceptions.

See Note 3 to the financial statements under "Kemper County Energy Facility" for additional information.

Allowance for Equity Funds Used During Construction

AFUDC equity decreased $52 million, or 41.9%, in 2017 as compared to 2016 as a result of the Kemper IGCC project suspension in June 2017. AFUDC equity increased $14 million, or 12.7%, in 2016 as compared to 2015 primarily due to a higher AFUDC rate and an increase in Kemper County energy facility CWIP subject to AFUDC prior to the suspension of the gasifier portion of the project, partially offset by placing the Plant Daniel scrubbers in service in November 2015. See ACCOUNTING POLICIES – "Application of Critical Accounting Policies and Estimates – Allowance for Funds Used During Construction" herein and Note 3 to the financial statements under "Kemper County Energy Facility" for additional information.

Interest Expense, Net of Amounts Capitalized

Interest expense, net of amounts capitalized decreased $32 million in 2017 compared to 2016. The decrease was primarily associated with a $36 million net reduction in interest following a settlement with the IRS related to research and experimental (R&E) deductions. Also contributing to the decrease was the amortization of $6 million in interest deferrals in accordance with the In-Service Asset Rate Order and a $7 million decrease in interest related to outstanding debt as a result of lower balances and lower rates. These decreases were partially offset by a $20 million reduction in interest capitalized following suspension of the Kemper County energy facility construction.

See Note 5 to the financial statements under "Section 174 Research and Experimental Deduction" for additional information.

Interest expense, net of amounts capitalized increased $67 million in 2016 compared to 2015. The increase was primarily due to an increase of $31 million of interest on deposits resulting from the 2015 reversal of interest associated with the termination of an asset purchase agreement between the Company and Cooperative Energy in May 2015; a $20 million increase due to additional long-term debt and a $30 million decrease in amounts capitalized primarily resulting from $17 million of capitalized interest and the amortization of $13 million in interest deferrals in accordance with the In-Service Asset Rate Order. These net increases were partially offset by a decrease of $16 million in interest accrued on the Mirror CWIP liability prior to refund in 2015.

Income Taxes (Benefit)

Income tax benefits increased $428 million, or 411.5%, in 2017 compared to 2016 primarily due to $809 million in tax benefits on the estimated probable losses on the Kemper IGCC, net of the non-deductible AFUDC equity portion and the related state valuation allowances, partially offset by $372 million resulting from Tax Reform Legislation. Tax Reform Legislation earnings impacts are primarily due to revaluing deferred tax assets related to the Kemper County energy facility. See FUTURE EARNINGS POTENTIAL – "Income Tax Matters" herein and Note 5 to the financial statements for additional information.

Income tax benefits increased $32 million, or 44.4%, in 2016 compared to 2015 primarily as a result of an increase in the estimated probable losses on the Kemper IGCC and an increase in AFUDC equity, which is non-taxable.

Effects of Inflation

The Company is subject to rate regulation that is generally based on the recovery of historical and projected costs. The effects of inflation can create an economic loss since the recovery of costs could be in dollars that have less purchasing power. Any adverse effect of inflation on the Company's results of operations has not been substantial in recent years.

FUTURE EARNINGS POTENTIAL

General

The Company operates as a vertically integrated utility providing electric service to retail customers within its traditional service territory located in southeast Mississippi and to wholesale customers in the Southeast. Prices for electricity provided by the Company to retail customers are set by the Mississippi PSC under cost-based regulatory principles. Retail rates and earnings are reviewed and may be adjusted periodically within certain limitations. Prices for wholesale electricity sales, interconnecting transmission lines, and the exchange of electric power are regulated by the FERC. See "FERC Matters" herein, ACCOUNTING POLICIES – "Application of Critical Accounting Policies and Estimates – Utility Regulation" herein, and Note 3 to the financial statements for additional information about regulatory matters.

The results of operations for the past three years are not necessarily indicative of future earnings potential. The level of the Company's future earnings depends on numerous factors that affect the opportunities, challenges, and risks of the Company's business of providing electric service. These factors include the Company's ability to recover its prudently-incurred costs, in a timely manner during a time of increasing costs, and its ability to prevail against legal challenges associated with the Kemper County energy facility. Future earnings will be driven primarily by customer growth. Earnings will also depend upon maintaining and growing sales, considering, among other things, the adoption and/or penetration rates of increasingly energy-efficient technologies and increasing volumes of electronic commerce transactions, both of which could contribute to a net reduction in customer usage. Earnings are subject to a variety of other factors. These factors include weather, competition, developing new and maintaining existing energy contracts and associated load requirements with other utilities and other wholesale customers, energy conservation practiced by customers, the use of alternative energy sources by customers, the price of electricity, the price elasticity of demand, and the rate of economic growth or decline in the Company's service territory. Demand for electricity is primarily driven by the pace of economic growth that may be affected by changes in regional and global economic conditions, which may impact future earnings.

The Company's retail base rates are set under the PEP, a rate plan approved by the Mississippi PSC. Two filings are made for each calendar year: the PEP projected filing, which is typically filed prior to the beginning of the year based on a projected revenue requirement, and the PEP lookback filing, which is filed after the end of the year and allows for review of the actual return compared to the allowed return range. See "Retail Regulatory Matters" herein and Note 3 to the financial statements under "Retail Regulatory Matters – Performance Evaluation Plan" for more information.

On October 4, 2017, the Company executed agreements with its largest retail customer, Chevron Products Company (Chevron), to continue providing retail service to the Chevron refinery in Pascagoula, Mississippi through 2038, subject to the approval of the Mississippi PSC. The new agreements are not expected to have a material impact on the Company's earnings; however, the co-generation assets located at the refinery are expected to be accounted for as a sales-type lease in accordance with the new lease accounting rules that become effective in 2019. These assets are also subject to a security interest granted to Chevron. See

FINANCIAL CONDITION AND LIQUIDITY – "Credit Rating Risk" herein for additional information. The ultimate outcome of this matter cannot be determined at this time.

On December 22, 2017, Tax Reform Legislation was signed into law and became effective on January 1, 2018, which among other things, reduces the federal corporate income tax rate to 21% and changes rates of depreciation and the business interest deduction. See "Income Tax Matters – Federal Tax Reform Legislation" and FINANCIAL CONDITION AND LIQUIDITY – "Credit Rating Risk" herein and Notes 3 and 5 to the financial statements for additional information.

The Company provides service under long-term contracts with rural electric cooperative associations and municipalities located in southeastern Mississippi under cost-based electric tariffs which are subject to regulation by the FERC. The contracts with these wholesale customers represented 19.3% of the Company's total operating revenues in 2017 and are largely subject to rolling 10-year cancellation notices. Historically, these wholesale customers have acted as a group and any changes in contractual relationships for one customer are likely to be followed by the other wholesale customers.

Environmental Matters

The Company's operations are regulated by state and federal environmental agencies through a variety of laws and regulations governing air, water, land, and protection of other natural resources. The Company maintains a comprehensive environmental compliance strategy to assess upcoming requirements and compliance costs associated with these environmental laws and regulations. The costs, including capital expenditures and operations and maintenance costs, required to comply with environmental laws and regulations may impact future unit retirement and replacement decisions, results of operations, cash flows, and financial condition. Compliance costs may result from the installation of additional environmental controls, closure and monitoring of CCR facilities, unit retirements, and adding or changing fuel sources for certain existing units, as well as related upgrades to the transmission system. A major portion of these compliance costs are expected to be recovered through existing ratemaking provisions. The ultimate impact of the environmental laws and regulations discussed below will depend on various factors, such as state adoption and implementation of requirements, the availability and cost of any deployed control technology, and the outcome of pending and/or future legal challenges.

New or revised environmental laws and regulations could affect many areas of the Company's operations. The impact of any such changes cannot be determined at this time. Environmental compliance costs could affect earnings if such costs cannot continue to be fully recovered in rates on a timely basis or through long-term wholesale agreements. Further, increased costs that are recovered through regulated rates could contribute to reduced demand for electricity, which could negatively affect results of operations, cash flows, and financial condition. Additionally, many commercial and industrial customers may also be affected by existing and future environmental requirements, which for some may have the potential to ultimately affect their demand for electricity. See Note 3 to the financial statements under "Retail Regulatory Matters – Environmental Compliance Overview Plan" for additional information.

Through 2017, the Company has invested approximately $643 million in environmental capital retrofit projects to comply with environmental requirements, with annual totals of approximately $9 million, $17 million, and $94 million for 2017, 2016, and 2015, respectively. Although the timing, requirements, and estimated costs could change as environmental laws and regulations are adopted or modified, as compliance plans are revised or updated, and as legal challenges to rules are initiated or completed, the Company's current compliance strategy estimates capital expenditures of $63 million from 2018 through 2022, with annual totals of approximately $14 million, $16 million, $17 million, $13 million, and $3 million for 2018, 2019, 2020, 2021, and 2022, respectively. These estimates do not include any potential compliance costs associated with the regulation of CO_2 emissions from fossil fuel-fired electric generating units. See "Global Climate Issues" herein for additional information. The Company also anticipates expenditures associated with ash pond closure and ground water monitoring under the Disposal of Coal Combustion Residuals from Electric Utilities rule (CCR Rule), which are reflected in the Company's ARO liabilities. See FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" herein and Note 1 to the financial statements under "Asset Retirement Obligations and Other Costs of Removal" for additional information.

Environmental Laws and Regulations

Air Quality

The EPA has set National Ambient Air Quality Standards (NAAQS) for six air pollutants (carbon monoxide, lead, nitrogen dioxide, ozone, particulate matter, and SO_2), which it reviews and revises periodically. Revisions to these standards can require additional emission controls, improvements in control efficiency, or fuel changes which can result in increased compliance and operational costs. NAAQS requirements can also adversely affect the siting of new facilities. In 2015, the EPA published a more stringent eight-hour ozone NAAQS. The EPA plans to complete designations for this rule by no later than April 30, 2018. No areas within the Company's service territory have been or are anticipated to be designated nonattainment under the 2015 ozone

NAAQS. In 2010, the EPA revised the NAAQS for SO_2, establishing a new one-hour standard, and is completing designations in multiple phases. The EPA has issued several rounds of area designations and no areas in the vicinity of Company-owned SO_2 sources have been designated nonattainment under the 2010 one-hour SO_2 NAAQS. However, final eight-hour ozone and SO_2 one-hour designations for certain areas are still pending and, if other areas are designated as nonattainment in the future, increased compliance costs could result.

In 2011, the EPA finalized the Cross-State Air Pollution Rule (CSAPR) and its NO_X annual, NO_X seasonal, and SO_2 annual programs. CSAPR is an emissions trading program that addresses the impacts of the interstate transport of SO_2 and NO_X emissions from fossil fuel-fired power plants located in upwind states in the eastern half of the U.S. on air quality in downwind states. The Company has fossil fuel-fired generation subject to these requirements. In October 2016, the EPA published a final rule that revised the CSAPR seasonal NO_X program, establishing more stringent NO_X emissions budgets in Alabama and Mississippi. The outcome of ongoing CSAPR litigation, to which the Company is a party, could have an impact on the State of Mississippi's allowance allocations under the CSAPR seasonal NO_X program. Increases in either future fossil fuel-fired generation or the cost of CSAPR allowances could have a negative financial impact on results of operations for the Company.

The EPA finalized regional haze regulations in 2005 and 2017. These regulations require states, tribal governments, and various federal agencies to develop and implement plans to reduce pollutants that impair visibility and demonstrate reasonable progress toward the goal of restoring natural visibility conditions in certain areas, including national parks and wilderness areas. States must submit a revised state implementation plan (SIP) to the EPA by July 31, 2021, demonstrating reasonable progress towards achieving visibility improvement goals. State implementation of reasonable progress could require further reductions in SO_2 or NO_X emissions, which could result in increased compliance costs.

In 2015, the EPA published a final rule requiring certain states (including Alabama and Mississippi) to revise or remove the provisions of their SIPs regulating excess emissions at industrial facilities, including electric generating facilities, during periods of startup, shut-down, or malfunction (SSM). The state excess emission rules provide necessary operational flexibility to affected units during periods of SSM and, if removed, could affect unit availability and result in increased operations and maintenance costs for the Company. The EPA has not yet responded to the SIP revisions proposed by states where the Company's generating units are located.

Water Quality

In 2014, the EPA finalized requirements under Section 316(b) of the Clean Water Act (CWA) to regulate cooling water intake structures at existing power plants and manufacturing facilities in order to minimize their effects on fish and other aquatic life. The regulation requires plant-specific studies to determine applicable measures to protect organisms that either get caught on the intake screens (impingement) or are drawn into the cooling system (entrainment). The ultimate impact of this rule will depend on the outcome of these plant-specific studies and any additional protective measures required to be incorporated into each plant's National Pollutant Discharge Elimination System (NPDES) permit based on site-specific factors.

In 2015, the EPA finalized the steam electric effluent limitations guidelines (ELG) rule that set national standards for wastewater discharges from steam electric generating units. The rule prohibits effluent discharges of certain wastestreams and imposes stringent arsenic, mercury, selenium, and nitrate/nitrite limits on scrubber wastewater discharges. The revised technology-based limits and compliance dates may require extensive modifications to existing ash and wastewater management systems or the installation and operation of new ash and wastewater management systems. Compliance with the ELG rule is expected to require capital expenditures and increased operational costs primarily affecting the Company's coal-fired electric generation. Compliance applicability dates range from November 1, 2018 to December 31, 2023 with state environmental agencies incorporating specific applicability dates in the NPDES permitting process based on information provided for each waste stream. The EPA has committed to a new rulemaking that could potentially revise the limitations and applicability dates of the ELG rule. The EPA expects to finalize this rulemaking in 2020.

In 2015, the EPA and the U.S. Army Corps of Engineers (Corps) jointly published a final rule that revised the regulatory definition of waters of the United States (WOTUS) for all CWA programs. The rule significantly expanded the scope of federal jurisdiction over waterbodies (such as rivers, streams, and canals), which could impact new generation projects and permitting and reporting requirements associated with the installation, expansion, and maintenance of transmission and distribution projects. On July 27, 2017, the EPA and the Corps proposed to rescind the 2015 WOTUS rule. The WOTUS rule has been stayed by the U.S. Court of Appeals for the Sixth Circuit since late 2015, but on January 22, 2018, the U.S. Supreme Court determined that federal district courts have jurisdiction over the pending challenges to the rule. On February 6, 2018, the EPA and the Corps published a final rule delaying implementation of the 2015 WOTUS rule to 2020.

Coal Combustion Residuals

In 2015, the EPA finalized non-hazardous solid waste regulations for the disposal of CCR, including coal ash and gypsum, in landfills and surface impoundments (CCR units) at active generating power plants. The CCR Rule requires CCR units to be evaluated against a set of performance criteria and potentially closed if minimum criteria are not met. Closure of existing CCR units could require installation of equipment and infrastructure to manage CCR in accordance with the rule. The EPA has announced plans to reconsider certain portions of the CCR Rule by no later than December 2019, which could result in changes to deadlines and corrective action requirements.

The EPA's reconsideration of the CCR Rule is due in part to a legislative development that impacts the potential oversight role of state agencies. Under the Water Infrastructure Improvements for the Nation Act, which became law in 2016, states are allowed to establish permit programs for implementing the CCR Rule.

Based on cost estimates for closure and monitoring of ash ponds pursuant to the CCR Rule, the Company recorded AROs for each CCR unit in 2015. As further analysis is performed and closure details are developed, the Company will continue to periodically update these cost estimates as necessary. In December 2016, the Mississippi PSC granted a CPCN to the Company authorizing certain projects associated with complying with the CCR Rule. Additionally in this order, the Mississippi PSC also authorized the Company to recover any costs associated with the CPCN, including future monitoring costs, through the ECO clause. See FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" herein and Note 1 to the financial statements under "Asset Retirement Obligations and Other Costs of Removal" for additional information regarding the Company's AROs as of December 31, 2017.

Environmental Remediation

The Company must comply with environmental laws and regulations governing the handling and disposal of waste and releases of hazardous substances. Under these various laws and regulations, the Company may also incur substantial costs to clean up affected sites. The Company has authority from the Mississippi PSC to recover approved environmental compliance costs through established regulatory mechanisms. The Company recognizes a liability for environmental remediation costs only when it determines a loss is probable and reasonably estimable.

Global Climate Issues

In 2015, the EPA published final rules limiting CO_2 emissions from new, modified, and reconstructed fossil fuel-fired electric generating units and guidelines for states to develop plans to meet EPA-mandated CO_2 emission performance standards for existing units (known as the Clean Power Plan or CPP). In February 2016, the U.S. Supreme Court granted a stay of the CPP, which will remain in effect through the resolution of litigation in the U.S. Court of Appeals for the District of Columbia challenging the legality of the CPP and any review by the U.S. Supreme Court. On March 28, 2017, the U.S. President signed an executive order directing agencies to review actions that potentially burden the development or use of domestically produced energy resources, including review of the CPP and other CO_2 emissions rules. On October 10, 2017, the EPA published a proposed rule to repeal the CPP and, on December 28, 2017, published an advanced notice of proposed rulemaking regarding a CPP replacement rule.

In 2015, parties to the United Nations Framework Convention on Climate Change, including the United States, adopted the Paris Agreement, which established a non-binding universal framework for addressing greenhouse gas (GHG) emissions based on nationally determined contributions. On June 1, 2017, the U.S. President announced that the United States would withdraw from the Paris Agreement and begin renegotiating its terms. The ultimate impact of this agreement or any renegotiated agreement depends on its implementation by participating countries.

The EPA's GHG reporting rule requires annual reporting of GHG emissions expressed in terms of metric tons of CO_2 equivalent emissions for a company's operational control of facilities. Based on ownership or financial control of facilities, the Company's 2016 GHG emissions were approximately 7 million metric tons of CO_2 equivalent. The preliminary estimate of the Company's 2017 GHG emissions on the same basis is approximately 8 million metric tons of CO_2 equivalent.

FERC Matters

Municipal and Rural Associations Tariff

The Company provides wholesale electric service to Cooperative Energy, East Mississippi Electric Power Association, and the City of Collins, all located in southeastern Mississippi, under a long-term cost-based, FERC regulated MRA tariff.

In March 2016, the Company reached a settlement agreement with its wholesale customers, which was subsequently approved by the FERC, for an increase in wholesale base revenues under the MRA cost-based electric tariff, primarily as a result of placing scrubbers for Plant Daniel Units 1 and 2 in service in 2015. The settlement agreement became effective for services rendered beginning May 1, 2016, resulting in an estimated annual revenue increase of $7 million under the MRA cost-based electric tariff. Additionally, under the settlement agreement, the tariff customers agreed to similar regulatory treatment for MRA tariff ratemaking as the treatment approved for retail ratemaking under the In-Service Asset Rate Order. This regulatory treatment primarily includes (i) recovery of the operational Kemper County energy facility assets providing service to customers and other related costs, (ii) amortization of the Kemper County energy facility-related regulatory assets included in rates under the settlement agreement over the 36 months ending April 30, 2019, (iii) Kemper County energy facility-related expenses included in rates under the settlement agreement no longer being deferred and charged to expense, and (iv) removing all of the Kemper County energy facility CWIP from rate base with a corresponding increase in accrual of AFUDC. The additional resulting AFUDC totaled approximately $22 million through the suspension of Kemper IGCC start-up activities and has been recorded as a charge to income.

The Company expects to make a subsequent MRA filing during the second quarter 2018. The filing is intended to be consistent with the February 6, 2018 Mississippi PSC order for cost recovery of the Kemper County energy facility, including the impact of Tax Reform Legislation. The ultimate outcome of this matter cannot be determined at this time.

On September 18, 2017, the Company and Cooperative Energy executed a Shared Service Agreement (SSA), as part of the MRA tariff, under which the Company and Cooperative Energy will share in providing electricity to all Cooperative Energy delivery points, in lieu of the current arrangement under which each delivery point is specifically assigned to either entity. The SSA accepted by the FERC on October 31, 2017 became effective on January 1, 2018 and may be cancelled by Cooperative Energy with 10 years notice after December 31, 2020. The SSA provides Cooperative Energy the option to decrease its use of the Company's generation services under the MRA tariff, subject to annual and cumulative caps and a one-year notice requirement. In the event Cooperative Energy elects to reduce these services, the related reduction in the Company's revenues is not expected to be significant through 2020.

Fuel Cost Recovery

The Company has a wholesale MRA and a Market Based (MB) fuel cost recovery factor. Effective with the first billing cycle for September 2016, fuel rates decreased $11 million annually for wholesale MRA customers and $1 million annually for wholesale MB customers. Effective January 1, 2018, the wholesale MRA fuel rate increased $11 million annually. At December 31, 2017, over-recovered wholesale MRA fuel costs were immaterial and at December 31, 2016 were approximately $13 million, which is included in over-recovered regulatory clause liabilities, current in the balance sheets.

The Company's operating revenues are adjusted for differences in actual recoverable fuel cost and amounts billed in accordance with the currently approved cost recovery rate. Accordingly, changes in the billing factor should have no significant effect on the Company's revenues or net income, but will affect cash flow.

Market-Based Rate Authority

The Company has authority from the FERC to sell electricity at market-based rates. Since 2008, that authority, for certain balancing authority areas, has been conditioned on compliance with the requirements of an energy auction, which the FERC found to be tailored mitigation that addresses potential market power concerns. In accordance with FERC regulations governing such authority, the traditional electric operating companies (including the Company) and Southern Power filed a triennial market power analysis in 2014, which included continued reliance on the energy auction as tailored mitigation. In 2015, the FERC issued an order finding that the traditional electric operating companies' (including the Company's) and Southern Power's existing tailored mitigation may not effectively mitigate the potential to exert market power in certain areas served by the traditional electric operating companies and in some adjacent areas. The FERC directed the traditional electric operating companies (including the Company) and Southern Power to show why market-based rate authority should not be revoked in these areas or to provide a mitigation plan to further address market power concerns. The traditional electric operating companies (including the Company) and Southern Power filed a request for rehearing and filed their response with the FERC in 2015.

In December 2016, the traditional electric operating companies (including the Company) and Southern Power filed an amendment to their market-based rate tariff that proposed certain changes to the energy auction, as well as several non-tariff changes. On February 2, 2017, the FERC issued an order accepting all such changes subject to an additional condition of cost-based price caps for certain sales outside of the energy auction, finding that all of these changes would provide adequate alternative mitigation for the traditional electric operating companies' (including the Company's) and Southern Power's potential to exert market power in certain areas served by the traditional electric operating companies (including the Company) and in some adjacent areas. On May 17, 2017, the FERC accepted the traditional electric operating companies' (including the Company's) and Southern Power's compliance filing accepting the terms of the order. While the FERC's February 2, 2017 order references the market power proceeding discussed above, it remains a separate, ongoing matter.

On October 25, 2017, the FERC issued an order in response to the traditional electric operating companies' (including the Company's) and Southern Power's June 29, 2017 triennial updated market power analysis. The FERC directed the traditional electric operating companies (including the Company) and Southern Power to show cause within 60 days why market-based rate authority should not be revoked in certain areas adjacent to the area presently under mitigation in accordance with the February 2, 2017 order or to provide a mitigation plan to further address market power concerns. On November 10, 2017, the traditional electric operating companies (including the Company) and Southern Power responded to the FERC and proposed to resolve matters by applying the alternative mitigation authorized by the February 2, 2017 order to the adjacent areas made the subject of the October 25, 2017 order.

The ultimate outcome of these matters cannot be determined at this time.

Cooperative Energy Power Supply Agreement

In 2008, the Company entered into a 10-year Power Supply Agreement (PSA) with Cooperative Energy for approximately 152 MWs, which became effective in 2011. Following certain plant retirements, the PSA capacity was reduced to 86 MWs. On February 5, 2018, the Company and Cooperative Energy executed an amendment to extend the PSA through March 31, 2021, effective April 1, 2018, with increased total capacity of 286 MWs.

Cooperative Energy also has a 10-year Network Integration Transmission Service Agreement (NITSA) with SCS for transmission service to certain delivery points on the Company's transmission system that became effective in 2011. As a result of the PSA amendments, Cooperative Energy and SCS amended the terms of the NITSA on January 12, 2018 to provide for the purchase of incremental transmission capacity for service beginning April 1, 2018 through March 31, 2021. This NITSA amendment remains subject to acceptance by the FERC. The ultimate outcome of these matters cannot be determined at this time.

Retail Regulatory Matters

General

The Company's rates and charges for service to retail customers are subject to the regulatory oversight of the Mississippi PSC. The Company's rates are a combination of base rates and several separate cost recovery clauses for specific categories of costs. These separate cost recovery clauses address such items as fuel and purchased power, energy efficiency programs, ad valorem taxes, property damage, and the costs of compliance with environmental laws and regulations. Costs not addressed through one of the specific cost recovery clauses are expected to be recovered through the Company's base rates. See Note 3 to the financial statements under "Retail Regulatory Matters" and "Kemper County Energy Facility" for additional information.

In 2012, the Mississippi PSC issued an order for the purpose of investigating and reviewing, for informational purposes only, the ROE formulas used by the Company and all other regulated electric utilities in Mississippi. In 2013, the MPUS filed with the Mississippi PSC its report on the ROE formulas used by the Company and all other regulated electric utilities in Mississippi.

In 2014, the Mississippi PSC issued an order for the purpose of investigating and reviewing the adoption of a uniform formula rate plan for the Company and other regulated electric utilities in Mississippi.

On January 26, 2018, the Mississippi PSC issued an order directing utilities to file within 30 days information regarding the impact on rates resulting from Tax Reform Legislation. The Company's Kemper County energy facility rates, approved on February 6, 2018, include the effects of Tax Reform Legislation. The Company's 2018 ECO, revised 2018 PEP, and 2018 SRR rate filings, all submitted in February 2018, include the effects of Tax Reform Legislation and are subject to approval by the Mississippi PSC.

The ultimate outcome of these matters cannot be determined at this time.

Performance Evaluation Plan

The Company's retail base rates are set under the PEP, a rate plan approved by the Mississippi PSC. Two filings are made for each calendar year: the PEP projected filing, which is typically filed prior to the beginning of the year based on a projected revenue requirement, and the PEP lookback filing, which is filed after the end of the year and allows for review of the actual revenue requirement compared to the projected filing.

In 2011, the Company submitted its annual PEP lookback filing for 2010, which recommended no surcharge or refund. Later in 2011, the MPUS disputed certain items in the 2010 PEP lookback filing. In 2012, the Mississippi PSC issued an order canceling the Company's PEP lookback filing for 2011. In 2013, the MPUS contested the Company's PEP lookback filing for 2012, which indicated a refund due to customers of $5 million. Unresolved matters related to the 2010 PEP lookback filing, which remain under review, also impact the 2012 PEP lookback filing.

In 2013, the Mississippi PSC approved the projected PEP filing for 2013, which resulted in a rate increase of 1.9%, or $15 million, annually, effective March 19, 2013. The Company may be entitled to $3 million in additional revenues related to 2013 as a result of the late implementation of the 2013 PEP rate increase.

In 2014, 2015, 2016, and 2017, the Company submitted its annual PEP lookback filings for the prior years, which for 2013 and 2014 each indicated no surcharge or refund and for each of 2015 and 2016 indicated a $5 million surcharge. Additionally, in July 2016, in November 2016, and on November 15, 2017, the Company submitted its annual projected PEP filings for 2016, 2017, and 2018, respectively, which for 2016 and 2017 indicated no change in rates and for 2018 indicated a rate increase of 4%, or $38 million in annual revenues. The Mississippi PSC suspended each of these filings to allow more time for review.

On February 7, 2018, the Company revised its annual projected PEP filing for 2018 to reflect the impacts of Tax Reform Legislation. The revised filing requests an increase of $26 million in annual revenues, based on a performance adjusted ROE of 9.33% and an increased equity ratio of 55%. See FUTURE EARNINGS POTENTIAL – "Income Tax Matters – Federal Tax Reform Legislation" herein and Note 5 to the financial statements for additional information.

The ultimate outcome of these matters cannot be determined at this time.

Energy Efficiency

In 2013, the Mississippi PSC approved an energy efficiency and conservation rule requiring electric and gas utilities in Mississippi serving more than 25,000 customers to implement energy efficiency programs and standards. Quick Start Plans, which include a portfolio of energy efficiency programs that are intended to provide benefits to a majority of customers, were extended by an order issued by the Mississippi PSC in July 2016, until the time the Mississippi PSC approves a comprehensive portfolio plan program. The ultimate outcome of this matter cannot be determined at this time.

On July 6, 2017, the Mississippi PSC issued an order approving the Company's Energy Efficiency Cost Rider 2017 compliance filing, which increased annual retail revenues by approximately $2 million effective with the first billing cycle for August 2017.

On November 30, 2017, the Company submitted its Energy Efficiency Cost Rider 2018 compliance filing, which included a small decrease in annual retail revenues. The ultimate outcome of this matter cannot be determined at this time.

See Note 3 to the financial statements under "Retail Regulatory Matters" for additional information.

Environmental Compliance Overview Plan

In 2012, the Mississippi PSC approved the Company's request for a CPCN to construct scrubbers on Plant Daniel Units 1 and 2, which were placed in service in 2015. These units are jointly owned by the Company and Gulf Power, with 50% ownership each. In 2014, the Company entered into a settlement agreement with the Sierra Club under which, among other things, the Company agreed to retire, repower with natural gas, or convert to an alternative non-fossil fuel source Plant Sweatt Units 1 and 2 (80 MWs) no later than December 2018 (and the units were retired in July 2016). The Company also agreed that it would cease burning coal and other solid fuel at Plant Watson Units 4 and 5 (750 MWs) and begin operating those units solely on natural gas no later than April 2015 (which occurred in April 2015) and cease burning coal and other solid fuel at Plant Greene County Units 1 and 2 (200 MWs) no later than April 2016 (which occurred in February and March 2016, respectively) and begin operating those units solely on natural gas (which occurred in June and July 2016, respectively).

In accordance with a 2011 accounting order from the Mississippi PSC, the Company has the authority to defer in a regulatory asset for future recovery all plant retirement- or partial retirement-related costs resulting from environmental regulations. The Mississippi PSC approved $41 million and $17 million of costs that were reclassified to regulatory assets associated with Plant Watson and Plant Greene County, respectively, for amortization over five-year periods that began in July 2016 and July 2017, respectively. As a result, these decisions are not expected to have a material impact on the Company's financial statements.

In August 2016, the Mississippi PSC approved the Company's revised ECO plan filing for 2016, which requested the maximum 2% annual increase in revenues, or approximately $18 million, primarily related to the Plant Daniel Units 1 and 2 scrubbers placed in service in 2015. The revised rates became effective with the first billing cycle for September 2016. Approximately $22 million of related revenue requirements in excess of the 2% maximum was deferred for inclusion in the 2017 filing, along with related carrying costs.

On May 4, 2017, the Mississippi PSC approved the Company's ECO plan filing for 2017, which requested the maximum 2% annual increase in revenues, or approximately $18 million, primarily related to the carryforward from the prior year. The rates became effective with the first billing cycle for June 2017. Approximately $26 million of related revenue requirements in excess of the 2% maximum was deferred for inclusion in the 2018 filing, along with related carrying costs.

On February 14, 2018, the Company submitted its ECO plan filing for 2018, including the effects of Tax Reform Legislation, which requested the maximum 2% annual increase in revenues, or approximately $17 million, primarily related to the carryforward from the prior year. Approximately $13 million of related revenue requirements in excess of the 2% maximum, along with related carrying costs, remains deferred for inclusion in the 2019 filing. The ultimate outcome of this matter cannot be determined at this time.

Fuel Cost Recovery

The Company establishes, annually, a retail fuel cost recovery factor that is approved by the Mississippi PSC. The Company is required to file for an adjustment to the retail fuel cost recovery factor annually. On January 12, 2017, the Mississippi PSC approved the 2017 retail fuel cost recovery factor, effective February 2017 through January 2018, which resulted in an annual revenue increase of approximately $55 million. On November 15, 2017, the Company filed its annual rate adjustment under the retail fuel cost recovery clause, requesting an additional increase of $39 million annually, which the Mississippi PSC approved on January 16, 2018 effective February 2018 through January 2019. At December 31, 2017, the amount of under-recovered retail fuel costs included in the balance sheet in customer accounts receivable was approximately $6 million compared to $37 million over recovered at December 31, 2016.

The Company's operating revenues are adjusted for differences in actual recoverable fuel cost and amounts billed in accordance with the currently approved cost recovery rate. Accordingly, changes in the billing factor should have no significant effect on the Company's revenues or net income, but will affect cash flow.

Ad Valorem Tax Adjustment

The Company establishes, annually, an ad valorem tax adjustment factor that is approved by the Mississippi PSC to collect the ad valorem taxes paid by the Company. On July 6, 2017, the Mississippi PSC approved the Company's annual ad valorem tax adjustment factor filing for 2017, which included an annual rate increase of 0.85%, or $8 million in annual retail revenues, primarily due to increased assessments.

System Restoration Rider

In February 2016, the Company submitted its 2016 SRR rate filing which proposed no changes to either the SRR rate or the annual property damage reserve accrual of $3 million annually. On February 3, 2017, the Company submitted its 2017 SRR rate filing, which proposed an increase in the property damage reserve accrual of $1 million. These filings were suspended by the Mississippi PSC for review.

On January 21, 2017, a tornado caused extensive damage to the Company's transmission and distribution infrastructure. Storm damage repairs were approximately $9 million. A portion of these costs was charged to the retail property damage reserve and was addressed in the 2018 SRR rate filing.

On February 1, 2018, the Company submitted its 2018 SRR rate filing, including the effects of Tax Reform Legislation, which proposed that the SRR rate remain at zero and the annual accrual for the property damage reserve be reduced to $2 million in 2018.

The ultimate outcome of these matters cannot be determined at this time. See Note 1 to the financial statements under "Provision for Property Damage" for additional information.

Storm Damage Cost Recovery

In connection with the damage associated with Hurricane Katrina, the Mississippi PSC authorized the issuance of system restoration bonds in 2006. In accordance with a Mississippi PSC order on January 24, 2017, the Company eliminated the applicable Storm Restoration Charge because the bond sinking fund managed by the Mississippi State Bond Commission is substantially funded.

Kemper County Energy Facility

Overview

The Kemper County energy facility was designed to utilize IGCC technology with an expected output capacity of 582 MWs and to be fueled by locally mined lignite (an abundant, lower heating value coal) from a mine owned by the Company and situated adjacent to the Kemper County energy facility. The mine, operated by North American Coal Corporation, started commercial operation in 2013. In connection with the Kemper County energy facility construction, the Company constructed approximately 61 miles of CO_2 pipeline infrastructure for the transport of captured CO_2 for use in enhanced oil recovery.

Schedule and Cost Estimate

In 2012, the Mississippi PSC issued the 2012 MPSC CPCN Order, confirming the CPCN originally approved by the Mississippi PSC in 2010 authorizing the acquisition, construction, and operation of the Kemper County energy facility. The certificated cost estimate of the Kemper County energy facility included in the 2012 MPSC CPCN Order was $2.4 billion, net of approximately $0.57 billion in Cost Cap Exceptions. The 2012 MPSC CPCN Order approved a construction cost cap of up to $2.88 billion, with recovery of prudently-incurred costs subject to approval by the Mississippi PSC. The Kemper County energy facility was originally projected to be placed in service in May 2014. The Company placed the combined cycle and the associated common facilities portion of the Kemper County energy facility in service in August 2014.

The initial production of syngas began on July 14, 2016 for gasifier "B" and on September 13, 2016 for gasifier "A." The Company achieved integrated operation of both gasifiers on January 29, 2017, including the production of electricity from syngas in both combustion turbines. During testing, the plant produced and captured CO_2, and produced sulfuric acid and ammonia, each of acceptable quality under the related off-take agreements. However, the Company experienced numerous challenges during the extended start-up process to achieve integrated operation of the gasifiers on a sustained basis. In May 2017, after achieving these milestones, the Company determined that a critical system component, the syngas coolers, would need replacement sooner than originally planned, which would require significant lead time and significant cost. In addition, the long-term natural gas price forecast had decreased significantly and the estimated cost of operating and maintaining the facility during the first five full years of operations had increased significantly since certification.

On June 21, 2017, the Mississippi PSC stated its intent to issue an order (which occurred on July 6, 2017) directing the Company to pursue a settlement under which the Kemper County energy facility would be operated as a natural gas plant, rather than an IGCC plant, and address all issues associated with the Kemper County energy facility. On June 28, 2017, the Company notified the Mississippi PSC that it would begin a process to suspend operations and start-up activities on the gasifier portion of the Kemper County energy facility, given the uncertainty as to its future.

At the time of project suspension in June 2017, the total cost estimate for the Kemper County energy facility was approximately $7.38 billion, including approximately $5.95 billion of costs subject to the construction cost cap, and was net of the $137 million in Additional DOE Grants. In the aggregate, the Company had recorded charges to income of $3.07 billion ($1.89 billion after tax) as a result of changes in the cost estimate above the cost cap for the Kemper IGCC through May 31, 2017.

Given the Mississippi PSC's stated intent regarding no further rate increase for the Kemper County energy facility and the subsequent suspension, cost recovery of the gasifier portions became no longer probable; therefore, the Company recorded an additional charge to income in June 2017 of $2.8 billion ($2.0 billion after tax), which included estimated costs associated with the gasifier portions of the plant and lignite mine. During the third and fourth quarters of 2017, the Company recorded charges to income of $242 million ($206 million after tax), including $164 million for ongoing project costs, estimated mine and gasifier-related costs, and certain termination costs during the suspension period prior to conclusion of the Kemper Settlement Docket, as well as the charge associated with the Kemper Settlement Agreement discussed below. Additional pre-tax cancellation costs, including mine and plant closure and contract termination costs, currently estimated at approximately $50 million to $100 million (excluding salvage), are expected to be incurred in 2018. The Company has begun efforts to dispose of or abandon the mine and gasifier-related assets.

Rate Recovery

Kemper Settlement Agreement

On February 6, 2018, the Mississippi PSC voted to approve the Kemper Settlement Agreement. The Kemper Settlement Agreement provides for an annual revenue requirement of approximately $99.3 million for costs related to the Kemper County energy facility, which includes the impact of Tax Reform Legislation. The revenue requirement is based on (i) a fixed ROE for 2018 of 8.6% excluding any performance adjustment, (ii) a ROE for 2019 calculated in accordance with PEP, excluding the performance adjustment, (iii) for future years, a performance-based ROE calculated pursuant to PEP, and (iv) amortization periods for the related regulatory assets and liabilities of eight years and six years, respectively. The revenue requirement also reflects a disallowance related to a portion of the Company's investment in the Kemper County energy facility requested for inclusion in rate base, which was recorded in the fourth quarter 2017 as an additional charge to income of approximately $78 million ($85 million net of accumulated depreciation of $7 million) pre-tax ($48 million after tax).

Under the Kemper Settlement Agreement, retail customer rates will reflect a reduction of approximately $26.8 million annually and include no recovery for costs associated with the gasifier portion of the Kemper County energy facility in 2018 or at any future date. On February 12, 2018, the Company made the required compliance filing with the Mississippi PSC. The Kemper

Settlement Agreement also requires (i) the CPCN for the Kemper County energy facility to be modified to limit it to natural gas combined cycle operation and (ii) the Company to file a reserve margin plan with the Mississippi PSC by August 2018.

As of December 31, 2017, the balances associated with the Kemper County energy facility regulatory assets and liabilities were $114 million and $26 million, respectively.

As a result of the Mississippi PSC order on February 6, 2018, rate recovery for the Kemper County energy facility is resolved, subject to any future legal challenges.

2015 Rate Case

On December 3, 2015, the Mississippi PSC issued the In-Service Asset Rate Order regarding the Kemper County energy facility assets that were commercially operational and currently providing service to customers (the transmission facilities, combined cycle, natural gas pipeline, and water pipeline) and other related costs. The In-Service Asset Rate Order provided for retail rate recovery of an annual revenue requirement of approximately $126 million, based on the Company's actual average capital structure, with a maximum common equity percentage of 49.733%, a 9.225% return on common equity, and actual embedded interest costs. The In-Service Asset Rate Order also included a prudence finding of all costs in the stipulated revenue requirement calculation for the in-service assets.

In connection with the implementation of the In-Service Asset Rate Order and wholesale rates, the Company began expensing certain ongoing project costs and certain retail debt carrying costs that previously were deferred and began amortizing certain regulatory assets associated with assets placed in service and consulting and legal fees over periods ranging from two years to 10 years. On July 6, 2017, the Mississippi PSC issued an order requiring the Company to establish a regulatory liability account to maintain current rates related to the Kemper County energy facility following the July 2017 completion of the amortization period for certain of these regulatory assets. See "FERC Matters" herein for additional information related to the 2016 settlement agreement with wholesale customers.

Lignite Mine and CO_2 Pipeline Facilities

The Company owns the lignite mine and equipment and mineral reserves located around the Kemper County energy facility site. The mine started commercial operation in June 2013.

In 2010, the Company executed a 40-year management fee contract with Liberty Fuels Company, LLC (Liberty Fuels), a wholly-owned subsidiary of The North American Coal Corporation, which developed, constructed, and is responsible for the mining operations through the end of the mine reclamation. As the mining permit holder, Liberty Fuels has a legal obligation to perform mine reclamation and the Company has a contractual obligation to fund all reclamation activities. The Company expects mine reclamation to begin in 2018. In addition to the obligation to fund the reclamation activities, the Company provided working capital support to Liberty Fuels through cash advances for capital purchases, payroll, and other operating expenses. See Note 1 to the financial statements under "Asset Retirement Obligations and Other Costs of Removal" and "Variable Interest Entities" for additional information.

In addition, the Company constructed the CO_2 pipeline for the planned transport of captured CO_2 for use in enhanced oil recovery and entered into an agreement with Denbury Onshore (Denbury) to purchase the captured CO_2. Denbury has the right to terminate the contract at any time because the Company did not place the Kemper IGCC in service by July 1, 2017.

The ultimate outcome of these matters cannot be determined at this time.

Litigation

On April 26, 2016, a complaint against the Company was filed in Harrison County Circuit Court (Circuit Court) by Biloxi Freezing & Processing Inc., Gulfside Casino Partnership, and John Carlton Dean, which was amended and refiled on July 11, 2016 to include, among other things, Southern Company as a defendant. The individual plaintiff alleges that the Company and Southern Company violated the Mississippi Unfair Trade Practices Act. All plaintiffs have alleged that the Company and Southern Company concealed, falsely represented, and failed to fully disclose important facts concerning the cost and schedule of the Kemper County energy facility and that these alleged breaches have unjustly enriched the Company and Southern Company. The plaintiffs seek unspecified actual damages and punitive damages; ask the Circuit Court to appoint a receiver to oversee, operate, manage, and otherwise control all affairs relating to the Kemper County energy facility; ask the Circuit Court to revoke any licenses or certificates authorizing the Company or Southern Company to engage in any business related to the Kemper County energy facility in Mississippi; and seek attorney's fees, costs, and interest. The plaintiffs also seek an injunction to prevent any Kemper County energy facility costs from being charged to customers through electric rates. On June 23, 2017, the Circuit Court ruled in favor of motions by Southern Company and the Company and dismissed the case. On July 7, 2017, the plaintiffs filed notice of an appeal. The Company believes this legal challenge has no merit; however, an adverse outcome in this proceeding could have a material impact on the Company's results of operations, financial condition, and liquidity. The Company intends to vigorously defend itself in this matter and the ultimate outcome of this matter cannot be determined at this time.

On June 9, 2016, Treetop, Greenleaf CO_2 Solutions, LLC (Greenleaf), Tenrgys, LLC, Tellus Energy, LLC, WCOA, LLC, and Tellus Operating Group filed a complaint against the Company, Southern Company, and SCS in the state court in Gwinnett County, Georgia. The complaint related to the cancelled CO_2 contract with Treetop and alleged fraudulent misrepresentation, fraudulent concealment, civil conspiracy, and breach of contract on the part of the Company, Southern Company, and SCS and sought compensatory damages of $100 million, as well as unspecified punitive damages. Southern Company, the Company, and SCS moved to compel arbitration pursuant to the terms of the CO_2 contract, which the court granted on May 4, 2017. On June 28, 2017, Treetop, Greenleaf, Tenrgys, LLC, Tellus Energy, LLC, WCOA, LLC, and Tellus Operating Group filed a claim for arbitration requesting $500 million in damages. On December 28, 2017, the Company reached a settlement agreement with Treetop, Greenleaf, Tenrgys, LLC, Tellus Energy, LLC, WCOA, LLC, and Tellus Operating Group and the arbitration was dismissed.

See Note 3 to the financial statements under "Kemper County Energy Facility" for additional information.

Income Tax Matters

Federal Tax Reform Legislation

On December 22, 2017, the Tax Reform Legislation was signed into law and became effective on January 1, 2018. The Tax Reform Legislation, among other things, reduces the federal corporate income tax rate to 21%, retains normalization provisions for public utility property and existing renewable energy incentives, and repeals the corporate alternative minimum tax.

Regulated utility businesses can continue deducting all business interest expense and are not eligible for bonus depreciation on capital assets acquired and placed in service after September 27, 2017. Projects with binding contracts before September 28, 2017 and placed in service after September 27, 2017 remain eligible for bonus depreciation under the Protecting Americans from Tax Hikes (PATH) Act.

In addition, under the Tax Reform Legislation, net operating losses (NOL) generated after December 31, 2017 can no longer be carried back to previous tax years but can be carried forward indefinitely, with utilization limited to 80% of taxable income in the subsequent tax year.

For the year ended December 31, 2017, implementation of the Tax Reform Legislation resulted in an estimated net tax expense of $372 million and a $375 million increase in regulatory liabilities as of December 31, 2017, primarily due to the impact of the reduction of the corporate income tax rate on deferred tax assets and liabilities.

The Tax Reform Legislation is subject to further interpretation and guidance from the IRS, as well as each respective state's adoption. In addition, the regulatory treatment of certain impacts of the Tax Reform Legislation is subject to the discretion of the FERC and the Mississippi PSC. On January 31, 2018, SCS, on behalf of the traditional electric operating companies (including the Company), filed with the FERC a reduction to the Company's open access transmission tariff charge for 2018 to reflect the revised federal corporate tax rate. See Note 3 to the financial statements under "Regulatory Matters" for additional information regarding the Company's rate filings to reflect the impacts of the Tax Reform Legislation.

See FINANCIAL CONDITION AND LIQUIDITY – "Credit Rating Risk" herein and Note 5 to the financial statements under "Current and Deferred Income Taxes" for additional information.

The ultimate outcome of these matters cannot be determined at this time.

Bonus Depreciation

Under the Tax Reform Legislation, projects with binding contracts prior to September 28, 2017 and placed in service after September 27, 2017 remain eligible for bonus depreciation under the PATH Act. The PATH Act allowed for 50% bonus depreciation for 2015 through 2017, 40% bonus depreciation for 2018, and 30% bonus depreciation for 2019 and certain long-lived assets placed in service in 2020. Based on provisional estimates, approximately $50 million of positive cash flows is expected to result from bonus depreciation for the 2017 tax year and approximately $10 million for the 2018 tax year. Should Southern Company have a NOL in 2018, all of these cash flows may not be fully realized in 2018. All projected tax benefits previously received for bonus depreciation related to the Kemper IGCC were repaid in connection with third quarter 2017 estimated tax payments. Additionally, Southern Company will record an abandonment loss on its 2018 corporate income tax return, which may not be fully realized should Southern Company have a NOL in 2018. See Notes 3 and 5 to the financial statements under "Kemper County Energy Facility" and "Current and Deferred Income Taxes," respectively, for additional information. The ultimate outcome of these matters cannot be determined at this time.

Section 174 Research and Experimental Deduction

Southern Company, on behalf of the Company, has reflected deductions for R&E expenditures related to the Kemper County energy facility in its federal income tax calculations since 2013 and filed amended federal income tax returns for 2008 through 2013 to also include such deductions. In December 2016, Southern Company and the IRS reached a proposed settlement, which was approved on September 8, 2017 by the U.S. Congress Joint Committee on Taxation (JCT), resolving a methodology for these deductions. As a result of this approval, the Company recognized $176 million of previously unrecognized tax benefits and reversed $36 million of associated accrued interest.

Other Matters

The Company is involved in various other matters being litigated and regulatory matters that could affect future earnings. In addition, the Company is subject to certain claims and legal actions arising in the ordinary course of business. The Company's business activities are subject to extensive governmental regulation related to public health and the environment, such as regulation of air emissions and water discharges. Litigation over environmental issues and claims of various types, including property damage, personal injury, common law nuisance, and citizen enforcement of environmental requirements, such as standards for air, water, land, and protection of other natural resources, has occurred throughout the U.S. This litigation has included claims for damages alleged to have been caused by CO_2 and other emissions, CCR, and alleged exposure to hazardous materials, and/or requests for injunctive relief in connection with such matters.

The ultimate outcome of such pending or potential litigation or regulatory matters cannot be predicted at this time; however, for current proceedings not specifically reported herein or in Note 3 to the financial statements, management does not anticipate that the ultimate liabilities, if any, arising from such current proceedings would have a material effect on the Company's financial statements. See Note 3 to the financial statements for a discussion of various other contingencies, regulatory matters, and other matters being litigated which may affect future earnings potential.

In 2013, the Company submitted a claim under the Deep Horizon Economic and Property Damages Settlement Agreement associated with the oil spill that occurred in the Gulf of Mexico. The ultimate outcome of this matter cannot be determined at this time.

In 2016, the SEC began conducting a formal investigation of Southern Company and the Company concerning the estimated costs and expected in-service date of the Kemper County energy facility. On November 30, 2017, the SEC staff notified Southern Company that it had concluded its investigation with no recommended enforcement action.

ACCOUNTING POLICIES

Application of Critical Accounting Policies and Estimates

The Company prepares its financial statements in accordance with GAAP. Significant accounting policies are described in Note 1 to the financial statements. In the application of these policies, certain estimates are made that may have a material impact on the Company's results of operations and related disclosures. Different assumptions and measurements could produce estimates that are significantly different from those recorded in the financial statements. Senior management has reviewed and discussed the following critical accounting policies and estimates with the Audit Committee of Southern Company's Board of Directors.

Utility Regulation

The Company is subject to retail regulation by the Mississippi PSC and wholesale regulation by the FERC. These regulatory agencies set the rates the Company is permitted to charge customers based on allowable costs. As a result, the Company applies accounting standards which require the financial statements to reflect the effects of rate regulation. Through the ratemaking process, the regulators may require the inclusion of costs or revenues in periods different than when they would be recognized by a non-regulated company. This treatment may result in the deferral of expenses and the recording of related regulatory assets based on anticipated future recovery through rates or the deferral of gains or creation of liabilities and the recording of related regulatory liabilities. The application of the accounting standards has a further effect on the Company's financial statements as a result of the estimates of allowable costs used in the ratemaking process. These estimates may differ from those actually incurred by the Company; therefore, the accounting estimates inherent in specific costs such as depreciation and pension and other postretirement benefits have less of a direct impact on the Company's results of operations and financial condition than they would on a non-regulated company.

As reflected in Note 1 to the financial statements, significant regulatory assets and liabilities have been recorded. Management reviews the ultimate recoverability of these regulatory assets and any requirement to refund these regulatory liabilities based on applicable regulatory guidelines and GAAP. However, adverse legislative, judicial, or regulatory actions could materially impact the amounts of such regulatory assets and liabilities and could adversely impact the Company's financial statements.

Kemper County Energy Facility Rate Recovery

For periods prior to the second quarter 2017, significant accounting estimates included Kemper County energy facility estimated construction costs, project completion date, and rate recovery. The Company recorded total pre-tax charges to income related to the Kemper County energy facility of $428 million ($264 million after tax) in 2016, $365 million ($226 million after tax) in 2015, $868 million ($536 million after tax) in 2014, and $1.2 billion ($729 million after tax) in prior years.

As a result of the Mississippi PSC's June 21, 2017 stated intent to issue an order (which occurred on July 6, 2017) directing the Company to pursue a settlement under which the Kemper County energy facility would be operated as a natural gas plant rather than an IGCC plant, as well as the Company's June 28, 2017 suspension of the operation and start-up of the gasifier portion of the Kemper County energy facility, the estimated construction costs and project completion date are no longer considered significant accounting estimates.

Given the Mississippi PSC's stated intent regarding no further rate increase for the Kemper County energy facility and the subsequent suspension, cost recovery of the gasifier portions became no longer probable; therefore, the Company recorded an additional charge to income in June 2017 of $2.8 billion ($2.0 billion after tax), which included estimated costs associated with the gasifier portions of the plant and lignite mine. During the third and fourth quarters of 2017, the Company recorded charges to income of $242 million ($206 million after tax), including $164 million for ongoing project costs, estimated mine and gasifier-related costs, and certain termination costs during the suspension period prior to conclusion of the Kemper Settlement Docket, as well as a charge of $78 million associated with the Kemper Settlement Agreement.

In the aggregate, since the Kemper County energy facility project started, the Company has incurred charges of $6.20 billion ($4.14 billion after tax) through December 31, 2017. See Note 11 to the financial statements for additional information on the individual charges by quarter.

As a result of the Mississippi PSC order on February 6, 2018, rate recovery for the Kemper County energy facility is resolved, subject to any future legal challenges, and no longer represents a critical accounting estimate.

See Note 3 to the financial statements under "Kemper County Energy Facility" for additional information.

Federal Tax Reform Legislation

Following the enactment of Tax Reform Legislation, the SEC staff issued Staff Accounting Bulletin 118 – "Income Tax Accounting Implications of the Tax Cuts and Jobs Act" (SAB 118), which provides for a measurement period of up to one year from the enactment date to complete accounting under GAAP for the tax effects of the legislation. Due to the complex and comprehensive nature of the enacted tax law changes, and their application under GAAP, the Company considers all amounts recorded in the financial statements as a result of Tax Reform Legislation to be "provisional" as discussed in SAB 118 and subject to revision. The Company is awaiting additional guidance from industry and income tax authorities in order to finalize its accounting. The ultimate impact of Tax Reform Legislation on deferred income tax assets and liabilities and the related regulatory assets and liabilities cannot be determined at this time. See FUTURE EARNINGS POTENTIAL – "Income Tax Matters – Federal Tax Reform Legislation" herein and Notes 3 and 5 to the financial statements under "Retail Regulatory Matters – Rate Plans" and "Current and Deferred Income Taxes," respectively, for additional information.

Asset Retirement Obligations

AROs are computed as the fair value of the estimated ultimate costs for an asset's future retirement and are recorded in the period in which the liability is incurred. The costs are capitalized as part of the related long-lived asset and depreciated over the asset's useful life. In the absence of quoted market prices, AROs are estimated using present value techniques in which estimates of future cash outlays associated with the asset retirements are discounted using a credit-adjusted risk-free rate. Estimates of the timing and amounts of future cash outlays are based on projections of when and how the assets will be retired and the cost of future removal activities.

The liability for AROs primarily relates to facilities that are subject to the CCR Rule, principally ash ponds. In addition, the Company has retirement obligations related to various landfill sites, underground storage tanks, deep injection wells, water wells, substation removal, mine reclamation, and asbestos removal. The Company also has identified retirement obligations related to certain transmission and distribution facilities and certain wireless communication towers. However, liabilities for the removal of these assets have not been recorded because the settlement timing for the retirement obligations related to these assets is indeterminable and, therefore, the fair value of the retirement obligations cannot be reasonably estimated. A liability for these AROs will be recognized when sufficient information becomes available to support a reasonable estimation of the ARO.

The cost estimates for AROs related to the disposal of CCR are based on information using various assumptions related to closure and post-closure costs, timing of future cash outlays, inflation and discount rates, and the potential methods for complying with the CCR Rule requirements for closure. As further analysis is performed and closure details are developed, the Company will continue to periodically update these cost estimates as necessary. See FUTURE EARNINGS POTENTIAL – "Environmental Matters – Environmental Laws and Regulations – Coal Combustion Residuals" herein and Note 1 to the financial statements under "Asset Retirement Obligations and Other Costs of Removal" for additional information.

Given the significant judgment involved in estimating AROs, the Company considers the liabilities for AROs to be critical accounting estimates.

Pension and Other Postretirement Benefits

The Company's calculation of pension and other postretirement benefits expense is dependent on a number of assumptions. These assumptions include discount rates, healthcare cost trend rates, expected long-term return on plan assets, mortality rates, expected salary and wage increases, and other factors. Components of pension and other postretirement benefits expense include interest and service cost on the pension and other postretirement benefit plans, expected return on plan assets, and amortization of certain unrecognized costs and obligations. Actual results that differ from the assumptions utilized are accumulated and amortized over future periods and, therefore, generally affect recognized expense and the recorded obligation in future periods. While the Company believes that the assumptions used are appropriate, differences in actual experience or significant changes in assumptions would affect its pension and other postretirement benefits costs and obligations.

Key elements in determining the Company's pension and other postretirement benefit expense are the expected long-term return on plan assets and the discount rate used to measure the benefit plan obligations and the periodic benefit plan expense for future periods. The expected long-term return on pension and other postretirement benefit plan assets is based on the Company's investment strategy, historical experience, and expectations for long-term rates of return that consider external actuarial advice. The Company determines the long-term return on plan assets by applying the long-term rate of expected returns on various asset classes to the Company's target asset allocation. For purposes of determining its liability related to the pension and other postretirement benefit plans, the Company discounts the future related cash flows using a single-point discount rate developed from the weighted average of market-observed yields for high quality fixed income securities with maturities that correspond to expected benefit payments. For 2015 and prior years, the Company computed the interest cost component of its net periodic pension and other postretirement benefit plan expense using the same single-point discount rate. Beginning in 2016, the Company adopted a full yield curve approach for calculating the interest cost component whereby the discount rate for each year is applied to the liability for that specific year. As a result, the interest cost component of net periodic pension and other postretirement benefit plan expense decreased by approximately $4 million in 2016.

A 25 basis point change in any significant assumption (discount rate, salaries, or long-term return on plan assets) would result in a $2 million or less change in total annual benefit expense and a $25 million or less change in projected obligations.

See Note 2 to the financial statements for additional information regarding pension and other postretirement benefits.

Allowance for Funds Used During Construction

In accordance with regulatory treatment, the Company records AFUDC, which represents the estimated debt and equity costs of capital funds that are necessary to finance the construction of new regulated facilities. While cash is not realized currently from such allowance, AFUDC increases the revenue requirement over the service life of the plant through a higher rate base and higher depreciation. The equity component of AFUDC is not included in the calculation of taxable income. The average annual AFUDC rate was 6.7%, 6.5%, and 5.99% for the years ended December 31, 2017, 2016, and 2015, respectively. The AFUDC rate is applied to CWIP consistent with jurisdictional regulatory treatment. AFUDC equity was $72 million, $124 million, and $110 million in 2017, 2016, and 2015, respectively. The decrease in 2017 resulted from the Kemper County energy facility project suspension in June 2017.

Unbilled Revenues

Revenues related to the retail sale of electricity are recorded when electricity is delivered to customers. However, the determination of KWH sales to individual customers is based on the reading of their meters, which is performed on a systematic basis throughout the month. At the end of each month, amounts of electricity delivered to customers, but not yet metered and billed, are estimated. Components of the unbilled revenue estimates include total KWH territorial supply, total KWH billed, estimated total electricity lost in delivery, and customer usage. These components can fluctuate as a result of a number of factors including weather, generation patterns, power delivery volume, and other operational constraints. These factors can be unpredictable and can vary from historical trends. As a result, the overall estimate of unbilled revenues could be significantly affected, which could have a material impact on the Company's results of operations.

Contingent Obligations

The Company is subject to a number of federal and state laws and regulations as well as other factors and conditions that subject it to environmental, litigation, income tax, and other risks. See FUTURE EARNINGS POTENTIAL herein and Note 3 to the financial statements for more information regarding certain of these contingencies. The Company periodically evaluates its exposure to such risks and records reserves for those matters where a non-tax-related loss is considered probable and reasonably estimable and records a tax asset or liability if it is more likely than not that a tax position will be sustained. The adequacy of reserves can be significantly affected by external events or conditions that can be unpredictable; thus, the ultimate outcome of such matters could materially affect the Company's results of operations, cash flows, or financial condition.

Recently Issued Accounting Standards

Revenue

In 2014, the FASB issued ASC 606, *Revenue from Contracts with Customers* (ASC 606), replacing the existing accounting standard and industry specific guidance for revenue recognition with a five-step model for recognizing and measuring revenue from contracts with customers. The underlying principle of the new standard is to recognize revenue to depict the transfer of goods or services to customers at the amount expected to be collected. The new standard also requires enhanced disclosures regarding the nature, amount, timing, and uncertainty of revenue and the related cash flows arising from contracts with customers.

Most of the Company's revenue, including energy provided to customers, is from tariff offerings that provide electricity without a defined contractual term, as well as longer-term contractual commitments, including PPAs.

The Company has completed the evaluation of all revenue streams and determined that the adoption of ASC 606 will not change the current timing of revenue recognition for such transactions. Some revenue arrangements, such as energy-related derivatives and alternative revenue programs, are excluded from the scope of ASC 606 and, therefore, will be accounted for and disclosed or presented separately from revenues under ASC 606 on the Company's financial statements, if material. The Company has concluded contributions in aid of construction are not in scope for ASC 606 and will continue to be accounted for as an offset to property, plant, and equipment.

The new standard is effective for reporting periods beginning after December 15, 2017. The Company applied the modified retrospective method of adoption effective January 1, 2018. The Company also utilized practical expedients which allowed it to apply the standard to open contracts at the date of adoption and to reflect the aggregate effect of all modifications when identifying performance obligations and allocating the transaction price for contracts modified before the effective date. Under the modified retrospective method of adoption, prior year reported results are not restated; however, a cumulative-effect adjustment to retained earnings at January 1, 2018 is recorded. In addition, quarterly disclosures will include comparative information on 2018 financial statement line items under current guidance. The adoption of ASC 606 did not result in a cumulative-effect adjustment.

Leases

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (ASU 2016-02). ASU 2016-02 requires lessees to recognize on the balance sheet a lease liability and a right-of-use asset for all leases. ASU 2016-02 also changes the recognition, measurement, and presentation of expense associated with leases and provides clarification regarding the identification of certain components of contracts that would represent a lease. The accounting required by lessors is relatively unchanged. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 and the Company will adopt the new standard effective January 1, 2019.

The Company is currently implementing an information technology system along with the related changes to internal controls and accounting policies that will support the accounting for leases under ASU 2016-02. In addition, the Company has substantially completed a detailed inventory and analysis of its leases. In terms of rental charges and duration of contracts, the most significant leases relate to equipment and cellular towers where the Company is the lessee and to equipment where the Company is the lessor. The Company is currently analyzing pole attachment agreements and a lease determination has not been made at this time. While the Company has not yet determined the ultimate impact, adoption of ASU 2016-02 is expected to have a significant impact on the Company's balance sheet.

Other

On March 10, 2017, the FASB issued ASU No. 2017-07, *Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost* (ASU 2017-07). ASU 2017-07 requires that an employer report the service cost component in the same line item or items as other compensation costs and requires the other components of net periodic pension and postretirement benefit costs to be separately presented in the income statement outside of income from operations. Additionally, only the service cost component is eligible for capitalization, when applicable. However, all cost components remain eligible for capitalization under FERC regulations. ASU 2017-07 will be applied retrospectively for the presentation of the service cost component and the other components of net periodic pension and postretirement benefit costs in the income statement. The capitalization of only the service cost component of net periodic pension and postretirement benefit costs in assets will be applied on a prospective basis. ASU 2017-07 is effective for periods beginning after December 15, 2017. The presentation changes required for net periodic pension and postretirement benefit costs will result in a decrease in the Company's operating income and an increase in other income for 2016 and 2017 and are expected to result in a decrease in operating income and an increase in other income for 2018. The Company adopted ASU 2017-07 effective January 1, 2018 with no material impact on its financial statements.

On August 28, 2017, the FASB issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities* (ASU 2017-12), amending the hedge accounting recognition and presentation requirements. ASU 2017-12 makes more financial and non-financial hedging strategies eligible for hedge accounting, amends the related presentation and disclosure requirements, and simplifies hedge effectiveness assessment requirements. ASU 2017-12 is effective for fiscal years beginning after December 15, 2018, with early adoption permitted. The Company adopted ASU 2017-12 effective January 1, 2018 with no material impact on its financial statements.

FINANCIAL CONDITION AND LIQUIDITY

Overview and Sources of Capital

Earnings for all periods presented were negatively affected by charges associated with the Kemper IGCC. See FUTURE EARNINGS POTENTIAL – "Kemper County Energy Facility" herein and Note 3 to the financial statements for additional information.

The Company's cash requirements primarily consist of funding ongoing operations, capital expenditures, and debt maturities. Capital expenditures and other investing activities include investments to maintain existing generation facilities, to comply with environmental regulations including adding environmental modifications to certain existing generating units, to expand and improve transmission and distribution facilities, and for restoration following major storms.

The Company's financial statement presentation contemplates continuation of the Company as a going concern as a result of Southern Company's anticipated ongoing financial support of the Company. Specifically, the Company has been informed by Southern Company that in the event sufficient funds are not available from external sources, Southern Company intends to provide the Company with loans and/or equity contributions sufficient to fund the remaining indebtedness scheduled to mature and other cash needs over the next 12 months. For additional information, see Note 6 to the financial statements under "Going Concern."

On February 28, 2017, the maturity dates for $551 million in promissory notes to Southern Company were extended to July 31, 2018. In the second quarter 2017, the Company borrowed an additional $40 million under a promissory note issued to Southern Company. In June 2017, Southern Company made equity contributions totaling $1.0 billion to the Company. The Company used a portion of the proceeds to (i) prepay $300 million of the outstanding principal amount under its $1.2 billion unsecured term loan; (ii) repay all of the $591 million outstanding principal amount of promissory notes to Southern Company; and (iii) repay $10 million of the outstanding principal amount of bank loans.

In September 2017, the Company issued a floating rate promissory note to Southern Company in an aggregate principal amount of up to $150 million bearing interest based on one-month LIBOR. The Company borrowed $109 million under this promissory note primarily to satisfy its federal income tax obligations for the quarter ended September 30, 2017 and subsequently repaid the promissory note upon receipt of its income tax refund from the U.S. government related to the settlement concerning deductible R&E expenditures. See Note 5 to the financial statements under "Section 174 Research and Experimental Deduction" for additional information.

As of December 31, 2017, the Company's current liabilities exceeded current assets by approximately $911 million primarily due to a $900 million unsecured term loan that matures on March 31, 2018. The Company expects to refinance the unsecured term loan with external security issuances and/or borrowings from financial institutions or Southern Company. To fund the Company's capital needs over the next 12 months, the Company intends to utilize operating cash flows, external security issuances, lines of credit, bank term loans, equity contributions from Southern Company, and, to the extent necessary, loans from Southern Company.

The Company's capital expenditures and debt maturities are expected to materially exceed operating cash flows through 2022. The Company plans to obtain the funds required for construction and other purposes from operating cash flows, lines of credit, bank term loans, external security issuances, commercial paper, to the extent the Company is eligible to participate, and loans and/or equity contributions from Southern Company.

The Company's investments in the qualified pension plan increased in value as of December 31, 2017 as compared to December 31, 2016. No contributions to the qualified pension plan were made for the year ended December 31, 2017 and no mandatory contributions to the qualified pension plan are anticipated during 2018.

Net cash provided from operating activities totaled $503 million for 2017, an increase of $274 million as compared to 2016. The increase in cash provided from operating activities in 2017 was primarily due to tax refunds associated with the approval by the JCT of the Section 174 R&E settlement, largely offset by a decrease in income taxes related to the Kemper County energy facility and Tax Reform Legislation. Net cash provided from operating activities totaled $229 million for 2016, an increase of $56 million as compared to 2015. The increase in cash provided from operating activities in 2016 was primarily due to repayment in 2015 of ITCs relating to the Kemper County energy facility, as well as the 2015 mirror CWIP refund, partially offset by lower income tax benefits related to the Kemper County energy facility in 2016 and lower fuel rates in 2016.

Net cash used for investing activities in 2017, 2016, and 2015 totaled $504 million, $697 million, and $906 million, respectively. The cash used for investing activities in all years presented was primarily due to gross property additions related to the Kemper County energy facility. The cash used for investing activities in 2016 was partially offset by the receipt of Additional DOE Grants. The cash used for investing activities in 2015 also included gross property additions related to the Plant Daniel scrubber project.

Net cash provided from financing activities totaled $25 million in 2017 primarily due to capital contributions from Southern Company, largely offset by redemptions of long-term debt and short-term borrowings. Net cash provided from financing activities totaled $594 million in 2016 primarily due to long-term debt financings and capital contributions from Southern Company, partially offset by a decrease in short-term borrowings and redemptions of long-term debt. Net cash provided from financing activities totaled $698 million in 2015 primarily due to short-term borrowings, capital contributions from Southern Company, and long-term debt financings, partially offset by redemptions of long-term debt.

Significant balance sheet changes as of December 31, 2017 compared to 2016 include decreases of $2.5 billion in CWIP, a net change of $1.0 billion in accumulated deferred income taxes, an increase in paid-in capital of $1.0 billion due to capital contributions from Southern Company, a portion of which was used to repay $300 million of securities due within one year, $591 million of long-term debt, and $10 million of short-term debt. Long-term debt decreased primarily due to the reclassification of $1.2 billion in unsecured term loans to securities due within one year – other. Securities due within one year – parent decreased $551 million due to the repayment of promissory notes to Southern Company. Other significant balance sheet changes include $326 million in deferred charges related to income taxes. All of these changes primarily resulted from the Kemper IGCC suspension and related estimated loss. Income taxes receivable and unrecognized tax benefits also decreased due to tax refunds associated with the approval by the JCT of the Section 174 R&E settlement. The Company also had an increase of $365 million in deferred credits related to income taxes primarily resulting from the impacts of Tax Reform Legislation. See FUTURE EARNINGS POTENTIAL – "Kemper County Energy Facility" and "Income Tax Matters – Federal Tax Reform Legislation" herein and Notes 3 and 5 to the financial statements under "Kemper County Energy Facility" and "Section 174 Research and Experimental Deduction," respectively, for additional information.

The Company's ratio of common equity to total capitalization plus short-term debt was 39% and 49% at December 31, 2017 and 2016, respectively. The decrease was due to Kemper IGCC losses. See Note 6 to the financial statements for additional information.

The issuance of securities by the Company is subject to regulatory approval by the FERC. Additionally, with respect to the public offering of securities, the Company files registration statements with the SEC under the Securities Act of 1933, as amended. The amounts of securities authorized by the FERC are continuously monitored and appropriate filings are made to ensure flexibility in raising capital. Any future financing through secured debt would also require approval by the Mississippi PSC.

The Southern Company system does not maintain a centralized cash or money pool. Therefore, funds of the Company are not commingled with funds of any other company in the Southern Company system.

At December 31, 2017, the Company had approximately $248 million of cash and cash equivalents. Committed credit arrangements with banks at December 31, 2017 were $100 million, all of which is unused. In November 2017, the Company amended its one-year credit arrangements in an aggregate amount of $100 million to extend the maturity dates from 2017 to 2018.

A portion of the $100 million unused credit arrangements with banks is allocated to provide liquidity support to the Company's revenue bonds. The amount of variable rate revenue bonds outstanding requiring liquidity support as of December 31, 2017 was approximately $40 million. In addition, the Company had approximately $50 million of fixed rate revenue bonds that were remarketed from a long-term interest rate mode to an index rate mode subsequent to December 31, 2017.

Most of these bank credit arrangements, as well as the Company's term loan agreement, contain covenants that limit debt levels and typically contain cross acceleration to other indebtedness (including guarantee obligations) of the Company. Such cross-acceleration provisions to other indebtedness would trigger an event of default if the Company defaulted on indebtedness, the payment of which was then accelerated. At December 31, 2017, the Company was in compliance with all such covenants. None of the bank credit arrangements contain material adverse change clauses at the time of borrowing.

Subject to applicable market conditions, the Company expects to seek to renew or replace its credit arrangements as needed, prior to expiration. In connection therewith, the Company may extend the maturity dates and/or increase or decrease the lending commitments thereunder.

See Note 6 to the financial statements under "Bank Credit Arrangements" for additional information.

Short-term borrowings are included in notes payable in the balance sheets. Details of short-term borrowing were as follows:

	Short-term Debt at the End of the Period		Short-term Debt During the Period (*)		
	Amount Outstanding	Weighted Average Interest Rate	Average Outstanding	Weighted Average Interest Rate	Maximum Amount Outstanding
	(in millions)		(in millions)		(in millions)
December 31, 2017	**$ 4**	**3.8%**	**$ 18**	**3.0%**	**$ 36**
December 31, 2016	$ 23	2.6%	$ 112	2.0%	$ 500
December 31, 2015	$ 500	1.4%	$ 372	1.3%	$ 515

(*) Average and maximum amounts are based upon daily balances during the 12-month periods ended December 31.

Financing Activities

In addition to any financings that may be necessary to meet capital requirements and contractual obligations, the Company plans, when economically feasible, to retire higher-cost securities and replace these obligations with lower-cost capital if market conditions permit.

Bank Term Loans and Senior Notes

In March 2017, the Company issued a $9 million short-term bank note bearing interest at 5% per annum, which was repaid in April 2017.

In June 2017, the Company used a portion of the proceeds from Southern Company equity contributions to prepay $300 million of the outstanding principal amount under its $1.2 billion unsecured term loan, which matures on March 30, 2018, and to repay $10 million of the outstanding principal amount of bank loans. See "Parent Company Loans and Equity Contributions" herein for more information.

This unsecured term loan has covenants that limit debt levels to 65% of total capitalization, as defined in the agreement. For purposes of this definition, debt excludes the long-term debt payable to affiliated trusts and other hybrid securities. In addition, this unsecured term loan contains cross-acceleration provisions to other debt (including guarantee obligations) that would be triggered if the Company defaulted on debt above a specified threshold, the payment of which was then accelerated. The Company is currently in compliance with all such covenants.

In August 2017, the Company repaid a $12.5 million short-term bank note.

In November 2017, the Company repaid at maturity $35 million aggregate principal amount of Series 2007A 5.60% Senior Notes.

Parent Company Loans and Equity Contributions

In February 2017, the Company amended $551 million in promissory notes to Southern Company extending the maturity dates of the notes from December 1, 2017 to July 31, 2018. In the second quarter 2017, the Company borrowed an additional $40 million under a promissory note issued to Southern Company.

In June 2017, Southern Company made equity contributions totaling $1.0 billion to the Company. The Company used a portion of the proceeds to (i) prepay $300 million of the outstanding principal amount under its $1.2 billion unsecured term loan, which matures on March 30, 2018; (ii) repay all of the $591 million outstanding principal amount of promissory notes to Southern Company; and (iii) repay a $10 million short-term bank loan.

In September 2017, the Company issued a floating rate promissory note to Southern Company in an aggregate principal amount of up to $150 million bearing interest based on one-month LIBOR. The Company borrowed $109 million under this promissory note primarily to satisfy its federal income tax obligations for the quarter ending September 30, 2017 and subsequently repaid the promissory note upon receipt of its income tax refund from the U.S. federal government related to the settlement concerning deductible R&E expenditures. See Note 5 to the financial statements under "Section 174 Research and Experimental Deduction" for additional information.

Credit Rating Risk

At December 31, 2017, the Company does not have any credit arrangements that would require material changes in payment schedules or terminations as a result of a credit rating downgrade.

On October 4, 2017, the Company executed agreements with its largest retail customer, Chevron, to continue providing retail service to the Chevron refinery in Pascagoula, Mississippi through 2038. The agreements grant Chevron a security interest in the co-generation assets, with a net book value of approximately $93 million, located at the refinery that is exercisable upon the occurrence of (i) certain bankruptcy events or (ii) other events of default coupled with specific reductions in steam output at the facility and a downgrade of the Company's credit rating to below investment grade by two of the three rating agencies.

There are certain contracts that have required or could require collateral, but not accelerated payment, in the event of a credit rating change to BBB and/or Baa2 or below. These contracts are for physical electricity purchases and sales, fuel transportation and storage, energy price risk management, and transmission. At December 31, 2017, the maximum amount of potential collateral requirements under these contracts at a rating of BBB and/or Baa2 or BBB- and/or Baa3 was not material. The maximum potential collateral requirements at a rating below BBB- and/or Baa3 equaled approximately $241 million.

Included in these amounts are certain agreements that could require collateral in the event that Alabama Power or Georgia Power has a credit rating change to below investment grade. Generally, collateral may be provided by a Southern Company guaranty, letter of credit, or cash. Additionally, a credit rating downgrade could impact the ability of the Company to access capital markets, or at a minimum the cost at which it does so.

On March 1, 2017, Moody's downgraded the senior unsecured debt rating of the Company to Ba1 from Baa3.

On March 24, 2017, S&P revised its consolidated credit rating outlook for Southern Company and its subsidiaries (including the Company) from stable to negative.

On March 30, 2017, Fitch placed the ratings of the Company on rating watch negative.

On June 22, 2017, Moody's placed the ratings of the Company on review for downgrade. On September 21, 2017, Moody's revised its rating outlook for the Company from under review to stable.

While it is unclear how the credit rating agencies, the FERC, and the Mississippi PSC may respond to the Tax Reform Legislation, certain financial metrics, such as the funds from operations to debt percentage, used by the credit rating agencies to assess Southern Company and its subsidiaries, including the Company, may be negatively impacted. Absent actions by Southern Company and its subsidiaries, including the Company, to mitigate the resulting impacts, which, among other alternatives, could include adjusting capital structure and/or monetizing regulatory assets, the Company's credit ratings could be negatively affected. See Note 3 to the financial statements under "Retail Regulatory Matters" for additional information.

Market Price Risk

Due to cost-based rate regulation and other various cost recovery mechanisms, the Company continues to have limited exposure to market volatility in interest rates, commodity fuel prices, and prices of electricity. To manage the volatility attributable to these exposures, the Company nets the exposures, where possible, to take advantage of natural offsets and enters into various derivative transactions for the remaining exposures pursuant to the Company's policies in areas such as counterparty exposure and risk management practices. The Company's policy is that derivatives are to be used primarily for hedging purposes and mandates strict adherence to all applicable risk management policies. Derivative positions are monitored using techniques that include, but are not limited to, market valuation, value at risk, stress testing, and sensitivity analysis.

To mitigate future exposure to a change in interest rates, the Company may enter into derivatives that have been designated as hedges. The weighted average interest rate on $40 million of long-term variable interest rate exposure at December 31, 2017 was 2.49%. If the Company sustained a 100 basis point change in interest rates for all long-term variable interest rate exposure, the change would have an immaterial effect on annualized interest expense at December 31, 2017. See Note 1 to the financial statements under "Financial Instruments" and Note 10 to the financial statements for additional information.

To mitigate residual risks relative to movements in electricity prices, the Company enters into physical fixed-price contracts for the purchase and sale of electricity through the wholesale electricity market and, to a lesser extent, financial hedge contracts for natural gas purchases. The Company continues to manage retail fuel-hedging programs implemented per the guidelines of the Mississippi PSC and wholesale fuel-hedging programs under agreements with wholesale customers. The Company had no material change in market risk exposure for the year ended December 31, 2017 when compared to the year ended December 31, 2016.

The changes in fair value of energy-related derivative contracts are substantially attributable to both the volume and the price of natural gas. For the years ended December 31, the changes in fair value of energy-related derivative contracts, the majority of which are composed of regulatory hedges, were as follows:

	2017 Changes	2016 Changes
	Fair Value	
	(in millions)	
Contracts outstanding at the beginning of the period, assets (liabilities), net	**$ (7)**	$ (47)
Contracts realized or settled	**8**	29
Current period changes(*)	**(8)**	11
Contracts outstanding at the end of the period, assets (liabilities), net	**$ (7)**	$ (7)

(*) Current period changes also include the changes in fair value of new contracts entered into during the period, if any.

The net hedge volumes of energy-related derivative contracts, all of which are natural gas swaps, for the years ended December 31 were as follows:

	2017	2016
	mmBtu Volume	
	(in millions)	
Total hedge volume	**53**	36

For natural gas hedges, the weighted average swap contract cost above market prices was approximately $0.14 per mmBtu as of December 31, 2017 and $0.19 per mmBtu as of December 31, 2016. The options outstanding were immaterial for the reporting periods presented. The costs associated with natural gas hedges are recovered through the Company's ECMs.

At December 31, 2017 and 2016, substantially all of the Company's energy-related derivative contracts were designated as regulatory hedges and were related to the Company's fuel-hedging program. Therefore, gains and losses are initially recorded as regulatory liabilities and assets, respectively, and then are included in fuel expense as they are recovered through the ECM clause.

The Company uses over-the-counter contracts that are not exchange traded but are fair valued using prices which are market observable, and thus fall into Level 2 of the fair value hierarchy. See Note 9 to the financial statements for further discussion of fair value measurements. The maturities of the energy-related derivative contracts, which are all Level 2 of the fair value hierarchy, at December 31, 2017 were as follows:

	Fair Value Measurements December 31, 2017		
	Total	Maturity	
	Fair Value	Year 1	Years 2&3
		(in millions)	
Level 1	$ —	$ —	$ —
Level 2	(7)	(5)	(2)
Level 3	—	—	—
Fair value of contracts outstanding at end of period	$ (7)	$ (5)	$ (2)

The Company is exposed to market price risk in the event of nonperformance by counterparties to the energy-related derivative contracts. The Company only enters into agreements and material transactions with counterparties that have investment grade credit ratings by Moody's and S&P or with counterparties who have posted collateral to cover potential credit exposure.

Therefore, the Company does not anticipate market risk exposure from nonperformance by the counterparties. For additional information, see Note 1 to the financial statements under "Financial Instruments" and Note 10 to the financial statements.

Capital Requirements and Contractual Obligations

Approximately $900 million will be required through December 31, 2018 to fund maturities of long-term debt. In addition, the Company has $40 million of tax-exempt variable rate demand obligations that are supported by short-term credit facilities and $50 million of fixed rate revenue bonds that were remarketed from a long-term interest rate mode to an index rate mode subsequent to December 31, 2017. See "Overview and Sources of Capital" herein for additional information.

The construction program of the Company is currently estimated to be $213 million for 2018, $199 million for 2019, $193 million for 2020, $167 million for 2021, and $118 million for 2022. These estimated program amounts also include capital expenditures covered under long-term service agreements. Estimated capital expenditures to comply with environmental laws and regulations included in these amounts are $14 million, $16 million, $17 million, $13 million, and $3 million for 2018, 2019, 2020, 2021, and 2022, respectively. These estimated expenditures do not include any potential compliance costs associated with the regulation of CO_2 emissions from fossil fuel-fired electric generating units. See FUTURE EARNINGS POTENTIAL – "Environmental Matters – Environmental Laws and Regulations" and "– Global Climate Issues" herein for additional information.

The Company also anticipates costs associated with closure and monitoring of ash ponds in accordance with the CCR Rule, which are reflected in the Company's ARO liabilities. These costs, which could change as the Company continues to refine its assumptions underlying the cost estimates and evaluate the method and timing of compliance activities, are estimated to be $23 million, $7 million, $7 million, $9 million, and $12 million for the years 2018, 2019, 2020, 2021, and 2022, respectively. See Note 1 to the financial statements under "Asset Retirement Obligations and Other Costs of Removal" for additional information.

The construction program is subject to periodic review and revision, and actual construction costs may vary from these estimates because of numerous factors. These factors include: changes in business conditions; changes in load projections; storm impacts; changes in environmental laws and regulations; the outcome of any legal challenges to the environmental rules; changes in generating plants, including unit retirements and replacements and adding or changing fuel sources at existing electric generating units, to meet regulatory requirements; changes in FERC rules and regulations; Mississippi PSC approvals; changes in the expected environmental compliance program; changes in legislation; the cost and efficiency of construction labor, equipment, and materials; project scope and design changes; and the cost of capital. In addition, there can be no assurance that costs related to capital expenditures will be fully recovered.

In addition, as discussed in Note 2 to the financial statements, the Company provides postretirement benefits to substantially all employees and funds trusts to the extent required by the FERC.

Other funding requirements related to obligations associated with scheduled maturities of long-term debt, as well as the related interest, derivative obligations, preferred stock dividends, unrecognized tax benefits, pension and other post-retirement benefit plans, leases, and other purchase commitments are detailed in the contractual obligations table that follows. See Notes 1, 2, 5, 6, 7, and 10 to the financial statements for additional information.

Contractual Obligations

Contractual obligations at December 31, 2017 were as follows:

	2018	2019-2020	2021-2022	After 2022	Total
			(in millions)		
Long-term debt[(a)] —					
Principal	$ 990	$ 125	$ 270	$ 673	$ 2,058
Interest	86	106	79	552	823
Preferred stock dividends[(b)]	2	3	3	—	8
Financial derivative obligations[(c)]	6	3	—	—	9
Operating leases[(d)]	3	5	4	7	19
Purchase commitments —					
Capital[(e)]	213	379	269	—	861
Fuel[(f)]	280	329	191	175	975
Long-term service agreements[(g)]	33	75	49	245	402
Purchased power[(h)]	11	29	36	454	530
Pension and other postretirement benefits plans[(i)]	7	15	—	—	22
Total	$ 1,631	$ 1,069	$ 901	$ 2,106	$ 5,707

(a) All amounts are reflected based on final maturity dates except for amounts related to certain revenue bonds. The Company plans to continue, when economically feasible, to retire higher-cost securities and replace these obligations with lower-cost capital if market conditions permit. Variable rate interest obligations are estimated based on rates as of December 31, 2017, as reflected in the statements of capitalization. Fixed rates include, where applicable, the effects of interest rate derivatives employed to manage interest rate risk. Long-term debt excludes capital lease amounts (shown separately). For additional information, see Note 6 to the financial statements.

(b) Preferred stock does not mature; therefore, amounts are provided for the next five years only.

(c) Derivative obligations are for energy-related derivatives. For additional information, see Notes 1 and 10 to the financial statements.

(d) See Note 7 to the financial statements for additional information.

(e) The Company provides estimated capital expenditures for a five-year period, including capital expenditures associated with environmental regulations. At December 31, 2017, significant purchase commitments were outstanding in connection with the construction program. These amounts exclude capital expenditures covered under long-term service agreements, which are reflected separately. See FUTURE EARNINGS POTENTIAL – "Environmental Matters" for additional information.

(f) Fuel commitments include coal and natural gas purchases, as well as the related transportation and storage. In most cases, these contracts contain provisions for price escalation, minimum purchase levels, and other financial commitments. Natural gas purchase commitments are based on various indices at the time of delivery. Amounts reflected for natural gas purchase commitments have been estimated based on the New York Mercantile Exchange future prices at December 31, 2017.

(g) Long-term service agreements include price escalation based on inflation indices.

(h) Purchased power represents estimated minimum long-term commitments for the purchase of solar energy. Energy costs associated with solar PPAs are recovered through the fuel clause. See Notes 3 and 7 to the financial statements for additional information.

(i) The Company forecasts contributions to the pension and other postretirement benefit plans over a three-year period. The Company anticipates no mandatory contributions to the qualified pension plan during the next three years. Amounts presented represent estimated benefit payments for the nonqualified pension plans, estimated non-trust benefit payments for the other postretirement benefit plans, and estimated contributions to the other postretirement benefit plan trusts, all of which will be made from the Company's corporate assets. See Note 2 to the financial statements for additional information related to the pension and other postretirement benefit plans, including estimated benefit payments. Certain benefit payments will be made through the related benefit plans. Other benefit payments will be made from the Company's corporate assets.

Cautionary Statement Regarding Forward-Looking Statements

The Company's 2017 Annual Report contains forward-looking statements. Forward-looking statements include, among other things, statements concerning retail rates, customer and sales growth, economic conditions, fuel and environmental cost recovery and other rate actions, current and proposed environmental regulations and related compliance plans and estimated expenditures, pending or potential litigation matters, access to sources of capital, projections for the qualified pension plan and postretirement benefit plans contributions, financing activities, filings with state and federal regulatory authorities, impacts of the Tax Reform Legislation, federal income tax benefits, estimated sales and purchases under power sale and purchase agreements, storm damage cost recovery and repairs, and estimated construction and other plans and expenditures. In some cases, forward-looking statements can be identified by terminology such as "may," "will," "could," "should," "expects," "plans," "anticipates," "believes," "estimates," "projects," "predicts," "potential," or "continue" or the negative of these terms or other similar terminology. There are various factors that could cause actual results to differ materially from those suggested by the forward-looking statements; accordingly, there can be no assurance that such indicated results will be realized. These factors include:

- the impact of recent and future federal and state regulatory changes, including environmental laws and regulations governing air, water, land, and protection of other natural resources, and also changes in tax and other laws and regulations to which the Company is subject, as well as changes in application of existing laws and regulations;
- the uncertainty surrounding the recently enacted Tax Reform Legislation, including implementing regulations and IRS interpretations, actions that may be taken in response by regulatory authorities, and its impact, if any, on the credit ratings of the Company;
- current and future litigation or regulatory investigations, proceedings, or inquiries;
- the effects, extent, and timing of the entry of additional competition in the markets in which the Company operates;
- variations in demand for electricity, including those relating to weather, the general economy, population and business growth (and declines), the effects of energy conservation and efficiency measures, including from the development and deployment of alternative energy sources such as self-generation and distributed generation technologies, and any potential economic impacts resulting from federal fiscal decisions;
- available sources and costs of fuels;
- effects of inflation;
- the ability to control costs and avoid cost overruns during the development and construction of facilities, to construct facilities in accordance with the requirements of permits and licenses, and to satisfy any environmental performance standards, including the requirements of any tax incentives;
- investment performance of the Company's employee and retiree benefit plans;
- advances in technology;
- state and federal rate regulations and the impact of pending and future rate cases and negotiations, including rate actions relating to fuel and other cost recovery mechanisms;
- the ability to successfully operate generating, transmission, and distribution facilities and the successful performance of necessary corporate functions;
- litigation related to the Kemper County energy facility;
- internal restructuring or other restructuring options that may be pursued;
- potential business strategies, including acquisitions or dispositions of assets or businesses, which cannot be assured to be completed or beneficial to the Company;
- the ability of counterparties of the Company to make payments as and when due and to perform as required;
- the ability to obtain new short- and long-term contracts with wholesale customers;
- the direct or indirect effect on the Company's business resulting from cyber intrusion or physical attack and the threat of physical attacks;
- interest rate fluctuations and financial market conditions and the results of financing efforts;
- changes in the Company's credit ratings, including impacts on interest rates, access to capital markets, and collateral requirements;
- the impacts of any sovereign financial issues, including impacts on interest rates, access to capital markets, impacts on foreign currency exchange rates, counterparty performance, and the economy in general;
- the ability of the Company to obtain additional generating capacity (or sell excess generating capacity) at competitive prices;

- catastrophic events such as fires, earthquakes, explosions, floods, tornadoes, hurricanes and other storms, droughts, pandemic health events such as influenzas, or other similar occurrences;
- the direct or indirect effects on the Company's business resulting from incidents affecting the U.S. electric grid or operation of generating resources;
- the effect of accounting pronouncements issued periodically by standard-setting bodies; and
- other factors discussed elsewhere herein and in other reports (including the Form 10-K) filed by the Company from time to time with the SEC.

The Company expressly disclaims any obligation to update any forward-looking statements.

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STATEMENTS OF OPERATIONS
For the Years Ended December 31, 2017, 2016, and 2015
Mississippi Power Company 2017 Annual Report

	2017	2016	2015
		(in millions)	
Operating Revenues:			
Retail revenues	**$ 854**	$ 859	$ 776
Wholesale revenues, non-affiliates	**259**	261	270
Wholesale revenues, affiliates	**56**	26	76
Other revenues	**18**	17	16
Total operating revenues	**1,187**	1,163	1,138
Operating Expenses:			
Fuel	**395**	343	443
Purchased power	**25**	34	12
Other operations and maintenance	**282**	312	274
Depreciation and amortization	**161**	132	123
Taxes other than income taxes	**104**	109	94
Estimated loss on Kemper IGCC	**3,362**	428	365
Total operating expenses	**4,329**	1,358	1,311
Operating Loss	**(3,142)**	(195)	(173)
Other Income and (Expense):			
Allowance for equity funds used during construction	**72**	124	110
Interest expense, net of amounts capitalized	**(42)**	(74)	(7)
Other income (expense), net	**(8)**	(7)	(8)
Total other income and (expense)	**22**	43	95
Loss Before Income Taxes	**(3,120)**	(152)	(78)
Income taxes (benefit)	**(532)**	(104)	(72)
Net Loss	**(2,588)**	(48)	(6)
Dividends on Preferred Stock	**2**	2	2
Net Loss After Dividends on Preferred Stock	**$ (2,590)**	$ (50)	$ (8)

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

STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
For the Years Ended December 31, 2017, 2016, and 2015
Mississippi Power Company 2017 Annual Report

	2017	2016	2015
		(in millions)	
Net Loss	**$ (2,588)**	$ (48)	$ (6)
Other comprehensive income (loss):			
Qualifying hedges:			
Changes in fair value, net of tax of $(1), $1, and $-, respectively	**(1)**	1	—
Reclassification adjustment for amounts included in net income, net of tax of $1, $1, and $1, respectively	**1**	1	1
Total other comprehensive income (loss)	**—**	2	1
Comprehensive Loss	**$ (2,588)**	$ (46)	$ (5)

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

STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2017, 2016, and 2015
Mississippi Power Company 2017 Annual Report

	2017	2016	2015
		(in millions)	
Operating Activities:			
Net loss	**$ (2,588)**	$ (48)	$ (6)
Adjustments to reconcile net loss to net cash provided from operating activities —			
Depreciation and amortization, total	**198**	157	126
Deferred income taxes	**(727)**	(67)	777
Investment tax credits	**—**	—	(210)
Allowance for equity funds used during construction	**(72)**	(124)	(110)
Pension and postretirement funding	**—**	(47)	—
Regulatory assets associated with Kemper IGCC	**(19)**	(12)	(61)
Estimated loss on Kemper IGCC	**3,179**	428	365
Income taxes receivable, non-current	**—**	—	(544)
Other, net	**(12)**	(20)	8
Changes in certain current assets and liabilities —			
-Receivables	**540**	13	28
-Fossil fuel stock	**24**	4	(4)
-Prepaid income taxes	**—**	39	(35)
-Other current assets	**(13)**	(12)	(14)
-Accounts payable	**(3)**	(14)	(34)
-Accrued interest	**(29)**	27	(2)
-Accrued taxes	**80**	14	(11)
-Over recovered regulatory clause revenues	**(51)**	(45)	96
-Mirror CWIP	**—**	—	(271)
-Customer liability associated with Kemper refunds	**(1)**	(73)	73
-Other current liabilities	**(3)**	9	2
Net cash provided from operating activities	**503**	229	173
Investing Activities:			
Property additions	**(429)**	(798)	(857)
Construction payables	**(47)**	(26)	(9)
Government grant proceeds	**—**	137	—
Other investing activities	**(28)**	(10)	(40)
Net cash used for investing activities	**(504)**	(697)	(906)
Financing Activities:			
Decrease in notes payable, net	**(18)**	—	—
Proceeds —			
Capital contributions from parent company	**1,002**	627	277
Long-term debt issuance to parent company	**40**	200	275
Other long-term debt	**—**	1,200	—
Short-term borrowings	**109**	—	505
Redemptions —			
Short-term borrowings	**(109)**	(478)	(5)
Long-term debt to parent company	**(591)**	(225)	—
Capital leases	**(71)**	(3)	(3)
Senior notes	**(35)**	(300)	—
Other long-term debt	**(300)**	(425)	(350)
Other financing activities	**(2)**	(2)	(1)
Net cash provided from financing activities	**25**	594	698
Net Change in Cash and Cash Equivalents	**24**	126	(35)
Cash and Cash Equivalents at Beginning of Year	**224**	98	133
Cash and Cash Equivalents at End of Year	**$ 248**	$ 224	$ 98
Supplemental Cash Flow Information:			
Cash paid (received) during the period for —			
Interest (net of $29, $49, and $66 capitalized, respectively)	**$ 65**	$ 50	$ 45
Income taxes (net of refunds)	**(424)**	(97)	(33)
Noncash transactions —			
Accrued property additions at year-end	**32**	78	105
Issuance of promissory note to parent related to repayment of interest-bearing refundable deposits and accrued interest	**—**	—	301

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

BALANCE SHEETS
At December 31, 2017 and 2016
Mississippi Power Company 2017 Annual Report

Assets	**2017**	2016
	(in millions)	
Current Assets:		
Cash and cash equivalents	**$ 248**	$ 224
Receivables —		
Customer accounts receivable	**36**	29
Unbilled revenues	**41**	42
Income taxes receivable, current	**4**	544
Affiliated	**16**	15
Other accounts and notes receivable	**12**	14
Fossil fuel stock	**17**	100
Materials and supplies, current	**44**	76
Other regulatory assets, current	**125**	115
Other current assets	**9**	8
Total current assets	**552**	1,167
Property, Plant, and Equipment:		
In service	**4,773**	4,865
Less: Accumulated provision for depreciation	**1,325**	1,289
Plant in service, net of depreciation	**3,448**	3,576
Construction work in progress	**84**	2,545
Total property, plant, and equipment	**3,532**	6,121
Other Property and Investments	**30**	12
Deferred Charges and Other Assets:		
Deferred charges related to income taxes	**35**	361
Other regulatory assets, deferred	**437**	518
Accumulated deferred income taxes	**247**	—
Other deferred charges and assets	**33**	56
Total deferred charges and other assets	**752**	935
Total Assets	**$ 4,866**	$ 8,235

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

BALANCE SHEETS
At December 31, 2017 and 2016
Mississippi Power Company 2017 Annual Report

Liabilities and Stockholder's Equity	**2017**	2016
	(in millions)	
Current Liabilities:		
Securities due within one year —		
Parent	**$ —**	$ 551
Other	**989**	78
Notes payable	**4**	23
Accounts payable —		
Affiliated	**59**	62
Other	**96**	135
Accrued taxes —		
Accrued income taxes	**40**	—
Other accrued taxes	**101**	99
Unrecognized tax benefits	**—**	383
Accrued interest	**16**	46
Accrued compensation	**39**	42
Asset retirement obligations, current	**37**	32
Over recovered regulatory clause liabilities	**—**	51
Other current liabilities	**82**	36
Total current liabilities	**1,463**	1,538
Long-Term Debt (See accompanying statements)	**1,097**	2,424
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	**—**	756
Deferred credits related to income taxes	**372**	7
Employee benefit obligations	**116**	115
Asset retirement obligations, deferred	**137**	146
Other cost of removal obligations	**178**	170
Other regulatory liabilities, deferred	**79**	77
Other deferred credits and liabilities	**33**	26
Total deferred credits and other liabilities	**915**	1,297
Total Liabilities	**3,475**	5,259
Cumulative Redeemable Preferred Stock (See accompanying statements)	**33**	33
Common Stockholder's Equity (See accompanying statements)	**1,358**	2,943
Total Liabilities and Stockholder's Equity	**$ 4,866**	$ 8,235
Commitments and Contingent Matters (See notes)		

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

STATEMENTS OF CAPITALIZATION
At December 31, 2017 and 2016
Mississippi Power Company 2017 Annual Report

	2017	2016	**2017**	2016
	(in millions)		*(percent of total)*	
Long-Term Debt:				
Long-term notes payable —				
5.60% due 2017	**$ —**	$ 35		
1.63% due 2018	**50**	50		
5.55% due 2019	**125**	125		
4.25% to 5.40% due 2035-2042	**630**	630		
Adjustable rate (3.05% at 12/31/17) due 2018	**900**	1,200		
Total long-term notes payable	**1,705**	2,040		
Other long-term debt —				
Pollution control revenue bonds —				
5.15% due 2028	**43**	43		
Variable rates (2.45% to 2.50% at 12/31/17) due 2018	**40**	40		
Plant Daniel revenue bonds (7.13%) due 2021	**270**	270		
Long-term debt payable to parent company (2.27%) due 2017	**—**	551		
Total other long-term debt	**353**	904		
Capitalized lease obligations	**—**	74		
Unamortized debt premium	**36**	45		
Unamortized debt discount	**(1)**	(2)		
Unamortized debt issuance expense	**(7)**	(8)		
Total long-term debt (annual interest requirement — $86 million)	**2,086**	3,053		
Less amount due within one year	**989**	629		
Long-term debt excluding amount due within one year	**1,097**	2,424	**44.1%**	44.9%
Cumulative Redeemable Preferred Stock:				
$100 par value —				
Authorized — 1,244,139 shares				
Outstanding — 334,210 shares				
4.40% to 5.25% (annual dividend requirement — $2 million)	**33**	33	**1.3**	0.6
Common Stockholder's Equity:				
Common stock, without par value —				
Authorized — 1,130,000 shares				
Outstanding — 1,121,000 shares	**38**	38		
Paid-in capital	**4,529**	3,525		
Accumulated deficit	**(3,205)**	(616)		
Accumulated other comprehensive loss	**(4)**	(4)		
Total common stockholder's equity	**1,358**	2,943	**54.6**	54.5
Total Capitalization	**$ 2,488**	$ 5,400	**100.0%**	100.0%

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

STATEMENTS OF COMMON STOCKHOLDER'S EQUITY
For the Years Ended December 31, 2017, 2016, and 2015
Mississippi Power Company 2017 Annual Report

	Number of Common Shares Issued	Common Stock	Paid-In Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Total
				(in millions)		
Balance at December 31, 2014	1	$ 38	$ 2,612	$ (559)	$ (7)	$ 2,084
Net loss after dividends on preferred stock	—	—	—	(8)	—	(8)
Capital contributions from parent company	—	—	281	—	—	281
Other comprehensive income (loss)	—	—	—	—	1	1
Other	—	—	—	1	—	1
Balance at December 31, 2015	1	38	2,893	(566)	(6)	2,359
Net loss after dividends on preferred stock	—	—	—	(50)	—	(50)
Capital contributions from parent company	—	—	632	—	—	632
Other comprehensive income (loss)	—	—	—	—	2	2
Balance at December 31, 2016	**1**	**38**	**3,525**	**(616)**	**(4)**	**2,943**
Net loss after dividends on preferred stock	**—**	**—**	**—**	**(2,590)**	**—**	**(2,590)**
Capital contributions from parent company	**—**	**—**	**1,004**	**—**	**—**	**1,004**
Other	**—**	**—**	**—**	**1**	**—**	**1**
Balance at December 31, 2017	**1**	**$ 38**	**$ 4,529**	**$ (3,205)**	**$ (4)**	**$ 1,358**

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

Index to the Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

Mississippi Power Company (the Company) is a wholly-owned subsidiary of Southern Company, which is the parent company of the Company and three other traditional electric operating companies, as well as Southern Power, Southern Company Gas (as of July 1, 2016), SCS, Southern Linc, Southern Company Holdings, Inc. (Southern Holdings), Southern Nuclear, PowerSecure, Inc. (PowerSecure) (as of May 9, 2016), and other direct and indirect subsidiaries. The traditional electric operating companies – Alabama Power, Georgia Power, Gulf Power, and the Company – are vertically integrated utilities providing electric service in four Southeastern states. The Company provides electric service to retail customers in southeast Mississippi and to wholesale customers in the Southeast. Southern Power develops, constructs, acquires, owns, and manages power generation assets, including renewable energy projects, and sells electricity at market-based rates in the wholesale market. Southern Company Gas distributes natural gas through utilities in seven states and is involved in several other complementary businesses including gas marketing services, wholesale gas services, and gas midstream operations. SCS, the system service company, provides, at cost, specialized services to Southern Company and its subsidiary companies. Southern Linc provides digital wireless communications for use by Southern Company and its subsidiary companies and also markets these services to the public and provides fiber optics services within the Southeast. Southern Holdings is an intermediate holding company subsidiary, primarily for Southern Company's investments in leveraged leases and for other electric services. Southern Nuclear operates and provides services to the Southern Company system's nuclear power plants. PowerSecure is a provider of products and services in the areas of distributed generation, energy efficiency, and utility infrastructure.

The Company is subject to regulation by the FERC and the Mississippi PSC. As such, the Company's financial statements reflect the effects of rate regulation in accordance with GAAP and comply with the accounting policies and practices prescribed by its regulatory commissions. The preparation of financial statements in conformity with GAAP requires the use of estimates, and the actual results may differ from those estimates. Certain prior years' data presented in the financial statements have been reclassified to conform to the current year presentation.

Recently Issued Accounting Standards

Revenue

In 2014, the FASB issued ASC 606, *Revenue from Contracts with Customers* (ASC 606), replacing the existing accounting standard and industry specific guidance for revenue recognition with a five-step model for recognizing and measuring revenue from contracts with customers. The underlying principle of the new standard is to recognize revenue to depict the transfer of goods or services to customers at the amount expected to be collected. The new standard also requires enhanced disclosures regarding the nature, amount, timing, and uncertainty of revenue and the related cash flows arising from contracts with customers.

Most of the Company's revenue, including energy provided to customers, is from tariff offerings that provide electricity without a defined contractual term, as well as longer-term contractual commitments, including PPAs.

The Company has completed the evaluation of all revenue streams and determined that the adoption of ASC 606 will not change the current timing of revenue recognition for such transactions. Some revenue arrangements, such as energy-related derivatives and alternative revenue programs, are excluded from the scope of ASC 606 and, therefore, will be accounted for and disclosed or presented separately from revenues under ASC 606 on the Company's financial statements, if material. The Company has concluded contributions in aid of construction are not in scope for ASC 606 and will continue to be accounted for as an offset to property, plant, and equipment.

The new standard is effective for reporting periods beginning after December 15, 2017. The Company applied the modified retrospective method of adoption effective January 1, 2018. The Company also utilized practical expedients which allowed it to apply the standard to open contracts at the date of adoption and to reflect the aggregate effect of all modifications when identifying performance obligations and allocating the transaction price for contracts modified before the effective date. Under the modified retrospective method of adoption, prior year reported results are not restated; however, a cumulative-effect adjustment to retained earnings at January 1, 2018 is recorded. In addition, quarterly disclosures will include comparative information on 2018 financial statement line items under current guidance. The adoption of ASC 606 did not result in a cumulative-effect adjustment.

Leases

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (ASU 2016-02). ASU 2016-02 requires lessees to recognize on the balance sheet a lease liability and a right-of-use asset for all leases. ASU 2016-02 also changes the recognition, measurement, and presentation of expense associated with leases and provides clarification regarding the identification of certain components of contracts that would represent a lease. The accounting required by lessors is relatively unchanged. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 and the Company will adopt the new standard effective January 1, 2019.

The Company is currently implementing an information technology system along with the related changes to internal controls and accounting policies that will support the accounting for leases under ASU 2016-02. In addition, the Company has substantially completed a detailed inventory and analysis of its leases. In terms of rental charges and duration of contracts, the most significant leases relate to equipment and cellular towers where the Company is the lessee and to equipment where the Company is the lessor. The Company is currently analyzing pole attachment agreements and a lease determination has not been made at this time. While the Company has not yet determined the ultimate impact, adoption of ASU 2016-02 is expected to have a significant impact on the Company's balance sheet.

Other

In March 2016, the FASB issued ASU No. 2016-09, *Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* (ASU 2016-09). ASU 2016-09 changes the accounting for income taxes and the cash flow presentation for share-based payment award transactions effective for fiscal years beginning after December 15, 2016. The new guidance requires all excess tax benefits and deficiencies related to the exercise or vesting of stock compensation to be recognized as income tax expense or benefit in the income statement. Previously, the Company recognized any excess tax benefits and deficiencies related to the exercise and vesting of stock compensation as additional paid-in capital. In addition, the new guidance requires excess tax benefits for share-based payments to be included in net cash provided from operating activities rather than net cash provided from financing activities on the statement of cash flows. The Company elected to adopt the guidance in 2016 and reflect the related adjustments as of January 1, 2016. Prior year's data presented in the financial statements has not been adjusted. The Company also elected to recognize forfeitures as they occur. The new guidance did not have a material impact on the results of operations, financial position, or cash flows of the Company. See Notes 5 and 8 for disclosures impacted by ASU 2016-09.

On March 10, 2017, the FASB issued ASU No. 2017-07, *Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost* (ASU 2017-07). ASU 2017-07 requires that an employer report the service cost component in the same line item or items as other compensation costs and requires the other components of net periodic pension and postretirement benefit costs to be separately presented in the income statement outside of income from operations. Additionally, only the service cost component is eligible for capitalization, when applicable. However, all cost components remain eligible for capitalization under FERC regulations. ASU 2017-07 will be applied retrospectively for the presentation of the service cost component and the other components of net periodic pension and postretirement benefit costs in the income statement. The capitalization of only the service cost component of net periodic pension and postretirement benefit costs in assets will be applied on a prospective basis. ASU 2017-07 is effective for periods beginning after December 15, 2017. The presentation changes required for net periodic pension and postretirement benefit costs will result in a decrease in the Company's operating income and an increase in other income for 2016 and 2017 and are expected to result in a decrease in operating income and an increase in other income for 2018. The Company adopted ASU 2017-07 effective January 1, 2018 with no material impact on its financial statements.

On August 28, 2017, the FASB issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities* (ASU 2017-12), amending the hedge accounting recognition and presentation requirements. ASU 2017-12 makes more financial and non-financial hedging strategies eligible for hedge accounting, amends the related presentation and disclosure requirements, and simplifies hedge effectiveness assessment requirements. ASU 2017-12 is effective for fiscal years beginning after December 15, 2018, with early adoption permitted. The Company adopted ASU 2017-12 effective January 1, 2018 with no material impact on its financial statements.

Affiliate Transactions

The Company has an agreement with SCS under which the following services are rendered to the Company at direct or allocated cost: general and design engineering, operations, purchasing, accounting, finance and treasury, tax, information technology, marketing, auditing, insurance and pension administration, human resources, systems and procedures, digital wireless communications, and other services with respect to business and operations, construction management, and power pool transactions. Costs for these services amounted to $140 million, $231 million, and $295 million during 2017, 2016, and 2015, respectively. Cost allocation methodologies used by SCS prior to the repeal of the Public Utility Holding Company Act of 1935, as amended, were approved by the SEC. Subsequently, additional cost allocation methodologies have been reported to the FERC and management believes they are reasonable. The FERC permits services to be rendered at cost by system service companies. See Note 7 under "Operating Leases" for additional information.

The Company has an agreement with Alabama Power under which the Company owns a portion of Greene County Steam Plant. Alabama Power operates Greene County Steam Plant, and the Company reimburses Alabama Power for its proportionate share of non-fuel expenditures and costs, which totaled $9 million, $13 million, and $11 million in 2017, 2016, and 2015, respectively. Also, the Company reimburses Alabama Power for any direct fuel purchases delivered from an Alabama Power transfer facility. There were no fuel purchases in 2017 or 2016. Fuel purchases were $8 million in 2015. The Company also has an agreement with Gulf Power under which Gulf Power owns a portion of Plant Daniel. The Company operates Plant Daniel, and Gulf Power reimburses the Company for its proportionate share of all associated expenditures and costs, which totaled $31 million, $26 million, and $27 million in 2017, 2016, and 2015, respectively. See Note 4 for additional information.

Total power purchased from affiliates through the power pool, included in purchased power in the statement of operations, totaled $16 million, $29 million, and $7 million in 2017, 2016, and 2015, respectively.

In June 2017, the Company received a capital contribution from Southern Company of $1.0 billion. The Company used a portion of the proceeds to repay all of the $591 million outstanding principal amount of promissory notes to Southern Company. See Note 6 for additional information.

On September 15, 2017, the Company issued a floating rate promissory note to Southern Company in an aggregate principal amount of up to $150 million bearing interest based on one-month LIBOR. The Company borrowed $109 million under this promissory note primarily to satisfy its federal income tax obligations for the quarter ending September 30, 2017 and subsequently repaid the promissory note upon receipt of its income tax refund from the U.S. federal government related to the settlement concerning deductible research and experimental (R&E) expenditures. See Note 5 under "Section 174 Research and Experimental Deduction" for additional information.

The Company also provides incidental services to and receives such services from other Southern Company subsidiaries which are generally minor in duration and amount. Except as described herein, the Company neither provided nor received any material services to or from affiliates in 2017, 2016, or 2015.

The traditional electric operating companies, including the Company, and Southern Power may jointly enter into various types of wholesale energy, natural gas, and certain other contracts, either directly or through SCS, as agent. Each participating company may be jointly and severally liable for the obligations incurred under these agreements. See Note 7 under "Fuel and Purchased Power Agreements" for additional information.

Regulatory Assets and Liabilities

The Company is subject to accounting requirements for the effects of rate regulation. Regulatory assets represent probable future revenues associated with certain costs that are expected to be recovered from customers through the ratemaking process. Regulatory liabilities represent probable future reductions in revenues associated with amounts that are expected to be credited to customers through the ratemaking process.

Regulatory assets and (liabilities) reflected in the balance sheets at December 31 relate to:

	2017	2016	Note
		(in millions)	
Retiree benefit plans – regulatory assets	**$ 174**	$ 173	(a)
Asset retirement obligations	**95**	83	(b)
Kemper County energy facility	**88**	194	(c)
Remaining net book value of retired assets	**44**	53	(d)
Property tax	**43**	37	(e)
Deferred charges related to income taxes	**36**	362	(d)
Plant Daniel Units 3 and 4	**36**	33	(f)
Other regulatory assets	**28**	28	(g)
ECO carryforward	**26**	22	(h)
Other regulatory liabilities	**—**	(1)	(i)
Deferred credits related to income taxes	**(377)**	(9)	(j)
Other cost of removal obligations	**(178)**	(170)	(k)
Property damage	**(57)**	(68)	(l)
Total regulatory assets (liabilities), net	**$ (42)**	$ 737	

Note: The recovery and amortization periods for these regulatory assets and (liabilities) are as follows:

(a) Recovered and amortized over the average remaining service period which may range up to 15 years. See Note 2 for additional information.

(b) To be recovered upon completion of removal activities over a period approved by the Mississippi PSC.

(c) Includes $114 million of regulatory assets and $26 million of regulatory liabilities to be recovered in rates over periods of eight and six years, respectively. For additional information, see Note 3 under "Kemper County Energy Facility – Rate Recovery – Kemper Settlement Agreement."

(d) Recovered over the related property lives up to 48 years.

(e) Recovered through the ad valorem tax adjustment clause over a 12-month period beginning in April of the following year. See Note 3 under "Retail Regulatory Matters – Ad Valorem Tax Adjustment" for additional information.

(f) Represents the difference between the revenue requirement under the purchase option and the revenue requirement assuming operating lease accounting treatment for the extended term, which will be amortized over a 10-year period beginning October 2021.

(g) Comprised of vacation pay, loss on reacquired debt, and other miscellaneous assets. These costs are recorded and recovered or amortized as approved by the Mississippi PSC over periods which may range up to 50 years. This amount also includes fuel-hedging assets and liabilities which are recorded over the life of the underlying hedged purchase contracts, which generally do not exceed three years. Upon final settlement, actual costs incurred are recovered through the ECM.

(h) Recovered through the ECO clause in the year following the deferral.

(i) Comprised of numerous immaterial components including deferred income tax credits and other miscellaneous liabilities that are recorded and refunded or amortized as approved by the Mississippi PSC generally over periods not exceeding one year.

(j) This amount includes excess deferred income taxes primarily associated with Tax Reform Legislation of $375 million, of which $273 million is related to protected deferred income taxes to be recovered over the related property lives utilizing the average rate assumption method in accordance with IRS normalization principles and $102 million related to unprotected (not subject to normalization) deferred income taxes to be amortized over a period approved by the Mississippi PSC or the FERC, as appropriate. Of the total excess deferred income taxes associated with Tax Reform Legislation, $129 million is associated with the Kemper County energy facility. The unprotected portion associated with the Kemper County energy facility is $54 million, of which $38 million is being amortized over eight years for retail as approved by the Mississippi PSC on February 6, 2018 and $16 million is wholesale-related. Currently, the Company is requesting eight-year amortization for the remaining portions of the unprotected deferred income taxes associated with Tax Reform Legislation in all of its retail and wholesale rate filings. See Note 3 under "Retail Regulatory Matters" and "Kemper County Energy Facility" and Note 5 for additional information.

(k) Collected in advance from customers to remove assets upon their retirement.

(l) For additional information, see Note 1 under "Provision for Property Damage."

In the event that a portion of the Company's operations is no longer subject to applicable accounting rules for rate regulation, the Company would be required to write off to income or reclassify to accumulated OCI related regulatory assets and liabilities that are not specifically recoverable through regulated rates. In addition, the Company would be required to determine if any impairment to other assets, including plant, exists and write down the assets, if impaired, to their fair values. All regulatory assets and liabilities are to be reflected in rates. See Note 3 under "Retail Regulatory Matters" and "Kemper County Energy Facility" for additional information.

Government Grants

In 2010, the DOE, through a cooperative agreement with SCS, agreed to fund $270 million of the Kemper County energy facility through the grants awarded to the project by the DOE under the Clean Coal Power Initiative Round 2 (Initial DOE Grants). Through December 31, 2017, the Company has received grant funds of $382 million, of which $245 million of the Initial DOE Grants were used for the construction of the Kemper County energy facility, which is reflected in the Company's financial statements as a reduction to the Kemper County energy facility capital costs, and $137 million received on April 8, 2016 (Additional DOE Grants), which are expected to be used to reduce future rate impacts. An additional $2 million is expected to be received for allowable costs through December 31, 2017. See Note 3 under "Kemper County Energy Facility – Schedule and Cost Estimate" for additional information.

Revenues

Energy and other revenues are recognized as services are provided. Wholesale capacity revenues from long-term contracts are recognized at the lesser of the levelized amount or the amount billable under the contract over the respective contract period. Unbilled revenues related to retail sales are accrued at the end of each fiscal period. The Company's retail and wholesale rates include provisions to adjust billings for fluctuations in fuel costs, fuel hedging, the energy component of purchased power costs, and certain other costs. Retail rates also include provisions to adjust billings for fluctuations in costs for ad valorem taxes and certain qualifying environmental costs. Revenues are adjusted for differences between these actual costs and projected amounts billed in current regulated rates. Under or over recovered regulatory clause revenues are recorded in the balance sheets and are recovered or returned to customers through adjustments to the billing factors. The Company is required to file with the Mississippi PSC for an adjustment to the fuel cost recovery, ad valorem, and environmental factors annually.

The Company serves long-term contracts with rural electric cooperative associations and municipalities located in southeastern Mississippi under cost-based MRA electric tariffs which are subject to regulation by the FERC. The contracts with these wholesale customers represented 19.3% of the Company's total operating revenues in 2017 and are largely subject to rolling 10-year cancellation notices. Historically, these wholesale customers have acted as a group and any changes in contractual relationships for one customer are likely to be followed by the other wholesale customers.

Except as described above for the Company's cost-based MRA electric tariff customers, the Company has a diversified base of customers and no single customer or industry comprises 10% or more of revenues. For all periods presented, uncollectible accounts averaged less than 1% of revenues.

See Note 3 under "Retail Regulatory Matters" for additional information.

Fuel Costs

Fuel costs are expensed as the fuel is used. Fuel expense generally includes fuel transportation costs and the cost of purchased emissions allowances as they are used. Fuel costs also include gains and/or losses from fuel-hedging programs as approved by the Mississippi PSC.

Income and Other Taxes

The Company uses the liability method of accounting for deferred income taxes and provides deferred income taxes for all significant income tax temporary differences. ITCs utilized are deferred and amortized to income over the average life of the related property. Taxes that are collected from customers on behalf of governmental agencies to be remitted to these agencies are presented net on the statements of operations.

The Company recognizes tax positions that are "more likely than not" of being sustained upon examination by the appropriate taxing authorities. See Note 5 under "Unrecognized Tax Benefits" for additional information.

Property, Plant, and Equipment

Property, plant, and equipment is stated at original cost less any regulatory disallowances and impairments. Original cost includes: materials; labor; minor items of property; appropriate administrative and general costs; payroll-related costs such as taxes, pensions, and other benefits; and the interest capitalized and cost of equity funds used during construction for projects where recovery of CWIP is not allowed in rates.

The Company's property, plant, and equipment in service consisted of the following at December 31:

		2017		2016
		(in millions)		
Generation	**$**	**2,801**	$	2,632
Transmission		**737**		712
Distribution		**946**		916
General		**204**		520
Plant acquisition adjustment		**85**		85
Total plant in service	**$**	**4,773**	$	4,865

The cost of replacements of property, exclusive of minor items of property, is capitalized. The cost of maintenance, repairs, and replacement of minor items of property is charged to other operations and maintenance expenses except for a portion of the railway track maintenance costs. The portion of railway track maintenance costs not charged to operations and maintenance expenses are charged to fuel stock and recovered through the Company's fuel clause.

Depreciation, Depletion, and Amortization

Depreciation of the original cost of utility plant in service is provided primarily by using composite straight-line rates, which approximated 3.7% in 2017, 4.2% in 2016, and 4.7% in 2015. The decrease in 2017 is primarily due to lower depreciation expense as a result of recording a loss on the lignite mine in June 2017. The decrease in the 2016 depreciation rate is primarily due to fully depreciating and retiring the ARO at Plant Watson, partially offset by the increase in depreciation for the Plant Daniel scrubbers for a full year. See "Asset Retirement Obligations and Other Costs of Removal" herein for additional information. Depreciation studies are conducted periodically to update the composite rates. The Mississippi PSC approved the 2014 study, with new rates effective January 1, 2015. When property subject to depreciation is retired or otherwise disposed of in the normal course of business, its original cost, together with the cost of removal, less salvage, is charged to accumulated depreciation. Minor items of property included in the original cost of the plant are retired when the related property unit is retired. Depreciation includes an amount for the expected cost of removal of facilities, except for the Kemper County energy facility combined cycle and related assets in service.

Asset Retirement Obligations and Other Costs of Removal

AROs are computed as the present value of the estimated ultimate costs for an asset's future retirement and are recorded in the period in which the liability is incurred. The costs are capitalized as part of the related long-lived asset and depreciated over the asset's useful life. In the absence of quoted market prices, AROs are estimated using present value techniques in which estimates of future cash outlays associated with the asset retirements are discounted using a credit-adjusted risk-free rate. Estimates of the timing and amounts of future cash outlays are based on projections of when and how the assets will be retired and the cost of future removal activities. The Company has received accounting guidance from the Mississippi PSC allowing the continued accrual of other future retirement costs for long-lived assets that the Company does not have a legal obligation to retire. Accordingly, the accumulated removal costs for these obligations are reflected in the balance sheets as a regulatory liability.

The liability for AROs primarily relates to facilities that are subject to the Disposal of Coal Combustion Residuals from Electric Utilities final rule published by the EPA in 2015 (CCR Rule), principally ash ponds. In addition, the Company has retirement obligations related to various landfill sites, underground storage tanks, deep injection wells, water wells, substation removal, mine reclamation, and asbestos removal. The Company also has identified AROs related to certain transmission and distribution facilities and certain wireless communication towers. However, liabilities for the removal of these assets have not been recorded because the settlement timing for the AROs related to these assets is indeterminable and, therefore, the fair value of the AROs cannot be reasonably estimated. A liability for these AROs will be recognized when sufficient information becomes available to support a reasonable estimation of the ARO. The Company will continue to recognize in the statements of operations allowed removal costs in accordance with its regulatory treatment. Any differences between costs recognized in accordance with accounting standards related to asset retirement and environmental obligations and those reflected in rates are recognized as either a regulatory asset or liability, as ordered by the Mississippi PSC, and are reflected in the balance sheets.

Details of the AROs included in the balance sheets are as follows:

	2017	2016
	(in millions)	
Balance at beginning of year	**$ 179**	$ 177
Liabilities incurred	**—**	15
Liabilities settled	**(23)**	(23)
Accretion	**5**	5
Cash flow revisions	**13**	5
Balance at end of year	**$ 174**	$ 179

The increase in cash flow revisions in 2017 is primarily related to a revision in the closure date of the lignite mine ARO.

The cost estimates for AROs related to the CCR Rule are based on information as of December 31, 2017 using various assumptions related to closure and post-closure costs, timing of future cash outlays, inflation and discount rates, and the potential methods for complying with the CCR Rule requirements for closure. As further analysis is performed and closure details are developed, the Company will continue to periodically update these cost estimates as necessary.

Allowance for Funds Used During Construction

The Company records AFUDC, which represents the estimated debt and equity costs of capital funds that are necessary to finance the construction of new regulated facilities. While cash is not realized currently, AFUDC increases the revenue requirement and is recovered over the service life of the plant through a higher rate base and higher depreciation. The equity component of AFUDC is not included in the calculation of taxable income. The average annual AFUDC rate was 6.7%, 6.5%, and 5.99% for the years ended December 31, 2017, 2016, and 2015, respectively. AFUDC equity was $72 million, $124 million, and $110 million in 2017, 2016, and 2015, respectively. The decrease in 2017 resulted from the Kemper IGCC project suspension in June 2017.

Impairment of Long-Lived Assets and Intangibles

The Company evaluates long-lived assets for impairment when events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. The determination of whether an impairment has occurred is based on either a specific regulatory disallowance or an estimate of undiscounted future cash flows attributable to the assets, as compared with the carrying value of the assets. If an impairment has occurred, the amount of the impairment recognized is determined by either the amount of regulatory disallowance or by estimating the fair value of the assets and recording a loss if the carrying value is greater than the fair value. For assets identified as held for sale, the carrying value is compared to the estimated fair value less the cost to sell in order to determine if an impairment loss is required. Until the assets are disposed of, their estimated fair value is re-evaluated when circumstances or events change.

Provision for Property Damage

The Company carries insurance for the cost of certain types of damage to generation plants and general property. However, the Company is self-insured for the cost of storm, fire, and other uninsured casualty damage to its property, including transmission and distribution facilities. As permitted by the Mississippi PSC and the FERC, the Company accrues for the cost of such damage through an annual expense accrual credited to regulatory liability accounts for the retail and wholesale jurisdictions. The cost of repairing actual damage resulting from such events that individually exceed $50,000 is charged to the reserve. Every three years the Mississippi PSC, the MPUS, and the Company will agree on SRR revenue level(s) for the ensuing period, based on historical data, expected exposure, type and amount of insurance coverage, excluding insurance cost, and any other relevant information. The accrual amount and the reserve balance are determined based on the SRR revenue level(s). If a significant change in circumstances occurs, then the SRR revenue level can be adjusted more frequently if the Company and the MPUS or the Mississippi PSC deem the change appropriate. The property damage reserve accrual will be the difference between the approved SRR revenues and the SRR revenue requirement, excluding any accrual to the reserve. In addition, SRR allows the Company to set up a regulatory asset, pending review, if the allowable actual retail property damage costs exceed the amount in the retail property damage reserve. The Company made retail accruals of $3 million, $4 million, and $3 million for 2017, 2016, and 2015, respectively. The Company also accrued $0.3 million annually in 2017, 2016, and 2015 for the wholesale jurisdiction. As of December 31, 2017, the property damage reserve balances were $56 million and $1 million for retail and wholesale, respectively.

Cash and Cash Equivalents

For purposes of the financial statements, temporary cash investments are considered cash equivalents. Temporary cash investments are securities with original maturities of 90 days or less.

Materials and Supplies

Generally, materials and supplies include the average cost of transmission, distribution, mining, and generating plant materials. Materials are charged to inventory when purchased and then expensed, capitalized to plant, or charged to fuel stock, as used, at weighted-average cost when utilized.

Fuel Inventory

Fuel inventory includes the average cost of coal, natural gas, oil, transportation, and emissions allowances. Fuel costs are recorded to inventory when purchased, and then expensed, at weighted average cost, as used and recovered by the Company through fuel cost recovery rates. The retail rate is approved by the Mississippi PSC and the wholesale rates are approved by the FERC. Emissions allowances granted by the EPA are included in inventory at zero cost.

Financial Instruments

The Company uses derivative financial instruments to limit exposure to fluctuations in interest rates, the prices of certain fuel purchases, and electricity purchases and sales. All derivative financial instruments are recognized as either assets or liabilities on the balance sheets (included in "Other" or shown separately as "Risk Management Activities") and are measured at fair value. See Note 9 for additional information regarding fair value. Substantially all of the Company's bulk energy purchases and sales contracts that meet the definition of a derivative are excluded from the fair value accounting requirements because they qualify for the "normal" scope exception, and are accounted for under the accrual method. Fuel and interest rate derivative contracts that qualify as cash flow hedges of anticipated transactions or are recoverable through the Mississippi PSC approved fuel-hedging program as discussed below result in the deferral of related gains and losses in OCI or regulatory assets and liabilities, respectively, until the hedged transactions occur. Other derivative contracts that qualify as fair value hedges are marked to market through current period income and are recorded on a net basis in the statements of operations. Cash flows from derivatives are classified on the statement of cash flows in the same category as the hedged item. See Note 10 for additional information regarding derivatives.

The Company offsets fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a netting arrangement. Additionally, the Company's collateral repayment obligations or rights to reclaim collateral arising from derivative instruments recognized at December 31, 2017 are immaterial.

The Company has an ECM clause which, among other things, allows the Company to utilize financial instruments to hedge its fuel commitments. Changes in the fair value of these financial instruments are recorded as regulatory assets or liabilities. Amounts paid or received as a result of financial settlement of these instruments are classified as fuel expense and are included in the ECM factor applied to customer billings. The Company's jurisdictional wholesale customers have a similar ECM mechanism, which has been approved by the FERC.

The Company is exposed to potential losses related to financial instruments in the event of counterparties' nonperformance. The Company has established controls to determine and monitor the creditworthiness of counterparties in order to mitigate the Company's exposure to counterparty credit risk.

Comprehensive Income

The objective of comprehensive income is to report a measure of all changes in common stock equity of an enterprise that result from transactions and other economic events of the period other than transactions with owners. Comprehensive income consists of net income, changes in the fair value of qualifying cash flow hedges, and reclassifications for amounts included in net income.

Variable Interest Entities

The primary beneficiary of a variable interest entity (VIE) is required to consolidate the VIE when it has both the power to direct the activities of the VIE that most significantly impact the VIE's economic performance and the obligation to absorb losses or the right to receive benefits from the VIE that could potentially be significant to the VIE.

The Company was required to provide financing for all costs associated with the mine development and operation under a contract with Liberty Fuels Company, LLC, a subsidiary of North American Coal Corporation (Liberty Fuels), in conjunction with the construction of the Kemper County energy facility. Liberty Fuels qualified as a VIE for which the Company was the primary beneficiary. As of December 31, 2016, the VIE consolidation resulted in an ARO asset and associated liability in the amounts of $20 million and $24 million, respectively. As of December 31, 2017, the VIE consolidation resulted in an ARO liability in the amount of $38 million. The associated ARO asset was included as part of an additional charge to income in 2017 as a result of the Company's assessment of the probability of disallowance by the Mississippi PSC. See Note 3 under "Kemper County Energy Facility" for additional information.

2. RETIREMENT BENEFITS

The Company has a defined benefit, trusteed, pension plan covering substantially all employees. This qualified pension plan is funded in accordance with requirements of the Employee Retirement Income Security Act of 1974, as amended (ERISA). No contributions to the qualified pension plan were made for the year ended December 31, 2017 and no mandatory contributions to the qualified pension plan are anticipated for the year ending December 31, 2018. The Company also provides certain defined benefit pension plans for a selected group of management and highly compensated employees. Benefits under these non-qualified pension plans are funded on a cash basis. In addition, the Company provides certain medical care and life insurance benefits for retired employees through other postretirement benefit plans. The Company funds its other postretirement trusts to the extent required by the FERC. For the year ending December 31, 2018, no other postretirement trust contributions are expected.

Actuarial Assumptions

The weighted average rates assumed in the actuarial calculations used to determine both the net periodic costs for the pension and other postretirement benefit plans for the following year and the benefit obligations as of the measurement date are presented below.

Assumptions used to determine net periodic costs:	2017	2016	2015
Pension plans			
Discount rate – benefit obligations	**4.44%**	4.69%	4.17%
Discount rate – interest costs	**3.81**	3.97	4.17
Discount rate – service costs	**4.83**	5.04	4.49
Expected long-term return on plan assets	**7.95**	8.20	8.20
Annual salary increase	**4.46**	4.46	3.59
Other postretirement benefit plans			
Discount rate – benefit obligations	**4.22%**	4.47%	4.03%
Discount rate – interest costs	**3.55**	3.66	4.03
Discount rate – service costs	**4.65**	4.88	4.38
Expected long-term return on plan assets	**6.88**	7.07	7.23
Annual salary increase	**4.46**	4.46	3.59

Assumptions used to determine benefit obligations:	2017	2016
Pension plans		
Discount rate	**3.80%**	4.44%
Annual salary increase	**4.46**	4.46
Other postretirement benefit plans		
Discount rate	**3.68%**	4.22%
Annual salary increase	**4.46**	4.46

The Company estimates the expected rate of return on pension plan and other postretirement benefit plan assets using a financial model to project the expected return on each current investment portfolio. The analysis projects an expected rate of return on each of eight different asset classes in order to arrive at the expected return on the entire portfolio relying on each trust's target asset allocation and reasonable capital market assumptions. The financial model is based on four key inputs: anticipated returns by asset class (based in part on historical returns), each trust's target asset allocation, an anticipated inflation rate, and the projected impact of a periodic rebalancing of each trust's portfolio.

An additional assumption used in measuring the accumulated other postretirement benefit obligations (APBO) was a weighted average medical care cost trend rate. The weighted average medical care cost trend rates used in measuring the APBO as of December 31, 2017 were as follows:

	Initial Cost Trend Rate	Ultimate Cost Trend Rate	Year That Ultimate Rate is Reached
Pre-65	6.50%	4.50%	2026
Post-65 medical	5.00	4.50	2026
Post-65 prescription	10.00	4.50	2026

An annual increase or decrease in the assumed medical care cost trend rate of 1% would affect the APBO and the service and interest cost components at December 31, 2017 as follows:

	1 Percent Increase	1 Percent Decrease
	(in millions)	
Benefit obligation	$ 5	$ 5
Service and interest costs	—	—

Pension Plans

The total accumulated benefit obligation for the pension plans was $541 million at December 31, 2017 and $479 million at December 31, 2016. Changes in the projected benefit obligations and the fair value of plan assets during the plan years ended December 31, 2017 and 2016 were as follows:

	2017	2016
	(in millions)	
Change in benefit obligation		
Benefit obligation at beginning of year	**$ 534**	$ 500
Service cost	**15**	13
Interest cost	**20**	19
Benefits paid	**(22)**	(20)
Actuarial (gain) loss	**55**	22
Balance at end of year	**602**	534
Change in plan assets		
Fair value of plan assets at beginning of year	**499**	430
Actual return (loss) on plan assets	**84**	39
Employer contributions	**2**	50
Benefits paid	**(22)**	(20)
Fair value of plan assets at end of year	**563**	499
Accrued liability	**$ (39)**	$ (35)

At December 31, 2017, the projected benefit obligations for the qualified and non-qualified pension plans were $571 million and $31 million, respectively. All pension plan assets are related to the qualified pension plan.

Amounts recognized in the balance sheets at December 31, 2017 and 2016 related to the Company's pension plans consist of the following:

	2017	2016
	(in millions)	
Other regulatory assets, deferred	**$ 158**	$ 154
Other current liabilities	**(3)**	(3)
Employee benefit obligations	**(36)**	(32)

Presented below are the amounts included in regulatory assets at December 31, 2017 and 2016 related to the defined benefit pension plans that had not yet been recognized in net periodic pension cost along with the estimated amortization of such amounts for 2018.

	2017	2016	**Estimated Amortization in 2018**
		(in millions)	
Prior service cost	**$ 3**	$ 3	**$ —**
Net (gain) loss	**155**	151	**10**
Regulatory assets	**$ 158**	$ 154	

The changes in the balance of regulatory assets related to the defined benefit pension plans for the years ended December 31, 2017 and 2016 are presented in the following table:

	2017	2016
	(in millions)	
Regulatory assets:		
Beginning balance	**$ 154**	$ 144
Net (gain) loss	**12**	16
Change in prior service costs	**—**	2
Reclassification adjustments:		
Amortization of prior service costs	**(1)**	(1)
Amortization of net gain (loss)	**(7)**	(7)
Total reclassification adjustments	**(8)**	(8)
Total change	**4**	10
Ending balance	**$ 158**	$ 154

Components of net periodic pension cost were as follows:

	2017	2016	2015
		(in millions)	
Service cost	**$ 15**	$ 13	$ 13
Interest cost	**20**	19	21
Expected return on plan assets	**(40)**	(35)	(33)
Recognized net (gain) loss	**7**	7	10
Net amortization	**1**	1	1
Net periodic pension cost	**$ 3**	$ 5	$ 12

Net periodic pension cost is the sum of service cost, interest cost, and other costs netted against the expected return on plan assets. The expected return on plan assets is determined by multiplying the expected rate of return on plan assets and the market-related value of plan assets. In determining the market-related value of plan assets, the Company has elected to amortize changes in the market value of all plan assets over five years rather than recognize the changes immediately. As a result, the accounting value of plan assets that is used to calculate the expected return on plan assets differs from the current fair value of the plan assets.

Future benefit payments reflect expected future service and are estimated based on assumptions used to measure the projected benefit obligation for the pension plans. At December 31, 2017, estimated benefit payments were as follows:

	Benefit Payments
	(in millions)
2018	$ 23
2019	24
2020	26
2021	27
2022	28
2023 to 2027	164

Other Postretirement Benefits

Changes in the APBO and in the fair value of plan assets during the plan years ended December 31, 2017 and 2016 were as follows:

	2017	2016
	(in millions)	
Change in benefit obligation		
Benefit obligation at beginning of year	**$ 97**	$ 97
Service cost	**1**	1
Interest cost	**3**	3
Benefits paid	**(6)**	(6)
Actuarial (gain) loss	**1**	1
Retiree drug subsidy	**1**	1
Balance at end of year	**97**	97
Change in plan assets		
Fair value of plan assets at beginning of year	**23**	23
Actual return (loss) on plan assets	**3**	1
Employer contributions	**4**	4
Benefits paid	**(5)**	(5)
Fair value of plan assets at end of year	**25**	23
Accrued liability	**$ (72)**	$ (74)

Amounts recognized in the balance sheets at December 31, 2017 and 2016 related to the Company's other postretirement benefit plans consist of the following:

	2017	2016
	(in millions)	
Other regulatory assets, deferred	**$ 18**	$ 21
Other regulatory liabilities, deferred	**(1)**	(2)
Employee benefit obligations	**(72)**	(74)

Approximately $17 million and $19 million was included in net regulatory assets at December 31, 2017 and 2016, respectively, related to the net loss for the other postretirement benefit plans that had not yet been recognized in net periodic other postretirement benefit cost. The estimated amortization of such amounts for 2018 is $1 million.

The changes in the balance of net regulatory assets (liabilities) related to the other postretirement benefit plans for the plan years ended December 31, 2017 and 2016 are presented in the following table:

	2017	2016
	(in millions)	
Net regulatory assets (liabilities):		
Beginning balance	**$ 19**	$ 18
Net (gain) loss	**(1)**	2
Reclassification adjustments:		
Amortization of net gain (loss)	**(1)**	(1)
Total reclassification adjustments	**(1)**	(1)
Total change	**(2)**	1
Ending balance	**$ 17**	$ 19

Components of the other postretirement benefit plans' net periodic cost were as follows:

	2017	2016	2015
		(in millions)	
Service cost	**$ 1**	$ 1	$ 1
Interest cost	**3**	3	4
Expected return on plan assets	**(1)**	(1)	(2)
Net amortization	**1**	1	1
Net periodic postretirement benefit cost	**$ 4**	$ 4	$ 4

Future benefit payments, including prescription drug benefits, reflect expected future service and are estimated based on assumptions used to measure the APBO for the other postretirement benefit plans. Estimated benefit payments are reduced by drug subsidy receipts expected as a result of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 as follows:

	Benefit Payments	**Subsidy Receipts**	**Total**
		(in millions)	
2018	$ 6	$ —	$ 6
2019	6	—	6
2020	6	(1)	5
2021	7	(1)	6
2022	7	(1)	6
2023 to 2027	34	(2)	32

Benefit Plan Assets

Pension plan and other postretirement benefit plan assets are managed and invested in accordance with all applicable requirements, including ERISA and the Internal Revenue Code of 1986, as amended (Internal Revenue Code). The Company's investment policies for both the pension plan and the other postretirement benefit plans cover a diversified mix of assets, including equity and fixed income securities, real estate, and private equity. Derivative instruments are used primarily to gain efficient exposure to the various asset classes and as hedging tools. The Company minimizes the risk of large losses primarily through diversification but also monitors and manages other aspects of risk.

The composition of the Company's pension plan and other postretirement benefit plan assets as of December 31, 2017 and 2016, along with the targeted mix of assets for each plan, is presented below:

	Target	**2017**	2016
Pension plan assets:			
Domestic equity	26%	**31%**	29%
International equity	25	**25**	22
Fixed income	23	**24**	29
Special situations	3	**1**	2
Real estate investments	14	**13**	13
Private equity	9	**6**	5
Total	100%	**100%**	100%
Other postretirement benefit plan assets:			
Domestic equity	21%	**25%**	23%
International equity	21	**20**	18
Domestic fixed income	37	**38**	43
Special situations	2	**1**	2
Real estate investments	12	**11**	10
Private equity	7	**5**	4
Total	100%	**100%**	100%

The investment strategy for plan assets related to the Company's qualified pension plan is to be broadly diversified across major asset classes. The asset allocation is established after consideration of various factors that affect the assets and liabilities of the pension plan including, but not limited to, historical and expected returns and interest rates, volatility, correlations of asset classes, the current level of assets and liabilities, and the assumed growth in assets and liabilities. Because a significant portion of the liability of the pension plan is long-term in nature, the assets are invested consistent with long-term investment expectations for return and risk. To manage the actual asset class exposures relative to the target asset allocation, the Company employs a formal rebalancing program. As additional risk management, external investment managers and service providers are subject to written guidelines to ensure appropriate and prudent investment practices. Management believes the portfolio is well-diversified with no significant concentrations of risk.

Investment Strategies

Detailed below is a description of the investment strategies for each major asset category for the pension and other postretirement benefit plans disclosed above:

- ***Domestic equity.*** A mix of large and small capitalization stocks with generally an equal distribution of value and growth attributes, managed both actively and through passive index approaches.
- ***International equity.*** A mix of growth stocks and value stocks with both developed and emerging market exposure, managed both actively and through passive index approaches.
- ***Fixed income.*** A mix of domestic and international bonds.
- ***Special situations.*** Investments in opportunistic strategies with the objective of diversifying and enhancing returns and exploiting short-term inefficiencies as well as investments in promising new strategies of a longer-term nature.
- ***Real estate investments.*** Investments in traditional private market, equity-oriented investments in real properties (indirectly through pooled funds or partnerships) and in publicly traded real estate securities.
- ***Private equity.*** Investments in private partnerships that invest in private or public securities typically through privately-negotiated and/or structured transactions, including leveraged buyouts, venture capital, and distressed debt.

Benefit Plan Asset Fair Values

Following are the fair value measurements for the pension plan and the other postretirement benefit plan assets as of December 31, 2017 and 2016. The fair values presented are prepared in accordance with GAAP. For purposes of determining the fair value of the pension plan and other postretirement benefit plan assets and the appropriate level designation, management relies on information provided by the plan's trustee. This information is reviewed and evaluated by management with changes made to the trustee information as appropriate.

Valuation methods of the primary fair value measurements disclosed in the following tables are as follows:

- ***Domestic and international equity.*** Investments in equity securities such as common stocks, American depositary receipts, and real estate investment trusts that trade on a public exchange are classified as Level 1 investments and are valued at the closing price in the active market. Equity investments with unpublished prices (i.e. pooled funds) are valued as Level 2, when the underlying holdings used to value the investment are comprised of Level 1 or Level 2 equity securities.
- ***Fixed income.*** Investments in fixed income securities are generally classified as Level 2 investments and are valued based on prices reported in the market place. Additionally, the value of fixed income securities takes into consideration certain items such as broker quotes, spreads, yield curves, interest rates, and discount rates that apply to the term of a specific instrument.
- ***Real estate investments, private equity, and special situations investments.*** Investments in real estate, private equity, and special situations are generally classified as Net Asset Value as a Practical Expedient, since the underlying assets typically do not have publicly available observable inputs. The fund manager values the assets using various inputs and techniques depending on the nature of the underlying investments. Techniques may include purchase multiples for comparable transactions, comparable public company trading multiples, discounted cash flow analysis, prevailing market capitalization rates, recent sales of comparable investments, and independent third-party appraisals. The fair value of partnerships is determined by aggregating the value of the underlying assets less liabilities.

The fair values of pension plan assets as of December 31, 2017 and 2016 are presented below. These fair value measurements exclude cash, receivables related to investment income, pending investments sales, and payables related to pending investment purchases.

	Fair Value Measurements Using				
As of December 31, 2017:	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Net Asset Value as a Practical Expedient (NAV)**	**Total**
			(in millions)		
Assets:					
Domestic equity(*)	$ 113	$ 55	$ —	$ —	$ 168
International equity(*)	73	66	—	—	139
Fixed income:					
U.S. Treasury, government, and agency bonds	—	40	—	—	40
Corporate bonds	—	56	—	—	56
Pooled funds	—	31	—	—	31
Cash equivalents and other	10	1	—	—	11
Real estate investments	22	—	—	56	78
Special situations	—	—	—	9	9
Private equity	—	—	—	32	32
Total	$ 218	$ 249	$ —	$ 97	$ 564

(*) Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds.

	Fair Value Measurements Using				
As of December 31, 2016:	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Net Asset Value as a Practical Expedient (NAV)**	**Total**
			(in millions)		
Assets:					
Domestic equity(*)	$ 95	$ 44	$ —	$ —	$ 139
International equity(*)	58	51	—	—	109
Fixed income:					
U.S. Treasury, government, and agency bonds	—	28	—	—	28
Mortgage- and asset-backed securities	—	1	—	—	1
Corporate bonds	—	46	—	—	46
Pooled funds	—	25	—	—	25
Cash equivalents and other	47	—	—	—	47
Real estate investments	15	—	—	54	69
Special situations	—	—	—	8	8
Private equity	—	—	—	26	26
Total	$ 215	$ 195	$ —	$ 88	$ 498

(*) Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds.

The fair values of other postretirement benefit plan assets as of December 31, 2017 and 2016 are presented below. These fair value measurements exclude cash, receivables related to investment income, pending investments sales, and payables related to pending investment purchases.

	Fair Value Measurements Using				
As of December 31, 2017:	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Net Asset Value as a Practical Expedient (NAV)**	**Total**
			(in millions)		
Assets:					
Domestic equity(*)	$ 4	$ 2	$ —	$ —	$ 6
International equity(*)	3	2	—	—	5
Fixed income:					
U.S. Treasury, government, and agency bonds	—	5	—	—	5
Corporate bonds	—	2	—	—	2
Pooled funds	—	1	—	—	1
Cash equivalents and other	1	—	—	—	1
Real estate investments	1	—	—	2	3
Private equity	—	—	—	1	1
Total	$ 9	$ 12	$ —	$ 3	$ 24

(*) Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds.

	Fair Value Measurements Using				
As of December 31, 2016:	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Net Asset Value as a Practical Expedient (NAV)**	**Total**
			(in millions)		
Assets:					
Domestic equity(*)	$ 4	$ 2	$ —	$ —	$ 6
International equity(*)	2	2	—	—	4
Fixed income:					
U.S. Treasury, government, and agency bonds	—	5	—	—	5
Corporate bonds	—	2	—	—	2
Pooled funds	—	1	—	—	1
Cash equivalents and other	2	—	—	—	2
Real estate investments	1	—	—	2	3
Private equity	—	—	—	1	1
Total	$ 9	$ 12	$ —	$ 3	$ 24

(*) Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds.

Employee Savings Plan

The Company also sponsors a 401(k) defined contribution plan covering substantially all employees. The Company matches a portion of the first 6% of employee base salary contributions. The maximum Company match is 5.1% of an employee's base salary. Total matching contributions made to the plan for 2017, 2016, and 2015 were $5 million each year.

3. CONTINGENCIES AND REGULATORY MATTERS

General Litigation Matters

The Company is subject to certain claims and legal actions arising in the ordinary course of business. In addition, the Company's business activities are subject to extensive governmental regulation related to public health and the environment, such as regulation of air emissions and water discharges. Litigation over environmental issues and claims of various types, including property damage, personal injury, common law nuisance, and citizen enforcement of environmental requirements such as standards for air, water, land, and protection of other natural resources, has occurred throughout the U.S. This litigation has included claims for damages alleged to have been caused by CO_2 and other emissions, CCR, and alleged exposure to hazardous materials, and/or requests for injunctive relief in connection with such matters. The ultimate outcome of such pending or potential litigation against the Company cannot be predicted at this time; however, for current proceedings not specifically reported herein, management does not anticipate that the ultimate liabilities, if any, arising from such current proceedings would have a material effect on the Company's financial statements.

Environmental Matters

Environmental Remediation

The Company must comply with environmental laws and regulations governing the handling and disposal of waste and releases of hazardous substances. Under these various laws and regulations, the Company may also incur substantial costs to clean up affected sites. The Company has authority from the Mississippi PSC to recover approved environmental compliance costs through established regulatory mechanisms. The Company recognizes a liability for environmental remediation costs only when it determines a loss is probable and reasonably estimable.

FERC Matters

Municipal and Rural Associations Tariff

The Company provides wholesale electric service to Cooperative Energy, East Mississippi Electric Power Association, and the City of Collins, all located in southeastern Mississippi, under a long-term cost-based, FERC regulated MRA tariff.

In March 2016, the Company reached a settlement agreement with its wholesale customers, which was subsequently approved by the FERC, for an increase in wholesale base revenues under the MRA cost-based electric tariff, primarily as a result of placing scrubbers for Plant Daniel Units 1 and 2 in service in 2015. The settlement agreement became effective for services rendered beginning May 1, 2016, resulting in an estimated annual revenue increase of $7 million under the MRA cost-based electric tariff. Additionally, under the settlement agreement, the tariff customers agreed to similar regulatory treatment for MRA tariff ratemaking as the treatment approved for retail ratemaking through an order issued by the Mississippi PSC in December 2015 (In-Service Asset Rate Order). This regulatory treatment primarily includes (i) recovery of the operational Kemper County energy facility assets providing service to customers and other related costs, (ii) amortization of the Kemper County energy facility-related regulatory assets included in rates under the settlement agreement over the 36 months ending April 30, 2019, (iii) Kemper County energy facility-related expenses included in rates under the settlement agreement no longer being deferred and charged to expense, and (iv) removing all of the Kemper County energy facility CWIP from rate base with a corresponding increase in accrual of AFUDC. The additional resulting AFUDC totaled approximately $22 million through the suspension of Kemper IGCC start-up activities and has been recorded as a charge to income.

On September 18, 2017, the Company and Cooperative Energy executed a Shared Service Agreement (SSA), as part of the MRA tariff, under which the Company and Cooperative Energy will share in providing electricity to all Cooperative Energy delivery points, in lieu of the current arrangement under which each delivery point is specifically assigned to either entity. The SSA accepted by the FERC on October 31, 2017 became effective on January 1, 2018 and may be cancelled by Cooperative Energy with 10 years notice after December 31, 2020. The SSA provides Cooperative Energy the option to decrease its use of the Company's generation services under the MRA tariff, subject to annual and cumulative caps and a one-year notice requirement. In the event Cooperative Energy elects to reduce these services, the related reduction in the Company's revenues is not expected to be significant through 2020.

Fuel Cost Recovery

The Company has a wholesale MRA and a Market Based (MB) fuel cost recovery factor. At December 31, 2017, over-recovered wholesale MRA fuel costs were immaterial and at December 31, 2016 were approximately $13 million, and is included in over-recovered regulatory clause liabilities, current in the balance sheet. Effective January 1, 2018, the wholesale MRA fuel rate increased $11 million annually.

The Company's operating revenues are adjusted for differences in actual recoverable fuel cost and amounts billed in accordance with the currently approved cost recovery rate. Accordingly, changes in the billing factor should have no significant effect on the Company's revenues or net income, but will affect cash flow.

Market-Based Rate Authority

The Company has authority from the FERC to sell electricity at market-based rates. Since 2008, that authority, for certain balancing authority areas, has been conditioned on compliance with the requirements of an energy auction, which the FERC found to be tailored mitigation that addresses potential market power concerns. In accordance with FERC regulations governing such authority, the traditional electric operating companies (including the Company) and Southern Power filed a triennial market power analysis in 2014, which included continued reliance on the energy auction as tailored mitigation. In 2015, the FERC issued an order finding that the traditional electric operating companies' (including the Company's) and Southern Power's existing tailored mitigation may not effectively mitigate the potential to exert market power in certain areas served by the traditional electric operating companies and in some adjacent areas. The FERC directed the traditional electric operating companies (including the Company) and Southern Power to show why market-based rate authority should not be revoked in these areas or to provide a mitigation plan to further address market power concerns. The traditional electric operating companies (including the Company) and Southern Power filed a request for rehearing and filed their response with the FERC in 2015.

In December 2016, the traditional electric operating companies (including the Company) and Southern Power filed an amendment to their market-based rate tariff that proposed certain changes to the energy auction, as well as several non-tariff changes. On February 2, 2017, the FERC issued an order accepting all such changes subject to an additional condition of cost-based price caps for certain sales outside of the energy auction, finding that all of these changes would provide adequate alternative mitigation for the traditional electric operating companies' (including the Company's) and Southern Power's potential to exert market power in certain areas served by the traditional electric operating companies (including the Company) and in some adjacent areas. On May 17, 2017, the FERC accepted the traditional electric operating companies' (including the Company's) and Southern Power's compliance filing accepting the terms of the order. While the FERC's February 2, 2017 order references the market power proceeding discussed above, it remains a separate, ongoing matter.

On October 25, 2017, the FERC issued an order in response to the traditional electric operating companies' (including the Company's) and Southern Power's June 29, 2017 triennial updated market power analysis. The FERC directed the traditional electric operating companies (including the Company) and Southern Power to show cause within 60 days why market-based rate authority should not be revoked in certain areas adjacent to the area presently under mitigation in accordance with the February 2, 2017 order or to provide a mitigation plan to further address market power concerns. On November 10, 2017, the traditional electric operating companies (including the Company) and Southern Power responded to the FERC and proposed to resolve matters by applying the alternative mitigation authorized by the February 2, 2017 order to the adjacent areas made the subject of the October 25, 2017 order.

The ultimate outcome of these matters cannot be determined at this time.

Cooperative Energy Power Supply Agreement

In 2008, the Company entered into a 10-year Power Supply Agreement (PSA) with Cooperative Energy for approximately 152 MWs, which became effective in 2011. Following certain plant retirements, the PSA capacity was reduced to 86 MWs. On February 5, 2018, the Company and Cooperative Energy executed an amendment to extend the PSA through March 31, 2021, effective April 1, 2018, with increased total capacity of 286 MWs.

Cooperative Energy also has a 10-year Network Integration Transmission Service Agreement (NITSA) with SCS for transmission service to certain delivery points on the Company's transmission system that became effective in 2011. As a result of the PSA amendments, Cooperative Energy and SCS amended the terms of the NITSA on January 12, 2018 to provide for the purchase of incremental transmission capacity for service beginning April 1, 2018 through March 31, 2021. This NITSA amendment remains subject to acceptance by the FERC. The ultimate outcome of these matters cannot be determined at this time.

Retail Regulatory Matters

General

In 2012, the Mississippi PSC issued an order for the purpose of investigating and reviewing, for informational purposes only, the ROE formulas used by the Company and all other regulated electric utilities in Mississippi. In 2013, the MPUS filed with the Mississippi PSC its report on the ROE formulas used by the Company and all other regulated electric utilities in Mississippi.

In 2014, the Mississippi PSC issued an order for the purpose of investigating and reviewing the adoption of a uniform formula rate plan for the Company and other regulated electric utilities in Mississippi.

On January 26, 2018, the Mississippi PSC issued an order directing utilities to file within 30 days information regarding the impact on rates resulting from Tax Reform Legislation. The Company's Kemper County energy facility rates, approved on February 6, 2018, include the effects of Tax Reform Legislation. The Company's 2018 ECO, revised 2018 PEP, and 2018 SRR rate filings, all submitted in February 2018, include the effects of Tax Reform Legislation and are subject to approval by the Mississippi PSC.

The ultimate outcome of these matters cannot be determined at this time.

Performance Evaluation Plan

The Company's retail base rates are set under the PEP, a rate plan approved by the Mississippi PSC. Two filings are made for each calendar year: the PEP projected filing, which is typically filed prior to the beginning of the year based on a projected revenue requirement, and the PEP lookback filing, which is filed after the end of the year and allows for review of the actual revenue requirement compared to the projected filing.

In 2011, the Company submitted its annual PEP lookback filing for 2010, which recommended no surcharge or refund. Later in 2011, the MPUS disputed certain items in the 2010 PEP lookback filing. In 2012, the Mississippi PSC issued an order canceling the Company's PEP lookback filing for 2011. In 2013, the MPUS contested the Company's PEP lookback filing for 2012, which indicated a refund due to customers of $5 million. Unresolved matters related to the 2010 PEP lookback filing, which remain under review, also impact the 2012 PEP lookback filing.

In 2013, the Mississippi PSC approved the projected PEP filing for 2013, which resulted in a rate increase of 1.9%, or $15 million, annually, effective March 19, 2013. The Company may be entitled to $3 million in additional revenues related to 2013 as a result of the late implementation of the 2013 PEP rate increase.

In 2014, 2015, 2016, and 2017, the Company submitted its annual PEP lookback filings for the prior years, which for 2013 and 2014 each indicated no surcharge or refund and for each of 2015 and 2016 indicated a $5 million surcharge. Additionally, in July 2016, in November 2016, and on November 15, 2017, the Company submitted its annual projected PEP filings for 2016, 2017, and 2018, respectively, which for 2016 and 2017 indicated no change in rates and for 2018 indicated a rate increase of 4%, or $38 million in annual revenues. The Mississippi PSC suspended each of these filings to allow more time for review.

On February 7, 2018, the Company revised its annual projected PEP filing for 2018 to reflect the impacts of Tax Reform Legislation. The revised filing requests an increase of $26 million in annual revenues, based on a performance adjusted ROE of 9.33% and an increased equity ratio of 55%. See Note 5 for additional information.

The ultimate outcome of these matters cannot be determined at this time.

Energy Efficiency

In 2013, the Mississippi PSC approved an energy efficiency and conservation rule requiring electric and gas utilities in Mississippi serving more than 25,000 customers to implement energy efficiency programs and standards. Quick Start Plans, which include a portfolio of energy efficiency programs that are intended to provide benefits to a majority of customers, were extended by an order issued by the Mississippi PSC in July 2016, until the time the Mississippi PSC approves a comprehensive portfolio plan program. The ultimate outcome of this matter cannot be determined at this time.

On July 6, 2017, the Mississippi PSC issued an order approving the Company's Energy Efficiency Cost Rider 2017 compliance filing, which increased annual retail revenues by approximately $2 million effective with the first billing cycle for August 2017.

On November 30, 2017, the Company submitted its Energy Efficiency Cost Rider 2018 compliance filing which included a small decrease in annual retail revenues. The ultimate outcome of this matter cannot be determined at this time.

Environmental Compliance Overview Plan

In 2012, the Mississippi PSC approved the Company's request for a CPCN to construct scrubbers on Plant Daniel Units 1 and 2, which were placed in service in 2015. These units are jointly owned by the Company and Gulf Power, with 50% ownership each. In 2014, the Company entered into a settlement agreement with the Sierra Club under which, among other things, the Company agreed to retire, repower with natural gas, or convert to an alternative non-fossil fuel source Plant Sweatt Units 1 and 2 (80 MWs) no later than December 2018 (and the units were retired in July 2016). The Company also agreed that it would cease burning coal and other solid fuel at Plant Watson Units 4 and 5 (750 MWs) and begin operating those units solely on natural gas no later than April 2015 (which occurred in April 2015) and cease burning coal and other solid fuel at Plant Greene County Units 1 and 2 (200 MWs) no later than April 2016 (which occurred in February and March 2016, respectively) and begin operating those units solely on natural gas (which occurred in June and July 2016, respectively).

In accordance with a 2011 accounting order from the Mississippi PSC, the Company has the authority to defer in a regulatory asset for future recovery all plant retirement- or partial retirement-related costs resulting from environmental regulations. The Mississippi PSC approved $41 million and $17 million of costs that were reclassified to regulatory assets associated with Plant Watson and Plant Greene County, respectively, for amortization over five-year periods that began in July 2016 and July 2017, respectively. As a result, these decisions are not expected to have a material impact on the Company's financial statements.

In August 2016, the Mississippi PSC approved the Company's revised ECO plan filing for 2016, which requested the maximum 2% annual increase in revenues, or approximately $18 million, primarily related to the Plant Daniel Units 1 and 2 scrubbers placed in service in 2015. The revised rates became effective with the first billing cycle for September 2016. Approximately $22 million of related revenue requirements in excess of the 2% maximum was deferred for inclusion in the 2017 filing, along with related carrying costs.

On May 4, 2017, the Mississippi PSC approved the Company's ECO plan filing for 2017, which requested the maximum 2% annual increase in revenues, or approximately $18 million, primarily related to the carryforward from the prior year. The rates became effective with the first billing cycle for June 2017. Approximately $26 million of related revenue requirements in excess of the 2% maximum was deferred for inclusion in the 2018 filing, along with related carrying costs.

On February 14, 2018, the Company submitted its ECO plan filing for 2018, including the effects of Tax Reform Legislation, which requested the maximum 2% annual increase in revenues, or approximately $17 million, primarily related to the carryforward from the prior year. Approximately $13 million of related revenue requirements in excess of the 2% maximum, along with related carrying costs, remains deferred for inclusion in the 2019 filing. The ultimate outcome of this matter cannot be determined at this time.

Fuel Cost Recovery

The Company establishes, annually, a retail fuel cost recovery factor that is approved by the Mississippi PSC. The Company is required to file for an adjustment to the retail fuel cost recovery factor annually. On January 12, 2017, the Mississippi PSC approved the 2017 retail fuel cost recovery factor, effective February 2017 through January 2018, which resulted in an annual revenue increase of approximately $55 million. On November 15, 2017, the Company filed its annual rate adjustment under the retail fuel cost recovery clause, requesting an additional increase of $39 million annually, which the Mississippi PSC approved on January 16, 2018 effective February 2018 through January 2019. At December 31, 2017, the amount of under-recovered retail fuel costs included in the balance sheet in customer accounts receivable was approximately $6 million compared to $37 million over recovered at December 31, 2016.

The Company's operating revenues are adjusted for differences in actual recoverable fuel cost and amounts billed in accordance with the currently approved cost recovery rate. Accordingly, changes in the billing factor should have no significant effect on the Company's revenues or net income, but will affect cash flow.

Ad Valorem Tax Adjustment

The Company establishes, annually, an ad valorem tax adjustment factor that is approved by the Mississippi PSC to collect the ad valorem taxes paid by the Company. On July 6, 2017, the Mississippi PSC approved the Company's annual ad valorem tax adjustment factor filing for 2017, which included an annual rate increase of 0.85%, or $8 million in annual retail revenues, primarily due to increased assessments.

System Restoration Rider

In February 2016, the Company submitted its 2016 SRR rate filing which proposed no changes to either the SRR rate or the annual property damage reserve accrual of $3 million annually. On February 3, 2017, the Company submitted its 2017 SRR rate filing, which proposed an increase in the property damage reserve accrual of $1 million. These filings were suspended by the Mississippi PSC for review.

On January 21, 2017, a tornado caused extensive damage to the Company's transmission and distribution infrastructure. Storm damage repairs were approximately $9 million. A portion of these costs was charged to the retail property damage reserve and was addressed in the 2018 SRR rate filing.

On February 1, 2018, the Company submitted its 2018 SRR rate filing, including the effects of Tax Reform Legislation, which proposed that the SRR rate remain at zero and the annual accrual for the property damage reserve be reduced to $2 million in 2018.

The ultimate outcome of these matters cannot be determined at this time. See Note 1 under "Provision for Property Damage" for additional information.

Storm Damage Cost Recovery

In connection with the damage associated with Hurricane Katrina, the Mississippi PSC authorized the issuance of system restoration bonds in 2006. In accordance with a Mississippi PSC order on January 24, 2017, the Company eliminated the applicable Storm Restoration Charge because the bond sinking fund managed by the Mississippi State Bond Commission is substantially funded.

Kemper County Energy Facility

Overview

The Kemper County energy facility was designed to utilize IGCC technology with an expected output capacity of 582 MWs and to be fueled by locally mined lignite (an abundant, lower heating value coal) from a mine owned by the Company and situated adjacent to the Kemper County energy facility. The mine, operated by North American Coal Corporation, started commercial operation in 2013. In connection with the Kemper County energy facility construction, the Company constructed approximately 61 miles of CO_2 pipeline infrastructure for the transport of captured CO_2 for use in enhanced oil recovery.

Schedule and Cost Estimate

In 2012, the Mississippi PSC issued the 2012 MPSC CPCN Order, confirming the CPCN originally approved by the Mississippi PSC in 2010 authorizing the acquisition, construction, and operation of the Kemper County energy facility. The certificated cost estimate of the Kemper County energy facility included in the 2012 MPSC CPCN Order was $2.4 billion, net of approximately $0.57 billion for the cost of the lignite mine and equipment, the cost of the CO_2 pipeline facilities, AFUDC, and certain general exceptions (Cost Cap Exceptions). The 2012 MPSC CPCN Order approved a construction cost cap of up to $2.88 billion, with recovery of prudently-incurred costs subject to approval by the Mississippi PSC. The Kemper County energy facility was originally projected to be placed in service in May 2014. The Company placed the combined cycle and the associated common facilities portion of the Kemper County energy facility in service in August 2014.

The initial production of syngas began on July 14, 2016 for gasifier "B" and on September 13, 2016 for gasifier "A." The Company achieved integrated operation of both gasifiers on January 29, 2017, including the production of electricity from syngas in both combustion turbines. During testing, the plant produced and captured CO_2, and produced sulfuric acid and ammonia, each of acceptable quality under the related off-take agreements. However, the Company experienced numerous challenges during the extended start-up process to achieve integrated operation of the gasifiers on a sustained basis. In May 2017, after achieving these milestones, the Company determined that a critical system component, the syngas coolers, would need replacement sooner than originally planned, which would require significant lead time and significant cost. In addition, the long-term natural gas price forecast had decreased significantly and the estimated cost of operating and maintaining the facility during the first five full years of operations had increased significantly since certification.

On June 21, 2017, the Mississippi PSC stated its intent to issue an order (which occurred on July 6, 2017) directing the Company to pursue a settlement under which the Kemper County energy facility would be operated as a natural gas plant, rather than an IGCC plant, and address all issues associated with the Kemper County energy facility (Kemper Settlement Order). The Kemper Settlement Order established a new docket for the purposes of pursuing a global settlement of the related costs (Kemper Settlement Docket). On June 28, 2017, the Company notified the Mississippi PSC that it would begin a process to suspend operations and start-up activities on the gasifier portion of the Kemper County energy facility, given the uncertainty as to its future. On February 6, 2018, the Mississippi PSC voted to approve a settlement agreement related to cost recovery for the Kemper County energy facility among the Company, the MPUS, and certain intervenors (Kemper Settlement Agreement).

At the time of project suspension in June 2017, the total cost estimate for the Kemper County energy facility was approximately $7.38 billion, including approximately $5.95 billion of costs subject to the construction cost cap, and was net of the $137 million in Additional DOE Grants. In the aggregate, the Company had recorded charges to income of $3.07 billion ($1.89 billion after tax) as a result of changes in the cost estimate above the cost cap for the Kemper IGCC through May 31, 2017.

Given the Mississippi PSC's stated intent regarding no further rate increase for the Kemper County energy facility and the subsequent suspension, cost recovery of the gasifier portions became no longer probable; therefore, the Company recorded an additional charge to income in June 2017 of $2.8 billion ($2.0 billion after tax), which included estimated costs associated with the gasifier portions of the plant and lignite mine. During the third and fourth quarters of 2017, the Company recorded charges to income of $242 million ($206 million after tax), including $164 million for ongoing project costs, estimated mine and gasifier-related costs, and certain termination costs during the suspension period prior to conclusion of the Kemper Settlement Docket, as well as the charge associated with the Kemper Settlement Agreement discussed below. Additional pre-tax cancellation costs, including mine and plant closure and contract termination costs, currently estimated at approximately $50 million to $100 million (excluding salvage), are expected to be incurred in 2018. The Company has begun efforts to dispose of or abandon the mine and gasifier-related assets.

Rate Recovery

Kemper Settlement Agreement

On February 6, 2018, the Mississippi PSC voted to approve the Kemper Settlement Agreement. The Kemper Settlement Agreement provides for an annual revenue requirement of approximately $99.3 million for costs related to the Kemper County energy facility, which includes the impact of Tax Reform Legislation. The revenue requirement is based on (i) a fixed ROE for 2018 of 8.6% excluding any performance adjustment, (ii) a ROE for 2019 calculated in accordance with PEP, excluding the performance adjustment, (iii) for future years, a performance-based ROE calculated pursuant to PEP, and (iv) amortization periods for the related regulatory assets and liabilities of eight years and six years, respectively. The revenue requirement also reflects a disallowance related to a portion of the Company's investment in the Kemper County energy facility requested for inclusion in rate base, which was recorded in the fourth quarter 2017 as an additional charge to income of approximately $78 million ($85 million net of accumulated depreciation of $7 million) pre-tax ($48 million after tax).

Under the Kemper Settlement Agreement, retail customer rates will reflect a reduction of approximately $26.8 million annually and include no recovery for costs associated with the gasifier portion of the Kemper County energy facility in 2018 or at any future date. On February 12, 2018, the Company made the required compliance filing with the Mississippi PSC. The Kemper Settlement Agreement also requires (i) the CPCN for the Kemper County energy facility to be modified to limit it to natural gas combined cycle operation and (ii) the Company to file a reserve margin plan with the Mississippi PSC by August 2018.

As of December 31, 2017, the balances associated with the Kemper County energy facility regulatory assets and liabilities were $114 million and $26 million, respectively.

As a result of the Mississippi PSC order on February 6, 2018, rate recovery for the Kemper County energy facility is resolved, subject to any future legal challenges.

2015 Rate Case

On December 3, 2015, the Mississippi PSC issued the In-Service Asset Rate Order regarding the Kemper County energy facility assets that were commercially operational and currently providing service to customers (the transmission facilities, combined cycle, natural gas pipeline, and water pipeline) and other related costs. The In-Service Asset Rate Order provided for retail rate recovery of an annual revenue requirement of approximately $126 million, based on the Company's actual average capital structure, with a maximum common equity percentage of 49.733%, a 9.225% return on common equity, and actual embedded interest costs. The In-Service Asset Rate Order also included a prudence finding of all costs in the stipulated revenue requirement calculation for the in-service assets.

In connection with the implementation of the In-Service Asset Rate Order and wholesale rates, the Company began expensing certain ongoing project costs and certain retail debt carrying costs that previously were deferred and began amortizing certain regulatory assets associated with assets placed in service and consulting and legal fees over periods ranging from two years to 10 years. On July 6, 2017, the Mississippi PSC issued an order requiring the Company to establish a regulatory liability account to maintain current rates related to the Kemper County energy facility following the July 2017 completion of the amortization period for certain of these regulatory assets. See "FERC Matters" herein for additional information related to the 2016 settlement agreement with wholesale customers.

Lignite Mine and CO_2 Pipeline Facilities

The Company owns the lignite mine and equipment and mineral reserves located around the Kemper County energy facility site. The mine started commercial operation in June 2013.

In 2010, the Company executed a 40-year management fee contract with Liberty Fuels Company, LLC (Liberty Fuels), a wholly-owned subsidiary of The North American Coal Corporation, which developed, constructed, and is responsible for the mining operations through the end of the mine reclamation. As the mining permit holder, Liberty Fuels has a legal obligation to perform mine reclamation and the Company has a contractual obligation to fund all reclamation activities. The Company expects mine reclamation to begin in 2018. In addition to the obligation to fund the reclamation activities, the Company provided working capital support to Liberty Fuels through cash advances for capital purchases, payroll, and other operating expenses. See Note 1 under "Asset Retirement Obligations and Other Costs of Removal" and "Variable Interest Entities" for additional information.

In addition, the Company constructed the CO_2 pipeline for the planned transport of captured CO_2 for use in enhanced oil recovery and entered into an agreement with Denbury Onshore (Denbury) to purchase the captured CO_2. Denbury has the right to terminate the contract at any time because the Company did not place the Kemper IGCC in service by July 1, 2017.

The ultimate outcome of these matters cannot be determined at this time.

Litigation

On April 26, 2016, a complaint against the Company was filed in Harrison County Circuit Court (Circuit Court) by Biloxi Freezing & Processing Inc., Gulfside Casino Partnership, and John Carlton Dean, which was amended and refiled on July 11, 2016 to include, among other things, Southern Company as a defendant. The individual plaintiff alleges that the Company and Southern Company violated the Mississippi Unfair Trade Practices Act. All plaintiffs have alleged that the Company and Southern Company concealed, falsely represented, and failed to fully disclose important facts concerning the cost and schedule of the Kemper County energy facility and that these alleged breaches have unjustly enriched the Company and Southern Company. The plaintiffs seek unspecified actual damages and punitive damages; ask the Circuit Court to appoint a receiver to oversee, operate, manage, and otherwise control all affairs relating to the Kemper County energy facility; ask the Circuit Court to revoke any licenses or certificates authorizing the Company or Southern Company to engage in any business related to the Kemper County energy facility in Mississippi; and seek attorney's fees, costs, and interest. The plaintiffs also seek an injunction to prevent any Kemper County energy facility costs from being charged to customers through electric rates. On June 23, 2017, the Circuit Court ruled in favor of motions by Southern Company and the Company and dismissed the case. On July 7, 2017, the plaintiffs filed notice of an appeal. The Company believes this legal challenge has no merit; however, an adverse outcome in this proceeding could have a material impact on the Company's results of operations, financial condition, and liquidity. The Company intends to vigorously defend itself in this matter and the ultimate outcome of this matter cannot be determined at this time.

On June 9, 2016, Treetop, Greenleaf CO_2 Solutions, LLC (Greenleaf), Tenrgys, LLC, Tellus Energy, LLC, WCOA, LLC, and Tellus Operating Group filed a complaint against the Company, Southern Company, and SCS in the state court in Gwinnett County, Georgia. The complaint related to the cancelled CO_2 contract with Treetop and alleged fraudulent misrepresentation, fraudulent concealment, civil conspiracy, and breach of contract on the part of the Company, Southern Company, and SCS and sought compensatory damages of $100 million, as well as unspecified punitive damages. Southern Company, the Company, and SCS moved to compel arbitration pursuant to the terms of the CO_2 contract, which the court granted on May 4, 2017. On June 28, 2017, Treetop, Greenleaf, Tenrgys, LLC, Tellus Energy, LLC, WCOA, LLC, and Tellus Operating Group filed a claim for arbitration requesting $500 million in damages. On December 28, 2017, the Company reached a settlement agreement with Treetop, Greenleaf, Tenrgys, LLC, Tellus Energy, LLC, WCOA, LLC, and Tellus Operating Group and the arbitration was dismissed.

4. JOINT OWNERSHIP AGREEMENTS

The Company and Alabama Power own, as tenants in common, Units 1 and 2 (total capacity of 500 MWs) at Greene County Steam Plant, which is located in Alabama and operated by Alabama Power. Additionally, the Company and Gulf Power, own as tenants in common, Units 1 and 2 (total capacity of 1,000 MWs) at Plant Daniel, which is located in Mississippi and operated by the Company. At December 31, 2017, the Company's percentage ownership and investment in these jointly-owned facilities in commercial operation were as follows:

Generating Plant	Company Ownership	Plant in Service	Accumulated Depreciation	CWIP
			(in millions)	
Greene County				
Units 1 and 2	40%	$ 164	$ 55	$ 1
Daniel				
Units 1 and 2	50%	$ 713	$ 189	$ 4

The Company's proportionate share of plant operating expenses is included in the statements of operations and the Company is responsible for providing its own financing.

5. INCOME TAXES

On behalf of the Company, Southern Company files a consolidated federal income tax return and various combined and separate state income tax returns. Under a joint consolidated income tax allocation agreement, each Southern Company subsidiary's current and deferred tax expense is computed on a stand-alone basis and no subsidiary is allocated more current expense than would be paid if it filed a separate income tax return. In accordance with IRS regulations, each company is jointly and severally liable for the federal tax liability.

Federal Tax Reform Legislation

Following the enactment of Tax Reform Legislation, the SEC staff issued Staff Accounting Bulletin 118 – "Income Tax Accounting Implications of the Tax Cuts and Jobs Act" (SAB 118), which provides for a measurement period of up to one year from the enactment date to complete accounting under GAAP for the tax effects of the legislation. Due to the complex and comprehensive nature of the enacted tax law changes, and their application under GAAP, the Company considers all amounts recorded in the financial statements as a result of Tax Reform Legislation to be "provisional" as discussed in SAB 118 and subject to revision. The Company is awaiting additional guidance from industry and income tax authorities in order to finalize its accounting. The ultimate impact of Tax Reform Legislation on deferred income tax assets and liabilities and the related regulatory assets and liabilities cannot be determined at this time. See Note 3 under "Regulatory Matters" for additional information.

Current and Deferred Income Taxes

Details of income tax provisions are as follows:

	2017	2016	2015
		(in millions)	
Federal —			
Current	**$ 194**	$ (31)	$ (768)
Deferred	**(753)**	(60)	704
	(559)	(91)	(64)
State —			
Current	**—**	(6)	(81)
Deferred	**27**	(7)	73
	27	(13)	(8)
Total	**$ (532)**	$ (104)	$ (72)

The tax effects of temporary differences between the carrying amounts of assets and liabilities in the financial statements and their respective tax bases, which give rise to deferred tax assets and liabilities, are as follows:

	2017	2016
	(in millions)	
Deferred tax liabilities —		
Accelerated depreciation	**$ 373**	$ 386
Property basis difference	**242**	852
Regulatory assets associated with AROs	**34**	72
Pensions and other benefits	**28**	49
Regulatory assets associated with employee benefit obligations	**45**	70
Regulatory assets associated with the Kemper County energy facility	**31**	82
Regulatory assets associated with Plant Daniel	**9**	13
Rate differential	**—**	141
Federal effect of state deferred taxes	**9**	—
Ad valorem over/under recovery	**11**	14
Regulatory assets for Mercury and Air Toxics Standards compliance	**11**	8
Other	**11**	91
Total	**804**	1,778
Deferred tax assets —		
Fuel clause over recovered	**—**	26
Estimated loss on Kemper IGCC	**722**	484
Pension and other benefits	**62**	96
Federal NOL	**40**	109
Property insurance	**15**	27
Premium on long-term debt	**7**	14
AROs	**34**	72
Property basis difference	**70**	—
Affirmative adjustments	**31**	—
Regulatory liability associated with Tax Reform Legislation (not subject to normalization)	**27**	—
Deferred state tax assets	**133**	113
Deferred federal tax assets	**—**	31
Federal effect of state deferred taxes	**—**	19
Other	**32**	31
Total	**1,173**	1,022
Valuation allowance (net of $35 million in federal benefit)	**122**	—
Accumulated deferred income tax (assets)/liabilities	**(247)**	756

The implementation of Tax Reform Legislation significantly reduced accumulated deferred income taxes, partially offset by bonus depreciation provisions in the Protecting Americans from Tax Hikes Act. Tax Reform Legislation also significantly reduced tax-related regulatory assets and increased tax-related regulatory liabilities.

At December 31, 2017, the tax-related regulatory assets were $36 million. These assets are primarily attributable to tax benefits flowed through to customers in prior years, deferred taxes previously recognized at rates lower than the current enacted tax law, and taxes applicable to capitalized interest.

At December 31, 2017, the tax-related regulatory liabilities were $376 million. These liabilities are primarily attributable to deferred taxes previously recognized at rates higher than the current enacted tax law and unamortized ITCs.

In accordance with regulatory requirements, deferred federal ITCs are amortized over the life of the related property with such amortization normally applied as a credit to reduce depreciation in the statements of operations. Credits for non-Kemper County energy facility related deferred ITCs amortized in this manner amounted to $1 million in each of 2017, 2016, and 2015.

At December 31, 2017, the Company had state of Mississippi NOL carryforwards totaling approximately $2.8 billion, resulting in deferred tax assets of approximately $111 million. The NOLs will expire between 2031 and 2037.

Effective Tax Rate

A reconciliation of the federal statutory income tax rate to the effective income tax rate is as follows:

	2017	2016	2015
Federal statutory rate	**(35.0)%**	(35.0)%	(35.0)%
State income tax, net of federal deduction	**0.6**	(5.7)	(6.3)
Non-deductible book depreciation	**0.1**	0.7	1.3
AFUDC-equity	**—**	(28.5)	(49.6)
Non-deductible equity portion on Kemper IGCC write-off	**5.3**	—	—
Tax Reform Legislation	**11.9**	—	—
Other	**—**	—	(2.9)
Effective income tax rate (benefit rate)	**(17.1)%**	(68.5)%	(92.5)%

The decrease in the Company's 2017 effective tax rate (benefit rate), as compared to 2016, is primarily due to an increase in estimated losses associated with the Kemper IGCC, a decrease in non-taxable AFUDC equity, and a decrease due to the remeasurement of deferred income taxes resulting from Tax Reform Legislation. The decrease in the Company's 2016 effective tax rate (benefit rate), as compared to 2015, is primarily due to an increase in estimated losses associated with the Kemper IGCC and an increase in non-taxable AFUDC equity.

Tax Reform Legislation reduced the corporate income tax rate from 35% to 21%. As a result of implementation, the Company restated future tax benefits/deductions recorded as deferred tax assets/liabilities to reflect the new rate. The implementation resulted in a $372 million increase in tax expense and a $375 million increase in regulatory liabilities.

In March 2016, the FASB issued ASU 2016-09, which changed the accounting for income taxes for share-based payment award transactions. Entities are required to recognize all excess tax benefits and deficiencies related to the exercise or vesting of stock compensation as income tax expense or benefit in the income statement. The adoption of ASU 2016-09 did not have a material impact on the Company's overall effective tax rate. See Note 1 under "Recently Issued Accounting Standards" for additional information.

Unrecognized Tax Benefits

Changes during the year in unrecognized tax benefits were as follows:

	2017	2016	2015
		(in millions)	
Unrecognized tax benefits at beginning of year	**$ 465**	$ 421	$ 165
Tax positions increase from current periods	**—**	26	32
Tax positions increase from prior periods	**2**	18	224
Tax positions decrease from prior periods	**(177)**	—	—
Reductions due to settlements	**(290)**	—	—
Balance at end of year	**$ —**	$ 465	$ 421

The tax positions increases from current periods and prior periods for 2017, 2016 and 2015 relate to state tax benefits, deductions for R&E expenditures, and charitable contribution carryforwards that were impacted as a result of the settlement of R&E expenditures associated with the Kemper County energy facility, as well as federal income tax benefits from deferred ITCs. The tax positions decrease from prior periods and reductions due to settlements for 2017 relate primarily to the settlement of R&E expenditures associated with the Kemper County energy facility. See "Section 174 Research and Experimental Deduction" herein for additional information. These amounts are presented on a gross basis without considering the related federal or state income tax impact.

The impact on the Company's effective tax rate, if recognized, is as follows:

	2017	2016	2015
		(in millions)	
Tax positions impacting the effective tax rate	**$ —**	$ 1	$ (2)
Tax positions not impacting the effective tax rate	**—**	464	423
Balance of unrecognized tax benefits	**$ —**	$ 465	$ 421

The tax positions not impacting the effective tax rate primarily relate to state tax benefits and charitable contribution carryforwards that were impacted as a result of the settlement of R&E expenditures associated with the Kemper County energy facility. See "Section 174 Research and Experimental Deduction" herein for additional information.

Accrued interest for unrecognized tax benefits was as follows:

	2017	2016	2015
		(in millions)	
Interest accrued at beginning of year	**$ 28**	$ 13	$ 3
Interest accrued during the year	**(28)**	15	10
Balance at end of year	**$ —**	$ 28	$ 13

The Company classifies interest on tax uncertainties as interest expense. The Company did not accrue any penalties on uncertain tax positions.

It is reasonably possible that the amount of the unrecognized tax benefits could change within 12 months. The settlement of federal and state audits could impact the balances significantly. At this time, an estimate of the range of reasonably possible outcomes cannot be determined.

The IRS has finalized its audits of Southern Company's consolidated federal income tax returns through 2016. Southern Company is a participant in the Compliance Assurance Process of the IRS. The audits for the Company's state income tax returns have either been concluded, or the statute of limitations has expired, for years prior to 2011.

Section 174 Research and Experimental Deduction

Southern Company, on behalf of the Company, has reflected deductions for R&E expenditures related to the Kemper County energy facility in its federal income tax calculations since 2013 and filed amended federal income tax returns for 2008 through 2013 to also include such deductions. In December 2016, Southern Company and the IRS reached a proposed settlement, which was approved on September 8, 2017 by the U.S. Congress Joint Committee on Taxation (JCT), resolving a methodology for these deductions. As a result of the JCT approval, Southern Company recognized $176 million of previously unrecognized tax benefits and reversed $36 million of associated accrued interest.

6. FINANCING

Going Concern

The Company's financial statement presentation contemplates continuation of the Company as a going concern as a result of Southern Company's anticipated ongoing financial support of the Company. Specifically, the Company has been informed by Southern Company that in the event sufficient funds are not available from external sources, Southern Company intends to provide the Company with loans and/or equity to fund the remaining indebtedness to mature and other cash needs over the next 12 months. As of December 31, 2017, the Company's current liabilities exceeded current assets by approximately $911 million primarily due to a $900 million unsecured term loan that matures on March 31, 2018. The Company expects to refinance the unsecured term loan with external security issuances and/or borrowings from financial institutions or Southern Company. To fund the Company's capital needs over the next 12 months, the Company intends to utilize operating cash flows, external security issuances, lines of credit, bank term loans, equity contributions from Southern Company and, to the extent necessary, loans from Southern Company.

Securities Due Within One Year

A summary of scheduled maturities and redemptions of securities due within one year at December 31, 2017 and 2016 was as follows:

	2017	2016
	(in millions)	
Parent company loans	**$ —**	$ 551
Senior notes	**—**	35
Bank term loans	**900**	—
Revenue bonds(*)	**90**	40
Capitalized leases	**—**	3
Unamortized debt issuance expense	**(1)**	—
Outstanding at December 31	**$ 989**	$ 629

(*) Includes $50 million in revenue bonds classified as short term at December 31, 2017 that were remarketed in an index rate mode subsequent to December 31, 2017. Also includes $40 million in pollution control revenue bonds classified as short term since they are variable rate demand obligations supported by short-term credit facilities; however, the final maturity dates range from 2020 to 2028.

Maturities through 2022 applicable to total long-term debt are as follows: $900 million in 2018, $125 million in 2019, and $270 million in 2021. For long-term debt, other than revenue bonds, there are no scheduled maturities for 2020 and 2022.

Parent Company Loans and Equity Contributions

At December 31, 2016, the Company had $551 million of outstanding promissory notes to Southern Company.

In February 2017, the Company amended $551 million in promissory notes to Southern Company extending the maturity dates of the notes from December 1, 2017 to July 31, 2018. In the second quarter 2017, the Company borrowed an additional $40 million under a promissory note issued to Southern Company.

In June 2017, Southern Company made equity contributions totaling $1.0 billion to the Company. The Company used a portion of the proceeds to (i) prepay $300 million of the outstanding principal amount under its $1.2 billion unsecured term loan, which matures on March 30, 2018; (ii) repay all of the $591 million outstanding principal amount of promissory notes to Southern Company; and (iii) repay a $10 million short-term bank loan.

In September 2017, the Company issued a floating rate promissory note to Southern Company in an aggregate principal amount of up to $150 million bearing interest based on one-month LIBOR. The Company borrowed $109 million under this promissory note primarily to satisfy its federal income tax obligations for the quarter ending September 30, 2017 and subsequently repaid the promissory note upon receipt of its income tax refund from the U.S. federal government related to the settlement concerning deductible R&E expenditures. See Note 5 under "Section 174 Research and Experimental Deduction" for additional information. At December 31, 2017, the Company had no outstanding promissory notes to Southern Company.

Bank Term Loans

In March 2017, the Company issued a $9 million short-term bank note bearing interest at 5% per annum, which was repaid in April 2017.

In June 2017, the Company used a portion of the proceeds from Southern Company equity contributions to prepay $300 million of the outstanding principal amount under its $1.2 billion unsecured term loan, which matures on March 30, 2018, and to repay $10 million of the outstanding principal amount of bank loans. See "Parent Company Loans and Equity Contributions" herein for more information.

This unsecured term loan has a covenant that limits debt levels to 65% of total capitalization, as defined in the agreement. For purposes of this definition, debt excludes any long-term debt payable to affiliated trusts and other hybrid securities. At December 31, 2017, the Company was in compliance with its debt limit.

In August 2017, the Company repaid a $12.5 million short-term bank note.

At December 31, 2017, the Company had a $900 million unsecured term loan outstanding, which was reflected in the statements of capitalization as securities due within one year. At December 31, 2016, the Company had a $1.2 billion unsecured term loan outstanding, which was reflected in the statements of capitalization as long-term debt.

Senior Notes

At December 31, 2017 and 2016, the Company had $755 million and $790 million of senior notes outstanding, respectively, which included senior notes due within one year. These senior notes are effectively subordinated to the secured debt of the Company. See "Plant Daniel Revenue Bonds" below for additional information regarding the Company's secured indebtedness.

Plant Daniel Revenue Bonds

In 2011, in connection with the Company's election under its operating lease of Plant Daniel Units 3 and 4 to purchase the assets, the Company assumed the obligations of the lessor related to $270 million aggregate principal amount of Mississippi Business Finance Corporation Taxable Revenue Bonds, 7.13% Series 1999A due October 20, 2021, issued for the benefit of the lessor. These bonds are secured by Plant Daniel Units 3 and 4 and certain related personal property. The bonds were recorded at fair value as of the date of assumption, or $346 million, reflecting a premium of $76 million. See "Assets Subject to Lien" herein for additional information.

Pollution Control Revenue Bonds

Pollution control obligations represent loans to the Company from public authorities of funds derived from sales by such authorities of pollution control revenue bonds issued to finance pollution control and solid waste disposal facilities. The Company is required to make payments sufficient for the authorities to meet principal and interest requirements of such bonds. The amount of tax-exempt pollution control revenue bonds outstanding at December 31, 2017 and 2016 was $83 million.

Other Revenue Bonds

Other revenue bond obligations represent loans to the Company from a public authority of funds derived from the sale by such authority of revenue bonds issued to finance a portion of the costs of constructing the Kemper County energy facility and related facilities.

The Company had $50 million of such obligations outstanding related to tax-exempt revenue bonds at December 31, 2017 and 2016. Such amounts are reflected in the statements of capitalization as long-term debt.

Capital Leases

In 2013, the Company entered into an agreement to sell the air separation unit for the Kemper County energy facility and also entered into a 20-year nitrogen supply agreement. The nitrogen supply agreement was determined to be a sale/leaseback agreement, which resulted in a capital lease obligation of $74 million at December 31, 2016. Following the suspension of the Kemper IGCC, the Company entered into an asset purchase and settlement agreement in December 2017 with the lessor, which terminated the capital lease obligation. There were no contingent rentals in the contract and a portion of the monthly payment specified in the agreement was related to executory costs for the operation and maintenance of the air separation unit and excluded from the minimum lease payments. The minimum lease payments for 2017 were $7 million. See Note 3 under "Kemper County Energy facility" for additional information.

Assets Subject to Lien

The revenue bonds assumed in conjunction with the purchase of Plant Daniel Units 3 and 4 are secured by Plant Daniel Units 3 and 4 and certain related personal property. There are no agreements or other arrangements among the Southern Company system companies under which the assets of one company have been pledged or otherwise made available to satisfy the obligations of Southern Company or another of its other subsidiaries. See "Plant Daniel Revenue Bonds" herein for additional information.

On October 4, 2017, the Company executed agreements with its largest retail customer, Chevron Products Company (Chevron), to continue providing retail service to the Chevron refinery in Pascagoula, Mississippi through 2038, subject to the approval of the Mississippi PSC. The agreements grant Chevron a security interest in its co-generation assets, with a net book value of approximately $93 million, located at Chevron's refinery that is exercisable upon the occurrence of (i) certain bankruptcy events or (ii) other events of default coupled with specific reductions in steam output at the facility and a downgrade of the Company's credit rating to below investment grade by two of the three rating agencies.

Outstanding Classes of Capital Stock

The Company currently has preferred stock (including depositary shares which represent one-fourth of a share of preferred stock) and common stock authorized and outstanding. The preferred stock of the Company contains a feature that allows the holders to elect a majority of the Company's board of directors if preferred dividends are not paid for four consecutive quarters. Because such a potential redemption-triggering event is not solely within the control of the Company, this preferred stock is presented as "Cumulative Redeemable Preferred Stock" in a manner consistent with temporary equity under applicable accounting standards. The Company's preferred stock and depositary preferred stock, without preference between classes, rank senior to the Company's common stock with respect to payment of dividends and voluntary or involuntary dissolution. The preferred stock and depositary preferred stock is subject to redemption at the option of the Company at a redemption price equal to 100% of the liquidation amount of the stock. Information for each outstanding series is in the table below:

Preferred Stock	Par Value/ Stated Capital Per Share	Shares Outstanding	Redemption Price Per Share
4.40% Preferred Stock	$ 100	8,867	$ 104.32
4.60% Preferred Stock	$ 100	8,643	$ 107.00
4.72% Preferred Stock	$ 100	16,700	$ 102.25
5.25% Preferred Stock(*)	$ 100	300,000	$ 100.00

(*) There are 1,200,000 outstanding depositary shares, each representing one-fourth of a share of the 5.25% preferred stock.

Dividend Restrictions

The Company can only pay dividends to Southern Company out of retained earnings or paid-in-capital.

Bank Credit Arrangements

At December 31, 2017, committed credit arrangements with banks were as follows:

Expires			Executable Term Loans		Expires Within One Year	
2018	Total	Unused	One Year	Two Years	Term Out	No Term Out
(in millions)	*(in millions)*		*(in millions)*		*(in millions)*	
$100	$100	$100	$—	$—	$—	$100

In November 2017, the Company amended certain of its one-year credit arrangements in an aggregate amount of $100 million to extend the maturity dates from 2017 to 2018.

Subject to applicable market conditions, the Company expects to renew its bank credit arrangements, as needed, prior to expiration. In connection therewith, the Company may extend the maturity dates and/or increase or decrease the lending commitments thereunder.

Most of these bank credit arrangements require payment of commitment fees based on the unused portions of the commitments or to maintain compensating balances with the banks. Commitment fees average less than 1/4 of 1% for the Company. Compensating balances are not legally restricted from withdrawal.

Most of these bank credit arrangements contain covenants that limit the Company's debt levels to 65% of total capitalization, as defined in the agreements. For purposes of these definitions, debt excludes certain hybrid securities.

A portion of the $100 million unused credit with banks is allocated to provide liquidity support to the Company's pollution control revenue bonds and its commercial paper borrowings. The amount of variable rate pollution control revenue bonds outstanding requiring liquidity support as of December 31, 2017 was $40 million. In addition, at December 31, 2017, the Company had approximately $50 million of fixed rate revenue bonds that were remarketed from a long-term interest rate mode to an index rate mode, subsequent to December 31, 2017.

At December 31, 2017 and 2016, there was no commercial paper debt outstanding.

At December 31, 2017 and 2016, there was $4 million and $23 million, respectively, of short-term debt outstanding.

7. COMMITMENTS

Fuel and Purchased Power Agreements

To supply a portion of the fuel requirements of its generating plants, the Company has entered into various long-term commitments for the procurement and delivery of fossil fuel which are not recognized on the balance sheets. In 2017, 2016, and 2015, the Company incurred fuel expense of $395 million, $343 million, and $443 million, respectively, the majority of which was purchased under long-term commitments. The Company expects that a substantial amount of its future fuel needs will continue to be purchased under long-term commitments.

SCS may enter into various types of wholesale energy and natural gas contracts acting as an agent for the Company and all of the other traditional electric operating companies and Southern Power. Under these agreements, each of the traditional electric operating companies and Southern Power may be jointly and severally liable. Accordingly, Southern Company has entered into keep-well agreements with the Company and each of the other traditional electric operating companies to ensure the Company will not subsidize or be responsible for any costs, losses, liabilities, or damages resulting from the inclusion of Southern Power as a contracting party under these agreements.

In addition, the Company has entered into various long-term commitments for the purchase of energy through PPAs associated with solar facilities. The energy related costs associated with PPAs are recovered through the fuel cost recovery clause.

Operating Leases

The Company has entered into operating leases with Southern Linc and third parties for the use of cellular tower space. These agreements have initial terms ranging from five to 10 years and renewal options of up to 20 years. The Company has other operating lease agreements with various terms and expiration dates. Total rent expense was $3 million, $3 million, and $5 million for 2017, 2016, and 2015, respectively. The Company includes any step rents, fixed escalations, lease concessions, and reasonably assured renewal periods in its computation of minimum lease payments.

Estimated minimum lease payments under operating leases at December 31, 2017 were as follows:

	Affiliate Operating Leases[(a)]	Non-Affiliate Operating Lease[(b)]	Total
		(in millions)	
2018	$ 2	$ 1	$ 3
2019	2	1	3
2020	2	1	3
2021	2	—	2
2022	2	—	2
2023 and thereafter	7	—	7
Total	$ 17	$ 3	$ 20

(a) Includes operating leases with affiliates primarily related to cellular towers.

(b) Primarily includes railcar and fuel handling equipment leases for Plant Daniel.

In addition to the above rental commitments, the Company entered into operating lease agreements for aluminum railcars for the transportation of coal at Plant Daniel, which is jointly owned with Gulf Power. The Company has the option to purchase the railcars at the greater of lease termination value or fair market value or to renew the leases at the end of the lease term. The Company also has separate lease agreements for other railcars that do not contain a purchase option.

The Company's 50% share of the lease costs, charged to fuel stock and recovered through the fuel cost recovery clause, was $1 million in 2017, $2 million in 2016, and $2 million in 2015.

In addition to railcar leases, the Company has other operating leases for fuel handling equipment at Plant Daniel. The Company's 50% share of the leases for fuel handling was charged to fuel handling expense annually from 2015 through 2017; however, those amounts were immaterial for the reporting period.

8. STOCK COMPENSATION

Stock-Based Compensation

Stock-based compensation primarily in the form of Southern Company performance share units and restricted stock units may be granted through the Omnibus Incentive Compensation Plan to a large segment of the Company's employees ranging from line management to executives. In 2015 and 2016, stock-based compensation consisted exclusively of performance share units. Beginning in 2017, stock-based compensation granted to employees includes restricted stock units in addition to performance share units. Prior to 2015, stock-based compensation also included stock options. As of December 31, 2017, there were 180 current and former employees participating in the stock option, performance share unit, and restricted stock unit programs.

Performance Share Units

Performance share units granted to employees vest at the end of a three-year performance period. All unvested performance share units vest immediately upon a change in control where Southern Company is not the surviving corporation. Shares of Southern Company common stock are delivered to employees at the end of the performance period with the number of shares issued ranging from 0% to 200% of the target number of performance share units granted, based on achievement of the performance goals established by the Compensation Committee of the Southern Company Board of Directors.

Southern Company issues performance share units with performance goals based on three performance goals to employees. These include performance share units with performance goals based on the total shareholder return (TSR) for Southern Company common stock during the three-year performance period as compared to a group of industry peers, performance share units with performance goals based on Southern Company's cumulative earnings per share (EPS) over the performance period, and performance share units with performance goals based on Southern Company's equity-weighted ROE over the performance period.

In 2015 and 2016, the EPS-based and ROE-based awards each represented 25% of the total target grant date fair value of the performance share unit awards granted. The remaining 50% of the total target grant date fair value consisted of TSR-based awards. Beginning in 2017, the total target grant date fair value of the stock compensation awards granted was comprised 20% each of EPS-based awards and ROE-based awards and 30% each of TSR-based awards and restricted stock units.

The fair value of TSR-based performance share unit awards is determined as of the grant date using a Monte Carlo simulation model to estimate the TSR of Southern Company's common stock among the industry peers over the performance period. The Company recognizes compensation expense on a straight-line basis over the three-year performance period without remeasurement.

The fair values of the EPS-based awards and the ROE-based awards are based on the closing stock price of Southern Company common stock on the date of the grant. Compensation expense for the EPS-based and ROE-based awards is generally recognized ratably over the three-year performance period initially assuming a 100% payout at the end of the performance period. Employees become immediately vested in the TSR-based performance share units, along with the EPS-based and ROE-based awards, upon retirement. As a result, compensation expense for employees that are retirement eligible at the grant date is recognized immediately while compensation expense for employees that become retirement eligible during the vesting period is recognized over the period from grant date to the date of retirement eligibility. The expected payout related to the EPS-based and ROE-based awards is reevaluated annually with expense recognized to date increased or decreased based on the number of shares currently expected to be issued. Unlike the TSR-based awards, the compensation expense ultimately recognized for the EPS-based awards and the ROE-based awards will be based on the actual number of shares issued at the end of the performance period.

For the years ended December 31, 2017, 2016, and 2015, employees of the Company were granted performance share units of 30,933, 62,435, and 53,909, respectively. The weighted average grant-date fair value of TSR-based performance share units granted during 2017, 2016, and 2015, determined using a Monte Carlo simulation model to estimate the TSR of Southern Company's stock among the industry peers over the performance period, was $49.24, $45.17, and $46.41, respectively. The weighted average grant-date fair value of both EPS-based and ROE-based performance share units granted during 2017, 2016, and 2015 was $49.22, $48.84, and $47.77, respectively.

For the years ended December 31, 2017, 2016, and 2015, total compensation cost for performance share units recognized in income was $2 million, $4 million, and $4 million, respectively, with the related tax benefit also recognized in income of $1 million, $1 million, and $2 million, respectively. The compensation cost related to the grant of Southern Company performance share units to the Company's employees is recognized in the Company's financial statements with a corresponding credit to equity, representing a capital contribution from Southern Company. As of December 31, 2017, total unrecognized compensation cost related to performance share award units was immaterial.

Restricted Stock Units

Beginning in 2017, stock-based compensation granted to employees included restricted stock units in addition to performance share units. One-third of the restricted stock units granted to employees vest each year throughout a three-year service period. All unvested restricted stock units vest immediately upon a change in control where Southern Company is not the surviving corporation. Shares of Southern Company common stock are delivered to employees at the end of the vesting period.

The fair value of restricted stock units is based on the closing stock price of Southern Company common stock on the date of the grant. Since one-third of the restricted stock units vest each year throughout a three-year service period, compensation expense for restricted stock unit awards is generally recognized over the corresponding one-, two-, or three-year period. Employees become immediately vested in the restricted stock units upon retirement. As a result, compensation expense for employees that are retirement eligible at the grant date is recognized immediately while compensation expense for employees that become retirement eligible during the vesting period is recognized over the period from grant date to the date of retirement eligibility.

For the year ended December 31, 2017, employees of the Company were granted 13,260 restricted stock units. The weighted average grant-date fair value of restricted stock units granted during 2017 was $49.22.

For the year ended December 31, 2017, total compensation cost for restricted stock units and the related tax benefit also recognized in income was immaterial. As of December 31, 2017, total unrecognized compensation cost related to restricted stock units was immaterial.

Stock Options

In 2015, Southern Company discontinued the granting of stock options. Stock options expire no later than 10 years after the grant date and the latest possible exercise will occur no later than November 2024.

The compensation cost related to the grant of Southern Company stock options to the Company's employees is recognized in the Company's financial statements with a corresponding credit to equity, representing a capital contribution from Southern Company. Compensation cost and related tax benefits recognized in the Company's financial statements were not material for any year presented. As of December 31, 2017, all compensation cost related to stock option awards has been recognized.

The total intrinsic value of options exercised during the years ended December 31, 2017, 2016, and 2015 was $2 million, $4 million, and $3 million, respectively. No cash proceeds are received by the Company upon the exercise of stock options. The actual tax benefit realized by the Company for the tax deductions from stock option exercises totaled $1 million, $2 million, and $1 million for the years ended December 31, 2017, 2016, and 2015, respectively. Prior to the adoption of ASU 2016-09 in 2016, the excess tax benefits related to the exercise of stock options were recognized in the Company's financial statements with a credit to equity. Upon the adoption of ASU 2016-09, beginning in 2016, all tax benefits related to the exercise of stock options are recognized in income. As of December 31, 2017, the aggregate intrinsic value for the options outstanding and exercisable was $4 million.

9. FAIR VALUE MEASUREMENTS

Fair value measurements are based on inputs of observable and unobservable market data that a market participant would use in pricing the asset or liability. The use of observable inputs is maximized where available and the use of unobservable inputs is minimized for fair value measurement and reflects a three-tier fair value hierarchy that prioritizes inputs to valuation techniques used for fair value measurement.

- Level 1 consists of observable market data in an active market for identical assets or liabilities.
- Level 2 consists of observable market data, other than that included in Level 1, that is either directly or indirectly observable.
- Level 3 consists of unobservable market data. The input may reflect the assumptions of the Company of what a market participant would use in pricing an asset or liability. If there is little available market data, then the Company's own assumptions are the best available information.

In the case of multiple inputs being used in a fair value measurement, the lowest level input that is significant to the fair value measurement represents the level in the fair value hierarchy in which the fair value measurement is reported.

As of December 31, 2017, assets and liabilities measured at fair value on a recurring basis during the period, together with their associated level of the fair value hierarchy, were as follows:

	Fair Value Measurements Using			
As of December 31, 2017:	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total**
		(in millions)		
Assets:				
Energy-related derivatives	$ —	$ 2	$ —	$ 2
Interest rate derivatives	—	1	—	1
Cash equivalents	224	—	—	224
Total	$ 224	$ 3	$ —	$ 227
Liabilities:				
Energy-related derivatives	$ —	$ 9	$ —	$ 9

As of December 31, 2016, assets and liabilities measured at fair value on a recurring basis during the period, together with their associated level of the fair value hierarchy, were as follows:

	Fair Value Measurements Using			
As of December 31, 2016:	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total**
		(in millions)		
Assets:				
Energy-related derivatives	$ —	$ 3	$ —	$ 3
Interest rate derivatives	—	3	—	3
Cash equivalents	206	—	—	206
Total	$ 206	$ 6	$ —	$ 212
Liabilities:				
Energy-related derivatives	$ —	$ 10	$ —	$ 10

Valuation Methodologies

The energy-related derivatives primarily consist of over-the-counter financial products for natural gas and physical power products, including, from time to time, basis swaps. These are standard products used within the energy industry and are valued using the market approach. The inputs used are mainly from observable market sources, such as forward natural gas prices, power prices, implied volatility, and overnight index swap interest rates. See Note 10 for additional information on how these derivatives are used.

As of December 31, 2017 and 2016, other financial instruments for which the carrying amount did not equal fair value were as follows:

	Carrying Amount	Fair Value
	(in millions)	
Long-term debt:		
2017	**$ 2,086**	**$ 2,076**
2016	$ 2,979	$ 2,922

The fair values are determined using Level 2 measurements and are based on quoted market prices for the same or similar issues or on the current rates offered to the Company.

10. DERIVATIVES

The Company is exposed to market risks, primarily commodity price risk and interest rate risk. To manage the volatility attributable to these exposures, the Company nets its exposures, where possible, to take advantage of natural offsets and enters into various derivative transactions for the remaining exposures pursuant to the Company's policies in areas such as counterparty exposure and risk management practices. The Company's policy is that derivatives are to be used primarily for hedging purposes and mandates strict adherence to all applicable risk management policies. Derivative positions are monitored using techniques including, but not limited to, market valuation, value at risk, stress testing, and sensitivity analysis. Derivative instruments are recognized at fair value in the balance sheets as either assets or liabilities and are presented on a net basis. See Note 9 for additional information. In the statements of cash flows, the cash impacts of settled energy-related and interest rate derivatives are recorded as operating activities.

Energy-Related Derivatives

The Company enters into energy-related derivatives to hedge exposures to electricity, gas, and other fuel price changes. However, due to cost-based rate regulations and other various cost recovery mechanisms, the Company has limited exposure to market volatility in energy-related commodity prices. The Company manages fuel-hedging programs, implemented per the guidelines of the Mississippi PSC, through the use of financial derivative contracts, which is expected to continue to mitigate price volatility.

Energy-related derivative contracts are accounted for under one of the following methods:

- *Regulatory Hedges* – Energy-related derivative contracts which are designated as regulatory hedges relate primarily to the Company's fuel-hedging programs, where gains and losses are initially recorded as regulatory liabilities and assets, respectively, and then are included in fuel expense as the underlying fuel is used in operations and ultimately recovered through the respective fuel cost recovery clauses.
- *Not Designated* – Gains and losses on energy-related derivative contracts that are not designated or fail to qualify as hedges are recognized in the statements of operations as incurred.

Some energy-related derivative contracts require physical delivery as opposed to financial settlement, and this type of derivative is both common and prevalent within the electric industry. When an energy-related derivative contract is settled physically, any cumulative unrealized gain or loss is reversed and the contract price is recognized in the respective line item representing the actual price of the underlying goods being delivered.

At December 31, 2017, the net volume of energy-related derivative contracts for natural gas positions totaled 53 million mmBtu for the Company, with the longest hedge date of 2021 over which the Company is hedging its exposure to the variability in future cash flows for forecasted transactions.

In addition to the volume discussed above, the Company enters into physical natural gas supply contracts that provide the option to sell back excess gas due to operational constraints. The maximum expected volume of natural gas subject to such a feature is 4 million mmBtu.

Interest Rate Derivatives

The Company may also enter into interest rate derivatives to hedge exposure to changes in interest rates. Derivatives related to existing variable rate securities or forecasted transactions are accounted for as cash flow hedges where the effective portion of the derivatives' fair value gains or losses is recorded in OCI and is reclassified into earnings at the same time the hedged transactions affect earnings. The derivatives employed as hedging instruments are structured to minimize ineffectiveness, which is recorded directly to income.

At December 31, 2017, the following interest rate derivatives were outstanding:

	Notional Amount	Interest Rate Received	Weighted Average Interest Rate Paid	Hedge Maturity Date	Fair Value Gain (Loss) December 31, 2017
	(in millions)				*(in millions)*
Cash Flow Hedges of Existing Debt	$ 900	1-month LIBOR	0.79%	March 2018	$ 1

The estimated pre-tax losses that will be reclassified from accumulated OCI to interest expense for the next 12-month period ending December 31, 2018 are $0.5 million. The Company has deferred gains and losses that are expected to be amortized into earnings through 2022.

Derivative Financial Statement Presentation and Amounts

The Company enters into energy-related and interest rate derivative contracts that may contain certain provisions that permit intra-contract netting of derivative receivables and payables for routine billing and offsets related to events of default and settlements. Fair value amounts of derivative assets and liabilities on the balance sheets are presented net to the extent that there are netting arrangements or similar agreements with counterparties.

At December 31, 2017 and 2016, the fair value of energy-related derivatives and interest rate derivatives was reflected on the balance sheets as follows:

	2017		2016	
Derivative Category and Balance Sheet Location	**Assets**	**Liabilities**	Assets	Liabilities
		(in millions)		
Derivatives designated as hedging instruments for regulatory purposes				
Energy-related derivatives:				
Other current assets/Other current liabilities	**$ 1**	**$ 6**	$ 2	$ 6
Other deferred charges and assets/Other deferred credits and liabilities	**1**	**3**	2	5
Total derivatives designated as hedging instruments for regulatory purposes	**$ 2**	**$ 9**	$ 4	$ 11
Derivatives designated as hedging instruments in cash flow and fair value hedges				
Interest rate derivatives:				
Other current assets/Other current liabilities	**$ 1**	**$ —**	$ 2	$ —
Other deferred charges and assets/Other deferred credits and liabilities	**—**	**—**	1	—
Total derivatives designated as hedging instruments in cash flow and fair value hedges	**$ 1**	**$ —**	$ 3	$ —
Gross amounts recognized	**$ 3**	**$ 9**	$ 7	$ 11
Gross amounts offset	**$ (2)**	**$ (2)**	$ (3)	$ (3)
Net amounts recognized in the Balance Sheets	**$ 1**	**$ 7**	$ 4	$ 8

Energy-related derivatives not designated as hedging instruments were immaterial for 2017 and 2016.

At December 31, 2017 and 2016, the pre-tax effects of unrealized derivative gains (losses) arising from energy-related derivatives designated as regulatory hedging instruments and deferred were as follows:

	Unrealized Losses			Unrealized Gains		
Derivative Category	**Balance Sheet Location**	**2017**	2016	**Balance Sheet Location**	**2017**	2016
		(in millions)			*(in millions)*	
Energy-related derivatives:	Other regulatory assets, current	**$ (5)**	$ (5)	Other current liabilities	**$ —**	$ 1
	Other regulatory assets, deferred	**(2)**	(3)	Other regulatory liabilities, deferred	**—**	—
Total energy-related derivative gains (losses)		**$ (7)**	$ (8)		**$ —**	$ 1

For all years presented, the pre-tax effects of energy-related derivatives not designated as hedging instruments on the statements of operations were immaterial.

For the years ended December 31, 2017, 2016, and 2015, the pre-tax effects of derivatives designated as cash flow hedging instruments on the statements of operations were immaterial.

Contingent Features

The Company does not have any credit arrangements that would require material changes in payment schedules or terminations as a result of a credit rating downgrade. There are certain derivatives that could require collateral, but not accelerated payment, in the event of various credit rating changes of certain affiliated companies. At December 31, 2017, the Company had no collateral posted with its derivative counterparties.

At December 31, 2017, the fair value of derivative liabilities with contingent features was $1 million. However, because of joint and several liability features underlying these derivatives, the maximum potential collateral requirements arising from the credit-risk-related contingent features, at a rating below BBB- and/or Baa3, were $12 million, and include certain agreements that could require collateral in the event that one or more Southern Company system power pool participants has a credit rating change to below investment grade.

Generally, collateral may be provided by a Southern Company guaranty, letter of credit, or cash. If collateral is required, fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral are not offset against fair value amounts recognized for derivatives executed with the same counterparty.

The Company is exposed to losses related to financial instruments in the event of counterparties' nonperformance. The Company only enters into agreements and material transactions with counterparties that have investment grade credit ratings by Moody's and S&P or with counterparties who have posted collateral to cover potential credit exposure. The Company has also established risk management policies and controls to determine and monitor the creditworthiness of counterparties in order to mitigate the Company's exposure to counterparty credit risk. Therefore, the Company does not anticipate a material adverse effect on the financial statements as a result of counterparty nonperformance.

11. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Summarized quarterly financial information for 2017 and 2016 is as follows:

Quarter Ended	Operating Revenues	Operating Income (Loss)	Net Income (Loss) After Dividends on Preferred Stock
		(in millions)	
March 2017	**$ 272**	**$ (62)**	**$ (20)**
June 2017	**303**	**(2,954)**	**(2,054)**
September 2017	**341**	**51**	**40**
December 2017	**271**	**(177)**	**(556)**
March 2016	$ 257	$ (10)	$ 11
June 2016	277	(28)	2
September 2016	352	9	26
December 2016	277	(166)	(89)

As a result of the revisions to the cost estimate for the Kemper IGCC and its June 2017 suspension, the Company recorded total pre-tax charges to income related to the Kemper IGCC of $208 million ($185 million after tax) in the fourth quarter 2017, $34 million ($21 million after tax) in the third quarter 2017, $3.0 billion ($2.1 billion after tax) in the second quarter 2017, $108 million ($67 million after tax) in the first quarter 2017, $206 million ($127 million after tax) in the fourth quarter 2016, $88 million ($54 million after tax) in the third quarter 2016, $81 million ($50 million after tax) in the second quarter 2016, and $53 million ($33 million after tax) in the first quarter 2016. See Note 3 under "Kemper County Energy Facility" for additional information.

As a result of Tax Reform Legislation, the Company recorded total income tax expense of $372 million in the fourth quarter 2017. See Note 5 for additional information.

The Company's business is influenced by seasonal weather conditions.

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SELECTED FINANCIAL AND OPERATING DATA 2013-2017
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	2017	2016	2015	2014	2013
Operating Revenues (in millions)	**$ 1,187**	$ 1,163	$ 1,138	$ 1,243	$ 1,145
Net Income (Loss) After Dividends on Preferred Stock (in millions)[(a)]	**$ (2,590)**	$ (50)	$ (8)	$ (329)	$ (477)
Cash Dividends on Common Stock (in millions)	**$ —**	$ —	$ —	$ —	$ 72
Return on Average Common Equity (percent)[(a)]	**(120.43)**	(1.87)	(0.34)	(15.43)	(24.28)
Total Assets (in millions)[(b)(c)]	**$ 4,866**	$ 8,235	$ 7,840	$ 6,642	$ 5,822
Gross Property Additions (in millions)	**$ 536**	$ 946	$ 972	$ 1,389	$ 1,773
Capitalization (in millions):					
Common stock equity	**$ 1,358**	$ 2,943	$ 2,359	$ 2,084	$ 2,177
Redeemable preferred stock	**33**	33	33	33	33
Long-term debt[(b)]	**1,097**	2,424	1,886	1,621	2,157
Total (excluding amounts due within one year)	**$ 2,488**	$ 5,400	$ 4,278	$ 3,738	$ 4,367
Capitalization Ratios (percent):					
Common stock equity	**54.6**	54.5	55.1	55.8	49.9
Redeemable preferred stock	**1.3**	0.6	0.8	0.9	0.7
Long-term debt[(b)]	**44.1**	44.9	44.1	43.3	49.4
Total (excluding amounts due within one year)	**100.0**	100.0	100.0	100.0	100.0
Customers (year-end):					
Residential	**153,115**	153,172	153,158	152,453	152,585
Commercial	**33,992**	33,783	33,663	33,496	33,250
Industrial	**452**	451	467	482	480
Other	**173**	175	175	175	175
Total	**187,732**	187,581	187,463	186,606	186,490
Employees (year-end)	**1,242**	1,484	1,478	1,478	1,344

(a) A significant loss to income was recorded by the Company related to the suspension of the Kemper IGCC in June 2017. Earnings in all periods presented were impacted by losses related to the Kemper IGCC.

(b) A reclassification of debt issuance costs from Total Assets to Long-term debt of $9 million and $11 million is reflected for years 2014 and 2013, respectively, in accordance with new accounting standards adopted in 2015 and applied retrospectively.

(c) A reclassification of deferred tax assets from Total Assets of $105 million and $16 million is reflected for years 2014 and 2013, respectively, in accordance with new accounting standards adopted in 2015 and applied retrospectively.

	2017	2016	2015	2014	2013
Operating Revenues (in millions):					
Residential	**$ 257**	$ 260	$ 238	$ 239	$ 242
Commercial	**285**	279	256	257	266
Industrial	**321**	313	287	291	289
Other	**(9)**	7	(5)	8	2
Total retail	**854**	859	776	795	799
Wholesale — non-affiliates	**259**	261	270	323	294
Wholesale — affiliates	**56**	26	76	107	35
Total revenues from sales of electricity	**1,169**	1,146	1,122	1,225	1,128
Other revenues	**18**	17	16	18	17
Total	**$ 1,187**	$ 1,163	$ 1,138	$ 1,243	$ 1,145
Kilowatt-Hour Sales (in millions):					
Residential	**1,944**	2,051	2,025	2,126	2,088
Commercial	**2,764**	2,842	2,806	2,860	2,865
Industrial	**4,841**	4,906	4,958	4,943	4,739
Other	**39**	39	40	40	40
Total retail	**9,588**	9,838	9,829	9,969	9,732
Wholesale — non-affiliates	**3,672**	3,920	3,852	4,191	3,929
Wholesale — affiliates	**2,024**	1,108	2,807	2,900	931
Total	**15,284**	14,866	16,488	17,060	14,592
Average Revenue Per Kilowatt-Hour (cents)(*):					
Residential	**13.22**	12.68	11.75	11.26	11.59
Commercial	**10.31**	9.82	9.12	8.99	9.27
Industrial	**6.63**	6.38	5.79	5.89	6.10
Total retail	**8.91**	8.73	7.90	7.97	8.21
Wholesale	**5.53**	5.71	5.20	6.06	6.76
Total sales	**7.65**	7.71	6.80	7.18	7.73
Residential Average Annual Kilowatt-Hour Use Per Customer	**12,692**	13,383	13,242	13,934	13,680
Residential Average Annual Revenue Per Customer	**$ 1,680**	$ 1,697	$ 1,556	$ 1,568	$ 1,585
Plant Nameplate Capacity Ratings (year-end) (megawatts)	**3,628**	3,481	3,561	3,867	3,088
Maximum Peak-Hour Demand (megawatts):					
Winter	**2,390**	2,195	2,548	2,618	2,083
Summer	**2,322**	2,384	2,403	2,345	2,352
Annual Load Factor (percent)	**63.1**	64.0	60.6	59.4	64.7
Plant Availability Fossil-Steam (percent)	**89.1**	91.4	90.6	87.6	89.3
Source of Energy Supply (percent):					
Coal	**7.5**	8.0	16.5	39.7	32.7
Oil and gas	**88.0**	84.9	81.6	55.3	57.1
Purchased power —					
From non-affiliates	**0.5**	(0.3)	0.4	1.4	2.0
From affiliates	**4.0**	7.4	1.5	3.6	8.2
Total	**100.0**	100.0	100.0	100.0	100.0

(*) The average revenue per kilowatt-hour (cents) is based on booked operating revenues and will not match billed revenue per kilowatt-hour.

DIRECTORS AND OFFICERS
Mississippi Power Company 2017 Annual Report

Directors

Carl J. Chaney
Executive Chairman, BCB Capital Group
Retired Director, President, and Chief Executive Officer
Hancock Holding Company
Gulfport, Mississippi. Elected 2009

L. Royce Cumbest
Chairman, President, and Chief Executive Officer
Merchants & Marine Bank and Merchants & Marine Bancorp, Inc.
Pascagoula, Mississippi. Elected 2010

Thomas A. Dews
President
C. L. Dews & Sons Foundry and Machinery Co., Inc.
Hattiesburg, Mississippi. Elected 2013
(Retired effective 2/1/17)

Thomas M. Duff
Co-Owner
Duff Capital Investors
Columbia, Mississippi. Elected 2018

Mark E. Keenum
President
Mississippi State University
Mississippi State, Mississippi. Elected 2013

Christine L. Pickering
Christy Pickering, CPA Public Accounting Firm
Biloxi, Mississippi. Elected 2007

Philip J. Terrell, Ph.D.
Retired Superintendent of Schools
Pass Christian Public School District
Pass Christian, Mississippi. Elected 1995

Marion L. Waters
Partner
Waters International Trucks, Inc., Waters Trucks and Tractor Co., Inc., and Waters Transportation, Inc.
Meridian, Mississippi. Elected 2010

Anthony L. Wilson
Chairman, President, and Chief Executive Officer
Mississippi Power Company
Gulfport, Mississippi. Elected 2016

Officers

Anthony L. Wilson
Chairman, President, and Chief Executive Officer

John W. Atherton
Vice President of Public Relations and Corporate Services

A. Nicole Faulk
Vice President of Customer Services Organization

Moses H. Feagin
Vice President, Chief Financial Officer, and Treasurer

R. Allen Reaves, Jr.
Vice President and Senior Production Officer

Billy F. Thornton
Vice President of External Affairs

Emile J. Troxclair III
Vice President of Kemper Development
(Resigned effective 12/2/17)

Cynthia F. Shaw
Comptroller

Vicki L. Pierce
Corporate Secretary and Assistant Treasurer

Stacy R. Kilcoyne
Vice President
(Resigned effective 3/2/17)

Melissa K. Caen
Assistant Secretary and Assistant Treasurer

CORPORATE INFORMATION
Mississippi Power Company 2017 Annual Report

General
This annual report is submitted for general information. It is not intended for use in connection with any sale or purchase of, or any solicitation of offers to buy or sell, securities.

Profile
The Company operates as a vertically integrated utility providing electric service to retail customers within its traditional service territory located within the State of Mississippi and to wholesale customers in the Southeast. The Company provides electric service to approximately 188,000 customers within its service territory. In 2017, retail energy sales accounted for 62.7% of the Company's total sales of 15.3 billion kilowatt-hours.

The Company is a wholly-owned subsidiary of The Southern Company, which is the parent of the Company and three other traditional electric operating companies as well as Southern Power Company and Southern Company Gas.

Registrar, Transfer Agent, and Dividend Paying Agent
All series of Preferred Stock
EQ Shareowner Services
P.O. Box 64856
St. Paul, MN 55154-0856
(800) 554-7626

shareowneronline.com

Trustee, Registrar, and Interest Paying Agent
All series of Senior Notes
Wells Fargo Bank, N.A.
Corporate, Municipal & Escrow Services
150 East 42nd Street
40th Floor
New York, NY 10017
(917) 260-1534

There is no market for the Company's common stock, all of which is owned by The Southern Company.

Dividends on the Company's common stock are payable at the discretion of the Company's board of directors. No dividends were declared by the Company to its common stockholder for the past two years.

Number of Preferred Shareholders of record as of December 31, 2017 was 181.

Form 10-K
A copy of the Form 10-K as filed with the Securities and Exchange Commission will be provided upon written request to the office of the Corporate Secretary at the Corporate Office address below.

The Form 10-K, as well as other documents filed by the Company pursuant to the Securities Exchange Act of 1934, as amended, are available electronically at http://www.sec.gov.

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Gulfport, Mississippi 39502