

MISSISSIPPI POWER COMPANY

2014 ANNUAL REPORT



A SOUTHERN COMPANY

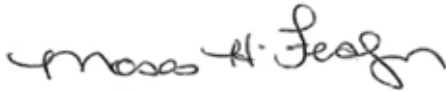
MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
Mississippi Power Company 2014 Annual Report

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, 2014.



G. Edison Holland, Jr.
Chairman, President, and Chief Executive Officer



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

March 2, 2015


REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**To the Board of Directors of
Mississippi Power Company**

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, 2014 and 2013, and 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, 2014. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, 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. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements (pages 39 to 87) present fairly, in all material respects, the financial position of Mississippi Power Company as of December 31, 2014 and 2013, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2014, in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads "Deloitte & Touche LLP". The signature is written in a cursive, flowing style.

Atlanta, Georgia
March 2, 2015

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 IGCC
AFUDC	Allowance for funds used during construction
Alabama Power	Alabama Power Company
APA	Asset purchase agreement
ASC	Accounting Standards Codification
Baseload Act	State of Mississippi legislation designed to enhance the Mississippi PSC's authority to facilitate development and construction of baseload generation in the State of Mississippi
CCR	Coal combustion residuals
Clean Air Act	Clean Air Act Amendments of 1990
CO ₂	Carbon dioxide
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
FERC	Federal Energy Regulatory Commission
GAAP	Generally accepted accounting principles
Georgia Power	Georgia Power Company
Gulf Power	Gulf Power Company
IGCC	Integrated coal gasification combined cycle
IRS	Internal Revenue Service
ITC	Investment tax credit
Kemper IGCC	IGCC facility under construction in Kemper County, Mississippi
KWH	Kilowatt-hour
LIBOR	London Interbank Offered Rate
Mirror CWIP	A regulatory liability account for use in mitigating future rate impacts for 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
OCI	Other comprehensive income
PEP	Performance evaluation plan
Plant Daniel Units 3 and 4	Combined cycle Units 3 and 4 at Plant Daniel
power pool	The operating arrangement whereby the integrated generating resources of the traditional operating companies and Southern Power Company are subject to joint commitment and dispatch in order to serve their combined load obligations
PPA	Power purchase agreement
PSC	Public Service Commission
ROE	Return on equity
S&P	Standard and Poor's Rating Services, a division of The McGraw Hill Companies, Inc.
scrubber	Flue gas desulfurization system

DEFINITIONS

(continued)

Term	Meaning
SCS	Southern Company Services, Inc. (the Southern Company system service company)
SEC	U.S. Securities and Exchange Commission
SMEPA	South Mississippi Electric Power Association
SouthernLINC Wireless.....	Southern Communications Services, Inc.
Southern Nuclear	Southern Nuclear Operating Company, Inc.
Southern Power	Southern Power Company and its subsidiaries
Southern Company system.....	The Southern Company, the traditional operating companies, Southern Power, Southern Electric Generating Company, Southern Nuclear, SCS, SouthernLINC Wireless, and other subsidiaries
SRR.....	System Restoration Rider
traditional operating companies ..	Alabama Power, Georgia Power, Gulf Power, and Mississippi Power Company

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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OVERVIEW

Business Activities

Mississippi Power Company (the Company) operates as a vertically integrated utility providing electricity 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 selling electricity. These factors include the Company's ability to maintain and grow energy sales and to maintain a constructive regulatory environment that provides timely recovery of prudently-incurred costs. These costs include those related to the completion and operation of major construction projects, primarily the Kemper IGCC and the Plant Daniel scrubber project, projected long-term demand growth, reliability, fuel, and increasingly stringent environmental standards, as well as ongoing capital expenditures required for maintenance. Appropriately balancing required costs and capital expenditures with customer prices will continue to challenge the Company for the foreseeable future.

The Company's retail base rates are set under the PEP, a rate plan approved by the Mississippi PSC. PEP was designed with the objective to reduce the impact of rate changes on customers and provide incentives for the Company to keep customer prices low and customer satisfaction and reliability high.

In 2010, the Mississippi PSC issued a CPCN authorizing the acquisition, construction, and operation of the Kemper IGCC. The certificated cost estimate of the Kemper IGCC established by the Mississippi PSC was \$2.4 billion with a construction cost cap of \$2.88 billion, net of \$245.3 million of grants awarded to the project by the DOE under the Clean Coal Power Initiative Round 2 (DOE Grants) and excluding the cost of the lignite mine and equipment, the cost of the CO₂ pipeline facilities, AFUDC, and certain general exceptions, including change of law, force majeure, and beneficial capital (which exists when the Company demonstrates that the purpose and effect of the construction cost increase is to produce efficiencies that will result in a neutral or favorable effect on customers relative to the original proposal for the CPCN) (Cost Cap Exceptions).

The Company's current cost estimate for the Kemper IGCC in total is approximately \$6.20 billion, which includes approximately \$4.93 billion of costs subject to the construction cost cap. The Company does not intend to seek any rate recovery or joint owner contributions for any related costs that exceed the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions. The Company has recorded pre-tax charges to income for revisions to the cost estimate of \$868.0 million (\$536.0 million after tax), \$1.10 billion (\$680.5 million after tax), and \$78.0 million (\$48.2 million after tax) in 2014, 2013 and 2012, respectively.

The Company placed the combined cycle and the associated common facilities portion of the Kemper IGCC project in service on August 9, 2014 and continues to focus on completing the remainder of the Kemper IGCC, including the gasifier and the gas clean-up facilities. The in-service date for the remainder of the Kemper IGCC is currently expected to occur in the first half of 2016. The current cost estimate includes costs through March 31, 2016. As a result of the additional factors that have the potential to impact start-up and operational readiness activities for this first-of-a-kind technology as described herein, the risk of further schedule extensions and/or cost increases, which could be material, remains. See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information, including the discussion of risks related to the Kemper IGCC.

On February 12, 2015, the Mississippi Supreme Court (Court) issued its decision in a legal challenge filed by Thomas A. Blanton with respect to the Mississippi PSC's March 2013 order that authorized the collection of \$156 million annually (2013 MPSC Rate Order) to be recorded as Mirror CWIP. The Court reversed the 2013 MPSC Rate Order, deemed the 2013 Settlement Agreement (defined below) between the Company and the Mississippi PSC unenforceable due to a lack of public notice for the related proceedings, and directed the Mississippi PSC to enter an order requiring the Company to refund the Mirror CWIP amounts collected pursuant to the 2013 MPSC Rate Order. As of December 31, 2014, \$257.2 million had been collected by the Company. The Company continues to analyze the Court's opinion and expects to file a motion for rehearing. See "2015 Mississippi Supreme Court Decision" herein for additional information.

Key Performance Indicators

The Company continues to focus on several key performance indicators, including the construction and start-up of the Kemper IGCC, to measure the Company's performance for customers and employees.

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

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)
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Company's allowed return. 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%). See Note 3 to the financial statements under "Retail Regulatory Matters – Performance Evaluation Plan" for more information on PEP.

In addition to the PEP performance indicators, the Company focuses on other performance measures, including broader measures of customer satisfaction, plant availability, system reliability, and net income after dividends on preferred stock. 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 the top quartile in measuring performance, which the Company achieved during 2014.

Peak season equivalent forced outage rate (Peak Season EFOR) is an indicator of fossil plant availability and efficient generation fleet operations during the months when generation needs are greatest. The rate is calculated by dividing the number of hours of forced outages by total generation hours. The Company's 2014 fossil Peak Season EFOR of 0.55% was better than the target. Transmission and distribution system reliability performance is measured by the frequency and duration of outages. Performance targets for reliability are set internally based on historical performance. The Company's 2014 performance was better than the target for these transmission and distribution reliability measures.

The Company uses net income (loss) after dividends on preferred stock as the primary measure of the Company's financial performance. The Company's results were below target for 2014 due to the increased cost estimate for the Kemper IGCC above the \$2.88 billion cost cap and the 2015 Court decision. See FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Performance Evaluation Plan" and FUTURE EARNINGS POTENTIAL – "Integrated Coal Gasification Combined Cycle" herein for additional information. See RESULTS OF OPERATIONS herein for additional information on the Company's financial performance.

Earnings

The Company's net income (loss) after dividends on preferred stock was (\$328.7) million in 2014 compared to (\$476.6) million in 2013. The decreased net loss in 2014 was primarily the result of lower pre-tax charges of \$868.0 million (\$536.0 million after tax) in 2014 compared to pre-tax charges of \$1.1 billion (\$680.5 million after-tax) in 2013 for revisions of estimated costs expected to be incurred on the Company's construction of the Kemper IGCC above the \$2.88 billion cost cap established by the Mississippi PSC, net of the DOE Grants and excluding the Cost Cap Exceptions. The change was also due to wholesale base rate increases, effective in April 2013 and May 2014, and an increase in AFUDC equity primarily related to the construction of the Kemper IGCC. These changes were partially offset by a decrease in retail revenues primarily as a result of the 2015 Court decision which required the reversal of revenues recorded in 2013, increases in non-fuel operations and maintenance expenses and interest expense. See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information regarding the Kemper IGCC.

The Company's net income (loss) after dividends on preferred stock was (\$476.6) million in 2013 compared to \$99.9 million in 2012. The decrease in 2013 was primarily the result of pre-tax charges of \$1.1 billion (\$680.5 million after-tax) for revisions of estimated costs expected to be incurred on the Company's construction of the Kemper IGCC above the \$2.88 billion cost cap established by the Mississippi PSC, net of the DOE Grants and excluding the Cost Cap Exceptions. These charges were partially offset by an increase in AFUDC equity primarily related to the construction of the Kemper IGCC which began in 2010 and an increase in revenues primarily due to retail and wholesale base rate increases and a retail rate increase related to the Kemper IGCC cost recovery that became effective in April 2013. See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information regarding the Kemper IGCC.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)
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RESULTS OF OPERATIONS

A condensed statement of operations follows:

	Amount		Increase (Decrease)
	2014	2014	from Prior Year
	<i>(in millions)</i>		
Operating revenues	\$ 1,242.6	\$ 97.5	\$ 109.2
Fuel	574.0	82.7	80.0
Purchased power	42.9	(5.4)	(6.8)
Other operations and maintenance	270.7	17.3	24.7
Depreciation and amortization	97.1	5.7	4.9
Taxes other than income taxes	79.1	(1.5)	1.2
Estimated loss on Kemper IGCC	868.0	(234.0)	1,024.0
Total operating expenses	1,931.8	(135.2)	1,128.0
Operating income	(689.2)	232.7	(1,018.8)
Allowance for equity funds used during construction	136.4	14.8	56.8
Interest expense, net of amounts capitalized	(45.3)	(8.8)	(4.4)
Other income (expense), net	(14.1)	(8.1)	(7.3)
Income taxes (benefit)	(285.2)	82.6	(388.4)
Net income (loss)	(327.0)	148.0	(576.5)
Dividends on preferred stock	1.7	—	—
Net income (loss) after dividends on preferred stock	\$ (328.7)	\$ 148.0	\$ (576.5)

Operating Revenues

Operating revenues for 2014 were \$1.2 billion, reflecting a \$97.5 million increase from 2013. Details of operating revenues were as follows:

	Amount	
	2014	2013
	<i>(in millions)</i>	
Retail — prior year	\$ 799.1	\$ 747.5
Estimated change resulting from —		
Rates and pricing	(11.5)	18.2
Sales growth (decline)	(1.5)	(0.7)
Weather	2.9	1.2
Fuel and other cost recovery	5.6	32.9
Retail — current year	794.6	799.1
Wholesale revenues —		
Non-affiliates	322.7	293.9
Affiliates	107.2	34.8
Total wholesale revenues	429.9	328.7
Other operating revenues	18.1	17.4
Total operating revenues	\$ 1,242.6	\$ 1,145.2
Percent change	8.5%	10.5%

Total retail revenues for 2014 decreased \$4.5 million, or 0.6%, compared to 2013 primarily as a result of \$10.3 million in revenues recorded in 2013 that were reversed in 2014 as a result of the 2015 Court decision. See Note 3 to the financial

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)
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statements under "Integrated Coal Gasification Combined Cycle – Rate Recovery of Kemper IGCC Costs – 2015 Mississippi Supreme Court Decision" for additional information. This decrease was partially offset by a PEP base rate increase, effective in March 2013, of \$2.8 million and a \$4.7 million refund in 2013 related to the annual PEP lookback filing. See Note 3 to the financial statements under "Retail Regulatory Matters – Performance Evaluation Plan" for additional information. Total retail revenues for 2013 increased \$51.6 million, or 6.9%, compared to 2012 primarily as a result of a base rate increase, a rate increase related to Kemper IGCC cost recovery that became effective in April 2013, and higher fuel cost recovery revenues in 2013 compared to 2012.

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. See FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Fuel Cost Recovery" herein for additional information. Fuel and other cost recovery revenues increased in 2014 and 2013 compared to prior years primarily as a result of higher recoverable fuel costs.

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.

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

	2014	2013	2012
		<i>(in millions)</i>	
Capacity and other	\$ 160.3	\$ 143.0	\$ 122.5
Energy	162.4	150.9	133.1
Total non-affiliated	\$ 322.7	\$ 293.9	\$ 255.6

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 service territory, and the availability of the Southern Company system's generation. Increases and decreases in 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. The Company serves 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 21.9% of the Company's total operating revenues in 2014 and are largely subject to rolling 10-year cancellation notices.

Wholesale revenues from sales to non-affiliates increased \$28.8 million, or 9.8%, in 2014 compared to 2013 as a result of a \$17.3 million increase in base revenues primarily resulting from wholesale base rate increases effective April 1, 2013 and May 1, 2014 and an \$11.5 million increase in energy revenues, of which \$10.0 million was associated with an increase in KWH sales and \$1.5 million was associated with higher fuel prices. Wholesale revenues from sales to non-affiliates increased \$38.4 million, or 15.0%, in 2013 compared to 2012 as a result of a \$20.5 million increase in base revenues primarily resulting from a wholesale base rate increase effective April 1, 2013 and a \$17.8 million increase in energy revenues, of which \$14.0 million was associated with higher fuel prices and \$3.8 million was associated with an increase in KWH sales.

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 \$72.4 million, or 208.3%, in 2014 compared to 2013 primarily due to a \$74.6 million increase in energy revenues of which \$69.3 million was associated with an increase in KWH sales and \$5.3 million was associated with higher prices, partially offset by a decrease in capacity revenues of \$2.2 million. Wholesale revenues from sales to affiliates increased \$18.4 million, or 112.0%, in 2013 compared to 2012 due to a \$1.3 million increase in capacity revenues and a \$17.1 million increase in energy revenues of which \$7.2 million was associated with higher prices and \$9.9 million was associated with an increase in KWH sales.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)
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Other operating revenues in 2014 increased \$0.7 million, or 4.2%, from 2013 primarily due to a \$1.3 million increase in transmission revenues, partially offset by a \$0.6 million decrease in microwave tower lease revenue and a \$0.2 million decrease in miscellaneous revenues from timber and easement sale proceeds. Other operating revenues in 2013 increased \$0.8 million, or 4.8%, from 2012 primarily due to a \$0.5 million increase in transmission revenues and a \$0.3 million increase in miscellaneous revenue from timber and easement sale proceeds.

Energy Sales

Changes in revenues are influenced heavily by the change in the volume of energy sold from year to year. KWH sales for 2014 and the percent change from the prior year were as follows:

	Total KWHs	Total KWH Percent Change		Weather-Adjusted Percent Change	
	2014	2014	2013	2014	2013
	<i>(in millions)</i>				
Residential	2,126	1.8%	2.0%	(2.3)%	—%
Commercial	2,859	(0.2)	(1.7)	0.1	(1.1)
Industrial	4,943	4.3	0.8	4.3	0.8
Other	41	1.1	4.0	1.1	4.0
Total retail	9,969	2.4	0.3%	1.6 %	0.1%
Wholesale					
Non-affiliated	4,191	6.7	2.9		
Affiliated	2,900	211.4	62.8		
Total wholesale	7,091	45.9	10.7		
Total energy sales	17,060	16.9%	3.5%		

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.

Residential energy sales increased 1.8% in 2014 compared to 2013 due to colder weather in the first quarter 2014 and warmer weather in the second and third quarters 2014 as compared to the corresponding periods in 2013. Weather-adjusted residential energy sales decreased 2.3% in 2014 compared to 2013 due to lower average usage per customer. Household income, one of the primary drivers of residential customer usage, was flat in 2014. Residential energy sales increased 2.0% in 2013 compared to 2012 due to less mild weather and a slight increase in the number of residential customers in 2013 compared to 2012.

Commercial energy sales decreased 1.7% in 2013 compared to 2012 due to decreased economic activity in 2013 compared to 2012.

Industrial energy sales increased 4.3% in 2014 compared to 2013 due to increased production related to expanded operation by many industrial customers. Industrial energy sales increased 0.8% in 2013 compared to 2012 due to increased usage by larger industrial customers as well as expansions by existing customers.

Wholesale energy sales to non-affiliates increased 6.7% in 2014 compared to 2013 primarily due to increased opportunity sales to the external market as a result of lower system prices. Wholesale energy sales to non-affiliates increased 2.9% in 2013 compared to 2012 primarily due to increased KWH sales to rural electric cooperative associations and municipalities located in southeastern Mississippi resulting from less mild weather in 2013 compared to 2012.

Wholesale sales to non-affiliates will vary depending on fuel prices, the market prices of wholesale energy compared to the cost of the Company and 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.

Wholesale energy sales to affiliates increased 211.4% in 2014 compared to 2013 primarily due to an increase in the Company's generation, resulting in more energy available to sell to affiliate companies. Wholesale energy sales to affiliates increased 62.8% in 2013 compared to 2012 primarily due to an increase in the Company's generation, resulting in more energy available to sell to affiliate companies.

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Fuel and Purchased Power Expenses

Fuel costs constitute the single largest expense 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:

	2014	2013	2012
Total generation (<i>millions of KWHs</i>)	16,881	13,721	12,750
Total purchased power (<i>millions of KWHs</i>)	886	1,559	1,961
Sources of generation (<i>percent</i>) –			
Coal	42	36	26
Gas	58	64	74
Cost of fuel, generated (<i>cents per net KWH</i>) –			
Coal	3.96	4.97	5.09
Gas	3.37	3.16	2.90
Average cost of fuel, generated (<i>cents per net KWH</i>)	3.64	3.87	3.53
Average cost of purchased power (<i>cents per net KWH</i>)	4.85	3.10	2.81

Fuel and purchased power expenses were \$616.9 million in 2014, an increase of \$77.3 million, or 14.3%, above the prior year costs. The increase was primarily due to a \$114.4 million increase in the total volume of KWHs generated, offset by a \$37.1 million decrease in the cost of fuel and purchased power. Fuel and purchased power expenses were \$539.6 million in 2013, an increase of \$73.2 million, or 15.7%, above the prior year costs. The increase was primarily due to a \$55.1 million increase in the total volume of KWHs generated and purchased and an \$18.1 million increase in the cost of fuel 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" and Note 1 to the financial statements under "Fuel Costs" for additional information.

Fuel

Fuel expense increased \$82.7 million, or 16.8%, in 2014 compared to 2013. The increase was the result of a 24.5% increase in the volume of KWHs generated in 2014, partially offset by a 5.9% decrease in the average cost of fuel per KWH generated. Fuel expense increased \$80.0 million, or 19.5%, in 2013 compared to 2012. The increase was the result of a 9.6% increase in the average cost of fuel per KWH generated and a 9.0% increase in the volume of KWHs generated resulting from increased non-territorial sales in 2013 compared to 2012.

Purchased Power - Non-Affiliates

Purchased power expense from non-affiliates increased \$12.1 million, or 210.3%, in 2014 compared to 2013. The increase was primarily the result of a 276.7% increase in the average cost per KWH purchased, partially offset by a 17.6% decrease in the volume of KWHs purchased. Purchased power expense from non-affiliates increased \$0.5 million, or 10.2%, in 2013 compared to 2012. The increase was the result of an 8.0% increase in the average cost per KWH purchased and a 2.0% increase in the volume of KWHs purchased. The increase in the average cost per KWH purchased was due to a higher marginal cost of fuel. The increase in the volume of KWHs purchased was due to a lower market cost of available energy compared to the cost of generation.

Energy purchases from non-affiliates will vary depending on the market prices of wholesale energy 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.

Purchased Power - Affiliates

Purchased power expense from affiliates decreased \$17.5 million, or 41.1%, in 2014 compared to 2013. The decrease in 2014 was primarily the result of a 49.5% decrease in the volume of KWHs purchased, offset by a 16.8% increase in the average cost per KWH purchased compared to 2013. Purchased power expense from affiliates decreased \$7.3 million, or 14.7%, in 2013 compared to 2012. The decrease was primarily the result of a 24.7% decrease in the volume of KWHs purchased, partially offset by a 13.2% increase in the average cost per KWH purchased compared to 2012.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)
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Energy purchases from affiliates will vary depending on demand for energy and the availability and cost of generating resources at each company within the Southern Company system. 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 increased \$17.3 million, or 6.8%, in 2014 compared to 2013 primarily due to a \$14.1 million increase in employee compensation and benefit expenses and a \$6.5 million increase in generation maintenance expenses. These increases in 2014 were partially offset by a \$2.0 million decrease in transmission expenses primarily related to overhead line maintenance and vegetation management, and a \$0.8 million decrease in customer accounting expenses primarily due to uncollectibles.

Other operations and maintenance expenses increased \$24.7 million, or 10.8%, in 2013 compared to 2012 primarily due to a \$9.8 million increase in generation maintenance expenses for several planned outages, a \$7.6 million increase in administrative and general expenses related to pension expense, a \$4.2 million increase in transmission maintenance expenses, a \$2.8 million increase in customer accounting primarily due to uncollectibles, and a \$2.5 million increase in distribution expenses related to overhead line maintenance and vegetation management. These increases were partially offset by a \$2.7 million decrease in labor expenses.

Depreciation and Amortization

Depreciation and amortization increased \$5.7 million, or 6.3%, in 2014 compared to 2013 primarily due to a \$4.2 million increase related to the reversal of a regulatory deferral associated with the Kemper IGCC municipal franchise taxes, a \$2.2 million increase in depreciation related to an increase in assets in service, and a \$2.2 million increase resulting from a regulatory deferral associated with the purchase of Plant Daniel Units 3 and 4. These increases were partially offset by a \$3.7 million decrease associated with a wholesale revenue requirement adjustment.

Depreciation and amortization increased \$4.9 million, or 5.7%, in 2013 compared to 2012 primarily due to a \$4.3 million increase in ECO Plan amortization, a \$2.0 million increase in amortization resulting from a regulatory deferral associated with the purchase of Plant Daniel Units 3 and 4, and a \$1.6 million increase in depreciation resulting from an increase in plant in service. These increases were partially offset by a \$2.1 million decrease in amortization primarily resulting from a regulatory deferral associated with the Kemper IGCC and a \$0.7 million decrease in amortization resulting from a regulatory deferral associated with the capital lease related to the Kemper IGCC air separation unit.

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

Taxes Other Than Income Taxes

Taxes other than income taxes decreased \$1.5 million, or 2.0%, in 2014 compared to 2013 primarily as a result of a \$6.0 million decrease in franchise taxes, partially offset by a \$3.2 million increase in ad valorem taxes and a \$1.3 million increase in payroll taxes. Taxes other than income taxes increased \$1.2 million, or 1.6%, in 2013 compared to 2012 primarily as a result of a \$3.5 million increase in franchise taxes, partially offset by a \$2.1 million decrease in ad valorem taxes and a \$0.2 million decrease in payroll taxes.

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

Estimated probable losses on the Kemper IGCC of \$868.0 million and \$1.1 billion were recorded in 2014 and 2013, respectively, to reflect revisions of estimated costs expected to be incurred on the construction of the Kemper IGCC in excess of the \$2.88 billion cost cap established by the Mississippi PSC, net of the DOE Grants and excluding the Cost Cap Exceptions.

See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information.

Allowance for Equity Funds Used During Construction

AFUDC equity increased \$14.8 million, or 12.2%, in 2014 as compared to 2013 and \$56.8 million, or 87.7%, in 2013 as compared to 2012. These increases in 2014 and 2013 were primarily due to CWIP related to the Company's Kemper IGCC. See ACCOUNTING POLICIES – "Application of Critical Accounting Policies and Estimates – Allowance for Funds Used During

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Construction" and Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information regarding the Kemper IGCC.

Interest Expense, Net of Amounts Capitalized

Interest expense, net of amounts capitalized increased \$8.8 million, or 24.2%, in 2014 compared to 2013, primarily due to an \$11.0 million increase in interest expense resulting from the receipt of \$75.0 million and \$50.0 million interest-bearing refundable deposits from SMEPA in January 2014 and October 2014, respectively, related to its pending purchase of an undivided interest in the Kemper IGCC, an \$8.2 million increase in interest expense on the regulatory liability related to the Kemper IGCC rate recovery, a \$4.6 million increase in interest expense primarily associated with the issuances of long-term debt in 2014, and a \$2.8 million increase in other interest expense. These increases in 2014 over the prior year were partially offset by a \$14.6 million increase in capitalized interest resulting from carrying costs associated with the Kemper IGCC and a \$3.2 million decrease in interest expense primarily associated with the redemption of long-term debt in late 2013.

Interest expense, net of amounts capitalized decreased \$4.4 million, or 10.7%, in 2013 compared to 2012, primarily due to a \$20.1 million increase in capitalized interest resulting from AFUDC debt associated with the Kemper IGCC and a \$2.6 million decrease in interest expense associated with the redemption of long-term debt in 2013. These decreases in 2013 from the prior year were partially offset by a \$12.2 million increase in interest expense primarily associated with the issuances of new long-term debt in 2013, a \$4.0 million increase in interest expense resulting from the receipt of a \$150.0 million interest-bearing refundable deposit from SMEPA in March 2012 related to its pending purchase of an undivided interest in the Kemper IGCC, and a \$2.7 million increase in interest expense in the regulatory liability related to the Kemper IGCC rate recovery.

See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle – Proposed Sale of Undivided Interest to SMEPA" for more information.

Other Income (Expense), Net

Other income (expense), net decreased \$8.1 million, or 133.7%, in 2014 compared to 2013 primarily due to \$7.0 million associated with the Sierra Club settlement and a \$1.1 million increase in consulting fees. Other income (expense), net decreased \$7.3 million in 2013 compared to 2012 primarily due to a \$5.9 million increase in consulting fees. See "Other Matters – Sierra Club Settlement Agreement" herein and Note 3 to the financial statements under "Other Matters – Sierra Club Settlement Agreement" for additional information.

Income Taxes (Benefit)

Income taxes (benefit) increased \$82.6 million, or 22.5%, in 2014 compared to 2013 and decreased \$388.4 million in 2013 compared to 2012 primarily resulting from the reduction in pre-tax losses related to the estimated probable losses on the Kemper IGCC.

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 electricity to retail customers within its traditional service area 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 – Electric Utility Regulation" herein, and Note 3 to the financial statements under "Retail Regulatory Matters" 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 selling electricity. These factors include the Company's ability to prevail against legal challenges associated with the Kemper IGCC, recover its prudently-incurred costs in a timely manner during a time of increasing costs and the completion and subsequent operation of the Kemper IGCC and the Plant Daniel scrubber project as well as other ongoing construction projects.

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Future earnings in the near term will depend, in part, upon maintaining and growing sales which are subject to a number of factors. These factors include weather, competition, new energy contracts with other utilities, 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. Changes in regional and global economic conditions may impact sales for the Company, as the pace of the economic recovery remains uncertain. The timing and extent of the economic recovery will impact growth and may impact future earnings.

Environmental Matters

Compliance costs related to federal and state environmental statutes and regulations could affect earnings if such costs cannot continue to be fully recovered in rates on a timely basis or through market-based contracts. Environmental compliance spending over the next several years may differ materially from the amounts estimated. The timing, specific requirements, and estimated costs could change as environmental statutes and regulations are adopted or modified. Further, higher 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. See Note 3 to the financial statements under "Environmental Matters" for additional information.

New Source Review Actions

As part of a nationwide enforcement initiative against the electric utility industry which began in 1999, the EPA brought civil enforcement actions in federal district court against Alabama Power alleging violations of the New Source Review provisions of the Clean Air Act at certain coal-fired electric generating units, including a unit co-owned by the Company. An adverse outcome could require substantial capital expenditures that cannot be determined at this time and could possibly require payment of substantial penalties. See Note 3 to the financial statements under "Environmental Matters – New Source Review Actions" for additional information. The ultimate outcome of these matters cannot be determined at this time.

Environmental Statutes and Regulations

General

The Company's operations are subject to extensive regulation by state and federal environmental agencies under a variety of statutes and regulations governing environmental media, including air, water, and land resources. Applicable statutes include the Clean Air Act; the Clean Water Act; the Comprehensive Environmental Response, Compensation, and Liability Act; the Resource Conservation and Recovery Act; the Toxic Substances Control Act; the Emergency Planning & Community Right-to-Know Act; the Endangered Species Act; and related federal and state regulations. Compliance with these environmental requirements involves significant capital and operating costs, a major portion of which is expected to be recovered through existing ratemaking provisions. Through 2014, the Company had invested approximately \$523 million in environmental capital retrofit projects to comply with these requirements, with annual totals of approximately \$118 million, \$104 million, and \$52 million for 2014, 2013, and 2012, respectively. The Company expects that capital expenditures to comply with environmental statutes and regulations will total approximately \$154 million from 2015 through 2017, with annual totals of approximately \$94 million, \$25 million, and \$35 million for 2015, 2016, and 2017, respectively. These estimated expenditures do not include any potential compliance costs that may arise from the EPA's proposed rules that would limit CO₂ emissions from new, existing, and modified or reconstructed fossil-fuel-fired electric generating units. See "Global Climate Issues" for additional information.

The Company's ultimate environmental compliance strategy, including potential unit retirement and replacement decisions, and future environmental capital expenditures will be affected by the final requirements of new or revised environmental regulations and regulations relating to global climate change that are promulgated, including the proposed environmental regulations described below; the outcome of any legal challenges to the environmental rules; the cost, availability, and existing inventory of emissions allowances; and the Company's fuel mix. Compliance costs may arise from existing unit retirements, installation of additional environmental controls, closure and monitoring of CCR facilities, and adding or changing fuel sources for certain existing units. The ultimate outcome of these matters cannot be determined at this time. See Note 3 to the financial statements under "Other Matters – Sierra Club Settlement Agreement" for additional information.

Compliance with any new federal or state legislation or regulations relating to air quality, water, CCR, global climate change, or other environmental and health concerns could significantly affect the Company. Although new or revised environmental legislation or regulations could affect many areas of the Company's operations, the full impact of any such changes cannot be determined at this time. Additionally, many of the Company's 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.

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Air Quality

Compliance with the Clean Air Act and resulting regulations has been and will continue to be a significant focus for the Company. Since 1990, the Company has spent approximately \$393 million in reducing and monitoring emissions pursuant to the Clean Air Act. Additional controls are currently planned or under consideration to further reduce air emissions, maintain compliance with existing regulations, and meet new requirements.

In 2012, the EPA finalized the Mercury and Air Toxics Standards (MATS) rule, which imposes stringent emissions limits for acid gases, mercury, and particulate matter on coal- and oil-fired electric utility steam generating units. Compliance for existing sources is required by April 16, 2015 up to April 16, 2016 for affected units for which extensions have been granted. On November 25, 2014, the U.S. Supreme Court granted a petition for review of the final MATS rule.

The EPA regulates ground level ozone concentrations through implementation of an eight-hour ozone National Ambient Air Quality Standard (NAAQS). On December 17, 2014, the EPA published a proposed rule to further reduce the current eight-hour ozone standard. The EPA is required by federal court order to complete this rulemaking by October 1, 2015. Finalization of a lower eight-hour ozone standard could result in the designation of new ozone nonattainment areas within the Company's service territory.

Final revisions to the NAAQS for sulfur dioxide (SO₂), which established a new one-hour standard, became effective in 2010. No areas within the Company's service territory have been designated as nonattainment under this rule. However, the EPA has announced plans to make additional designation decisions for SO₂ in the future, which could result in nonattainment designations for areas within the Company's service territory. Implementation of the revised SO₂ standard could require additional reductions in SO₂ emissions and increased compliance and operational costs.

On February 13, 2014, the EPA proposed to delete from the Alabama State Implementation Plan (SIP) the Alabama opacity rule that the EPA approved in 2008, which provides operational flexibility to affected units, including units co-owned by the Company. In March 2013, the U.S. Court of Appeals for the Eleventh Circuit ruled in favor of Alabama Power and the Company and vacated an earlier attempt by the EPA to rescind its 2008 approval. The EPA's latest proposal characterizes the proposed deletion as an error correction within the meaning of the Clean Air Act. Alabama Power and the Company believe this interpretation of the Clean Air Act to be incorrect. If finalized, this proposed action could affect unit availability and result in increased operations and maintenance costs for affected units, including units co-owned by the Company.

The Company's service territory is subject to the requirements of the Cross State Air Pollution Rule (CSAPR). CSAPR is an emissions trading program that limits SO₂ and nitrogen oxide emissions from power plants in 28 states in two phases, with Phase I beginning in 2015 and Phase II beginning in 2017. In 2012, the U.S. Court of Appeals for the District of Columbia Circuit vacated CSAPR in its entirety, but on April 29, 2014, the U.S. Supreme Court overturned that decision and remanded the case back to the U.S. Court of Appeals for the District of Columbia Circuit for further proceedings. The U.S. Court of Appeals for the District of Columbia Circuit granted the EPA's motion to lift the stay of the rule, and the first phase of CSAPR took effect on January 1, 2015.

The EPA finalized the Clean Air Visibility Rule (CAVR) in 2005, with a goal of restoring natural visibility conditions in certain areas (primarily national parks and wilderness areas) by 2064. The rule involves the application of best available retrofit technology to certain sources, including fossil fuel-fired generating facilities, built between 1962 and 1977 and any additional emissions reductions necessary for each designated area to achieve reasonable progress toward the natural visibility conditions goal by 2018 and for each 10-year period thereafter.

In 2012, the EPA published proposed revisions to the New Source Performance Standard (NSPS) for Stationary Combustion Turbines (CTs). If finalized as proposed, the revisions would apply the NSPS to all new, reconstructed, and modified CTs (including CTs at combined cycle units), during all periods of operation, including startup and shutdown, and alter the criteria for determining when an existing CT has been reconstructed.

In February 2013, the EPA proposed a rule that would require certain states to revise the provisions of their SIPs relating to the regulation of excess emissions at industrial facilities, including fossil fuel-fired generating facilities, during periods of startup, shut-down, or malfunction (SSM). The EPA proposed to supplement the 2013 proposed rule on September 17, 2014, making it more stringent. The EPA has entered into a settlement agreement requiring it to finalize the proposed rule by May 22, 2015. The proposed rule would require states subject to the rule (including Alabama and Mississippi) to revise their SSM provisions within 18 months after issuance of the final rule.

The Company has developed and continually updates a comprehensive environmental compliance strategy to assess compliance obligations associated with the current and proposed environmental requirements discussed above. The impacts of the eight-hour ozone and SO₂ NAAQS, the Alabama opacity rule, CSAPR, CAVR, the MATS rule, the NSPS for CTs, and the SSM rule on the

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Company cannot be determined at this time and will depend on the specific provisions of the proposed and final rules, the resolution of pending and future legal challenges, and/or the development and implementation of rules at the state level. These regulations could result in significant additional compliance costs that could affect future unit retirement and replacement decisions and results of operations, cash flows, and financial condition if such costs are not recovered through regulated rates.

See Note 3 to the financial statements under "Retail Regulatory Matters – Environmental Compliance Overview Plan" and "Other Matters – Sierra Club Settlement Agreement" for additional information.

Water Quality

The EPA's final rule establishing standards for reducing effects on fish and other aquatic life caused by new and existing cooling water intake structures at existing power plants and manufacturing facilities became effective on October 14, 2014. The effect of this final rule will depend on the results of additional studies and implementation of the rule by regulators based on site-specific factors. The ultimate impact of this rule will also depend on the outcome of ongoing legal challenges and cannot be determined at this time.

In June 2013, the EPA published a proposed rule which requested comments on a range of potential regulatory options for addressing revised technology-based limits for certain wastestreams from steam electric power plants and best management practices for CCR surface impoundments. The EPA has entered into a consent decree requiring it to finalize revisions to the steam electric effluent guidelines by September 30, 2015. The ultimate impact of the rule will also depend on the specific technology requirements of the final rule and the outcome of any legal challenges and cannot be determined at this time.

On April 21, 2014, the EPA and the U.S. Army Corps of Engineers jointly published a proposed rule to revise the regulatory definition of waters of the U.S. for all Clean Water Act (CWA) programs, which would significantly expand the scope of federal jurisdiction under the CWA. In addition, the rule as proposed could have significant impacts on economic development projects which could affect customer demand growth. The ultimate impact of the proposed rule will depend on the specific requirements of the final rule and the outcome of any legal challenges and cannot be determined at this time. If finalized as proposed, this rule could significantly increase permitting and regulatory requirements and costs associated with the siting of new facilities and the installation, expansion, and maintenance of transmission and distribution lines.

These proposed and final water quality regulations could result in significant additional capital expenditures and compliance costs that could affect future unit retirement and replacement decisions. Also, results of operations, cash flows, and financial condition could be significantly impacted if such costs are not recovered through regulated rates.

Coal Combustion Residuals

The Company currently manages two electric generating plants in Mississippi and is also part owner of a plant located in Alabama, each with onsite CCR storage units consisting of landfills and surface impoundments (CCR Units). In addition to on-site storage, the Company also sells a portion of its CCR to third parties for beneficial reuse. Individual states regulate CCR and the States of Mississippi and Alabama each have their own regulatory requirements. The Company has an inspection program in place to assist in maintaining the integrity of its coal ash surface impoundments.

On December 19, 2014, the EPA issued the Disposal of Coal Combustion Residuals from Electric Utilities final rule (CCR Rule), but has not yet published it in the Federal Register. The CCR Rule will regulate the disposal of CCR, including coal ash and gypsum, as non-hazardous solid waste in CCR Units at active generating power plants. The CCR Rule does not mandate closure of CCR Units, but includes minimum criteria for active and inactive surface impoundments containing CCR and liquids, lateral expansions of existing units, and active landfills. Failure to meet the minimum criteria can result in the mandated closure of a CCR Unit. Although the EPA does not require individual states to adopt the final criteria, states have the option to incorporate the federal criteria into their state solid waste management plans in order to regulate CCR in a manner consistent with federal standards. The EPA's final rule continues to exclude the beneficial use of CCR from regulation.

The ultimate impact of the CCR Rule cannot be determined at this time and will depend on the Company's ongoing review of the CCR Rule, the results of initial and ongoing minimum criteria assessments, and the outcome of legal challenges. The cost and timing of potential ash pond closure and ongoing monitoring activities that may be required in connection with the CCR Rule is also uncertain; however, the Company has developed a preliminary nominal dollar estimate of costs associated with closure and groundwater monitoring of ash ponds in place of approximately \$64 million and ongoing post-closure care of approximately \$12 million. The Company will record asset retirement obligations (ARO) for the estimated closure costs required under the CCR Rule during 2015. The Company's results of operations, cash flows, and financial condition could be significantly impacted if such costs are not recovered through regulated rates.

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Environmental Remediation

The Company must comply with other environmental laws and regulations that cover the handling and disposal of waste and releases of hazardous substances. Under these various laws and regulations, the Company could incur substantial costs to clean up properties. The Company conducts studies to determine the extent of any required cleanup and has recognized in its financial statements the costs to clean up known impacted sites. Amounts for cleanup and ongoing monitoring costs were not material for any year presented. The Company has authority from the Mississippi PSC to recover approved environmental compliance costs through its ECO clause. The Company may be liable for some or all required cleanup costs for additional sites that may require environmental remediation. See Note 3 to the financial statements under "Environmental Matters – Environmental Remediation" for additional information.

Global Climate Issues

In 2014, the EPA published three sets of proposed standards that would limit CO₂ emissions from new, existing, and modified or reconstructed fossil-fuel-fired electric generating units. On January 8, 2014, the EPA published proposed standards for new units, and, on June 18, 2014, the EPA published proposed standards governing existing units, known as the Clean Power Plan, and separate standards governing CO₂ emissions from modified and reconstructed units. The EPA's proposed Clean Power Plan establishes guidelines for states to develop plans to address CO₂ emissions from existing fossil fuel-fired electric generating units. The EPA's proposed guidelines establish state-specific interim and final CO₂ emission rate goals to be achieved between 2020 and 2029 and in 2030 and thereafter. The proposed guidelines and standards could result in operational restrictions and material compliance costs, including capital expenditures, which could affect future unit retirement and replacement decisions. The Company's results of operations, cash flows, and financial condition could be significantly impacted if such costs are not recovered through regulated rates or through market-based contracts.

The Southern Company system filed comments on the EPA's proposed Clean Power Plan on December 1, 2014. These comments addressed legal and technical issues in addition to providing a preliminary estimated cost of complying with the proposed guidelines utilizing one of the EPA's compliance scenarios. Costs associated with this proposal could be significant to the utility industry and the Southern Company system. However, the ultimate financial and operational impact of the proposed Clean Power Plan on the Southern Company system cannot be determined at this time and will depend upon numerous known and unknown factors. Some of the unknown factors include: the structure, timing, and content of the EPA's final guidelines; individual state implementation of these guidelines, including the potential that state plans impose different standards; additional rulemaking activities in response to legal challenges and related court decisions; the impact of future changes in generation and emissions-related technology and costs; the impact of future decisions regarding unit retirement and replacement, including the type and amount of any such replacement capacity; and the time periods over which compliance will be required.

Over the past several years, the U.S. Congress has also considered many proposals to reduce greenhouse gas emissions, mandate renewable or clean energy, and impose energy efficiency standards. Such proposals are expected to continue to be considered by the U.S. Congress. International climate change negotiations under the United Nations Framework Convention on Climate Change are also continuing.

The EPA's greenhouse gas reporting rule requires annual reporting of CO₂ equivalent emissions in metric tons for a company's operational control of facilities. Based on ownership or financial control of facilities, the Company's 2013 greenhouse gas emissions were approximately 10 million metric tons of CO₂ equivalent. The preliminary estimate of the Company's 2014 greenhouse gas emissions on the same basis is approximately 11 million metric tons of CO₂ equivalent. The level of greenhouse gas emissions from year to year will depend on the level of generation, the mix of fuel sources, and other factors.

FERC Matters

In May 2013, the FERC accepted a settlement agreement entered into by the Company with its wholesale customers which approved, among other things, the same regulatory treatment for tariff ratemaking as the treatment approved for retail ratemaking by the Mississippi PSC for certain items. The regulatory treatment includes (i) approval to establish a regulatory asset for the portion of non-capitalizable Kemper IGCC-related costs which have been and will continue to be incurred during the construction period for the Kemper IGCC, (ii) authorization to defer as a regulatory asset, for the 10-year period ending October 2021, the difference between the revenue requirement under the purchase option of Plant Daniel Units 3 and 4 (assuming a remaining 30-year life) and the revenue requirement assuming the continuation of the operating lease regulatory treatment with the accumulated deferred balance at the end of the deferral being amortized into wholesale rates over the remaining life of Plant Daniel Units 3 and 4, and (iii) authority to defer in a regulatory asset costs related to the retirement or partial retirement of generating units as a result of environmental compliance rules. See Note 3 to the financial statements under "FERC Matters" for more information.

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On March 31, 2014, the Company reached a settlement agreement with its wholesale customers and filed a request with the FERC for an increase in the MRA cost-based electric tariff. The settlement agreement, accepted by the FERC on May 20, 2014, provides that base rates under the MRA cost-based electric tariff will increase approximately \$10.1 million annually, with revised rates effective for services rendered beginning May 1, 2014.

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 the Kemper IGCC, 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 recovered through the Company's base rates. See Note 3 to the financial statements under "Retail Regulatory Matters" and "Integrated Coal Gasification Combined Cycle" 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 March 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. The ultimate outcome of this matter cannot be determined at this time.

Energy Efficiency

In July 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.

On June 3, 2014, the Mississippi PSC approved the Company's 2014 Energy Efficiency Quick Start Plan filing, which includes a portfolio of energy efficiency programs. On October 20, 2014, the Company filed a revised compliance filing, which proposed an increase of \$6.7 million in retail revenues for the period December 2014 through December 2015. The Mississippi PSC approved the revised filing on November 4, 2014.

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 projected revenue requirement, and the PEP lookback filing, which is filed after 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 Company received a letter from the MPUS disputing 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 May 2013, the MPUS contested the Company's PEP lookback filing for 2012, which indicated a refund due to customers of \$4.7 million. Unresolved matters related to certain costs included in the 2010 PEP lookback filing, which are currently under review, also impact the 2012 PEP lookback filing.

In March 2013, the Mississippi PSC approved the projected PEP filing for 2013, which resulted in a rate increase of 1.9%, or \$15.3 million, annually, effective March 19, 2013. The Company may be entitled to \$3.3 million in additional revenues related to 2013 as a result of the late implementation of the 2013 PEP rate increase.

On March 18, 2014, the Company submitted its annual PEP lookback filing for 2013, which indicated no surcharge or refund. On March 31, 2014, the Mississippi PSC suspended the filing to allow more time for review.

On June 3, 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.

The ultimate outcome of these matters 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 are scheduled to be placed in service in September and November 2015, respectively. These units are jointly owned by the Company and Gulf Power, with 50% ownership each. On August 1, 2014, the Company entered into a settlement agreement with

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the Sierra Club (Sierra Club Settlement Agreement) that, among other things, requires the Sierra Club to dismiss or withdraw all pending legal and regulatory challenges to the issuance of the CPCN to construct scrubbers on Plant Daniel Units 1 and 2. In addition, and consistent with the Company's ongoing evaluation of recent environmental rules and regulations, 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. 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, and cease burning coal and other solid fuel at Plant Greene County Units 1 and 2 (200 MWs) and begin operating those units solely on natural gas no later than April 2016. On August 28, 2014, the Chancery Court of Harrison County, Mississippi dismissed the Sierra Club's appeal related to the CPCN to construct scrubbers on Plant Daniel Units 1 and 2.

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. This request was made to minimize the potential rate impact to customers arising from pending and final environmental regulations which may require the premature retirement of some generating units. As of December 31, 2014, \$5.6 million of Plant Greene County costs and \$2.0 million of costs related to Plant Watson have been reclassified as a regulatory asset. These costs are expected to be recovered through the ECO plan and other existing cost recovery mechanisms. Additional costs associated with the remaining net book value of coal-related equipment will be reclassified to a regulatory asset at the time of retirement for Plants Watson and Greene County in 2015 and 2016, respectively. Approved regulatory asset costs will be amortized over a period to be determined by the Mississippi PSC. As a result, these decisions are not expected to have a material impact on the Company's financial statements.

See Note 3 to the financial statements under "Other Matters – Sierra Club Settlement Agreement" for additional information.

On February 25, 2015, the Company submitted its annual ECO filing for 2015, which indicated an annual increase in revenues of approximately \$8.1 million.

The ultimate outcome of these matters 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; the most recent filing occurred on November 17, 2014. On January 13, 2015, the Mississippi PSC approved the 2015 retail fuel cost recovery factor, effective January 21, 2015. The retail fuel cost recovery factor will result in an annual increase of approximately \$7.9 million. At December 31, 2014, the amount of under-recovered retail fuel costs included in the balance sheets was \$2.5 million compared to a \$14.5 million over-recovered balance at December 31, 2013.

The Company also has a wholesale MRA and a Market Based (MB) fuel cost recovery factor. Effective January 1, 2015, the wholesale MRA fuel rate decreased resulting in an annual decrease of \$1.1 million. Effective February 1, 2015, the wholesale MB fuel rate decreased, resulting in an annual decrease of \$0.1 million. At December 31, 2014, the amount of over-recovered wholesale MRA fuel costs included in the balance sheets was \$0.2 million compared to an over-recovered balance of \$7.3 million at December 31, 2013. At December 31, 2014, the amount of over-recovered wholesale MB fuel costs included in the balance sheets was immaterial compared to an over-recovered balance of \$0.3 million at December 31, 2013. In addition, at December 31, 2014, the amount of over-recovered MRA emissions allowance cost included in the balance sheets was \$0.3 million compared to a \$3.8 million under-recovered balance at December 31, 2013. 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 May 6, 2014, the Mississippi PSC approved the Company's annual ad valorem tax adjustment factor filing for 2014, in which the Company requested an annual rate increase of 0.38%, or \$3.6 million in annual retail revenues, primarily due to an increase in property tax rates.

See RESULTS OF OPERATIONS – "Taxes Other Than Income Taxes" herein for additional information.

Baseload Act

In 2008, the Baseload Act was signed by the Governor of Mississippi. The Baseload Act authorizes, but does not require, the Mississippi PSC to adopt a cost recovery mechanism that includes in retail base rates, prior to and during construction, all or a

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portion of the prudently-incurred pre-construction and construction costs incurred by a utility in constructing a base load electric generating plant. Prior to the passage of the Baseload Act, such costs would traditionally be recovered only after the plant was placed in service. The Baseload Act also provides for periodic prudence reviews by the Mississippi PSC and prohibits the cancellation of any such generating plant without the approval of the Mississippi PSC. In the event of cancellation of the construction of the plant without approval of the Mississippi PSC, the Baseload Act authorizes the Mississippi PSC to make a public interest determination as to whether and to what extent the utility will be afforded rate recovery for costs incurred in connection with such cancelled generating plant. In the Court decision, the Court declined to rule on the constitutionality of the Baseload Act. See "Integrated Coal Gasification Combined Cycle – Rate Recovery of Kemper IGCC Costs" and " – 2015 Mississippi Supreme Court Decision" herein for additional information.

Integrated Coal Gasification Combined Cycle

Kemper IGCC Overview

Construction of the Kemper IGCC is nearing completion and start-up activities will continue until the Kemper IGCC is placed in service. The Kemper IGCC will utilize an IGCC technology with an output capacity of 582 MWs. The Kemper IGCC will 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 IGCC. The mine, operated by North American Coal Corporation, started commercial operation in June 2013. In connection with the Kemper IGCC, the Company constructed and plans to operate approximately 61 miles of CO₂ pipeline infrastructure for the planned transport of captured CO₂ for use in enhanced oil recovery.

Kemper IGCC Schedule and Cost Estimate

In 2012, the Mississippi PSC issued the 2012 MPSC CPCN Order, a detailed order confirming the CPCN originally approved by the Mississippi PSC in 2010 authorizing the acquisition, construction, and operation of the Kemper IGCC.

The certificated cost estimate of the Kemper IGCC included in the 2012 MPSC CPCN Order was \$2.4 billion, net of \$245.3 million of DOE Grants and excluding the cost of the lignite mine and equipment, the cost of the CO₂ pipeline facilities, and AFUDC related to the Kemper IGCC. 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 IGCC 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 IGCC in service on natural gas on August 9, 2014 and continues to focus on completing the remainder of the Kemper IGCC, including the gasifier and the gas clean-up facilities, for which the in-service date is currently expected to occur in the first half of 2016.

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Recovery of the Kemper IGCC costs subject to the cost cap and the Cost Cap Exceptions remain subject to review and approval by the Mississippi PSC. The Company's Kemper IGCC 2010 project estimate, current cost estimate (which includes the impacts of the Court's decision), and actual costs incurred as of December 31, 2014, as adjusted for the Court's decision, are as follows:

Cost Category	2010 Project Estimate ^(f)	Current Estimate	Actual Costs at 12/31/2014
		<i>(in billions)</i>	
Plant Subject to Cost Cap ^(a)	\$ 2.40	\$ 4.93	\$ 4.23
Lignite Mine and Equipment	0.21	0.23	0.23
CO ₂ Pipeline Facilities	0.14	0.11	0.10
AFUDC ^{(b)(c)}	0.17	0.63	0.45
Combined Cycle and Related Assets Placed in Service – Incremental ^(d)	—	0.02	0.00
General Exceptions	0.05	0.10	0.07
Deferred Costs ^{(c)(e)}	—	0.18	0.12
Total Kemper IGCC^{(a)(c)}	\$ 2.97	\$ 6.20	\$ 5.20

- (a) The 2012 MPSC CPCN Order approved a construction cost cap of up to \$2.88 billion, net of the DOE Grants and excluding the Cost Cap Exceptions. The Current Estimate and Actual Costs include non-incremental operating and maintenance costs related to the combined cycle and associated common facilities placed in service on August 9, 2014 that are subject to the \$2.88 billion cost cap and excludes post-in-service costs for the lignite mine. See "Rate Recovery of Kemper IGCC Costs – 2013 MPSC Rate Order" for additional information.
- (b) The Company's original estimate included recovery of financing costs during construction rather than the accrual of AFUDC. This approach was not approved by the Mississippi PSC in 2012 as described in "Rate Recovery of Kemper IGCC Costs."
- (c) Amounts in the Current Estimate reflect estimated costs through March 31, 2016.
- (d) Incremental operating and maintenance costs related to the combined cycle and associated common facilities placed in service on August 9, 2014, net of costs related to energy sales. See "Rate Recovery of Kemper IGCC Costs – 2013 MPSC Rate Order" for additional information.
- (e) The 2012 MPSC CPCN Order approved deferral of non-capital Kemper IGCC-related costs during construction as described in "Rate Recovery of Kemper IGCC Costs – Regulatory Assets and Liabilities."
- (f) The 2010 Project Estimate is the certificated cost estimate adjusted to include the certificated estimate for the CO₂ pipeline facilities which was approved in 2011 by the Mississippi PSC.

Of the total costs, including post-in-service costs for the lignite mine, incurred as of December 31, 2014, \$3.04 billion was included in property, plant, and equipment (which is net of the DOE Grants and estimated probable losses of \$2.05 billion), \$1.8 million in other property and investments, \$44.7 million in fossil fuel stock, \$32.5 million in materials and supplies, \$147.7 million in other regulatory assets, \$11.6 million in other deferred charges and assets, and \$23.6 million in AROs in the balance sheet, with \$1.1 million previously expensed.

The Company does not intend to seek any rate recovery or joint owner contributions for any costs related to the construction of the Kemper IGCC that exceed the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions. The Company recorded pre-tax charges to income for revisions to the cost estimate of \$868.0 million (\$536.0 million after tax), \$1.10 billion (\$680.5 million after tax), and \$78.0 million (\$48.2 million after tax) in 2014, 2013 and 2012, respectively. The increases to the cost estimate in 2014 primarily reflected costs related to extension of the project's schedule to ensure the required time for start-up activities and operational readiness, completion of construction, additional resources during start-up, and ongoing construction support during start-up and commissioning activities. The current estimate includes costs through March 31, 2016. Any further extension of the in-service date is currently estimated to result in additional base costs of approximately \$25 million to \$30 million per month, which includes maintaining necessary levels of start-up labor, materials, and fuel, as well as operational resources required to execute start-up and commissioning activities. Any further extension of the in-service date with respect to the Kemper IGCC would also increase costs for the Cost Cap Exceptions, which are not subject to the \$2.88 billion cost cap established by the Mississippi PSC. These costs include AFUDC, which is currently estimated to total approximately \$13 million per month, as well as carrying costs and operating expenses on Kemper IGCC assets placed in service and consulting and legal fees, which are being deferred as regulatory assets and are estimated to total approximately \$7 million per month.

Any further cost increases and/or extensions of the in-service date with respect to the Kemper IGCC may result from factors including, but not limited to, labor costs and productivity, adverse weather conditions, shortages and inconsistent quality of equipment, materials, and labor, contractor or supplier delay, non-performance under construction or other agreements,

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operational readiness, including specialized operator training and required site safety programs, unforeseen engineering or design problems, start-up activities for this first-of-a-kind technology (including major equipment failure and system integration), and/or operational performance (including additional costs to satisfy any operational parameters ultimately adopted by the Mississippi PSC). In subsequent periods, any further changes in the estimated costs to complete construction and start-up of the Kemper IGCC subject to the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions, will be reflected in the Company's statements of operations and these changes could be material.

Rate Recovery of Kemper IGCC Costs

See "FERC Matters" for additional information regarding the Company's MRA cost-based tariff relating to recovery of a portion of the Kemper IGCC costs from the Company's wholesale customers. Rate recovery of the retail portion of the Kemper IGCC is subject to the jurisdiction of the Mississippi PSC. See Note 3 to the financial statements under "Retail Regulatory Matters – Baseload Act" for additional information. See "Income Tax Matters" herein for additional tax information related to the Kemper IGCC.

The ultimate outcome of the rate recovery matters discussed herein, including the resolution of legal challenges, determinations of prudence, and the specific manner of recovery of prudently-incurred costs, cannot be determined at this time, but could have a material impact on the Company's results of operations, financial condition, and liquidity.

2012 MPSC CPCN Order

The 2012 MPSC CPCN Order included provisions relating to both the Company's recovery of financing costs during the course of construction of the Kemper IGCC and the Company's recovery of costs following the date the Kemper IGCC is placed in service. With respect to recovery of costs following the in-service date of the Kemper IGCC, the 2012 MPSC CPCN Order provided for the establishment of operational cost and revenue parameters based upon assumptions in the Company's petition for the CPCN. The Company expects the Mississippi PSC to apply operational parameters in connection with the evaluation of the Rate Mitigation Plan (defined below) and other related proceedings during the operation of the Kemper IGCC. To the extent the Mississippi PSC determines the Kemper IGCC does not meet the operational parameters ultimately adopted by the Mississippi PSC or the Company incurs additional costs to satisfy such parameters, there could be a material adverse impact on the Company's financial statements.

2013 Settlement Agreement

In January 2013, the Company entered into a settlement agreement with the Mississippi PSC that, among other things, established the process for resolving matters regarding cost recovery related to the Kemper IGCC (2013 Settlement Agreement). Under the 2013 Settlement Agreement, the Company agreed to limit the portion of prudently-incurred Kemper IGCC costs to be included in retail rate base to the \$2.4 billion certificated cost estimate, plus the Cost Cap Exceptions, but excluding AFUDC, and any other costs permitted or determined to be excluded from the \$2.88 billion cost cap by the Mississippi PSC. The 2013 Settlement Agreement also allowed the Company to secure alternate financing for costs not otherwise recovered in any Mississippi PSC rate proceedings contemplated by the 2013 Settlement Agreement. The Court found the 2013 Settlement Agreement unenforceable due to a lack of public notice for the related proceedings. See "2015 Mississippi Supreme Court Decision" below for additional information.

Legislation to authorize a multi-year rate plan and legislation to provide for alternate financing through securitization of up to \$1.0 billion of prudently-incurred costs was enacted into law in February 2013. The Company's intent under the 2013 Settlement Agreement was to securitize (1) prudently-incurred costs in excess of the certificated cost estimate and up to the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions, (2) accrued AFUDC, and (3) other prudently-incurred costs, which include carrying costs from the estimated in-service date until securitization is finalized and other costs not included in the Rate Mitigation Plan as approved by the Mississippi PSC.

The Court's decision did not impact the Company's ability to utilize alternate financing through securitization, the 2012 MPSC CPCN Order, or the February 2013 legislation. See "2015 Mississippi Supreme Court Decision" below for additional information.

2013 MPSC Rate Order

Consistent with the terms of the 2013 Settlement Agreement, in March 2013, the Mississippi PSC issued the 2013 MPSC Rate Order approving retail rate increases of 15% effective March 19, 2013 and 3% effective January 1, 2014, which collectively were designed to collect \$156 million annually beginning in 2014. For the period from March 2013 through December 31, 2014, \$257.2 million had been collected primarily to be used to mitigate customer rate impacts after the Kemper IGCC is placed in service.

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Because the 2013 MPSC Rate Order did not provide for the inclusion of CWIP in rate base as permitted by the Baseload Act, the Company continues to record AFUDC on the Kemper IGCC through the in-service date. The Company will not record AFUDC on any additional costs of the Kemper IGCC that exceed the \$2.88 billion cost cap, except for Cost Cap Exception amounts. The Company will continue to record AFUDC and collect and defer the approved rates through the in-service date until directed to do otherwise by the Mississippi PSC.

On August 18, 2014, the Company provided an analysis of the costs and benefits of placing the combined cycle and the associated common facilities portion of the Kemper IGCC in service, including the expected accounting treatment. The Company's analysis requested, among other things, confirmation of the Company's accounting treatment by the Mississippi PSC of the continued collection of rates as prescribed by the 2013 MPSC Rate Order, with the current recognition as revenue of the related equity return on all assets placed in service and the deferral of all remaining rate collections under the 2013 MPSC Rate Order to a regulatory liability account. See "2015 Mississippi Supreme Court Decision" for additional information regarding the decision of the Court which would discontinue the collection of, and require the refund of, all amounts previously collected under the 2013 MPSC Rate Order.

In addition, the Company's August 18, 2014 filing with the Mississippi PSC requested confirmation of the Company's accounting treatment by the Mississippi PSC of the continued accrual of AFUDC through the in-service date of the remainder of the Kemper IGCC and the deferral of operating costs for the combined cycle as regulatory assets. Under the Company's proposal, non-incremental costs that would have been incurred whether or not the combined cycle was placed in service would be included in a regulatory asset and would continue to be subject to the \$2.88 billion cost cap. Additionally, incremental costs that would not have been incurred if the combined cycle had not gone into service would be included in a regulatory asset and would not be subject to the cost cap because these costs are incurred to support operation of the combined cycle. All energy revenues associated with the combined cycle variable operating and maintenance expenses would be credited to this regulatory asset. See "Regulatory Assets and Liabilities" for additional information. Any action by the Mississippi PSC that is inconsistent with the treatment requested by the Company could have a material impact on the results of operations, financial condition, and liquidity of the Company.

2015 Mississippi Supreme Court Decision

On February 12, 2015, the Court issued its decision in the legal challenge to the 2013 MPSC Rate Order filed by Thomas A. Blanton. The Court reversed the 2013 MPSC Rate Order based on, among other things, its findings that (1) the Mirror CWIP rate treatment was not provided for under the Baseload Act and (2) the Mississippi PSC should have determined the prudence of Kemper IGCC costs before approving rate recovery through the 2013 MPSC Rate Order. The Court also found the 2013 Settlement Agreement unenforceable due to a lack of public notice for the related proceedings. The Court's ruling remands the matter to the Mississippi PSC to (1) fix by order the rates that were in existence prior to the 2013 MPSC Rate Order, (2) fix no rate increases until the Mississippi PSC is in compliance with the Court's ruling, and (3) enter an order refunding amounts collected under the 2013 MPSC Rate Order. Through December 31, 2014, the Company had collected \$257.2 million through rates under the 2013 MPSC Rate Order. Any required refunds would also include carrying costs. The Court's decision will become legally effective upon the issuance of a mandate to the Mississippi PSC. Absent specific instruction from the Court, the Mississippi PSC will determine the method and timing of the refund. The Company is reviewing the Court's decision and expects to file a motion for rehearing which would stay the Court's mandate until either the case is reheard and decided or seven days after the Court issues its order denying the Company's request for rehearing. The Company is also evaluating its regulatory options.

Rate Mitigation Plan

In March 2013, the Company, in compliance with the 2013 MPSC Rate Order, filed a revision to the proposed rate recovery plan with the Mississippi PSC for the Kemper IGCC for cost recovery through 2020 (Rate Mitigation Plan), which is still under review by the Mississippi PSC. The revenue requirements set forth in the Rate Mitigation Plan assume the sale of a 15% undivided interest in the Kemper IGCC to SMEPA and utilization of bonus depreciation, which currently requires that the related long-term asset be placed in service in 2015. In the Rate Mitigation Plan, the Company proposed recovery of an annual revenue requirement of approximately \$156 million of Kemper IGCC-related operational costs and rate base amounts, including plant costs equal to the \$2.4 billion certificated cost estimate. The 2013 MPSC Rate Order, which increased rates beginning in March 2013, was integral to the Rate Mitigation Plan, which contemplates amortization of the regulatory liability balance at the in-service date to be used to mitigate customer rate impacts through 2020, based on a fixed amortization schedule that requires approval by the Mississippi PSC. Under the Rate Mitigation Plan, the Company proposed annual rate recovery to remain the same from 2014 through 2020, with the proposed revenue requirement approximating the forecasted cost of service for the period 2014 through 2020. Under the Company's proposal, to the extent the actual annual cost of service differs from the approved forecast for certain items, the difference would be deferred as a regulatory asset or liability, subject to accrual of carrying costs, and would be included in the next year's rate recovery calculation. If any deferred balance remains at the end of 2020, the Mississippi PSC

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would review the amount and, if approved, determine the appropriate method and period of disposition. See "Regulatory Assets and Liabilities" and "Income Tax Matters" for additional information.

To the extent that refunds of amounts collected under the 2013 MPSC Rate Order are required on a schedule different from the amortization schedule proposed in the Rate Mitigation Plan, the customer billing impacts proposed under the Rate Mitigation Plan would no longer be viable. See "2015 Mississippi Supreme Court Decision" above for additional information.

In the event that the Mirror CWIP regulatory liability is refunded to customers prior to the in-service date of the Kemper IGCC and is, therefore, not available to mitigate rate impacts under the Rate Mitigation Plan, the Mississippi PSC does not approve a refund schedule that facilitates rate mitigation, or the Company withdraws the Rate Mitigation Plan, the Company would seek rate recovery through alternate means, which could include a traditional rate case.

In addition to current estimated costs at December 31, 2014 of \$6.20 billion, the Company anticipates that it will incur additional costs after the Kemper IGCC in-service date until the Kemper IGCC cost recovery approach is finalized. These costs include, but are not limited to, regulatory costs and additional carrying costs which could be material. Recovery of these costs would be subject to approval by the Mississippi PSC.

Prudence Reviews

The Mississippi PSC's review of Kemper IGCC costs is ongoing. On August 5, 2014, the Mississippi PSC ordered that a consolidated prudence determination of all Kemper IGCC costs be completed after the entire project has been placed in service and has demonstrated availability for a reasonable period of time as determined by the Mississippi PSC and the MPUS. The Mississippi PSC has encouraged the parties to work in good faith to settle contested issues and the Company is working to reach a mutually acceptable resolution. As a result of the Court's decision, the Company intends to request that the Mississippi PSC reconsider its prudence review schedule. See "2015 Mississippi Supreme Court Decision" for additional information.

Regulatory Assets and Liabilities

Consistent with the treatment of non-capital costs incurred during the pre-construction period, the Mississippi PSC issued an accounting order in 2011 granting the Company the authority to defer all non-capital Kemper IGCC-related costs to a regulatory asset through the in-service date, subject to review of such costs by the Mississippi PSC. Such costs include, but are not limited to, carrying costs on Kemper IGCC assets currently placed in service, costs associated with Mississippi PSC and MPUS consultants, prudence costs, legal fees, and operating expenses associated with assets placed in service.

On August 18, 2014, the Company requested confirmation by the Mississippi PSC of the Company's authority to defer all operating expenses associated with the operation of the combined cycle subject to review of such costs by the Mississippi PSC. In addition, the Company is authorized to accrue carrying costs on the unamortized balance of such regulatory assets at a rate and in a manner to be determined by the Mississippi PSC in future cost recovery mechanism proceedings. As of December 31, 2014, the regulatory asset balance associated with the Kemper IGCC was \$147.7 million. The projected balance at March 31, 2016 is estimated to total approximately \$269.8 million. The amortization period of 40 years proposed by the Company for any such costs approved for recovery remains subject to approval by the Mississippi PSC.

The 2013 MPSC Rate Order approved retail rate increases of 15% effective March 19, 2013 and 3% effective January 1, 2014, which collectively were designed to collect \$156 million annually beginning in 2014. On February 12, 2015, the Court ordered the Mississippi PSC to refund Mirror CWIP and to fix by order the rates that were in existence prior to the 2013 MPSC Rate Order. The Company is deferring the collections under the approved rates in the Mirror CWIP regulatory liability until otherwise directed by the Mississippi PSC. The Company is also accruing carrying costs on the unamortized balance of the Mirror CWIP regulatory liability for the benefit of retail customers. As of December 31, 2014, the balance of the Mirror CWIP regulatory liability, including carrying costs, was \$270.8 million.

See "2015 Mississippi Supreme Court Decision" for additional information.

See Note 1 to the financial statements under "Regulatory Assets and Liabilities" for additional information.

Lignite Mine and CO₂ Pipeline Facilities

In conjunction with the Kemper IGCC, the Company will own the lignite mine and equipment and has acquired and will continue to acquire mineral reserves located around the Kemper IGCC 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 operating and managing the mining operations. The contract with Liberty Fuels is effective 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

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reclamation activities. In addition to the obligation to fund the reclamation activities, the Company currently provides 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 has constructed and will operate the CO₂ pipeline for the planned transport of captured CO₂ for use in enhanced oil recovery. The Company has entered into agreements with Denbury Onshore (Denbury), a subsidiary of Denbury Resources Inc., and Treetop Midstream Services, LLC (Treetop), an affiliate of Tellus Operating Group, LLC and a subsidiary of Tengrys, LLC, pursuant to which Denbury will purchase 70% of the CO₂ captured from the Kemper IGCC and Treetop will purchase 30% of the CO₂ captured from the Kemper IGCC. The agreements with Denbury and Treetop provide termination rights in the event that the Company does not satisfy its contractual obligation with respect to deliveries of captured CO₂ by May 11, 2015. While the Company has received no indication from either Denbury or Treetop of their intent to terminate their respective agreements, any termination could result in a material reduction in future chemical product sales revenues and could have a material financial impact on the Company to the extent the Company is not able to enter into other similar contractual arrangements.

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

Proposed Sale of Undivided Interest to SMEPA

In 2010, the Company and SMEPA entered into an APA whereby SMEPA agreed to purchase a 17.5% undivided interest in the Kemper IGCC. In 2012, the Mississippi PSC approved the sale and transfer of the 17.5% undivided interest in the Kemper IGCC to SMEPA. Later in 2012, the Company and SMEPA signed an amendment to the APA whereby SMEPA reduced its purchase commitment percentage from a 17.5% to a 15% undivided interest in the Kemper IGCC. In March 2013, the Company and SMEPA signed an amendment to the APA whereby the Company and SMEPA agreed to amend the power supply agreement entered into by the parties in 2011 to reduce the capacity amounts to be received by SMEPA by half (approximately 75 MWs) at the sale and transfer of the undivided interest in the Kemper IGCC to SMEPA. Capacity revenues under the 2011 power supply agreement were \$16.7 million in 2014. In December 2013, the Company and SMEPA agreed to extend SMEPA's option to purchase through December 31, 2014.

By letter agreement dated October 6, 2014, the Company and SMEPA agreed in principle on certain issues related to SMEPA's proposed purchase of a 15% undivided interest in the Kemper IGCC. The letter agreement contemplated certain amendments to the APA, which the parties anticipated to be incorporated into the APA on or before December 31, 2014. The parties agreed to further amend the APA as follows: (1) the Company agreed to cap at \$2.88 billion the portion of the purchase price payable for development and construction costs, net of the Cost Cap Exceptions, title insurance reimbursement, and AFUDC and/or carrying costs through the Closing Commitment Date (defined below); (2) SMEPA agreed to close the purchase within 180 days after the date of the execution of the amended APA or before the Kemper IGCC in-service date, whichever occurs first (Closing Commitment Date), subject only to satisfaction of certain conditions; and (3) AFUDC and/or carrying costs will continue to be accrued on the capped development and construction costs, the Cost Cap Exceptions, and any operating costs, net of revenues until the amended APA is executed by both parties, and thereafter AFUDC and/or carrying costs and payment of interest on SMEPA's deposited money will be suspended and waived provided closing occurs by the Closing Commitment Date. The letter agreement also provided for certain post-closing adjustments to address any differences between the actual and the estimated amounts of post-in-service date costs (both expenses and capital) and revenue credits for those portions of the Kemper IGCC previously placed in service.

By letter dated December 18, 2014, SMEPA notified the Company that SMEPA decided not to extend the estimated closing date in the APA or revise the APA to include the contemplated amendments; however, both parties agree that the APA will remain in effect until closing or until either party gives notice of termination.

The closing of this transaction is also conditioned upon execution of a joint ownership and operating agreement, the absence of material adverse effects, receipt of all construction permits, and appropriate regulatory approvals, as well as SMEPA's receipt of Rural Utilities Service (RUS) funding. In 2012, SMEPA received a conditional loan commitment from RUS for the purchase.

In 2012, on January 2, 2014, and on October 9, 2014, the Company received \$150 million, \$75 million, and \$50 million, respectively, of interest-bearing refundable deposits from SMEPA to be applied to the purchase. While the expectation is that these amounts will be applied to the purchase price at closing, the Company would be required to refund the deposits upon the termination of the APA or within 15 days of a request by SMEPA for a full or partial refund. Given the interest-bearing nature of the deposits and SMEPA's ability to request a refund, the deposits have been presented as a current liability in the balance sheet and as financing proceeds in the statement of cash flow. In July 2013, Southern Company entered into an agreement with SMEPA

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under which Southern Company has agreed to guarantee the obligations of the Company with respect to any required refund of the deposits.

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

Income Tax Matters

See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information about the Kemper IGCC. The ultimate outcome of these tax matters cannot be determined at this time.

Bonus Depreciation

On December 19, 2014, the Tax Increase Prevention Act of 2014 (TIPA) was signed into law. The TIPA retroactively extended several tax credits through 2014 and extended 50% bonus depreciation for property placed in service in 2014 (and for certain long-term production-period projects to be placed in service in 2015). The extension of 50% bonus depreciation had a positive impact on the Company's cash flows and combined with bonus depreciation allowed in 2014 under the American Taxpayer Relief Act of 2012, resulted in approximately \$130 million of positive cash flows related to the combined cycle and associated common facilities portion of the Kemper IGCC for the 2014 tax year. The estimated cash flow benefit of bonus depreciation related to TIPA is expected to be approximately \$45 million to \$50 million for the 2015 tax year.

Investment Tax Credits

The IRS allocated \$279.0 million (Phase II) of Internal Revenue Code of 1986, as amended (Internal Revenue Code), Section 48A tax credits to the Company in connection with the Kemper IGCC. Through December 31, 2014, the Company had recorded tax benefits totaling \$276.4 million for the Phase II credits, of which approximately \$210 million had been utilized through that date. These credits will be amortized as a reduction to depreciation and amortization over the life of the Kemper IGCC and are dependent upon meeting the IRS certification requirements, including an in-service date no later than April 19, 2016 and the capture and sequestration (via enhanced oil recovery) of at least 65% of the CO₂ produced by the Kemper IGCC during operations in accordance with the Internal Revenue Code. The Company currently expects to place the Kemper IGCC in service in the first half of 2016. In addition, a portion of the Phase II tax credits will be subject to recapture upon completion of SMEPA's proposed purchase of an undivided interest in the Kemper IGCC as described above.

Section 174 Research and Experimental Deduction

Southern Company, on behalf of the Company, reduced tax payments for 2014 and included in its 2013 consolidated federal income tax return deductions for research and experimental (R&E) expenditures related to the Kemper IGCC. Due to the uncertainty related to this tax position, the Company recorded an unrecognized tax benefit of approximately \$160 million as of December 31, 2014. See Note 5 to the financial statements under "Unrecognized Tax Benefits" for additional information.

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 air quality and water standards, has occurred throughout the U.S. This litigation has included claims for damages alleged to have been caused by CO₂ 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 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 February 2013, the Company submitted a claim under the Deepwater Horizon Economic and Property Damages Settlement Agreement associated with the oil spill that occurred in April 2010 in the Gulf of Mexico. The ultimate outcome of this matter cannot be determined at this time.

Sierra Club Settlement Agreement

On August 1, 2014, the Company entered into the Sierra Club Settlement Agreement that, among other things, requires the Sierra Club to dismiss or withdraw all pending legal and regulatory challenges of the Kemper IGCC and the scrubber project at Plant Daniel Units 1 and 2. In addition, the Sierra Club agreed to refrain from initiating, intervening in, and/or challenging certain legal and regulatory proceedings for the Kemper IGCC, including, but not limited to, the prudence review, and Plant Daniel for a period of three years from the date of the Sierra Club Settlement Agreement. On August 4, 2014, the Sierra Club filed all of the required motions necessary to dismiss or withdraw all appeals associated with certification of the Kemper IGCC and the Plant Daniel Units 1 and 2 scrubber project, which the applicable courts subsequently granted.

Under the Sierra Club Settlement Agreement, the Company agreed to, among other things, fund a \$15 million grant payable over a 15-year period for an energy efficiency and renewable program and contribute \$2 million to a conservation fund. In accordance with the Sierra Club Settlement Agreement, the Company paid \$7 million in 2014, recognized in other income (expense), net in the statement of operations. In addition, and consistent with the Company's ongoing evaluation of recent environmental rules and regulations, 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. 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, and cease burning coal and other solid fuel at Plant Greene County Units 1 and 2 (200 MWs) and begin operating those units solely on natural gas no later than April 2016. See Note 3 under "Retail Regulatory Matters – Environmental Compliance Overview Plan" for additional information.

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.

Electric 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 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.

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, in accordance with GAAP, 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 financial position, results of operations, or cash flows.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)
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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.

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 in accordance with GAAP 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 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. The Company discounts the future cash flows related to its postretirement benefit plans 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 purposes of its December 31, 2014 measurement date, the Company adopted new mortality tables for its pension plans and retiree life and medical plans, which reflect increased life expectancies in the U.S. The adoption of new mortality tables increased the projected benefit obligations for the Company's pension plans and other postretirement benefit plans by approximately \$30.2 million and \$5.2 million, respectively. The adoption of new mortality tables will increase net periodic costs related to the Company's pension plans and other postretirement benefit plans in 2015 by \$4.1 million and \$0.6 million, respectively.

A 25 basis point change in any significant assumption (discount rate, salaries, or long-term return on plan assets) would result in a \$1.8 million or less change in total annual benefit expense and a \$22.7 million or less change in projected obligations.

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 6.91%, 6.89%, and 7.04% for the years ended December 31, 2014, 2013, and 2012, respectively. The AFUDC rate is applied to CWIP consistent with jurisdictional regulatory treatment. AFUDC equity was \$136.4 million, \$121.6 million, and \$64.8 million in 2014, 2013, and 2012, respectively.

Kemper IGCC Estimated Construction Costs, Project Completion Date, and Rate Recovery

During 2014, the Company further extended the scheduled in-service date for the Kemper IGCC to the first half of 2016 and revised its cost estimate to complete construction and start-up of the Kemper IGCC to an amount that exceeds the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions. The Company does not intend to seek any rate recovery or any joint owner contributions for any costs related to the construction of the Kemper IGCC that exceed the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions.

As a result of the revisions to the cost estimate, the Company recorded total pre-tax charges to income for the estimated probable losses on the Kemper IGCC of \$70.0 million (\$43.2 million after tax) in the fourth quarter 2014, \$418.0 million (\$258.1 million after tax) in the third quarter 2014, \$380.0 million (\$234.7 million after tax) in the first quarter 2014, \$40.0 million (\$24.7 million

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after tax) in the fourth quarter 2013, \$150.0 million (\$92.6 million after tax) in the third quarter 2013, \$450.0 million (\$277.9 million after tax) in the second quarter 2013, \$462.0 million (\$285.3 million after tax) in the first quarter 2013, and \$78.0 million (\$48.2 million after tax) in the fourth quarter 2012. In the aggregate, the Company has incurred charges of \$2.05 billion (\$1.26 billion after tax) as a result of changes in the cost estimate for the Kemper IGCC through December 31, 2014.

The Company has experienced, and may continue to experience, material changes in the cost estimate for the Kemper IGCC. In subsequent periods, any further changes in the estimated costs to complete construction and start-up of the Kemper IGCC subject to the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions, will be reflected in the statements of operations and these changes could be material. Any further cost increases and/or extensions of the in-service date with respect to the Kemper IGCC may result from factors including, but not limited to, labor costs and productivity, adverse weather conditions, shortages and inconsistent quality of equipment, materials, and labor, contractor or supplier delay, non-performance under construction or other agreements, operational readiness, including specialized operator training and required site safety programs, unforeseen engineering or design problems, start-up activities for this first-of-a-kind technology (including major equipment failure and system integration), and/or operational performance (including additional costs to satisfy any operational parameters ultimately adopted by the Mississippi PSC).

The Company's revised cost estimate includes costs through March 31, 2016. Any further extension of the in-service date is currently estimated to result in additional base costs of approximately \$25 million to \$30 million per month, which includes maintaining necessary levels of start-up labor, materials, and fuel, as well as operational resources required to execute start-up and commissioning activities. Any further extension of the in-service date with respect to the Kemper IGCC would also increase costs for the Cost Cap Exceptions, which are not subject to the \$2.88 billion cost cap established by the Mississippi PSC. These costs include AFUDC, which is currently estimated to total approximately \$13 million per month, as well as carrying costs and operating expenses on Kemper IGCC assets placed in service and consulting fees and legal fees which are being deferred as regulatory assets and are estimated to total approximately \$7 million per month.

Given the significant judgment involved in estimating the future costs to complete construction and start-up, the project completion date, the ultimate rate recovery for the Kemper IGCC, and the potential impact on the results of operations, the Company considers these items to be critical accounting estimates. See FUTURE EARNINGS POTENTIAL – "Integrated Coal Gasification Combined Cycle" herein and Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information.

Recently Issued Accounting Standards

On May 28, 2014, the Financial Accounting Standards Board issued ASC 606, Revenue from Contracts with Customers. ASC 606 revises the accounting for revenue recognition and is effective for fiscal years beginning after December 15, 2016. The Company continues to evaluate the requirements of ASC 606. The ultimate impact of the new standard has not yet been determined.

FINANCIAL CONDITION AND LIQUIDITY

Overview

Earnings in 2014 and 2013 were negatively affected by revisions to the cost estimate for the Kemper IGCC and by the Court's decision to reverse the 2013 MPSC Rate order; however, the Company's financial condition remained stable at December 31, 2014 and December 31, 2013 as a result of capital contributions to the Company by Southern Company. The Company's cash requirements primarily consist of funding debt maturities, including \$775 million of bank loans maturing in 2015, ongoing operations, capital expenditures, and the potential requirement to refund amounts collected under the 2013 MPSC Rate Order (\$257.2 million through December 31, 2014) and additional amounts for associated carrying costs. See FUTURE EARNINGS POTENTIAL – Integrated Coal Gasification Combined Cycle – "Rate Recovery of Kemper IGCC Costs – 2013 MPSC Rate Order" and " – 2015 Mississippi Supreme Court Decision" herein for additional information. For the three-year period from 2015 through 2017, the Company's capital expenditures and debt maturities are expected to materially exceed operating cash flows. In addition to the Kemper IGCC, projected capital expenditures in that period include investments to maintain existing generation facilities, including the Plant Daniel scrubber project, to add environmental equipment for existing generating units, to add or change fuel sources for certain existing units, and to expand and improve transmission and distribution facilities. Through December 31, 2014, the Company has incurred non-recoverable cash expenditures of \$1.3 billion and is expected to incur approximately \$702 million in additional non-recoverable cash expenditures through completion of the Kemper IGCC.

In 2014, the Company received \$450.0 million in equity contributions and a \$220.0 million loan from Southern Company which was repaid on September 29, 2014. In January 2015, the Company received an additional \$75.0 million in equity contributions from Southern Company. The Company is currently negotiating to refinance its maturing bank loans and to obtain additional bank loans. The Company also intends to utilize cash from operations and commercial paper and lines of credit as market conditions

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permit, as well as, under certain circumstances, equity contributions and/or loans from Southern Company, to fund the Company's short-term capital needs.

See "Sources of Capital," "Financing Activities," and "Capital Requirements and Contractual Obligations" herein for additional information.

The Company's investments in the qualified pension plan increased in value as of December 31, 2014 as compared to December 31, 2013. In December 2014, the Company voluntarily contributed \$33 million to the qualified pension plan. No mandatory contributions to the qualified pension plan are anticipated for the year ending December 31, 2015.

Net cash provided from operating activities totaled \$734.4 million for 2014, an increase of \$286.8 million as compared to the corresponding period in 2013. The increase in net cash provided from operating activities was primarily due to deferred income taxes and Mirror CWIP, net of the Kemper IGCC regulatory deferral, partially offset by a decrease in ITCs received related to the Kemper IGCC, an increase in prepaid income taxes, increases in fossil fuel stock, and an increase in regulatory assets associated with the Kemper IGCC. Net cash provided from operating activities totaled \$447.6 million for 2013, an increase of \$212.2 million as compared to the corresponding period in 2012. The increase in net cash provided from operating activities was primarily due to an increase in ITCs received related to the Kemper IGCC, increases in rate recovery related to the Kemper IGCC, and decreases in fossil fuel stock, partially offset by a decrease in over-recovered regulatory clause revenues and an increase in regulatory assets associated with the Kemper IGCC.

Net cash used for investing activities totaled \$1.3 billion for 2014 primarily due to gross property additions primarily related to the Kemper IGCC and the Plant Daniel scrubber project. Net cash used for investing activities totaled \$1.6 billion for 2013 primarily due to gross property additions primarily related to the Kemper IGCC and the Plant Daniel scrubber project, partially offset by proceeds from asset sales.

Net cash provided from financing activities totaled \$592.6 million in 2014 primarily due to capital contributions from Southern Company, long-term debt financings, and the receipts of interest bearing refundable deposits related to a pending asset sale, partially offset by redemptions of long-term debt. Net cash provided from financing activities totaled \$1.2 billion in 2013 primarily due to an increase in capital contributions from Southern Company and an increase in long-term debt financings, partially offset by redemptions of long-term debt.

Significant balance sheet changes as of December 31, 2014 compared to 2013 included an increase in securities due within one year of \$763.9 million and a decrease in long-term debt of \$536.6 million, primarily due to bank loans maturing in 2015, as well as an increase in the interest-bearing refundable deposit from SMEPA of \$125.0 million. See "Financing Activities" herein for additional information. Total property, plant, and equipment increased \$416.6 million and other regulatory assets, deferred increased \$184.8 million primarily due to the Kemper IGCC and results of an actuarial study. See "Integrated Coal Gasification Combined Cycle" herein for additional information. Other regulatory liabilities, deferred decreased \$81.3 million and Mirror CWIP increased \$270.8 million primarily due to the reclassification of Kemper regulatory liabilities. Additional changes included an increase in accrued income taxes of \$136.9 million primarily due to R&E tax deductions, an increase in prepaid income taxes of \$155.9 million primarily due to ITCs related to the Kemper IGCC and an increase in taxes on Mirror CWIP, a net increase in accumulated deferred income taxes of \$194.7 million primarily related to the Kemper combined cycle and associated common facilities placed in service on August 9, 2014 offset by the estimated probable loss on the Kemper IGCC, an increase in employee benefit obligations of \$53.1 million, and an increase in deferred charges related to income taxes of \$81.8 million. See Note 2 and Note 5 to the financial statements for additional information. Total common stockholder's equity decreased \$92.3 million primarily due to the estimated probable loss on the Kemper IGCC partially offset by the receipt of \$450.0 million in capital contributions from Southern Company.

The Company's ratio of common equity to total capitalization, including long-term debt due within one year, was 46.1% in 2014 and 49.6% in 2013. See Note 6 to the financial statements for additional information.

Sources of Capital

Except as described herein, the Company plans to obtain the funds required for construction and other purposes from operating cash flows, security issuances, term loans, and/or short-term debt, as well as, under certain circumstances, equity contributions and/or loans from Southern Company. Operating cash flows would be adversely impacted by \$156 million annually with the removal of rates implemented under the 2013 MPSC Rate Order. The amount, type, and timing of future financings will depend upon regulatory approval, prevailing market conditions, and other factors, which may include resolution of Kemper IGCC cost recovery. See "Capital Requirements and Contractual Obligations" herein for additional information. See FUTURE EARNINGS POTENTIAL – "Integrated Coal Gasification Combined Cycle – Rate Recovery of Kemper IGCC Costs – 2013 MPSC Rate Order" and " – 2015 Mississippi Supreme Court Decision" included herein for additional information.

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The Company had no short-term borrowings in 2012 and 2014. Details of short-term borrowing for 2013 were as follows:

	Commercial Paper at the End of the Period		Commercial Paper During the Period ^(a)		
	Amount Outstanding	Weighted Average Interest Rate	Average Outstanding	Weighted Average Interest Rate	Maximum Amount Outstanding
	<i>(in millions)</i>		<i>(in millions)</i>		<i>(in millions)</i>
December 31, 2013	\$—	—%	\$23	0.2%	\$148

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

Financing Activities

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

Bank Term Loans

In January 2014, the Company entered into an 18-month floating rate bank loan bearing interest based on one-month LIBOR. The term loan was for \$250 million aggregate principal amount, and the proceeds were used for working capital and other general corporate purposes, including the Company's continuous construction program.

This and other bank loans and the other revenue bonds described below have covenants that limit debt levels to 65% of total capitalization, as defined in the agreements. For purposes of these definitions, debt excludes the long-term debt payable to affiliated trusts, other hybrid securities, and securitized debt relating to the securitization of certain costs of the Kemper IGCC. At December 31, 2014, the Company was in compliance with its debt limits.

In addition, this and other bank loans and the other revenue bonds described below contain cross default provisions to other debt (including guarantee obligations) that would be triggered if the Company defaulted on debt above a specified threshold. The Company is currently in compliance with all such covenants.

Other Revenue Bonds

In May 2014 and August 2014, the Mississippi Business Finance Corporation (MBFC) issued \$12.3 million and \$10.5 million, respectively, aggregate principal amount of MBFC Taxable Revenue Bonds (Mississippi Power Company Project), Series 2013A for the benefit of the Company and proceeds were used to reimburse the Company for the cost of the acquisition, construction, equipping, installation, and improvement of certain equipment and facilities for the lignite mining facility related to the Kemper IGCC. In December 2014, the MBFC Taxable Revenue Bonds (Mississippi Power Company Project), Series 2013A of \$22.87 million and Series 2013B of \$11.25 million were paid at maturity.

Other Obligations

In 2012, January 2014, and October 2014, the Company received \$150 million, \$75 million, and \$50 million, respectively, of interest-bearing refundable deposits from SMEPA to be applied to the sale price for the pending sale of an undivided interest in the Kemper IGCC. Until the sale is closed, the deposits bear interest at the Company's AFUDC rate adjusted for income taxes, which was 10.134% per annum for 2014, 9.932% per annum for 2013, and 9.967% per annum for 2012, and are refundable to SMEPA upon termination of the APA related to such purchase or within 15 days of a request by SMEPA for a full or partial refund. In July 2013, Southern Company entered into an agreement with SMEPA under which Southern Company has agreed to guarantee the obligations of the Company with respect to any required refund of the deposits.

In May 2014, the Company issued a 19-month floating rate promissory note to Southern Company for a loan bearing interest based on one-month LIBOR. This loan was for \$220 million aggregate principal amount and the proceeds were used for working capital and other general corporate purposes, including the Company's construction program. This loan was repaid on September 29, 2014.

Credit Rating Risk

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.

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There are certain contracts that could require collateral, but not accelerated payment, in the event of a credit rating change to below BBB- and/or Baa3. These contracts are for physical electricity sales, fuel transportation and storage, and energy price risk management. At December 31, 2014, the maximum amount of potential collateral requirements under these contracts at a rating below BBB- and/or Baa3 equaled approximately \$280 million. Included in these amounts are 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. Additionally, any credit rating downgrade could impact the Company's ability to access capital markets, particularly the short-term debt market and the variable rate pollution control revenue bond market.

Subsequent to December 31, 2014, Moody's affirmed the senior unsecured debt rating of the Company and revised the ratings outlook for the Company from stable to negative.

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, foreign currency exchange 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 \$815 million of long-term variable interest rate exposure at December 31, 2014 was 0.96%. If the Company sustained a 100 basis point change in interest rates for all long-term variable interest rate exposure, the change would affect annualized interest expense by approximately \$8 million at January 1, 2015. 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, 2014 when compared to the year ended December 31, 2013.

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:

	2014 Changes	2013 Changes
	Fair Value	
	<i>(in thousands)</i>	
Contracts outstanding at the beginning of the period, assets (liabilities), net	\$ (5,478)	\$ (16,927)
Contracts realized or settled	(2,655)	11,271
Current period changes ^(a)	(37,231)	178
Contracts outstanding at the end of the period, assets (liabilities), net	\$ (45,364)	\$ (5,478)

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

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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:

	2014	2013
	mmBtu Volume	
	<i>(in thousands)</i>	
Total hedge volume	54,220	56,440

The weighted average swap contract cost above market prices was approximately \$0.84 per mmBtu as of December 31, 2014 and \$0.10 per mmBtu as of December 31, 2013. There were no options outstanding as of the reporting periods presented. The costs associated with natural gas hedges are recovered through the Company's ECMs.

At December 31, 2014 and 2013, 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. Gains and losses on energy-related derivatives that are designated as cash flow hedges are used to hedge anticipated purchases and sales and are initially deferred in OCI before being recognized in income in the same period as the hedged transaction. 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 and were not material for any year presented. The pre-tax gains and losses reclassified from OCI to revenue and fuel expense were not material for any period presented and are not expected to be material for 2015.

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. 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, 2014 were as follows:

	Fair Value Measurements			
	December 31, 2014			
	Total Fair Value	Maturity		
Year 1		Years 2&3	Years 4&5	
	<i>(in thousands)</i>			
Level 1	\$ —	\$ —	\$ —	\$ —
Level 2	(45,364)	(26,227)	(18,620)	(517)
Level 3	—	—	—	—
Fair value of contracts outstanding at end of period	\$ (45,364)	\$ (26,227)	\$ (18,620)	\$ (517)

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

The construction program of the Company is currently estimated to be \$1.0 billion for 2015, \$328 million for 2016, and \$221 million for 2017, which includes expenditures related to the construction of the Kemper IGCC of \$801 million in 2015 and \$132 million in 2016. The amounts related to the construction and start-up of the Kemper IGCC exclude SMEPA's proposed acquisition of a 15% ownership share of the Kemper IGCC for approximately \$596 million (including construction costs for all prior periods relating to its proposed ownership interest). Capital expenditures to comply with environmental statutes and regulations included in these estimated amounts are \$94 million, \$25 million, and \$35 million for 2015, 2016, and 2017, respectively. These estimated amounts also include capital expenditures covered under long-term service agreements. These estimated expenditures do not include any potential compliance costs that may arise from the EPA's proposed rules that would limit CO₂ emissions from new, existing, and modified or reconstructed fossil-fuel-fired electric generating units. See "Global Climate Issues" for additional information.

See FUTURE EARNINGS POTENTIAL – "Environmental Matters – Environmental Statutes and Regulations" and – "Integrated Coal Gasification Combined Cycle" for additional information.

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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 statutes 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 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. See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information and further risks related to the estimated schedule and costs and rate recovery for the Kemper IGCC.

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, 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.

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Contractual Obligations

	2015	2016- 2017	2018- 2019	After 2019	Total
	<i>(in thousands)</i>				
Long-term debt ^(a) —					
Principal	\$ 775,000	\$ 335,000	\$ 125,000	\$ 1,032,695	\$ 2,267,695
Interest	77,715	132,442	120,904	723,455	1,054,516
Preferred stock dividends ^(b)	1,733	3,465	3,465	—	8,663
Financial derivative obligations ^(c)	26,270	18,623	536	—	45,429
Unrecognized tax benefits ^(d)	164,821	—	—	—	164,821
Operating leases ^(e)	3,950	2,601	—	—	6,551
Capital leases ^(f)	2,667	5,741	6,331	64,940	79,679
Purchase commitments —					
Capital ^(g)	1,016,215	491,886	—	—	1,508,101
Fuel ^(h)	266,934	299,888	255,396	289,215	1,111,433
Long-term service agreements ⁽ⁱ⁾	27,109	23,367	20,596	128,832	199,904
Pension and other postretirement benefits plans ^(j)	6,187	13,112	—	—	19,299
Total	\$ 2,368,601	\$ 1,326,125	\$ 532,228	\$ 2,239,137	\$ 6,466,091

- (a) All amounts are reflected based on final maturity dates. The Company plans to continue 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 January 1, 2015, 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).
- (b) Preferred stock does not mature; therefore, amounts are provided for the next five years only.
- (c) For additional information, see Notes 1 and 10 to the financial statements.
- (d) See Note 5 to the financial statements under "Unrecognized Tax Benefits" for additional information.
- (e) See Note 7 to the financial statements for additional information.
- (f) Capital lease related to a 20-year nitrogen supply agreement for the Kemper IGCC. See Note 6 to the financial statements for additional information.
- (g) The Company provides estimated capital expenditures for a three-year period, including capital expenditures and compliance costs associated with environmental regulations. Estimates related to the construction and start-up of the Kemper IGCC exclude SMEPA's proposed acquisition of a 15% ownership share of the Kemper IGCC. At December 31, 2014, 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 – Environmental Statutes and Regulations" for additional information. See Note 3 to the financial statements under "Integrated Coal Gasification Combined Cycle" for additional information.
- (h) Includes commitments to purchase coal and natural gas, 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, 2014.
- (i) Long-term service agreements include price escalation based on inflation indices.
- (j) 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 2014 Annual Report contains forward-looking statements. Forward-looking statements include, among other things, statements concerning retail rates, economic recovery, fuel and environmental cost recovery and other rate actions, current and proposed environmental regulations and related compliance plans and estimated expenditures, access to sources of capital, projections for the qualified pension plan and postretirement benefit plan, financing activities, completion of construction projects, filings with state and federal regulatory authorities, impact of the TIPA, 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 legislative and regulatory initiatives regarding deregulation and restructuring of the electric utility industry, environmental laws including regulation of water, CCR, and emissions of sulfur, nitrogen, CO₂, soot, particulate matter, hazardous air pollutants, including mercury, and other substances, 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;
- current and future litigation, regulatory investigations, proceedings, or inquiries, including FERC matters, the pending EPA civil action, and IRS and state tax audits;
- 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 and recovery from the last recession, 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, which include the development and construction of generating facilities with designs that have not been finalized or previously constructed, including changes in labor costs and productivity, adverse weather conditions, shortages and inconsistent quality of equipment, materials, and labor, contractor or supplier delay, non-performance under construction or other agreements, operational readiness, including specialized operator training and required site safety programs, unforeseen engineering or design problems, start-up activities (including major equipment failure and system integration), and/or operational performance (including additional costs to satisfy any operational parameters ultimately adopted by the Mississippi PSC);
- the ability to construct facilities in accordance with the requirements of permits and licenses, to satisfy any operational and environmental performance standards, including any PSC requirements and the requirements of tax credits and other incentives, and to integrate facilities into the Southern Company system upon completion of construction;
- 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;
- actions related to cost recovery for the Kemper IGCC, including actions relating to proposed securitization, Mississippi PSC approval of a rate recovery plan, including the ability to complete the proposed sale of an interest in the Kemper IGCC to SMEPA, the ability to utilize bonus depreciation, which currently requires that assets be placed in service in 2015, and satisfaction of requirements to utilize ITCs and grants;
- Mississippi PSC review of the prudence of Kemper IGCC costs;
- the ultimate outcome and impact of the February 2015 decision of the Mississippi Supreme Court and any further legal or regulatory proceedings regarding any settlement agreement between the Company and the Mississippi PSC, the March 2013 rate order regarding retail rate increases, or the Baseload Act;

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)
Mississippi Power Company 2014 Annual Report

- 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 terrorist incidents and the threat of terrorist incidents;
- 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 currency exchange rates, counterparty performance, and the economy in general;
- the ability of the Company to obtain additional generating capacity at competitive prices;
- catastrophic events such as fires, earthquakes, explosions, floods, 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, 2014, 2013, and 2012
Mississippi Power Company 2014 Annual Report

	2014	2013	2012
	<i>(in thousands)</i>		
Operating Revenues:			
Retail revenues	\$ 794,643	\$ 799,139	\$ 747,453
Wholesale revenues, non-affiliates	322,659	293,871	255,557
Wholesale revenues, affiliates	107,210	34,773	16,403
Other revenues	18,099	17,374	16,583
Total operating revenues	1,242,611	1,145,157	1,035,996
Operating Expenses:			
Fuel	573,936	491,250	411,226
Purchased power, non-affiliates	17,848	5,752	5,221
Purchased power, affiliates	25,096	42,579	49,907
Other operations and maintenance	270,669	253,329	228,675
Depreciation and amortization	97,120	91,398	86,510
Taxes other than income taxes	79,112	80,694	79,445
Estimated loss on Kemper IGCC	868,000	1,102,000	78,000
Total operating expenses	1,931,781	2,067,002	938,984
Operating Income (Loss)	(689,170)	(921,845)	97,012
Other Income and (Expense):			
Allowance for equity funds used during construction	136,436	121,629	64,793
Interest expense, net of amounts capitalized	(45,322)	(36,481)	(40,838)
Other income (expense), net	(14,097)	(6,030)	1,264
Total other income and (expense)	77,017	79,118	25,219
Earnings (Loss) Before Income Taxes	(612,153)	(842,727)	122,231
Income taxes (benefit)	(285,205)	(367,835)	20,556
Net Income (Loss)	(326,948)	(474,892)	101,675
Dividends on Preferred Stock	1,733	1,733	1,733
Net Income (Loss) After Dividends on Preferred Stock	\$ (328,681)	\$ (476,625)	\$ 99,942

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

STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
For the Years Ended December 31, 2014, 2013, and 2012
Mississippi Power Company 2014 Annual Report

	2014	2013	2012
	<i>(in thousands)</i>		
Net Income (Loss)	\$ (326,948)	\$ (474,892)	\$ 101,675
Other comprehensive income (loss):			
Qualifying hedges:			
Changes in fair value, net of tax of \$-, \$-, and \$(296) respectively	—	—	(479)
Reclassification adjustment for amounts included in net income, net of tax of \$526, \$526, and \$411, respectively	849	849	663
Total other comprehensive income (loss)	849	849	184
Comprehensive Income (Loss)	\$ (326,099)	\$ (474,043)	\$ 101,859

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

STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2014, 2013, and 2012
Mississippi Power Company 2014 Annual Report

	2014	2013	2012
	<i>(in thousands)</i>		
Operating Activities:			
Net income (loss)	\$ (326,948)	\$ (474,892)	\$ 101,675
Adjustments to reconcile net income (loss) to net cash provided from operating activities —			
Depreciation and amortization, total	104,422	92,465	86,981
Deferred income taxes	145,417	(396,400)	17,688
Investment tax credits received	(38,366)	144,036	82,464
Allowance for equity funds used during construction	(136,436)	(121,629)	(64,793)
Pension, postretirement, and other employee benefits	(28,899)	13,953	(35,425)
Hedge settlements	—	—	(15,983)
Stock based compensation expense	2,903	2,510	2,084
Regulatory assets associated with Kemper IGCC	(71,816)	(35,220)	(15,445)
Estimated loss on Kemper IGCC	868,000	1,102,000	78,000
Kemper regulatory deferral	—	90,524	—
Other, net	14,022	14,585	10,516
Changes in certain current assets and liabilities —			
-Receivables	(19,065)	(25,001)	(6,589)
-Under recovered regulatory clause revenues	(2,471)	—	—
-Fossil fuel stock	13,121	63,093	(36,206)
-Materials and supplies	(15,496)	(11,087)	(3,473)
-Prepaid income taxes	(50,457)	16,644	(3,852)
-Other current assets	(3,940)	(4,363)	(19,851)
-Other accounts payable	32,661	12,693	8,814
-Accrued interest	29,349	16,768	17,627
-Accrued taxes	39,392	11,141	13,768
-Accrued compensation	17,008	(6,382)	(183)
-Over recovered regulatory clause revenues	(17,826)	(58,979)	16,836
-Mirror CWIP	180,255	—	—
-Other current liabilities	(446)	1,109	757
Net cash provided from operating activities	734,384	447,568	235,410
Investing Activities:			
Property additions	(1,257,440)	(1,640,782)	(1,620,047)
Investment in restricted cash	(10,548)	—	—
Distribution of restricted cash	10,548	—	—
Cost of removal net of salvage	(13,418)	(10,386)	(4,355)
Construction payables	(49,532)	(50,000)	78,961
Capital grant proceeds	—	4,500	13,372
Proceeds from asset sales	—	79,020	—
Other investing activities	(19,217)	14,903	(16,706)
Net cash used for investing activities	(1,339,607)	(1,602,745)	(1,548,775)
Financing Activities:			
Proceeds —			
Capital contributions from parent company	451,387	1,077,088	702,971
Bonds — Other	22,866	42,342	51,471
Senior notes issuances	—	—	600,000
Interest-bearing refundable deposit	125,000	—	150,000
Other long-term debt issuances	470,000	475,000	50,000
Redemptions —			
Bonds — Other	(34,116)	(82,563)	—
Capital Leases	(2,539)	(697)	(633)
Senior notes	—	(50,000)	(90,000)
Other long-term debt	(220,000)	(125,000)	(115,000)
Return of paid in capital	(219,720)	(104,804)	—
Payment of preferred stock dividends	(1,733)	(1,733)	(1,733)
Payment of common stock dividends	—	(71,956)	(106,800)
Other financing activities	1,414	(2,343)	6,512
Net cash provided from financing activities	592,559	1,155,334	1,246,788
Net Change in Cash and Cash Equivalents	(12,664)	157	(66,577)
Cash and Cash Equivalents at Beginning of Year	145,165	145,008	211,585
Cash and Cash Equivalents at End of Year	\$ 132,501	\$ 145,165	\$ 145,008
Supplemental Cash Flow Information:			
Cash paid (received) during the period for —			
Interest (net of \$68,679, \$54,118 and \$32,816 capitalized, respectively)	\$ 6,992	\$ 20,285	\$ 32,589
Income taxes (net of refunds)	(379,158)	(134,198)	(77,580)
Noncash transactions —			
Accrued property additions at year-end	114,469	164,863	214,863
Capital lease obligation	—	82,915	—

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

BALANCE SHEETS
At December 31, 2014 and 2013
Mississippi Power Company 2014 Annual Report

Assets	2014	2013
	<i>(in thousands)</i>	
Current Assets:		
Cash and cash equivalents	\$ 132,501	\$ 145,165
Receivables —		
Customer accounts receivable	40,648	40,978
Unbilled revenues	35,494	38,895
Under recovered regulatory clause revenues	2,471	—
Other accounts and notes receivable	11,256	4,600
Affiliated companies	51,060	34,920
Accumulated provision for uncollectible accounts	(825)	(3,018)
Fossil fuel stock, at average cost	100,164	113,285
Materials and supplies, at average cost	61,582	45,347
Other regulatory assets, current	72,840	48,583
Prepaid income taxes	190,631	34,751
Other current assets	6,209	9,357
Total current assets	704,031	512,863
Property, Plant, and Equipment:		
In service	4,378,087	3,458,770
Less accumulated provision for depreciation	1,172,715	1,095,352
Plant in service, net of depreciation	3,205,372	2,363,418
Construction work in progress	2,160,646	2,586,031
Total property, plant, and equipment	5,366,018	4,949,449
Other Property and Investments	5,498	4,857
Deferred Charges and Other Assets:		
Deferred charges related to income taxes	225,507	143,747
Other regulatory assets, deferred	385,410	200,620
Accumulated deferred income taxes	17,388	—
Other deferred charges and assets	52,876	36,673
Total deferred charges and other assets	681,181	381,040
Total Assets	\$ 6,756,728	\$ 5,848,209

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

BALANCE SHEETS
At December 31, 2014 and 2013
Mississippi Power Company 2014 Annual Report

Liabilities and Stockholder's Equity	2014	2013
	<i>(in thousands)</i>	
Current Liabilities:		
Securities due within one year	\$ 777,667	\$ 13,789
Interest-bearing refundable deposit	275,000	150,000
Accounts payable —		
Affiliated	85,882	70,299
Other	177,736	210,191
Customer deposits	14,970	14,379
Accrued taxes —		
Accrued income taxes	142,461	5,590
Other accrued taxes	83,686	77,958
Accrued interest	76,494	47,144
Accrued compensation	26,331	9,324
Other regulatory liabilities, current	2,164	14,480
Over recovered regulatory clause liabilities	532	18,358
Mirror CWIP	270,779	—
Other current liabilities	44,701	21,413
Total current liabilities	1,978,403	652,925
Long-Term Debt (See accompanying statements)	1,630,487	2,167,067
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	284,849	72,808
Deferred credits related to income taxes	9,370	10,191
Accumulated deferred investment tax credits	282,816	284,248
Employee benefit obligations	147,536	94,430
Asset retirement obligations	48,248	41,197
Other cost of removal obligations	165,999	156,683
Other regulatory liabilities, deferred	63,681	144,992
Other deferred credits and liabilities	28,299	14,337
Total deferred credits and other liabilities	1,030,798	818,886
Total Liabilities	4,639,688	3,638,878
Cumulative Redeemable Preferred Stock (See accompanying statements)	32,780	32,780
Common Stockholder's Equity (See accompanying statements)	2,084,260	2,176,551
Total Liabilities and Stockholder's Equity	\$ 6,756,728	\$ 5,848,209
Commitments and Contingent Matters (See notes)		

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

STATEMENTS OF CAPITALIZATION
At December 31, 2014 and 2013
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	2014	2013	2014	2013
	<i>(in thousands)</i>		<i>(percent of total)</i>	
Long-Term Debt:				
Long-term notes payable —				
2.35% due 2016	\$ 300,000	\$ 300,000		
5.60% due 2017	35,000	35,000		
5.55% due 2019	125,000	125,000		
1.63% to 5.40% due 2035-2042	680,000	680,000		
Adjustable rate (1.29% at 1/1/14) due 2014	—	11,250		
Adjustable rates (0.77% to 1.17% at 1/1/15) due 2015	775,000	525,000		
Total long-term notes payable	1,915,000	1,676,250		
Other long-term debt —				
Pollution control revenue bonds:				
5.15% due 2028	42,625	42,625		
Variable rates (0.02% to 0.06% at 1/1/15) due 2020-2028	40,070	40,070		
Plant Daniel revenue bonds (7.13%) due 2021	270,000	270,000		
Total other long-term debt	352,695	352,695		
Capitalized lease obligations	79,679	82,217		
Unamortized debt premium	62,701	71,807		
Unamortized debt discount	(1,921)	(2,113)		
Total long-term debt (annual interest requirement — \$78 million)	2,408,154	2,180,856		
Less amount due within one year	777,667	13,789		
Long-term debt excluding amount due within one year	1,630,487	2,167,067	43.5%	49.6%
Cumulative Redeemable Preferred Stock:				
\$100 par value				
Authorized — 1,244,139 shares				
Outstanding — 334,210 shares				
4.40% to 5.25% (annual dividend requirement — \$1.7 million)	32,780	32,780	0.9	0.7
Common Stockholder's Equity:				
Common stock, without par value —				
Authorized — 1,130,000 shares				
Outstanding — 1,121,000 shares	37,691	37,691		
Paid-in capital	2,612,136	2,376,595		
Accumulated deficit	(558,552)	(229,871)		
Accumulated other comprehensive loss	(7,015)	(7,864)		
Total common stockholder's equity	2,084,260	2,176,551	55.6	49.7
Total Capitalization	\$ 3,747,527	\$ 4,376,398	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, 2014, 2013, and 2012
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	Number of Common Shares Issued	Common Stock	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	<i>(in thousands)</i>					
Balance at December 31, 2011	1,121	\$ 37,691	\$ 694,855	\$ 325,568	\$ (8,897)	\$ 1,049,217
Net income after dividends on preferred stock	—	—	—	99,942	—	99,942
Capital contributions from parent company	—	—	706,665	—	—	706,665
Other comprehensive income (loss)	—	—	—	—	184	184
Cash dividends on common stock	—	—	—	(106,800)	—	(106,800)
Balance at December 31, 2012	1,121	37,691	1,401,520	318,710	(8,713)	1,749,208
Net loss after dividends on preferred stock	—	—	—	(476,625)	—	(476,625)
Capital contributions from parent company	—	—	975,075	—	—	975,075
Other comprehensive income (loss)	—	—	—	—	849	849
Cash dividends on common stock	—	—	—	(71,956)	—	(71,956)
Balance at December 31, 2013	1,121	37,691	2,376,595	(229,871)	(7,864)	2,176,551
Net loss after dividends on preferred stock	—	—	—	(328,681)	—	(328,681)
Capital contributions from parent company	—	—	235,541	—	—	235,541
Other comprehensive income (loss)	—	—	—	—	849	849
Balance at December 31, 2014	1,121	\$ 37,691	\$2,612,136	\$ (558,552)	\$ (7,015)	\$ 2,084,260

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

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1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

Mississippi Power Company (the Company) is a wholly owned subsidiary of The Southern Company (Southern Company), which is the parent company of the Company and three other traditional operating companies, as well as Southern Power, SCS, SouthernLINC Wireless, Southern Company Holdings, Inc. (Southern Holdings), Southern Nuclear, and other direct and indirect subsidiaries. The traditional operating companies – Alabama Power, Georgia Power, Gulf Power, and the Company – are vertically integrated utilities providing electric service in four Southeastern states. The Company operates as a vertically integrated utility providing electricity to retail customers in southeast Mississippi and to wholesale customers in the Southeast. Southern Power constructs, acquires, owns, and manages generation assets, including renewable energy projects, and sells electricity at market-based rates in the wholesale market. SCS, the system service company, provides, at cost, specialized services to Southern Company and its subsidiary companies. SouthernLINC Wireless provides digital wireless communications for use by Southern Company and its subsidiary companies and also markets these services to the public and provides fiber cable services within the Southeast. Southern Holdings is an intermediate holding company subsidiary, primarily for Southern Company's investments in leveraged leases. Southern Nuclear operates and provides services to the Southern Company system's nuclear power plants.

The Company is subject to regulation by the FERC and the Mississippi PSC. The Company follows GAAP in the U.S. and complies 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

On May 28, 2014, the Financial Accounting Standards Board issued ASC 606, Revenue from Contracts with Customers. ASC 606 revises the accounting for revenue recognition and is effective for fiscal years beginning after December 15, 2016. The Company continues to evaluate the requirements of ASC 606. The ultimate impact of the new standard has not yet been determined.

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 \$259.0 million, \$205.0 million, and \$212.7 million during 2014, 2013, and 2012, 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.

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 \$13.4 million, \$12.5 million, and \$11.7 million in 2014, 2013, and 2012, respectively. Also, the Company reimburses Alabama Power for any direct fuel purchases delivered from an Alabama Power transfer facility, which were \$34.5 million, \$27.1 million, and \$28.1 million in 2014, 2013, and 2012, respectively. 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 \$30.5 million, \$16.5 million, and \$21.2 million in 2014, 2013, and 2012, respectively. See Note 4 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 2014 or 2013. The Company received storm assistance from other Southern Company subsidiaries totaling \$2.0 million in 2012.

The traditional 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

NOTES (continued)
Mississippi Power Company 2014 Annual Report

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 the provisions of the Financial Accounting Standards Board in accounting 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:

	2014	2013	Note
		<i>(in thousands)</i>	
Retiree benefit plans – regulatory assets	\$ 169,317	\$ 82,799	(a,g)
Property damage	(61,648)	(60,092)	(i)
Deferred income tax charges	222,599	140,185	(c)
Property tax	27,680	31,206	(d)
Vacation pay	11,172	10,214	(e,g)
Loss on reacquired debt	8,542	9,178	(k)
Plant Daniel Units 3 and 4 regulatory assets	23,013	18,821	(j)
Other regulatory assets	16,270	5,415	(b)
Fuel-hedging (realized and unrealized) losses	46,631	10,340	(f,g)
Asset retirement obligations	10,845	8,918	(c)
Deferred income tax credits	(9,370)	(10,191)	(c)
Other cost of removal obligations	(165,999)	(156,683)	(c)
Kemper IGCC regulatory assets	147,689	75,873	(h)
Mirror CWIP / Kemper regulatory deferral	(270,779)	(90,524)	(h)
Other regulatory liabilities	(4,198)	(8,855)	(b)
Total regulatory assets (liabilities), net	\$ 171,764	\$ 66,604	

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 14 years. See Note 2 for additional information.
- (b) Recorded and recovered (amortized) as approved by the Mississippi PSC.
- (c) Asset retirement and removal assets and liabilities and deferred income tax assets are recovered, and removal assets and deferred income tax liabilities are amortized over the related property lives, which may range up to 49 years. Asset retirement and removal assets and liabilities will be settled and trued up following completion of the related activities.
- (d) Recovered through the ad valorem tax adjustment clause over a 12-month period beginning in April of the following year. See Note 3 under "Ad Valorem Tax Adjustment" for additional information.
- (e) Recorded as earned by employees and recovered as paid, generally within one year. This includes both vacation and banked holiday pay.
- (f) Fuel-hedging assets and liabilities are recorded over the life of the underlying hedged purchase contracts, which generally do not exceed four years. Upon final settlement, costs are recovered through the ECM.
- (g) Not earning a return as offset in rate base by a corresponding asset or liability.
- (h) For additional information, see Note 3 under "Integrated Coal Gasification Combined Cycle – Rate Recovery of Kemper IGCC Costs – Regulatory Assets and Liabilities."
- (i) For additional information, see Note 1 under "Provision for Property Damage."
- (j) Deferred and amortized over a 10-year period beginning October 2021, as approved by the Mississippi PSC for the difference between the revenue requirement under the purchase option and the revenue requirement assuming operating lease accounting treatment for the extended term.
- (k) Recovered over the remaining life of the original issue or, if refinanced, over the life of the new issue, which may range up to 50 years.

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 any 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

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rates. See Note 3 under "Retail Regulatory Matters" and "Integrated Coal Gasification Combined Cycle" for additional information.

Government Grants

In 2010, the DOE, through a cooperative agreement with SCS, agreed to fund \$270.0 million of the Kemper IGCC through the DOE Grants funds. Through December 31, 2014, the Company has received grant funds of \$245.3 million, used for the construction of the Kemper IGCC, which is reflected in the Company's financial statements as a reduction to the Kemper IGCC capital costs. An additional \$25 million is expected to be received for its initial operation. See Note 3 under "Kemper IGCC 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 21.9% of the Company's total operating revenues in 2014 and are largely subject to rolling 10-year cancellation notices.

The Company has a diversified base of customers. 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.

In accordance with accounting standards related to the uncertainty in income taxes, 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.

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

	2014	2013
	<i>(in thousands)</i>	
Generation	\$ 2,293,511	\$ 1,475,264
Transmission	664,618	633,903
Distribution	853,835	828,470
General	484,711	439,721
Plant acquisition adjustment	81,412	81,412
Total plant in service	\$ 4,378,087	\$ 3,458,770

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 all costs associated with operating and maintaining the Kemper IGCC assets already placed in service and a portion of the railway track maintenance costs, which are charged to fuel stock and recovered through the Company's fuel clause or charged to regulatory assets to be recovered through rates over the life of the assets starting after the Kemper plant is placed in service. In addition, the cost of maintenance, repairs, and replacement of minor items of property for Kemper IGCC assets in service, excluding the lignite mine, are deferred in regulatory assets. See Note 3 under "Integrated Coal Gasification Combined Cycle" for additional information.

Depreciation, Depletion, and Amortization

Depreciation of the original cost of plant in service is provided primarily by using composite straight-line rates, which approximated 3.3% in 2014, 3.4% in 2013, and 3.5% in 2012. Depreciation studies are conducted periodically to update the composite rates. 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.

In January 2012, the Mississippi PSC issued an order allowing the Company to defer in a regulatory asset the difference between the revenue requirement under the purchase option of Plant Daniel Units 3 and 4 and the revenue requirement assuming operating lease accounting treatment for the extended term. The regulatory asset will be deferred for a 10-year period ending October 2021. At the conclusion of the deferral period, the unamortized deferral balance will be amortized into rates over the remaining life of the units.

The Kemper IGCC will 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 IGCC. The mine, operated by North American Coal Corporation, started commercial operation in June 2013. Depreciation associated with fixed assets, amortization associated with rolling stock, and depletion associated with minerals and minerals rights is recognized and charged to fuel stock and is expected to be recovered through the Company's fuel clause. Depreciation associated with in-service Kemper IGCC-related assets has been deferred as a regulatory asset to be recovered over the life of the Kemper IGCC.

Asset Retirement Obligations and Other Costs of Removal

Asset retirement obligations (ARO) are computed as the present value of the 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. 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 Company has AROs 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, certain wireless communication towers, and certain structures authorized by the U.S. Army Corps of Engineers. 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

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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 ARO included in the balance sheets are as follows:

	2014	2013
	<i>(in thousands)</i>	
Balance at beginning of year	\$ 41,910	\$ 42,115
Liabilities settled	(2,529)	(24)
Accretion	1,969	1,840
Cash flow revisions	6,898	(2,021)
Balance at end of year	\$ 48,248	\$ 41,910

The increase in cash flow revisions in 2014 related to the Company's AROs associated with Watson landfill and Greene County asbestos.

On December 19, 2014, the EPA issued the Disposal of Coal Combustion Residuals from Electric Utilities final rule (CCR Rule), but has not yet published it in the Federal Register. The CCR Rule will regulate the disposal of CCR, including coal ash and gypsum, as non-hazardous solid waste in landfills and surface impoundments at active generating power plants. The ultimate impact of the CCR Rule cannot be determined at this time and will depend on the Company's ongoing review of the CCR Rule, the results of initial and ongoing minimum criteria assessments, and the outcome of legal challenges. The cost and timing of potential ash pond closure and ongoing monitoring activities that may be required in connection with the CCR Rule is also uncertain; however, the Company has developed a preliminary nominal dollar estimate of costs associated with closure and groundwater monitoring of ash ponds in place of approximately \$64 million and ongoing post-closure care of approximately \$12 million. The Company will record AROs for the estimated closure costs required under the CCR Rule during 2015. The Company's results of operations, cash flows, and financial condition could be significantly impacted if such costs are not recovered through regulated rates.

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 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 6.91%, 6.89%, and 7.04% for the years ended December 31, 2014, 2013, and 2012, respectively. AFUDC equity was \$136.4 million, \$121.6 million, and \$64.8 million in 2014, 2013, and 2012, respectively.

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. See Note 3 under "Integrated Coal Gasification Combined Cycle – Kemper IGCC Schedule and Cost Estimate" for additional information.

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, 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

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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. In 2014, 2013, and 2012, the Company made retail accruals of \$3.3 million, \$3.2 million, and \$3.5 million, respectively. The Company accrued \$0.3 million annually in 2014, 2013, and 2012 for the wholesale jurisdiction. As of December 31, 2014, the property damage reserve balances were \$60.7 million and \$1.0 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 appropriate, at weighted-average cost when utilized.

Fuel Inventory

Fuel inventory includes the average cost of coal, lignite, natural gas, oil, transportation and emissions allowances. Fuel is charged to inventory when purchased, except for the cost of owning and operating the lignite mine related to the Kemper IGCC which is charged to inventory as incurred, and then expensed, at weighted average cost, as used and recovered by the Company through fuel cost recovery rates or capitalized as part of the Kemper IGCC costs if used for testing. 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, electricity purchases and sales, and occasionally foreign currency exchange rates. All derivative financial instruments are recognized as either assets or liabilities (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 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. Foreign currency exchange rate hedges are designated as fair value hedges. Settled foreign currency exchange hedges are recorded in CWIP. Any ineffectiveness arising from these would be recognized currently in net income; however, the Company has regulatory approval allowing it to defer any ineffectiveness arising from hedging instruments relating to the Kemper IGCC to a regulatory asset. 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. The amounts related to derivatives on the cash flow statement are classified in the same category as the items being hedged. See Note 10 for additional information regarding derivatives.

The Company does not offset fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a master netting arrangement. Additionally, the Company has no outstanding collateral repayment obligations or rights to reclaim collateral arising from derivative instruments recognized at December 31, 2014.

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 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, certain changes in pension and other postretirement benefit plans, and reclassifications for amounts included in net income.

Variable Interest Entities

The primary beneficiary of a 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 is 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 IGCC. Liberty Fuels qualifies as a VIE for which the Company is the primary beneficiary. For the year ended December 31, 2014, the VIE consolidation resulted in an ARO asset and associated liability in the amounts of \$21.0 million and \$23.6 million, respectively. For the year ended December 31, 2013, the VIE consolidation resulted in an ARO and an associated liability in the amounts of \$21.0 million and \$22.7 million, respectively. For the year ended December 31, 2012, the VIE consolidation resulted in an ARO and associated liability in the amounts of \$21.0 million and \$21.8 million, respectively. See Note 3 under "Integrated Coal Gasification Combined Cycle" 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). In December 2014, the Company voluntarily contributed \$33 million to the qualified pension plan. No mandatory contributions to the qualified pension plan are anticipated for the year ending December 31, 2015. 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, 2015, no other postretirement trust contributions are expected.

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Actuarial Assumptions

The weighted average rates assumed in the actuarial calculations used to determine both the benefit obligations as of the measurement date and the net periodic costs for the pension and other postretirement benefit plans for the following year are presented below. Net periodic benefit costs were calculated in 2011 for the 2012 plan year using discount rates for the pension plans and the other postretirement benefit plans of 4.98% and 4.87%, respectively, and an annual salary increase of 3.84%.

	2014	2013	2012
Discount rate:			
Pension plans	4.17%	5.01%	4.26%
Other postretirement benefit plans	4.03	4.85	4.04
Annual salary increase	3.59	3.59	3.59
Long-term return on plan assets:			
Pension plans	8.20	8.20	8.20
Other postretirement benefit plans	7.30	7.04	6.96

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 seven 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.

For purposes of its December 31, 2014 measurement date, the Company adopted new mortality tables for its pension plans and retiree life and medical plans, which reflect increased life expectancies in the U.S. The adoption of new mortality tables increased the projected benefit obligations for the Company's pension plans and other postretirement benefit plans by approximately \$30.2 million and \$5.2 million, respectively.

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, 2014 were as follows:

	Initial Cost Trend Rate	Ultimate Cost Trend Rate	Year That Ultimate Rate is Reached
Pre-65	9.00%	4.50%	2024
Post-65 medical	6.00	4.50	2024
Post-65 prescription	6.75	4.50	2024

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, 2014 as follows:

	1 Percent Increase	1 Percent Decrease
	<i>(in thousands)</i>	
Benefit obligation	\$ 6,241	\$ (5,289)
Service and interest costs	250	(212)

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Pension Plans

The total accumulated benefit obligation for the pension plans was \$462 million at December 31, 2014 and \$370 million at December 31, 2013. Changes in the projected benefit obligations and the fair value of plan assets during the plan years ended December 31, 2014 and 2013 were as follows:

	2014	2013
	<i>(in thousands)</i>	
Change in benefit obligation		
Benefit obligation at beginning of year	\$ 409,395	\$ 432,553
Service cost	10,123	11,067
Interest cost	20,093	18,062
Benefits paid	(17,499)	(16,207)
Actuarial (gain) loss	90,735	(36,080)
Balance at end of year	512,847	409,395
Change in plan assets		
Fair value of plan assets at beginning of year	387,403	351,749
Actual return on plan assets	40,051	49,431
Employer contributions	35,526	2,430
Benefits paid	(17,499)	(16,207)
Fair value of plan assets at end of year	445,481	387,403
Accrued liability	\$ (67,366)	\$ (21,992)

At December 31, 2014, the projected benefit obligations for the qualified and non-qualified pension plans were \$481 million and \$32 million, respectively. All pension plan assets are related to the qualified pension plan.

Amounts recognized in the balance sheets at December 31, 2014 and 2013 related to the Company's pension plans consist of the following:

	2014	2013
	<i>(in thousands)</i>	
Prepaid pension costs	\$ —	\$ 5,698
Other regulatory assets, deferred	150,972	77,572
Other current liabilities	(2,337)	(2,134)
Employee benefit obligations	(65,029)	(25,556)

Presented below are the amounts included in regulatory assets at December 31, 2014 and 2013 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 2015.

	2014	2013	Estimated Amortization in 2015
	<i>(in thousands)</i>		
Prior service cost	\$ 3,030	\$ 4,118	\$ 1,088
Net (gain) loss	147,942	73,454	10,293
Regulatory assets	\$ 150,972	\$ 77,572	

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The changes in the balance of regulatory assets related to the defined benefit pension plans for the years ended December 31, 2014 and 2013 are presented in the following table:

	2014	2013
	<i>(in thousands)</i>	
Regulatory assets:		
Beginning balance	\$ 77,572	\$ 146,838
Net (gain) loss	79,425	(58,662)
Reclassification adjustments:		
Amortization of prior service costs	(1,088)	(1,143)
Amortization of net gain (loss)	(4,937)	(9,461)
Total reclassification adjustments	(6,025)	(10,604)
Total change	73,400	(69,266)
Ending balance	\$ 150,972	\$ 77,572

Components of net periodic pension cost were as follows:

	2014	2013	2012
	<i>(in thousands)</i>		
Service cost	\$ 10,123	\$ 11,067	\$ 9,416
Interest cost	20,093	18,062	18,019
Expected return on plan assets	(28,742)	(26,849)	(24,121)
Recognized net (gain) loss	4,937	9,461	4,100
Net amortization	1,088	1,143	1,309
Net periodic pension cost	\$ 7,499	\$ 12,884	\$ 8,723

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, 2014, estimated benefit payments were as follows:

	Benefit Payments
	<i>(in thousands)</i>
2015	\$ 23,304
2016	19,551
2017	20,816
2018	21,905
2019	23,337
2020 to 2024	135,320

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Other Postretirement Benefits

Changes in the APBO and in the fair value of plan assets during the plan years ended December 31, 2014 and 2013 were as follows:

	2014	2013
	<i>(in thousands)</i>	
Change in benefit obligation		
Benefit obligation at beginning of year	\$ 80,940	\$ 91,783
Service cost	1,025	1,151
Interest cost	3,812	3,619
Benefits paid	(4,887)	(4,080)
Actuarial (gain) loss	14,259	(11,959)
Retiree drug subsidy	506	426
Balance at end of year	95,655	80,940
Change in plan assets		
Fair value of plan assets at beginning of year	23,277	21,990
Actual return on plan assets	1,814	2,379
Employer contributions	3,413	2,562
Benefits paid	(4,381)	(3,654)
Fair value of plan assets at end of year	24,123	23,277
Accrued liability	\$ (71,532)	\$ (57,663)

Amounts recognized in the balance sheets at December 31, 2014 and 2013 related to the Company's other postretirement benefit plans consist of the following:

	2014	2013
	<i>(in thousands)</i>	
Other regulatory assets, deferred	\$ 18,345	\$ 5,227
Other regulatory liabilities, deferred	(2,011)	(3,111)
Employee benefit obligations	(71,532)	(57,663)

Presented below are the amounts included in net regulatory assets (liabilities) at December 31, 2014 and 2013 related to the other postretirement benefit plans that had not yet been recognized in net periodic other postretirement benefit cost along with the estimated amortization of such amounts for 2015.

	2014	2013	Estimated Amortization in 2015
	<i>(in thousands)</i>		
Prior service cost	\$ (2,123)	\$ (2,311)	\$ (188)
Net (gain) loss	18,457	4,427	778
Net regulatory assets	\$ 16,334	\$ 2,116	

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The changes in the balance of net regulatory assets (liabilities) related to the other postretirement benefit plans for the plan years ended December 31, 2014 and 2013 are presented in the following table:

	2014	2013
	<i>(in thousands)</i>	
Net regulatory assets (liabilities):		
Beginning balance	\$ 2,116	\$ 15,454
Net (gain) loss	14,030	(12,867)
Reclassification adjustments:		
Amortization of prior service costs	188	188
Amortization of net gain (loss)	—	(659)
Total reclassification adjustments	188	(471)
Total change	14,218	(13,338)
Ending balance	\$ 16,334	\$ 2,116

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

	2014	2013	2012
	<i>(in thousands)</i>		
Service cost	\$ 1,025	\$ 1,151	\$ 1,038
Interest cost	3,812	3,619	4,155
Expected return on plan assets	(1,585)	(1,472)	(1,552)
Net amortization	(188)	471	470
Net periodic postretirement benefit cost	\$ 3,064	\$ 3,769	\$ 4,111

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
	<i>(in thousands)</i>		
2015	\$ 5,387	\$ (512)	\$ 4,875
2016	5,632	(566)	5,066
2017	5,911	(622)	5,289
2018	6,185	(680)	5,505
2019	6,475	(735)	5,740
2020 to 2024	34,139	(3,744)	30,395

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.

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The composition of the Company's pension plan and other postretirement benefit plan assets as of December 31, 2014 and 2013, along with the targeted mix of assets for each plan, is presented below:

	Target	2014	2013
Pension plan assets:			
Domestic equity	26%	30%	31%
International equity	25	23	25
Fixed income	23	27	23
Special situations	3	1	1
Real estate investments	14	14	14
Private equity	9	5	6
Total	100%	100%	100%
Other postretirement benefit plan assets:			
Domestic equity	21%	24%	25%
International equity	21	19	20
Domestic fixed income	37	41	38
Special situations	3	1	1
Real estate investments	11	11	11
Private equity	7	4	5
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.

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, 2014 and 2013. 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

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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 depository 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 and private equity.** Investments in private equity and real estate are generally classified as Level 3 as the underlying assets typically do not have observable inputs. The fund manager values the assets using various inputs and techniques depending on the nature of the underlying investments. In the case of private equity, techniques may include purchase multiples for comparable transactions, comparable public company trading multiples, and discounted cash flow analysis. Real estate managers generally use prevailing market capitalization rates, recent sales of comparable investments, and independent third-party appraisals to value underlying real estate investments. The fair value of partnerships is determined by aggregating the value of the underlying assets.

The fair values of pension plan assets as of December 31, 2014 and 2013 are presented below. These fair value measurements exclude cash, receivables related to investment income, pending investments sales, and payables related to pending investment purchases. Assets that are considered special situations investments, primarily real estate investments and private equities, are presented in the tables below based on the nature of the investment.

As of December 31, 2014:	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	<i>(in thousands)</i>			
Assets:				
Domestic equity*	\$ 78,344	\$ 32,366	\$ —	\$ 110,710
International equity*	49,170	45,313	—	94,483
Fixed income:				
U.S. Treasury, government, and agency bonds	—	32,145	—	32,145
Mortgage- and asset-backed securities	—	8,646	—	8,646
Corporate bonds	—	52,185	—	52,185
Pooled funds	—	23,632	—	23,632
Cash equivalents and other	133	30,327	—	30,460
Real estate investments	13,479	—	51,520	64,999
Private equity	—	—	26,203	26,203
Total	\$ 141,126	\$ 224,614	\$ 77,723	\$ 443,463
Liabilities:				
Derivatives	\$ (89)	\$ —	\$ —	\$ (89)
Total	\$ 141,037	\$ 224,614	\$ 77,723	\$ 443,374

* Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds. Management believes that the portfolio is well-diversified with no significant concentrations of risk.

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As of December 31, 2013:	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	<i>(in thousands)</i>			
Assets:				
Domestic equity*	\$ 63,558	\$ 37,206	\$ —	\$ 100,764
International equity*	48,829	45,146	—	93,975
Fixed income:				
U.S. Treasury, government, and agency bonds	—	26,582	—	26,582
Mortgage- and asset-backed securities	—	6,904	—	6,904
Corporate bonds	—	43,420	—	43,420
Pooled funds	—	20,905	—	20,905
Cash equivalents and other	38	9,896	—	9,934
Real estate investments	11,546	—	44,341	55,887
Private equity	—	—	25,316	25,316
Total	\$ 123,971	\$ 190,059	\$ 69,657	\$ 383,687
Liabilities:				
Derivatives	\$ —	\$ (115)	\$ —	\$ (115)
Total	\$ 123,971	\$ 189,944	\$ 69,657	\$ 383,572

* Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds. Management believes that the portfolio is well-diversified with no significant concentrations of risk.

Changes in the fair value measurement of the Level 3 items in the pension plan assets valued using significant unobservable inputs for the years ended December 31, 2014 and 2013 were as follows:

	2014		2013	
	Real Estate Investments	Private Equity	Real Estate Investments	Private Equity
	<i>(in thousands)</i>			
Beginning balance	\$ 44,341	\$ 25,316	\$ 37,196	\$ 26,240
Actual return on investments:				
Related to investments held at year end	5,253	3,269	3,385	378
Related to investments sold during the year	1,525	(745)	1,316	2,300
Total return on investments	6,778	2,524	4,701	2,678
Purchases, sales, and settlements	401	(1,637)	2,444	(3,602)
Ending balance	\$ 51,520	\$ 26,203	\$ 44,341	\$ 25,316

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The fair values of other postretirement benefit plan assets as of December 31, 2014 and 2013 are presented below. These fair value measurements exclude cash, receivables related to investment income, pending investments sales, and payables related to pending investment purchases. Assets that are considered special situations investments, primarily real estate investments and private equities, are presented in the tables below based on the nature of the investment.

As of December 31, 2014:	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	<i>(in thousands)</i>			
Assets:				
Domestic equity*	\$ 3,450	\$ 1,425	\$ —	\$ 4,875
International equity*	2,165	1,997	—	4,162
Fixed income:				
U.S. Treasury, government, and agency bonds	—	5,279	—	5,279
Mortgage- and asset-backed securities	—	380	—	380
Corporate bonds	—	2,301	—	2,301
Pooled funds	—	1,041	—	1,041
Cash equivalents and other	589	1,337	—	1,926
Real estate investments	593	—	2,269	2,862
Private equity	—	—	1,154	1,154
Total	\$ 6,797	\$ 13,760	\$ 3,423	\$ 23,980
Liabilities:				
Derivatives	\$ (5)	\$ —	\$ —	\$ (5)
Total	\$ 6,792	\$ 13,760	\$ 3,423	\$ 23,975

* Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds. Management believes that the portfolio is well-diversified with no significant concentrations of risk.

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As of December 31, 2013:	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	<i>(in thousands)</i>			
Assets:				
Domestic equity*	\$ 3,089	\$ 1,809	\$ —	\$ 4,898
International equity*	2,375	2,193	—	4,568
Fixed income:				
U.S. Treasury, government, and agency bonds	—	5,213	—	5,213
Mortgage- and asset-backed securities	—	337	—	337
Corporate bonds	—	2,109	—	2,109
Pooled funds	—	1,016	—	1,016
Cash equivalents and other	1	968	—	969
Real estate investments	560	—	2,156	2,716
Private equity	—	—	1,231	1,231
Total	\$ 6,025	\$ 13,645	\$ 3,387	\$ 23,057
Liabilities:				
Derivatives	\$ —	\$ (5)	\$ —	\$ (5)
Total	\$ 6,025	\$ 13,640	\$ 3,387	\$ 23,052

* Level 1 securities consist of actively traded stocks while Level 2 securities consist of pooled funds. Management believes that the portfolio is well-diversified with no significant concentrations of risk.

Changes in the fair value measurement of the Level 3 items in the other postretirement benefit plan assets valued using significant unobservable inputs for the years ended December 31, 2014 and 2013 were as follows:

	2014		2013	
	Real Estate Investments	Private Equity	Real Estate Investments	Private Equity
	<i>(in thousands)</i>			
Beginning balance	\$ 2,156	\$ 1,231	\$ 1,865	\$ 1,293
Actual return on investments:				
Related to investments held at year end	28	28	158	18
Related to investments sold during the year	67	(33)	64	110
Total return on investments	95	(5)	222	128
Purchases, sales, and settlements	18	(72)	69	(190)
Ending balance	\$ 2,269	\$ 1,154	\$ 2,156	\$ 1,231

Employee Savings Plan

The Company also sponsors a 401(k) defined contribution plan covering substantially all employees. The Company provides an 85% matching contribution on up to 6% of an employee's base salary. Total matching contributions made to the plan for 2014, 2013, and 2012 were \$4.6 million, \$4.1 million, and \$3.9 million, respectively.

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

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property damage, personal injury, common law nuisance, and citizen enforcement of environmental requirements such as air quality and water standards, has occurred throughout the U.S. This litigation has included claims for damages alleged to have been caused by CO₂ 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

New Source Review Actions

As part of a nationwide enforcement initiative against the electric utility industry which began in 1999, the EPA brought civil enforcement actions in federal district court against Alabama Power alleging violations of the New Source Review (NSR) provisions of the Clean Air Act at certain coal-fired electric generating units, including a unit co-owned by the Company. These civil actions seek penalties and injunctive relief, including orders requiring installation of the best available control technologies at the affected units. These actions were filed concurrently with the issuance of notices of violation to the Company with respect to the Company's Plant Watson. The case against Alabama Power (including claims involving a unit co-owned by the Company) has been actively litigated in the U.S. District Court for the Northern District of Alabama, resulting in a settlement in 2006 of the alleged NSR violations at Plant Miller; voluntary dismissal of certain claims by the EPA; and a grant of summary judgment for Alabama Power on all remaining claims and dismissal of the case with prejudice in 2011. In September 2013, the U.S. Court of Appeals for the Eleventh Circuit affirmed in part and reversed in part the 2011 judgment in favor of Alabama Power, and the case has been transferred back to the U.S. District Court for the Northern District of Alabama for further proceedings.

The Company believes it complied with applicable laws and regulations in effect at the time the work in question took place. The Clean Air Act authorizes maximum civil penalties of \$25,000 to \$37,500 per day, per violation, depending on the date of the alleged violation. An adverse outcome could require substantial capital expenditures that cannot be determined at this time and could possibly require payment of substantial penalties. Such expenditures could affect future results of operations, cash flows, and financial condition if such costs are not recovered through regulated rates. The ultimate outcome of this matter cannot be determined at this time.

Environmental Remediation

The Company must comply with environmental laws and regulations that cover 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 properties. The Company has authority from the Mississippi PSC to recover approved environmental compliance costs through regulatory mechanisms.

In 2003, the Company and numerous other entities were designated by the Texas Commission on Environmental Quality (TCEQ) as potentially responsible parties at a site that was owned by an electric transformer company that handled the Company's transformers. The TCEQ approved the final site remediation plan in December 2013 and, on March 28, 2014, the impacted utilities, including the Company, agreed to commence remediation actions on the site. The Company's environmental remediation liability is \$0.5 million as of December 31, 2014 and is expected to be recovered through the ECO Plan.

The final outcome of this matter cannot now be determined. However, based on the currently known conditions at this site and the nature and extent of activities relating to this site, the Company does not believe that additional liabilities, if any, at this site would be material to the financial statements.

FERC Matters

In 2012, the Company entered into a settlement agreement with its wholesale customers with respect to the Company's request for revised rates under the wholesale cost-based electric tariff. The settlement agreement provided that base rates under the cost-based electric tariff increase by approximately \$22.6 million over a 12-month period with revised rates effective April 1, 2012. A significant portion of the difference between the requested base rate increase and the agreed upon rate increase was due to a change in the recovery methodology for the return on the Kemper IGCC CWIP. Under the settlement agreement, a portion of CWIP will continue to accrue AFUDC. The tariff customers specifically agreed to the same regulatory treatment for tariff ratemaking as the treatment approved for retail ratemaking by the Mississippi PSC with respect to (i) the accounting for Kemper IGCC-related costs that cannot be capitalized, (ii) the accounting for the lease termination and purchase of Plant Daniel Units 3 and 4, and (iii) the establishment of a regulatory asset for certain potential plant retirement costs.

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Also in 2012, the FERC approved a motion to place interim rates into effect beginning in May 2012. Later in 2012, the Company, with its wholesale customers, filed a final settlement agreement with the FERC. In May 2013, the Company received an order from the FERC accepting the settlement agreement.

In April 2013, the Company reached a settlement agreement with its wholesale customers and filed a request with the FERC for an additional increase in the MRA cost-based electric tariff, which was accepted by the FERC in May 2013. The 2013 settlement agreement provided that base rates under the MRA cost-based electric tariff will increase by approximately \$24.2 million annually, effective April 1, 2013.

On March 31, 2014, the Company reached a settlement agreement with its wholesale customers and filed a request with the FERC for an increase in the MRA cost-based electric tariff. The settlement agreement, accepted by the FERC on May 20, 2014, provides that base rates under the MRA cost-based electric tariff will increase approximately \$10.1 million annually, with revised rates effective for services rendered beginning May 1, 2014.

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 March 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. The ultimate outcome of this matter cannot be determined at this time.

Energy Efficiency

In July 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 required to be filed within six months of the order and will be in effect for two to three years. An annual report addressing the performance of all energy efficiency programs is required.

On June 3, 2014, the Mississippi PSC approved the Company's 2014 Energy Efficiency Quick Start Plan filing, which includes a portfolio of energy efficiency programs. On October 20, 2014, the Company filed a revised compliance filing, which proposed an increase of \$6.7 million in retail revenues for the period December 2014 through December 2015. The Mississippi PSC approved the revised filing on November 4, 2014.

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 projected revenue requirement, and the PEP lookback filing, which is filed after the year and allows for review of the actual revenue requirement compared to the projected filing. PEP was designed with the objective to reduce the impact of rate changes on the customer and provide incentives for the Company to keep customer prices low and customer satisfaction and reliability high. PEP is a mechanism for rate adjustments based on three indicators: price, customer satisfaction, and service reliability.

In 2011, the Company submitted its annual PEP lookback filing for 2010, which recommended no surcharge or refund. Later in 2011, the Company received a letter from the MPUS disputing 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 May 2013, the MPUS contested the Company's PEP lookback filing for 2012, which indicated a refund due to customers of \$4.7 million. Unresolved matters related to certain costs included in the 2010 PEP lookback filing, which are currently under review, also impact the 2012 PEP lookback filing.

In March 2013, the Mississippi PSC approved the projected PEP filing for 2013, which resulted in a rate increase of 1.9%, or \$15.3 million, annually, effective March 19, 2013. The Company may be entitled to \$3.3 million in additional revenues related to 2013 as a result of the late implementation of the 2013 PEP rate increase.

On March 18, 2014, the Company submitted its annual PEP lookback filing for 2013, which indicated no surcharge or refund. On March 31, 2014, the Mississippi PSC suspended the filing to allow more time for review.

On June 3, 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.

The ultimate outcome of these matters 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 are scheduled to be placed in service in September and November 2015, respectively. These units are jointly owned by the Company and Gulf Power, with 50% ownership each. The estimated total cost of the project is approximately \$660 million, with the Company's portion being \$330 million, excluding AFUDC. The Company's portion of the cost is expected to be recovered through the ECO Plan following the scheduled completion of the project. As of December 31, 2014, total project expenditures were \$518.2 million, of which the Company's portion was \$263.4 million, excluding AFUDC of \$19.2 million.

In August 2013, the Mississippi PSC approved the Company's 2013 ECO Plan filing which proposed no change in rates.

On August 1, 2014, the Company entered into a settlement agreement with the Sierra Club (Sierra Club Settlement Agreement) that, among other things, requires the Sierra Club to dismiss or withdraw all pending legal and regulatory challenges to the issuance of the CPCN to construct scrubbers on Plant Daniel Units 1 and 2. In addition, and consistent with the Company's ongoing evaluation of recent environmental rules and regulations, 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. 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, and cease burning coal and other solid fuel at Plant Greene County Units 1 and 2 (200 MWs) and begin operating those units solely on natural gas no later than April 2016. On August 28, 2014, the Chancery Court of Harrison County, Mississippi dismissed the Sierra Club's appeal related to the CPCN to construct scrubbers on Plant Daniel Units 1 and 2.

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. This request was made to minimize the potential rate impact to customers arising from pending and final environmental regulations which may require the premature retirement of some generating units. As of December 31, 2014, \$5.6 million of Plant Greene County costs and \$2.0 million of costs related to Plant Watson have been reclassified as a regulatory asset. These costs are expected to be recovered through the ECO plan and other existing cost recovery mechanisms. Additional costs associated with the remaining net book value of coal-related equipment will be reclassified to a regulatory asset at the time of retirement for Plants Watson and Greene County in 2015 and 2016, respectively. Approved regulatory asset costs will be amortized over a period to be determined by the Mississippi PSC. As a result, these decisions are not expected to have a material impact on the Company's financial statements. See "Other Matters – Sierra Club Settlement Agreement" herein for additional information.

The ultimate outcome of these matters 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; the most recent filing occurred on November 17, 2014. On January 13, 2015, the Mississippi PSC approved the 2015 retail fuel cost recovery factor, effective January 21, 2015. The retail fuel cost recovery factor will result in an annual increase of approximately \$7.9 million. At December 31, 2014, the amount of under-recovered retail fuel costs included in the balance sheets was \$2.5 million compared to a \$14.5 million over-recovered balance at December 31, 2013.

The Company also has a wholesale MRA and a Market Based (MB) fuel cost recovery factor. Effective January 1, 2015, the wholesale MRA fuel rate decreased resulting in an annual decrease of \$1.1 million. Effective February 1, 2015, the wholesale MB fuel rate decreased, resulting in an annual decrease of \$0.1 million. At December 31, 2014, the amount of over-recovered wholesale MRA fuel costs included in the balance sheets was \$0.2 million compared to an over-recovered balance of \$7.3 million at December 31, 2013. At December 31, 2014, the amount of over-recovered wholesale MB fuel costs included in the balance sheets was immaterial compared to an over-recovered balance of \$0.3 million at December 31, 2013. In addition, at December 31, 2014, the amount of over-recovered MRA emissions allowance cost included in the balance sheets was \$0.3 million compared to a \$3.8 million under-recovered balance at December 31, 2013. 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 May 6, 2014, the Mississippi PSC approved the Company's annual ad valorem tax adjustment factor filing for 2014, in which the Company requested an annual rate increase of 0.38%, or \$3.6 million in annual retail revenues, primarily due to an increase in property tax rates.

Baseload Act

In 2008, the Baseload Act was signed by the Governor of Mississippi. The Baseload Act authorizes, but does not require, the Mississippi PSC to adopt a cost recovery mechanism that includes in retail base rates, prior to and during construction, all or a portion of the prudently-incurred pre-construction and construction costs incurred by a utility in constructing a base load electric generating plant. Prior to the passage of the Baseload Act, such costs would traditionally be recovered only after the plant was placed in service. The Baseload Act also provides for periodic prudence reviews by the Mississippi PSC and prohibits the cancellation of any such generating plant without the approval of the Mississippi PSC. In the event of cancellation of the construction of the plant without approval of the Mississippi PSC, the Baseload Act authorizes the Mississippi PSC to make a public interest determination as to whether and to what extent the utility will be afforded rate recovery for costs incurred in connection with such cancelled generating plant. In the 2015 Mississippi Supreme Court (Court) decision, the Court declined to rule on the constitutionality of the Baseload Act. See "Integrated Coal Gasification Combined Cycle – Rate Recovery of Kemper IGCC Costs" and " – 2015 Mississippi Supreme Court Decision" herein for additional information.

Integrated Coal Gasification Combined Cycle

Kemper IGCC Overview

Construction of the Kemper IGCC is nearing completion and start-up activities will continue until the Kemper IGCC is placed in service. The Kemper IGCC will utilize an IGCC technology with an output capacity of 582 MWs. The Kemper IGCC will 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 IGCC. The mine, operated by North American Coal Corporation, started commercial operation in June 2013. In connection with the Kemper IGCC, the Company constructed and plans to operate approximately 61 miles of CO₂ pipeline infrastructure for the planned transport of captured CO₂ for use in enhanced oil recovery.

Kemper IGCC Schedule and Cost Estimate

In 2012, the Mississippi PSC issued the 2012 MPSC CPCN Order, a detailed order confirming the CPCN originally approved by the Mississippi PSC in 2010 authorizing the acquisition, construction, and operation of the Kemper IGCC.

The certificated cost estimate of the Kemper IGCC included in the 2012 MPSC CPCN Order was \$2.4 billion, net of \$245.3 million of DOE Grants and excluding the cost of the lignite mine and equipment, the cost of the CO₂ pipeline facilities, and AFUDC related to the Kemper IGCC. 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 IGCC 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 IGCC in service on natural gas on August 9, 2014 and continues to focus on completing the remainder of the Kemper IGCC, including the gasifier and the gas clean-up facilities, for which the in-service date is currently expected to occur in the first half of 2016.

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Recovery of the Kemper IGCC cost of the lignite mine and equipment, the cost of the CO₂ pipeline facilities, AFUDC, and certain general exceptions, including change of law, force majeure, and beneficial capital (which exists when the Company demonstrates that the purpose and effect of the construction cost increase is to produce efficiencies that will result in a neutral or favorable effect on customers relative to the original proposal for the CPCN) (Cost Cap Exceptions) and costs subject to the cost cap remain subject to review and approval by the Mississippi PSC. The Company's Kemper IGCC 2010 project estimate, current cost estimate (which includes the impacts of the Court's decision), and actual costs incurred as of December 31, 2014, as adjusted for the Court's decision, are as follows:

Cost Category	2010 Project Estimate ^(f)	Current Estimate	Actual Costs at 12/31/2014
	<i>(in billions)</i>		
Plant Subject to Cost Cap ^(a)	\$ 2.40	\$ 4.93	\$ 4.23
Lignite Mine and Equipment	0.21	0.23	0.23
CO ₂ Pipeline Facilities	0.14	0.11	0.10
AFUDC ^{(b)(c)}	0.17	0.63	0.45
Combined Cycle and Related Assets Placed in Service – Incremental ^(d)	—	0.02	0.00
General Exceptions	0.05	0.10	0.07
Deferred Costs ^{(e)(e)}	—	0.18	0.12
Total Kemper IGCC^{(a)(c)}	\$ 2.97	\$ 6.20	\$ 5.20

- (a) The 2012 MPSC CPCN Order approved a construction cost cap of up to \$2.88 billion, net of the DOE Grants and excluding the Cost Cap Exceptions. The Current Estimate and Actual Costs include non-incremental operating and maintenance costs related to the combined cycle and associated common facilities placed in service on August 9, 2014 that are subject to the \$2.88 billion cost cap and excludes post-in-service costs for the lignite mine. See "Rate Recovery of Kemper IGCC Costs – 2013 MPSC Rate Order" for additional information.
- (b) The Company's original estimate included recovery of financing costs during construction rather than the accrual of AFUDC. This approach was not approved by the Mississippi PSC in 2012 as described in "Rate Recovery of Kemper IGCC Costs."
- (c) Amounts in the Current Estimate reflect estimated costs through March 31, 2016.
- (d) Incremental operating and maintenance costs related to the combined cycle and associated common facilities placed in service on August 9, 2014, net of costs related to energy sales. See "Rate Recovery of Kemper IGCC Costs – 2013 MPSC Rate Order" for additional information.
- (e) The 2012 MPSC CPCN Order approved deferral of non-capital Kemper IGCC-related costs during construction as described in "Rate Recovery of Kemper IGCC Costs – Regulatory Assets and Liabilities."
- (f) The 2010 Project Estimate is the certificated cost estimate adjusted to include the certificated estimate for the CO₂ pipeline facilities which was approved in 2011 by the Mississippi PSC.

Of the total costs, including post-in-service costs for the lignite mine, incurred as of December 31, 2014, \$3.04 billion was included in property, plant, and equipment (which is net of the DOE Grants and estimated probable losses of \$2.05 billion), \$1.8 million in other property and investments, \$44.7 million in fossil fuel stock, \$32.5 million in materials and supplies, \$147.7 million in other regulatory assets, \$11.6 million in other deferred charges and assets, and \$23.6 million in AROs in the balance sheet, with \$1.1 million previously expensed.

The Company does not intend to seek any rate recovery or joint owner contributions for any costs related to the construction of the Kemper IGCC that exceed the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions. The Company recorded pre-tax charges to income for revisions to the cost estimate of \$868.0 million (\$536.0 million after tax), \$1.10 billion (\$680.5 million after tax), and \$78.0 million (\$48.2 million after tax) in 2014, 2013 and 2012, respectively. The increases to the cost estimate in 2014 primarily reflected costs related to extension of the project's schedule to ensure the required time for start-up activities and operational readiness, completion of construction, additional resources during start-up, and ongoing construction support during start-up and commissioning activities. The current estimate includes costs through March 31, 2016. Any further extension of the in-service date is currently estimated to result in additional base costs of approximately \$25 million to \$30 million per month, which includes maintaining necessary levels of start-up labor, materials, and fuel, as well as operational resources required to execute start-up and commissioning activities. Any further extension of the in-service date with respect to the Kemper IGCC would also increase costs for the Cost Cap Exceptions, which are not subject to the \$2.88 billion cost cap established by the Mississippi PSC. These costs include AFUDC, which is currently estimated to total approximately \$13 million per month, as well as carrying costs and operating expenses on Kemper IGCC assets placed in service and consulting and legal fees, which are being deferred as regulatory assets and are estimated to total approximately \$7 million per month.

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Any further cost increases and/or extensions of the in-service date with respect to the Kemper IGCC may result from factors including, but not limited to, labor costs and productivity, adverse weather conditions, shortages and inconsistent quality of equipment, materials, and labor, contractor or supplier delay, non-performance under construction or other agreements, operational readiness, including specialized operator training and required site safety programs, unforeseen engineering or design problems, start-up activities for this first-of-a-kind technology (including major equipment failure and system integration), and/or operational performance (including additional costs to satisfy any operational parameters ultimately adopted by the Mississippi PSC). In subsequent periods, any further changes in the estimated costs to complete construction and start-up of the Kemper IGCC subject to the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions, will be reflected in the Company's statements of operations and these changes could be material.

Rate Recovery of Kemper IGCC Costs

See "FERC Matters" for additional information regarding the Company's MRA cost-based tariff relating to recovery of a portion of the Kemper IGCC costs from the Company's wholesale customers. Rate recovery of the retail portion of the Kemper IGCC is subject to the jurisdiction of the Mississippi PSC. See Note 3 under "Retail Regulatory Matters – Baseload Act" for additional information. See "Investment Tax Credits and Bonus Depreciation" and "Section 174 Research and Experimental Deduction" herein for additional tax information related to the Kemper IGCC.

The ultimate outcome of the rate recovery matters discussed herein, including the resolution of legal challenges, determinations of prudence, and the specific manner of recovery of prudently-incurred costs, cannot be determined at this time, but could have a material impact on the Company's results of operations, financial condition, and liquidity.

2012 MPSC CPCN Order

The 2012 MPSC CPCN Order included provisions relating to both the Company's recovery of financing costs during the course of construction of the Kemper IGCC and the Company's recovery of costs following the date the Kemper IGCC is placed in service. With respect to recovery of costs following the in-service date of the Kemper IGCC, the 2012 MPSC CPCN Order provided for the establishment of operational cost and revenue parameters based upon assumptions in the Company's petition for the CPCN. The Company expects the Mississippi PSC to apply operational parameters in connection with the evaluation of the Rate Mitigation Plan (defined below) and other related proceedings during the operation of the Kemper IGCC. To the extent the Mississippi PSC determines the Kemper IGCC does not meet the operational parameters ultimately adopted by the Mississippi PSC or the Company incurs additional costs to satisfy such parameters, there could be a material adverse impact on the Company's financial statements.

2013 Settlement Agreement

In January 2013, the Company entered into a settlement agreement with the Mississippi PSC that, among other things, established the process for resolving matters regarding cost recovery related to the Kemper IGCC (2013 Settlement Agreement). Under the 2013 Settlement Agreement, the Company agreed to limit the portion of prudently-incurred Kemper IGCC costs to be included in retail rate base to the \$2.4 billion certificated cost estimate, plus the Cost Cap Exceptions, but excluding AFUDC, and any other costs permitted or determined to be excluded from the \$2.88 billion cost cap by the Mississippi PSC. The 2013 Settlement Agreement also allowed the Company to secure alternate financing for costs not otherwise recovered in any Mississippi PSC rate proceedings contemplated by the 2013 Settlement Agreement. The Court found the 2013 Settlement Agreement unenforceable due to a lack of public notice for the related proceedings. See "2015 Mississippi Supreme Court Decision" below for additional information.

Legislation to authorize a multi-year rate plan and legislation to provide for alternate financing through securitization of up to \$1.0 billion of prudently-incurred costs was enacted into law in February 2013. The Company's intent under the 2013 Settlement Agreement was to securitize (1) prudently-incurred costs in excess of the certificated cost estimate and up to the \$2.88 billion cost cap, net of the DOE Grants and excluding the Cost Cap Exceptions, (2) accrued AFUDC, and (3) other prudently-incurred costs, which include carrying costs from the estimated in-service date until securitization is finalized and other costs not included in the Rate Mitigation Plan as approved by the Mississippi PSC.

The Court's decision did not impact the Company's ability to utilize alternate financing through securitization, the 2012 MPSC CPCN Order, or the February 2013 legislation. See "2015 Mississippi Supreme Court Decision" below for additional information.

2013 MPSC Rate Order

Consistent with the terms of the 2013 Settlement Agreement, in March 2013, the Mississippi PSC issued the 2013 MPSC Rate Order approving retail rate increases of 15% effective March 19, 2013 and 3% effective January 1, 2014, which collectively were designed to collect \$156 million annually beginning in 2014. For the period from March 2013 through December 31, 2014,

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\$257.2 million had been collected primarily to be used to mitigate customer rate impacts after the Kemper IGCC is placed in service.

Because the 2013 MPSC Rate Order did not provide for the inclusion of CWIP in rate base as permitted by the Baseload Act, the Company continues to record AFUDC on the Kemper IGCC through the in-service date. The Company will not record AFUDC on any additional costs of the Kemper IGCC that exceed the \$2.88 billion cost cap, except for Cost Cap Exception amounts. The Company will continue to record AFUDC and collect and defer the approved rates through the in-service date until directed to do otherwise by the Mississippi PSC.

On August 18, 2014, the Company provided an analysis of the costs and benefits of placing the combined cycle and the associated common facilities portion of the Kemper IGCC in service, including the expected accounting treatment. The Company's analysis requested, among other things, confirmation of the Company's accounting treatment by the Mississippi PSC of the continued collection of rates as prescribed by the 2013 MPSC Rate Order, with the current recognition as revenue of the related equity return on all assets placed in service and the deferral of all remaining rate collections under the 2013 MPSC Rate Order to a regulatory liability account. See "2015 Mississippi Supreme Court Decision" for additional information regarding the decision of the Court which would discontinue the collection of, and require the refund of, all amounts previously collected under the 2013 MPSC Rate Order.

In addition, the Company's August 18, 2014 filing with the Mississippi PSC requested confirmation of the Company's accounting treatment by the Mississippi PSC of the continued accrual of AFUDC through the in-service date of the remainder of the Kemper IGCC and the deferral of operating costs for the combined cycle as regulatory assets. Under the Company's proposal, non-incremental costs that would have been incurred whether or not the combined cycle was placed in service would be included in a regulatory asset and would continue to be subject to the \$2.88 billion cost cap. Additionally, incremental costs that would not have been incurred if the combined cycle had not gone into service would be included in a regulatory asset and would not be subject to the cost cap because these costs are incurred to support operation of the combined cycle. All energy revenues associated with the combined cycle variable operating and maintenance expenses would be credited to this regulatory asset. See "Regulatory Assets and Liabilities" for additional information. Any action by the Mississippi PSC that is inconsistent with the treatment requested by the Company could have a material impact on the results of operations, financial condition, and liquidity of the Company.

2015 Mississippi Supreme Court Decision

On February 12, 2015, the Court issued its decision in the legal challenge to the 2013 MPSC Rate Order filed by Thomas A. Blanton. The Court reversed the 2013 MPSC Rate Order based on, among other things, its findings that (1) the Mirror CWIP rate treatment was not provided for under the Baseload Act and (2) the Mississippi PSC should have determined the prudence of Kemper IGCC costs before approving rate recovery through the 2013 MPSC Rate Order. The Court also found the 2013 Settlement Agreement unenforceable due to a lack of public notice for the related proceedings. The Court's ruling remands the matter to the Mississippi PSC to (1) fix by order the rates that were in existence prior to the 2013 MPSC Rate Order, (2) fix no rate increases until the Mississippi PSC is in compliance with the Court's ruling, and (3) enter an order refunding amounts collected under the 2013 MPSC Rate Order. Through December 31, 2014, the Company had collected \$257.2 million through rates under the 2013 MPSC Rate Order. Any required refunds would also include carrying costs. The Court's decision will become legally effective upon the issuance of a mandate to the Mississippi PSC. Absent specific instruction from the Court, the Mississippi PSC will determine the method and timing of the refund. The Company is reviewing the Court's decision and expects to file a motion for rehearing which would stay the Court's mandate until either the case is reheard and decided or seven days after the Court issues its order denying the Company's request for rehearing. The Company is also evaluating its regulatory options.

Rate Mitigation Plan

In March 2013, the Company, in compliance with the 2013 MPSC Rate Order, filed a revision to the proposed rate recovery plan with the Mississippi PSC for the Kemper IGCC for cost recovery through 2020 (Rate Mitigation Plan), which is still under review by the Mississippi PSC. The revenue requirements set forth in the Rate Mitigation Plan assume the sale of a 15% undivided interest in the Kemper IGCC to SMEPA and utilization of bonus depreciation, which currently requires that the related long-term asset be placed in service in 2015. In the Rate Mitigation Plan, the Company proposed recovery of an annual revenue requirement of approximately \$156 million of Kemper IGCC-related operational costs and rate base amounts, including plant costs equal to the \$2.4 billion certificated cost estimate. The 2013 MPSC Rate Order, which increased rates beginning in March 2013, was integral to the Rate Mitigation Plan, which contemplates amortization of the regulatory liability balance at the in-service date to be used to mitigate customer rate impacts through 2020, based on a fixed amortization schedule that requires approval by the Mississippi PSC. Under the Rate Mitigation Plan, the Company proposed annual rate recovery to remain the same from 2014

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through 2020, with the proposed revenue requirement approximating the forecasted cost of service for the period 2014 through 2020. Under the Company's proposal, to the extent the actual annual cost of service differs from the approved forecast for certain items, the difference would be deferred as a regulatory asset or liability, subject to accrual of carrying costs, and would be included in the next year's rate recovery calculation. If any deferred balance remains at the end of 2020, the Mississippi PSC would review the amount and, if approved, determine the appropriate method and period of disposition. See "Regulatory Assets and Liabilities" and "Investment Tax Credits and Bonus Depreciation" for additional information.

To the extent that refunds of amounts collected under the 2013 MPSC Rate Order are required on a schedule different from the amortization schedule proposed in the Rate Mitigation Plan, the customer billing impacts proposed under the Rate Mitigation Plan would no longer be viable. See "2015 Mississippi Supreme Court Decision" above for additional information.

In the event that the Mirror CWIP regulatory liability is refunded to customers prior to the in-service date of the Kemper IGCC and is, therefore, not available to mitigate rate impacts under the Rate Mitigation Plan, the Mississippi PSC does not approve a refund schedule that facilitates rate mitigation, or the Company withdraws the Rate Mitigation Plan, the Company would seek rate recovery through alternate means, which could include a traditional rate case.

In addition to current estimated costs at December 31, 2014 of \$6.20 billion, the Company anticipates that it will incur additional costs after the Kemper IGCC in-service date until the Kemper IGCC cost recovery approach is finalized. These costs include, but are not limited to, regulatory costs and additional carrying costs which could be material. Recovery of these costs would be subject to approval by the Mississippi PSC.

Prudence Reviews

The Mississippi PSC's review of Kemper IGCC costs is ongoing. On August 5, 2014, the Mississippi PSC ordered that a consolidated prudence determination of all Kemper IGCC costs be completed after the entire project has been placed in service and has demonstrated availability for a reasonable period of time as determined by the Mississippi PSC and the MPUS. The Mississippi PSC has encouraged the parties to work in good faith to settle contested issues and the Company is working to reach a mutually acceptable resolution. As a result of the Court's decision, the Company intends to request that the Mississippi PSC reconsider its prudence review schedule. See "2015 Mississippi Supreme Court Decision" for additional information.

Regulatory Assets and Liabilities

Consistent with the treatment of non-capital costs incurred during the pre-construction period, the Mississippi PSC issued an accounting order in 2011 granting the Company the authority to defer all non-capital Kemper IGCC-related costs to a regulatory asset through the in-service date, subject to review of such costs by the Mississippi PSC. Such costs include, but are not limited to, carrying costs on Kemper IGCC assets currently placed in service, costs associated with Mississippi PSC and MPUS consultants, prudence costs, legal fees, and operating expenses associated with assets placed in service.

On August 18, 2014, the Company requested confirmation by the Mississippi PSC of the Company's authority to defer all operating expenses associated with the operation of the combined cycle subject to review of such costs by the Mississippi PSC. In addition, the Company is authorized to accrue carrying costs on the unamortized balance of such regulatory assets at a rate and in a manner to be determined by the Mississippi PSC in future cost recovery mechanism proceedings. As of December 31, 2014, the regulatory asset balance associated with the Kemper IGCC was \$147.7 million. The projected balance at March 31, 2016 is estimated to total approximately \$269.8 million. The amortization period of 40 years proposed by the Company for any such costs approved for recovery remains subject to approval by the Mississippi PSC.

The 2013 MPSC Rate Order approved retail rate increases of 15% effective March 19, 2013 and 3% effective January 1, 2014, which collectively were designed to collect \$156 million annually beginning in 2014. On February 12, 2015, the Court ordered the Mississippi PSC to refund Mirror CWIP and to fix by order the rates that were in existence prior to the 2013 MPSC Rate Order. The Company is deferring the collections under the approved rates in the Mirror CWIP regulatory liability until otherwise directed by the Mississippi PSC. The Company is also accruing carrying costs on the unamortized balance of the Mirror CWIP regulatory liability for the benefit of retail customers. As of December 31, 2014, the balance of the Mirror CWIP regulatory liability, including carrying costs, was \$270.8 million.

See "2015 Mississippi Supreme Court Decision" for additional information.

See Note 1 under "Regulatory Assets and Liabilities" for additional information.

Lignite Mine and CO₂ Pipeline Facilities

In conjunction with the Kemper IGCC, the Company will own the lignite mine and equipment and has acquired and will continue to acquire mineral reserves located around the Kemper IGCC site. The mine started commercial operation in June 2013.

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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 operating and managing the mining operations. The contract with Liberty Fuels is effective 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. In addition to the obligation to fund the reclamation activities, the Company currently provides 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 has constructed and will operate the CO₂ pipeline for the planned transport of captured CO₂ for use in enhanced oil recovery. The Company has entered into agreements with Denbury Onshore (Denbury), a subsidiary of Denbury Resources Inc., and Treetop Midstream Services, LLC (Treetop), an affiliate of Tellus Operating Group, LLC and a subsidiary of Tengrys, LLC, pursuant to which Denbury will purchase 70% of the CO₂ captured from the Kemper IGCC and Treetop will purchase 30% of the CO₂ captured from the Kemper IGCC. The agreements with Denbury and Treetop provide termination rights in the event that the Company does not satisfy its contractual obligation with respect to deliveries of captured CO₂ by May 11, 2015. While the Company has received no indication from either Denbury or Treetop of their intent to terminate their respective agreements, any termination could result in a material reduction in future chemical product sales revenues and could have a material financial impact on the Company to the extent the Company is not able to enter into other similar contractual arrangements.

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

Proposed Sale of Undivided Interest to SMEPA

In 2010, the Company and SMEPA entered into an APA whereby SMEPA agreed to purchase a 17.5% undivided interest in the Kemper IGCC. In 2012, the Mississippi PSC approved the sale and transfer of the 17.5% undivided interest in the Kemper IGCC to SMEPA. Later in 2012, the Company and SMEPA signed an amendment to the APA whereby SMEPA reduced its purchase commitment percentage from a 17.5% to a 15% undivided interest in the Kemper IGCC. In March 2013, the Company and SMEPA signed an amendment to the APA whereby the Company and SMEPA agreed to amend the power supply agreement entered into by the parties in 2011 to reduce the capacity amounts to be received by SMEPA by half (approximately 75 MWs) at the sale and transfer of the undivided interest in the Kemper IGCC to SMEPA. Capacity revenues under the 2011 power supply agreement were \$16.7 million in 2014. In December 2013, the Company and SMEPA agreed to extend SMEPA's option to purchase through December 31, 2014.

By letter agreement dated October 6, 2014, the Company and SMEPA agreed in principle on certain issues related to SMEPA's proposed purchase of a 15% undivided interest in the Kemper IGCC. The letter agreement contemplated certain amendments to the APA, which the parties anticipated to be incorporated into the APA on or before December 31, 2014. The parties agreed to further amend the APA as follows: (1) the Company agreed to cap at \$2.88 billion the portion of the purchase price payable for development and construction costs, net of the Cost Cap Exceptions, title insurance reimbursement, and AFUDC and/or carrying costs through the Closing Commitment Date (defined below); (2) SMEPA agreed to close the purchase within 180 days after the date of the execution of the amended APA or before the Kemper IGCC in-service date, whichever occurs first (Closing Commitment Date), subject only to satisfaction of certain conditions; and (3) AFUDC and/or carrying costs will continue to be accrued on the capped development and construction costs, the Cost Cap Exceptions, and any operating costs, net of revenues until the amended APA is executed by both parties, and thereafter AFUDC and/or carrying costs and payment of interest on SMEPA's deposited money will be suspended and waived provided closing occurs by the Closing Commitment Date. The letter agreement also provided for certain post-closing adjustments to address any differences between the actual and the estimated amounts of post-in-service date costs (both expenses and capital) and revenue credits for those portions of the Kemper IGCC previously placed in service.

By letter dated December 18, 2014, SMEPA notified the Company that SMEPA decided not to extend the estimated closing date in the APA or revise the APA to include the contemplated amendments; however, both parties agree that the APA will remain in effect until closing or until either party gives notice of termination.

The closing of this transaction is also conditioned upon execution of a joint ownership and operating agreement, the absence of material adverse effects, receipt of all construction permits, and appropriate regulatory approvals, as well as SMEPA's receipt of Rural Utilities Service (RUS) funding. In 2012, SMEPA received a conditional loan commitment from RUS for the purchase.

In 2012, on January 2, 2014, and on October 9, 2014, the Company received \$150 million, \$75 million, and \$50 million, respectively, of interest-bearing refundable deposits from SMEPA to be applied to the purchase. While the expectation is that these amounts will be applied to the purchase price at closing, the Company would be required to refund the deposits upon the termination of the APA or within 15 days of a request by SMEPA for a full or partial refund. Given the interest-bearing nature of

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the deposits and SMEPA's ability to request a refund, the deposits have been presented as a current liability in the balance sheet and as financing proceeds in the statement of cash flow. In July 2013, Southern Company entered into an agreement with SMEPA under which Southern Company has agreed to guarantee the obligations of the Company with respect to any required refund of the deposits.

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

Investment Tax Credits and Bonus Depreciation

The IRS allocated \$279.0 million (Phase II) of Internal Revenue Code Section 48A tax credits to the Company in connection with the Kemper IGCC. Through December 31, 2014, the Company had recorded tax benefits totaling \$276.4 million for the Phase II credits, of which approximately \$210.0 million had been utilized through that date. These credits will be amortized as a reduction to depreciation and amortization over the life of the Kemper IGCC and are dependent upon meeting the IRS certification requirements, including an in-service date no later than April 19, 2016 and the capture and sequestration (via enhanced oil recovery) of at least 65% of the CO₂ produced by the Kemper IGCC during operations in accordance with the Internal Revenue Code. The Company currently expects to place the Kemper IGCC in service in the first half of 2016. In addition, a portion of the Phase II tax credits will be subject to recapture upon completion of SMEPA's proposed purchase of an undivided interest in the Kemper IGCC as described above.

On December 19, 2014, the Tax Increase Prevention Act of 2014 (TIPA) was signed into law. The TIPA retroactively extended several tax credits through 2014 and extended 50% bonus depreciation for property placed in service in 2014 (and for certain long-term production-period projects to be placed in service in 2015). The extension of 50% bonus depreciation had a positive impact on the Company's cash flows and combined with bonus depreciation allowed in 2014 under the American Taxpayer Relief Act of 2012, resulted in approximately \$130 million of positive cash flows related to the combined cycle and associated common facilities portion of the Kemper IGCC for the 2014 tax year. The estimated cash flow benefit of bonus depreciation related to TIPA is expected to be approximately \$45 million to \$50 million for the 2015 tax year.

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, reduced tax payments for 2014 and included in its 2013 consolidated federal income tax return deductions for research and experimental (R&E) expenditures related to the Kemper IGCC. Due to the uncertainty related to this tax position, the Company recorded an unrecognized tax benefit of approximately \$160 million as of December 31, 2014. See Note 5 under "Unrecognized Tax Benefits" for additional information.

Other Matters

Sierra Club Settlement Agreement

On August 1, 2014, the Company entered into the Sierra Club Settlement Agreement that, among other things, requires the Sierra Club to dismiss or withdraw all pending legal and regulatory challenges of the Kemper IGCC and the scrubber project at Plant Daniel Units 1 and 2. In addition, the Sierra Club agreed to refrain from initiating, intervening in, and/or challenging certain legal and regulatory proceedings for the Kemper IGCC, including, but not limited to, the prudence review, and Plant Daniel for a period of three years from the date of the Sierra Club Settlement Agreement. On August 4, 2014, the Sierra Club filed all of the required motions necessary to dismiss or withdraw all appeals associated with certification of the Kemper IGCC and the Plant Daniel Units 1 and 2 scrubber project, which the applicable courts subsequently granted.

Under the Sierra Club Settlement Agreement, the Company agreed to, among other things, fund a \$15 million grant payable over a 15-year period for an energy efficiency and renewable program and contribute \$2 million to a conservation fund. In accordance with the Sierra Club Settlement Agreement, the Company paid \$7 million in 2014, recognized in other income (expense), net in the statement of operations. In addition, and consistent with the Company's ongoing evaluation of recent environmental rules and regulations, 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. 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, and cease burning coal and other solid fuel at Plant Greene County Units 1 and 2 (200 MWs) and begin operating those units solely on natural gas no later than April 2016. See Note 3 under "Retail Regulatory Matters – Environmental Compliance Overview Plan" for additional information.

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.

In August 2014, a decision was made to cease coal operations at Greene County Steam Plant and convert to natural gas no later than April 16, 2016. As a result, active construction projects related to these assets were cancelled in September 2014. Associated amounts in CWIP of \$5.6 million, reflecting the Company's share of the costs, were subsequently transferred to regulatory assets. See Note 3 under "Retail Regulatory Matters-Environmental Compliance Overview Plan" herein for additional information.

At December 31, 2014, 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
<i>(in thousands)</i>				
Greene County				
Units 1 and 2	40%	\$ 102,384	\$ 51,911	\$ 902
Daniel				
Units 1 and 2	50%	\$ 299,440	\$ 155,606	\$ 286,240

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.

See Note 3 under "Retail Regulatory Matters – Environmental Compliance Overview Plan" for additional information.

5. INCOME TAXES

On behalf of the Company, Southern Company files a consolidated federal income tax return and combined state income tax returns for the States of Alabama and Mississippi. 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.

Current and Deferred Income Taxes

Details of income tax provisions are as follows:

	2014	2013	2012
<i>(in thousands)</i>			
Federal —			
Current	\$ (431,077)	\$ 23,345	\$ 1,212
Deferred	183,461	(342,870)	16,994
	(247,616)	(319,525)	18,206
State —			
Current	455	5,219	1,656
Deferred	(38,044)	(53,529)	694
	(37,589)	(48,310)	2,350
Total	\$ (285,205)	\$ (367,835)	\$ 20,556

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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:

	2014	2013
	<i>(in thousands)</i>	
Deferred tax liabilities —		
Accelerated depreciation	\$ 1,068,242	\$ 371,553
Property basis differences	—	130,679
ECM under recovered	—	1,777
Regulatory assets associated with AROs	19,299	16,764
Pensions and other benefits	35,200	23,769
Regulatory assets associated with employee benefit obligations	67,727	33,127
Regulatory assets associated with the Kemper IGCC	61,561	30,708
Rate differential	89,040	56,074
Federal effect of state deferred taxes	1,279	30,615
Fuel clause under recovered	3,288	—
Other	52,215	35,583
Total	1,397,851	730,649
Deferred tax assets —		
Fuel clause over recovered	—	7,741
Estimated loss on Kemper IGCC	631,326	472,000
Pension and other benefits	92,232	57,999
Property insurance	24,315	23,693
Premium on long-term debt	20,694	23,736
Unbilled fuel	14,535	12,136
AROs	19,299	16,764
Interest rate hedges	4,544	5,094
Kemper rate factor - regulatory liability retail	108,312	36,210
Property basis difference	263,430	—
ECM over recovered	905	—
Deferred state tax assets	56,736	—
Other	15,111	18,094
Total	1,251,439	673,467
Total deferred tax liabilities, net	146,412	57,182
Portion included in (accrued) prepaid income taxes, net	121,049	15,626
Deferred state tax asset	17,388	—
Accumulated deferred income taxes	\$ 284,849	\$ 72,808

The application of bonus depreciation provisions in current tax law has significantly increased deferred tax liabilities related to accelerated depreciation.

At December 31, 2014, the tax-related regulatory assets were \$226.2 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 to taxes applicable to capitalized interest.

At December 31, 2014, the tax-related regulatory liabilities were \$9.4 million. These liabilities are primarily attributable to deferred taxes previously recognized at rates higher than the current enacted tax law and to 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 IGCC

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related deferred ITCs amortized in this manner amounted to \$1.4 million, \$1.2 million, and \$1.2 million for 2014, 2013, and 2012, respectively. At December 31, 2014, all non-Kemper IGCC ITCs available to reduce federal income taxes payable had been utilized.

In 2010, the Company began recognizing ITCs associated with the construction expenditures related to the Kemper IGCC. At December 31, 2014, the Company had \$276.4 million in unamortized ITCs associated with the Kemper IGCC, which will be amortized over the life of the Kemper IGCC once placed in service and are dependent upon meeting the IRS certification requirements, including an in-service date no later than April 19, 2016 and the capture and sequestration (via enhanced oil recovery) of at least 65% of the CO₂ produced by the Kemper IGCC during operation in accordance with the Internal Revenue Code. A portion of the tax credits will be subject to recapture upon successful completion of SMEPA's proposed purchase of an undivided interest in the Kemper IGCC.

Effective Tax Rate

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

	2014	2013	2012
Federal statutory rate	(35.0)%	(35.0)%	35.0%
State income tax, net of federal deduction	(4.0)	(3.7)	1.3
Non-deductible book depreciation	0.1	0.1	0.3
AFUDC-equity	(7.8)	(5.0)	(18.6)
Other	0.1	(0.1)	(1.2)
Effective income tax rate (benefit rate)	(46.6)%	(43.7)%	16.8%

The increase in the Company's 2014 effective tax rate (benefit rate), as compared to 2013, is primarily due to an increase in non-taxable AFUDC equity. The decrease in the Company's 2013 effective tax rate, as compared to 2012, is primarily due to an increase in the estimated losses associated with the Kemper IGCC and an increase in non-taxable AFUDC equity.

Unrecognized Tax Benefits

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

	2014	2013	2012
		<i>(in thousands)</i>	
Unrecognized tax benefits at beginning of year	\$ 3,840	\$ 5,755	\$ 4,964
Tax positions from current periods	58,148	226	1,186
Tax positions from prior periods	102,833	(2,141)	(26)
Settlements with taxing authorities	—	—	(369)
Balance at end of year	\$ 164,821	\$ 3,840	\$ 5,755

The increases in tax positions from current periods and prior periods for 2014 relate to deductions for R&E expenditures related to the Kemper IGCC. See Note 3 under "Integrated Coal Gasification Combined Cycle – Section 174 Research and Experimental Deduction" for more information. The decrease in tax positions from prior periods for 2013 relates primarily to the tax accounting method change for repairs related to generation assets. See "Tax Method of Accounting for Repairs" below for additional information.

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

	2014	2013	2012
		<i>(in thousands)</i>	
Tax positions impacting the effective tax rate	\$ 4,341	\$ 3,840	\$ 3,656
Tax positions not impacting the effective tax rate	160,480	—	2,099
Balance of unrecognized tax benefits	\$ 164,821	\$ 3,840	\$ 5,755

The tax positions impacting the effective tax rate primarily relate to state income tax credits. The tax positions not impacting the effective tax rate for 2014 relate to a deduction for R&E related to the Kemper IGCC. The tax positions not impacting the

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effective tax rate for 2012 relate to the tax accounting method change for repairs related to generation assets. These amounts are presented on a gross basis without considering the related federal or state income tax impact.

Accrued interest for unrecognized tax benefits was as follows:

	2014	2013	2012
		<i>(in thousands)</i>	
Interest accrued at beginning of year	\$ 1,171	\$ 772	\$ 680
Interest accrued during the year	1,698	399	92
Balance at end of year	\$ 2,869	\$ 1,171	\$ 772

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 2012. Southern Company has filed its 2013 federal income tax return and has received a partial acceptance letter from the IRS; however, the IRS has not finalized its audit. 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.

Tax Method of Accounting for Repairs

In 2011, the IRS published regulations on the deduction and capitalization of expenditures related to tangible property that generally apply for tax years beginning on or after January 1, 2014. Additionally, in April 2013, the IRS issued Revenue Procedure 2013-24, which provides guidance for taxpayers related to the deductibility of repair costs associated with generation assets. Based on a review of the regulations, Southern Company incorporated provisions related to repair costs for generation assets into its consolidated 2012 federal income tax return and reversed all related unrecognized tax positions. In September 2013, the IRS issued Treasury Decision 9636, "Guidance Regarding Deduction and Capitalization of Expenditures Related to Tangible Property," which are final tangible property regulations applicable to taxable years beginning on or after January 1, 2014. Southern Company continues to review this guidance; however, these regulations are not expected to have a material impact on the Company's financial statements.

6. FINANCING

Bank Term Loans

In January 2014, the Company entered into an 18-month floating rate bank loan bearing interest based on one-month LIBOR. The term loan was for \$250 million aggregate principal amount and the proceeds were used for working capital and other general corporate purposes, including the Company's continuous construction program.

At December 31, 2014 and 2013, the Company had \$775 million and \$525 million of bank loans outstanding, respectively, which are reflected in the statements of capitalization as securities due within one year and long-term debt.

These bank loans have covenants that limit debt levels to 65% of total capitalization, as defined in the agreements. For purposes of these definitions, debt excludes any long-term debt payable to affiliated trusts, other hybrid securities, and any securitized debt relating to the securitization of certain costs of the Kemper IGCC. At December 31, 2014, the Company was in compliance with its debt limits.

Senior Notes

At December 31, 2014 and 2013, the Company had \$1.1 billion of senior notes outstanding. 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.

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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 \$346.1 million, reflecting a premium of \$76.1 million.

Securities Due Within One Year

A summary of scheduled maturities and redemptions of securities due within one year at December 31, 2014 and 2013 was as follows:

	2014	2013
	<i>(in millions)</i>	
Bank term loans	\$ 775.0	\$ —
Revenue bonds	—	11.3
Capitalized leases	2.7	2.5
Outstanding at December 31	\$ 777.7	\$ 13.8

Maturities through 2019 applicable to total long-term debt are as follows: \$777.7 million in 2015, \$302.8 million in 2016, \$37.9 million in 2017, \$3.1 million in 2018, and \$128.2 million in 2019.

Pollution Control Revenue Bonds

Pollution control obligations represent loans to the Company from public authorities of funds derived from sales by such authorities of 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, 2014 and 2013 was \$82.7 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 IGCC and related facilities.

In November 2013, the MBFC entered into an agreement to issue up to \$33.75 million aggregate principal amount of MBFC Taxable Revenue Bonds, Series 2013A (Mississippi Power Company Project) and up to \$11.25 million aggregate principal amount of MBFC Taxable Revenue Bonds, Series 2013B (Mississippi Power Company Project) for the benefit of the Company. In November 2013, the MBFC issued \$11.25 million aggregate principal amount of MBFC Taxable Revenue Bonds (Mississippi Power Company Project), Series 2013B for the benefit of the Company.

In May 2014 and August 2014, the MBFC issued \$12.3 million and \$10.5 million, respectively, aggregate principal amount of MBFC Taxable Revenue Bonds (Mississippi Power Company Project), Series 2013A for the benefit of the Company and proceeds were used to reimburse the Company for the cost of the acquisition, construction, equipping, installation, and improvement of certain equipment and facilities for the lignite mining facility related to the Kemper IGCC. In December 2014, the MBFC Taxable Revenue Bonds (Mississippi Power Company Project), Series 2013A of \$22.87 million and Series 2013B of \$11.25 million were paid at maturity. The Company had \$50.0 million of such obligations outstanding related to tax-exempt revenue bonds at December 31, 2014 and 2013. The Company had no obligation as of December 31, 2014 and \$11.3 million of such obligations related to taxable revenue bonds outstanding at December 31, 2013. Such amounts are reflected in the statements of capitalization as long-term senior notes and debt.

The Company's agreements relating to the taxable revenue bonds include covenants limiting debt levels consistent with those described above under "Bank Term Loans."

Capital Leases

In September 2013, the Company entered into an agreement to sell the air separation unit for the Kemper IGCC 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 at December 31, 2014 of \$80.0 million with an annual interest rate of 4.9%. There are no contingent rentals in the contract and a portion of the monthly payment specified in the agreement is 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 2014 were \$6.5 million and will be \$6.5 million each year thereafter. Amortization of the capital lease asset for the air separation unit will begin when the Kemper IGCC is placed in service.

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Other Obligations

In 2012, January 2014, and October 2014, the Company received \$150 million, \$75 million, and \$50 million, respectively, interest-bearing refundable deposits from SMEPA to be applied to the sale price for the pending sale of an undivided interest in the Kemper IGCC. Until the sale is closed, the deposits bear interest at the Company's AFUDC rate adjusted for income taxes, which was 10.134% per annum for 2014, 9.932% per annum for 2013, and 9.967% per annum for 2012, and are refundable to SMEPA upon termination of the APA related to such purchase or within 15 days of a request by SMEPA for a full or partial refund.

In May 2014, the Company issued a 19-month floating rate promissory note to Southern Company for a loan bearing interest based on one-month LIBOR. This loan was for \$220 million aggregate principal amount and the proceeds were used for working capital and other general corporate purposes, including the Company's construction program. This loan was repaid in September 2014.

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.

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.

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, 2014, committed credit arrangements with banks were as follows:

<u>Expires</u>				<u>Executable Term-Loans</u>		<u>Due Within One Year</u>	
<u>2015</u>	<u>2016</u>	<u>Total</u>	<u>Unused</u>	<u>One Year</u>	<u>Two Years</u>	<u>Term Out</u>	<u>No Term Out</u>
		<i>(in millions)</i>					
\$135	\$165	\$300	\$300	\$25	\$40	\$65	\$70

Subject to applicable market conditions, the Company expects to renew its bank credit arrangements, as needed, prior to expiration.

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 and any securitized debt relating to the securitization of certain costs of the Kemper IGCC.

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A portion of the \$300 million unused credit with banks is allocated to provide liquidity support to the Company's variable rate 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, 2014 was \$40.1 million.

The Company makes short-term borrowings primarily through a commercial paper program that has the liquidity support of the Company's committed bank credit arrangements.

At December 31, 2014 and 2013, there was no 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 2014, 2013, and 2012, the Company incurred fuel expense of \$573.9 million, \$491.3 million, and \$411.2 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.

Coal commitments include a management fee associated with a 40-year management contract with Liberty Fuels related to the Kemper IGCC with the remaining amount as of December 31, 2014 of \$38.4 million. Additional commitments for fuel will be required to supply the Company's future needs.

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 operating companies and Southern Power. Under these agreements, each of the traditional 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 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.

Operating Leases

The Company has operating lease agreements with various terms and expiration dates. Total rent expense was \$12.7 million, \$10.1 million, and \$11.1 million for 2014, 2013, and 2012, respectively.

The Company and Gulf Power have jointly entered into operating lease agreements for aluminum railcars for the transportation of coal at Plant Daniel. 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 has one remaining operating lease which has 229 aluminum railcars. The Company and Gulf Power also have separate lease agreements for other railcars that do not contain a purchase option.

The Company's share (50%) of the leases, charged to fuel stock and recovered through the fuel cost recovery clause, was \$4.9 million in 2014, \$3.1 million in 2013, and \$3.6 million in 2012. The Company's annual railcar lease payments for 2015 through 2017 will average approximately \$1.6 million. The Company has no lease obligations for the period 2018 and thereafter.

In addition to railcar leases, the Company has other operating leases for fuel handling equipment at Plants Daniel and Watson and operating leases for barges and tow/shift boats for the transport of coal at Plant Watson. The Company's share (50% at Plant Daniel and 100% at Plant Watson) of the leases for fuel handling was charged to fuel handling expense in the amount of \$0.2 million annually from 2012 through 2014. The Company's annual lease payment for 2015 is expected to be \$0.1 million for fuel handling equipment. The Company charged to fuel stock and recovered through fuel cost recovery the barge transportation leases in the amount of \$7.5 million in 2014, \$6.7 million in 2013, and \$7.3 million in 2012 related to barges and tow/shift boats. The Company's annual lease payment for 2015 with respect to these barge transportation leases is expected to be \$1.8 million.

8. STOCK COMPENSATION

Stock Options

Southern Company provides non-qualified stock options through its Omnibus Incentive Compensation Plan to a large segment of the Company's system employees ranging from line management to executives. As of December 31, 2014, there were 244 current and former employees of the Company participating in the stock option program. The prices of options were at the fair market value of the shares on the dates of grant. These options become exercisable pro rata over a maximum period of three years from the date of grant. The Company generally recognizes stock option expense on a straight-line basis over the vesting period which equates to the requisite service period; however, for employees who are eligible for retirement, the total cost is expensed at the

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grant date. Options outstanding will expire no later than 10 years after the date of grant, unless terminated earlier by the Southern Company Board of Directors in accordance with the Omnibus Incentive Compensation Plan. Stock options held by employees of a company undergoing a change in control vest upon the change in control.

For the years ended December 31, 2014, 2013, and 2012, employees of the Company were granted stock options for 578,256 shares, 345,830 shares, and 278,709 shares, respectively. The weighted average grant-date fair value of stock options granted during 2014, 2013, and 2012, derived using the Black-Scholes stock option pricing model, was \$2.20, \$2.93, and \$3.39, respectively.

The compensation cost and tax benefits related to the grant of Southern Company stock options to the Company's employees and the exercise of stock options are recognized in the Company's financial statements with a corresponding credit to equity, representing a capital contribution from Southern Company. No cash proceeds are received by the Company upon the exercise of stock options. The amounts were not material for any year presented.

As of December 31, 2014, the amount of unrecognized compensation cost related to stock option awards not yet vested was immaterial.

The total intrinsic value of options exercised during the years ended December 31, 2014, 2013, and 2012 was \$5.4 million, \$2.7 million, and \$4.9 million, respectively. The actual tax benefit realized by the Company for the tax deductions from stock option exercises totaled \$2.1 million, \$1.1 million, and \$1.9 million for the years ended December 31, 2014, 2013, and 2012, respectively. As of December 31, 2014, the aggregate intrinsic value for the options outstanding and options exercisable was \$18.4 million and \$12.3 million, respectively.

Performance Shares

Southern Company provides performance share award units through its Omnibus Incentive Compensation Plan to a large segment of the Company's employees ranging from line management to executives. The performance share units granted under the plan vest at the end of a three-year performance period which equates to the requisite service period. Employees that retire prior to the end of the three-year period receive a pro rata number of shares, issued at the end of the performance period, based on actual months of service prior to retirement. The value of the award units is based on Southern Company's total shareholder return (TSR) over the three-year performance period which measures Southern Company's relative performance against a group of industry peers. The performance shares are delivered in common stock following the end of the performance period based on Southern Company's actual TSR and may range from 0% to 200% of the original target performance share amount. Performance share units held by employees of a company undergoing a change in control vest upon the change in control.

For the years ended December 31, 2014, 2013, and 2012, employees of the Company were granted performance share units of 49,579, 36,769, and 33,077, respectively. The weighted average grant-date fair value of performance share units granted during 2014, 2013, and 2012, 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 \$37.54, \$40.50, and \$41.99, respectively.

The Company recognizes compensation expense on a straight-line basis over the three-year performance period without remeasurement. Compensation expense for awards where the service condition is met is recognized regardless of the actual number of shares issued. For the years ended December 31, 2014, 2013, and 2012, total compensation cost for performance share units recognized in income was \$1.7 million, \$1.5 million, and \$1.2 million, respectively, with the related tax benefit also recognized in income of \$0.6 million, \$0.6 million, and \$0.4 million, respectively. The compensation cost and tax benefits related to the grant of Southern Company performance share units to the Company's employees are recognized in the Company's financial statements with a corresponding credit to equity, representing a capital contribution from Southern Company. As of December 31, 2014, there was \$1.8 million of total unrecognized compensation cost related to performance share award units that will be recognized over a weighted-average period of approximately 20 months.

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.

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- 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, 2014, assets and liabilities measured at fair value on a recurring basis during the period, together with the level of the fair value hierarchy in which they fall, were as follows:

	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
As of December 31, 2014:				
	<i>(in thousands)</i>			
Assets:				
Energy-related derivatives	\$ —	\$ 65	\$ —	\$ 65
Cash equivalents	114,900	—	—	114,900
Total	\$ 114,900	\$ 65	\$ —	\$ 114,965
Liabilities:				
Energy-related derivatives	\$ —	\$ 45,429	\$ —	\$ 45,429

As of December 31, 2013, assets and liabilities measured at fair value on a recurring basis during the period, together with the level of the fair value hierarchy in which they fall, were as follows:

	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
As of December 31, 2013:				
	<i>(in thousands)</i>			
Assets:				
Energy-related derivatives	\$ —	\$ 4,803	\$ —	\$ 4,803
Cash equivalents	125,000	—	—	125,000
Total	\$ 125,000	\$ 4,803	\$ —	\$ 129,803
Liabilities:				
Energy-related derivatives	\$ —	\$ 10,281	\$ —	\$ 10,281
Foreign currency derivatives	—	1	—	1
Total	\$ —	\$ 10,282	\$ —	\$ 10,282

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. Foreign currency derivatives are also standard over-the-counter financial products valued using the market approach. Inputs for foreign currency derivatives are from observable market sources. See Note 10 for additional information on how these derivatives are used.

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As of December 31, 2014 and 2013, the fair value measurements of investments calculated at net asset value per share (or its equivalent), as well as the nature and risks of those investments, were as follows:

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
As of December 31, 2014:				
	<i>(in thousands)</i>			
Cash equivalents:				
Money market funds	\$ 114,900	None	Daily	Not applicable
As of December 31, 2013:				
Cash equivalents:				
Money market funds	\$ 125,000	None	Daily	Not applicable

The money market funds are short-term investments of excess funds in various money market mutual funds, which are portfolios of short-term debt securities. The money market funds are regulated by the SEC and typically receive the highest rating from credit rating agencies. Regulatory and rating agency requirements for money market funds include minimum credit ratings and maximum maturities for individual securities and a maximum weighted average portfolio maturity. Redemptions are available on a same day basis up to the full amount of the Company's investment in the money market funds.

As of December 31, 2014 and 2013, other financial instruments for which the carrying amount did not equal fair value were as follows:

	Carrying Amount	Fair Value
	<i>(in thousands)</i>	
Long-term debt:		
2014	\$ 2,328,476	\$ 2,382,050
2013	\$ 2,098,639	\$ 2,045,519

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 and occasionally foreign currency 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 gross 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 and the cash impacts of settled foreign currency derivatives are recorded as investing 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 commodity fuel prices and prices of electricity. 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.

To mitigate residual risks relative to movements in electricity prices, the Company may enter into physical fixed-price or heat rate contracts for the purchase and sale of electricity through the wholesale electricity market. To mitigate residual risks relative to movements in gas prices, the Company may enter into fixed-price contracts for natural gas purchases; however, a significant portion of contracts are priced at market.

Energy-related derivative contracts are accounted for in one of three methods:

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- *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.
- *Cash Flow Hedges* – Gains and losses on energy-related derivatives designated as cash flow hedges which are mainly used to hedge anticipated purchases and sales and are initially deferred in OCI before being recognized in the statements of operations in the same period as the hedged transactions are reflected in earnings.
- *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, 2014, the net volume of energy-related derivative contracts for natural gas positions for the Company, together with the longest hedge date over which it is hedging its exposure to the variability in future cash flows for forecasted transactions and the longest date for derivatives not designated as hedges, were as follows:

Net Purchased mmBtu	Longest Hedge Date	Longest Non-Hedge Date
<i>(in millions)</i> 54	2018	—

For cash flow hedges, the amounts expected to be reclassified from accumulated OCI to earnings for the next 12-month period ending December 31, 2015 are immaterial.

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, 2014, there were no interest rate derivatives outstanding.

The estimated pre-tax losses that will be reclassified from accumulated OCI to interest expense for the 12-month period ending December 31, 2015 are \$1.4 million. The Company has deferred gains and losses that are expected to be amortized into earnings through 2022.

Foreign Currency Derivatives

The Company may enter into foreign currency derivatives to hedge exposure to changes in foreign currency exchange rates arising from purchases of equipment denominated in a currency other than U.S. dollars. Derivatives related to a firm commitment in a foreign currency transaction are accounted for as a fair value hedge where the derivatives' fair value gains or losses and the hedged items' fair value gains or losses are both recorded directly to earnings. Derivatives related to a forecasted transaction are accounted for as a cash flow hedge 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. Any ineffectiveness is typically recorded directly to earnings; however, the Company has regulatory approval allowing it to defer any ineffectiveness associated with firm commitments related to the Kemper IGCC to a regulatory asset. During 2011, certain fair value hedges were de-designated and subsequently settled in 2012. The ineffectiveness related to the de-designated hedges was recorded as a regulatory asset and was immaterial to the Company. The derivatives employed as hedging instruments are structured to minimize ineffectiveness.

At December 31, 2014, there were no foreign currency derivatives outstanding.

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Derivative Financial Statement Presentation and Amounts

At December 31, 2014 and 2013, the fair value of energy-related derivatives and foreign currency derivatives was reflected in the balance sheets as follows:

Derivative Category	Asset Derivatives			Liability Derivatives		
	Balance Sheet Location	2014	2013	Balance Sheet Location	2014	2013
		<i>(in thousands)</i>			<i>(in thousands)</i>	
Derivatives designated as hedging instruments for regulatory purposes						
Energy-related derivatives:						
	Other current assets	\$ 30	\$ 3,352	Other current liabilities	\$ 26,259	\$ 3,652
	Other deferred charges and assets	22	1,451	Other deferred credits and liabilities	19,159	6,629
Total derivatives designated as hedging instruments for regulatory purposes		\$ 52	\$ 4,803		\$ 45,418	\$ 10,281
Derivatives designated as hedging instruments in cash flow and fair value hedges						
Foreign currency derivatives:						
	Other current assets	\$ —	\$ —	Other current liabilities	\$ —	\$ 1
Total		\$ 52	\$ 4,803		\$ 45,418	\$ 10,282

Energy-related derivatives not designated as hedging instruments were immaterial for 2014 and 2013. The derivative contracts of the Company are not subject to master netting arrangements or similar agreements and are reported gross on the Company's financial statements. Some of these energy-related derivative contracts 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. Amounts related to energy-related derivative contracts at December 31, 2014 and 2013 are presented in the following tables.

Assets	Fair Value				
	2014	2013	Liabilities	2014	2013
	<i>(in thousands)</i>			<i>(in thousands)</i>	
Energy-related derivatives presented in the Balance Sheet ^(a)	\$ 65	\$ 4,803	Energy-related derivatives presented in the Balance Sheet ^(a)	\$ 45,429	\$ 10,282
Gross amounts not offset in the Balance Sheet ^(b)	(64)	(3,856)	Gross amounts not offset in the Balance Sheet ^(b)	(64)	(3,856)
Net energy-related derivative assets	\$ 1	\$ 947	Net energy-related derivative liabilities	\$ 45,365	\$ 6,426

(a) The Company does not offset fair value amounts for multiple derivative instruments executed with the same counterparty on the balance sheets; therefore, gross and net amounts of derivative assets and liabilities presented on the balance sheets are the same.

(b) Includes gross amounts subject to netting terms that are not offset on the balance sheets and any cash/financial collateral pledged or received.

NOTES (continued)
Mississippi Power Company 2014 Annual Report

At December 31, 2014 and 2013, the pre-tax effects of unrealized derivative gains (losses) arising from energy-related derivative instruments designated as regulatory hedging instruments and deferred on the balance sheets were as follows:

Derivative Category	Balance Sheet Location	Unrealized Losses		Balance Sheet Location	Unrealized Gains	
		2014	2013		2014	2013
		<i>(in thousands)</i>			<i>(in thousands)</i>	
Energy-related derivatives:	Other regulatory assets, current	\$ (26,259)	\$ (3,652)	Other regulatory liabilities, current	\$ 30	\$ 3,352
	Other regulatory assets, deferred	(19,159)	(6,629)	Other regulatory liabilities, deferred	22	1,451
Total energy-related derivative gains (losses)		\$ (45,418)	\$(10,281)		\$ 52	\$ 4,803

The pre-tax effects of unrealized gains (losses) arising from energy-related derivative instruments not designated as hedging instruments was immaterial for 2014 and 2013.

For the years ended December 31, 2014, 2013, and 2012, the pre-tax effects of derivatives designated as cash flow hedging instruments on the statements of operations were as follows:

Derivatives in Cash Flow Hedging Relationships	Gain (Loss) Recognized in OCI on Derivative (Effective Portion)			Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Amount		
	2014	2013	2012		Statements of Operations Location		
Derivative Category	2014	2013	2012	2014	2013	2012	
	<i>(in thousands)</i>				<i>(in thousands)</i>		
Energy-related derivatives	\$ —	\$ —	\$ —	Fuel	\$ —	\$ —	\$ —
Interest rate derivatives	—	—	(774)	Interest Expense	(1,375)	(1,375)	(1,073)
Total	\$ —	\$ —	\$ (774)		\$ (1,375)	\$ (1,375)	\$ (1,073)

There was no material ineffectiveness recorded in earnings for any period presented.

For the years ended December 31, 2014, 2013, and 2012, 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, 2014 and 2013, the pre-tax effects of foreign currency derivatives designated as fair value hedging instruments on the Company's statements of operations were immaterial. For the year ended December 31, 2012, the pre-tax effect of foreign currency derivatives designated as fair value hedging instruments, which include a pretax loss associated with the de-designated hedges prior to de-designation, was a \$0.6 million gain. These amounts were offset by changes in the fair value of the purchase commitment related to equipment purchases. Therefore, there is no impact on the Company's statements of operations.

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, 2014, the Company's collateral posted with its derivative counterparties was immaterial.

At December 31, 2014, the fair value of derivative liabilities with contingent features was \$9.9 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 \$54.5 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.

NOTES (continued)
Mississippi Power Company 2014 Annual Report

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 2014 and 2013 is as follows:

Quarter Ended	Operating Revenues	Operating Income (Loss)	Net Income (Loss) After Dividends on Preferred Stock
		<i>(in thousands)</i>	
March 2014	\$ 331,161	\$ (325,460)	\$ (172,048)
June 2014	310,975	56,021	62,495
September 2014	354,623	(349,010)	(195,070)
December 2014	245,852	(70,721)	(24,058)
March 2013	\$ 245,934	\$ (429,148)	\$ (246,321)
June 2013	306,435	(388,395)	(219,110)
September 2013	325,206	(79,890)	(24,115)
December 2013	267,582	(24,412)	12,921

As a result of the revisions to the cost estimate for the Kemper IGCC, the Company recorded total pre-tax charges to income for the estimated probable losses on the Kemper IGCC of \$70.0 million (\$43.2 million after tax) in the fourth quarter 2014, \$418.0 million (\$258.1 million after tax) in the third quarter 2014, \$380.0 million (\$234.7 million after tax) in the first quarter 2014, \$40.0 million (\$24.7 million after tax) in the fourth quarter 2013, \$150.0 million (\$92.6 million after tax) in the third quarter 2013, \$450.0 million (\$277.9 million after tax) in the second quarter 2013, \$462.0 million (\$285.3 million after tax) in the first quarter 2013, and \$78.0 million (\$48.2 million after tax) in the fourth quarter 2012. In the aggregate, the Company has incurred charges of \$2.05 billion (\$1.26 billion after tax) as a result of changes in the cost estimate for the Kemper IGCC through December 31, 2014. See Note 3 under "Integrated Coal Gasification Combined Cycle" for additional information.

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

SELECTED FINANCIAL AND OPERATING DATA 2010-2014
Mississippi Power Company 2014 Annual Report

	2014	2013	2012	2011	2010
Operating Revenues (in thousands)	\$ 1,242,611	\$ 1,145,157	\$ 1,035,996	\$ 1,112,877	\$ 1,143,068
Net Income (Loss) After Dividends on Preferred Stock (in thousands)	\$ (328,681)	\$ (476,625)	\$ 99,942	\$ 94,182	\$ 80,217
Cash Dividends on Common Stock (in thousands)	\$ —	\$ 71,956	\$ 106,800	\$ 75,500	\$ 68,600
Return on Average Common Equity (percent)	(15.43)	(24.28)	7.14	10.54	11.49
Total Assets (in thousands)	\$ 6,756,728	\$ 5,848,209	\$ 5,373,621	\$ 3,671,842	\$ 2,476,321
Gross Property Additions (in thousands)	\$ 1,388,711	\$ 1,773,332	\$ 1,665,498	\$ 1,205,704	\$ 340,162
Capitalization (in thousands):					
Common stock equity	\$ 2,084,260	\$ 2,176,551	\$ 1,749,208	\$ 1,049,217	\$ 737,368
Redeemable preferred stock	32,780	32,780	32,780	32,780	32,780
Long-term debt	1,630,487	2,167,067	1,564,462	1,103,596	462,032
Total (excluding amounts due within one year)	\$ 3,747,527	\$ 4,376,398	\$ 3,346,450	\$ 2,185,593	\$ 1,232,180
Capitalization Ratios (percent):					
Common stock equity	55.6	49.7	52.3	48.0	59.8
Redeemable preferred stock	0.9	0.7	1.0	1.5	2.7
Long-term debt	43.5	49.6	46.7	50.5	37.5
Total (excluding amounts due within one year)	100.0	100.0	100.0	100.0	100.0
Customers (year-end):					
Residential	152,453	152,585	152,265	151,805	151,944
Commercial	33,496	33,250	33,112	33,200	33,121
Industrial	482	480	472	496	504
Other	175	175	175	175	187
Total	186,606	186,490	186,024	185,676	185,756
Employees (year-end)	1,478	1,344	1,281	1,264	1,280

SELECTED FINANCIAL AND OPERATING DATA 2010-2014 (continued)
Mississippi Power Company 2014 Annual Report

	2014	2013	2012	2011	2010
Operating Revenues (in thousands):					
Residential	\$ 239,330	\$ 241,956	\$ 226,847	\$ 246,510	\$ 256,994
Commercial	257,189	265,506	250,860	263,256	266,406
Industrial	290,902	289,272	262,978	275,752	267,588
Other	7,222	2,405	6,768	6,945	6,924
Total retail	794,643	799,139	747,453	792,463	797,912
Wholesale — non-affiliates	322,659	293,871	255,557	273,178	287,917
Wholesale — affiliates	107,210	34,773	16,403	30,417	41,614
Total revenues from sales of electricity	1,224,512	1,127,783	1,019,413	1,096,058	1,127,443
Other revenues	18,099	17,374	16,583	16,819	15,625
Total	\$ 1,242,611	\$ 1,145,157	\$ 1,035,996	\$ 1,112,877	\$ 1,143,068
Kilowatt-Hour Sales (in thousands):					
Residential	2,126,115	2,087,704	2,045,999	2,162,419	2,296,157
Commercial	2,859,617	2,864,947	2,915,934	2,870,714	2,921,942
Industrial	4,942,689	4,738,714	4,701,681	4,586,356	4,466,560
Other	40,595	40,139	38,588	38,684	38,570
Total retail	9,969,016	9,731,504	9,702,202	9,658,173	9,723,229
Wholesale — non-affiliates	4,190,812	3,929,177	3,818,773	4,009,637	4,284,289
Wholesale — affiliates	2,899,814	931,153	571,908	648,772	774,375
Total	17,059,642	14,591,834	14,092,883	14,316,582	14,781,893
Average Revenue Per Kilowatt-Hour (cents)*:					
Residential	11.26	11.59	11.09	11.40	11.19
Commercial	8.99	9.27	8.60	9.17	9.12
Industrial	5.89	6.10	5.59	6.01	5.99
Total retail	7.97	8.21	7.70	8.21	8.21
Wholesale	6.06	6.76	6.19	6.52	6.51
Total sales	7.18	7.73	7.23	7.66	7.63
Residential Average Annual Kilowatt-Hour Use Per Customer	13,934	13,680	13,426	14,229	15,130
Residential Average Annual Revenue Per Customer	\$ 1,568	\$ 1,585	\$ 1,489	\$ 1,622	\$ 1,693
Plant Nameplate Capacity Ratings (year-end) (megawatts)	3,867	3,088	3,088	3,156	3,156
Maximum Peak-Hour Demand (megawatts):					
Winter	2,618	2,083	2,168	2,618	2,792
Summer	2,345	2,352	2,435	2,462	2,638
Annual Load Factor (percent)	59.4	64.7	61.9	59.1	57.9
Plant Availability Fossil-Steam (percent)**	87.6	89.3	91.5	87.7	93.8
Source of Energy Supply (percent):					
Coal	39.7	32.7	22.8	34.9	43.0
Oil and gas	55.3	57.1	63.9	51.5	41.9
Purchased power —					
From non-affiliates	1.4	2.0	2.0	1.4	1.3
From affiliates	3.6	8.2	11.3	12.2	13.8
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.

** Beginning in 2012, plant availability is calculated as a weighted equivalent availability.

DIRECTORS AND OFFICERS
Mississippi Power Company 2014 Annual Report

Directors

Carl J. Chaney

Retired 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

G. Edison Holland, Jr.

Chairman of the Board, President, and
Chief Executive Officer
Mississippi Power Company
Gulfport, Mississippi. Elected 2013

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

Officers

G. Edison Holland, Jr.

Chairman of the Board, President, and Chief
Executive Officer

John W. Atherton

Vice President of Corporate Services and
Community Relations

Moses H. Feagin

Vice President, Chief Financial Officer, and
Treasurer

Jeff G. Franklin

Vice President of Customer Services Organization
(Resigned effective April 1, 2015)

Michael A. Hazelton

Vice President of Customer Services Organization
(Elected effective 4/1/2015)

John C. Huggins

Vice President of Generation Development
(Retired effective 2/20/2015)

R. Allen Reaves

Vice President and Senior Production Officer

Billy F. Thornton

Vice President of Legislative and Regulatory
Affairs

Emile J. Troxclair III

Vice President of Kemper Development
(Elected effective 12/10/2014)

Cynthia F. Shaw

Comptroller

Vicki L. Pierce

Corporate Secretary and Assistant Treasurer

Stacy R. Kilcoyne

Vice President

Melissa K. Caen

Assistant Secretary and Assistant Treasurer

CORPORATE INFORMATION
Mississippi Power Company 2014 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 electricity to retail customers within its traditional service area located within the State of Mississippi and to wholesale customers in the Southeast. The Company sells electricity to approximately 187,000 customers within its service area of more than 11,000 square miles in southeast Mississippi. In 2014, retail energy sales accounted for 58.4% of the Company's total sales of 17.1 billion kilowatt-hours.

The Company is a wholly-owned subsidiary of The Southern Company, which is the parent company of four traditional operating companies, a wholesale generation subsidiary, and other direct and indirect subsidiaries.

Registrar, Transfer Agent, and Dividend Paying Agent

All series of Preferred Stock
Computershare Inc.
P.O. Box 30170
College Station, TX 77842-3170
(800) 554-7626

www.computershare.com/investor

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. The dividends declared by the Company to its common stockholder for the past two years were as follows:

Quarter	2014	2013
	<i>(in thousands)</i>	
First	\$54,930	\$44,190
Second	54,930	44,190
Third	54,930	44,190
Fourth	54,930	44,190

Number of Preferred Shareholders of record as of December 31, 2014 was 184.

Form 10-K

A copy of 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.

Corporate Office

Mississippi Power Company
2992 West Beach Boulevard
Gulfport, Mississippi 39501
(228) 864-1211

Auditors

Deloitte & Touche LLP
Suite 2000
191 Peachtree Street, N.E.
Atlanta, Georgia 30303

Legal Counsel

Balch & Bingham LLP
P.O. Box 130
Gulfport, Mississippi 39502

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