II-VI INC
Form 10-K
August 28, 2015

United States

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended June 30, 2015

¨ Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to .

Commission File Number: 0-16195

II-VI INCORPORATED

(Exact name of registrant as specified in its charter)

PENNSYLVANIA (State or other jurisdiction of incorporation or organization)	25-1214948 (I.R.S. Employer Identification No.)
375 Saxonburg Boulevard Saxonburg, PA (Address of principal executive offices)	16056 (Zip code)

Registrant's telephone number, including area code: 724-352-4455

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, no par value	Nasdaq Global Select Market

Securities registered pursuant to Section 12(g) of the Act:

None

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

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

Large accelerated filer	x	Accelerated filer	¨
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

Aggregate market value of outstanding Common Stock, no par value, held by non-affiliates of the Registrant at December 31, 2014, was approximately $798,334,460 based on the closing sale price reported on the Nasdaq Global Select Market. For purposes of this calculation only, directors and executive officers of the Registrant and their spouses are deemed to be affiliates of the Registrant.

Number of outstanding shares of Common Stock, no par value, at August 20, 2015, was 61,222,480.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement, which will be issued in connection with the 2015 Annual Meeting of Shareholders of II-VI Incorporated, are incorporated by reference into Part III of this Annual Report on Form 10-K.

Forward-Looking Statements

This Annual Report on Form 10-K (including certain information incorporated herein by reference) contains forward-looking statements made pursuant to Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements can be identified as those that may predict, forecast, indicate or imply future results, performance or advancements and by forward-looking words such as "expects," "anticipates," "intends," "plans," "projects," "believes," "estin or similar expressions. Forward-looking statements address, among other things, our expectations, our growth strategies, our efforts to increase bookings, sales and revenues, projections of our future profitability, results of operations, capital expenditures, our financial condition or other "forward-looking" information and include statements about revenues, earnings, spending, margins, costs or our actions, plans or strategies.

The forward-looking statements in this Annual Report on Form 10-K involve risks and uncertainties, which could cause actual results, performance or trends to differ materially from those expressed in the forward-looking statements herein or in previous disclosures. II-VI Incorporated believes that all forward-looking statements made by it have a reasonable basis, but there can be no assurance that these expectations, beliefs or projections will actually occur or prove to be correct. Actual results could materially differ from such statements.

The following factors, among others, in some cases have affected and in the future could affect our financial performance and actual results, and could cause actual results for fiscal 2016 and beyond to differ materially from those expressed or implied in any forward-looking statements included in this Annual Report on Form 10-K or otherwise made by our management:

- Dependency on international sales and successful management of global operations,
- Our ability to develop and market new products and processes,
- Our ability to keep pace with key industry developments,
- Our ability to successfully integrate and capitalize on newly acquired businesses,
- Decline in the operating performance of a business segment resulting in impairment of the segment's goodwill and indefinite-lived intangible assets,
- Global economic and political uncertainties,
- Our ability to protect our intellectual property,
- Changes in or interpretations of U.S. and non-U.S. laws governing trade, funds flow, employment, social and property taxes and foreign investment,
- Potential costs for violations of applicable environmental, health and safety laws and the costs of complying with governmental regulations,
- Disruption of information and communication technologies, including outages or control breakdowns,
- The future availability and prices of raw materials,
- The use of defective or contaminated materials in our products which we may be unable to detect until deployment by customers,
- Changes in defense spending and cancellation or changes in defense programs or initiatives,
- Changes in tax rates, liabilities or accounting rules,
- Competition in the markets that we serve,
- Our ability to attract and retain key personnel,

- The impact of natural disasters or other global or regional catastrophic events in our areas of operation,
- Historically high cyclicality of our customers' end markets,
- Impact of commodity prices,

- The fluctuation of the price of our Common Stock, and
- Provisions in our Articles of Incorporation and By-Laws, which may limit the price investors are willing to pay for our Common Stock.

The foregoing and additional risk factors are described in more detail herein under Item 1A. “Risk Factors”. In addition, we operate in a highly competitive and rapidly changing environment and therefore, new risk factors can arise. It is not possible for management to predict all such risk factors, assess the impact of all such risk factors on our business nor estimate the extent to which any individual risk factor, or combination of risk factors, may cause results to differ materially from those contained in any forward-looking statement. The forward-looking statements included in this Annual Report on Form 10-K speak only as of the date of this Annual Report on Form 10-K. We do not assume any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or developments, or otherwise, except as may be required by the securities laws. We caution you not to rely on them unduly.

Investors should also be aware that while the Company does communicate with securities analysts, from time to time, such communications are conducted in accordance with applicable securities laws. Investors should not assume that the Company agrees with any statement or report issued by any analyst irrespective of the content of the statement or report.

PART I

Item 1. BUSINESS
Introduction

II-VI Incorporated (“II-VI,” the “Company,” “we,” “us,” or “our”) was incorporated in Pennsylvania in 1971. Our executive offices are located at 375 Saxonburg Boulevard, Saxonburg, Pennsylvania 16056. Our telephone number is 724-352-4455. Reference to “II-VI,” the “Company,” “we,” “us,” or “our” in this Annual Report on Form 10-K, unless the context requires otherwise, refers to II-VI Incorporated and its wholly-owned subsidiaries. The Company’s name is pronounced “Two Six Incorporated.” The majority of our revenues are attributable to the sale of engineered materials and opto-electronic components for industrial, military and medical laser applications, optical communications products, compound semiconductor substrate-based products and elements for material processing and refinement. Reference to “fiscal” or “fiscal year” means our fiscal year ended June 30 for the year referenced.

Effective July 1, 2014, the Company realigned its organizational structure into three reporting segments for the purpose of making operational decisions and assessing financial performance: (i) II-VI Laser Solutions, (ii) II-VI Photonics, and (iii) II-VI Performance Products. The segment information (revenue through operating income) for all periods presented in this document reflects the realigned segment organization.

- The II-VI Laser Solutions segment contains the former Infrared Optics segment, the semiconductor laser portion of the former Active Optical Products segment (now II-VI Laser Enterprise), and smaller units of high-power laser technology from the former Near-Infrared Optics segment (now II-VI Suwtech) and the former Advanced Products Group segment (now II-VI Lasertech).
- The II-VI Photonics segment contains the remaining majority of the former Near-Infrared Optics segment (now part of both II-VI Photop and II-VI Optical Communications) as well as the pump laser and optical amplifier businesses of the former Active Optical Products segment (now II-VI Optical Communications).
- The II-VI Performance Products segment contains the former Military & Materials and the majority of the former Advanced Products Group segments.

In August 2013, the Company announced that its subsidiary, II-VI Performance Metals, a business in the II-VI Performance Products segment, would discontinue its tellurium product line. In addition, the Company downsized its selenium product line and now only provides selenium metal to the Company’s II-VI Laser Solutions segment, while maintaining production of its rare earth element. The Company’s goal was to provide a reliable supply of selenium for the Company’s internal needs while significantly decreasing write-downs and profit volatility associated with minor metal index pricing. Financial and operational data included herein for all periods presented reflects the presentation of the tellurium product line as a discontinued operation.

Our Internet address is www.ii-vi.com. Information contained on our website is not part of, and should not be construed as being incorporated by reference into, this Annual Report on Form 10-K. We post the following reports on our website as soon as reasonably practical after they are electronically filed with or furnished to the Securities and Exchange Commission (the “SEC”): our Annual Reports on Form 10-K, our Quarterly Reports on Form 10-Q, our Current Reports on Form 8-K, and any amendments to those reports or statements filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act. In addition, we post our proxy statements on

Schedule 14A related to our annual shareholders' meetings as well as reports filed by our directors, officers and ten-percent beneficial owners pursuant to Section 16 of the Exchange Act. In addition, all filings are available via the SEC's website (www.sec.gov). We also make our corporate governance documents available on our website, including the Company's Code of Business Conduct and Ethics, governance guidelines and the charters for various board committees. All such documents are located on the Investors page of our website and are available free of charge.

Information Regarding Market Segments and Foreign Operations

Financial data regarding our revenues, results of operations, industry segments and international sales for the three years ended June 30, 2015 are set forth in the Consolidated Statements of Earnings and in Note 11 to the Company's Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K and are incorporated herein by reference. We also discuss certain Risk Factors set forth in Item 1A of this Annual Report on Form 10-K related to our foreign operations, which are incorporated herein by reference.

General Description of Business

We develop and manufacture engineered materials, opto-electronic components and products for precision use in industrial, optical communications, military, semiconductor and life science applications. We use advanced engineered material growth technologies coupled with proprietary high-precision fabrication, micro-assembly, thin-film coating and electronic integration to enable complex opto-electronic devices and modules. Our products are deployed in applications that we believe reduce costs and improve performance and reliability in a variety of applications, including:

- Laser cutting, welding and marking operations,
- Optical communication products,
- Intelligence, surveillance and reconnaissance,
- Semiconductor processing and tooling,
- Medical procedures and
- Thermo electric cooling and power generation solutions.

A key Company strategy is to develop and manufacture high performance materials that are differentiated from those produced by our competitors. We focus on providing critical components to the heart of our customers' assembly lines for products serving the above noted applications.

Our U.S. production and research and development operations are located in Pennsylvania, California, New Jersey, Texas, Mississippi, Massachusetts, Connecticut, Delaware, New York and Florida and our non-U.S. production operations are based in China, Singapore, Vietnam, the Philippines, Germany and Switzerland. We also utilize contract manufacturers in Thailand and China. In addition to sales offices at most of our manufacturing sites, we have sales and marketing subsidiaries in Hong Kong, Japan, Germany, China, Switzerland, Belgium, the United Kingdom ("U.K."), Italy and South Korea. Approximately 63% of our revenues for the fiscal year ended June 30, 2015 were generated from sales to customers outside of the U.S.

Our Products

The main products for each of our markets are described as follows:

II-VI Laser Solutions Segment

II-VI Infrared Optics Group:

We supply a broad line of precision infrared opto-electronic components such as lenses, output couplers, windows, mirrors and scan-lenses for use in CO_2 lasers. Our precision opto-electronic components are used to attenuate the amount of laser energy, enhance the properties of the laser beam and focus and direct laser beams to a target work surface. The opto-electronic components include both reflective and transmissive optics and are made from materials such as zinc selenide, zinc sulfide, copper, silicon, gallium arsenide and germanium. Transmissive optics used with CO_2 lasers are predominately made from zinc selenide. We believe we are the largest manufacturer of zinc selenide in the world. We supply replacement optics to end users of CO_2 lasers. Over time, optics may become contaminated and must be replaced to maintain peak laser operations. This aftermarket portion of our business continues to grow as laser applications proliferate worldwide and the installed base of serviceable laser systems increases each year. We estimate that 85% to 90% of our infrared optics sales service this installed base of CO_2 laser systems. We serve the aftermarket via a combination of selling to OEMs and directly to system end users. We are also one of the leading producers of CVD Diamond substrates for applications including multi-spectral laser optics, dielectric windows, heat sinks, and other applications. Diamond is the ultimate material for a wide variety of applications because of its outstanding physical properties, including extreme hardness and strength, high thermal conductivity, low thermal expansion, excellent dielectric properties, resistance to chemical attack, and optical transmission over a wide spectral range.

II-VI HIGHYAG Division:

Our broad expertise in laser technology, optics, sensor technology and laser applications enables us to supply a broad array of tools for laser materials processing, including modular laser processing heads for fiber lasers, YAG lasers and other one-micron laser systems. We also manufacture beam delivery systems including fiber optic cables and modular beam systems.

II-VI Laser Enterprise Division:

Our semiconductor laser diode products cover a broad wavelength from 750 nm to 1500 nm and varying optical output power ranges. The laser diode products are available as integrated modules with and without active cooling, fiber pigtails or assemblies.

II-VI Suwtech Division:

We supply high-power laser, green laser, narrow linewidth laser and Q-switched laser solutions for various applications, including laser leveling, range finding, bio-medical instrumentation, Raman spectroscopy, machine vision, laser entertainment and display, and digital printing.

II-VI Lasertech Division:

The need for industry to be able to process very hard materials is growing as more applications for materials such as CVD and PCD Diamond, Poly Crystalline Boron Nitride, and ultra-hard ceramics emerge. The laser cutting machines manufactured by II-VI Lasertech are specifically designed to cut, drill and etch these kinds of materials.

II-VI Photonics Segment

II-VI Photop Group:

We manufacture products across a broad spectral range in the visible and near-infrared wavelengths. We offer a wide variety of standard and custom laser gain materials, optics, optical components and optical module assemblies for optical communications, laser systems, and photonic applications in the medical, life science, industrial, scientific and research and development markets. Laser gain materials are produced to stringent industry specifications and precisely fabricated to customer specifications. Key materials and precision optical components for YAG, fiber lasers and other solid-state laser systems are an important part of our product offerings. We manufacture lenses, windows, prisms, mirrors, gratings, wave-plates, and polarizers for visible and near-infrared applications, which are used to control or alter visible or near-infrared energy and its polarization. In addition, we manufacture specialty coated glass wafers used as optical filters in the life science and optical communications markets, and coated windows used as debris shields in the industrial and medical laser aftermarkets. We offer fiber optics, micro optics and photonic crystal parts for optical communications, instrumentation and laser applications, optical components and modules for optical communication networks, as well as diode pumped solid-state laser devices for optical instruments, display and biotechnology.

II-VI Optical Communications Group:

We manufacture a broad range of passive optical components and modules, leveraging our core micro optics platform for the filtering, combining, splitting, attenuating and monitoring of optical wavelengths within optical communication systems. We supply a broad portfolio of cooled and uncooled pumps, both single and multi-mode designs in single chip and multi-chip configurations based on our gallium arsenide (GaAs) chip technology, facet passivation processes and wafer fab and module manufacturing capabilities. The single chip designs are predominantly used as low noise pump sources for EDFA covering gain block, single channel to multi-channel data wavelength-division multiplexing (DWDM), addressing access, cross-connect, metro and also long haul requirements of the telecom market. Our dual chip pump solutions are designed and able to address the arrayed amplifier market where 8 or 16 amplification stages are required. Our single mode high-power uncooled pump modules address both the single channel and small form factor terrestrial market and also the stringent high reliability demands of the submarine (subsea) network market. The latter is a testament to the stability of our chip, module design technology and manufacturing capabilities. Finally, we are able to address segments of the cable television market with both single mode and uncooled multimode GaAs pump lasers, typically used for distribution amplification. In addition, we offer a wide variety of standard, semi-custom and customer amplifiers. These products are offered at varying levels of sophistication ranging from a simple collection of active and passive components mounted to a printed circuit board assembly ("PCBA") through assemblies with large amounts of firmware and software which are either mounted onto our customer's PCBA's controlled amplifier modules or plug directly into our customers' equipment shelf line cards. We offer EDFA and Raman amplifiers as well as amplifiers which are combined with wavelength selective switches. Also, we are starting to offer a range of 40G and 100G transceivers which are focused on meeting the transmission needs within data centers.

II-VI Performance Products Segment

II-VI Optical Systems operation:

We offer optics and optical sub-assemblies for UV, Visible, and Infrared systems including thermal imaging, night vision, laser designation, missile warning, targeting and navigation systems. Our product offering is comprised of missile domes, electro-optical windows and sub-assemblies, imaging lenses, UV filter assemblies, laser cavity optics and prisms and other optical components. Our precision optical products utilize optical materials such as sapphire, germanium, zinc sulfide, zinc selenide, silicon and spinel. In addition, our products also include crystalline materials such as calcium fluoride, barium fluoride, YAG, YLF and fused silica. Our products are currently utilized on the F-35 Joint Strike Fighter, F-16 fighter jet, Apache Attack Helicopter, unmanned platforms such as the Predator and Reaper UAV and ground vehicles such as the Abrams M-1 Tank and Bradley Fighting Vehicle.

II-VI Performance Metals operation:

Our product offering includes a rare earth element in specific purity levels and forms.

II-VI Marlow operation:

We supply a broad array of TEMs and related assemblies to various market segments. In the defense market, TEMs are used in guidance systems, smart weapons and night vision systems, as well as soldier cooling. TEMs are also used in products providing temperature stabilization for telecommunication lasers that generate and amplify optical signals for fiber optic communication systems. TEMs are also used in the personal comfort market. We also produce and sell a variety of solutions from thermoelectric components to complete sub-assemblies used in the medical equipment market and other industrial, commercial and personal comfort applications. Thermoelectric modules, used as power generators, are also applied in a range of end-use applications. We offer single-stage TEMs, micro TEMs, multi-stage TEMs, planar multi-stage TEMs, extended life thermo-cyclers, thermoelectric thermal reference sources, power generators and thermoelectric assemblies.

II-VI M Cubed operation:

We supply a diverse array of products to several market segments. In the semiconductor market, reaction bonded SiC is used to produce wafer chucks, robot end effectors, structural components, and mechanical stage assemblies. In the defense market, we supply next generation personnel armor, monolithic helicopter seats, and vehicle and aviation armor sub systems. In the industrial market, we supply wear resistant components, refractory assemblies, and precision optical substrates for chemical, refractory, and scientific applications.

II-VI Advanced Materials operation:

Our product offerings include 6H-SiC (semi-insulating) and 4H-SiC (semi-insulating and semi-conducting) substrates which are used in the wireless communications infrastructure, radio frequency ("RF") electronics, thermal management, highly efficient (green energy) power conversion and power switching markets. We are also one of the leading producers of CVD Diamond substrates for applications including multi-spectral laser optics, dielectric windows, heat sinks, and other applications. Diamond is the ultimate material for a wide variety of applications because of its outstanding physical properties, including extreme hardness and strength, high thermal conductivity, low thermal expansion, excellent dielectric properties, resistance to chemical attack, and optical transmission over a wide spectral range. Our CVD diamond materials are being utilized in semiconductor equipment manufacturing, microwave frequency windows and thermal management applications.

Our Markets

Our market-focused businesses are organized by technology and products. Our businesses are composed of the following primary markets:

II-VI Laser Solutions Segment

II-VI Infrared Optics Group:

- Design, manufacture and marketing of engineered materials and opto-electronic components for industrial applications.

Increases in the installed worldwide base of laser machines for a variety of laser processing applications have driven CO_2 laser optics component consumption. It is estimated that there are over 75,000 CO_2 laser systems currently deployed in the world. CO_2 lasers offer benefits in a wide variety of cutting, welding, drilling, ablation, cladding, heat treating and marking applications for materials such as steel alloys, non-ferrous metals, plastics, wood, paper, fiberboard, ceramics and composites. Laser systems enable manufacturers to reduce parts cost and improve quality, as well as improve process precision, speed, throughput, flexibility, repeatability and automation. Automobile manufacturers, for example, deploy lasers both to cut body components and to weld those parts together in high-throughput production lines. Manufacturers of motorcycles, lawn mowers and garden tractors cut, trim, and weld metal parts with lasers to reduce post-processing steps and, therefore, lower overall manufacturing costs. Furniture manufacturers utilize lasers because of their easily reconfigurable, low-cost prototyping and production capabilities for customer-specified designs. In high-speed food and pharmaceutical packaging lines, laser marking is used to provide automated product, date and lot coding on containers. In addition to being installed by original equipment manufacturers ("OEMs") of laser systems in new machine builds, our optical components are purchased as replacement parts by end-users of laser machines to maintain proper system performance. In newer and developing market segments, SiC and CVD Diamond both exhibit very high thermal conductivities for use in high-end applications in the semiconductor and opto-electronic markets. CVD Diamond also has applications in the windows, tooling, microwave and radiation detection markets. We believe that the current addressable markets serviced by our II-VI Infrared Optics operations are approximately $500 million.

II-VI HIGHYAG Division:

- Design, manufacture and marketing of customized technology for laser material processing to deliver both low-power and high-power one-micron laser light for industrial applications.

In many areas of material processing, laser technology has proven to be a better alternative to conventional production techniques. It has also enabled novel processing steps not previously achievable with legacy technologies. The precise cut and elegant seam are visible proof of a laser beam's machining efficiency. Industrial applications such as welding, drilling and cutting have driven the recent market growth of the one-micron laser systems, and are demanding increased performance, lower total cost of ownership, ease of use and portability of the one-micron laser systems. One-micron laser systems require efficient and reliable tools, including modular laser processing heads for fiber lasers, beam delivery systems, including fiber optic cables, and modular beam systems. We believe that the current addressable markets serviced by our II-VI HIGHYAG operations are approximately $700 million.

II-VI Laser Enterprise Division:

- Design, manufacture and marketing of advanced semiconductor laser diodes and low-power polarization locked laser diodes.

We market advanced laser technology diodes for material processing, medical, cosmetic, 3-D sensing and printing applications and are exploring other new market opportunities for our high-power lasers. In addition, we sell low-power polarization locked products for optical mouse and finger navigation applications. Our market opportunities for Vertical-Cavity Surface-Emitting Laser ("VCSEL") products are expanding to include optical high-speed datacom applications and high-power sensing for consumer electronics applications. We believe that the current addressable markets serviced by our II-VI Laser Enterprise operations are approximately $300 million.

II-VI Suwtech & II-VI Lasertech Divisions:

- Design, manufacture and marketing of high-power lasers for industrial applications and green lasers for consumer, life science and industrial applications by our II-VI Suwtech division.
- Design, manufacture and marketing of ultra-hard material laser cutting machines for industrial applications by our II-VI Lasertech division.

The need for high-power and green laser for industrial and medical applications continue to grow as does the need for a laser cutting device capable of processing the next generation of ultra-hard materials like diamond. We believe that the current addressable markets serviced by our II-VI Lasertech and II-VI Suwtech operations are approximately $400 million.

II-VI Photonics Segment

II-VI Photop Group:

- Design, manufacture and marketing of a diverse range of customized optics, optical assemblies for consumer and commercial applications such as fiber optic communications, projection and display products, lasers, medical equipment and bio-medical instrumentation.
- Design, manufacture and marketing of crystal ad optical components to OEM customers for fiber, solid state and gas laser systems used in industrial and medical applications.

The II-VI Photop market is driven by applications in the optical communications, medical and life science, and industrial markets. The optical communications market segment requires delivery of ever-increasing data bandwidth and necessitates innovations in performance and cost of the underlying optics and optical components. Medical and life science applications continue to gain traction in the market and include aesthetic, vision correction, dental, ophthalmic and diagnostic lasers and instruments. Industrial market segments are addressed by solid state lasers and fiber lasers, which are used in high-power applications such as cutting, welding, drilling, and lower power applications such as marking and engraving. These industrial applications are demanding higher performance levels for less cost and more efficiency, creating competition for other technologies. II-VI Photop also addresses opportunities in the semiconductor processing, instrumentation, test and measurement and research segments. We believe that the current addressable markets serviced by our II-VI Photop operations are approximately $1.4 billion.

II-VI Optical Communications Group:

- Design, manufacture and marketing of optical components, assemblies and modules for use in telecommunications and CATV networks and data centers.
- Design, manufacture and marketing of 980 nanometer (“nm”) pump laser diodes for high-power, reliable pump sources for EDFAs in terrestrial and submarine applications.
- Design, manufacture and marketing of Erbium Doped Fiber Amplifiers (“EDFA”) used to compensate for losses in optical fiber and other optical components and modules in optical transmission systems.
- Design, manufacture and marketing of optical monitoring products for communications networks.
- Design, manufacture and marketing of transceivers for data networks.

The optical communications market is being driven in part by demand for high-bandwidth communication capabilities through increasing worldwide usage of the Internet and data services, the growing number of broadband users, mobile device and cloud computing users, and the greater reliance on high-bandwidth capabilities in our daily lives. High-bandwidth communication networks are being extended closer to the end user with fiber-to-the-home and other fiber optic networks. Mobile data traffic also is increasing as smart phones continue to proliferate with increasingly sophisticated audio, photo, video, email and Internet capabilities, as well as data connection and storage through cloud computing networks. The resulting traffic, in turn, is felt throughout the network, including the core that depends on optical technology. Our passive components, assemblies and modules are used for filtering, switching, combining and routing optical wavelengths within optical networks. Our monitoring products are used for measuring the performance of optical channels and systems. Our 980 nm pump laser diodes are designed for use as high-power, highly reliable pump sources for EDFAs in terrestrial access, cross-connect, metro to long haul and undersea (submarine) repeater applications. Single mode high-power uncooled modules are designed for both the single channel and small form factor terrestrial market and also the stringent high reliability demands of the submarine (subsea) network market. In addition, we market EDFAs which are used to compensate for losses in optical fiber and other optical components and modules in optical transmission systems. We offer optical amplifiers at all levels of functionality, from simple optical modules through full circuit cards, which plug directly into our customers’ equipment racks and service the metro, regional and long-haul optical transmission markets. In some cases, we add additional switching and monitoring functionality to the base amplifier. We believe that the currently addressable markets serviced by our II-VI Optical Communications Group operations are approximately $1.9 billion.

II-VI Performance Products Segment

II-VI Optical Systems operation:

- Design, manufacture and marketing of Ultra Violet ("UV"), Visible ("VIS") and Infrared ("IR") optical components and high precision optical assemblies, laser gain material and micro-fine conductive mesh patterns for intelligence, surveillance, reconnaissance and other military, life science and commercial laser and imaging applications.

We provide several key assemblies and optical components such as windows, domes, laser rods and optics and related subassemblies to military, semiconductor, medical, and life sciences markets for UV, Visible, and Infrared applications in night vision, targeting, navigation, missile warning, and Homeland Security intelligence, surveillance and reconnaissance ("ISR") systems. Infrared window and window assemblies for navigational and targeting systems are deployed on fixed and rotary-wing aircraft, such as the F-35 Joint Strike Fighter, F-16 fighter jet, Apache Attack Helicopter, unmanned platforms such as the Predator and Reaper Unmanned Aerial Vehicle ("UAV") and ground vehicles such as the Abrams M-1 Tank and Bradley Fighting Vehicle. Additionally, multiple fighter jets, including the F-16, are being equipped with large area sapphire windows, as a key component for the aircraft, providing advanced targeting and imaging systems. Our ability to grow large sapphire materials and manufacture these materials into large area sapphire windows has played a key role in our ability to provide an even larger suite of sapphire panels, which are a key component of the F-35 Joint Strike Fighter Electro Optical Targeting System. Infrared domes are used on missiles with infrared guidance systems ranging from small, man-portable designs to larger designs mounted on helicopters, fixed-wing aircraft and ground vehicles. High-precision domes are an integral component of a missile's targeting system, providing efficient tactical capability, while serving as a protective cover to its internal components. The Company also offers precision optical engineering and manufacturing, with particular efficiency in designing to customer end-item specifications, assisting with co-engineering designs, and designing for manufacturability. The high precision optical components and assemblies programs include Deep Impact Comet Flyby HRI & MRI, Lunar Reconnaissance Orbiter, Hellfire II Missile Optics, Missile launch detection sensor optical assembly, and High Altitude Observatory telescopes among others. In addition to imaging, many of these systems employ laser designation and range-finding capabilities supported by our YAG material growth and competency in short wave infrared and visible optics. Turreted systems and mounted targeting pods employ these capabilities in addition to hand-held soldier systems. Rotary and fixed-wing platforms also use missile warning systems to protect against shoulder fired man-portable missiles. Our competencies in material growth for UV crystals and our optical assembly capabilities provide significant support to these missile warning systems. A key attribute to several of these systems is the ability to filter electro-magnetic interference using micro-fine conductive mesh patterns. This technology is also applied to non-optical applications for absorbing and transmitting energy from the surfaces of aircraft and missiles. Our military optical and non-optical products are sold primarily to U.S. Government prime contractors and directly to various U.S. Government agencies. Certain products have applications in commercial, medical and life science markets. We believe that the current addressable markets serviced by our II-VI Optical Systems operations business are approximately $1.6 billion.

II-VI Performance Metals operation:

- Refinement, reclamation, and marketing of a rare earth element for a green energy application.

Rare earth elements are used in many electronic and alternative green energy applications. We believe that the current addressable market serviced by our II-VI Performance Metals business for its rare earth element is approximately $40 million.

II-VI Marlow operation:

- Design, manufacture and marketing of thermoelectric modules and assemblies for cooling, heating and power generation applications in the defense, telecommunications, medical, consumer and industrial markets.

Thermoelectric Modules (“TEMs”) are solid-state semiconductor devices that act as small heat pumps to cool, heat and temperature stabilize a wide range of materials, components and systems. Conversely, the principles underlying thermoelectrics allow TEMs to be used as a source of power when subjected to temperature differences. TEMs are more reliable than alternative cooling solutions that require moving parts and provide more precise temperature control solutions than competing technologies. TEMs also have many other advantages which have spurred their adoption in a variety of industries and applications including defense and space applications that involve infrared cooled and uncooled night vision technologies and thermal reference sources that are deployed in state-of-the-art weapons, as well as cooling high-powered lasers used for range-finding target designation by military personnel. TEMs also allow for temperature stabilization of telecommunication lasers that generate and amplify optical signals for fiber optics systems. Thermoelectric-based solutions appear in a variety of medical applications including instrumentation and analytical applications such as DNA replication, blood analyzers and medical laser equipment. The industrial, commercial and consumer markets provide a variety of niche applications ranging from desktop refrigerators and wine coolers to personal comfort technology, semiconductor processes and test equipment. In addition, power generation applications are expanding into fields such as waste heat recovery, heat scavenging and co-generation. We believe that the current addressable markets serviced by our II-VI Marlow operations are approximately $250 million.

II-VI M Cubed operation:

- Design, manufacture and marketing of advanced ceramic materials and precision products for the semiconductor, display, industrial and defense markets.

Metal matrix composites (“MMC”) and reaction bonded ceramics products are found in applications requiring precision, lightweight, strength, hardness and matched coefficient of thermal expansion. Each market has its own unique requirements and applications that drive material selection. This is especially true in semiconductor tool applications that require advanced materials to meet the need for increased tolerance, enhanced thermal stability, faster wafer transfer speeds, increased yields and reduced stage settling times. The semiconductor markets employ SiC for wafer chucks, light-wave scanning stages and high temperature, corrosion resistant wafer support systems. Cooled SiC mirrors are used in the illumination systems of lithography tools. The industrial market uses a variety of ceramic materials for applications requiring chemical inertness or high temperature tolerance such as in flat panel display capital equipment, and refractory components. The defense market uses MMCs for protective body armor as well as protection for ground, air and naval resources. We believe that the current addressable markets serviced by our II-VI M Cubed operations are approximately $400 million.

II-VI Advanced Materials operation:

- Design, manufacture and marketing of single crystal SiC substrates and polycrystalline CVD diamond materials for use in the mobile communications, renewable energy, industrial, defense, semiconductor equipment and thermal management markets.

SiC is a wide bandgap semiconductor material that offers high-temperature, high-power and high-frequency capabilities as a substrate for applications at the high-performance end of the defense, telecommunication and industrial markets. SiC has a high number of intrinsic physical and electronic advantages over competing semiconductor materials such as silicon and gallium arsenide. For example, the high thermal conductivity of SiC enables SiC-based devices to operate at high-power levels and still dissipate the excess heat generated. II-VI Advanced Materials supplies the base SiC substrates into this market. SiC based structures are being developed and deployed for the manufacture of a wide variety of microwave and power switching devices. High-power, high-frequency SiC-based microwave devices are used in next generation wireless switching telecommunication applications and in both commercial and military radar applications. SiC-based, high-power, high-speed devices improve the performance, efficiency and reliability of electrical power transmission and distribution systems (“smart grid”). They also provide power conditioning and switching in power supplies and motor controls in a wide variety of applications including aircraft, hybrid vehicles, industrial, communications and green energy applications. Both SiC and CVD Diamond are being utilized in optical and electronic applications requiring high thermal conductivity for advanced thermal management. CVD Diamond also has applications in the semiconductor equipment (EUV Lithography), windows, tooling, microwave and radiation detection markets. We believe that the current addressable markets serviced by our II-VI Advanced Materials operations are approximately $125 million.

Our Strategy

Our strategy is to build businesses with core world-class engineered materials capabilities to penetrate new markets through innovative technologies and platforms, new product introductions and performance improvements. Our materials capabilities include:

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II-VI Infrared Optics: Zinc Selenide (ZnSe), Zinc Sulfide (ZnS), Zinc Sulfide Multi Spectral (ZnS-MS), and CVD Diamond

- II-VI Laser Enterprise: Epitaxial growth of Aluminum Indium Gallium Arsenide (AlInGaAs) based semiconductor laser materials
- II-VI Photonics: Yttrium Aluminum Garnet (YAG), Yttrium Lithium Fluoride (YLF), Calcium Fluoride (CaF_2), Yttrium Vanadate (YVO_4), Potassium Titanyl Phosphate (KTP), Barium Borate Oxide (BBO), Terbium Gallium Garnet (TGG) and Amorphous Silicon (a-Si)
- II-VI Optical Systems: Germanium (Ge), Silicon (Si), Sapphire (Al_2O_3), Yttrium Aluminum Garnet (YAG), Yttrium Lithium Fluoride (YLF), and Calcium Fluoride (CaF_2)
- II-VI Performance Metals: Processing and Refinement: Selenium (Se) for internal consumption and a Rare Earth Element
- II-VI Marlow: Bismuth Telluride (Bi_2Te_3)

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- II-VI M Cubed: Metal Matrix Composites (“MMC”), Reaction Bonded Ceramic (RB SiC and RB B_4C) and Aluminum Silicon Carbide (Al-SiC)
- II-VI Advanced Materials: SiC Substrates, CVD Diamond

A substantial portion of our business is based on sales orders with market leaders, which enable our forward planning and production efficiencies. We intend to continue capitalizing and executing on this proven model, participating effectively in the growth of the markets discussed above, and continuing our focus on operational excellence as we execute additional growth initiatives in the areas of:

- Identify New Products and Markets. We intend to identify new technologies, products and markets to meet evolving customer requirements for high performance engineered materials through our dedicated corporate research and development program to increase new product revenue and maximize return on investment.
- Balanced Approach to Research and Development. Our research and development program includes both internally and externally funded research and development expenditures, targeting an overall investment of between 7 and 9 percent of revenues. We are committed to accepting the right mix of internally and externally funded research that ties closely to our long-term strategic objectives.
- Leverage Vertical Integration. By combining the capabilities of our various business segments and operating units, we have created opportunities for our businesses to address manufacturing opportunities across multiple disciplines and markets and to reduce cost and lead time, thus enhancing competiveness, time to market and profitability. Where appropriate, we develop and/or acquire technological capabilities in areas such as material refinement, crystal growth, fabrication, diamond-turning, thin-film coating, metrology and assembly.
- Investment in Low Cost Manufacturing. We strategically invest in our manufacturing operations worldwide, including Asia, to increase production capacity, capabilities and cost effectiveness. The majority of our capital expenditures are used in our manufacturing operations.
- Enhance Our Performance and Reputation as a Quality and Customer Service Leader. We have established ourselves as a consistent, high-quality supplier of components into our customers’ products and are committed to continuous improvement. In many cases, we deliver on a just-in-time basis. We are implementing a global quality transformation process eliminating costs of non-conforming materials and processes.
- Identify and Complete Strategic Acquisitions and Alliances. From time to time we carefully evaluate strategic acquisitions and alliances with companies whose products or technologies may complement our current products, expand our market opportunities or create synergies with our current capabilities. We seek to identify acquisition opportunities that accelerate our access to emerging high-growth segments of the markets we serve and further leverage our competencies and economies of scale.

Research, Development and Engineering

During the current fiscal year ended June 30, 2015, the Company launched a new initiative to identify, invest in and focus our research and development on new products across the Company in an effort to accelerate our organic growth. This initiative is managed under a disciplined innovation program that we refer to as the “II-VI Phase Gate Process”.

Our research and development program includes internally and externally funded research and development expenditures targeting an overall annual investment of between 7 and 9 percent of product revenues. From time to time, the ratio of externally funded contract activity to internally funded contract activity varies due to the unevenness of government funded research programs and changes in the focus of our internally funded research programs. We are committed to having the right mix of internally and externally funded research that ties closely to our long-term strategic objectives. The Company continues to believe that externally funded research and development will decrease in the near term due to governmental budget constraints.

We devote significant resources to research, development and engineering programs directed at the continuous improvement of our existing products and processes and to the timely development of new technologies, materials and products. We believe that our research, development and engineering activities are essential to establish and maintain a leadership position in each of the markets we serve. As of June 30, 2015, we employed 1,010 people in research, development and engineering functions, 645 of whom are engineers or scientists. In addition, certain manufacturing personnel support or participate in our research and development efforts on an ongoing basis. We believe this interaction between the development and manufacturing functions enhances the direction of our projects and design for manufacturing, reducing costs and accelerating technology transfers.

During the fiscal year ended June 30, 2015, we focused our research and development investments in the following areas:

- Silicon Carbide Technology: SiC substrate technology development efforts continued to move forward, with emphasis in the areas of defect density reduction, substrate fabrication, surface polishing, diameter expansion and cost reduction. Through these efforts, we have become one of the leading suppliers of high quality 150mm SiC material and have emerged as the first supplier of 200mm SiC material. Our research and development efforts have been both internally and externally funded.
- CVD Diamond Technology: The Company continued to develop CVD synthetic diamond materials for various optical applications, including EUV lithography. The Company's efforts are focused on improving performance and quality, reducing cost and broadening our product portfolio beyond infrared window applications. Our research and development efforts in this area have been internally funded.
- Photonics Design: We have ongoing efforts to design, refine and improve our photonic crystal materials, precision optical and micro-optical parts, passive and active optical components and modules, components for fiber lasers and laser devices for instrumentation and display. Our research and development efforts in this area have been internally funded.
- Micro-Optics Manufacturing: Systems are driving towards smaller, more compact platforms and packages which are also reducing the size of the optical components that support these systems. The Company invests in equipment to manufacture substrates using high-volume, computer-controlled manufacturing processes. Our research and development efforts in this area have been both internally and externally funded.
- Thermoelectric Materials and Devices: We continued to develop the industry-leading Bi_2Te_3 for thermoelectric cooling and heating applications. Our research and development has focused on achieving levels of miniaturization and watt density beyond materials produced by standard crystal growth techniques. In addition, we are developing capabilities in thermoelectric power generation materials that, combined with our intellectual property position, will allow us to bring to market new thermoelectric products. Our research and development efforts in this area have been both internally and externally funded.
- Metal Matrix Composites and Reaction Bonded Ceramics: We continued to support OEMs in connection with new product development relating to process, inspection and test measurement tools in both the front and back ends of the semiconductor fabrication. Our research and development efforts in this area have been both internally and externally funded.
- High-power Laser Diodes and High Volume Components: Our engineering efforts focus on increasing the fiber coupled optical output power of our multi-emitter modules. The Company is focusing on the development of high-power VCSELs for applications in consumer devices as well as on the development of next generation high speed VCSELs for datacom applications. Our research and development efforts in this area have been internally funded.
- Pump Lasers: We continued our investment in next generation GaAs pump chip and module for both terrestrial high-power and undersea improved reliability and performance. We are developing an indium phosphide growth and processing capability in order to address the market with performance competitive design elements brought across from the high volume 980nm pump capability. Our research and development efforts in this area have been internally funded.
- Optical Amplifiers: We continued to invest in broadening the range of semi-custom and custom amplifiers to service our tier 1 customers. Our research and development efforts in this area have been internally funded.
- Optical Monitoring: We continued our investment in optical channel monitors. We also started efforts on developing Optical Time Domain Reflectometer ("OTDR") monitors for measuring the health of the outside fiber plant and connections within central offices. Our research and development efforts in this area have been internally funded.
- Transceivers: We continued our investment in developing 40G and 100G transceivers for use within data centers. Our research and development activities in this area have been internally funded.

The development of our products and manufacturing processes is largely based on proprietary technical know-how and expertise. We rely on a combination of contract provisions, trade secret laws, invention disclosures and patents to protect our proprietary rights. We have entered into selective intellectual property licensing agreements. When faced with potential infringement of our proprietary information, we have in the past and will continue to assert and vigorously protect our intellectual property rights.

Internally funded research and development expenditures were $51.3 million, $42.5 million and $22.7 million for the fiscal years ended June 30, 2015, 2014 and 2013, respectively. For these same periods, externally funded research and development expenditures were $9.5 million, $3.5 million and $4.5 million, respectively.

Marketing and Sales

We market our products through a direct sales force and through representatives and distributors around the world. Our market strategy is focused on understanding our customers' requirements and building market awareness and acceptance of our products. New products are continually being produced and sold to our new and established customers in all markets.

Each of our subsidiaries is responsible for its own worldwide marketing and sales functions, although certain subsidiaries sell more than one product line. However, there is significant cooperation and coordination among our subsidiaries to utilize the most efficient and appropriate marketing channel when addressing diverse applications within markets.

Our sales forces develop effective communications with our OEM and end-user customers worldwide. Products are actively marketed through targeted mailings, telemarketing, select advertising and attendance at trade shows and customer partnerships. Our sales force includes a highly-trained team of application engineers to assist customers in designing, testing and qualifying our parts as key components of our customers' systems. As of June 30, 2015, we employed 293 individuals in sales, marketing and support.

We do business with a number of customers in the defense industry, who in turn generally contract with a governmental entity, typically a U.S. governmental agency. Most governmental programs are subject to funding approval and can be modified or terminated without warning by a legislative or administrative body. For further information regarding our exposure to government markets, see the discussion set forth in Item 1A of this Annual Report on Form 10-K.

Manufacturing Technology and Processes

As noted in the "Our Strategy" section, many of the products we produce depend on our ability to manufacture and refine technically challenging materials and components. The ability to produce, process and refine these difficult materials and to control their quality and yields is an expertise of the Company that is critical to the performance of our customers' instruments and systems. In the markets we serve, there are a limited number of suppliers of many of the components we manufacture and there are very few industry-standard products.

Our network of worldwide manufacturing sites allows us to manufacture our products in regions that provide cost-effective advantages and proximity to our customers. We employ numerous advanced manufacturing technologies and systems at our manufacturing facilities. These include automated CNC (Computer Numeric Control) optical fabrication, high throughput thin-film coaters, micro-precision metrology and custom-engineered automated furnace controls for the crystal growth processes. Manufacturing products for use across the electro-magnetic spectrum requires the capability to repeatedly produce products with high yields to atomic tolerances. We embody a technology and quality mindset that gives our customers the confidence to utilize our products on a just-in-time basis straight into the heart of their production lines.

Export and Import Compliance

We are required to comply with various export/import control and economic sanction laws, including:

- The International Traffic in Arms Regulations ("ITAR") administered by the U.S. Department of State, Directorate of Defense Trade Controls, which, among other things, imposes license requirements on the export from the U.S. of defense articles and defense services, which are items specifically designed or adapted for a military application and/or listed on the U.S. Munitions List;

- The Export Administration Regulations ("EAR") administered by the U.S. Department of Commerce, Bureau of Industry and Security, which, among other things, imposes licensing requirements on the export or re-export of certain dual-use goods, technology and software, which are items that potentially have both commercial and military applications;
- The regulations administered by the U.S. Department of Treasury, Office of Foreign Assets Control, which implement economic sanctions imposed against designated countries, governments and persons based on U.S. foreign policy and national security considerations; and
- The import regulatory activities of the U.S. Customs and Border Protection.

Foreign governments have also implemented similar export and import control regulations, which may affect our operations or transactions subject to their jurisdiction. For additional discussions regarding our import and export compliance, see the discussion set forth in Item 1A of this Annual Report Form on Form 10-K.

Sources of Supply

The major raw materials we use include zinc, selenium, zinc selenide, zinc sulfide, hydrogen selenide, hydrogen sulfide, tellurium, yttrium oxide, aluminum oxide, iridium, platinum, bismuth, silicon, thorium fluoride, antimony, carbon, gallium arsenide, copper, germanium, molybdenum, quartz, optical glass, diamond, and other materials. Excluding our own production, there are more than two external suppliers for all of the above materials except for zinc sulfide, hydrogen selenide and thorium fluoride, for which there is only one proven source of supply outside of the Company's capabilities, and zinc selenide, for which there are no other proven external sources of supply. For many materials, we have entered into purchase arrangements which provide discounts for annual volume purchases in excess of specified amounts.

The continued high-quality of and access to these materials is critical to the stability and predictability of our manufacturing yields. We test materials at the onset of the production process. Additional research and capital investment may be needed to better define future starting material specifications. We have not experienced significant production delays due to shortages of materials. However, we do occasionally experience problems associated with vendor-supplied materials not meeting contract specifications for quality or purity. As discussed in greater detail in Item 1A, of this Annual Report on Form 10-K, significant failure of our suppliers to deliver sufficient quantities of necessary high-quality materials on a timely basis could have a materially adverse effect on our results of our operations.

Customers

The main groups of customers by segments are as follows:

Segment:	Group/Division:	Our Customers Are:	Representative Customers:
II-VI Laser Solutions	II-VI Infrared Optics Group	OEM and system integrators of industrial, medical and military laser systems.	·Trumpf, Inc. ·Bystronic, Inc. ·Rofin-Sinar Technologies, Inc.
		Laser end users who require replacement optics for their existing laser systems.	·Caterpillar, Inc. ·Honda of America Mfg., Inc.
		Military, aerospace and commercial customers requiring products for use in advanced targeting, navigation and surveillance.	·Lockheed Martin Corporation ·Northrop Grumman Corporation.
	II-VI HIGHYAG Division	Automotive manufacturers, laser manufacturers and system integrators.	·Volkswagen AG ·Laserline GmbH.
	II-VI Laser Enterprise Division	Manufacturers of industrial laser components and optical communication equipment.	·Laserline GmbH ·Huawei Technologies, Co., Ltd. ·Cisco Systems, Inc.
II-VI Photonics	II-VI Photop Group and	Worldwide network system and sub-system providers of telecommunications, data communications and cable TV.	·Huawei Technologies, Co., Ltd.
	II-VI Optical Communications Group	Global manufacturers of commercial and consumer products used in a wide array of instruments, fiber lasers, display and projection devices.	·Cisco Systems, Inc. ·Corning Incorporated ·Google, Inc.
II-VI Performance	II-VI Optical Systems	Manufacturers of equipment and devices for aerospace, defense, life science and commercial markets.	·Lockheed Martin Corporation

Products			·Raytheon Company ·BAE Systems ·Boeing Corporation ·Northrup Grumman Corporation
	II-VI Marlow	Manufacturers and developers of equipment and devices for defense, space, telecommunications, medical, industrial, automotive, personal comfort and commercial markets.	·Bio-Rad Laboratories, Inc. ·Raytheon Company ·Flextronics International Ltd.
	II-VI M Cubed	Manufacturers and developers of integrated circuit capital equipment for the semiconductor industry.	·ASML Holding NV ·Nikon Corporation ·KLA-Tencor
		Manufacturers and developers of products and components for various defense and industrial markets.	·BAE Systems ·Corning Incorporated.
	II-VI Advanced Materials	Manufacturers and developers of equipment and devices for high-power RF electronics and high-power and voltage switching and power conversion systems for both commercial and military applications. Manufacturers of high-power optical and electronic devices requiring advanced thermal management solutions.	·IQE plc ·Infineon Technologies

Competition

We believe we are a global leader in many of our product families. We compete on the basis of the highly engineered nature of our products, quality, delivery time, technical support and pricing. We believe that we compete favorably with respect to these factors and that our vertical integration, manufacturing facilities and equipment, experienced technical and manufacturing employees and worldwide marketing and distribution channels provide us with competitive advantages. The main groups of our competitors are as follows:

Segment:	Areas of Competition:	Competitors:
II-VI Laser Solutions	Infrared laser optics	·Sumitomo Electric Industries, Ltd. ·Newport Corporation
	Automated equipment and laser material processing tools to deliver high-power one-micron laser systems	·Optoskand AB ·Precitec, Inc
	Semiconductor laser diodes for the industrial and consumer markets	·JDSU Uniphase Corporation ·Finisar Corporation ·Avago Technologies ·Sumitomo Electric Industries, Ltd. ·Koninklijke Philips N.V ·Jenoptik AG ·Osram Licht AG
II-VI Photonics	Optical component and optics products	·O-Net Communications Group Ltd. ·OPLINK Communication, LLC ·Axsun
	Optical amplifier modules	·JDSU Uniphase Corporation ·Finisar Corporation ·Accelink ·O-Net Communications Group, Ltd.
II-VI Performance Products	Infrared optics for military applications	·DRS Technologies, Inc. ·UTC Aerospace Systems (formerly Goodrich Corporation) ·In-house fabrication and thin-film coating capabilities of major military customers

TEMs	·Komatsu, Ltd. ·Laird plc ·Ferrotec Corporation
MMCs and reaction bonded ceramics products	·Berliner Glas ·CoorsTek, Inc.
Single crystal SiC substrates	·Cree, Inc. ·Dow Corning Corporation ·Nippon Steel & Sumitomo Metal ·SiCrystal AG

In addition to competitors who manufacture products similar to those we produce, there are other technologies and products available that may compete with our technologies and products.

Bookings and Backlog

We define our bookings as customer orders received that are expected to be converted to revenues over the next twelve months. For long-term customer orders, to address the inherent uncertainty of orders that extend far into the future, the Company records only those orders which are expected to be converted into revenues within twelve months from the end of the reporting period. Bookings are adjusted if changes in customer demands or production schedules move a delivery beyond twelve months. For the year ended June 30, 2015, our bookings were approximately $762 million compared to bookings of approximately $691 million for the year ended June 30, 2014.

We define our backlog as bookings that have not been converted to revenues by the end of the reporting period. As of June 30, 2015, our backlog was approximately $242 million, compared to approximately $220 million at June 30, 2014.

Employees

As of June 30, 2015, we employed 8,490 persons worldwide. Of these employees, 1,010 were engaged in research, development and engineering, 6,516 in direct production (of which 1,114 are employees of Photop in China who work under contract manufacturing arrangements for customers of the Company) and the remaining balance of the Company's employees work in sales and marketing, administration, finance and support services. Our production staff includes highly skilled optical craftsmen. We have a long-standing practice of encouraging active employee participation in areas of operations management. We believe our relations with our employees are good. We reward our employees with incentive compensation based on achievement of performance goals. There are 131 employees located in the United States and the Philippines who are covered under collective bargaining agreements. The Company's collective bargaining agreement in the Philippines will expire in June 2016. The collective bargaining agreement covering certain U.S. based employees expired August 5, 2015. The Company is currently in negotiations to extend the collective bargaining agreement that expired in the U.S.

Trade Secrets, Patents and Trademarks

We rely on a combination of trade secrets, proprietary know-how, invention disclosures, patents and contractual provisions to help us develop and maintain our competitive position with respect to our products and manufacturing processes. We aggressively pursue process and product patents in certain areas of our businesses. We have entered into selective intellectual property licensing agreements. When faced with potential infringement of our proprietary information, we have in the past and will continue to assert and vigorously protect our intellectual property rights. We have confidentiality and noncompetition agreements with certain personnel. We require that all U.S. employees sign a confidentiality and noncompetition agreement upon their commencement of employment with us.

The processes and specialized equipment utilized in crystal growth, infrared materials fabrication and infrared optical coatings as developed by us are complex and difficult to duplicate. However, there can be no assurance that others will not develop or patent similar technology or that all aspects of our proprietary technology will be protected. Others have obtained patents covering a variety of infrared optical configurations and processes, and others could obtain patents covering technology similar to our technology. We may be required to obtain licenses under such patents, and there can be no assurance that we would be able to obtain such licenses, if required, on commercially reasonable terms, or that claims regarding rights to technology will not be asserted which may adversely affect our results of operations. In addition, our research and development contracts with agencies of the U.S. Government present a risk that project-specific technology could be disclosed to competitors as contract reporting requirements are fulfilled.

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Item 1A. RISK FACTORS

The Company cautions investors that its performance and, therefore, any forward-looking statement, is subject to risks and uncertainties. The following material risk factors may cause the Company's future results to differ materially from those projected in any forward-looking statement. You should carefully consider these factors, as well as the other information contained in this Annual Report on Form 10-K when evaluating an investment in our securities.

Our Future Success Depends on International Sales and Successful Management of Global Operations

Sales to customers in countries other than the U.S. accounted for approximately 63%, 65% and 56% of revenues during the years ended June 30, 2015, 2014 and 2013, respectively. We anticipate that international sales will continue to account for a significant portion of our revenues for the foreseeable future. In addition, we manufacture products in China, Singapore, Vietnam, the Philippines, Germany, and Switzerland, and through contract manufacturers in Thailand and China, and maintain direct sales offices in Hong Kong, Japan, Germany, Switzerland, the U.K., Belgium, China, Singapore, Italy and South Korea. Sales and operations outside of the U.S. are subject to certain inherent risks, including fluctuations in the value of the U.S. dollar relative to foreign currencies, global economic uncertainties, tariffs, quotas, taxes and other market barriers, political and economic instability, restrictions on the export or import of technology, potentially limited intellectual property protection, difficulties in staffing and managing international operations and potentially adverse tax consequences, and required compliance with U.S.- and non-U.S. laws and regulations. More specifically, we are subject to laws and regulations worldwide affecting our operations outside the U.S. in areas including, but not limited to, IP ownership and infringement, tax, customs, import and export requirements, anti-corruption and anti-bribery, foreign exchange controls and cash repatriation restrictions, foreign investment, data privacy requirements, anti-competition, pensions and social insurance, employment, and environment, health, and safety. Compliance with these laws and regulations may be onerous and expensive and requirements may differ among jurisdictions. Further, the promulgation of new laws, changing in existing laws and abrogation of local regulations by national laws may have a negative impact on our business and prospects. In addition, certain laws and regulations are relatively new and their interpretation and enforcement involve significant uncertainties. There can be no assurance that any of these factors will not have a material adverse effect on our business, results of operations or financial condition.

Our Continued Success Depends on Our Ability to Develop New Products and Processes

In order to meet our strategic objectives, we must continue to develop, manufacture and market new products, develop new processes and improve existing processes. As a result, we expect to continue to make significant investments in research and development and to continue to consider from time to time the strategic acquisition of businesses, products or technologies complementary to our business. Our success in developing, introducing and selling new and enhanced products depends upon a variety of factors including product selection, timely and efficient completion of product design and development, timely and efficient implementation of manufacturing and assembly processes, effective sales and marketing and product performance in the field. There can be no assurance that we will be able to develop and introduce new products or enhancements to our existing products and processes in a manner which satisfies customer needs or achieves market acceptance. The failure to do so could have a material adverse effect on our ability to grow our business.

Keeping Pace with Key Industry Developments is Essential

The introduction of products or processes utilizing new developments could render existing products or processes obsolete or unmarketable. Our continued success will depend upon our ability to develop and introduce, in a timely and cost-effective manner, new products, processes and applications that keep pace with developments and address increasingly sophisticated customer requirements. There can be no assurance that we will be successful in identifying, developing and marketing new products, applications and processes and that we will not experience difficulties that could delay or prevent the successful development, introduction and marketing of product or process enhancements or new products, applications or processes, or that our products, applications or processes will adequately meet the requirements of the marketplace and achieve market acceptance. Our business, results of operations and financial condition could be materially and adversely affected if we were to incur delays in developing new products, applications or processes or if they do not achieve market acceptance.

We May Expand Product Lines and Markets by Acquiring Other Businesses, Which May Adversely Affect our Results and Affect the Value of our Stock Following Such Acquisitions

Our business strategy includes expanding our product lines and markets through both internal product development and acquisitions. We have completed various acquisitions in recent years and the success of these acquisitions will depend, in part, on our ability to realize the anticipated benefits from integrating and successfully running the businesses acquired. The strategic acquisition of businesses, products or technologies complementary to our business involves numerous potential risks, including difficulties in the assimilation of the acquired business and products, uncertainties associated with operating in new markets, working with new customers and the potential loss of the acquired company’s key personnel. In addition, acquired businesses may experience operating losses as of, and subsequent to, the acquisition date. Further, we significantly increased our long-term debt to finance these acquisitions, the costs of which (in terms of interest expense and similar debt service costs), must be weighed against the potential benefits of such acquisitions. The anticipated benefits and cost savings of an acquisition may not be realized fully, or at all, or may take longer to realize than expected, and as a result our results of operations, financial position, and cash flow may be adversely affected.

Further, any future business acquisitions completed by us may result in potentially dilutive issuances of our equity securities, the incurrence of debt, contingent liabilities and amortization expense related to intangible assets acquired, any of which could have a material adverse effect on our business, results of operations or financial condition.

Declines in the Operating Performance of One of Our Business Segments Could Result in an Impairment of the Segment's Goodwill and Indefinite-Lived Intangible Assets

As of June 30, 2015, we had goodwill and indefinite-lived intangible assets of approximately $195.9 million and $14.4 million, respectively, on our Consolidated Balance Sheet. In accordance with applicable accounting guidance, we test our goodwill and indefinite-lived intangible assets for impairment on an annual basis or when an indication of possible impairment exists, to determine whether the carrying value of our assets is still supported by the fair value of the underlying business. To the extent that it is not, we are required to record an impairment charge to reduce the asset to fair value. A decline in the operating performance of any of our business segments could result in an impairment charge which could have a material adverse effect on our results of operations or financial condition.

General Global Economic Conditions May Adversely Affect Our Business, Operating Results and Financial Condition

Current and future conditions in the global economy have an inherent degree of uncertainty. As a result, it is difficult to estimate the level of growth or contraction for the global economy as a whole. It is even more difficult to estimate growth or contraction in various parts, sectors and regions of the economy, including industrial, military, optical communications, telecommunications, semiconductor, and medical and life science markets in which we participate. Because all components of our forecasting are dependent upon estimates of growth or contraction in the markets we serve and demand for our products, the prevailing global economic uncertainties render estimates of future income and expenditures very difficult to make. In addition, changes in general economic conditions may affect industries in which our customers operate. These changes could include decreases in the rate of consumption or use of our customers' products due to economic downturn, and such conditions could have a material adverse effect on demand for our customers' products, and in turn, on demand for our products. Adverse changes may occur in the future as a result of declining or flat global or regional economic conditions, fluctuations in currency and commodity prices, wavering confidence, capital expenditure reductions, unemployment, decline in stock markets, contraction of credit availability or other factors affecting economic conditions. For example, factors that may affect our operating results include disruptions to the credit and financial markets in the U.S., Europe and elsewhere; adverse effects of ongoing stagnation in the European economy; slowdown in the Chinese economy; contractions or limited growth in consumer spending or consumer credit; and adverse economic conditions that may be specific to the Internet, e-commerce and payments industries. These changes may negatively affect sales of products, increase exposure to losses from bad debt and commodity prices, increase the cost and availability of financing and increase costs associated with manufacturing and distributing products. Any economic downturn could have a material adverse effect on our business, results of operations or financial condition.

There Are Limitations on the Protection of Our Intellectual Property

We rely on a combination of trade secret, patent, copyright and trademark laws combined with employee noncompetition and nondisclosure agreements to protect our intellectual property rights. There can be no assurance that the steps taken by us will be adequate to prevent misappropriation of our technology or intellectual property. Furthermore, there can be no assurance that third-parties will not assert infringement claims against us in the future. Asserting our intellectual property rights or defending against third-party claims could involve substantial expense, thus materially and adversely affecting our business, results of operations or financial condition. In the event a third-party were successful in a claim that one of our processes infringed its proprietary rights, we could be required to pay substantial damages or royalties, or expend substantial amounts in order to obtain a license or modify processes so that they no longer infringe such proprietary rights, any of which could have a material adverse effect on our business, results of operations or financial condition.

We Are Subject to Governmental Regulation

We are subject to the passage of and changes in the interpretation of regulation by U.S. government entities at the federal, state and local levels and non-U.S. agencies, including, but not limited to, the following:

- We are required to comply with various import laws and export control and economic sanctions laws, which may affect our transactions with certain customers, business partners and other persons, including in certain cases dealings with or

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between our employees and subsidiaries. In certain circumstances, export control and economic sanctions regulations may prohibit the export of certain products, services and technologies, and in other circumstances we may be required to obtain an export license before exporting the controlled item. Compliance with the various import laws that apply to our businesses may restrict our access to, and may increase the cost of obtaining, certain products and could interrupt our supply of imported inventory.

- Exported technology necessary to develop and manufacture certain Company products are subject to U.S. export control laws and similar laws of other jurisdictions, and the Company may be subject to adverse regulatory consequences, including government oversight of facilities and export transactions, monetary penalties and other sanctions for violations of these laws. In certain instances, these regulations may prohibit the Company from developing or manufacturing certain of its products for specific end applications outside the U.S.
- Our agreements relating to the sale of products to government entities may be subject to termination, reduction or modification in the event of changes in government requirements, reductions in federal spending and other factors. We are also subject to investigation and audit for compliance with the requirements of government contracts, including requirements related to procurement integrity, export control, employment practices, the accuracy of records and the recording of costs. A failure to comply with these requirements might result in suspension of these contracts and suspension or debarment from government contracting or subcontracting.

In addition, failure to comply with any of these laws and regulations could result in civil and criminal, monetary and non-monetary penalties, disruptions to our business, limitations on our ability to import and export products and services and damage to our reputation.

We Are Subject to Stringent Environmental Regulation

We use or generate certain hazardous substances in our research and manufacturing facilities. We believe that our handling of such substances is in material compliance with applicable local, state and federal environmental, safety and health regulations at each operating location. We invest substantially in proper protective equipment, process controls and specialized training to minimize risks to employees, surrounding communities and the environment resulting from the presence and handling of such hazardous substances. We regularly conduct employee physical examinations and workplace monitoring regarding such substances. When exposure problems or potential exposure problems have been uncovered, corrective actions have been implemented and re-occurrence has been minimal or non-existent. We do not carry environmental impairment insurance.

We have in place an emergency response plan with respect to our generation and use of the hazardous substance Hydrogen Selenide. Special attention has been given to all procedures pertaining to this gaseous material to minimize the chances of its accidental release into the atmosphere.

With respect to the manufacturing, use, storage and disposal of the low-level radioactive material Thorium Fluoride, our facilities and procedures have been inspected and licensed by the Nuclear Regulatory Commission. Thorium-bearing by-products are collected and shipped as solid waste to a government-approved low-level radioactive waste disposal site in Clive, Utah.

The generation, use, collection, storage and disposal of all other hazardous by-products, such as suspended solids containing heavy metals or airborne particulates, are believed by us to be in material compliance with regulations. We believe that we have obtained all of the permits and licenses required for operation of our business.

Although we do not know of any material environmental, safety or health problems in our properties or processes, there can be no assurance that problems will not develop in the future which could have a material adverse effect on our business, results of operations or financial condition.

We May Be Adversely Affected by Climate Change Regulation

In many of the countries in which we operate, government bodies are increasingly enacting or contemplating enacting legislation and regulations in response to potential impacts of climate change. These laws and regulations may be mandatory or voluntary, and have the potential to impact our operations directly or indirectly through implications on our customers or our supply chain. Inconsistency of regulations may also affect the costs of compliance with such laws and regulations. Assessments of the potential impact of future climate change legislation, regulation and international treaties and accords are uncertain, given the wide scope of potential regulatory change in countries in which we operate. We may incur increased capital expenditures resulting from required compliance with revised or new legislation or regulations, costs to purchase or profits from sales of, allowances or credits under a “cap and trade” system, increased insurance premiums and deductibles as new actuarial tables are developed to reshape coverage, a change in competitive position relative to industry peers and changes to profit or loss arising from increased or decreased demand for goods produced by us and indirectly, from changes in costs of goods sold.

Regulations Related to Conflict Minerals Could Adversely Impact Our Business.

The Dodd-Frank Wall Street Reform and Consumer Protection Act contain provisions to improve transparency and accountability concerning the supply of gold, columbite-tantalite (coltan), cassiterite and wolframite, including their derivatives, which are limited to tantalum, tin and tungsten, known as “conflict minerals,” originating from the Democratic Republic of Congo (DRC) and adjoining countries (collectively known as the "covered countries"). Pursuant to these rules, the SEC has adopted certain annual disclosure and reporting requirements for those companies that use conflict minerals in their products, regardless of whether such minerals were mined from the covered countries, compliance with which began in 2014. We could incur significant costs associated with complying with these disclosure requirements, including costs related to our due diligence efforts to determine the sources of any conflict minerals used in our products. These rules could adversely affect the sourcing, supply and pricing of materials we use in our products, particularly if it turns out that there are only a limited number of suppliers offering conflict minerals that are not from recycled or scrap sources, can be traced to a country of origin other than the covered countries, or can be traced to a source within the covered countries that definitely does not finance or benefit armed groups in those countries. We cannot be sure that we will be able to obtain products from such suppliers in sufficient quantities or at competitive prices. Also, we may face reputational challenges if we determine that certain of our products contain conflict minerals originating from the covered countries and we cannot definitively determine whether the conflict minerals financed or otherwise benefited armed groups, or if we are unable to sufficiently verify the origins of all of the conflict minerals used in our products through the due diligence procedures we implement.

Data Breach Incidents and Breakdown of Information and Communication Technologies Could Disrupt our Operations and Impact Our Financial Results

In the course of our business, we collect and store sensitive data, including intellectual property [both proprietary and of our customers], as well as proprietary business information. We could be subject to service outages or breaches of security systems which may result in disruption, unauthorized access, misappropriation, or corruption of this information. Security breaches of our network or data including physical or electronic break-ins, vendor service outages, computer viruses, attacks by hackers or similar breaches can create system disruptions, shutdowns, or unauthorized disclosure of confidential information. Although we have not experienced an incident, if we are unable to prevent such security or privacy breaches, our operations could be disrupted or we may suffer legal claims, loss of reputation, financial loss, property damage, or regulatory penalties because of lost or misappropriated information.

We Depend on Highly Complex Manufacturing Processes That Require Products from Limited Sources of Supply

We utilize high-quality, optical grade zinc selenide (ZnSe) in the production of many of our infrared optical products. We are the leading producer of ZnSe for our internal use and for external sale. The production of ZnSe is a complex process requiring a highly controlled environment. A number of factors, including defective or contaminated materials, could adversely affect our ability to achieve acceptable manufacturing yields of high quality ZnSe. No proven external sources of ZnSe are currently available. Lack of adequate availability of high quality ZnSe could have a material adverse effect upon us. There can be no assurance that we will not experience manufacturing yield inefficiencies which could have a material adverse effect on our business, results of operations or financial condition.

We produce Hydrogen Selenide gas which is used in our production of ZnSe. There are risks inherent in the production and handling of such material. Our lack of proper handling of Hydrogen Selenide could require us to curtail our production of Hydrogen Selenide. Hydrogen Selenide is available from only one outside source whose quantities and quality may be limited. The cost of purchasing such material is greater than the cost of internal production. As a result, the purchase of a substantial portion of such material from the outside source would increase our ZnSe production costs. Therefore, our inability to internally produce Hydrogen Selenide could have a material adverse effect on our business, results of operations or financial condition.

In addition, we produce and utilize other high purity and relatively uncommon materials and compounds to manufacture our products including, but not limited to, Zinc Sulfide (ZnS), Yttrium Aluminum Garnet (YAG), Yttrium Lithium Fluoride (YLF), Calcium Fluoride (CaF_2), Germanium (Ge), Selenium (Se), Telluride (Te), Bismuth Telluride (Bi_2Te_3) and Silicon Carbide (SiC). A significant failure of our internal production processes or our suppliers to deliver sufficient quantities of these necessary materials on a timely basis could have a material adverse effect on our business, results of operations or financial condition.

Some Systems That Utilize our Products Are Complex in Design and May Contain Defects that Are Not Detected Until Deployed Which Could Increase Our Costs and Reduce Our Revenues

Some systems that utilize our products are inherently complex in design and require ongoing maintenance. Our customers may discover defects in our products after the products have been fully deployed and operated under peak stress conditions. In addition, some of our products are combined with products from other vendors, and these third-party products may contain defects. Should problems occur, it may be difficult to identify the source of the problem. If we are unable to correct defects or other problems, we could experience, among other things: loss of customers; increased costs of product returns and warranty expenses; damage to our brand reputation; failure to attract new customers or achieve market acceptance; diversion of development and engineering resources; or legal action by our customers. The occurrence of any one or more of the foregoing factors could have a material adverse effect on our business, results of operations or financial condition.

Continued U.S. Budget Deficits Could Result in Significant Defense Spending Cuts and/or Reductions in Defense Programs, which Could Adversely Impact the Company

Specific to the military business within our II-VI Laser Solutions and II-VI Performance Products segments, sales to customers in the defense industry totaled approximately 12% of revenues for the fiscal year ended June 30, 2015. These customers in turn generally contract with a governmental entity, typically a U.S. governmental agency. Future reductions in defense spending could result from the current or future economic or political environment, such as the ongoing sequestration of the defense budget, which could result in reductions in demand for defense-related products that we produce. Further, changes to existing defense procurement laws and regulations could adversely affect our results of operations. Most governmental programs are subject to funding approval and can be modified or terminated with no warning upon the determination of a legislative or administrative body. The loss of or failure to obtain certain contracts or the loss of a major government customer could have a material adverse effect on our business, results of operations or financial condition.

Changes in Tax Rates, Tax Liabilities or Tax Accounting Rules Could Affect Future Results

As a global company, we are subject to taxation in the U.S. and various other countries and jurisdictions. As such, we must exercise a level of judgment in determining our worldwide tax liabilities. Our future tax rates could be affected by changes in the composition of earnings in countries with differing tax rates or changes in tax laws. Changes in tax laws or tax rulings may have a significantly adverse impact on our effective tax rate. For example, proposals for fundamental U.S. international tax reform, if enacted, could have a significant adverse impact on our effective tax rate. In addition, we are subject to regular examination of our income tax returns by the Internal Revenue Service and other tax authorities. We regularly assess the likelihood of favorable or unfavorable outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. Although we believe our tax estimates are reasonable, there can be no assurance that any final determination will not be materially different than the treatment reflected in our historical income tax provision and accruals, which could materially and adversely affect our business, results of operation or financial condition.

We May Encounter Substantial Competition

We may encounter substantial competition from other companies in the same market, including established companies with significant resources. Some of our competitors may have financial, technical, marketing or other capabilities that are more extensive than ours and may be able to respond more quickly than we can to new or emerging technologies and other competitive pressures. We may not be able to compete successfully against our present or future competitors, and such competition could have a material adverse effect on our business, results of operations or financial condition.

Our Success Depends on Our Ability to Retain Key Personnel

We are highly dependent upon the experience and continuing services of certain scientists, engineers, production and management personnel. Competition for the services of these personnel is intense, and there can be no assurance that we will be able to retain or attract the personnel necessary for our success. The loss of the services of our key personnel could have a material adverse effect on our business, results of operations or financial condition.

Natural Disasters or Other Global or Regional Catastrophic Events Could Disrupt Our Operations and Adversely Affect Results

We may be exposed to business interruptions due to catastrophe, natural disaster, pandemic, terrorism or acts of war that are beyond our control. Disruptions to our facilities or systems, or to those of our key suppliers, could also interrupt operational processes and adversely impact our ability to manufacture our products and provide services and support to our customers. As a result, our business, results of operations or financial condition could be materially adversely affected.

A Significant Portion of Our Business is Dependent on Cyclical Industries

Our business is significantly dependent on the demand for products produced by end-users of industrial lasers and optical communication products. Many of these end-users are in industries that have historically experienced a highly cyclical demand for their products. As a result, demand for our products is subject to these cyclical fluctuations. This cyclical demand could have a material adverse effect on our business, results of operations or financial condition.

Commodity Prices May Adversely Affect Our Results of Operations and Financial Condition

We are exposed to a variety of market risks, including the effects of changes in commodity prices. Our businesses purchase, produce and sell high purity selenium and other raw materials based upon quoted market prices from minor metal exchanges. As a result, the negative impact from changes in commodity prices may not be recovered through our product sales, and as such could have a material adverse effect on our net earnings and financial condition.

The Market Price of Our Common Stock Can Be Highly Volatile

Factors that could cause fluctuation in our stock price include, among other things: general economic and market conditions; actual or anticipated variations in operating results; changes in financial estimates by securities analysts; our inability to meet or exceed securities analysts' estimates or expectations; conditions or trends in the industries in which our products are purchased; announcements by us or our competitors of significant acquisitions, strategic partnerships, divestitures, joint ventures or other strategic initiatives; capital commitments; additions or departures of key personnel; and sales of our Common Stock.

Many of these factors are beyond our control. These factors could cause the market price of our Common Stock to decline, regardless of our actual operating performance.

Provisions in Our Articles of Incorporation and By-Laws May Limit the Price that Investors May be Willing to Pay in the Future for Shares of Our Common Stock

Our Articles of Incorporation and By-Laws contain provisions that could make us a less attractive target for a hostile takeover and could make more difficult or discourage a merger proposal, a tender offer or a proxy contest. Such provisions include: a requirement that shareholder-nominated director nominees be nominated in advance of the meeting at which directors are elected and that specific information be provided in connection with such nomination; the ability of the board of directors to issue additional shares of Common Stock or preferred stock without shareholder approval; and certain provisions requiring supermajority approval (at least two-thirds of the votes cast by all shareholders entitled to vote thereon, voting together as a single class). In addition, the Pennsylvania Business Corporation Law contains provisions that may have the effect of delaying or preventing a change in control of the Company. All of these provisions may limit the price that investors may be willing to pay for shares of our Common Stock.

Because We Do Not Currently Intend to Pay Dividends, Shareholders Will Benefit From an Investment in our Common Stock Only if it Appreciates in Value

We have never declared or paid any dividends on our Common Stock, and do not expect to pay cash dividends in the foreseeable future, as we currently anticipate that we will retain any future earnings to support operations and to finance the development of our business. As a result, the success of an investment in our Common Stock will depend entirely upon any future appreciation in its value. There is no guarantee that our Common Stock will maintain its value or appreciate in value.

RECENTLY ISSUED FINANCIAL ACCOUNTING STANDARDS

In July 2015, the Financial Accounting Standards Board (“FASB”) issued an Accounting Standard Update (“ASU”) 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. This update simplifies the measurement of inventory valuation at the lower of cost or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The new inventory measurement requirements are effective for the Company’s 2018 fiscal year and will replace the current inventory valuation guidance that requires the use of a lower of cost or market framework. The adoption of these changes is not expected to have a material impact to the Company’s Consolidated Financial Statements.

In April 2015, the FASB issued as final, ASU 2015-05, Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement. This update provides guidance about whether a cloud computing arrangement includes a software license. The update is effective for annual reporting periods, including interim periods within those annual periods, beginning after December 15, 2015. Early adoption is permitted. The update allows for the use of either a prospective or retrospective adoption approach. Management is currently evaluating the available transition methods and the potential impact of adoption on the Company’s Consolidated Financial Statements.

In April 2015, the FASB issued ASU 2015-03, Interest – Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs. This ASU requires entities to present debt issuance costs in the balance sheet as a direct deduction from the carrying amount of the corresponding debt liability, consistent with debt discounts. The guidance does not address situations in which debt issuance costs do not have an associated debt liability or exceed the carrying amount of the associated debt liability. This ASU will be effective beginning in fiscal year 2017. Management is currently evaluating the potential impact of adoption on the Company's Consolidated Financial Statements.

In February 2015, the FASB issued as final, ASU 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis, which affects reporting organizations that are required to evaluate whether they should consolidate certain legal entities. The update is effective for interim and annual reporting periods in fiscal years beginning after December 15, 2015. Early adoption is permitted, including adoption in an interim period. The update allows for the use of either a full retrospective or a modified retrospective adoption approach. Management is currently evaluating the available transition methods and the potential impact of adoption on the Company’s Consolidated Financial Statements.

In January 2015, the FASB issued ASU 2015-01, Income Statement - Extraordinary and Unusual Items. This ASU eliminates the requirement to separately present and disclose extraordinary and unusual items in the financial statements. This ASU will be effective beginning in 2016. The adoption of this ASU is not expected to have a material effect on our Consolidated Financial Statements.

In May 2014, the FASB issued ASU 2014-09: Revenue from Contracts with Customers (Topic 606) which supersedes virtually all existing revenue recognition guidance under U.S. GAAP. The update's core principle is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The update allows for the use of either the retrospective or modified retrospective approach of adoption. On July 9, 2015 the FASB approved a one year deferral of the effective date of the update. The update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017 (the first quarter of our fiscal year 2019). We have not yet selected a transition method and are currently evaluating the impact of this guidance on our Consolidated Financial Statements.

In April 2014, the FASB issued ASU 2014-08: Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity, which changes the criteria for determining which disposals can be presented as discontinued operations and modifies related disclosure requirements. Under the new guidance, a discontinued operation is defined as a disposal of a component or group of components that is disposed of or is classified as held for sale and represents a strategic shift that has or will have a major effect on an entity's operations and financial results. The new standard will be effective for annual periods beginning on or after December 15, 2014, with early adoption permitted and will be effective for the Company beginning in the first quarter of fiscal year 2016. The adoption of this standard is not expected to have a significant impact on the Company’s Consolidated Financial Statements.

In July 2013, the FASB issued ASU 2013-11: Presentation of an Unrecognized Tax benefit when a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit carryforward Exists. The ASU changes how certain unrecognized tax benefits are to be presented on the consolidated balance sheet. This ASU clarified existing guidance to require that an unrecognized tax benefit, or a portion thereof, be presented in the consolidated balance sheet as a reduction to a deferred tax asset for a net operating loss (“NOL”) carryforward, similar tax loss, or a tax credit carryforward, except when an NOL carryforward, similar tax loss, or tax credit carryforward is not available under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position. In such a case, the unrecognized tax benefit would be presented in the consolidated balance sheet as a liability. This update was effective for fiscal years beginning after December 15, 2013 and was effective for the Company for the fiscal quarter ended September 30, 2014. The adoption of this standard did not have a significant impact on the Company's Consolidated Financial Statements.

Item 1B. UNRESOLVED STAFF COMMENTS

None.

Item 2. PROPERTIES

Information regarding our principal U.S. properties at June 30, 2015 is set forth below:

Location	Primary Use(s)	Primary Business Segment(s)	Square Footage	Ownership
Saxonburg, PA	Manufacturing, Corporate Headquarters and Research and Development	II-VI Laser Solutions and II-VI Performance Products	252,000	Owned and Leased
Newark, DE	Manufacturing and Research and Development	II-VI Performance Products	90,000	Leased
Temecula, CA	Manufacturing and Research and Development	II-VI Performance Products	87,000	Leased
Dallas, TX	Manufacturing and Research and Development	II-VI Performance Products	68,000	Owned and Leased
New Port Richey and Port Richey, FL	Manufacturing and Research and Development	II-VI Photonics and II-VI Performance Products	67,000	Owned
Monroe, CT	Manufacturing and Research and Development	II-VI Performance Products	48,000	Leased
Tustin, CA	Manufacturing and Research and Development	II-VI Performance Products	37,000	Leased
Santa Rosa, CA	Manufacturing and Research and Development	II-VI Photonics	33,000	Leased
Philadelphia, PA	Manufacturing and Research and Development	II-VI Performance Products	30,000	Leased
Pine Brook, NJ	Manufacturing and Research and Development	II-VI Performance Products	26,000	Leased
Newtown, CT	Manufacturing and Research and Development	II-VI Performance Products	19,000	Leased
Woburn, MA	Manufacturing and Research and Development	II-VI Photonics	17,000	Leased
Horseheads, NY	Research and Development	II-VI Photonics	15,000	Leased
Vista, CA	Manufacturing and Research and Development	II-VI Performance Products	10,000	Leased
Starkville, MS	Manufacturing	II-VI Performance Products	10,000	Leased

Flemington, NJ	Manufacturing and Research and Development	II-VI Photonics	5,000	Leased
San Jose, CA	Research and Development	II-VI Photonics	5,000	Leased
Sunnyvale, CA	Distribution	II-VI Photonics	2,300	Leased

Information regarding our principal foreign properties at June 30, 2015 is set forth below:

Location	Primary Use(s)	Primary Business Segment(s)	Square Footage	Ownership
China	Manufacturing, Research and Development, and Distribution	II-VI Laser Solutions, II-VI Photonics and II-VI Performance Products	1,125,000	Leased
Philippines	Manufacturing	II-VI Performance Products	249,000	Leased
Vietnam	Manufacturing	II-VI Photonics and II-VI Performance Products	207,000	Leased
Switzerland	Manufacturing, Research and Development, and Distribution	II-VI Laser Solutions	134,000	Leased
Germany	Manufacturing and Distribution	II-VI Laser Solutions, II-VI Photonics and II-VI Performance Products	78,000	Owned and Leased
Singapore	Manufacturing	II-VI Laser Solutions	35,000	Leased
Japan	Distribution	II-VI Laser Solutions, II-VI Photonics and II-VI Performance Products	4,000	Leased
Belgium	Distribution	II-VI Laser Solutions	3,000	Leased
Italy	Distribution	II-VI Laser Solutions and II-VI Photonics	2,000	Leased
South Korea	Distribution	II-VI Laser Solutions	2,000	Leased
United Kingdom	Distribution	II-VI Laser Solutions and II-VI Photonics	1,500	Leased

The square footage listed for each of the above properties represents facility square footage, except in the case of the Philippines location, which includes land.

Item 3. LEGAL PROCEEDINGS

The Company and its subsidiaries are involved in various claims and lawsuits incidental to its business. The resolution of each of these matters is subject to various uncertainties, and it is possible that these matters may be resolved unfavorably to the Company. Management believes, after consulting with legal counsel, that the ultimate liabilities, if any, resulting from such legal proceedings will not materially affect the Company’s financial condition, liquidity or results of operation.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

EXECUTIVE OFFICERS OF THE REGISTRANT

The executive officers of the Company and their respective ages and positions are set forth below. Each executive officer listed has been appointed by the Board of Directors to serve until removed or until such person’s successor is appointed and qualified.

Name	Age	Position
Francis J. Kramer	66	Chairman, Chief Executive Officer and Director
Vincent D. Mattera, Jr.	59	President and Chief Operating Officer and Director
Mary Jane Raymond	55	Chief Financial Officer and Treasurer
Giovanni Barbarossa	53	Vice President II-VI Laser Solutions and Chief Technology Officer
David G. Wagner	52	Vice President, Human Resources

Francis J. Kramer has been employed by the Company since 1983, has been its Chairman since 2014, and has been its Chief Executive Officer since July 2007. Mr. Kramer has served as a Director of the Company since 1989. Previously, Mr. Kramer served as the Company’s Chief Operating Officer from 1985 through June 2007. Mr. Kramer joined the Company as Vice President and General Manager of Manufacturing and was named Executive Vice President and General Manager of Manufacturing in 1984. Prior to his employment by the Company, Mr. Kramer was the Director of Operations for the Utility Communications Systems Group of Rockwell International Corp. Mr. Kramer graduated from the University of Pittsburgh with a B.S. degree in Industrial Engineering and from Purdue University with a M.S. degree in Industrial Administration. Mr. Kramer has served as Director of Barnes Group Inc., a publicly traded aerospace and industrial manufacturing company (NYSE: B), since 2012.

Vincent D. Mattera, Jr. has been employed by the Company since 2004 and has been its President and Chief Operating Officer since 2013. Dr. Mattera has served as a Director of the Company since 2012. Previously, Dr. Mattera served as Executive Vice President from 2010 to 2013 and was Vice President of the Advanced Products Group from 2004 to 2010. Dr. Mattera served as Vice President, Undersea Optical Transport, Agere Systems (formerly Lucent Technologies, Microelectronics and Communications Technologies Group) from 2001 to 2004. Previously, Dr. Mattera served as Optoelectronic Device Manufacturing and Process Development Vice President with Lucent Technologies, Microelectronics and Communications Technologies Group from 2000 until 2001. He was Director of Optoelectronic Device Manufacturing and Development at Lucent Technologies, Microelectronics Group from 1997 to 2000. From 1995 to 1997 he served as Director, Indium Phosphide Semiconductor Laser Chip Design and Process Development with Lucent Technologies, Microelectronics Group. From 1984 to 1995 he held management positions with AT&T Bell Laboratories. Dr. Mattera holds B.S. and Ph.D. degrees in Chemistry from the University of Rhode Island and Brown University, respectively.

Mary Jane Raymond has been employed by the Company as its Chief Financial Officer and Treasurer since March 2014. Previously, Ms. Raymond was the Chief Financial Officer of Hudson Global, Inc. from 2005 to 2013. Ms. Raymond was the Chief Risk Officer and Vice President and Corporate Controller at Dun and Bradstreet, Inc. from 2002 to 2005. Additionally, she was the Vice President, Merger Integration at Lucent Technologies, Inc. from 1997 to 2002 and held several management positions at Cummins Engine Company from 1988 to 1997. Ms. Raymond holds a B.A. degree in Public Management from St. Joseph’s University, and an MBA from Stanford University.

Giovanni Barbarossa has been employed by the Company since 2012 and has been Vice President, II-VI Laser Solutions segment since 2014 and Chief Technology Officer since 2012. Dr. Barbarossa was employed at Avanex Corporation from 2000-2009, serving in various executive positions in product development and general management, ultimately becoming its Chief Executive Officer. When Avanex merged with Bookham Technology plc, forming Oclaro Inc., Dr. Barbarossa became a member of the Board of Directors of Oclaro and served as such from 2009 to 2011. Dr. Barbarossa graduated from the University of Bari, Italy with a B.S. in Electrical Engineering and a Ph.D. in Photonics from the University of Glasgow, U.K.

David G. Wagner has been employed by the Company since 2008 and has been the Vice President, Human Resources since 2011 Prior to his employment with the Company, Mr. Wagner was employed with Owens Corning (NYSE: OC) from 1985-2008, serving in various human resource management positions, ultimately becoming the Vice President, Human Resources for Owens Corning’s global sales forces. Mr. Wagner graduated with a B.S. degree in Human Resources Management from Juniata College in 1985.

PART II

Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Company's Common Stock is traded on the NASDAQ Global Select Market ("NASDAQ") under the symbol "IIVI." The following table sets forth the range of high and low closing sale prices per share of the Company's Common Stock for the fiscal periods indicated, as reported by NASDAQ.

	High	Low
Fiscal 2015		
First Quarter	$14.71	$11.77
Second Quarter	$14.44	$10.95
Third Quarter	$18.70	$12.67
Fourth Quarter	$19.53	$17.68

	High	Low
Fiscal 2014		
First Quarter	$20.76	$16.51
Second Quarter	$19.16	$15.25
Third Quarter	$17.47	$14.72
Fourth Quarter	$15.62	$12.79

On August 20, 2015, the last reported sale price for the Company's Common Stock was $17.82 per share. As of such date, there were approximately 785 holders of record of our Common Stock. The Company historically has not paid cash dividends and does not presently anticipate paying cash dividends in the future.

ISSUER PURCHASES OF EQUITY SECURITIES

In August 2014, the Board of Directors authorized the Company to purchase up to $50.0 million of its Common Stock. The repurchase program calls for shares to be purchased in the open market or in private transactions from time to time. Shares purchased by the Company are retained as treasury stock and available for general corporate purposes. During the fiscal year ended June 30, 2015 the Company purchased 936,049 shares of its Common Stock pursuant to the repurchase program for approximately $12.7 million.

The following table provides information with respect to purchases of the Company's equity securities during the quarter ended June 30, 2015.

	Total Number of Shares Purchased as Part of Publicly	Dollar Value of Shares That May Yet be Purchased

Period	Total Number of Shares Purchased		Average Price Paid Per Share	Announced Plans or Programs (a)	Under the Plan or Program
April 1, 2015 to April 30, 2015	-		$ -	-	$37,255,646
May 1, 2015 to May 31, 2015	432	(a)	$ 18.66	-	$37,255,646
June 1, 2015 to June 30, 2015	-		$ -	-	$37,255,646

(a) Includes 432 shares of our Common Stock transferred to the Company from employees in satisfaction of minimum tax withholding obligations associated with the vesting of restricted share awards.

The information incorporated by reference in Item 12 of this Annual Report on Form 10-K from our 2015 Proxy Statement under the heading “Equity Compensation Plan Information” is hereby also incorporated by reference into this Item 5.

PERFORMANCE GRAPH

The following graph compares cumulative total shareholder return on the Company’s Common Stock with the cumulative total shareholder return of the Nasdaq Composite Index and with a peer group of companies constructed by the Company for the period from June 30, 2010, through June 30, 2015. The Company’s peer group includes Cabot Microelectronics Corporation, Franklin Electric Co., Inc., MKS Instruments, Inc., Rofin-Sinar Technologies, Inc. and Silicon Laboratories.

Item 6. SELECTED FINANCIAL DATA
Five-Year Financial Summary

The following selected financial data for the five fiscal years presented are derived from II-VI's audited Consolidated Financial Statements as adjusted to reflect the Company's II-VI Performance Metals tellurium product line as a discontinued operation. All periods presented have been adjusted to present this product line on a discontinued operations basis. The data should be read in conjunction with the Consolidated Financial Statements and the related notes thereto included elsewhere in this Annual Report on Form 10-K.

Year Ended June 30, ($000 except per share data)	2015	2014	2013	2012	2011
Statement of Earnings					
Net revenues from continuing operations	$741,961	$683,261	$551,075	$516,403	$486,638
Earnings from continuing operations	65,975	38,316	58,720	70,718	79,676
Earnings (loss) from discontinued operations	-	133	(6,789)	(9,443)	3,342
Net earnings attributable to redeemable noncontrolling interest	-				

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Operational Goals	Description	Why It Is Important
Customer Satisfaction	Customer satisfaction surveys evaluate performance. The survey results provide an overall ranking for each traditional operating company, as well as a ranking for each customer segment: residential, commercial, and industrial.	Customer satisfaction is key to operations. Performance of all operational goals affects customer satisfaction.
Reliability	Transmission and distribution system reliability performance is measured by the frequency and duration of outages. Performance targets for reliability are set internally based on recent historical performance.	Reliably delivering power to customers is essential to operations.
Availability	Peak season equivalent forced outage rate is an indicator of availability and efficient generation fleet operations during the months when generation needs are greatest. Availability is measured as a percentage of the hours of forced outages out of the total generation hours.	Availability of sufficient power during peak season fulfills the obligation to serve and provide customers with the least cost generating resources.
Nuclear Plant Operations	Nuclear plant performance is evaluated by measuring nuclear safety as rated by independent industry evaluators, as well as by a quantitative score comprised of various plant performance indicators. Plant reliability and operational availability are measured as a percentage of time the nuclear plant is operating. The reliability and availability metrics take generation reductions associated with planned outages into consideration.	Safe and efficient operation of the nuclear fleet is important for delivering clean energy at a reasonable price.
Major Projects Plant Vogtle Units 3 and 4 and Kemper IGCC	The Southern Company system is committed to the safe, compliant, and high-quality construction and licensing of two new nuclear generating units under construction at Georgia Power s Plant Vogtle (Plant Vogtle Units 3 and 4) and the Kemper IGCC, as well as excellence in transition to operations and prudent decision-making related to these two major projects. An executive review committee is in place for each project to assess progress. A combination of subjective and objective measures is considered in assessing the degree of achievement. Final assessments for each project are approved by either the Company s Chief Executive Officer or the Company s Chief Operating Officer and confirmed by the Nuclear/Operations Committee.	Strategic projects enable the Southern Company system to expand capacity to provide clean, affordable energy to customers across the region.
Safety	The Company s Target Zero program is focused on continuous improvement in having a safe work environment. The performance is measured by the applicable company s ranking, as compared to peer utilities in the Southeastern Electric Exchange.	Essential for the protection of employees, customers, and communities.
Culture	The culture goal seeks to improve the Company s inclusive workplace. This goal includes measures for work environment (employee satisfaction survey), representation of minorities and females in leadership roles (subjectively assessed), and supplier diversity.	Supports workforce development efforts and helps to assure diversity of suppliers.

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The ranges of performance levels established for the primary operational goals are detailed below, along with actual corporate results for 2014 performance.

Level of Performance	Customer Satisfaction	Reliability	Availability	Nuclear Plant Operations	Safety	Plant Vogtle Units 3 and 4 and Kemper IGCC	Culture
Maximum	Top quartile for all customer segments and overall	Significantly exceed targets	Industry best	Significantly exceed targets	Greater than 90th percentile or 5-year Company best	Significantly exceed targets	Significant improvement
Target	Top quartile overall	Meet targets	Top quartile	Meet targets	60th percentile	Meet targets	Improvement
Threshold	2nd quartile overall	Significantly below targets	2nd quartile	Significantly below targets	40th percentile	Significantly below targets	Significantly below expectations
Corporate Achievement	200%	195%	190%	150%	167%	Plant Vogtle: 175% Kemper IGCC: 75%	150%

The Compensation Committee approves specific objective performance schedules to calculate performance between the threshold, target, and maximum levels for each of the operational goals. If goal achievement is below threshold, there is no payout associated with the applicable goal.

Actual 2014 operational goal achievement is shown in the following tables.

Corporate (Ms. Greene and Messrs. Fanning and Beattie)

Company Corporate/Aggregate Goal	Achievement Percentage

Customer Satisfaction		200
Reliability		195
Availability		190
Safety		167
Culture		150
Major Projects	Plant Vogtle Units 3 and 4 Assessment	175
Major Projects	Kemper IGCC Assessment	75
Total Operational Goal Performance Factor		172

Alabama Power (Mr. McCrary)

Goal	**Achievement Percentage**
Customer Satisfaction	200
Reliability	177
Availability	200
Safety	165
Culture	130
Total Operational Goal Performance Factor	176

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Georgia Power (Mr. Bowers)

Goal		Achievement Percentage
Customer Satisfaction		200
Reliability		172
Availability		200
Safety		80
Major Projects	Plant Vogtle Units 3 and 4 Assessment	175
Culture		137
Total Operational Goal Performance Factor		162

Southern Nuclear (Mr. Kuczynski)

Goal		Achievement Percentage
Nuclear Safety		0
Plant Operations		150
Major Projects	Plant Vogtle Units 3 and 4 Assessment	175
Culture		131
Total Operational Goal Performance Factor		123

Calculating Payouts

Each named executive officer had a target Performance Pay Program opportunity, based on his or her position, set by the Compensation Committee at the beginning of 2014. Targets are set as a percentage of base salary.

All of the named executive officers are paid based on EPS performance. The business unit goals that determine payout levels vary based on the named executive officer s leadership role. For Ms. Greene and Messrs. Fanning and Beattie, payout is based on the equity-weighted average net income payout results for the traditional operating companies and Southern Power and the system-wide operational goal results. For Messrs. Bowers and McCrary, payout is based on achievement of the net income and operational goals of Georgia Power and Alabama Power,

respectively. Mr. McCrary s payout is prorated based on the amount of time he was employed at Alabama Power during 2014. Mr. Kuczynski s payout is based on the achievement percentages of the net income goals of Alabama Power (50%) and Georgia Power (50%) and the Southern Nuclear operational goal results.

A total performance factor is determined by adding the EPS and applicable business unit financial and operational goal performance results and dividing by three. The total performance factor is multiplied by the target Performance Pay Program opportunity to determine the payout for each named executive officer. The table below shows the calculation of the total performance factor for each of the named executive officers, based on results shown above.

	Southern Company EPS Result (%) 1/3 weight (1)	Business Unit Financial Goal Result (%) 1/3 weight (1)	Business Unit Operational Goal Result (%) 1/3 weight	Total Performance Factor (%)
T. A. Fanning	176	163	172	170
A. P. Beattie	176	163	172	170
W. P. Bowers	176	166	162	168
K. S. Greene	176	163	172	170
S. E. Kuczynski	176	171	123	157

C. D. McCrary	176	176	176	176

(1) Excluding impact of the 2014 Kemper IGCC Charges and Adjustments.

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The table below shows the pay opportunity at target-level performance and the actual payout based on the actual performance shown above.

	Target Annual Performance Pay Program Opportunity (%)	Target Annual Performance Pay Program Opportunity ($)	Total Performance Factor (%) (1)	Actual Annual Performance Pay Program Payout ($) (2)
T. A. Fanning	120	1,440,000	170	1,713,600
A. P. Beattie	75	505,123	170	772,839
W. P. Bowers	75	590,503	168	892,841
K. S. Greene	70	455,000	170	580,125
S. E. Kuczynski	70	467,875	157	734,564
C. D. McCrary (3)	75	602,435	176	333,990

(1) Shown as modified and described above.

(2) As described above, the Compensation Committee reduced the final payouts for Ms. Greene (25%) and Messrs. Fanning (30%), Beattie (10%), and Bowers (10%) after the adjustments to performance results in connection with the 2014 Kemper IGCC Charges and Adjustments.

(3) Mr. McCrary retired from Alabama Power effective May 1, 2014; therefore, his Performance Pay Program payout was prorated based on the amount of time he was employed in 2014. The target amount shown is his full target opportunity as if he had been employed for the entire year. The actual amount shown is the prorated amount Mr. McCrary received.

Long-Term Performance-Based Compensation

2014 Long-Term Pay Program Highlights

¡ StockOptions:

¡ Rewardlong-term Common Stock price appreciation

¡ Represent40% of long-term target value

¡ Vestover three years

¡ Ten-yearterm

¡ PerformanceShares:

¡ Rewardtotal shareholder return relative to industry peers and stock price appreciation

¡ Represent60% of long-term target value

¡ Three-yearperformance period

¡ Performanceresults can range from 0% to 200% of target

¡ Paidin Common Stock at end of performance period

¡ RestrictedStock Units

¡ Usedto promote retention of key employees or to attract key employees by replacing award values forfeited upon leaving a former employer

¡ Continuedemployment until vesting date(s) is required

¡ Paidin Common Stock upon vesting

¡ PerformanceSummary:

¡ Stockoptions: for options granted in 2014, year-end stock price exceeded option exercise price by nearly 19%

¡ Performanceshares: paid out at 14% of target

¡ Restrictedstock units: one new grant in 2014 to Mr. Kuczynski

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Long-term performance-based awards are intended to promote long-term success and increase stockholder value by directly tying a substantial portion of the named executive officers total compensation to the interests of stockholders. Long-term performance-based awards also benefit the Southern Company system s customers by providing competitive compensation that allows the Southern Company system to attract, retain, and engage employees who provide focus on serving customers and delivering safe and reliable electric service.

Stock options represent 40% of the long-term performance target value, and performance

shares represent the remaining 60%. The Compensation Committee elected this mix because it concluded that doing so represented an appropriate balance between incentives. Stock options only generate value if the price of the stock appreciates after the grant date, and performance shares reward employees based on Southern Company s total shareholder return relative to industry peers, as well as Common Stock price. The Compensation Committee also awards restricted stock units occasionally, typically as retention awards or to attract key employees by replacing the value of awards that are forfeited upon leaving a former employer.

The following table shows the grant date fair value of the long-term performance-based awards granted in 2014, except restricted stock units.

	Value of Options ($)	Value of Performance Shares ($)	Total Long-Term Value ($)
T. A. Fanning	2,255,999	3,383,968	5,639,967
A. P. Beattie	619,617	929,415	1,549,032
W. P. Bowers	724,350	1,086,520	1,810,870
K. S. Greene	467,999	701,998	1,169,997
S. E. Kuczynski	454,507	681,726	1,136,233
C. D. McCrary	722,920	1,084,380	1,807,300

Stock Options

Stock options granted have a 10-year term, vest over a three-year period, fully vest upon retirement or termination of employment following a change in control, and expire at the earlier of five years from the date of retirement or the end of the 10-year term. For the grants made in 2014, unvested options are forfeited if the named executive officer retires from the Southern Company system and accepts a position with a peer company within two years of retirement. The grants made to Mr. McCrary in 2014 vested upon his retirement; however, he will forfeit those options that vested upon retirement if he accepts a position with a peer company within two years of his retirement. The value of each stock option was derived using the Black-Scholes stock option pricing model. The assumptions used in calculating that amount are

discussed in Note 8 to the Financial Statements. For 2014, the Black-Scholes value on the grant date was $2.20 per stock option, and the exercise price is $41.28.

Performance Shares

2014-2016 Grant

Performance shares are denominated in units, meaning no actual shares are issued on the grant date. A grant date fair value per unit was determined. For the grant made in 2014, the value per unit was $37.54. See the Summary Compensation Table and the information accompanying it for more information on the grant date fair value. The total target value for performance share units is divided by the value per unit to determine the number of

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performance share units granted to each participant, including the named executive officers. Each performance share unit represents one share of Common Stock.

At the end of the three-year performance period (January 1, 2014 through December 31, 2016), the number of units will be adjusted up or down (0% to 200%) based on the Company s total shareholder return relative to that of its peers in a custom peer group. While in previous years the Company s total shareholder return was measured relative to two peer groups (a custom peer group and the Philadelphia Utility Index), the Compensation Committee decided to streamline the performance share peer group for the 2014 grant by eliminating the Philadelphia Utility Index and establishing one custom peer group. The companies in the custom peer group

are those that are believed to be most similar to the Company in both business model and investors, creating a peer group that is even more aligned with the Company s strategy. For performance shares granted in previous years using the dual peer group structure, the final result will be measured using both peer groups as approved by the Compensation Committee at the time of the grant. The custom peer group varies from the Market Data peer group discussed previously due to the timing and criteria of the peer selection process; however, there is significant overlap. The number of performance share units earned will be paid in Common Stock at the end of the three-year performance period. No dividends or dividend equivalents will be paid or earned on the performance share units.

The companies in the custom peer group on the grant date are listed in the following table.

Alliant Energy Corporation	Integrys Energy Group
Ameren Corporation	Pepco Holdings, Inc.
American Electric Power Company, Inc.	PG&E Corporation
CMS Energy Corporation	Pinnacle West Capital Corporation
Consolidated Edison, Inc.	PPL Corporation
DTE Energy Company	SCANA Corporation
Duke Energy Corporation	Wisconsin Energy Corporation

Edison International	Xcel Energy Inc.
Eversource Energy	

The scale below will determine the number of units paid in Common Stock following the last year of the performance period, based on the 2014 through 2016 performance period. Payout for performance between points will be interpolated on a straight-line basis.

Performance vs. Peer Group	Payout (% of Each Performance Share Unit Paid)
90th percentile or higher (Maximum)	200
50th percentile (Target)	100
10th percentile (Threshold)	0

Performance shares are not earned until the end of the three-year performance period. A participant who terminates, other than due to retirement or death, forfeits all unearned performance shares. Participants who retire or

die during the performance period only earn a prorated number of units, based on the number of months they were employed during the performance period.

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2012-2014 Payouts

Performance share grants were made in 2012 with a three-year performance period that ended on December 31, 2014. Based on the Company s total shareholder return achievement relative to that of the Philadelphia Utility Index (28% payout) and the custom peer group (0% payout) as shown in the chart below, the payout percentage was 14% of target, which is the average of the two peer groups.

The following table shows the target and actual awards of performance shares for the named executive officers. Actual payouts were significantly below the target grant value due to lower relative total shareholder return.

	Target Performance Shares (#)	Target Value of Performance Shares ($)	Performance Shares Earned (#)	Value of Performance Shares Earned ($)
T. A. Fanning	72,338	3,037,473	10,127	497,337
A. P. Beattie	18,417	773,330	2,578	126,606
W. P. Bowers	23,906	1,003,813	3,347	164,371
K. S. Greene (1)	0	0	0	0
S. E. Kuczynski	14,717	617,967	2,060	101,167
C. D. McCrary (2)	25,121	1,054,831	2,735	134,316

(1) Ms. Greene was not employed by the Southern Company system when the Compensation Committee granted performance shares in 2012.

(2) The number of performance shares earned by Mr. McCrary is prorated based on the time he was employed by Alabama Power during the performance period.

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Restricted Stock Units

In limited situations, restricted stock units are granted to address specific needs, including retention. These awards serve two primary purposes. They further align the recipient s interests with those of the Company s stockholders, and they provide strong retention value. For information on treatment upon termination or change in control, see Potential Payments Upon Termination or Change-in-Control.

In October 2014, the Compensation Committee granted Mr. Kuczynski restricted stock units valued at $1,000,016 on the grant date that will vest in October 2017 if he remains employed with the Southern Company system through the vesting date. The Compensation Committee believes that, given Mr. Kuczynski s expertise and the competitiveness of the nuclear labor market, there is a retention risk and, therefore, providing a retention award was in the best interest of the Company. The Compensation Committee sought advice from Pay Governance in determining market practice and the appropriate value of the award.

Restricted stock units were granted to Ms. Greene in 2013 and will vest incrementally each year starting April 1, 2015 and ending April 1, 2018 if she remains employed with the Southern Company system.

Restricted stock units were granted to Mr. McCrary in 2012 with a vesting date of December 31, 2014 in order to retain Mr. McCrary until his successor was named and expiration of an appropriate transition period. Mr. McCrary s successor was announced in February 2014, and Mr. McCrary retired effective May 1, 2014. The Compensation Committee modified the vesting date to April 30, 2014.

See the Summary Compensation Table, the Grants of Plan-Based Awards table, the Outstanding Equity Awards at 2014 Fiscal Year End table, and accompanying information for more information on restricted stock unit awards.

Timing of Performance-Based Compensation

As discussed above, the 2014 annual Performance Pay Program goals and the total shareholder return goals applicable to performance shares were established early in the year by the Compensation Committee. Annual stock option grants also were made by the Compensation Committee. The establishment of performance-based compensation goals and the granting of equity awards were not timed with the release of material, non-public information. This procedure is consistent with prior practices. Stock option grants are made to new hires or newly-eligible participants on preset, regular quarterly dates that were approved by the Compensation Committee. The exercise price of options granted to employees in 2014 was the closing price of the Common Stock on the grant date or the last trading day before the grant date, if the grant date was not a trading day.

Retirement and Severance Benefits

Certain post-employment compensation is provided to employees, including the named executive officers, consistent with the Company s goal of providing market-based compensation and benefits.

Retirement Benefits

Generally, all full-time employees of the Southern Company system participate in the funded Pension Plan after completing one year of service. Normal retirement benefits become payable when participants attain age 65 and complete five years of participation. The Company also provides unfunded benefits that count salary and annual Performance Pay Program payouts that are ineligible to be counted under the Pension Plan. See the Pension Benefits table and accompanying information for more pension-related benefits information.

The Company also provides the Deferred Compensation Plan, which is an unfunded plan that permits participants to defer income as well as certain federal, state, and local taxes until a specified date or their retirement, disability, death, or other separation from service. Up to 50% of base salary and up to 100% of performance-based non-equity compensation may be deferred at the election of eligible employees. All of the named executive officers are eligible to participate in the Deferred Compensation Plan. See the Nonqualified Deferred Compensation table and accompanying information for more information about the Deferred Compensation Plan.

Change-in-Control Protections

Change-in-control protections, including severance pay and, in some situations, vesting or payment of long-term performance-based awards, are provided upon a change in control of the Company coupled with an involuntary termination not for cause or a voluntary termination for Good Reason. This means there is a double trigger before severance benefits are paid; *i.e.,* there must be both a change in control and a termination of employment. Severance payment amounts are two times salary plus target Performance Pay Program opportunity for the named executive officers,

except for Mr. Fanning whose severance payment amount is three times salary plus Performance Pay Program target opportunity. No excise tax gross-up would be provided. Change-in-control protections allow executive officers to focus on potential transactions that are in the best interest of shareholders. More information about severance arrangements is included under Potential Payments upon Termination or Change-in-Control.

Perquisites

The Company provides limited ongoing perquisites to its executive officers, including the named executive officers, consistent with the Company s goal of providing market-based compensation and benefits. The perquisites provided in 2014, including amounts, are described in detail in the information accompanying the Summary Compensation Table. No tax assistance is provided on perquisites, except on certain relocation-related benefits.

PERFORMANCE-BASED COMPENSATION PROGRAM CHANGES FOR 2015

In early 2015, the Compensation Committee made several changes to the Company s performance-based compensation programs, impacting 2015 compensation. These changes affect both the annual Performance Pay Program as well as the long-term performance-based compensation program and are described below.

Annual Performance-Based Pay Program

Beginning in 2015, the annual performance-based pay program will incorporate individual goals for all executive officers of the Company. Currently, the goals are equally weighted between the EPS goal, the applicable business

unit net income goal, and the applicable business unit operational goals. Starting with the 2015 annual Performance Pay Program goals, the Compensation Committee eliminated the business unit net income goal for the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), added an individual goal component, and changed the weights for the EPS goal and operational goals. All other executive officers will now have four goals: EPS, business unit net income, business unit operational goals, and their individual goals. The table below outlines the new weights for each goal.

	EPS	Net Income	Operational	Individual
CEO and CFO	40%	0%	30%	30%
All other executive officers	30%	30%	30%	10%

Long-Term Performance-Based Compensation

Since 2010, the Company s long-term performance-based compensation program has

included two components: stock options and performance shares. After reviewing current market practices with Pay Governance, the Compensation Committee decided to modify the Company s long-term performance-based

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compensation program to further align the Company s compensation program with its peers in the utility industry and create better alignment of pay with long-term Company performance. Beginning with long-term performance-based equity grants made in early 2015, the long-term performance-based program consists exclusively of performance shares. The new structure maintains the three-year performance cycle described earlier in this CD&A for performance shares but expands the performance metrics from one (relative total shareholder return) to three metrics. The new program now includes relative total shareholder return (50%), cumulative EPS from ongoing operations over a three-year period (25%), and equity-weighted return on equity (ROE) (25%). Under the new program, dividends will accrue on performance shares throughout the performance period, and eligible new hires and newly promoted employees will receive interim prorated grants of performance shares instead of stock options.

The continued use of relative total shareholder return as a metric in the long-term performance program maintains consistency with the previous program as well as allows the Company to measure its performance against a custom group of regulated peers. The new EPS goal measures cumulative EPS from ongoing operations over a three-year period and motivates ongoing earnings growth to support the Company s dividend and achievement of

strategic financial objectives. The new equity-weighted ROE goal measures traditional operating company performance from ongoing operations over a three-year period and is set to encourage top quartile ROE performance. Both the EPS and ROE goals are subject to a gateway goal focused on the Company s credit ratings. If the Company fails to meet the credit rating requirements established by the Compensation Committee, there will be no payout associated with the EPS and ROE goals.

Executive Stock Ownership Requirements

Officers of the Company and its subsidiaries that are in a position of Vice President or above are subject to stock ownership requirements. All of the named executive officers are covered by the requirements. Ownership requirements further align the interest of officers and stockholders by promoting a long-term focus and long-term share ownership.

The types of ownership arrangements counted toward the requirements are shares owned outright, those held in Company-sponsored plans, and Common Stock accounts in the Deferred Compensation Plan and the Supplemental Benefit Plan. One-third of vested stock options may be counted, but, if so, the ownership requirement is doubled. The ownership requirement is reduced by one-half at age 60. Mr. Beattie is 60.

The requirements are expressed as a multiple of base salary as shown below.

	Multiple of Salary without Counting Stock Options	**Multiple of Salary Counting 1/3 of Vested Options**
T. A. Fanning	5 Times	10 Times

A. P. Beattie	1.5 Times	3 Times
W. P. Bowers	3 Times	6 Times
K. S. Greene	3 Times	6 Times
S. E. Kuczynski	3 Times	6 Times

Newly-elected officers have approximately five years from the date of their election to meet the applicable ownership requirement. Newly-promoted officers have approximately five years from the date of their promotion to meet the increased ownership requirement. All of the named executive officers are meeting their respective ownership requirements. Mr. McCrary retired and is therefore no longer subject to stock ownership requirements.

IMPACT OF ACCOUNTING AND TAX TREATMENTS ON COMPENSATION

Section 162(m) of the Internal Revenue Code of 1986, as amended (Code), limits the tax deductibility of the compensation of the named executive officers, except Messrs. Beattie and McCrary, that exceeds $1 million per year unless the compensation is paid under a performance-based plan as defined in the Code that has been approved by stockholders. The Company has obtained stockholder approval of the Omnibus Incentive Compensation Plan, under which most of the performance-based compensation is paid. Because the Company s policy is to maximize long-term stockholder value, as described fully in this CD&A, tax deductibility is not the only factor considered in setting compensation. The Compensation Committee has the discretion to award compensation that may not be tax deductible.

The Compensation Committee approved a formula in February 2014 that represented a maximum annual performance-based compensation amount payable to the affected named executive officers. For 2014 performance, the Compensation Committee used negative discretion from the approved formula amount to

determine the actual payouts for the affected named executive officers under the annual performance-based compensation program pursuant to the methodologies described above.

POLICY ON RECOVERY OF AWARDS

The Company s Omnibus Incentive Compensation Plan provides that, if the Company is required to prepare an accounting restatement due to material noncompliance as a result of misconduct, and if an executive officer of the Company knowingly or grossly negligently engaged in or failed to prevent the misconduct or is subject to automatic forfeiture under the Sarbanes-Oxley Act of 2002, the executive officer must repay the Company the amount of any payment in settlement of awards earned or accrued during the 12-month period following the first public issuance or filing that was restated.

POLICY REGARDING HEDGING THE ECONOMIC RISK OF STOCK OWNERSHIP

The Company s policy is that employees and outside Directors will not trade Company options on the options market and will not engage in short sales.

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REALIZABLE PERFORMANCE-BASED COMPENSATION ANALYSIS

The SEC has promulgated rules regarding how total compensation is calculated in the Summary Compensation Table. These rules include accounting assumptions that affect the value reported for equity grants. However, as the Company s performance changes over time, the Common Stock price can fluctuate, affecting the value of equity grants made to the named executive officers. The Compensation Committee believes it is important to look at those changes to fully understand the value of the compensation received because the reported value is only realized if the Company meets certain performance criteria. In order to supplement the SEC-required disclosure, the chart below compares the target or grant date value of performance-based compensation granted to Mr. Fanning in 2012, 2013, and 2014 with the value actually received or as measured on December 31, 2014.

The realizable amount shown for short-term performance pay includes the actual amount paid to Mr. Fanning for 2012, 2013, and 2014 under the Performance Pay Program.

The realizable amount shown for stock options includes the intrinsic value of all stock options granted to Mr. Fanning in 2012, 2013, and 2014 calculated using the Common Stock closing price on December 31, 2014. This amount is subject to change based on changes in the Common Stock price.

The realizable amount shown for performance shares includes the value Mr. Fanning received based on the payout of the performance shares granted in 2012 for the 2012 through 2014 performance period as well as the projected amounts based on performance levels relative to peers as of December 31, 2014 for the 2013 and 2014 grants. This amount is subject to change based on the Company s performance relative to its peers at the end of the applicable three-year performance period. See Performance Shares in this CD&A for a description of the Company s performance share peer group.

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COMPENSATION AND MANAGEMENT SUCCESSION COMMITTEE REPORT

The Compensation Committee met with management to review and discuss the CD&A. Based on such review and discussion, the Compensation Committee recommended to the Board of Directors that the CD&A be included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2014 and in this Proxy Statement. The Board of Directors approved that recommendation.

Members of the Compensation Committee:

Henry A. Clark III, Chair

David J. Grain

Veronica M. Hagen

William G. Smith, Jr.

Steven R. Specker

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SUMMARY COMPENSATION TABLE

The Summary Compensation Table shows the amount and type of compensation received or earned in 2012, 2013, and 2014 by the named executive officers, except as noted below.

Name and Principal Position (a)	Year (b)	Salary ($) (c)	Bonus ($) (d)	Stock Awards ($) (e)	Option Awards ($) (f)	Non-Equity Incentive Plan Compensation ($) (g)	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($) (h)	All Other Compensation ($) (i)	Total ($) (j)
Thomas A. Fanning	2014	1,192,067		3,383,968	2,255,999	1,713,600	2,899,537	70,822	11,515,993
	2013	1,152,389		3,128,625	2,085,747	1,199,307	805,738	66,485	8,438,291
Chairman, President, and Chief Executive Officer	2012	1,114,846		3,037,473	2,025,000	2,078,158	4,712,413	67,458	13,035,348
Art P. Beattie	2014	668,516		929,415	619,617	772,839	1,396,842	37,293	4,424,522
	2013	644,039		796,514	531,025	437,126	402,101	122,037	2,932,842
Executive Vice President and Chief Financial Officer	2012	615,378		773,330	515,558	737,382	2,747,374	34,352	5,423,374

W. Paul Bowers	2014	782,928	45	1,086,520	724,350	892,841	1,504,316	46,986	5,037,986
	2013	760,482		1,031,940	687,964	498,775		44,375	3,023,536
Chairman, President, and Chief Executive Officer, Georgia Power	2012	739,587	42	1,003,813	669,227	1,013,366	2,024,578	50,830	5,501,443
Kimberly S. Greene	2014	650,000		701,998	467,999	580,125	326,334	605,315	3,331,771
Executive Vice President and Chief Operating Officer	2013	475,000		2,000,005	1,039,997	310,811	212,666	656,035	4,694,514
Stephen E. Kuczynski	2014	667,120		1,681,742	454,507	734,564	217,633	39,117	3,794,683
	2013	658,378		635,283	423,534	426,183	126,714	42,692	2,312,784
President and Chief Executive Officer, Southern Nuclear	2012	640,289		617,967	411,997	619,288	77,727	101,886	2,469,154
	2014	389,266		2,896,902	722,920	333,990	923,064	96,937	5,363,079
	2013	799,124		1,084,347	722,922	650,630	414,103	45,396	3,716,522
Charles D. McCrary Former Chairman, President, and Chief Executive Officer, Alabama Power	2012	777,167		3,054,840	703,232	1,028,204	2,437,448	44,722	8,045,613

Column (a)

Ms. Greene was not an executive officer of the Company prior to 2013.

Column (d)

This amount shown for Mr. Bowers reflects the value of a non-cash safety award for Mr. Bowers. All employees of Georgia Power with a perfect individual safety record in 2014 received the award.

Column (e)

This column does not reflect the value of stock awards that were actually earned or received in

2014. Rather, as required by applicable rules of the SEC, this column reports the aggregate grant date fair value of performance shares granted in 2014. The value reported is based on the probable outcome of the performance conditions as of the grant date, using a Monte Carlo simulation model. No amounts will be earned until the end of the three-year performance period on December 31, 2016. The value then can be earned based on performance ranging from 0 to 200%, as established by the Compensation Committee. The aggregate grant date fair value of the performance shares granted in 2014 to Ms. Greene and Messrs. Fanning, Beattie, Bowers, and Kuczynski, assuming that the highest level of performance is achieved, is $1,403,996, $6,767,936, $1,858,830, $2,173,040, and $1,363,453, respectively (200% of the amount shown in the table). Because Mr. McCrary retired from Alabama Power effective May 1, 2014, the maximum amount he could earn is $241,007, which is prorated based on the number of months he was employed during the performance period. The amount reflected in column (e) for Mr. McCrary also includes the incremental fair value related to the modification of the vesting date of the restricted stock units granted to Mr. McCrary in 2012 and discussed in the CD&A. See Note 8 to the Financial Statements for a discussion of the assumptions used in calculating these amounts.

Column (f)

This column reports the aggregate grant date fair value of stock options granted in the applicable year. See Note 8 to the Financial Statements for a discussion of the assumptions used in calculating these amounts.

Column (g)

The amounts in this column are the payouts under the annual Performance Pay Program. The amount reported for the Performance Pay Program is for the one-year performance period that ended on December 31, 2014. The Performance Pay Program is described in detail in the CD&A.

Column (h)

This column reports the aggregate change in the actuarial present value of each named executive officer s accumulated benefit under the Pension Plan and the supplemental pension plans (collectively, Pension Benefits) as of December 31, 2012, 2013, and 2014. Because Mr. McCrary retired in 2014, the amount reported for him in 2014 reflects the actual benefits expected to be paid after the measurement date. The Pension Benefits as of each measurement date are based on the named executive officer s age, pay, and service accruals and the plan provisions applicable as of the measurement date. The actuarial present values as of each measurement date reflect the

assumptions the Company selected for cost purposes as of that measurement date; however, the named executive officers were assumed to remain employed at the Company or any Company subsidiary until their benefits commence at the pension plans stated normal retirement date, generally age 65. As a result, the amounts in column (h) related to Pension Benefits represent the combined impact of several factors: growth in the named executive officer s Pension Benefits over the measurement year; impact on the total present values of one year shorter discounting period due to the named executive officer being one year closer to normal retirement; impact on the total present values attributable to changes in assumptions from measurement date to measurement date; and impact on the total present values attributable to plan changes between measurement dates. In general, pension values increased for all named executive officers due to a decrease in discount rates and updated mortality rates.

For more information about the Pension Benefits and the assumptions used to calculate the actuarial present value of accumulated benefits as of December 31, 2014, see the information following the Pension Benefits table. The key differences between assumptions used for the actuarial present values of accumulated benefits calculations as of December 31, 2013 and December 31, 2014 are:

- Discount rate for the Pension Plan was decreased to 4.20% as of December 31, 2014 from 5.05% as of December 31, 2013;

- Discount rate for the supplemental pension plans was decreased to 3.75% as of December 31, 2014 from 4.50% as of December 31, 2013; and

- Mortality rates for all plans were updated due to the release of new mortality tables.

This column also reports above-market earnings on deferred compensation under the Deferred Compensation Plan (DCP). However, there were no above-market earnings on deferred compensation in the years reported.

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Column (i)

This column reports the following items: perquisites; tax reimbursements on certain relocation-related benefits and retirement-related financial planning assistance; employer contributions in 2014 to the Southern Company Employee Savings Plan (ESP), which is a tax-

qualified defined contribution plan intended to meet requirements of Section 401(k) of the Code; and contributions in 2014 under the Southern Company Supplemental Benefit Plan (Non-Pension Related) (SBP). The SBP is described more fully in the information following the Nonqualified Deferred Compensation table.

The amounts reported for 2014 are itemized below.

	Perquisites ($)	Tax Reimbursements ($)	ESP ($)	SBP ($)	Total ($)
T. A. Fanning	10,023		13,260	47,539	70,822
A. P. Beattie	5,022		11,437	20,834	37,293
W. P. Bowers	7,464		12,853	26,669	46,986
K. S. Greene	400,708	171,457	13,260	19,890	605,315
S. E. Kuczynski	9,241		9,113	20,763	39,117
C. D. McCrary	84,345		11,199	1,393	96,937

Description of Perquisites

Personal Financial Planning is provided for most officers of the Company, including all of the named executive officers. The Company pays for the services of a financial planner on behalf of the officers, up to a maximum amount of $8,700 per year, after the initial year that the benefit is provided. In the initial year, the allowed amount is $15,000. The Company also provides a five-year allowance of $6,000 for estate planning and tax return preparation fees.

Relocation Benefits are provided to cover the costs associated with geographic relocation. In 2014, Ms. Greene received relocation-related benefits in the amount of $363,155 in connection with her 2014 relocation from Atlanta, Georgia to Birmingham, Alabama. This amount was for the shipment of household goods, incidental expenses related to her move, and home sale and home repurchase assistance. Also, as provided in the Company s relocation policy, tax assistance is provided on the taxable relocation benefits. If Ms. Greene terminates within two years of her relocation, these amounts must be repaid.

Personal Use of Corporate Aircraft. The Southern Company system has aircraft that are used to facilitate business travel. All flights on these aircraft must have a business purpose, except limited personal use that is associated with

business travel is permitted. The amount reported for such personal use is the incremental cost of providing the benefit, primarily fuel costs. Also, if seating is available, the Company permits a spouse or other family member to accompany an employee on a flight. However, because in such cases the aircraft is being used for a business purpose, there is no incremental cost associated with the family travel, and no amounts are included for such travel. Any additional expenses incurred that are related to family travel are included. The perquisite amount shown above for Mr. Bowers includes $1,664 for approved personal use of corporate aircraft. In connection with Ms. Greene s relocation, the Compensation Committee approved personal use of the corporate aircraft for weekly round-trip flights between Atlanta and Birmingham for the first twelve months following her relocation to Birmingham. The perquisite amount shown above for Ms. Greene includes $32,379 for this approved personal use of corporate aircraft.

Other Miscellaneous Perquisites. The amount included reflects the full cost to the Company of providing the following items: personal use of Company-provided tickets for sporting and other entertainment events and gifts distributed to and activities provided to attendees at Company-sponsored events.

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GRANTS OF PLAN-BASED AWARDS IN 2014

This table provides information on stock option grants made and goals established for future payouts under the performance-based compensation programs during 2014 by the Compensation Committee.

		Estimated Future Payouts Under Non-Equity Incentive Plan Awards			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards: Number of Shares of Stock or Units	All Other Option Awards: Number of Securities Underlying Options	Exercise or Base Price of Option Awards	Grant Date Fair Value of Stock and Option Awards
ame	Grant Date	Threshold ($)	Target ($)	Maximum ($)	Threshold (#)	Target (#)	Maximum (#)	(#)	(#)	($/Sh)	($)
a)	(b)	(c)	(d)	(e)	(h)	(g)	(h)	(i)	(j)	(k)	(l)
. A.		14,400	1,440,000	2,880,000							
	2/10/2014				901	90,143	180,286				3,383,968
anning	2/10/2014								1,025,454	41.28	2,255,999
. P.		5,051	505,123	1,010,247							
	2/10/2014				247	24,758	49,516				929,415
eattie	2/10/2014								281,644	41.28	619,617
. P. owers		5,905	590,503	1,181,007							
	2/10/2014				289	28,943	57,886				1,086,520

	2/10/2014								329,250	41.28	724,350
K. S.		4,550	455,000	910,000							
	2/10/2014				187	18,700	37,400				701,998
Greene	2/10/2014								212,727	41.28	467,999
. E.		4,679	467,875	935,750							
	2/10/2014				181	18,160	36,320				681,726
Kuczynski	2/10/2014								206,594	41.28	454,507
	10/20/2014							21,377			1,000,016
C. D.		1,898	189,767	379,534							
McCrary	2/10/2014				288	28,886	57,772				1,084,380
	2/10/2014								328,600	41.28	722,920
	2/10/2014							43,908			1,812,522

Columns (c), (d), and (e)

These columns reflect the annual Performance Pay Program opportunity granted to the named executive officers in 2014 as described in the CD&A. The information shown as Threshold, Target, and Maximum reflects the range of potential payouts established by the Compensation Committee. The actual amounts earned are disclosed in the Summary Compensation Table. The amounts shown for Mr. McCrary are prorated based on the amount of time he was employed at Alabama Power in 2014.

Columns (f), (g), and (h)

These columns reflect the performance shares granted to the named executive officers in 2014, as described in the CD&A. The information shown as Threshold, Target, and Maximum reflects the range of potential payouts established by the Compensation Committee. Earned performance shares will be paid out in Common Stock following the end of the 2014 through 2016 performance period, based on the extent to which the performance goals are achieved. Any shares not earned are forfeited.

The number of shares shown for Mr. McCrary reflects the full grant he received in February

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2014. However, since Mr. McCrary retired in May 2014, the ultimate number of performance shares he will receive will be prorated based on the number of months he was employed by Alabama Power during the performance period.

Column (i)

This column reflects the number of restricted stock units granted to Mr. Kuczynski on the grant date as described in the CD&A. This column also reflects the restricted stock units granted to Mr. McCrary in 2012 and modified by the Compensation Committee in February 2014, as described in the CD&A.

Columns (j) and (k)

Column (j) reflects the number of stock options granted to the named executive officers in 2014, as described in the CD&A, and column (k) reflects the exercise price of the stock options, which was the closing price on the grant date.

Column (l)

This column reflects the aggregate grant date fair value of the performance shares, stock options, and restricted stock units granted in 2014. This column also reflects the incremental fair value of the restricted stock units granted to Mr. McCrary in 2012 and modified in February 2014. For performance shares, the value is based on the probable outcome of the performance conditions as of the grant date using a Monte Carlo simulation model. For stock options, the value is derived using the Black-Scholes stock option pricing model. For the restricted stock units granted to Mr. Kuczynski, the value is based on the closing price of Common Stock on the grant date. According to SEC rules, the incremental fair value of the restricted stock units granted to Mr. McCrary in 2012 and modified in February 2014 is reported using the value on the modification date. The assumptions used in calculating these amounts are discussed in Note 8 to the Financial Statements.

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OUTSTANDING EQUITY AWARDS AT 2014 FISCAL YEAR-END

This table provides information pertaining to all outstanding stock options and stock awards (performance shares and restricted stock units) held by or granted to the named executive officers as of December 31, 2014.

	Option Awards				Stock Awards			
Name (a)	Number of Securities Underlying Unexercised Options Exercisable (#) (b)	Number of Securities Underlying Unexercised Options Unexercisable (#) (c)	Option Exercise Price ($) (d)	Option Expiration Date (e)	Number of Shares or Units of Stock That Have Not Vested (#) (f)	Market Value of Shares or Units of Stock That Have Not Vested ($) (g)	Equity Incentive Plan Awards: Number of Unearned Shares, Units, or Other Rights That Have Not Vested (#) (h)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units, or Other Rights That Have Not Vested ($) (i)
T. A. Fanning	398,230	199,115	44.42	2/13/2022				
	238,099	476,198	44.06	2/11/2023				
		1,025,454	41.28	2/10/2024				

							77,250	3,793,748
							90,143	4,426,923
A. P. Beattie	140,384		37.97	2/14/2021				
	101,388	50,694	44.42	2/13/2022				
	60,620	121,238	44.06	2/11/2023				
		281,644	41.28	2/10/2024				
							19,667	965,846
							24,758	1,215,865
W. P. Bowers	70,680		36.42	2/19/2017				
	85,151		35.78	2/18/2018				
	90,942		31.39	2/16/2019				
	233,477		31.17	2/15/2020				
	164,377		37.97	2/14/2021				
	131,608	65,804	44.42	2/13/2022				
	78,535	157,069	44.06	2/11/2023				
		329,250	41.28	2/10/2024				
							25,480	1,251,323
							28,943	1,421,391
K. S. Greene	109,705	219,408	46.74	4/1/2023				
		212,727	41.28	2/10/2024				
							18,700	918,357
					46,425	2,279,932		
S. E. Kuczynski	332,225		40.14	7/11/2021				
	81,022	40,511	44.42	2/13/2022				
	48,349	96,697	44.06	2/11/2023				
		206,594	41.28	2/10/2024				
							15,686	770,339
							18,160	891,838
					30,931	1,519,021		
C. D. McCrary	207,443		44.42	2/13/2022				
	247,576		44.06	2/11/2023				
	328,600		41.28	2/10/2024				
							26,774	1,314,871
							28,886	1,418,591

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Columns (b), (c), (d), and (e)

Stock options vest one-third per year on the anniversary of the grant date. Options granted from 2007 through 2011 with expiration dates from 2017 through 2021 were fully vested as of December 31, 2014. The options granted in 2012, 2013, and 2014 become fully vested as shown below.

Year Option Granted	Expiration Date	Date Fully Vested
2012	February 13, 2022	February 13, 2015
2013	February 11, 2023	February 11, 2016
2014	February 10, 2024	February 10, 2017

Options also fully vest upon death, total disability, or retirement and expire three years following death or total disability or five years following retirement, or on the original expiration date if earlier. Please see Potential Payments upon Termination or Change-in-Control for more information about the treatment of stock options under different termination and change-in-control events.

Columns (f) and (g)

These columns reflect the number of restricted stock units, including the deemed reinvestment of dividends, held as of December 31, 2014. The value in column (g) is based on the Common Stock closing price on December 31, 2014 ($49.11). The restricted stock units for Ms. Greene vest incrementally each year starting April 1, 2015 and ending April 1, 2018 if she remains employed with the Southern Company system. The restricted stock units for Mr. Kuczynski vest on December 31, 2017 if he remains employed with the Southern Company system on the vesting date. See further discussion of restricted stock units in the CD&A. See also Potential Payments upon Termination or Change-in-Control for more information about the treatment of restricted stock units under different termination and change-in-control events.

Columns (h) and (i)

In accordance with SEC rules, column (h) reflects the target number of performance shares that can be earned at the end of each three-year performance period (December 31, 2015 and 2016) that were granted in 2013 and 2014, respectively. The performance shares granted for the 2012 through 2014 performance period vested on December 31, 2014 and are shown in the Option Exercises and Stock Vested in 2014 table below.

The value in column (i) is derived by multiplying the number of shares in column (h) by the Common Stock closing price on December 31, 2014 ($49.11). The ultimate number of shares earned, if any, will be based on the actual performance results at the end of each respective performance period. The ultimate number of shares earned by

Mr. McCrary will be prorated based on the number of months he was employed by Alabama Power during the performance periods. See further discussion of performance shares in the CD&A. See also Potential Payments upon Termination or Change-in-Control for more information about the treatment of performance shares under different termination and change-in-control events.

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OPTION EXERCISES AND STOCK VESTED IN 2014

	Option Awards		Stock Awards	
Name (a)	Number of Shares Acquired on Exercise (#) (b)	Value Realized on Exercise ($) (c)	Number of Shares Acquired on Vesting (#) (d)	Value Realized on Vesting ($) (e)
T. A. Fanning	1,049,185	10,336,745	10,127	497,337
A. P. Beattie	57,983	547,091	2,578	126,606
W. P. Bowers	128,093	1,628,963	3,347	164,371
K. S. Greene				
S. E. Kuczynski			2,060	101,167
C. D. McCrary	452,498	4,169,084	50,311	2,314,724

Columns (b) and (c)

Column (b) reflects the number of shares acquired upon the exercise of stock options during 2014, and column (c) reflects the value realized. The value realized is the difference in the market price over the exercise price on the exercise date.

Columns (d) and (e)

Column (d) includes the performance shares awarded for the 2012 through 2014 performance period that vested on December 31, 2014. The value reflected in column (e) is derived by multiplying the number of shares that vested by the market value of the underlying shares on the vesting date ($49.11).

Because Ms. Greene was not an employee of the Southern Company system when performance shares were awarded in 2012, column (d) does not reflect any vested performance shares for her.

Certain restricted stock units with reinvested dividends vested on April 30, 2014 and are reflected in column (d) for Mr. McCrary. The value of the restricted stock units as shown in column (e) is derived by multiplying the number of restricted stock units and reinvested dividends that vested (47,576) by the market value of the underlying shares on the vesting date ($45.83).

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PENSION BENEFITS AT 2014 FISCAL YEAR-END

Name (a)	Plan Name (b)	Number of Years Credited Service (#) (c)	Present Value of Accumulated Benefit ($) (d)	Payments During Last Fiscal Year ($) (e)
T. A. Fanning	Pension Plan	33.0	1,359,877	
	Supplemental Benefit Plan (Pension-Related)	33.0	10,947,004	
	Supplemental Executive Retirement Plan	33.0	4,468,682	
A. P. Beattie	Pension Plan	37.92	1,737,633	
	Supplemental Benefit Plan (Pension-Related)	37.92	5,206,128	
	Supplemental Executive Retirement Plan	37.92	2,011,301	
W. P. Bowers	Pension Plan	34.67	1,445,025	
	Supplemental Benefit Plan (Pension-Related)	34.67	5,671,484	
	Supplemental Executive Retirement Plan	34.67	1,860,971	
K. S. Greene	Pension Plan	7.17	203,653	
	Supplemental Benefit Plan (Pension-Related)	7.17	192,443	
	Supplemental Executive Retirement Plan	7.17	255,522	
S. E. Kuczynski	Pension Plan	2.58	89,419	
	Supplemental Benefit Plan (Pension-Related)	2.58	223,065	
	Supplemental Executive Retirement Plan	2.58	109,590	
C. D. McCrary	Pension Plan	39.33	1,931,424	77,806
	Supplemental Benefit Plan (Pension-Related)	39.33	8,522,909	920,251
	Supplemental Executive Retirement Plan	39.33	2,688,067	290,241

Pension Plan

The Pension Plan is a tax-qualified, funded plan. It is the Company s primary retirement plan. Generally, all full-time Southern Company system employees participate in this plan after one year of service. Normal retirement benefits become payable when participants attain age 65 and complete five years of participation. The plan benefit equals the greater of amounts computed using a 1.7% offset formula and a 1.25% formula, as described below. Benefits are limited to a statutory maximum.

The 1.7% offset formula amount equals 1.7% of final average pay times years of participation less an offset related to Social Security benefits. The offset equals a service ratio times 50% of the anticipated Social Security benefits in excess of $4,200. The service ratio adjusts the offset for the portion of a full career that a participant has

worked. The highest three rates of pay out of a participant s last 10 calendar years of service are averaged to derive final average pay. The rates of pay considered for this formula are the base salary rates with no adjustments for voluntary deferrals after 2008. A statutory limit restricts the amount considered each year; the limit for 2014 was $260,000.

The 1.25% formula amount equals 1.25% of final average pay times years of participation. For this formula, the final average pay computation is the same as above, but annual performance-based compensation earned each year is added to the base salary rates.

Early retirement benefits become payable once plan participants have, during employment, attained age 50 and completed 10 years of participation. Participants who retire early from active service receive benefits equal to the amounts computed using the same formulas employed at normal retirement. However, a 0.3% reduction applies for each month (3.6% for each year) prior to normal retirement that participants elect to have their benefit payments commence. For example, 64% of the formula benefits are payable starting at age 55. As of December 31, 2014, all of the named executive officers are retirement-eligible except Ms. Greene and Mr. Kuczynski.

The Pension Plan s benefit formulas produce amounts payable monthly over a participant s post-retirement lifetime. At retirement, plan participants can choose to receive their benefits in one of seven alternative forms of payment. All forms pay benefits monthly over the lifetime of the retiree or the joint lifetimes of the retiree and a spouse. A reduction applies if a retiring participant chooses a payment form other than a single life annuity. The reduction makes the value of the benefits paid in the form chosen comparable to what it would have been if benefits were paid as a single life annuity over the retiree s life.

Participants vest in the Pension Plan after completing five years of service. As of December 31, 2014, all of the named executive officers are vested in their Pension Plan benefits except Mr. Kuczynski. Ms. Greene received years of credited service for her previous employment with the Southern Company system. Participants who terminate employment after vesting can elect to have their pension benefits commence at age 50 if they participated in the Pension Plan for 10 years. If such an election is made, the early retirement reductions that apply are actuarially determined factors and are larger than 0.3% per month.

If a participant dies while actively employed and is either age 50 or vested in the Pension Plan as of date of death, benefits will be paid to a surviving spouse. A survivor s benefit equals 45% of the monthly benefit that the participant had earned before his or her death. Payments to a surviving spouse of a participant who could have retired will begin immediately. Payments to a survivor of a participant who was not retirement-eligible will begin when the deceased participant would have attained age 50. After commencing, survivor

benefits are payable monthly for the remainder of a survivor s life. Participants who are eligible for early retirement may opt to have an 80% survivor benefit paid if they die; however, there is a charge associated with this election.

If participants become totally disabled, periods that Social Security or employer-provided disability income benefits are paid will count as service for benefit calculation purposes. The crediting of this additional service ceases at the point a disabled participant elects to commence retirement payments. Outside of this extra service crediting, the normal Pension Plan provisions apply to disabled participants.

The Southern Company Supplemental Benefit Plan (Pension-Related) (SBP-P)

The SBP-P is an unfunded retirement plan that is not tax qualified. This plan provides high-paid employees any benefits that the Pension Plan cannot pay due to statutory pay/benefit limits. The SBP-P s vesting and early retirement provisions mirror those of the Pension Plan. Its disability provisions mirror those of the Pension Plan but cease upon a participant s separation from service.

The amounts paid by the SBP-P are based on the additional monthly benefit that the Pension Plan would pay if the statutory limits and pay deferrals were ignored. When a SBP-P participant separates from service, vested monthly benefits provided by the benefit formulas are converted into a single sum value. It equals the present value of what would have been paid monthly for an actuarially determined average post-retirement lifetime. The discount rate used in the calculation is based on the 30-year U.S. Treasury yields for the September preceding the calendar year of separation, but not more than six percent.

Vested participants terminating prior to becoming eligible to retire will be paid their single sum value as of September 1 following the calendar year of separation. If the terminating participant is retirement-eligible, the single sum value will be paid in 10 annual installments starting shortly after separation. The unpaid balance of a retiree s single sum will be credited with interest at the prime rate published in *The Wall Street Journal*. If the separating participant is a key man under Section 409A of the Code, the first installment will be delayed for six months after the date of separation.

If a SBP-P participant dies after becoming vested in the Pension Plan, the spouse of the deceased participant will receive the installments the participant would have been paid upon retirement. If a vested participant s death occurs prior to age 50, the installments will be paid to a spouse as if the participant had survived to age 50.

The Southern Company Supplemental Executive Retirement Plan (SERP)

The SERP is also an unfunded retirement plan that is not tax qualified. This plan provides high-paid employees additional benefits that the Pension Plan and the SBP-P would pay if the 1.7% offset formula calculations reflected a portion of annual performance-based compensation. To derive the SERP benefits, a final average pay is determined reflecting participants base rates of pay and their annual performance-based compensation amounts, whether or not deferred, to the extent they exceed 15% of those base rates (ignoring statutory limits). This final average pay is used in the 1.7% offset formula to derive a gross benefit. The Pension Plan and the SBP-P benefits are subtracted from the gross benefit to calculate the SERP benefit. The SERP s early retirement, survivor benefit, disability, and form of payment provisions mirror the SBP-P s provisions. However, except upon a change in control, SERP benefits do not vest until participants retire, so no benefits are paid if a participant terminates prior to becoming retirement-eligible. More information about vesting and payment of SERP benefits following a change in control is included under Potential Payments upon Termination or Change-in-Control.

Pension Benefit Assumptions

The following assumptions were used in the present value calculations for all pension benefits:

- Discount rate 4.20% Pension Plan and 3.75% supplemental plans as of December 31, 2014,
- Retirement date Normal retirement age (65 for all named executive officers),
- Mortality after normal retirement RP-2014 mortality tables with generational projections,
- Mortality, withdrawal, disability, and retirement rates prior to normal retirement None,
- Form of payment for Pension Benefits:
  - Male retirees: 25% single life annuity; 25% level income annuity; 25% joint and 50% survivor annuity; and 25% joint and 100% survivor annuity
  - Female retirees: 75% single life annuity; 15% level income annuity; 5% joint and 50% survivor annuity; and 5% joint and 100% survivor annuity

- Spouse ages Wives two years younger than their husbands,

- Annual performance-based compensation earned but unpaid as of the measurement date 130% of target opportunity percentages times base rate of pay for year amount is earned, and

- Installment determination 3.75 % discount rate for single sum calculation and 4.25% prime rate during installment payment period.

For all of the named executive officers, the number of years of credited service is one year less than the number of years of employment. The number of years of credited service for Ms. Greene reflects her previous employment with the Southern Company system.

Columns (d) and (e)

For Mr. McCrary, who retired effective May 1, 2014, column (d) reflects the actual benefits expected to be paid, and column (e) reflects the actual amount paid under the Pension Plan in 2014, as described above.

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NONQUALIFIED DEFERRED COMPENSATION AS OF 2014 FISCAL YEAR-END

Name (a)	Executive Contributions in Last FY ($) (b)	Employer Contributions in Last FY ($) (c)	Aggregate Earnings in Last FY ($) (d)	Aggregate Withdrawals/ Distributions ($) (e)	Aggregate Balance at Last FYE ($) (f)
T. A. Fanning	239,141	47,539	337,542		3,360,041
A. P. Beattie		20,834	53,350		554,209
W. P. Bowers	149,632	26,669	650,324		4,510,207
K. S. Greene		19,890	4,795		35,944
S. E. Kuczynski		20,763	11,919		71,858
C. D. McCrary		1,393	113,931	1,709,936	3,967

The Company provides the DCP, which is designed to permit participants to defer income as well as certain federal, state, and local taxes until a specified date or their retirement or other separation from service. Up to 50% of base salary and up to 100% of performance-based non-equity compensation may be deferred at the election of eligible employees. All of the named executive officers are eligible to participate in the DCP.

Participants have two options for the deemed investments of the amounts deferred the Stock Equivalent Account and the Prime Equivalent Account. Under the terms of the DCP, participants are permitted to transfer between investments at any time.

The amounts deferred in the Stock Equivalent Account are treated as if invested at an equivalent rate of return to that of an actual investment in Common Stock, including the crediting of dividend equivalents as such are paid by Southern Company from time to time. It provides participants with an equivalent opportunity for the capital appreciation (or loss) and income of that of a Company stockholder. During 2014, the rate of return in the Stock Equivalent Account was 25.27%.

Alternatively, participants may elect to have their deferred compensation deemed invested in the Prime Equivalent Account, which is treated as if invested at a prime interest rate compounded monthly, as published in *The Wall Street Journal* as the base rate on corporate loans posted as of

the last business day of each month by at least 75% of the United States largest banks. The interest rate earned on amounts deferred during 2014 in the Prime Equivalent Account was 3.25%.

Column (b)

This column reports the actual amounts of compensation deferred under the DCP by each named executive officer in 2014. The amount of salary deferred by the named executive officers, if any, is included in the Salary column in the Summary Compensation Table. The amounts of performance-based compensation deferred in 2014 were the amounts that were earned as of December 31, 2013 but were not payable until the first quarter of 2014. These amounts are not reflected in the Summary Compensation Table because that table reports performance-based compensation that was earned in 2014 but not payable until early 2015. These deferred amounts may be distributed in a lump sum or in up to 10 annual installments at termination of employment or in a lump sum at a specified date, at the election of the participant.

Column (c)

This column reflects contributions under the SBP. Under the Code, employer-matching contributions are prohibited under the ESP on employee contributions above stated limits in the ESP, and, if applicable, above legal limits set forth in the Code. The SBP is a nonqualified deferred compensation plan under which contributions are made that are prohibited from being made in the ESP. The contributions are treated as if invested in Common Stock and are payable in cash upon termination of employment in a lump sum or in up to 20 annual installments, at the election of the participant. The amounts reported in this column also were reported in the All Other Compensation column in the Summary Compensation Table.

Column (d)

This column reports earnings or losses on both compensation the named executive officers elected to defer and on employer contributions under the SBP.

Column (f)

This column includes amounts that were deferred under the DCP and contributions under the SBP in prior years. The following chart shows the amounts previously reported.

	Amounts Deferred under the DCP prior to 2014 and previously reported ($)	Employer Contributions under the SBP prior to 2014 and previously reported ($)	Total ($)
T. A. Fanning	1,936,157	368,900	2,305,057
A. P. Beattie	34,781	61,314	96,095
W. P. Bowers	1,981,253	143,292	2,124,545
K. S. Greene	0	11,220	11,220
S. E. Kuczynski	0	19,905	19,905

C. D. McCrary	489,924	376,220	866,144

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POTENTIAL PAYMENTS UPON TERMINATION OR CHANGE-IN-CONTROL

This section describes and estimates payments that could be made to the named executive officers serving as of December 31, 2014 under different termination and change-in-control events. The estimated payments would be made under the terms of Southern Company s compensation and benefit program or the change-in-control severance program. All of the named executive officers are participants in Southern Company s change-in-control severance program for officers. The amount of potential payments is calculated as if the triggering events occurred as of December 31, 2014 and assumes that the price of Common Stock is the closing market price on December 31, 2014.

Description of Termination and Change-in-Control Events

The following charts list different types of termination and change-in-control events that can affect the treatment of payments under the compensation and benefit programs. No payments are made under the change-in-control severance program unless, within two years of the change in control, the named executive officer is involuntarily terminated or voluntarily terminates for Good Reason. (See the description of Good Reason below.)

Traditional Termination Events

¡ Retirement or Retirement-Eligible Termination of a named executive officer who is at least 50 years old and has at least 10 years of credited service.

¡ Resignation Voluntary termination of a named executive officer who is not retirement-eligible.

¡ Lay Off Involuntary termination of a named executive officer who is not retirement-eligible not for cause.

¡ Involuntary Termination Involuntary termination of a named executive officer for cause. Cause includes individual performance
below minimum performance standards and misconduct, such as violation of the Company s Drug and Alcohol Policy.

¡ Death or Disability Termination of a named executive officer due to death or disability.

Change-in-Control-Related Events

At the Company or the subsidiary company level:

¡ Company Change-in-Control I Consummation of an acquisition by another entity of 20% or more of Common Stock or, following consummation of a merger with another entity, the Company s stockholders own 65% or less of the entity surviving the merger.

¡ Company Change-in-Control II Consummation of an acquisition by another entity of 35% or more of Common Stock or, following consummation of a merger with another entity, the Company s stockholders own less than 50% of the Company surviving the merger.

¡ Company Termination Consummation of a merger or other event and the Company is not the surviving company or Common Stock is no longer publicly traded.

¡ Subsidiary Company Change-in-Control Consummation of an acquisition by another entity, other than another subsidiary of the Company, of 50% or more of the stock of any of the Company s subsidiaries, consummation of a merger with another entity and the Company s subsidiary is not the surviving company, or the sale of substantially all the assets of any of the Company s subsidiaries.

At the employee level:

Involuntary Change-in-Control Termination or Voluntary Change-in-Control Termination for Good Reason Employment is terminated within two years of a change in control, other than for cause, or the employee voluntarily terminates for Good Reason. Good Reason for

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voluntary termination within two years of a change in control generally is satisfied when there is a material reduction in salary,

performance-based compensation opportunity or benefits, relocation of over 50 miles, or a diminution in duties and responsibilities.

The following chart describes the treatment of different pay and benefit elements in connection with the Traditional Termination Events as described above.

Program	Retirement/ Retirement-Eligible	Lay Off (Involuntary Termination Not For Cause)	Resignation	Death or Disability	Involuntary Termination (For Cause)
Pension Benefits Plans	Benefits payable as described in the notes following the Pension Benefits table.	Same as Retirement.	Same as Retirement.	Same as Retirement.	Same as Retirement.
Annual Performance Pay Program	Prorated if retire before 12/31.	Same as Retirement.	Forfeit.	Same as Retirement.	Forfeit.
Stock Options	Vest; expire earlier of original expiration date or five years.	Vested options expire in 90 days; unvested are forfeited.	Same as Lay Off.	Vest; expire earlier of original expiration date or three years.	Forfeit.
Performance Shares		Forfeit.	Forfeit.	Same as Retirement.	Forfeit.

	Prorated if retire prior to end of performance period.				
Restricted Stock Units	Forfeit.	Vest.	Forfeit.	Vest.	Forfeit.
Financial Planning Perquisite	Continues for one year.	Terminates.	Terminates.	Same as Retirement.	Terminates.
DCP	Payable per prior elections (lump sum or up to 10 annual installments).	Same as Retirement.	Same as Retirement.	Payable to beneficiary or participant per prior elections. Amounts deferred prior to 2005 can be paid as a lump sum per the benefit administration committee s discretion.	Same as Retirement.
SBP non-pension related	Payable per prior elections (lump sum or up to 20 annual installments).	Same as Retirement.	Same as Retirement.	Same as the DCP	Same as Retirement.

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The following chart describes the treatment of payments under compensation and benefit programs under different change-in-control events, except the Pension Plan. The Pension Plan is not affected by change-in-control events.

rogram	Company Change-in-Control I	Company Change-in-Control II	Company Termination or Subsidiary Company Change-in-Control	Involuntary Change-in-Control-Related Termination or Voluntary Change-in-Control-Related Termination for Good Reason
onqualified Pension enefits	All SERP-related benefits vest if participants vested in tax-qualified pension benefits; otherwise, no impact. SBP - pension-related benefits vest for all participants and single sum value of benefits earned to change-in-control date paid following termination or retirement.	Benefits vest for all participants and single sum value of benefits earned to the change-in-control date paid following termination or retirement.	Same as Company Change-in-Control II.	Based on type of change-in-control event.
nnual Performance ay Program	If no program termination, paid at greater of target or actual performance. If program terminated within two years of change-in-control, prorated at target performance level.	Same as Company Change-in-Control I.	Prorated at target performance level.	If not otherwise eligible for payment, if the program is still in effect, prorated at target performance level.
ock Options	Not affected by change-in-control events.	Not affected by change-in-control events.	Vest and convert to surviving company s securities; if cannot convert, pay spread in cash.	Vest.
erformance Shares	Not affected by change-in-control events.	Not affected by change-in-control events.	Vest and convert to surviving company s securities; if cannot	Vest.

			convert, pay spread in cash.	
SUs	Not affected by change-in-control events.	Not affected by change-in-control events.	Vest and convert to surviving company s securities; if cannot convert, pay spread in cash.	Vest.
CP	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.
3P	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.
everance Benefits	Not applicable.	Not applicable.	Not applicable.	Two or three times base salary plus targe annual performance-based pay.
ealthcare Benefits	Not applicable.	Not applicable.	Not applicable.	Up to five years participation in grou healthcare plan plus payment of two or three years premiu amounts.
utplacement ervices	Not applicable.	Not applicable.	Not applicable.	Six months.

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Potential Payments

This section describes and estimates payments that would become payable to the named executive officers upon a termination or change in control as of December 31, 2014.

Pension Benefits

The amounts that would have become payable to the named executive officers if the Traditional Termination Events occurred as of December 31, 2014 under the Pension Plan, the SBP-P, and the SERP are itemized in the following chart. The amounts shown under the Retirement column are amounts that would have become payable to the named executive officers that were retirement-eligible on December 31, 2014 and are the monthly Pension Plan benefits and the first of 10 annual installments from the SBP-P and the SERP. The amounts shown under the Resignation or Involuntary Termination column are the amounts that would have become payable to the named executive officers who were not retirement-eligible on December 31, 2014 and are the monthly Pension Plan benefits that would become payable as of the earliest possible date under the Pension Plan and the single sum value of benefits earned up to the

termination date under the SBP-P, paid as a single payment rather than in 10 annual installments. Benefits under the SERP would be forfeited. The amounts shown that are payable to a spouse in the event of the death of the named executive officer are the monthly amounts payable to a spouse under the Pension Plan and the first of 10 annual installments from the SBP-P and the SERP. The amounts in this chart are very different from the pension values shown in the Summary Compensation Table and the Pension Benefits table. Those tables show the present values of all the benefit amounts anticipated to be paid over the lifetimes of the named executive officers and their spouses. Those plans are described in the notes following the Pension Benefits table. Of the named executive officers, Ms. Greene and Mr. Kuczynski were not retirement-eligible on December 31, 2014.

		Retirement ($)	Resignation or Involuntary Termination	Death (payments to a spouse) ($)
T. A. Fanning	Pension	8,207	treated as retiring	4,998
	SBP-P	1,239,797	treated as retiring	1,239,797
	SERP	506,098	treated as retiring	506,098
A. P. Beattie	Pension	10,689	treated as retiring	5,740
	SBP-P	568,034	treated as retiring	568,034

	SERP	219,450	treated as retiring	219,450
W. P. Bowers	Pension	8,737	treated as retiring	5,256
	SBP-P	640,352	treated as retiring	640,352
	SERP	210,117	treated as retiring	210,117
K. S. Greene	Pension		628	1,031
	SBP-P		192,311	22,072
	SERP			29,307
S. E. Kuczynski	Pension			406
	SBP-P			
	SERP			

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As described in the Change-in-Control chart, the only change in the form of payment, acceleration, or enhancement of the pension benefits is that the single sum value of benefits earned up to the change-in-control date under the SBP-P and the SERP could be paid as a single payment rather than in 10 annual installments. Also, the SERP benefits vest for participants who are not retirement-eligible upon a change in control. Estimates of the single

sum payment that would have been made to the named executive officers, assuming termination as of December 31, 2014 following a change-in-control-related event, other than a Company Change-in-Control I (which does not impact how pension benefits are paid), are itemized below. These amounts would be paid instead of the benefits shown in the Traditional Termination Events chart above; they are not paid in addition to those amounts.

	SBP-P ($)	SERP ($)	Total ($)
T. A. Fanning	12,397,974	5,060,983	17,458,957
A. P. Beattie	5,680,337	2,194,503	7,874,840
W. P. Bowers	6,403,519	2,101,171	8,504,690
K. S. Greene	188,182	249,865	438,047
S. E. Kuczynski			

The pension benefit amounts in the tables above were calculated as of December 31, 2014 assuming payments would begin as soon as possible under the terms of the plans. Accordingly, appropriate early retirement reductions were applied. Any unpaid annual performance-based compensation was assumed to be paid at 1.30 times the target level. Pension Plan benefits were calculated assuming each named executive officer chose a single life annuity form of payment, because that results in the greatest monthly benefit. The single sum values were based on a 3.79% discount rate.

Annual Performance Pay Program

The amount payable if a change in control had occurred on December 31, 2014 is the greater of target or actual performance. Because actual payouts for 2014 performance were above the target level for all of the named executive officers, the amount that would have been payable was the actual amount paid as reported in the CD&A and the Summary Compensation Table.

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Stock Options, Performance Shares, and Restricted Stock Units (Equity Awards)

Equity Awards would be treated as described in the Termination and Change-in-Control charts above. Under a Southern Company Termination, all Equity Awards vest. In addition, if there is an Involuntary Change-in-Control Termination or Voluntary Change-in-Control Termination for Good Reason, Equity Awards vest. There is no payment associated with Equity Awards unless there is a Southern Company Termination and the participants Equity Awards cannot be converted into surviving company awards. In that event, the value of outstanding Equity Awards would be paid to the named executive officers. For stock options, the value is the excess

of the exercise price and the closing price of Common Stock on December 31, 2014. The value of performance shares and restricted stock units is calculated using the closing price of Common Stock on December 31, 2014. The chart below shows the number of stock options for which vesting would be accelerated under a Southern Company Termination and the amount that would be payable under a Southern Company Termination if there were no conversion to the surviving company s stock options. It also shows the number and value of performance shares and restricted stock units that would be paid.

	Number of Equity Awards with Accelerated Vesting (#)			Total Number of Equity Awards Following Accelerated Vesting (#)			Total Payable in Cash without Conversion of Equity Awards ($)
	Stock Options	Performance Shares	Restricted Stock Units	Stock Options	Performance Shares	Restricted Stock Units	
T. A. Fanning	1,700,767	167,393		2,337,096	167,393		22,658,723
A. P. Beattie	453,576	44,425		755,968	44,425		7,582,510
W. P. Bowers	552,123	54,423		1,406,893	54,423		17,029,625
K. S. Greene	432,135	18,700	46,425	541,840	18,700	46,425	5,643,939

S. E. Kuczynski	343,802	33,846	30,931	805,398	33,846	30,931	9,081,360

DCP and SBP

The aggregate balances reported in the Nonqualified Deferred Compensation table would be payable to the named executive officers as described in the Traditional Termination and Change-in-Control-Related Events charts above. There is no enhancement or acceleration of payments under these plans associated with termination or change-in-control events, other than the lump-sum payment opportunity described in the above charts. The lump sums that would be payable are those that are reported in the Nonqualified Deferred Compensation table.

Healthcare Benefits

All of the named executive officers, except Ms. Greene and Mr. Kuczynski, are retirement-eligible. Healthcare benefits are provided to retirees, and there is no incremental payment associated with the termination or change-in-control events, except in the case of a change-in-control-related termination, as described in

the Change-in-Control-Related Events chart. The estimated cost of providing healthcare insurance premiums for up to a maximum of three years is $44,826 for Ms. Greene and $45,975 for Mr. Kuczynski.

Financial Planning Perquisite

An additional year of the financial planning perquisite, which is set at a maximum of $8,700 per year, will be provided after retirement for retirement-eligible named executive officers.

There are no other perquisites provided to the named executive officers under any of the traditional termination or change-in-control-related events.

Severance Benefits

The named executive officers are participants in a change-in-control severance plan. The plan provides severance benefits, including outplacement services, if within two years of a change in control, they are involuntarily terminated, not for cause, or they voluntarily

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terminate for Good Reason. The severance benefits are not paid unless the named executive officer releases the employing company from any claims he or she may have against the employing company.

The estimated cost of providing the six months of outplacement services is $6,000 per named executive officer. The severance payment is three times the base salary and target payout under the annual Performance Pay Program for Mr. Fanning and two times the base salary and target payout under the annual Performance Pay Program for the other named executive officers. If any portion of the severance amount constitutes an excess parachute payment under Section 280G of the Code and is therefore subject to an excise tax, the severance amount will be reduced unless the after-tax unreduced

amount exceeds the after-tax reduced amount. Excise tax gross-ups will not be provided on change-in-control severance payments.

The table below estimates the severance payments that would be made to the named executive officers if they were terminated as of December 31, 2014 in connection with a change in control.

	Severance Amount ($)
T. A. Fanning	7,920,000
A. P. Beattie	2,357,242
W. P. Bowers	2,755,683
K. S. Greene	2,210,000
S.E. Kuczynski	2,272,536

COMPENSATION RISK ASSESSMENT

The Company reviewed its compensation policies and practices and concluded that excessive risk-taking is not encouraged. This conclusion was based on an assessment of the mix of pay components and performance goals, the annual pay/performance analysis by the Compensation Committee s independent consultant, stock ownership requirements, compensation governance practices, and the claw-back provision. The assessment was reviewed with the Compensation Committee.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

The Compensation Committee is made up of independent Directors of the Company who have never served as executive officers of the Company. During 2014, none of the Company s executive officers served on the Board of Directors of any entities whose executive officers serve on the Compensation Committee.

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EQUITY COMPENSATION PLAN INFORMATION

The following table provides information as of December 31, 2014 concerning shares of Common Stock authorized for issuance under Southern Company s existing non-qualified equity compensation plans.

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights (a)	Weighted-average exercise price of outstanding options, warrants, and rights (b)	Number of securities remai available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders	39,929,319	$ 40.55	15,179,865(1)
Equity compensation plans not approved by security holders	n/a	n/a	n/a

(1) Represents shares available for future issuance under the Omnibus Incentive Compensation Plan.

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AUDIT

ITEM NO. 5 RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Audit Committee of the Board of Directors is directly responsible for the appointment, retention, and oversight of the independent registered public accounting firm retained to audit the Company s financial statements, including the compensation of such firm and the related audit fee negotiations.

Deloitte & Touche has served as the Company s independent registered public accounting firm since 2002. To ensure continuing independence, the Audit Committee periodically considers whether there should be a change in the independent registered public accounting firm. The Audit Committee and its Chair also participate in the selection of Deloitte & Touche s lead engagement partner in connection with the mandatory rotation requirements of the SEC.

The Audit Committee has appointed Deloitte & Touche as the Company s independent registered public accounting firm for 2015. This appointment is being submitted to stockholders for ratification, and the Audit Committee and the Board of Directors believe that the continued retention of Deloitte & Touche to serve as the Company s independent registered public accounting firm is in the best interests of the Company and its stockholders.

Representatives of Deloitte & Touche will be present at the 2015 Annual Meeting to respond to appropriate questions from stockholders and will have the opportunity to make a statement if they desire to do so.

The affirmative vote of a majority of the votes cast is required for ratification of the appointment of the independent registered public accounting firm.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR ITEM NO. 5.

AUDIT COMMITTEE REPORT

The Audit Committee oversees the Company s financial reporting process on behalf of the Board of Directors. Management has the primary responsibility for establishing and maintaining adequate internal controls over financial reporting, including disclosure controls and procedures, and for preparing the Company s consolidated financial statements. In fulfilling its oversight responsibilities, the Audit Committee reviewed the audited consolidated financial statements of the Company and its subsidiaries and management s report on the Company s internal control over financial reporting in the 2014 Annual Report to Stockholders attached hereto as Appendix D with management. The Audit Committee also reviews the Company s quarterly and annual reporting on Forms 10-Q and 10-K prior to filing with the SEC. The Audit Committee s review process includes discussions of the quality, not just the acceptability, of the accounting principles, the reasonableness of significant judgments and estimates, and the clarity of disclosures in the financial statements.

The independent registered public accounting firm is responsible for expressing opinions on the conformity of the consolidated financial statements with accounting principles generally accepted in the United States and the effectiveness of the Company s internal control over financial reporting with the criteria established in Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Audit Committee has discussed with the independent registered public accounting firm the matters that are required to be discussed by the Public Company Accounting Oversight Board (PCAOB) Auditing Standard No. 16, *Communications with Audit Committees* and SEC Rule 2-07 of Regulation S-X, *Communications with Audit Committees*. In addition, the Audit Committee has discussed with the independent registered public accounting firm its independence from management and the Company as required under rules of the PCAOB

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and has received the written disclosures and letter from the independent registered public accounting firm required by the rules of the PCAOB. The Audit Committee also has considered whether the independent registered public accounting firm s provision of non-audit services to the Company is compatible with maintaining the firm s independence.

The Audit Committee discussed the overall scope and plans with the Company s internal auditors and independent registered public accounting firm for their respective audits. The Audit Committee meets with the internal auditors and the independent registered public accounting firm, with and without management present, to discuss the results of their audits, evaluations by management and the independent registered public accounting firm of the Company s internal control over financial reporting, and the overall quality of the Company s financial reporting. The Audit Committee also meets privately with the Company s compliance officer. The Audit Committee held ten meetings during 2014.

In reliance on the reviews and discussions referred to above, the Audit Committee recommended to the Board of Directors (and the Board approved) that the audited consolidated financial statements be included in the Company s Annual Report on Form 10-K for the year ended December 31, 2014 and filed with the SEC. The Audit Committee also reappointed Deloitte & Touche as the Company s independent registered public accounting firm for 2015. Stockholders will be asked to ratify that selection at the 2015 Annual Meeting.

Members of the Audit Committee as of December 31, 2014:

Jon A. Boscia, Chair

Juanita Powell Baranco

Warren A. Hood, Jr.

Larry D. Thompson

Principal Independent Registered Public Accounting Firm Fees

The following represents the fees billed to the Company for the two most recent fiscal years by Deloitte & Touche the Company s principal independent registered public accounting firm for 2014 and 2013.

	2014	2013
	(in thousands)	
Audit Fees (1)	$ 11,794	$ 11,704

Audit-Related Fees (2)	126	110
Tax Fees		50
All Other Fees (3)	191	29
Total	$ 12,111	$ 11,893

(1) Includes services performed in connection with financing transactions.

(2) Includes non-statutory audit services in both 2014 and 2013.

(3) Represents registration fees for attendance at Deloitte & Touche-sponsored education seminars in 2013 and 2014, subscription fees for Deloitte & Touche s technical accounting research tool in 2013 and 2014, information technology consulting services related to general ledger software of the Company in 2014, and travel expenses for Deloitte & Touche s training facilitator in 2013.

The Audit Committee has adopted a Policy on Engagement of the Independent Auditor for Audit and Non-Audit Services (see Appendix C) that includes requirements for the Audit Committee to pre-approve services provided by Deloitte & Touche. This policy was initially adopted in July 2002 and, since that time, all services included in the chart above have been pre-approved by the Audit Committee.

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STOCKHOLDER PROPOSALS

ITEM NO. 6 STOCKHOLDER PROPOSAL ON PROXY ACCESS

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ITEM NO. 6

The Company has been advised that a stockholder proposes to submit the following resolution at the 2015 Annual Meeting. The name, address, and beneficial ownership of such stockholder are available upon request.

RESOLVED: Shareholders of The Southern Company (the Company) ask the board of directors (the Board) to adopt, and present for shareholder approval, a proxy access bylaw. Such a bylaw shall require the Company to include in proxy materials prepared for a shareholder meeting at which directors are to be elected the name, Disclosure and Statement (as defined herein) of any person nominated for election to the board by a shareholder or group (the Nominator) that meets the criteria established below. The Company shall allow shareholders to vote on such nominee on the Company s proxy card.

The number of shareholder-nominated candidates appearing in proxy materials shall not exceed one quarter of the directors then serving. This bylaw, which shall supplement existing rights under Company bylaws, should provide that a Nominator must:

a) have beneficially owned 3% or more of the Company s outstanding common stock continuously for at least three years before submitting the nomination;

b) give the Company, within the time period identified in its bylaws, written notice of the information required by the bylaws and any Securities and Exchange Commission rules about (i) the nominee, including consent to being named in the proxy materials and to serving as director if elected; and (ii) the Nominator, including proof it owns the required shares (the Disclosure); and

c) certify that (i) it will assume liability stemming from any legal or regulatory violation arising out of the Nominator s communications with the Company shareholders, including the Disclosure and Statement; (ii) it will comply with all applicable laws and regulations if it uses soliciting material other than the Company s proxy materials; and (c) to the best of its knowledge, the required shares were acquired in the ordinary course of business and not to change or influence control at the Company.

The Nominator may submit with the Disclosure a statement not exceeding 500 words in support of the nominee (the Statement). The Board shall adopt procedures for promptly resolving disputes over whether notice of a nomination was timely, whether the Disclosure and Statement satisfy the bylaw and applicable federal regulations, and the priority to be given to multiple nominations exceeding the one-quarter limit.

SUPPORTING STATEMENT

We believe proxy access is a fundamental shareholder right that will make directors more accountable and contribute to increased shareholder value. The CFA Institute s 2014 assessment of pertinent academic studies and the use of proxy access in other markets similarly concluded that proxy access:

¡ Would benefit both the markets and corporate boardrooms, with little cost or disruption.

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- Has the potential to raise overall US market capitalization by up to $140.3 billion if adopted market-wide. (http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2014.n9.1)

The proposed bylaw terms enjoy strong investor support votes for similar shareholder proposals averaged 55% from 2012 through September 2014 and similar bylaws have been adopted by companies of various sizes across industries, including Chesapeake Energy, Hewlett-Packard, Western Union and Verizon.

We urge shareholders to vote FOR this proposal.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ITEM NO. 6 FOR THE FOLLOWING REASONS:

Proxy access, which refers to the ability of stockholders holding a small percentage of the Company s shares to require the Company to undertake the effort and expense of including their Director nominees in the Company s proxy materials and thus trigger a proxy contest, is an untested governance feature for U.S. companies. The Board of Directors continually evaluates the Company s governance profile and believes that proxy access should not be implemented in the absence of a compelling rationale. The proponent s proxy access proposal does not seek to remedy any specific governance or performance deficiency at the Company; in fact, it appears the Company was targeted with this proposal solely because its business involves the consumption of fossil fuels and not because of any development related to proxy access.

The Company s stockholders already have significant and meaningful corporate governance rights. This includes the ability to recommend Director candidates for independent consideration by the Governance Committee and the ability to register disapproval of individual Directors or the full Board, on an annual basis, by means of the Company s majority voting standard and Director resignation policy. In addition, stockholders holding as few as 10% of the outstanding shares of Common Stock have the right to request a special meeting of stockholders.

Southern Company has consistently created value for its stockholders and there is no need for proxy access.

- The most recent dividend, paid March 6, 2015, marks the 269th consecutive quarter the Company has paid a dividend equal to or higher than the previous quarter.

- The Southern Company generation system s Equivalent Forced Outage Rate is at industry-leading levels (1.9% compared to five-year national average of approximately 9.0%).

- The Company and its four traditional operating company subsidiaries occupied the top five spots for customer satisfaction for all customer classes combined in the customer value benchmark survey, an annual peer comparison of U.S. electric utilities.

- With respect to compensation matters, the Company has received stockholder support in its annual say-on-pay vote of in excess of 94% of votes cast since the vote was first held in 2011.

Southern Company stockholders already have access to robust and effective procedures to communicate with and influence the Board of Directors and hold it accountable.

- The full Board of Directors is elected annually and the Company has a majority voting standard in uncontested Director elections, combined with a resignation policy for candidates who fail to receive a majority of votes cast (see page 13).

- Management proactively engages with stockholders on corporate governance issues (see page 12).

- The Company holds an annual say-on-pay vote on executive compensation (see page 24).

- The Board of Directors has established a mechanism for stockholders to directly communicate with the Board or with specified Directors (see page 12).

- The Company regularly engages with stockholders and other concerned parties on environmental issues and has provided significant voluntary disclosure.

Southern Company already has significant corporate governance practices that protect stockholder rights and interests.

- The Company has a threshold of just 10% of outstanding shares for stockholders to request a special meeting.

- Stockholders must approve amendments to the Company s certificate of incorporation and By-Laws, so the Board of Directors cannot unilaterally take away any rights granted to stockholders in the Company s governing documents.

- The Company has not adopted a poison pill stockholder rights plan and the Board of Directors does not have the authority to issue blank check preferred stock.

- If Proposal No. 3 is approved by stockholders, the Company s certificate of incorporation and By-Laws will not restrict stockholders ability to act by written consent to the fullest extent allowed by applicable Delaware law (see page 9).

The Board of Directors is already highly-qualified, diverse, and independent.

All members of the Board of Directors, other than the Chief Executive Officer, are independent of management and the Board has a strong Lead Independent Director to provide a source of independent leadership (see page 15). The Board periodically refreshes its membership to ensure it adds helpful experience and fresh perspectives and maintains appropriate diversity. Since the beginning of 2014, the Board of Directors has added three new members Ms. Hudson and Messrs. Thompson and Johns, which means the Board now includes three female members and three ethnic minorities. The Board s commitment to refreshment is reflected in its overall average Board tenure, which is less than six years.

Implementing proxy access could negatively affect the Company s corporate governance.

Bypassing the independent Governance Committee process for nominations.

Implementing proxy access would provide a small percentage of stockholders, who do not have a fiduciary obligation to other stockholders and who may have a narrow agenda, the right to include Director nominees in the Company s proxy statement, bypassing the Company s independent nomination process. Currently, absent a proxy contest, all nominees are recommended to the full Board of Directors for nomination by the Governance Committee. Stockholders may participate in this process by submitting recommendations of candidates for consideration by the Governance Committee (see page 19). The Governance Committee is composed entirely of independent Directors, and the Board and the Governance Committee each have a fiduciary duty to make nominations that are in the best interests of all stockholders. The Board of Directors and the Governance Committee are in the best position to evaluate Director candidates, in light of the need for a full Board that is composed of a group of Directors with complementary skills, experience, and perspectives and that meets the unique needs of the Company.

Increasing the influence of special interests and fragmenting the Board of Directors.

If proxy access were implemented, a small minority of stockholders could nominate Director candidates to further a special interest agenda that may not be in the best interest of the Company as a whole. Opposing such candidates in a contested election would be time-consuming and costly for the

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Company. Accordingly, even if special interest Directors were not elected, such stockholders could still attempt to use proxy access to extract concessions from the Company related to their special interests. Moreover, the election of Directors nominated by a small percentage of stockholders with special interests could also result in the creation of factions on the Board of Directors, making it more difficult for the Board to reach consensus on behalf of all stockholders, thereby delaying important decision-making.

Proxy access could lead to continually contested elections, which would impose costs on the Company, divert management s and the Board s attention, and potentially discourage highly-qualified Directors from serving.

Providing proxy access for a group of stockholders owning just 3% of the Company s outstanding shares could make contested elections much more commonplace. Currently, stockholders seeking to nominate Director candidates must, like the Company, bear their own costs of soliciting votes for their proposed nominees. This existing system helps ensure that a stockholder is serious about its intention to nominate Directors, because the stockholder must bear the cost of its own solicitation. Proxy access would shift this cost to the Company, at no risk to the stockholder. In addition, the prospect of having to stand in a contested election routinely could cause highly-qualified Directors to be reluctant to serve on the Board of Directors.

The vote needed to pass the proponent s resolution is the affirmative vote of a majority of the votes cast.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ITEM NO. 6.

ITEM NO. 7 GREENHOUSE GAS EMISSIONS REDUCTION GOALS 2015

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ITEM NO. 7.

The Company has been advised that a stockholder, together with multiple co-filers, proposes to submit the following resolution at the 2015 Annual Meeting. The names, addresses, and beneficial ownership of such stockholder and co-filers are available upon request.

RESOLVED:

Shareholders request that Southern Company adopt absolute, quantitative time-bound goals for reducing total greenhouse gas (GHG) emissions from operations and report to shareholders by November 1, 2015 on its plans to achieve these goals (omitting proprietary information and prepared at reasonable cost.)

WHEREAS:

The 2014 *Synthesis Report* of the Intergovernmental Panel on Climate Change (IPCC) warns that continued greenhouse gas (GHG) emissions and subsequent global warming will have severe, pervasive and irreversible impacts for people and ecosystems. The *Risky Business* report forecasts significant economic costs to agriculture, labor productivity, and property.

To mitigate the worst impacts of climate change and limit warming to below 2°C, as agreed in the Copenhagen Accord, the IPCC estimates that a fifty percent reduction in GHG emissions globally is needed by 2050, relative to 1990 levels.

Our country s fleet of fossil fueled power plants is the single largest source of carbon pollution in the U.S., accounting for over one-third of total carbon emissions, according to the Environmental Protection Agency (EPA.) Plans for increased regulation of GHG emissions are already underway, posing regulatory risk to the company. President Obama committed to reduce emissions by 26-28

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percent by 2025. The EPA s Clean Power Plan would strengthen emissions standards for power plants, seeking an overall 30 percent reduction of CO2 emissions by 2030. With the fourth highest power generation from burning coal in the country and the third highest level of carbon emissions of U.S. power producers, compliance with this rule will likely require substantial adjustments to Southern facilities, entailing emissions reductions, increased use of renewable energy and deployment of energy efficiency. Meanwhile, Southern has publicly stated that it does not support this regulation.

Southern Company has made significant investments in renewable energy, efficiencies, and a more diversified energy mix. Setting clear proactive goals to manage greenhouse gas emissions at Southern Company and its operating companies would enable the Company to manage climate risk and align with a growing global commitment to contain emissions. Sixty percent of Fortune 100 companies have set GHG reduction goals or renewable energy targets. Southern lags behind peers including American Electric Power, CMS Energy, Exelon and Duke Energy which have set absolute and/or intensity carbon reduction goals. NRG Energy announced its aim to reduce its carbon emissions 50 percent by 2030 and 90 percent by 2050.

SUPPORTING STATEMENT:

A disciplined business strategy to cut emissions includes setting goals, striving to meet them and reporting on progress. Leading practices for electric utilities to manage carbon across the enterprise include pursuing all cost-effective energy efficiency opportunities, deploying large-scale and distributed renewable energy, utilizing smart grid technologies for consumer and system benefit, and serving as a systems integrator providing services to meet varying customer needs; and conducting robust and transparent resource planning. Two commonly used options for setting GHG targets are GHG intensity or absolute targets. Absolute GHG reduction goals compare total GHG emissions in the goal year to those in a base year.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ITEM NO. 7 FOR THE FOLLOWING REASONS:

The Board of Directors does not believe it is in the best interests of the Company or its stockholders at this time to establish voluntary, absolute quantitative goals for reducing total greenhouse gas (GHG) emissions from the Southern Company system s operations. Independently establishing these types of goals would not add value to the Company s already robust research, development, and deployment efforts relating to new technology to reduce GHG emissions, would be premature given the Environmental Protection Agency s (EPA) proposed regulations relating to GHG emissions from new and existing sources, and would not be an efficient use of additional Company resources given the ongoing reporting and significant policy engagement by the Company in this area.

The Southern Company system is committed to a diverse energy mix. With a strong base of natural gas, coal, nuclear, hydro, and growing renewable generating capacity, the Southern Company system s fleet is flexible, allowing it to choose the most cost effective fuel source to best serve customers with clean, safe, reliable, and affordable energy. The Southern Company system is dedicated to a full portfolio of resources for the United States energy future twenty-first century coal, natural gas, renewables, new nuclear, and energy efficiency.

Currently, the EPA is in the process of promulgating carbon dioxide regulations that will affect new, existing, and modified and reconstructed power plants. Final emission standards for new sources and for modified and reconstructed sources and final emission reduction guidelines for existing sources are expected this year from the

EPA. Independently establishing reduction goals without the benefit of these final rules is premature. Even absent regulations, the Southern Company system s GHG emissions in 2014 were almost 20% lower than 2005 levels.

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The Southern Company system is a leader in the industry in developing technologies to reduce GHG emissions in the generation of electric energy and has committed substantial financial and human resources to research, develop, and deploy such technologies. This leadership is best evidenced by the Southern Company system s efforts to develop carbon capture and storage. The Southern Company system was selected by the U.S. Department of Energy (DOE) to manage and operate the DOE s National Carbon Capture Center in Alabama, a focal point of national efforts to reduce GHG emissions from coal-based power plants through technological innovation. Additionally, the Company has joined the DOE and other partners to demonstrate carbon capture and storage at a coal-based power plant in Alabama. The Company and its partners have developed an advanced coal gasification technology known as Transport Integrated Gasification (TRIG™) designed to produce less carbon dioxide emissions than the current fleet of existing coal plants. The Company s subsidiary, Mississippi Power, is constructing the Kemper IGCC using TRIG™ technology, which is designed to include the capture and sequestration (via enhanced oil recovery) of at least 65 percent of the carbon dioxide produced by the Kemper IGCC during operations.

Additionally, as nuclear power re-emerges as a viable way to meet new demand for electricity, with the added benefit of no emissions of GHG, Southern Company, through its subsidiary Georgia Power, is leading the nation s nuclear energy renaissance with the construction of two new nuclear units at Plant Vogtle.

The Company has created a number of reports disclosing its actions related to GHG and other emissions. In 2006, the Company s long-standing Environmental Progress Reports evolved into its *Corporate Responsibility Report*, which includes data on emissions and actions being undertaken to address those emissions. Additionally, the Company has also published for a number of years its climate and carbon disclosure reports, which describe specific current and long-term activities to address GHG emissions. The reports are updated on an annual basis. These reports are available either through the Company s external website at http://www.southerncompany.com/what-doing/corporate-responsibility/home.cshtml or by contacting Melissa K. Caen, Corporate Secretary, Southern Company, 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308 and requesting a copy.

For a number of years, the Company also has actively engaged its stakeholders regarding environmental matters affecting the Southern Company system. Since 2011, the Company has held environmental stakeholder forums, webinars, calls, and meetings covering a range of topics from regulatory and policy issues and system risk and planning to renewables, energy efficiency, and GHG issues.

In summary, the Board of Directors does not believe it is in the best interests of the Company or its stockholders to independently establish at this time voluntary, absolute quantitative goals for reducing total GHG emissions from the Southern Company system s operations due to (1) the Southern Company system s already robust research, development, and deployment efforts relating to new technology to reduce GHG emissions, (2) the EPA s pending regulations governing GHG emissions from new and existing sources, which are not yet finalized, and (3) the Company s ongoing practice of reporting emissions data, emission reduction results, investment, and significant policy engagement. A separate report as requested in the proposal regarding plans to achieve such goals would not be an efficient use of additional Company resources or add value to the Company s current efforts in this area.

The vote needed to pass the proponents resolution is the affirmative vote of a majority of the votes cast.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ITEM NO. 7.

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OTHER INFORMATION

FREQUENTLY ASKED QUESTIONS

Q: When will the Proxy Statement be mailed?

A: The Proxy Statement will be mailed on or about April 10, 2015.

Q: Who is entitled to vote?

A: All stockholders of record at the close of business on the record date of March 30, 2015 may vote.

Q: How do I give voting instructions?

A: You may attend the meeting and give instructions in person or give instructions by internet, by phone, or by mail. Information for giving instructions is on the form of proxy and trustee voting instruction form (proxy form). For those investors whose shares are held by a broker, bank, or other nominee, you must complete and return the voting instruction form provided by your broker, bank, or nominee in order to instruct your broker, bank, or nominee on how to vote. The Proxies, named on the enclosed proxy form, will vote all properly executed proxies that are delivered pursuant to this solicitation and not subsequently revoked in accordance with the instructions given by you.

Q: Why is my vote important?

A: It is the right of every investor to vote on certain matters that affect the Company.

Q: Can I change my vote?

A: Yes. If you are a holder of record, you may revoke your proxy by submitting a subsequent proxy, or by written request received by the Company s Corporate Secretary prior to the meeting, or by attending the meeting and voting your shares. If your shares are held through a broker, bank, or other nominee, you must follow the instructions of your broker, bank, or other nominee to revoke your voting instructions.

Q: How are votes counted?

A: Each share counts as one vote. A quorum is required to transact business at the 2015 Annual Meeting. Stockholders of record holding shares of stock constituting a majority of the shares entitled to be cast shall constitute a quorum. Abstentions that are marked on the proxy form and broker non-votes are included for the purpose of determining a quorum, but shares that otherwise are not voted are not counted toward a quorum. Neither abstentions, broker non-votes, nor shares that otherwise are not voted are counted for or against each of the matters being considered at the 2015 Annual Meeting and thus will not affect the outcome of the vote for these items, except that abstentions will have the same effect as votes against Item No. 3.

Q: What are broker non-votes?

A: Broker non-votes occur on a matter up for vote when a broker, bank, or other holder of shares you own in street name is not permitted to vote on that particular matter without instructions from you, you do not give such instructions, and the broker, bank, or other nominee indicates on its proxy form, or otherwise notifies the Company, that it does not have authority to vote its shares on that matter. Whether a broker has authority to vote its shares on uninstructed matters is determined by NYSE rules.

Q: What does it mean if I get more than one proxy form?

A: You will receive a proxy form for each account that you have. Please vote proxies for all accounts to ensure that all of your shares are voted. If you wish to consolidate multiple registered accounts, please contact Shareowner Services at Computershare Inc. at (800) 554-7626.

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Q: Can the Proxy Statement be accessed from the internet?

A: Yes. You can access the Company s website at **http://investor.southerncompany.com/proxy** to view the Proxy Statement.

Q: How do I attend the 2015 Annual Meeting in person?

A: All attendees need to bring photo identification, such as a driver s license, to gain admission to the 2015 Annual Meeting. If you are a holder of record, the top half of your proxy card is your admission ticket. If you hold your shares in street name, you will need proof of ownership to be admitted to the meeting. Examples of proof of ownership are a recent brokerage statement or a letter from your bank or broker. If you want to vote your shares held in street name, you must get a legal proxy in your name from the broker, bank, or other nominee that holds your shares. Please note that cameras, sound or video recording equipment, cellular telephones, smartphones or other similar equipment, and electronic devices are not permitted to be used during the 2015 Annual Meeting.

Q: Does the Company offer electronic delivery of proxy materials?

A: Yes. Most stockholders can elect to receive an email that will provide an electronic link to the Proxy Statement, which includes the 2014 Annual Report as an appendix. Opting to receive your proxy materials on-line will save the Company the cost of producing and mailing documents and also will give you an electronic link to the proxy voting site.

You may sign up for electronic delivery when you vote your proxy via the internet or by visiting www.icsdelivery.com/so. Once you enroll for electronic delivery, you will receive proxy materials electronically as long as your account remains active or until you cancel your enrollment. If you consent to electronic access, you will be responsible for your usual internet-related charges (e.g., on-line fees and telephone charges) in connection with electronic viewing and

printing of the Proxy Statement, which includes the 2014 Annual Report as an appendix. The Company will continue to distribute printed materials to stockholders who do not consent to access these materials electronically.

Q: What is householding?

A: Stockholders sharing a single address may receive only one copy of the Proxy Statement, which includes the 2014 Annual Report as an appendix, unless the transfer agent, broker, bank, or other nominee has received contrary instructions from any owner at that address. This practice known as householding is designed to reduce printing and mailing costs. If a stockholder of record would like to either participate or cancel participation in householding, he or she may contact Shareowner Services at Computershare Inc. at (800) 554-7626 or by mail at The Southern Company, c/o Computershare, P.O. Box 30170, College Station, TX 77842-3170. If you own indirectly through a broker, bank, or other nominee, please contact your financial institution.

Q: What is the Board s recommendation for the proposals?

A: The Board of Directors recommends votes FOR each of Item Nos. 1, 2, 3, 4, and 5 and votes AGAINST Item Nos. 6 and 7 in this Proxy Statement.

Q: How many votes are needed to approve each of the items of business?

A: The affirmative vote of a majority of the votes cast is required for approval of each of Item Nos. 1, 2, 4, 5, 6, and 7. For Item No. 3, the affirmative vote of a majority of the shares represented in person or by proxy and entitled to vote at the 2015 Annual Meeting is required for approval.

Q: When are stockholder proposals due for the 2016 Annual Meeting of Stockholders?

A: The deadline for the receipt of stockholder proposals to be considered for inclusion in the Company s proxy materials for the 2016

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Annual Meeting of Stockholders is December 12, 2015. Proposals must be submitted in writing to Melissa K. Caen, Corporate Secretary, Southern Company, 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308. Additionally, the proxy solicited by the Board of Directors for next year s meeting will confer discretionary authority to vote on any stockholder proposal presented at that meeting that is not included in the Company s proxy materials unless the Company is provided written notice of such proposal no later than February 25, 2016.

Q: Who is soliciting these proxies and who pays the expense of such solicitations?

A: These proxies are being solicited on behalf of the Company s Board of Directors. The Company pays the cost of soliciting proxies. The Company has retained Georgeson Inc. to assist with the solicitation of proxies for a fee of $12,500, plus additional fees for telephone and other solicitation of proxies or other services, if needed, and reimbursement of out-of-pocket expenses. The officers or other employees of the Company or its subsidiaries may solicit proxies to have a larger representation at the meeting. None of these officers or other employees of the Company will receive any additional compensation for these services. Upon request, the Company will reimburse brokerage houses and other custodians, nominees, and fiduciaries for their reasonable out-of-pocket expenses for forwarding solicitation material to the beneficial owners of the Company s common stock.

Section 16(a) Beneficial Ownership Reporting Compliance

Based on the Company s review of Forms 3, 4, and 5 and amendments thereto in the Company s possession and written representations furnished to the Company, the Company believes that no reporting person of the Company failed to file, on a timely basis, the reports required by Section 16(a) of the Securities Exchange Act of 1934, as amended, except for an inadvertent late filing of a Form 4 to disclose one transaction by David J. Grain.

Certain Relationships and Related Transactions

Mr. Donald M. James, a Director of the Company, served as the Chief Executive Officer of Vulcan Materials Company from 1997 to 2014. During 2014, subsidiaries of the Company purchased approximately $2.1 million of goods and services from Vulcan Materials Company and its affiliates, primarily related to on-going construction projects.

Mr. E. Jenner Wood III, a Director of the Company, is Chairman, President, and Chief Executive Officer of the Atlanta Division of SunTrust Bank and Executive Vice President of SunTrust Banks, Inc. During 2014, subsidiaries of the Company made payments of approximately $1.1 million to certain subsidiaries of SunTrust Banks, Inc., substantially related to aircraft leases.

During 2014, certain subsidiaries of SunTrust Banks, Inc. also furnished a number of regular banking services in the ordinary course of business to the Company and its subsidiaries and served as an underwriter for certain securities offerings of the Company and its subsidiaries for which $1.7 million was received by these certain subsidiaries of SunTrust Banks, Inc. The Company and its subsidiaries intend to maintain normal banking relations with SunTrust Banks, Inc. and its subsidiaries in the future.

The Company does not have a written policy pertaining solely to the approval or ratification of related party transactions. The Company has a Code of Ethics as well as a Contract Manual and other formal written procurement policies and procedures that guide the purchase of goods and services, including requiring competitive bids for most transactions above $10,000 or approval based on documented business needs for sole sourcing arrangements. The approval and ratification of any related party transactions would be subject to these written policies and procedures which include a determination of the need for the goods and services; preparation and evaluation of requests for proposals by supply chain management; the writing of contracts; controls and guidance regarding the evaluation of the proposals; and negotiation of contract terms and conditions. As appropriate, these

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contracts are also reviewed by individuals in the legal, accounting, and/or risk management/services departments prior to being approved by the responsible individual. The responsible individual will vary depending on the

department requiring the goods and services, the dollar amount of the contract, and the appropriate individual within that department who has the authority to approve a contract of the applicable dollar amount.

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APPENDIX A

OUTSIDE DIRECTORS STOCK PLAN

OUTSIDE DIRECTORS STOCK PLAN FOR

THE SOUTHERN COMPANY AND ITS SUBSIDIARIES

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Outside Directors Stock Plan for The Southern Company and its Subsidiaries

Article I Purpose and Adoption of Plan

1.1 Adoption. The Southern Company hereby adopts the Outside Directors Stock Plan for The Southern Company and Its Subsidiaries, effective June 1, 2015 subject to (a) the approval of the Plan by the stockholders of the Company at the annual meeting thereof to be held on May 27, 2015 and (b) registration of the Stock to be issued pursuant to the Plan.

1.2 Purpose. The Plan is designed to more closely align the interests of Directors with the interests of the stockholders of the Company through ownership of Stock.

Article II Definitions

2.1 Affiliated Employer shall mean any corporation which is a member of the controlled group of corporations of which the Company is the common parent corporation.

2.2 Board of Directors shall mean either the Southern Board or a System Company Board, as applicable to a Director.

2.3 Commission shall mean the Securities and Exchange Commission.

2.4 Company shall mean The Southern Company.

2.5 Company Board shall mean the Board of Directors of The Southern Company.

2.6 Director shall mean any person who is not an active employee of the Company or a System Company and who either serves on the Company Board or a System Company Board.

2.7 Effective Date shall mean June 1, 2015.

2.8 Exchange Act shall mean the Securities Exchange Act of 1934, as amended.

2.9 Market Value shall mean the following:

(a) With respect to Stock that is issued by the Company, the closing price of the Stock, as published in the Wall Street Journal in its report of New York Stock Exchange composite transactions, on the date such Market Value is to be determined, as specified herein.

(b) With respect to Stock that is purchased on the open market, the actual purchase price paid for the Stock on the date purchased.

2.10 Participant shall mean each Director who meets the requirements of Section 3.1 of the Plan.

2.11 Plan shall mean the Outside Directors Stock Plan for The Southern Company and Its Subsidiaries, as amended from time to time.

2.12 Plan Administrator shall mean the Governance Committee of the Company Board.

2.13 Plan Year shall mean the calendar year.

2.14 Retainer Fee shall mean the annual rate of the fees paid to a Director as determined by the Board of Directors from time-to-time, but excluding reimbursements for expenses and any additional fees or compensation for (a) attendance at the meetings of the Board of Directors or any committee, (b) service on a committee and (c) service at the request of the Board of Directors or a committee.

2.15 Stock shall mean the Company s common stock, par value $5.00 per share.

2.16 System Company shall mean any Affiliated Employer which adopted the Outside Directors Stock Plan for Directors of The Southern Company and its Subsidiaries that was effective May 26, 2004 and any additional Affiliated Employer the Company Board may from time to time determine to bring under the Plan and which shall adopt the Plan. The System Companies that have adopted the Plan are listed in Schedule A, attached hereto, as such Schedule may be amended from time to time.

2.17 System Company Board shall mean the Board of Directors of a System Company.

The masculine pronoun shall be construed to include the feminine pronoun and the singular shall include the plural, where the context so requires.

Article III Eligibility

3.1 Eligibility Requirements.

(a) Except as provided in Subsection (b), each Director shall become a Participant in the Plan on the first date such Director serves on the Board of Directors.

(b) For purposes of the 2015 Plan Year, a Director who is serving on a Board of Directors as of the Effective Date shall become a Participant in the Plan on the Effective Date.

Article IV Form and Time of Benefit Distributions

4.1 Stock Grant. Each Participant shall receive a portion of his Retainer Fee in Stock. Any remainder of such Retainer Fee and any meeting attendance fees, in increments elected by the Director in accordance with Section 4.2, may be paid in cash or in Stock. The portion of the Retainer Fee required to be paid in Stock pursuant to this Section 4.1 may be denominated in dollars or a fixed number of shares of Stock and shall be stated in Schedule B, attached hereto, as such Schedule shall be amended from time to time by the Board of Directors.

4.2 Election to Determine Percentage or Amount of Compensation to be Paid in Stock. Prior to the beginning of each Plan Year, each Participant shall have an opportunity to elect to have the non-Stock portion of his Retainer Fee paid in cash or Stock of the Company, or a combination thereof. Each Participant also shall have an opportunity to elect to have a portion of any meeting attendance fees paid in Stock. Nothing contained in this Section 4.2 shall be interpreted in such a manner as would disqualify the Plan from treatment as a formula plan under Rule 16b-3, as promulgated by the Commission under the Exchange Act, as that rule may be amended from time to time.

4.3 Amount of Stock Compensation Denominated in Dollars. For Stock compensation that is denominated in dollars, the number of shares of Stock due to a Participant, including any fractional shares, shall be determined by dividing the prescribed dollar amount by the Market Value on the compensation payment date.

4.4 Deferral of Stock Compensation. Any portion of the Retainer Fee that is required to be paid in Stock pursuant to Section 4.1 may be deferred in accordance with the terms of the Deferred Compensation Plan maintained by the Company or System Company for its Directors. Any other Director compensation that a participant may elect to receive in Stock under the Plan may be similarly deferred.

4.5 Death Benefits. No grants of Stock shall be made to any beneficiary of a Participant following a Participant s death.

Article V Administration of Plan

5.1 Administrator. The general administration of the Plan shall be the responsibility of the Plan Administrator.

5.2 Powers. The Plan Administrator shall administer the Plan

(a) The Plan Administrator shall administer the Plan in accordance with its terms and shall have all powers necessary to carry out the provisions of the Plan. It shall interpret the Plan and shall have the discretion to determine all questions arising in the administration, interpretation and application of the Plan, including any ambiguities contained herein or any questions of fact. Any such determination by it shall be conclusive and binding on all persons. It may adopt such procedures as it deems desirable for the conduct of its affairs. It may appoint such accountants, counsel, actuaries, specialists and other persons as it deems necessary or desirable in connection with the administration of the Plan, and shall be the agent for the service of process.

(b) The Plan Administrator may delegate to such officers, employees or departments of the Company or an affiliate of the Company, such authority, duties and responsibilities of the Plan Administrator as it, in its sole discretion, considers necessary or appropriate for the proper and efficient operation of the Plan, including, without limitation, interpretation of the Plan and establishment of procedures for administration of the Plan.

5.3 Indemnification. The System Companies and the Company shall indemnify the Plan Administrator against any and all claims, losses, damages, expenses and liability arising from any action or failure to act, except when the same is finally judicially determined to be due to gross negligence or willful misconduct. The System Companies and the Company may purchase at their own expense sufficient liability insurance for the Plan Administrator to cover any and all claims, losses, damages and expenses arising from any action or failure to act in connection with the execution of the duties as Plan Administrator.

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Article VI Miscellaneous

6.1 Assignment. Neither the Participant nor his legal representative shall have any rights to sell, assign, transfer or otherwise convey the right to receive the payment of any benefit due hereunder, which payment and the right thereto are expressly declared to be nonassignable and nontransferable. Any attempt to assign or transfer the right to payment under the Plan shall be null and void and of no effect.

6.2 Amendment and Termination. The Plan may be wholly or partially amended or otherwise modified, suspended or terminated at any time by the Company Board or by its Governance Committee with the approval of the Company Board, upon execution of a duly authorized written document; provided, however, that, without the approval of the stockholders of the Company entitled to vote thereon, no amendment may be made which would, absent such stockholder approval, disqualify the Plan for coverage under Rule 16b-3, as promulgated by the Commission under the Exchange Act, as that rule may be amended from time to time. Notwithstanding the foregoing, no such amendment or termination shall impair any rights to payments to which a Participant may be entitled prior to the effective date of such amendment or termination.

6.3 No Guarantee of Continued or Future Service on a Board of Directors. Participation hereunder shall not be construed as creating a right in any Director to continued service or future service on the Board of Directors. Participation hereunder does not constitute an employment contract between any Director and any System Company or the Company as the case may be.

6.4 Construction. This Plan shall be construed in accordance with and governed by the laws of the State of Georgia, to the extent such laws are not otherwise superseded by the laws of the United States.

IN WITNESS WHEREOF, the Company Board, through its duly authorized officers, has adopted this Outside Directors Stock Plan for The Southern Company and Its Subsidiaries this 9th day of February, 2015, to be effective as provided herein.

THE SOUTHERN COMPANY:

By:
Its: Secretary

Attest:

By:
Its: Assistant Secretary

Schedule A

The System Companies as of May 27, 2015 are:

Alabama Power Company

Georgia Power Company

Gulf Power Company

Mississippi Power Company

Schedule B

As of June 1, 2015

The portion of a Participant s Retainer Fee required to be distributed in Stock shall be determined in accordance with the following schedule:

Company	Dollar Amount of Required Stock Distribution
Southern Company	$105,000
Alabama Power Company	$30,000
Georgia Power Company	$30,000
Gulf Power Company	$19,500
Mississippi Power Company	$19,500

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APPENDIX B

PROPOSED AMENDMENT TO SECTION 46 OF THE COMPANY S BY-LAWS

The text of the proposed amendment to Section 46 of the Company s By-Laws, marked to show changes to the current Section 46, is set forth as follows:

46. The By-Laws of the Corporation may be altered, amended or repealed (a) at any meeting of the Board of Directors by the vote of a majority of the entire Board then in office, or (b) by the vote of the holders of a majority of that part of the capital stock of the Corporation having voting powers which is represented in person or by proxy at any annual meeting of stockholders or at any special meeting called for that purpose (provided that a lawful quorum of stockholders be there represented in person or by proxy), or (c) without a meeting by the written consent of the holders of ~~all of~~ not less than the minimum number of the issued and outstanding shares of capital stock of the Corporation having voting powers that would be necessary to take such action at a meeting at which all shares entitled to vote thereon were present and voted; provided, however, that the Board of Directors shall not have power to alter, amend or repeal the provisions of Sections 5, 44 or 46 of the By-Laws and provided, further, that an alteration, amendment or repeal of any other provision of the By-Laws by the Board of Directors shall cease to be effective unless submitted to and ratified or approved at the next annual or special meeting at which a lawful quorum of stockholders is represented in person or by proxy by the vote of the holders of a majority of that part of the capital stock of the Corporation having voting powers which is represented in person or by proxy at such meeting.

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APPENDIX C

Policy on Engagement of the Independent Auditor for Audit and Non-Audit Services

A. Southern Company (including its subsidiaries) will not engage the independent auditor to perform any services that are prohibited by the Sarbanes-Oxley Act of 2002. It shall further be the policy of the Company not to retain the independent auditor for non-audit services unless there is a compelling reason to do so and such retention is otherwise pre-approved consistent with this policy. Non-audit services that are prohibited include:

1. Bookkeeping and other services related to the preparation of accounting records or financial statements of the Company or its subsidiaries.

2. Financial information systems design and implementation.

3. Appraisal or valuation services, fairness opinions, or contribution-in-kind reports.

4. Actuarial services.

5. Internal audit outsourcing services.

6. Management functions or human resources.

7. Broker or dealer, investment adviser, or investment banking services.

8. Legal services or expert services unrelated to financial statement audits.

9. Any other service that the Public Company Accounting Oversight Board determines, by regulation, is impermissible.

B. Effective January 1, 2003, officers of the Company (including its subsidiaries) may not engage the independent auditor to perform any personal services, such as personal financial planning or personal income tax services.

C. All audit services (including providing comfort letters and consents in connection with securities issuances) and permissible non-audit services provided by the independent auditor must be pre-approved by the Southern Company Audit Committee.

D. Under this Policy, the Audit Committee s approval of the independent auditor s annual arrangements letter shall constitute pre-approval for all services covered in the letter.

E. By adopting this Policy, the Audit Committee hereby pre-approves the engagement of the independent auditor to provide services related to the issuance of comfort letters and consents required for securities sales by the Company and its subsidiaries and services related to consultation on routine accounting and tax matters. The actual amounts expended for such services each calendar quarter shall be reported to the Committee at a subsequent Committee meeting.

F. The Audit Committee also delegates to its Chairman the authority to grant pre-approvals for the engagement of the independent auditor to provide any permissible service up to a limit of $50,000 per engagement. Any engagements pre-approved by the Chairman shall be presented to the full Committee at its next scheduled regular meeting.

G. The Southern Company Comptroller shall establish processes and procedures to carry out this Policy.

Approved by the Southern Company Audit Committee

December 9, 2002

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APPENDIX D

SOUTHERN COMPANY

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SOUTHERN COMPANY COMMON STOCK AND DIVIDEND INFORMATION

The common stock of Southern Company is listed and traded on the New York Stock Exchange. The common stock is also traded on regional exchanges across the United States. The high and low stock prices as reported on the New York Stock Exchange for each quarter of the past two years were as follows:

	High	Low	Dividend
2014			
First Quarter	$ 44.00	$ 40.27	$ 0.5075
Second Quarter	46.81	42.55	0.5250
Third Quarter	45.47	41.87	0.5250
Fourth Quarter	51.28	43.55	0.5250
2013			
First Quarter	$ 46.95	$ 42.82	$ 0.4900
Second Quarter	48.74	42.32	0.5075
Third Quarter	45.75	40.63	0.5075
Fourth Quarter	42.94	40.03	0.5075

FIVE-YEAR CUMULATIVE PERFORMANCE GRAPH

This performance graph compares the cumulative total shareholder return on the Company s common stock with the Standard & Poor s Electric Utility Index and the Standard & Poor s 500 index for the past five years. The graph assumes that $100 was invested on December 31, 2009 in the Company s common stock and each of the above indices and that all dividends were reinvested. The stockholder return shown below for the five-year historical period may not be indicative of future performance.

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TWENTY-YEAR CUMULATIVE PERFORMANCE GRAPH

This performance graph compares the cumulative total shareholder return on the Company s common stock with the Standard & Poor s Electric Utility Index and the Standard & Poor s 500 index for the past 20 years. The graph assumes that $100 was invested on December 31, 1994 in the Company s common stock and each of the above indices and that all dividends were reinvested. The distribution of shares of Mirant Corporation stock to the Company s stockholders in 2001 is treated as a special dividend for purposes of calculating the Company s shareholder return. The stockholder return shown below for the twenty-year historical period may not be indicative of future performance.

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MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Southern Company and Subsidiary Companies 2014 Annual Report

The management of The Southern Company (Southern 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 Southern 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 Southern Company s internal control over financial reporting was effective as of December 31, 2014.

Deloitte & Touche LLP, an independent registered public accounting firm, as auditors of Southern Company s financial statements, has issued an attestation report on the effectiveness of Southern Company s internal control over financial reporting as of December 31, 2014. Deloitte & Touche LLP s report on Southern Company s internal control over financial reporting is included herein.

Thomas A. Fanning
Chairman, President, and Chief Executive Officer

Art P. Beattie
Executive Vice President and Chief Financial Officer

March 2, 2015

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

The Southern Company

We have audited the accompanying consolidated balance sheets and consolidated statements of capitalization of The Southern Company and Subsidiary Companies (the Company) as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, stockholders equity, and cash flows for each of the three years in the period ended December 31, 2014. We also have audited the Company s internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company s management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report on Internal Control Over Financial Reporting (page D-1). Our responsibility is to express an opinion on these financial statements and an opinion on the Company s internal control over financial reporting 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 and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included 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, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements (pages D-36 to D-101) referred to above present fairly, in all material respects, the financial position of Southern Company and Subsidiary Companies as of December 31, 2014 and 2013, and the results of their operations and their 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. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on the criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Atlanta, Georgia
March 2, 2015

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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
2013 ARP	Alternative Rate Plan approved by the Georgia PSC for Georgia Power for the years 2014 through 2016
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
EPA	U.S. Environmental Protection Agency
FERC	Federal Energy Regulatory Commission
FFB	Federal Financing Bank
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
Mississippi Power	Mississippi Power Company
mmBtu	Million British thermal units
Moody s	Moody s Investors Service, Inc.
MPUS	Mississippi Public Utilities Staff
MW	Megawatt
NCCR	Georgia Power s Nuclear Construction Cost Recovery
NDR	Alabama Power s Natural Disaster Reserve
NRC	U.S. Nuclear Regulatory Commission
OCI	Other comprehensive income
Plant Vogtle Units 3 and 4	Two new nuclear generating units under construction at Plant Vogtle
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
Rate CNP	Alabama Power s Rate Certificated New Plant
Rate CNP Environmental	Alabama Power s Rate Certificated New Plant Environmental
Rate CNP PPA	Alabama Power s Rate Certificated New Plant Power Purchase Agreement
Rate ECR	Alabama Power s rate energy cost recovery
Rate NDR	Alabama Power s natural disaster reserve rate
Rate RSE	Alabama Power s rate stabilization and equalization plan
ROE	Return on equity
S&P	Standard and Poor s Rating Services, a division of The McGraw Hill Companies, Inc.
SCS	Southern Company Services, Inc. (the Southern Company system service company)
SEC	U.S. Securities and Exchange Commission
SEGCO	Southern Electric Generating Company

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DEFINITIONS (continued)

Term	Meaning
SMEPA	South Mississippi Electric Power Association
Southern Company system	The Southern Company, the traditional operating companies, Southern Power, SEGCO, Southern Nuclear, SCS, SouthernLINC Wireless, and other subsidiaries
SouthernLINC Wireless	Southern Communications Services, Inc.
Southern Nuclear	Southern Nuclear Operating Company, Inc.
Southern Power	Southern Power Company and its subsidiaries
traditional operating companies	Alabama Power, Georgia Power, Gulf Power, and Mississippi Power

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

Southern Company and Subsidiary Companies 2014 Annual Report

OVERVIEW

Business Activities

The Southern Company (Southern Company or the Company) is a holding company that owns all of the common stock of the Southern Company system, which consists of the traditional operating companies, Southern Power, and other direct and indirect subsidiaries. The primary business of the Southern Company system is electricity sales by the traditional operating companies and Southern Power. The four traditional operating companies are vertically integrated utilities providing electric service in four Southeastern states. Southern Power constructs, acquires, owns, and manages generation assets, including renewable energy projects, and sells electricity at market-based rates in the wholesale market.

Many factors affect the opportunities, challenges, and risks of the Southern Company system s electricity business. These factors include the traditional operating companies ability to maintain a constructive regulatory environment, to maintain and grow energy sales, and to effectively manage and secure timely recovery of costs. These costs include those related to projected long-term demand growth, increasingly stringent environmental standards, reliability, fuel, capital expenditures, including new plants, and restoration following major storms. Subsidiaries of Southern Company are constructing Plant Vogtle Units 3 and 4 and the Kemper IGCC. Georgia Power has a 45.7% ownership interest in Plant Vogtle Units 3 and 4, each with approximately 1,100 MWs, and Mississippi Power is ultimately expected to hold an 85% ownership interest in the 582-MW Kemper IGCC.

Each of the traditional operating companies has various regulatory mechanisms that operate to address cost recovery. Effectively operating pursuant to these regulatory mechanisms and appropriately balancing required costs and capital expenditures with customer prices will continue to challenge the Southern Company system for the foreseeable future. See Note 3 to the financial statements under Retail Regulatory Matters and Integrated Coal Gasification Combined Cycle for additional information.

Another major factor is the profitability of the competitive market-based wholesale generating business. Southern Power s strategy is to acquire, construct, and sell power plants, including renewable energy projects, and to enter into PPAs primarily with investor-owned utilities, independent power producers, municipalities, and electric cooperatives.

Southern Company s other business activities include investments in leveraged lease projects and telecommunications. Management continues to evaluate the contribution of each of these activities to total shareholder return and may pursue acquisitions and dispositions accordingly.

Key Performance Indicators

In striving to achieve superior risk-adjusted returns while providing cost-effective energy to more than four million customers, the Southern Company system continues to focus on several key performance indicators. These indicators include customer satisfaction, plant availability, system reliability, execution of major construction projects, and earnings per share (EPS). Southern 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 and reliability indicators to evaluate the results of the Southern Company system.

Peak season equivalent forced outage rate (Peak Season EFOR) is an indicator of fossil/hydro 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 Southern Company system s fossil/hydro 2014 Peak Season EFOR 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 Southern Company system s performance for 2014 was better than the target for these reliability measures. Primarily as a result of charges for estimated probable losses related to construction of the Kemper IGCC, Southern Company s EPS for 2014 did not meet the target on a GAAP basis. See RESULTS OF OPERATIONS Estimated Loss on Kemper IGCC and Note 3 to the financial statements under Integrated Coal Gasification Combined Cycle for additional information.

Excluding the charges for estimated probable losses related to construction of the Kemper IGCC and the 2015 Mississippi Supreme Court decision, Southern Company s 2014 results compared with its targets for some of these key indicators are reflected in the following chart:

Key Performance Indicator	**2014 Target Performance**	**2014 Actual Performance**
System Customer Satisfaction	**Top quartile in customer surveys**	**Top quartile**
Peak Season System EFOR fossil/hydro	**5.51% or less**	**1.93%**
Basic EPS As Reported	**$2.72-$2.80**	**$2.19**
Kemper IGCC Impacts		**$0.61**
EPS, excluding items*		**$2.80**

* Does not reflect EPS as calculated in accordance with GAAP. The non-GAAP measure of EPS, excluding estimated probable losses relating to Mississippi Power s construction of the Kemper IGCC and the 2015 Mississippi Supreme Court decision, is calculated by excluding from EPS, as

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

determined in accordance with GAAP, the following items: (1) estimated probable losses of $536 million after-tax, or $0.59 per share, relating to Mississippi Power s construction of the Kemper IGCC and (2) an aggregate of $17 million after-tax, or $0.02 per share, relating to the reversal of previously recognized revenues recorded in 2014 and 2013 and the recognition of carrying costs associated with the 2015 Mississippi Supreme Court decision which reversed the Mississippi PSC s March 2013 rate order related to the Kemper IGCC. The estimated probable losses relating to the construction of the Kemper IGCC significantly impacted the presentation of EPS in the table above, and any similar charges are items that may occur with uncertain frequency in the future. In addition, neither the estimated probable losses relating to the construction of the Kemper IGCC nor the 2015 Mississippi Supreme Court decision were anticipated or incorporated in the assumptions used to develop the EPS target performance for 2014 reflected in the table above. See RESULTS OF OPERATIONS Estimated Loss on Kemper IGCC and Note 3 to the financial statements under Integrated Coal Gasification Combined Cycle for additional information on the estimated probable losses relating to the Kemper IGCC and the 2015 Mississippi Supreme Court decision. Southern Company management uses the non-GAAP measure of EPS, excluding these items, to evaluate the performance of Southern Company s ongoing business activities and its 2014 performance on a basis consistent with the assumptions used in developing the 2014 performance targets and to compare certain results to prior periods. Southern Company believes this presentation is useful to investors by providing additional information for purposes of evaluating the performance of Southern Company s business activities. This presentation is not meant to be considered a substitute for financial measures prepared in accordance with GAAP.

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

Earnings

Southern Company s net income after dividends on preferred and preference stock of subsidiaries was $2.0 billion in 2014, an increase of $319 million, or 19.4%, from the prior year. The increase was primarily related to an increase in retail revenues due to retail base rate increases, as well as 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. The increase in net income was also the result of lower pre-tax charges of $868 million ($536 million after tax) recorded in 2014 compared to pre-tax charges of $1.2 billion ($729 million after tax) recorded in 2013 for revisions of estimated costs expected to be incurred on Mississippi Power s construction of the Kemper IGCC. These increases were partially offset by increases in non-fuel operations and maintenance expenses.

Southern Company s net income after dividends on preferred and preference stock of subsidiaries was $1.6 billion in 2013, a decrease of $706 million, or 30.0%, from the prior year. The decrease was primarily the result of pre-tax charges of $1.2 billion ($729 million after-tax) for revisions of estimated costs expected to be incurred on Mississippi Power s construction of the Kemper IGCC. Also contributing to the decrease in net income were increases in depreciation and amortization and non-fuel operations and maintenance expenses, partially offset by increases in retail revenues and AFUDC.

Basic EPS was $2.19 in 2014, $1.88 in 2013, and $2.70 in 2012. Diluted EPS, which factors in additional shares related to stock-based compensation, was $2.18 in 2014, $1.87 in 2013, and $2.67 in 2012. EPS for 2014 was negatively impacted by $0.06 per share as a result of an increase in the average shares outstanding. See FINANCIAL CONDITION AND LIQUIDITY Financing Activities herein for additional information.

Dividends

Southern Company has paid dividends on its common stock since 1948. Dividends paid per share of common stock were $2.0825 in 2014, $2.0125 in 2013, and $1.9425 in 2012. In January 2015, Southern Company declared a quarterly dividend of 52.50 cents per share. This is the 269th consecutive quarter that Southern Company has paid a dividend equal to or higher than the previous quarter. For 2014, the actual dividend payout ratio was 95%, while the payout ratio of net income excluding estimated probable losses relating to Mississippi Power s construction of the Kemper IGCC and the 2015 Mississippi Supreme Court decision was 74%.

RESULTS OF OPERATIONS

Discussion of the results of operations is divided into two parts the Southern Company system s primary business of electricity sales and its other business activities.

	Amount		
	2014	2013	2012
		(in millions)	
Electricity business	**$ 1,969**	$ 1,652	$ 2,321
Other business activities	**(6)**	(8)	29
Net Income	**$ 1,963**	$ 1,644	$ 2,350

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Electricity Business

Southern Company s electric utilities generate and sell electricity to retail and wholesale customers in the Southeast.

A condensed statement of income for the electricity business follows:

	Amount 2014	Increase (Decrease) from Prior Year 2014	2013
		(in millions)	
Electric operating revenues	**$ 18,406**	**$ 1,371**	$ 557
Fuel	**6,005**	**495**	453
Purchased power	**672**	**211**	(83)
Other operations and maintenance	**4,259**	**481**	83
Depreciation and amortization	**1,929**	**43**	114
Taxes other than income taxes	**979**	**47**	20
Estimated loss on Kemper IGCC	**868**	**(312)**	1,180
Total electric operating expenses	**14,712**	**965**	1,767
Operating income	**3,694**	**406**	(1,210)
Allowance for equity funds used during construction	**245**	**55**	47
	18		(4)

Interest income					
Interest expense, net of amounts capitalized		**794**		**6**	(32)
Other income (expense), net		**(73)**		**(18)**	2
Income taxes		**1,053**		**118**	(465)
Net income		**2,037**		**319**	(668)
Dividends on preferred and preference stock of subsidiaries		**68**		**2**	1
Net income after dividends on preferred and preference stock of subsidiaries	**$**	**1,969**	**$**	**317**	$ (669)

Electric Operating Revenues

Electric operating revenues for 2014 were $18.4 billion, reflecting a $1.4 billion increase from 2013. Details of electric operating revenues were as follows:

	Amount	
	2014	2013
	(in millions)	
Retail prior year	**$ 14,541**	$ 14,187
Estimated change resulting from		
Rates and pricing	**300**	137
Sales growth (decline)	**35**	(2)
Weather	**236**	(40)
Fuel and other cost recovery	**438**	259
	15,550	14,541

Retail current year		
Wholesale revenues	**2,184**	1,855
Other electric operating revenues	**672**	639
Electric operating revenues	**$ 18,406**	$ 17,035
Percent change	**8.0%**	3.4%

Retail revenues increased $1.0 billion, or 6.9%, in 2014 as compared to the prior year. The significant factors driving this change are shown in the preceding table. The increase in rates and pricing in 2014 was primarily due to increased revenues at Georgia Power related to base tariff increases effective January 1, 2014, as approved by the Georgia PSC in the 2013 ARP, and increases in collections for financing costs related to the construction of Plant Vogtle Units 3 and 4 through the NCCR tariff, as well as higher contributions from market-driven rates from commercial and industrial customers. Also contributing to the increase were increased revenues at Alabama Power associated with Rate CNP Environmental primarily resulting from the inclusion of pre-2005 environmental assets and increased revenues at Gulf Power primarily resulting from a retail base rate increase and an increase in the environmental cost recovery clause rate, both effective January 2014, as approved by the Florida PSC.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Retail revenues increased $354 million, or 2.5%, in 2013 as compared to the prior year. The significant factors driving this change are shown in the preceding table. The increase in rates and pricing in 2013 was primarily due to base tariff increases at Georgia Power effective April 1, 2012 and January 1, 2013, as approved by the Georgia PSC, related to placing new generating units at Plant McDonough-Atkinson in service and collecting financing costs related to the construction of Plant Vogtle Units 3 and 4 through the NCCR tariff, as well as higher contributions from market-driven rates from commercial and industrial customers.

See Note 3 to the financial statements of Southern Company under Retail Regulatory Matters Alabama Power Rate CNP, Georgia Power Rate Plans, and Gulf Power Retail Base Rate Case and Integrated Coal Gasification Combined Cycle Rate Recovery of Kemper IGCC Costs 2015 Mississippi Supreme Court Decision for additional information. Also see Energy Sales below for a discussion of changes in the volume of energy sold, including changes related to sales growth (decline) and weather.

Electric rates for the traditional operating companies 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. The traditional operating companies may also have one or more regulatory mechanisms to recover other costs such as environmental, storm damage, new plants, and PPAs.

Wholesale revenues consist of PPAs with investor-owned utilities and electric cooperatives and short-term opportunity sales. Wholesale revenues from PPAs (other than solar PPAs) have both capacity and energy components. Capacity revenues reflect the recovery of fixed costs and a return on investment. Energy revenues will vary depending on fuel prices, the market prices of wholesale energy compared to 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 energy revenues that are driven by fuel prices are accompanied by an increase or decrease in fuel costs and do not have a significant impact on net income. Wholesale revenues at Mississippi Power include FERC-regulated municipal and rural association sales as well as market-based sales. Short-term opportunity sales are made at market-based rates that generally provide a margin above the Southern Company system s variable cost to produce the energy.

Wholesale revenues from power sales were as follows:

	2014	2013	2012
		(in millions)	
Capacity and other	**$ 974**	$ 971	$ 899
Energy	**1,210**	884	776
	$ 2,184	$ 1,855	$ 1,675

Total

In 2014, wholesale revenues increased $329 million, or 17.7%, as compared to the prior year due to a $326 million increase in energy revenues and a $3 million increase in capacity revenues. The increase in energy revenues was primarily related to increased revenue under existing contracts as well as new solar PPAs and requirements contracts primarily at Southern Power, increased demand resulting from colder weather in the first quarter 2014 as compared to the corresponding period in 2013, and an increase in the average cost of natural gas. The increase in capacity revenues was primarily due to wholesale base rate increases at Mississippi Power, partially offset by a decrease in capacity revenues primarily due to lower customer demand and the expiration of certain requirements contracts at Southern Power.

In 2013, wholesale revenues increased $180 million, or 10.7%, as compared to the prior year due to a $108 million increase in energy revenues and a $72 million increase in capacity revenues. The increase in energy revenues was primarily related to an increase in the average price of energy and new solar contracts served by Southern Power s Plants Campo Verde and Spectrum, which began in 2013, partially offset by a decrease in volume related to milder weather as compared to the prior year. The increase in capacity revenues was primarily due to a new PPA served by Southern Power s Plant Nacogdoches, which began in June 2012, and an increase in capacity revenues under existing PPAs.

Other Electric Revenues

Other electric revenues increased $33 million, or 5.2%, and $23 million, or 3.7%, in 2014 and 2013, respectively, as compared to the prior years. The 2014 increase was primarily due to increases in open access transmission tariff revenues and transmission service revenues primarily at Alabama Power and Georgia Power, an increase in co-generation steam revenues at Alabama Power, increases in outdoor lighting and solar application fee revenues at Georgia Power, as well as an increase in franchise fees at Gulf Power. The 2013 increase in other electric revenues was primarily a result of increases in transmission revenues related to the open access transmission tariff and rents from electric property related to pole attachments.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

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 2014 (in billions)	Total KWH Percent Change 2014	Total KWH Percent Change 2013	Weather-Adjusted Percent Change 2014	Weather-Adjusted Percent Change 2013*
Residential	**53.4**	**5.5%**	0.2%	**%**	(0.3)%
Commercial	**53.2**	**1.3**	(0.9)	**(0.4)**	(0.1)
Industrial	**54.1**	**3.3**	1.5	**3.3**	1.5
Other	**0.9**	**0.9**	(1.8)	**0.7**	(1.9)
Total retail	**161.6**	**3.3**	0.3	**0.9%**	0.4%
Wholesale	**32.8**	**21.7**	(2.2)		
Total energy sales	**194.4**	**6.0%**	(0.1)%		

* In the first quarter 2012, Georgia Power began using new actual advanced meter data to compute unbilled revenues. The weather-adjusted KWH sales variances shown above reflect an adjustment to the estimated allocation of Georgia Power s unbilled January 2012 KWH sales among customer classes that is consistent with the actual allocation in 2013. Without this adjustment, 2013 weather-adjusted residential KWH sales decreased 0.5% as compared to 2012 while 2013 weather-adjusted commercial KWH sales increased 0.2% as compared to 2012.

Changes in retail energy sales are generally the result of changes in electricity usage by customers, changes in weather, and changes in the number of customers. Retail energy sales increased 5.2 billion KWHs in 2014 as compared to the prior year. This increase was primarily the result of 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 and customer growth, partially offset by a decrease in customer usage. The increase in industrial KWH energy sales was primarily due to increased sales in the primary metals, chemicals, paper, non-manufacturing, transportation, and stone, clay, and glass sectors. Weather-adjusted commercial KWH energy sales decreased primarily due to decreased customer usage, partially offset by customer growth. Weather-adjusted residential KWH energy sales were flat compared to the prior year as a result of customer growth offset by decreased customer usage. Household income, one of the primary drivers of residential customer usage, was flat in 2014.

Retail energy sales increased 403 million KWHs in 2013 as compared to the prior year. This increase was primarily the result of customer growth, partially offset by milder weather and a decrease in customer usage. Weather-adjusted residential and commercial energy sales remained relatively flat compared to the prior year with a decrease in customer usage, offset by customer growth. The increase in industrial energy sales was primarily due to increased demand in the paper, primary metals, and stone, clay, and glass sectors.

Wholesale energy sales increased 5.8 billion KWHs in 2014 as compared to the prior year. The increase was primarily related to higher natural gas prices and increased energy sales as a result of 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. Wholesale energy sales decreased 619 million KWHs in 2013 as compared to the prior year. The decrease was primarily related to lower customer demand resulting from milder weather as compared to the prior year.

Fuel and Purchased Power Expenses

Fuel costs constitute the single largest expense for the electric utilities. 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 electric utilities purchase a portion of their electricity needs from the wholesale market.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

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

	2014	**2013**	**2012**
Total generation *(billions of KWHs)*	**191**	179	175
Total purchased power *(billions of KWHs)*	**12**	12	16
Sources of generation *(percent)*			
Coal	**42**	39	38
Nuclear	**16**	17	18
Gas	**39**	40	42
Hydro	**3**	4	2
Cost of fuel, generated *(cents per net KWH)*			
Coal	**3.81**	4.01	3.96
Nuclear	**0.87**	0.87	0.83
Gas	**3.63**	3.29	2.86
Average cost of fuel, generated *(cents per net KWH)*	**3.25**	3.17	2.93
Average cost of purchased power *(cents per net KWH)**	**7.13**	5.27	4.45

* Average cost of purchased power includes fuel purchased by the Southern Company system for tolling agreements where power is generated by the provider.

In 2014, total fuel and purchased power expenses were $6.7 billion, an increase of $706 million, or 11.8%, as compared to the prior year. The increase was primarily the result of a $422 million increase in the volume of KWHs generated primarily due to increased demand resulting from 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 and a $286 million increase in the average cost of fuel and purchased power primarily due to higher natural gas prices.

In 2013, total fuel and purchased power expenses were $6.0 billion, an increase of $370 million, or 6.6%, as compared to the prior year. This increase was primarily the result of a $446 million increase in the average cost of fuel and purchased power primarily due to higher natural gas prices and a $113 million increase in the volume of KWHs generated, partially offset by a $189 million decrease in the volume of KWHs purchased as the marginal cost of generation available was lower than the market cost of available energy.

Fuel and purchased power energy transactions at the traditional operating companies are generally offset by fuel revenues and do not have a significant impact on net income. See FUTURE EARNINGS POTENTIAL Retail Regulatory Matters Retail Fuel Cost Recovery herein for additional information. Fuel expenses incurred under Southern Power s PPAs are generally the responsibility of the counterparties and do not significantly impact net income.

Fuel

In 2014, fuel expense was $6.0 billion, an increase of $495 million, or 9.0%, as compared to the prior year. The increase was primarily due to a 12.7% increase in the volume of KWHs generated by coal, a 10.3% increase in the average cost of natural gas per KWH generated, and a 30.7% decrease in the volume of KWHs generated by hydro facilities resulting from less rainfall, partially offset by a 5.0% decrease in the average cost of coal per KWH generated.

In 2013, fuel expense was $5.5 billion, an increase of $453 million, or 9.0%, as compared to the prior year. The increase was primarily due to a 15.0% increase in the average cost of natural gas per KWH generated, partially offset by a 125.9% increase in the volume of KWHs generated by hydro facilities resulting from greater rainfall.

Purchased Power

In 2014, purchased power expense was $672 million, an increase of $211 million, or 45.8%, as compared to the prior year. The increase was primarily due to a 35.3% increase in the average cost per KWH purchased.

In 2013, purchased power expense was $461 million, a decrease of $83 million, or 15.3%, as compared to the prior year. The decrease was primarily due to a 25.9% decrease in the volume of KWHs purchased as the marginal cost of generation available was lower than the market cost of available energy, partially offset by an 18.4% increase in the average cost per KWH purchased.

Energy purchases will vary depending on demand for energy within the Southern Company system s service territory, the market prices of wholesale energy as compared to the cost of the Southern Company system s generation, and the availability of the Southern Company system s generation.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Other Operations and Maintenance Expenses

Other operations and maintenance expenses increased $481 million, or 12.7%, in 2014 as compared to the prior year. The increase was primarily related to increases of $149 million in scheduled outage costs at generation facilities, $103 million in other generation expenses primarily related to commodity and labor costs, $103 million in transmission and distribution costs primarily related to overhead line maintenance, $42 million in net employee compensation and benefits including pension costs, and $31 million in customer accounts, service, and sales costs primarily related to customer incentive and demand-side management programs.

Other operations and maintenance expenses increased $83 million, or 2.2%, in 2013 as compared to the prior year. Other operations and maintenance expenses in 2013 were significantly below normal levels as a result of cost containment efforts undertaken primarily at Georgia Power to offset the impact of significantly milder than normal weather conditions. Administrative and general expenses increased $63 million primarily as a result of an increase in pension costs. Transmission and distribution expenses increased $27 million primarily due to increases at Georgia Power in transmission system load expense resulting from billing adjustments with integrated transmission system owners.

Production expenses and transmission and distribution expenses fluctuate from year to year due to variations in outage and maintenance schedules and normal changes in the cost of labor and materials.

Depreciation and Amortization

Depreciation and amortization increased $43 million, or 2.3%, in 2014 as compared to the prior year primarily due to increases in depreciation rates related to environmental assets and the amortization of certain regulatory assets at Alabama Power and the completion of the amortization of certain regulatory liabilities at Georgia Power. Also contributing to the increase were increases at Southern Power in plant in service related to the addition of solar facilities in 2013 and 2014, an increase related to equipment retirements resulting from accelerated outage work, and additional component depreciation as a result of increased production. These increases were largely offset by the amortization of $120 million of the regulatory liability for other cost of removal obligations at Alabama Power. See Note 3 to the financial statements under Retail Regulatory Matters Alabama Power Rate CNP and Cost of Removal Accounting Order for additional information.

Depreciation and amortization increased $114 million, or 6.4%, in 2013 as compared to the prior year primarily due to additional plant in service related to the completion of Georgia Power s Plant McDonough-Atkinson Units 5 and 6 in April 2012 and October 2012, respectively, and six Southern Power plants between June 2012 and October 2013, certain coal unit retirement decisions (with respect to the portion of such units dedicated to wholesale service) at Georgia Power, and additional transmission and distribution projects. See FUTURE EARNINGS POTENTIAL Retail Regulatory Matters Georgia Power Integrated Resource Plans for additional information on Georgia Power s unit retirement decisions. These increases were partially offset by a net reduction in amortization primarily related to amortization of a regulatory liability for state income tax credits at Georgia Power and by the deferral of certain expenses under an accounting order at Alabama Power. See Note 3 to the financial statements under Retail Regulatory Matters Alabama Power Compliance and Pension Cost Accounting Order for additional information on Alabama Power s accounting order.

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

Taxes Other Than Income Taxes

Taxes other than income taxes increased $47 million, or 5.0%, in 2014 as compared to the prior year primarily due to increases of $34 million in municipal franchise fees related to higher retail revenues in 2014 and $16 million in payroll taxes primarily related to higher employee benefits.

Taxes other than income taxes increased $20 million, or 2.2%, in 2013 as compared to the prior year primarily due to increases in property taxes.

Estimated Loss on Kemper IGCC

In 2014 and 2013, estimated probable losses on the Kemper IGCC of $868 million and $1.2 billion, respectively, were recorded at Southern Company. These losses reflect revisions of estimated costs expected to be incurred on Mississippi Power s construction of the Kemper IGCC in excess of the $2.88 billion cost cap established by the Mississippi PSC, net of $245 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 CO_2 pipeline facilities, AFUDC, and certain general exceptions, including change of law, force majeure, and beneficial capital (which exists when Mississippi Power 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). See FUTURE EARNINGS POTENTIAL Construction Program herein and Note 3 to the financial statements under Integrated Coal Gasification Combined Cycle for additional information.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Allowance for Equity Funds Used During Construction

AFUDC equity increased $55 million, or 28.9%, in 2014 as compared to the prior year primarily due to additional capital expenditures at the traditional operating companies, primarily related to environmental and transmission projects, as well as Mississippi Power s Kemper IGCC.

AFUDC equity increased $47 million, or 32.9%, in 2013 as compared to the prior year primarily due to an increase in CWIP related to Mississippi Power s Kemper IGCC and increased capital expenditures at Alabama Power, partially offset by the completion of Georgia Power s Plant McDonough-Atkinson Units 5 and 6 in 2012.

See 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 $6 million, or 0.8%, in 2014 as compared to the prior year primarily due to a higher amount of outstanding long-term debt and an increase in interest expense resulting from the deposits received by Mississippi Power in January and October 2014 related to SMEPA s pending purchase of an undivided interest in the Kemper IGCC, partially offset by a decrease in interest expense related to the refinancing of long-term debt at lower rates and an increase in capitalized interest. See Note 6 to the financial statements for additional information.

Interest expense, net of amounts capitalized decreased $32 million, or 3.9%, in 2013 as compared to the prior year primarily due to lower interest rates, the timing of issuances and redemptions of long-term debt, an increase in capitalized interest primarily resulting from AFUDC debt associated with Mississippi Power s Kemper IGCC, and an increase in capitalized interest associated with the construction of Southern Power s Plants Campo Verde and Spectrum. These decreases were partially offset by a decrease in capitalized interest resulting from the completion of Southern Power s Plants Nacogdoches and Cleveland, a reduction in AFUDC debt due to the completion of Georgia Power s Plant McDonough-Atkinson Units 5 and 6, and the conclusion of certain state and federal tax audits in 2012.

Other Income (Expense), Net

Other income (expense), net decreased $18 million, or 32.7%, in 2014 as compared to the prior year primarily due to an $8 million decrease in wholesale operating fee revenue at Georgia Power and $7 million associated with Mississippi Power s settlement with the Sierra Club. See Note 3 to the financial statements under Other Matters Sierra Club Settlement Agreement for additional information.

Income Taxes

Income taxes increased $118 million, or 12.6%, in 2014 as compared to the prior year primarily due to higher pre-tax earnings, partially offset by an increase in non-taxable AFUDC equity and an increase in tax benefits related to federal ITCs.

Income taxes decreased $465 million, or 33.2%, in 2013 as compared to the prior year primarily due to lower pre-tax earnings, an increase in tax benefits recognized from ITCs at Southern Power, and a net increase in non-taxable AFUDC equity, partially offset by a decrease in state income tax credits, primarily at Georgia Power.

Other Business Activities

Southern Company s other business activities include the parent company (which does not allocate operating expenses to business units), investments in leveraged lease projects, and telecommunications. These businesses are classified in general categories and may comprise one or both of the following subsidiaries: Southern Company Holdings, Inc. (Southern Holdings) invests in various projects, including leveraged lease projects, and 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.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

A condensed statement of income for Southern Company s other business activities follows:

	Amount 2014	Increase (Decrease) from Prior Year 2014	2013
		(in millions)	
Operating revenues	**$ 61**	**$ 9**	$ (7)
Other operations and maintenance	**95**	**27**	(9)
Depreciation and amortization	**16**	**1**	
Taxes other than income taxes	**2**		
Total operating expenses	**113**	**28**	(9)
Operating income (loss)	**(52)**	**(19)**	2
Interest income	**1**		(17)
Other income (expense), net	**10**	**36**	(45)
Interest expense	**41**	**5**	(3)
Income taxes	**(76)**	**10**	(20)
Net income (loss)	**$ (6)**	**$ 2**	$ (37)

Operating Revenues

Southern Company s non-electric operating revenues for these other business activities increased $9 million, or 17.3%, in 2014 as compared to the prior year. The increase was primarily related to higher operating revenues at Southern Holdings, partially offset by decreases in revenues at SouthernLINC Wireless related to lower average per subscriber revenue and fewer subscribers due to continued competition in the industry. Non-electric operating revenues for these other businesses decreased $7 million, or 11.9%, in 2013 as compared to the prior year. The decrease was primarily the result of decreases in revenues at SouthernLINC Wireless related to lower average per subscriber revenue and fewer subscribers due to continued competition in the industry.

Other Operations and Maintenance Expenses

Other operations and maintenance expenses for these other business activities increased $27 million, or 39.7%, in 2014 as compared to the prior year. The increase was primarily due to insurance proceeds received in 2013 related to a litigation settlement with MC Asset Recovery, LLC and higher operating expenses at Southern Holdings. Other operations and maintenance expenses for these other business activities decreased $9 million, or 11.7%, in 2013 as compared to the prior year. The decrease was primarily related to lower operating expenses at SouthernLINC Wireless and decreases in consulting and legal fees, partially offset by higher operating expenses at Southern Holdings and a decrease in the amount of insurance proceeds received in 2013 related to a litigation settlement with MC Asset Recovery, LLC as compared to the amount received in 2012. See Note 3 to the financial statements under Insurance Recovery for additional information related to the litigation settlement with MC Asset Recovery, LLC.

Interest Income

Interest income for these other business activities decreased $17 million in 2013 as compared to the prior year primarily due to the conclusion of certain federal income tax audits in 2012.

Other Income (Expense), Net

Other income (expense), net for these other business activities increased $36 million in 2014 as compared to the prior year. The increase was primarily due to the restructuring of a leveraged lease investment in the first quarter of 2013 and a decrease in charitable contributions in 2014. Other income (expense), net for these other business activities decreased $45 million in 2013 as compared to the prior year. The decrease was primarily due to the restructuring of a leveraged lease investment and an increase in charitable contributions.

Southern Company has several leveraged lease agreements which relate to international and domestic energy generation, distribution, and transportation assets. Southern Company receives federal income tax deductions for depreciation and amortization, as well as interest on long-term debt related to these investments. See Note 1 under Leveraged Leases for additional information.

Interest Expense

Interest expense for these other business activities increased $5 million, or 13.9%, in 2014 as compared to the prior year. The increase was primarily due to a higher amount of outstanding long-term debt, partially offset by the refinancing of long-term debt at lower rates.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Income Taxes

Income taxes for these other business activities increased $10 million, or 11.6%, in 2014 and decreased $20 million, or 30.3%, in 2013 as compared to the prior year primarily as a result of changes in pre-tax earnings (losses).

Effects of Inflation

The traditional operating companies are 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. Southern Power is party to long-term contracts reflecting market-based rates, including inflation expectations. Any adverse effect of inflation on Southern Company s results of operations has not been substantial in recent years.

FUTURE EARNINGS POTENTIAL

General

The four traditional operating companies operate as vertically integrated utilities providing electricity to customers within their service areas in the Southeast. Prices for electricity provided to retail customers are set by state PSCs under cost-based regulatory principles. Prices for wholesale electricity sales, interconnecting transmission lines, and the exchange of electric power are regulated by the FERC. Retail rates and earnings are reviewed and may be adjusted periodically within certain limitations. Southern Power continues to focus on long-term capacity contracts, optimized by limited energy trading activities. See ACCOUNTING POLICIES Application of Critical Accounting Policies and Estimates Electric Utility Regulation herein and Note 3 to the financial statements for additional information about regulatory matters.

The results of operations for the past three years are not necessarily indicative of future earnings potential. The level of Southern Company s future earnings depends on numerous factors that affect the opportunities, challenges, and risks of the Southern Company system s primary business of selling electricity. These factors include the traditional operating companies ability to maintain a constructive regulatory environment that continues to allow for the timely recovery of prudently-incurred costs during a time of increasing costs and the completion and subsequent operation of the Kemper IGCC and Plant Vogtle Units 3 and 4 as well as other ongoing construction projects. Other major factors include the profitability of the competitive wholesale business and successfully expanding investments in renewable energy projects. Future earnings for the electricity business 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 and other wholesale customers, energy conservation practiced by customers, the use of alternative energy sources by customers, the price of electricity, the price elasticity of demand, and the rate of economic growth or decline in the service territory. In addition, the level of future earnings for the wholesale business also depends on numerous factors including creditworthiness of customers, total generating capacity available and related costs, future acquisitions and construction of generating facilities, including the impact of ITCs, and the successful remarketing of capacity as current contracts expire. Changes in regional and global economic conditions may impact sales for the traditional operating companies and Southern Power, 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.

As part of its ongoing effort to adapt to changing market conditions, Southern Company continues to evaluate and consider a wide array of potential business strategies. These strategies may include business combinations, partnerships, and acquisitions involving other utility or non-utility businesses or properties, disposition of certain assets, internal restructuring, or some combination thereof. Furthermore, Southern Company may engage in new business ventures that arise from competitive and regulatory changes in the utility industry. Pursuit of any of the above strategies, or any combination thereof, may significantly affect the business operations, risks, and financial condition of Southern Company.

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 and Georgia Power alleging violations of the New Source Review provisions of the Clean Air Act at certain coal-fired electric generating units, including units co-owned by Gulf Power and Mississippi Power. An adverse outcome could require substantial capital expenditures that cannot be determined at this

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

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 electric utilities 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 traditional operating companies had invested approximately $10.6 billion in environmental capital retrofit projects to comply with these requirements, with annual totals of approximately $1.1 billion, $0.7 billion, and $0.3 billion for 2014, 2013, and 2012, respectively. The Southern Company system expects that capital expenditures to comply with environmental statutes and regulations will total approximately $2.1 billion from 2015 through 2017, with annual totals of approximately $1.0 billion, $0.5 billion, and $0.6 billion 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 CO_2 emissions from new, existing, and modified or reconstructed fossil-fuel-fired electric generating units. See Global Climate Issues for additional information.

The Southern Company system 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 fuel mix of the electric utilities. Compliance costs may arise from existing unit retirements, installation of additional environmental controls, upgrades to the transmission system, 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 Retail Regulatory Matters Alabama Power Environmental Accounting Order and Retail Regulatory Matters Georgia Power Integrated Resource Plans herein and Note 3 to the financial statements under Other Matters Sierra Club Settlement Agreement for additional information on planned unit retirements and fuel conversions at Alabama Power, Georgia Power, and Mississippi Power.

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 electric utilities operations, the full impact of any such changes cannot be determined at this time. Additionally, many of the electric utilities 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.

Air Quality

Compliance with the Clean Air Act and resulting regulations has been and will continue to be a significant focus for the Southern Company system. Since 1990, the electric utilities have spent approximately $9.5 billion 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). In 2008, the EPA adopted a more stringent eight-hour ozone NAAQS, which it began to implement in 2011. In 2012, the EPA published its final determination of nonattainment areas based on the 2008 eight-hour ozone NAAQS. The only area within the traditional operating companies service territory designated as an ozone nonattainment area is a 15-county area within metropolitan Atlanta. 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 traditional operating companies service territory.

The EPA regulates fine particulate matter concentrations on an annual and 24-hour average basis. All areas within the traditional operating companies service territory have achieved attainment with the 1997 and 2006 particulate matter NAAQS

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

and, with the exception of the Atlanta area, the EPA has officially redesignated former nonattainment areas within the service territory as attainment for these standards. A redesignation request for the Atlanta area is pending with the EPA. In 2012, the EPA issued a final rule that increases the stringency of the annual fine particulate matter standard. The EPA promulgated final designations for the 2012 annual standard on December 18, 2014, and no new nonattainment areas were designated within the traditional operating companies service territory. The EPA has, however, deferred designation decisions for certain areas in Alabama, Florida, and Georgia, so future nonattainment designations in these areas are possible.

Final revisions to the NAAQS for sulfur dioxide (SO_2), which established a new one-hour standard, became effective in 2010. No areas within the Southern Company system s service territory have been designated as nonattainment under this rule. However, the EPA has announced plans to make additional designation decisions for SO_2 in the future, which could result in nonattainment designations for areas within the Southern Company system s service territory. Implementation of the revised SO_2 standard could require additional reductions in SO_2 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. In March 2013, the U.S. Court of Appeals for the Eleventh Circuit ruled in favor of Alabama Power 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 believes 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 owned by Alabama Power, units co-owned with Mississippi Power, and units owned by SEGCO, which is jointly owned by Alabama Power and Georgia Power.

Each of the states in which the Southern Company system has fossil generation is subject to the requirements of the Cross State Air Pollution Rule (CSAPR). CSAPR is an emissions trading program that limits SO_2 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, Florida, Georgia, Mississippi, and North Carolina) to revise their SSM provisions within 18 months after issuance of the final rule.

The Southern Company system has developed and continually updates a comprehensive environmental compliance strategy to assess compliance obligations associated with the current and proposed environmental requirements discussed above. As part of this strategy, certain of the traditional operating companies have developed a compliance plan for the MATS rule which includes reliance on existing emission control technologies, the construction of baghouses to provide an additional level of control on the emissions of mercury and particulates from certain generating units, the use of additives or other injection technology, the use of existing or additional natural gas capability, and unit retirements. Additionally, certain transmission system upgrades are required. The impacts of the eight-hour ozone, fine particulate matter and SO_2 NAAQS, the Alabama opacity rule, CSAPR, CAVR, the MATS rule, the NSPS for CTs, and the SSM rule on the Southern Company system 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.

In addition to the federal air quality laws described above, Georgia Power is also subject to the requirements of the 2007 State of Georgia Multi-Pollutant Rule. The Multi-Pollutant Rule, as amended, is designed to reduce emissions of mercury, SO_2, and nitrogen oxide state-wide by requiring the installation of specified control technologies at certain coal-fired generating units by specific dates between December 31, 2008 and April 16, 2015. A companion rule requires a 95% reduction in SO_2 emissions

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

from the controlled units on the same or similar timetable. Through December 31, 2014, Georgia Power had installed the required controls on 14 of its coal-fired generating units with two additional projects to be completed before the unit-specific installation deadlines.

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 or through PPAs.

Coal Combustion Residuals

The traditional operating companies currently manage CCR at onsite storage units consisting of landfills and surface impoundments (CCR Units) at 22 electric generating plants. In addition to on-site storage, the traditional operating companies also sell a portion of their CCR to third parties for beneficial reuse. Individual states regulate CCR and the states in the Southern Company system s service territory each have their own regulatory requirements. Each traditional operating 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 traditional operating companies 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, Southern Company has developed a preliminary nominal dollar estimate of costs associated with closure and groundwater monitoring of ash ponds in place of approximately $860 million and ongoing post-closure care of approximately $140 million. Certain of the traditional operating companies have previously recorded asset retirement obligations (ARO) associated with ash ponds of $506 million, or $468 million on a nominal dollar basis, based on existing state requirements. During 2015, the traditional operating companies will record AROs for any incremental estimated closure costs resulting from acceleration in the timing of any currently planned closures and for differences between existing state requirements and the requirements of the CCR Rule. Southern Company s results of operations, cash flows, and financial condition could be significantly impacted if such costs are not recovered through regulated rates.

Environmental Remediation

The Southern Company system 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 Southern Company system could incur substantial costs to clean up properties. The traditional operating companies conduct studies to determine the extent of any required cleanup and the Company has recognized in its financial statements the costs to clean up known

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

impacted sites. Amounts for cleanup and ongoing monitoring costs were not material for any year presented. The traditional operating companies have each received authority from their respective state PSCs to recover approved environmental compliance costs through regulatory mechanisms. These rates are adjusted annually or as necessary within limits approved by the state PSCs. The traditional operating companies 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 CO_2 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 CO_2 emissions from modified and reconstructed units. The EPA s proposed Clean Power Plan establishes guidelines for states to develop plans to address CO_2 emissions from existing fossil fuel-fired electric generating units. The EPA s proposed guidelines establish state-specific interim and final CO_2 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. Southern 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 CO_2 equivalent emissions in metric tons for a company s operational control of facilities. Based on ownership or financial control of facilities, the Southern Company system s 2013 greenhouse gas emissions were approximately 102 million metric tons of CO_2 equivalent. The preliminary estimate of the Southern Company system s 2014 greenhouse gas emissions on the same basis is approximately 112 million metric tons of CO_2 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.

Retail Regulatory Matters

Alabama Power

Alabama Power s revenues from regulated retail operations are collected through various rate mechanisms subject to the oversight of the Alabama PSC. Alabama Power currently recovers its costs from the regulated retail business primarily through Rate RSE, Rate CNP, Rate ECR, and Rate NDR. In addition, the Alabama PSC issues accounting orders to address current events impacting Alabama Power. See Note 3 to the financial statements under Retail Regulatory Matters Alabama Power for additional information regarding Alabama Power s rate mechanisms and accounting orders.

Rate RSE

Alabama Power s Rate RSE adjustments are based on forward-looking information for the applicable upcoming calendar year. Rate adjustments for any two-year period, when averaged together, cannot exceed 4.0% and any annual adjustment is limited to 5.0%. If Alabama Power s actual retail return is above the allowed weighted cost of equity (WCE) range, customer refunds will be required; however, there is no provision for additional customer billings should the actual retail return fall below the WCE range.

On December 1, 2014, Alabama Power submitted the required annual filing under Rate RSE to the Alabama PSC. The Rate RSE increase was 3.49%, or $181 million annually, effective January 1, 2015. The revenue adjustment includes the performance based adder of 0.07%. Under the terms of Rate RSE, the maximum increase for 2016 cannot exceed 4.51%.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Rate CNP

Alabama Power s retail rates, approved by the Alabama PSC, provide for adjustments to recognize the placing of new generating facilities into retail service under Rate CNP. Alabama Power may also recover retail costs associated with certificated PPAs under Rate CNP PPA. On March 4, 2014, the Alabama PSC issued a consent order that Alabama Power leave in effect the current Rate CNP PPA factor for billings for the period April 1, 2014 through March 31, 2015. It is anticipated that no adjustment will be made to Rate CNP PPA in 2015.

Alabama Power has elected the normal purchase normal sale (NPNS) scope exception under the derivative accounting rules for its two wind PPAs, which total approximately 400 MWs. The NPNS exception allows the PPAs to be recorded at a cost, rather than fair value, basis. The industry s application of the NPNS exception to certain physical forward transactions in nodal markets was previously under review by the SEC at the request of the electric utility industry. In June 2014, the SEC requested the Financial Accounting Standards Board to address the issue through the Emerging Issues Task Force (EITF). Any accounting decisions will now be subject to EITF deliberations. The outcome of the EITF s deliberations cannot be determined at this time. If Alabama Power is ultimately required to record these PPAs at fair value, an offsetting regulatory asset or regulatory liability will be recorded.

Rate CNP Environmental allows for the recovery of Alabama Power s retail costs associated with environmental laws, regulations, or other such mandates. Rate CNP Environmental is based on forward-looking information and provides for the recovery of these costs pursuant to a factor that is calculated annually. Environmental costs to be recovered include operations and maintenance expenses, depreciation, and a return on certain invested capital. The Rate CNP Environmental increase effective January 1, 2015 is 1.5%, or $75 million annually, based upon projected billings.

Environmental Accounting Order

Based on an order from the Alabama PSC, Alabama Power is allowed to establish a regulatory asset to record the unrecovered investment costs, including the unrecovered plant asset balance and the unrecovered costs associated with site removal and closure associated with future unit retirements caused by environmental regulations. These costs would be amortized over the affected unit s remaining useful life, as established prior to the decision regarding early retirement. See Environmental Matters Environmental Statutes and Regulations herein for additional information regarding environmental regulations.

As part of its environmental compliance strategy, Alabama Power plans to retire Plant Gorgas Units 6 and 7. These units represent 200 MWs of Alabama Power s approximately 12,200 MWs of generating capacity. Alabama Power also plans to cease using coal at Plant Barry Units 1 and 2 (250 MWs), but such units will remain available on a limited basis with natural gas as the fuel source. Additionally, Alabama Power expects to cease using coal at Plant Barry Unit 3 (225 MWs) and Plant Greene County Units 1 and 2 (300 MWs) and begin operating those units solely on natural gas. These plans are expected to be effective no later than April 2016.

In accordance with an accounting order from the Alabama PSC, Alabama Power will transfer the unrecovered plant asset balances to a regulatory asset at their respective retirement dates. The regulatory asset will be amortized through Rate CNP Environmental over the remaining useful lives, as established prior to the decision for retirement. As a result, these decisions will not have a significant impact on Southern Company s financial statements.

Cost of Removal Accounting Order

In accordance with an accounting order issued on November 3, 2014 by the Alabama PSC, at December 31, 2014, Alabama Power fully amortized the balance of $123 million in certain regulatory asset accounts, and offset this amortization expense with the amortization of $120 million of the regulatory liability for other cost of removal obligations. The regulatory asset account balances amortized as of December 31, 2014 represented costs previously deferred under a compliance and pension cost accounting order as well as a non-nuclear outage accounting order, which were approved by the Alabama PSC in 2012 and August 2013, respectively. Approximately $95 million of non-nuclear outage costs and $28 million of compliance and pension costs were fully amortized at December 31, 2014.

The cost of removal accounting order also required Alabama Power to terminate, as of December 31, 2014, the regulatory asset accounts created pursuant to the compliance and pension cost accounting order and the non-nuclear outage accounting order. Consequently, Alabama Power will not defer any expenditures in 2015, 2016, and 2017 related to critical electric infrastructure and domestic nuclear facilities, as allowed under the previous orders.

Non-Environmental Federal Mandated Costs Accounting Order

On December 9, 2014, pending the development of a new cost recovery mechanism, the Alabama PSC issued an accounting order authorizing the deferral as a regulatory asset of up to $50 million of costs associated with non-environmental federal mandates that would otherwise impact rates in 2015.

On February 17, 2015, Alabama Power filed a proposed modification to Rate CNP Environmental with the Alabama PSC to include compliance costs for both environmental and non-environmental mandates. The non-environmental costs that would be recovered through the revised mechanism concern laws, regulations, and other mandates directed at the utility industry

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

involving the security, reliability, safety, sustainability, or similar considerations impacting Alabama Power s facilities or operations. If approved as requested, the effective date for the revised mechanism would be March 20, 2015, upon which the regulatory asset balance would be reclassified to the under recovered balance for Rate CNP Environmental, and the related customer rates would not become effective before January 2016. The ultimate outcome of this matter cannot be determined at this time.

Georgia Power

Georgia Power s revenues from regulated retail operations are collected through various rate mechanisms subject to the oversight of the Georgia PSC. Georgia Power currently recovers its costs from the regulated retail business through the 2013 ARP, which includes traditional base tariff rates, Demand-Side Management (DSM) tariffs, Environmental Compliance Cost Recovery (ECCR) tariffs, and Municipal Franchise Fee (MFF) tariffs. In addition, financing costs related to the construction of Plant Vogtle Units 3 and 4 are being collected through the NCCR tariff and fuel costs are collected through separate fuel cost recovery tariffs. See Note 3 to the financial statements under Retail Regulatory Matters Georgia Power for additional information.

Rate Plans

In December 2013, the Georgia PSC voted to approve the 2013 ARP. The 2013 ARP reflects the settlement agreement among Georgia Power, the Georgia PSC s Public Interest Advocacy Staff, and 11 of the 13 intervenors, which was filed with the Georgia PSC in November 2013.

On January 1, 2014, in accordance with the 2013 ARP, Georgia Power increased its tariffs as follows: (1) traditional base tariff rates by approximately $80 million; (2) ECCR tariff by approximately $25 million; (3) DSM tariffs by approximately $1 million; and (4) MFF tariff by approximately $4 million, for a total increase in base revenues of approximately $110 million.

On February 19, 2015, in accordance with the 2013 ARP, the Georgia PSC approved adjustments to traditional base, ECCR, DSM, and MFF tariffs effective January 1, 2015 as follows:

- Traditional base tariffs by approximately $107 million to cover additional capacity costs;
- ECCR tariff by approximately $23 million;
- DSM tariffs by approximately $3 million; and
- MFF tariff by approximately $3 million to reflect the adjustments above.

The sum of these adjustments resulted in a base revenue increase of approximately $136 million in 2015.

The 2016 base rate increase, which was approved in the 2013 ARP, will be determined through a compliance filing expected to be filed in late 2015, and will be subject to review by the Georgia PSC.

Under the 2013 ARP, Georgia Power s retail ROE is set at 10.95% and earnings are evaluated against a retail ROE range of 10.00% to 12.00%. Two-thirds of any earnings above 12.00% will be directly refunded to customers, with the remaining one-third retained by Georgia Power. There will be no recovery of any earnings shortfall below 10.00% on an actual basis. However, if at any time during the term of the 2013 ARP, Georgia Power projects that its retail earnings will be below 10.00% for any calendar year, it may petition the Georgia PSC for implementation of the Interim Cost Recovery (ICR) tariff that would be used to adjust Georgia Power s earnings back to a 10.00% retail ROE. The Georgia PSC would have 90 days to rule on Georgia Power s request. The ICR tariff will expire at the earlier of January 1, 2017 or the end of the calendar year in which the ICR tariff becomes effective. In lieu of requesting implementation of an ICR tariff, or if the Georgia PSC chooses not to implement the ICR tariff, Georgia Power may file a full rate case. In 2014, Georgia Power s retail ROE exceeded 12.00%, and Georgia Power expects to refund to retail customers approximately $13 million in 2015, subject to review and approval by the Georgia PSC.

Except as provided above, Georgia Power will not file for a general base rate increase while the 2013 ARP is in effect. Georgia Power is required to file a general rate case by July 1, 2016, in response to which the Georgia PSC would be expected to determine whether the 2013 ARP should be continued, modified, or discontinued.

Integrated Resource Plans

See Environmental Matters Environmental Statutes and Regulations Air Quality, Water Quality, Coal Combust Residuals, and Global Climate Issues, and Rate Plans herein for additional information regarding proposed and final EPA rules and regulations, including the MATS rule for coal- and oil-fired electric utility steam generating units, revisions to effluent limitations guidelines for steam electric power plants, and additional regulations of CCR and CO_2; the State of Georgia s Multi-Pollutant Rule; and Georgia Power s analysis of the potential costs and benefits of installing the required controls on its fossil generating units in light of these regulations.

In July 2013, the Georgia PSC approved Georgia Power s latest triennial Integrated Resource Plan (2013 IRP) including Georgia Power s request to decertify 16 coal- and oil-fired units totaling 2,093 MWs. Several factors, including the cost to comply with existing and future environmental regulations, recent and forecasted economic conditions, and lower natural gas prices, contributed to the decision to close these units.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Plant Branch Units 3 and 4 (1,016 MWs), Plant Yates Units 1 through 5 (579 MWs), and Plant McManus Units 1 and 2 (122 MWs) will be decertified and retired by April 16, 2015, the compliance date of the MATS rule. The decertification date of Plant Branch Unit 1 (250 MWs) was extended from December 31, 2013 as specified in the final order in the 2011 Integrated Resource Plan Update (2011 IRP Update) to coincide with the decertification date of Plant Branch Units 3 and 4. The decertification and retirement of Plant Kraft Units 1 through 4 (316 MWs) were also approved and will be effective by April 16, 2016, based on a one-year extension of the MATS rule compliance date that was approved by the State of Georgia Environmental Protection Division in September 2013 to allow for necessary transmission system reliability improvements. In July 2013, the Georgia PSC approved the switch to natural gas as the primary fuel for Plant Yates Units 6 and 7. In September 2013, Plant Branch Unit 2 (319 MWs) was retired as approved by the Georgia PSC in the 2011 IRP Update in order to comply with the State of Georgia s Multi-Pollutant Rule.

In the 2013 ARP, the Georgia PSC approved the amortization of the CWIP balances related to environmental projects that will not be completed at Plant Branch Units 1 through 4 and Plant Yates Units 6 and 7 over nine years beginning in January 2014 and the amortization of any remaining net book values of Plant Branch Unit 2 from October 2013 to December 2022, Plant Branch Unit 1 from May 2015 to December 2020, Plant Branch Unit 3 from May 2015 to December 2023, and Plant Branch Unit 4 from May 2015 to December 2024. The Georgia PSC deferred a decision regarding the appropriate recovery period for the costs associated with unusable materials and supplies remaining at the retiring plants to Georgia Power s next base rate case, which Georgia Power expects to file in 2016 (2016 Rate Case). In the 2013 IRP, the Georgia PSC also deferred decisions regarding the recovery of any fuel related costs that could be incurred in connection with the retirement units to be addressed in future fuel cases.

On July 1, 2014, the Georgia PSC approved Georgia Power s request to cancel the proposed biomass fuel conversion of Plant Mitchell Unit 3 (155 MWs) because it would not be cost effective for customers. Georgia Power expects to request decertification of Plant Mitchell Unit 3 in connection with the triennial Integrated Resource Plan to be filed in 2016. Georgia Power plans to continue to operate the unit as needed until the MATS rule becomes effective in April 2015.

The decertification of these units and fuel conversions are not expected to have a material impact on Southern Company s financial statements; however, the ultimate outcome depends on the Georgia PSC s order in the 2016 Rate Case and future fuel cases and cannot be determined at this time.

Retail Fuel Cost Recovery

The traditional operating companies each have established fuel cost recovery rates approved by their respective state PSCs. Fuel cost recovery revenues are adjusted for differences in actual recoverable fuel costs and amounts billed in current regulated rates. Accordingly, changes in the billing factor will not have a significant effect on Southern Company s revenues or net income, but will affect cash flow. The traditional operating companies continuously monitor their under or over recovered fuel cost balances. On January 20, 2015, the Georgia PSC approved the deferral of Georgia Power s next fuel case filing until at least June 30, 2015.

See Note 1 to the financial statements under Revenues and Note 3 to the financial statements under Retail Regulatory Matters Alabama Power Rate ECR and Retail Regulatory Matters Georgia Power Fuel Cost Recovery for addition information.

Construction Program

The subsidiary companies of Southern Company are engaged in continuous construction programs to accommodate existing and estimated future loads on their respective systems. The Southern Company system intends to continue its strategy of developing and constructing new generating facilities, as well as adding or changing fuel sources for certain existing units, adding environmental control equipment, and expanding the transmission and distribution systems. For the traditional operating companies, major generation construction projects are subject to state PSC approval in order to be included in retail rates. While Southern Power generally constructs and acquires generation assets covered by long-term PPAs, any uncontracted capacity could negatively affect future earnings. The construction programs of the traditional operating companies and Southern Power are currently estimated to include an investment of approximately $6.7 billion, $5.4 billion, and $4.3 billion for 2015, 2016, and 2017, respectively.

The two largest construction projects currently underway in the Southern Company system are Plant Vogtle Units 3 and 4 and the Kemper IGCC. Georgia Power has a 45.7% ownership interest in Plant Vogtle Units 3 and 4, each with approximately 1,100 MWs, and Mississippi Power is ultimately expected to hold an 85% ownership interest in the 582-MW Kemper IGCC. See Note 3 to the financial statements under Retail Regulatory Matters Georgia Power Nuclear Construction and Integrated Coal Gasification Combined Cycle for additional information.

From 2013 through December 31, 2014, the Company recorded pre-tax charges totaling $2.05 billion ($1.26 billion after-tax) for revisions of estimated costs expected to be incurred on Mississippi Power 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. In subsequent periods, any further changes in the estimated costs to complete construction 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 income and these changes could be material.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

On January 29, 2015, Georgia Power announced that it was notified by the consortium consisting of Westinghouse Electric Company LLC and Stone & Webster, Inc., a subsidiary of The Shaw Group Inc., which was acquired by Chicago Bridge & Iron Company N.V. (collectively, Contractor) of the Contractor s revised forecast for completion of Plant Vogtle Units 3 and 4, which would incrementally delay the previously disclosed estimated in-service dates by 18 months (from the fourth quarter of 2017 to the second quarter of 2019 for Unit 3 and from the fourth quarter of 2018 to the second quarter of 2020 for Unit 4).

While Georgia Power has not agreed to any change to the guaranteed substantial completion dates (April 2016 for Unit 3 and April 2017 for Unit 4) included in the engineering, procurement, and construction agreement relating to Plant Vogtle Units 3 and 4, Georgia Power s twelfth Vogtle Construction Monitoring (VCM) report, filed February 27, 2015, includes a requested amendment to the Plant Vogtle Units 3 and 4 certificate to reflect the Contractor s revised forecast, to include the estimated owner s costs associated with the proposed 18-month Contractor delay, and to increase the estimated in-service capital cost of Plant Vogtle Units 3 and 4 from $4.4 billion to $5.0 billion. No Contractor costs related to the Contractor s proposed 18-month delay are included in the twelfth VCM report. The twelfth VCM report estimates total associated financing costs during the construction period to be approximately $2.5 billion.

Additionally, there are certain risks associated with the construction program in general and certain risks associated with the licensing, construction, and operation of nuclear generating units in particular, including potential impacts that could result from a major incident at a nuclear facility anywhere in the world. The ultimate outcome of these events cannot be determined at this time.

See FINANCIAL CONDITION AND LIQUIDITY Capital Requirements and Contractual Obligations for additional information.

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 will have a positive impact on Southern Company s cash flows and, combined with bonus depreciation allowed under the American Taxpayer Relief Act of 2012 (ATRA), will result in approximately $630 million of positive cash flows. Additionally, the estimated cash flow benefit impact of bonus depreciation for long-term production-period projects to be placed in service in 2015 related to TIPA is expected to be approximately $220 million to $240 million for the 2015 tax year.

Tax Credits

The IRS allocated $279 million (Phase II) of Internal Revenue Code of 1986, as amended (Internal Revenue Code) Section 48A tax credits to Mississippi Power in connection with the Kemper IGCC. Through December 31, 2014, Southern Company had recorded tax benefits totaling $276 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 CO_2 produced by the Kemper IGCC during operations in accordance with the Internal Revenue Code. Mississippi Power 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.

In 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009 (ARRA). Major tax incentives in the ARRA included renewable energy incentives. In January 2013, the ATRA was signed into law. The ATRA retroactively extended several renewable energy incentives through 2013, including extending federal ITCs for biomass projects which began construction before January 1, 2014. The current law provides for a 30% federal ITC for solar facilities placed in service through 2016 and, unless extended, will adjust to 10% for solar facilities placed in service thereafter. The Company has received ITCs in connection with Southern Power s investments in solar and biomass facilities. See Note 1 to the financial statements under Income and Other Taxes for additional information regarding credits amortized and the tax benefit related to basis differences in 2014, 2013, and 2012.

Additionally, the TIPA extended the production tax credit for wind and certain other renewable sources of electricity to facilities for which construction had commenced by the end of 2014.

Section 174 Research and Experimental Deduction

Southern Company reduced tax payments for 2014 and included in its 2013 consolidated federal income tax return deductions for research and experimental expenditures related to the Kemper IGCC. Due to the uncertainty related to this tax position, Southern 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.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Other Matters

Southern Company and its subsidiaries are involved in various other matters being litigated and regulatory matters that could affect future earnings. In addition, Southern Company and its subsidiaries are subject to certain claims and legal actions arising in the ordinary course of business. The business activities of Southern Company s subsidiaries 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 CO_2 and other emissions, CCR, and alleged exposure to hazardous materials, and/or requests for injunctive relief in connection with such matters.

The ultimate outcome of such pending or potential litigation against Southern Company and its subsidiaries 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 Southern 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.

ACCOUNTING POLICIES

Application of Critical Accounting Policies and Estimates

Southern Company prepares its consolidated 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 Southern 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

Southern Company s traditional operating companies, which comprised approximately 94% of Southern Company s total operating revenues for 2014, are subject to retail regulation by their respective state PSCs and wholesale regulation by the FERC. These regulatory agencies set the rates the traditional operating companies are permitted to charge customers based on allowable costs, including a reasonable return on equity. As a result, the traditional operating companies apply 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 traditional operating companies; therefore, the accounting estimates inherent in specific costs such as depreciation, AROs, 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

Southern 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. Southern 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 Southern Company s financial position, results of operations, or cash flows.

Pension and Other Postretirement Benefits

Southern 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,

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

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 Southern 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 Southern Company s investment strategy, historical experience, and expectations for long-term rates of return that consider external actuarial advice. Southern Company determines the long-term return on plan assets by applying the long-term rate of expected returns on various asset classes to Southern Company s target asset allocation. Southern Company discounts the future cash flows related to its postretirement benefit plans using a single-point discount rate for each plan 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 $636 million and $92 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 $86 million and $10 million, respectively.

The following table illustrates the sensitivity to changes in Southern Company s long-term assumptions with respect to the assumed discount rate, the assumed salaries, and the assumed long-term rate of return on plan assets:

Change in Assumption	Increase/(Decrease) in Total Benefit Expense for 2015	Increase/(Decrease) in Projected Obligation for Pension Plan at December 31, 2014	Increase/(Decrease) in Projected Obligation for Other Postretirement Benefit Plans at December 31, 2014
		(in millions)	
25 basis point change in discount rate	$36/$(34)	$409/$(385)	$64/$(61)
25 basis point change in salaries	$19/$(18)	$103/$(99)	$ /$
25 basis point change in long-term return on plan assets	$24/$(24)	N/A	N/A

N/A Not applicable

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

During 2014, Mississippi Power 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. Mississippi Power 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, Southern 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, and $540.0 million ($333.5 million after tax) in the first quarter 2013. In the aggregate, Southern 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.

Mississippi Power 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 Southern Company s statements of income 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

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

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).

Mississippi Power 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 Southern Company s results of operations, Southern Company considers these items to be critical accounting estimates. See 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. Southern 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; however, Southern Company s financial condition remained stable at December 31, 2014 and December 31, 2013. Through December 31, 2014, Southern 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. Southern Company s cash requirements primarily consist of funding ongoing operations, common stock dividends, capital expenditures, and debt maturities. The Southern Company system s capital expenditures and other investing activities include investments to meet projected long-term demand requirements, to comply with environmental regulations, and for restoration following major storms. Operating cash flows provide a substantial portion of the Southern Company system s cash needs. For the three-year period from 2015 through 2017, Southern Company s projected common stock dividends, capital expenditures, and debt maturities are expected to exceed operating cash flows. The Southern Company system s projected capital expenditures in that period include investments to build new generation facilities, to maintain existing generation facilities, 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. Southern Company plans to finance future cash needs in excess of its operating cash flows primarily by accessing borrowings from financial institutions and through debt and equity issuances in the capital markets. Southern Company intends to continue to monitor its access to short-term and long-term capital markets as well as its bank credit arrangements to meet future capital and liquidity needs. See Sources of Capital, Financing Activities, and Capital Requirements and Contractual Obligations herein for additional information.

Southern Company s investments in the qualified pension plan and the nuclear decommissioning trust funds increased in value as of December 31, 2014 as compared to December 31, 2013. In December 2014, certain of the traditional operating companies and other subsidiaries voluntarily contributed an aggregate of $500 million to the qualified pension plan. No mandatory contributions to the qualified pension plan are anticipated for the year ending December 31, 2015. See Contractual Obligations herein and Notes 1 and 2 to the financial statements under Nuclear Decommissioning and Pension Plans, respectively, for additional information.

Net cash provided from operating activities in 2014 totaled $5.8 billion, a decrease of $282 million from 2013. Significant changes in operating cash flow for 2014 as compared to 2013 include $500 million of voluntary contributions to the qualified pension plan and an increase in receivables due to under recovered fuel costs, partially offset by an increase in accrued compensation. Net cash provided from operating activities in 2013 totaled $6.1 billion, an increase of $1.2 billion from 2012. The most significant change in operating cash flow for 2013 as compared to 2012 was a decrease in fossil fuel stock due to an increase in KWH generation.

Net cash used for investing activities in 2014, 2013, and 2012 totaled $6.4 billion, $5.7 billion, and $5.2 billion, respectively. The cash used for investing activities in each of these years was primarily due to gross property additions for installation of equipment to comply with environmental standards, construction of generation, transmission, and distribution facilities, acquisitions of solar facilities, and purchases of nuclear fuel.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Net cash provided from financing activities totaled $644 million in 2014 due to issuances of long-term debt and common stock, partially offset by common stock dividend payments, redemptions of long-term debt, and a reduction in short-term debt. Net cash used for financing activities totaled $324 million in 2013 due to redemptions of long-term debt and payments of common stock dividends, partially offset by issuances of long-term debt and common stock and an increase in notes payable. Fluctuations in cash flow from financing activities vary from year to year based on capital needs and the maturity or redemption of securities.

Significant balance sheet changes in 2014 included an increase of $3.7 billion in total property, plant, and equipment for the installation of equipment to comply with environmental standards and construction of generation, transmission, and distribution facilities and a $1.8 billion increase in other regulatory assets, deferred related to pension and other postretirement benefits. Other significant changes included a $2.9 billion increase in short-term debt primarily related to debt maturing within the next year and borrowings to fund the Southern Company subsidiaries continuous construction programs, a $1.2 billion increase in stockholders equity, a $1.0 billion increase in accumulated deferred income taxes primarily as a result of bonus depreciation, and a $971 million increase in employee benefit obligations primarily as a result of changes in actuarial assumptions. See Note 2 and Note 5 to the financial statements for additional information regarding retirement benefits and deferred income taxes, respectively.

At the end of 2014, the market price of Southern Company s common stock was $49.11 per share (based on the closing price as reported on the New York Stock Exchange) and the book value was $21.98 per share, representing a market-to-book value ratio of 223%, compared to $41.11, $21.43, and 192%, respectively, at the end of 2013.

Sources of Capital

Southern Company intends to meet its future capital needs through operating cash flow, short-term debt, term loans, and external security issuances. Equity capital can be provided from any combination of the Company s stock plans, private placements, or public offerings. The amount and timing of additional equity capital to be raised in 2015, as well as in subsequent years, will be contingent on Southern Company s investment opportunities and the Southern Company system s capital requirements.

Except as described herein, the traditional operating companies and Southern Power plan to obtain the funds required for construction and other purposes from operating cash flows, external security issuances, term loans, short-term borrowings, and equity contributions or loans from Southern Company. However, the amount, type, and timing of any future financings, if needed, will depend upon prevailing market conditions, regulatory approval, and other factors.

On February 20, 2014, Georgia Power and the DOE entered into a loan guarantee agreement (Loan Guarantee Agreement), pursuant to which the DOE agreed to guarantee borrowings to be made by Georgia Power under a multi-advance credit facility (FFB Credit Facility) among Georgia Power, the DOE, and the FFB. Georgia Power is obligated to reimburse the DOE for any payments the DOE is required to make to the FFB under the guarantee. Georgia Power s reimbursement obligations to the DOE are full recourse and also are secured by a first priority lien on (i) Georgia Power s 45.7% ownership interest in Plant Vogtle Units 3 and 4 (primarily the units under construction, the related real property, and any nuclear fuel loaded in the reactor core) and (ii) Georgia Power s rights and obligations under the principal contracts relating to Plant Vogtle Units 3 and 4. Under the FFB Credit Facility, Georgia Power may make term loan borrowings through the FFB. Proceeds of borrowings made under the FFB Credit Facility will be used to reimburse Georgia Power for a portion of certain costs of construction relating to Plant Vogtle Units 3 and 4 that are eligible for financing under the Loan Guarantee Agreement (Eligible Project Costs). Aggregate borrowings under the FFB Credit Facility may not exceed the lesser of (i) 70% of Eligible Project Costs or (ii) approximately $3.46 billion. See Note 6 to the financial statements under DOE Loan Guarantee Borrowings for additional information regarding the Loan Guarantee Agreement and Note 3 to the financial statements under Retail Regulatory Matters Georgia Power Nuclear Construction for additional information regarding Plant Vogtle Units 3 and 4.

Eligible Project Costs incurred through December 31, 2014 would allow for borrowings of up to $2.1 billion under the FFB Credit Facility. Through December 31, 2014, Georgia Power had borrowed $1.2 billion under the FFB Credit Facility, leaving $0.9 billion of currently available borrowing ability.

Mississippi Power received $245 million of DOE Grants in prior years that were used for the construction of the Kemper IGCC. An additional $25 million of DOE Grants is expected to be received for the commercial operation of the Kemper IGCC. See Note 3 to the financial statements under Integrated Coal Gasification Combined Cycle for information regarding legislation related to the securitization of certain costs of the Kemper IGCC.

The issuance of securities by the traditional operating companies is generally subject to the approval of the applicable state PSC. The issuance of all securities by Mississippi Power and Southern Power and short-term securities by Georgia Power is generally subject to regulatory approval by the FERC. Additionally, with respect to the public offering of securities, Southern Company and certain of its subsidiaries file registration statements with the SEC under the Securities Act of 1933, as amended (1933 Act). The amounts of securities authorized by the appropriate regulatory authorities, as well as the securities registered under the 1933 Act, are continuously monitored and appropriate filings are made to ensure flexibility in the capital markets.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Southern Company, each traditional operating company, and Southern Power obtain financing separately without credit support from any affiliate. See Note 6 to the financial statements under Bank Credit Arrangements for additional information. The Southern Company system does not maintain a centralized cash or money pool. Therefore, funds of each company are not commingled with funds of any other company in the Southern Company system.

As of December 31, 2014, Southern Company s current liabilities exceeded current assets by $2.6 billion, primarily due to long-term debt of the traditional operating companies and Southern Power that is due within one year of $3.3 billion. To meet short-term cash needs and contingencies, Southern Company has substantial cash flow from operating activities and access to capital markets and financial institutions.

At December 31, 2014, Southern Company and its subsidiaries had approximately $710 million of cash and cash equivalents. Committed credit arrangements with banks at December 31, 2014 were as follows:

	Expires						Executable Term Loans		Due Within One Year	
							One	Two	Term	No Term
Company	**2015**	**2016**	**2017**	**2018**	**Total**	**Unused**	**Year**	**Years**	**Out**	**Out**
					(in millions)		*(in millions)*		*(in millions)*	
Southern Company	$	$	$	$ 1,000	$ 1,000	$ 1,000	$	$	$	$
Alabama Power	228	50		1,030	1,308	1,308	58		58	170
Georgia Power		150		1,600	1,750	1,736				
Gulf Power	80	165	30		275	275	50		50	30
Mississippi Power	135	165			300	300	25	40	65	70
				500	500	488				

Southern Power																			
Other		70								70		70		20				20		50
Total	$	513	$	530	$	30	$	4,130	$	5,203	$	5,177	$	153	$	40	$	193	$	320

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

A portion of the unused credit with banks is allocated to provide liquidity support to the traditional operating companies variable rate pollution control revenue bonds and commercial paper programs. The amount of variable rate pollution control revenue bonds outstanding requiring liquidity support as of December 31, 2014 was approximately $1.8 billion. In addition, at December 31, 2014, the traditional operating companies had $476 million of fixed rate pollution control revenue bonds outstanding that were required to be remarketed within the next 12 months. As of December 31, 2014, $98 million of certain pollution control revenue bonds of Georgia Power were reclassified to securities due within one year in anticipation of their redemption in connection with unit retirement decisions.

Subject to applicable market conditions, Southern Company and its subsidiaries expect to renew their bank credit arrangements as needed, prior to expiration.

Most of these bank credit arrangements contain covenants that limit debt levels and contain cross default provisions to other indebtedness (including guarantee obligations) that are restricted only to the indebtedness of the individual company. Such cross default provisions to other indebtedness would trigger an event of default if the applicable borrower defaulted on indebtedness or guarantee obligations over a specified threshold. Southern Company, the traditional operating companies, and Southern Power are currently in compliance with all such covenants. None of the bank credit arrangements contain material adverse change clauses at the time of borrowings.

Southern Company, the traditional operating companies, and Southern Power make short-term borrowings primarily through commercial paper programs that have the liquidity support of the committed bank credit arrangements described above. Southern Company, the traditional operating companies, and Southern Power may also borrow through various other arrangements with banks. Commercial paper and short-term bank term loans are included in notes payable in the balance sheets.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Details of short-term borrowings were as follows:

	Short-term Debt at the End of the Period		Short-term Debt During the Period [a]		
	Amount Outstanding *(in millions)*	Weighted Average Interest Rate	Average Outstanding *(in millions)*	Weighted Average Interest Rate	Maximum Amount Outstanding *(in millions)*
December 31, 2014:					
Commercial paper	**$ 803**	**0.3%**	**$ 754**	**0.2%**	**$ 1,582**
Short-term bank debt		**%**	**98**	**0.8%**	**400**
Total	**$ 803**	**0.3%**	**$ 852**	**0.3%**	
December 31, 2013:					
Commercial paper	$ 1,082	0.2%	$ 993	0.3%	$ 1,616
Short-term bank debt	400	0.9%	107	0.9%	400
Total	$ 1,482	0.4%	$ 1,100	0.3%	
December 31, 2012:					
Commercial paper	$ 820	0.3%	$ 550	0.3%	$ 938
		%	116	1.2%	300

Short-term bank debt						
Total	$	820	0.3%	$	666	0.5%

(a) Average and maximum amounts are based upon daily balances during the twelve-month periods ended December 31, 2014, 2013, and 2012.

The Company believes the need for working capital can be adequately met by utilizing commercial paper programs, lines of credit, bank notes, and cash from operations.

Financing Activities

During 2014, Southern Company issued approximately 20.8 million shares of common stock (including approximately 5.0 million treasury shares) for approximately $806 million through the employee and director stock plans and the Southern Investment Plan. The Company may satisfy its obligations with respect to the plans in several ways, including through using newly issued shares or treasury shares or acquiring shares on the open market through the independent plan administrators.

From August 2013 through December 2014, Southern Company used shares held in treasury, to the extent available, and newly issued shares to satisfy the requirements under the Southern Investment Plan and the employee savings plan. Beginning in January 2015, Southern Company ceased issuing additional shares under the Southern Investment Plan and the employee savings plan. All sales under these plans are now being funded with shares acquired on the open market by the independent plan administrators.

Beginning in 2015, Southern Company expects to repurchase shares of common stock to offset all or a portion of the incremental shares issued under its employee and director stock plans, including through stock option exercises. The Southern Company Board of Directors has approved the repurchase of up to 20 million shares of common stock for such purpose until December 31, 2017. Repurchases may be made by means of open market purchases, privately negotiated transactions, or accelerated or other share repurchase programs, in accordance with applicable securities laws.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

The following table outlines the long-term debt financing activities for Southern Company and its subsidiaries for the year ended December 31, 2014:

Company	Senior Note Issuances	Senior Note Maturities	Revenue Bond Issuances and Remarketings of Purchased Bonds[(a)]	Revenue Bond Redemptions	Other Long-Term Debt Issuances	Other Long-Term Debt Redemptions[(b)] and Maturities
	(in millions)					
Southern Company	$ 750	$ 350	$	$	$	$
Alabama Power	400		254	254		
Georgia Power			40	37	1,200	5
Gulf Power	200	75	42	29		
Mississippi Power					493	256
Southern Power					10	10
Other						19
Elimination[(c)]					(220)	(220)
	$ 1,350	$ 425	$ 336	$ 320	$ 1,483	$ 70

Total

(a) Includes remarketing by Gulf Power of $13 million aggregate principal amount of revenue bonds previously purchased and held by Gulf Power since December 2013 and remarketing by Georgia Power of $40 million aggregate principal amount of revenue bonds previously purchased and held by Georgia Power since 2010.

(b) Includes reductions in capital lease obligations resulting from cash payments under capital leases.

(c) Intercompany loan from Southern Company to Mississippi Power eliminated in Southern Company s Consolidated Financial Statements. This loan was repaid on September 29, 2014.

In May 2014, Southern Company s $350 million aggregate principal amount of its Series 2009A 4.15% Senior Notes due May 15, 2014 matured.

In August 2014, Southern Company issued $400 million aggregate principal amount of Series 2014A 1.30% Senior Notes due August 15, 2017 and $350 million aggregate principal amount of Series 2014B 2.15% Senior Notes due September 1, 2019. The proceeds were used to pay a portion of Southern Company s outstanding short-term indebtedness and for other general corporate purposes.

Southern Company s subsidiaries used the proceeds of the debt issuances shown in the table above for the redemptions and maturities shown in the table above, to repay short-term indebtedness, and for general corporate purposes, including their respective continuous construction programs.

In addition to the amounts reflected in the table above, in June 2014, Southern Company entered into a 90-day floating rate bank loan bearing interest based on one-month LIBOR. This short-term loan was for $250 million aggregate principal amount and the proceeds were used for working capital and other general corporate purposes, including the investment by Southern Company in its subsidiaries. This bank loan was repaid in August 2014.

In addition to the amounts reflected in the table above, in January 2014 and October 2014, Mississippi Power received an additional $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. See Note 3 to the financial statements under Integrated Coal Gasification Combined Cycle Proposed Sale of Undivided Interest to SMEPA for additional information.

Georgia Power s Other Long-Term Debt Issuances reflected in the table above include borrowings under the FFB Credit Facility in an aggregate principal amount of $1.0 billion on February 20, 2014 and $200 million on December 11, 2014. The interest rate applicable to $500 million of the initial advance under the FFB Credit Facility is 3.860% for an interest period that extends to 2044 and the interest rate applicable to the remaining $500 million is 3.488% for an interest period that extends to 2029 and is expected to be reset from time to time thereafter through 2044. The interest rate applicable to the $200 million advance in December 2014 is 3.002% for an interest period that extends to 2044. The final maturity date for all advances under the FFB Credit Facility is February 20, 2044. The proceeds of the borrowings in 2014 under the FFB Credit Facility were used to reimburse Georgia Power for Eligible Project Costs relating to the construction of Plant Vogtle Units 3 and 4. In connection with its entry into the agreements with the DOE and the FFB, Georgia Power incurred issuance costs of approximately $66 million, which are being amortized over the life of the borrowings under the FFB Credit Facility.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Under the Loan Guarantee Agreement, Georgia Power is subject to customary events of default, as well as cross-defaults to other indebtedness and events of default relating to any failure to make payments under the engineering, procurement, and construction contract, as amended, relating to Plant Vogtle Units 3 and 4 or certain other agreements providing intellectual property rights for Plant Vogtle Units 3 and 4. The Loan Guarantee Agreement also includes events of default specific to the DOE loan guarantee program, including the failure of Georgia Power or Southern Nuclear to comply with requirements of law or DOE loan guarantee program requirements. See Note 6 to the financial statements under DOE Loan Guarantee Borrowings for additional information.

In February 2014, Georgia Power repaid three four-month floating rate bank loans in an aggregate principal amount of $400 million.

During 2014, Alabama Power entered into forward-starting interest rate swaps to hedge exposure to interest rate changes related to an anticipated debt issuance. The notional amount of the swaps totaled $200 million.

In October 2014, Georgia Power entered into interest rate swaps to hedge exposure to interest rate changes related to existing debt. The notional amount of the swaps totaled $900 million.

In November and December 2014, Georgia Power entered into forward-starting interest rate swaps to hedge exposure to interest rate changes related to anticipated borrowings under the FFB Credit Facility in 2015. The notional amount of the swaps totaled $700 million.

Subsequent to December 31, 2014, Alabama Power announced the redemption of $250 million aggregate principal amount of its Series DD 5.65% Senior Notes due March 15, 2035, which will occur on March 16, 2015.

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

Credit Rating Risk

Southern Company and its subsidiaries do 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 contracts that could require collateral, but not accelerated payment, in the event of a credit rating change of certain subsidiaries to BBB and Baa2, or BBB- and/or Baa3 or below. These contracts are for physical electricity purchases and sales, fuel purchases, fuel transportation and storage, energy price risk management, interest rate derivatives, and construction of new generation at Plant Vogtle Units 3 and 4.

The maximum potential collateral requirements under these contracts at December 31, 2014 were as follows:

Credit Ratings	Maximum

	Potential Collateral Requirements
	(in millions)
At BBB and Baa2	$ 9
At BBB- and/or Baa3	435
Below BBB- and/or Baa3	2,305

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

Generally, collateral may be provided by a Southern Company guaranty, letter of credit, or cash. Additionally, any credit rating downgrade could impact the ability of Southern Company and its subsidiaries to access capital markets, particularly the short-term debt market and the variable rate pollution control revenue bond market.

Market Price Risk

The Southern Company system is exposed to market risks, primarily commodity price risk and interest rate risk. The Southern Company system may also occasionally have limited exposure to foreign currency exchange rates. To manage the volatility attributable to these exposures, the applicable 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 applicable company s policies in areas such as counterparty exposure and risk management practices. The Southern Company system 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.

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

To mitigate future exposure to a change in interest rates, Southern Company and certain of its subsidiaries enter into derivatives that have been designated as hedges. Derivatives outstanding at December 31, 2014 have a notional amount of $2.1 billion and are related to fixed and floating rate obligations. The weighted average interest rate on $3.4 billion of long-term variable interest rate exposure at January 1, 2015 was 0.94%. If Southern 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 $34 million at January 1, 2015. See Note 1 to the financial statements under Financial Instruments and Note 11 to the financial statements for additional information.

Due to cost-based rate regulation and other various cost recovery mechanisms, the traditional operating companies continue to have limited exposure to market volatility in interest rates, foreign currency, commodity fuel prices, and prices of electricity. In addition, Southern Power s exposure to market volatility in commodity fuel prices and prices of electricity is limited because its long-term sales contracts shift substantially all fuel cost responsibility to the purchaser. However, Southern Power has been and may continue to be exposed to market volatility in energy-related commodity prices as a result of uncontracted generating capacity. To mitigate residual risks relative to movements in electricity prices, the traditional operating companies enter 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 traditional operating companies continue to manage fuel-hedging programs implemented per the guidelines of their respective state PSCs. Southern 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	2013
	Changes	Changes
	Fair Value	
	(in millions)	
Contracts outstanding at the beginning of the period, assets (liabilities), net	**$ (32)**	$ (85)
Contracts realized or settled:		
Swaps realized or settled	**(9)**	43
Options realized or settled	**6**	19

Current period changes[(a)]:		
Swaps	**(131)**	2
Options	**(22)**	(11)
Contracts outstanding at the end of the period, assets (liabilities), net	**$ (188)**	$ (32)

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

The net hedge volumes of energy-related derivative contracts for the years ended December 31 were as follows:

		2014	2013
		mmBtu Volume *(in millions)*	
Commodity	Natural gas swaps	**200**	216
Commodity	Natural gas options	**44**	59
Total hedge volume		**244**	275

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. The change in option fair value is primarily attributable to the volatility of the market and the underlying change in the natural gas price. The majority of the natural gas hedge gains and losses are recovered through the traditional operating companies fuel cost recovery clauses.

At December 31, 2014 and 2013, substantially all of the Southern Company system s energy-related derivative contracts were designated as regulatory hedges and were related to the applicable 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 energy cost recovery clause. Certain other gains and losses on energy-related derivatives, designated as cash flow hedges, 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 income as incurred and were not material for any year presented.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

Southern 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 10 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	Maturity		
	Fair Value	Year 1	Years 2&3	Years 4&5
	(in millions)			
Level 1	$	$	$	$
Level 2	(188)	(109)	(76)	(3)
Level 3				
Fair value of contracts outstanding at end of period	$ (188)	$ (109)	$ (76)	$ (3)

Southern Company is exposed to market price risk in the event of nonperformance by counterparties to energy-related and interest rate derivative contracts. Southern 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, Southern 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 11 to the financial statements.

Southern Company performs periodic reviews of its leveraged lease transactions, both domestic and international, and the creditworthiness of the lessees, including a review of the value of the underlying leased assets and the credit ratings of the lessees. Southern Company s domestic lease transactions generally do not have any credit enhancement mechanisms; however, the lessees in its international lease transactions have pledged various deposits as additional security to secure the obligations. The lessees in the Company s international lease transactions are also required to provide additional collateral in the event of a credit downgrade below a certain level.

Capital Requirements and Contractual Obligations

The Southern Company system s construction program is currently estimated to be $6.7 billion for 2015, $5.4 billion for 2016, and $4.3 billion for 2017, which includes expenditures related to the construction and start-up of the Kemper IGCC of $801 million for 2015 and $132 million for 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 $1.0 billion, $0.5 billion, and $0.6 billion for 2015, 2016, and 2017, respectively. The Southern Company system s amounts include capital expenditures related to contractual purchase commitments for nuclear fuel and 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 CO_2 emissions from new, existing, and modified or reconstructed fossil-fuel-fired electric generating units. See FUTURE EARNINGS POTENTIAL Environmental Matters Global Climate Issues for additional information.

See FUTURE EARNINGS POTENTIAL Environmental Matters Environmental Statutes and Regulations herein for additional information.

The construction programs are 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; 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; 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; storm impacts; and the cost of capital. In addition, there can be no assurance that costs related to capital expenditures will be fully recovered. Additionally, planned expenditures for plant acquisitions may vary due to market opportunities and Southern Power s ability to execute its growth strategy. See Note 3 to the financial statements under Retail Regulatory Matters Georgia Power Nuclear Construction and Integrated Coal Gasification Combined Cycle for information regarding additional factors that may impact construction expenditures.

In addition, the construction program includes the development and construction of new generating facilities with designs that have not been finalized or previously constructed, including first-of-a-kind technology, which may result in revised estimates during construction. The ability to control costs and avoid cost overruns during the development and construction of new facilities is subject to a number of factors, including, but not limited to, labor costs and productivity, adverse weather conditions,

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MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

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 any PSC).

As a result of NRC requirements, Alabama Power and Georgia Power have external trust funds for nuclear decommissioning costs; however, Alabama Power currently has no additional funding requirements. For additional information, see Note 1 to the financial statements under Nuclear Decommissioning.

In addition, as discussed in Note 2 to the financial statements, Southern Company provides postretirement benefits to substantially all employees and funds trusts to the extent required by the traditional operating companies respective regulatory commissions.

Other funding requirements related to obligations associated with scheduled maturities of long-term debt, as well as the related interest, derivative obligations, preferred and preference stock dividends, leases, and other purchase commitments are detailed in the contractual obligations table that follows. See Notes 1, 2, 5, 6, 7, and 11 to the financial statements for additional information.

Contractual Obligations

	2015	2016-2017	2018-2019	After 2019	Total
			(in millions)		
Long-term debt[a]					
Principal	$ 3,302	$ 3,345	$ 2,050	$ 15,282	$ 23,979
Interest	857	1,563	1,355	11,379	15,154
Preferred and preference stock dividends[b]	68	136	136		340
Financial derivative obligations[c]	138	76	3		217
	100	154	73	248	575

Operating leases[d]					
Capital leases[d]	31	25	22	81	159
Unrecognized tax benefits[e]	170				170
Purchase commitments					
Capital[f]	6,222	8,899			15,121
Fuel[g]	4,012	5,155	3,321	9,869	22,357
Purchased power[h]	327	738	761	3,892	5,718
Other[i]	233	476	378	1,369	2,456
Trusts					
Nuclear decommissioning[j]	5	11	11	110	137
Pension and other postretirement benefit plans[k]	112	224			336
Total	$ 15,577	$ 20,802	$ 8,110	$ 42,230	$ 86,719

(a) All amounts are reflected based on final maturity dates. Southern Company and its subsidiaries plan to continue, when economically feasible, to retire higher-cost securities and replace these obligations with lower-cost capital if market conditions permit. Variable rate interest obligations are estimated based on rates as of 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) Represents preferred and preference stock of subsidiaries. Preferred and preference stock do not mature; therefore, amounts are provided for the next five years only.

(c) Includes derivative liabilities related to cash flow hedges of forecasted debt, as well as energy-related derivatives. For additional information, see Notes 1 and 11 to the financial statements.

(d) Excludes PPAs that are accounted for as leases and included in purchased power.

(e) See Note 5 to the financial statements under Unrecognized Tax Benefits for additional information.

(f) The Southern Company system 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. See Note 3 to the financial statements under Integrated Coal Gasification Combined Cycle for additional information. These amounts exclude contractual purchase commitments for nuclear fuel and capital expenditures covered under long-term service agreements which are reflected separately. At December 31, 2014, significant purchase commitments were outstanding in connection with the construction program. See FUTURE EARNINGS POTENTIAL Environmental Matters Environmental Statutes and Regulations herein for additional information.

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

(g) Primarily includes commitments to purchase coal, nuclear fuel, 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.

(h) Estimated minimum long-term obligations for various PPA purchases from gas-fired, biomass, and wind-powered facilities. A total of $1.1 billion of biomass PPAs is contingent upon the counterparties meeting specified contract dates for commercial operation and may change as a result of regulatory action. See FUTURE EARNINGS POTENTIAL Retail Regulatory Matters Georgia Power Renewables Development for additional information.

(i) Includes long-term service agreements and contracts for the procurement of limestone. Long-term service agreements include price escalation based on inflation indices.

(j) Projections of nuclear decommissioning trust fund contributions for Plant Hatch and Plant Vogtle Units 1 and 2 are based on the 2013 ARP for Georgia Power. Alabama Power also has external trust funds for nuclear decommissioning costs; however, Alabama Power currently has no additional funding requirements. See Note 1 to the financial statements under Nuclear Decommissioning for additional information.

(k) The Southern Company system forecasts contributions to the pension and other postretirement benefit plans over a three-year period. Southern 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 corporate assets of Southern Company s subsidiaries. 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 corporate assets of Southern Company s subsidiaries.

Cautionary Statement Regarding Forward-Looking Statements

Southern Company s 2014 Annual Report contains forward-looking statements. Forward-looking statements include, among other things, statements concerning retail rates, the strategic goals for the wholesale business, 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, postretirement benefit plan, and nuclear decommissioning trust fund contributions, financing activities, completion dates of acquisitions and construction projects, filings with state and federal regulatory authorities, impact of the TIPA, estimated sales and purchases under power sale and purchase agreements, 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, p 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, CO_2, soot, particulate matter, hazardous air pollutants, including mercury, and other substances, and also changes in tax and other laws and regulations to which Southern Company and its subsidiaries are subject, as well as changes in application of existing laws and regulations;

current and future litigation, regulatory investigations, proceedings, or inquiries, including pending EPA civil actions against certain Southern Company subsidiaries, FERC matters, and IRS and state tax audits;

the effects, extent, and timing of the entry of additional competition in the markets in which Southern Company s subsidiaries operate;

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 any 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;

MANAGEMENT S DISCUSSION AND ANALYSIS (continued)

investment performance of Southern Company s employee and retiree benefit plans and the Southern Company system s nuclear decommissioning trust funds;

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;

legal proceedings and regulatory approvals and actions related to Plant Vogtle Units 3 and 4, including Georgia PSC approvals and NRC actions and related legal proceedings involving the commercial parties;

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 Mississippi Power and the Mississippi PSC, the March 2013 rate order regarding retail rate increases, or the Baseload Act;

the ability to successfully operate the electric utilities generating, transmission, and distribution facilities and the successful performance of necessary corporate functions;

the inherent risks involved in operating and constructing nuclear generating facilities, including environmental, health, regulatory, natural disaster, terrorism, or financial risks;

the performance of projects undertaken by the non-utility businesses and the success of efforts to invest in and develop new opportunities;

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 Southern Company or its subsidiaries;

the ability of counterparties of Southern Company and its subsidiaries 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 Southern Company system 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 Southern Company s or any of its subsidiaries 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, as well as potential impacts on the benefits of the DOE loan guarantees;

the ability of Southern Company s subsidiaries 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 Southern Company system 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 Southern Company from time to time with the SEC.

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

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CONSOLIDATED STATEMENTS OF INCOME

For the Years Ended December 31, 2014, 2013, and 2012

Southern Company and Subsidiary Companies 2014 Annual Report

	2014	2013	2012
		(in millions)	
Operating Revenues:			
Retail revenues	**$ 15,550**	$ 14,541	$ 14,187
Wholesale revenues	**2,184**	1,855	1,675
Other electric revenues	**672**	639	616
Other revenues	**61**	52	59
Total operating revenues	**18,467**	17,087	16,537
Operating Expenses:			
Fuel	**6,005**	5,510	5,057
Purchased power	**672**	461	544
Other operations and maintenance	**4,354**	3,846	3,772
Depreciation and amortization	**1,945**	1,901	1,787
Taxes other than income taxes	**981**	934	914
	868	1,180	

Estimated loss on Kemper IGCC						
Total operating expenses		**14,825**		13,832		12,074
Operating Income		**3,642**		3,255		4,463
Other Income and (Expense):						
Allowance for equity funds used during construction		**245**		190		143
Interest income		**19**		19		40
Interest expense, net of amounts capitalized		**(835)**		(824)		(859)
Other income (expense), net		**(63)**		(81)		(38)
Total other income and (expense)		**(634)**		(696)		(714)
Earnings Before Income Taxes		**3,008**		2,559		3,749
Income taxes		**977**		849		1,334
Consolidated Net Income		**2,031**		1,710		2,415
Dividends on Preferred and Preference Stock of Subsidiaries		**68**		66		65
Consolidated Net Income After Dividends on Preferred and Preference Stock of Subsidiaries	**$**	**1,963**	$	1,644	$	2,350
Common Stock Data:						
Earnings per share (EPS)						
Basic EPS	**$**	**2.19**	$	1.88	$	2.70

Diluted EPS	**2.18**	1.87	2.67
Average number of shares of common stock outstanding (in millions)			
Basic	**897**	877	871
Diluted	**901**	881	879

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

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

For the Years Ended December 31, 2014, 2013, and 2012

Southern Company and Subsidiary Companies 2014 Annual Report

	2014	2013	2012
		(in millions)	
Consolidated Net Income	**$ 2,031**	$ 1,710	$ 2,415
Other comprehensive income:			
Qualifying hedges:			
Changes in fair value, net of tax of $(6), $-, and $(7), respectively	**(10)**		(12)
Reclassification adjustment for amounts included in net income, net of tax of $3, $5, and $7, respectively	**5**	9	11
Marketable securities:			
Change in fair value, net of tax of $-, $(2), and $-, respectively		(3)	
Pension and other postretirement benefit plans:			
Benefit plan net gain (loss), net of tax of $(32), $22, and $(2), respectively	**(51)**	36	(3)
Reclassification adjustment for amounts included in net income, net of tax of $2, $4, and $(4), respectively	**3**	6	(8)
Total other comprehensive income (loss)	**(53)**	48	(12)
	(68)	(66)	(65)

Dividends on preferred and preference stock of subsidiaries			
Consolidated Comprehensive Income	**$ 1,910**	$ 1,692	$ 2,338

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2014, 2013, and 2012

Southern Company and Subsidiary Companies 2014 Annual Report

	2014	2013	2012
		(in millions)	
Operating Activities:			
Consolidated net income	**$ 2,031**	$ 1,710	$ 2,415
Adjustments to reconcile consolidated net income to net cash provided from operating activities			
Depreciation and amortization, total	**2,293**	2,298	2,145
Deferred income taxes	**709**	496	1,096
Investment tax credits	**35**	302	128
Allowance for equity funds used during construction	**(245)**	(190)	(143)
Pension, postretirement, and other employee benefits	**(515)**	131	(398)
Stock based compensation expense	**63**	59	55
Estimated loss on Kemper IGCC	**868**	1,180	
Other, net	**(38)**	(41)	51
Changes in certain current assets and liabilities			
-Receivables	**(352)**	(153)	234
-Fossil fuel stock	**408**	481	(452)
-Materials and supplies	**(67)**	36	(97)
-Other current assets	**(57)**	(11)	(37)
-Accounts payable	**267**	72	(89)
-Accrued taxes	**(105)**	(85)	(71)
-Accrued compensation	**255**	(138)	(28)
-Mirror CWIP	**180**		
-Other current liabilities	**85**	(50)	89
Net cash provided from operating activities	**5,815**	6,097	4,898
Investing Activities:			
Property additions	**(5,977)**	(5,463)	(4,809)
Investment in restricted cash	**(11)**	(149)	(280)
Distribution of restricted cash	**57**	96	284
Nuclear decommissioning trust fund purchases	**(916)**	(986)	(1,046)
Nuclear decommissioning trust fund sales	**914**	984	1,043
Cost of removal, net of salvage	**(170)**	(131)	(149)
Change in construction payables, net	**(107)**	(126)	(84)
Prepaid long-term service agreement	**(181)**	(91)	(146)
Other investing activities	**(17)**	124	19
Net cash used for investing activities	**(6,408)**	(5,742)	(5,168)
Financing Activities:			
Increase (decrease) in notes payable, net	**(676)**	662	(30)
Proceeds			

Long-term debt issuances	**3,169**	2,938	4,404
Interest-bearing refundable deposit	**125**		150
Preference stock		50	
Common stock issuances	**806**	695	397
Redemptions and repurchases			
Long-term debt	**(816)**	(2,830)	(3,169)
Common stock repurchased	**(5)**	(20)	(430)
Payment of common stock dividends	**(1,866)**	(1,762)	(1,693)
Payment of dividends on preferred and preference stock of subsidiaries	**(68)**	(66)	(65)
Other financing activities	**(25)**	9	19
Net cash provided from (used for) financing activities	**644**	(324)	(417)
Net Change in Cash and Cash Equivalents	**51**	31	(687)
Cash and Cash Equivalents at Beginning of Year	**659**	628	1,315
Cash and Cash Equivalents at End of Year	**$ 710**	$ 659	$ 628

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

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CONSOLIDATED BALANCE SHEETS

At December 31, 2014 and 2013

Southern Company and Subsidiary Companies 2014 Annual Report

Assets	2014	2013
	(in millions)	
Current Assets:		
Cash and cash equivalents	**$ 710**	$ 659
Receivables		
Customer accounts receivable	**1,090**	1,027
Unbilled revenues	**432**	448
Under recovered regulatory clause revenues	**136**	58
Other accounts and notes receivable	**307**	304
Accumulated provision for uncollectible accounts	**(18)**	(18)
Fossil fuel stock, at average cost	**930**	1,339
Materials and supplies, at average cost	**1,039**	959
Vacation pay	**177**	171
Prepaid expenses	**665**	278
	506	143

Deferred income taxes, current		
Other regulatory assets, current	**346**	207
Other current assets	**50**	39
Total current assets	**6,370**	5,614
Property, Plant, and Equipment:		
In service	**70,013**	66,021
Less accumulated depreciation	**24,059**	23,059
Plant in service, net of depreciation	**45,954**	42,962
Other utility plant, net	**211**	240
Nuclear fuel, at amortized cost	**911**	855
Construction work in progress	**7,792**	7,151
Total property, plant, and equipment	**54,868**	51,208
Other Property and Investments:		
Nuclear decommissioning trusts, at fair value	**1,546**	1,465
Leveraged leases	**743**	665
Miscellaneous property and investments	**203**	218
Total other property and investments	**2,492**	2,348

Deferred Charges and Other Assets:		
Deferred charges related to income taxes	**1,510**	1,436
Prepaid pension costs		419
Unamortized debt issuance expense	**202**	139
Unamortized loss on reacquired debt	**243**	269
Other regulatory assets, deferred	**4,334**	2,495
Other deferred charges and assets	**904**	618
Total deferred charges and other assets	**7,193**	5,376
Total Assets	**$ 70,923**	$ 64,546

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

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CONSOLIDATED BALANCE SHEETS

At December 31, 2014 and 2013

Southern Company and Subsidiary Companies 2014 Annual Report

Liabilities and Stockholders Equity		**2014**		2013
		(in millions)		
Current Liabilities:				
Securities due within one year	**$**	**3,333**	$	469
Interest-bearing refundable deposit		**275**		150
Notes payable		**803**		1,482
Accounts payable		**1,593**		1,376
Customer deposits		**390**		380
Accrued taxes				
Accrued income taxes		**151**		13
Other accrued taxes		**487**		456
Accrued interest		**295**		251
Accrued vacation pay		**223**		217
Accrued compensation		**576**		303
		26		82

Other regulatory liabilities, current		
Mirror CWIP	**271**	
Other current liabilities	**544**	346
Total current liabilities	**8,967**	5,525
Long-Term Debt (See accompanying statements)	**20,841**	21,344
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	**11,568**	10,563
Deferred credits related to income taxes	**192**	203
Accumulated deferred investment tax credits	**1,208**	966
Employee benefit obligations	**2,432**	1,461
Asset retirement obligations	**2,168**	2,006
Other cost of removal obligations	**1,215**	1,275
Other regulatory liabilities, deferred	**398**	479
Other deferred credits and liabilities	**594**	585
Total deferred credits and other liabilities	**19,775**	17,538
Total Liabilities	**49,583**	44,407
Redeemable Preferred Stock of Subsidiaries (See accompanying statements)	**375**	375
	39	

Redeemable Noncontrolling Interest (See accompanying statements)				
Total Stockholders Equity (See accompanying statements)		**20,926**		19,764
Total Liabilities and Stockholders Equity	**$**	**70,923**	$	64,546
Commitments and Contingent Matters (See notes)				

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

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CONSOLIDATED STATEMENTS OF CAPITALIZATION

At December 31, 2014 and 2013

Southern Company and Subsidiary Companies 2014 Annual Report

		2014	2013	**2014**	2013
		(in millions)		*(percent of total)*	
Long-Term Debt:					
Long-term debt payable to affiliated trusts					
Variable rate (3.36% at 1/1/15) due 2042		**$ 206**	$ 206		
Total long-term debt payable to affiliated trusts		**206**	206		
Long-term senior notes and debt					
Maturity	Interest Rates				
2014	3.25% to 4.90%		428		
2015	0.55% to 5.25%	**2,375**	2,375		
2016	1.95% to 5.30%	**1,360**	1,360		
2017	1.30% to 5.90%	**1,495**	1,095		
2018	2.20% to 5.40%	**850**	850		
2019	2.15% to 5.55%	**1,175**	825		
2020 through 2051	1.63% to 6.38%	**10,574**	9,973		
Variable rate (1.29% at 1/1/14) due 2014			11		
Variable rates (0.77% to 1.17% at 1/1/15) due 2015		**775**	525		
Variable rates (0.56% to 0.63% at 1/1/15) due 2016		**450**	450		
Total long-term senior notes and debt		**19,054**	17,892		
Other long-term debt					
Pollution control revenue bonds					
Maturity	Interest Rates				
2019	4.55%	**25**	25		
2022 through 2049	0.28% to 6.00%	**1,466**	1,453		
Variable rates (0.03% to 0.04% at 1/1/15) due 2015		**152**	54		
Variable rate (0.04% at 1/1/15) due 2016		**4**	4		
Variable rate (0.04% to 0.06% at 1/1/15) due 2017		**36**	36		
Variable rate (0.04% at 1/1/14) due 2018			19		
Variable rates (0.01% to 0.09% at 1/1/15) due 2020 to 2052		**1,566**	1,642		
Plant Daniel revenue bonds (7.13%) due 2021		**270**	270		
FFB loans (3.00% to 3.86%) due 2044		**1,200**			
Total other long-term debt		**4,719**	3,503		
Capitalized lease obligations		**159**	163		
Unamortized debt premium		**69**	79		
Unamortized debt discount		**(33)**	(30)		
Total long-term debt (annual interest requirement	$857 million)	**24,174**	21,813		
Less amount due within one year		**3,333**	469		
Long-term debt excluding amount due within one year		**20,841**	21,344	**49.4%**	51.5%
Redeemable Preferred Stock of Subsidiaries:					

Cumulative preferred stock				
$100 par or stated value 4.20% to 5.44%				
Authorized 20 million shares				
Outstanding 1 million shares	**81**	81		
$1 par value 5.20% to 5.83%				
Authorized 28 million shares				
Outstanding 12 million shares: $25 stated value	**294**	294		
Total redeemable preferred stock of subsidiaries (annual dividend requirement $20 million)	**375**	375	**0.9**	0.9
Redeemable Noncontrolling Interest	**39**		**0.1**	

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CONSOLIDATED STATEMENTS OF CAPITALIZATION (continued)

At December 31, 2014 and 2013

Southern Company and Subsidiary Companies 2014 Annual Report

	2014	2013	**2014**	2013
	(in millions)		*(percent of total)*	
Common Stockholders Equity:				
Common stock, par value $5 per share	**4,539**	4,461		
Authorized 1.5 billion shares				
Issued 2014: 909 million shares				
2013: 893 million shares				
Treasury 2014: 0.7 million shares				
2013: 5.7 million shares				
Paid-in capital	**5,955**	5,362		
Treasury, at cost	**(26)**	(250)		
Retained earnings	**9,609**	9,510		
Accumulated other comprehensive loss	**(128)**	(75)		
Total common stockholders equity	**19,949**	19,008	**47.3**	45.8
Preferred and Preference Stock of Subsidiaries and Noncontrolling Interest:				
Non-cumulative preferred stock				
$25 par value 6.00% to 6.13%				
Authorized 60 million shares				
Outstanding 2 million shares	**45**	45		
Preference stock				
Authorized 65 million shares				
Outstanding $1 par value	**343**	343		
5.63% to 6.50% 14 million shares (non-cumulative)				
Outstanding $100 par or stated value	**368**	368		
5.60% to 6.50% 4 million shares (non-cumulative)				
Noncontrolling Interest	**221**			
Total preferred and preference stock of subsidiaries and noncontrolling interest (annual dividend requirement $48 million)	**977**	756	**2.3**	1.8
Total stockholders equity	**20,926**	19,764		
Total Capitalization	**$ 42,181**	$ 41,483	**100.0%**	100.0%

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

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CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

For the Years Ended December 31, 2014, 2013, and 2012

Southern Company and Subsidiary Companies 2014 Annual Report

	Southern Company Common Stockholders Equity									
	Number of Common Shares		Common Stock				Accumulated Other Comprehensive Income (Loss)	Preferred and Preference Stock of Subsidiaries	Noncontrolling Interest	Total
	Issued	Treasury	Par Value	Paid-In Capital	Treasury	Retained Earnings				
	(in thousands)		*(in millions)*							
Balance at December 31, 2011	865,664	(539)	$ 4,328	$ 4,410	$ (17)	$ 8,968	$ (111)	$ 707	$	$ 18,285
Net income after dividends on preferred and preference stock of subsidiaries						2,350				2,350
Other comprehensive income (loss)							(12)			(12)
Stock issued	12,139		61	336						397
Stock repurchased, at cost		(9,440)			(430)					(430)
Stock-based compensation				106						106
Cash dividends of $1.9425 per share						(1,693)				(1,693)
Other		(56)		3	(3)	1				1
Balance at December 31, 2012	877,803	(10,035)	4,389	4,855	(450)	9,626	(123)	707		19,004
Net income after dividends on preferred and preference						1,644				1,644

stock of subsidiaries										
Other comprehensive income (loss)							48			48
Stock issued	14,930	4,443	72	441	203			49		765
Stock-based compensation				65						65
Cash dividends of $2.0125 per share						(1,762)				(1,762)
Other		(55)		1	(3)	2				
Balance at December 31, 2013	**892,733**	**(5,647)**	**4,461**	**5,362**	**(250)**	**9,510**	**(75)**	**756**		**19,764**
Net income after dividends on preferred and preference stock of subsidiaries						**1,963**				**1,963**
Other comprehensive income (loss)							**(53)**			**(53)**
Stock issued	**15,769**	**4,996**	**78**	**501**	**227**					**806**
Stock-based compensation				**86**						**86**
Cash dividends of $2.0825 per share						**(1,866)**				**(1,866)**
Contributions from noncontrolling interest									**221**	**221**
Net income attributable to noncontrolling interest									**(2)**	**(2)**
Other		**(74)**		**6**	**(3)**	**2**			**2**	**7**
Balance at December 31, 2014	**908,502**	**(725)**	**$ 4,539**	**$ 5,955**	**$ (26)**	**$ 9,609**	**$ (128)**	**$ 756**	**$ 221**	**$ 20,926**

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

NOTES TO FINANCIAL STATEMENTS

Southern Company and Subsidiary Companies 2014 Annual Report

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NOTES (continued)

Southern Company and Subsidiary Companies 2014 Annual Report

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

The Southern Company (Southern Company or the Company) is the parent company of four traditional operating companies, 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 Mississippi Power are vertically integrated utilities providing electric service in four Southeastern states. 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 financial statements reflect Southern Company s investments in the subsidiaries on a consolidated basis. The equity method is used for entities in which the Company has significant influence but does not control and for variable interest entities where the Company has an equity investment, but is not the primary beneficiary. All material intercompany transactions have been eliminated in consolidation.

The traditional operating companies, Southern Power, and certain of their subsidiaries are subject to regulation by the FERC, and the traditional operating companies are also subject to regulation by their respective state PSCs. The companies follow GAAP in the U.S. and comply with the accounting policies and practices prescribed by their respective 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. Southern Company continues to evaluate the requirements of ASC 606. The ultimate impact of the new standard has not yet been determined.

Regulatory Assets and Liabilities

The traditional operating companies are 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.

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NOTES (continued)

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

	2014	2013	Note
	(in millions)		
Retiree benefit plans	**$ 3,469**	$ 1,760	(a,p)
Deferred income tax charges	**1,458**	1,376	(b)
Loss on reacquired debt	**267**	293	(c)
Fuel-hedging-asset	**202**	58	(d,p)
Deferred PPA charges	**185**	180	(e,p)
Vacation pay	**177**	171	(f,p)
Under recovered regulatory clause revenues	**157**	70	(g)
Kemper IGCC regulatory assets	**148**	76	(h)
Asset retirement obligations-asset	**119**	145	(b,p)
Nuclear outage	**99**	78	(g)
Property damage reserves-asset	**98**	37	(i)
Cancelled construction projects	**67**	70	(j)
Environmental remediation-asset	**64**	62	(k,p)
Deferred income tax charges Medicare subsidy	**57**	65	(l)
Other regulatory assets	**195**	222	(m)
Other cost of removal obligations	**(1,229)**	(1,289)	(b)
Kemper regulatory liability (Mirror CWIP)	**(271)**	(91)	(h)
Deferred income tax credits	**(192)**	(203)	(b)
Property damage reserves-liability	**(181)**	(191)	(n)
Asset retirement obligations-liability	**(130)**	(139)	(b,p)
Other regulatory liabilities	**(95)**	(126)	(o)
Total regulatory assets (liabilities), net	**$ 4,664**	$ 2,624	

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

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

(b) Asset retirement and removal assets and liabilities are recorded, deferred income tax assets are recovered, and deferred income tax liabilities are amortized over the related property lives, which may range up to 70 years. Asset retirement and removal assets and liabilities will be settled and trued up following completion of the related activities. At December 31, 2014, other cost of removal obligations included $29 million that will be amortized over the two-year period from January 2015 through December 2016 in accordance with Georgia Power s 2013 ARP. See Note 3 under Retail Regulatory Matters Georgia Power Rate Plans for additional information. At December 31, 2014, other cost of removal obligations included $8.4 million recorded as authorized by the Florida

PSC in the Settlement Agreement approved in December 2013 (Gulf Power Settlement Agreement).

(c) Recovered over either the remaining life of the original issue or, if refinanced, over the remaining life of the new issue, which may range up to 50 years.

(d) Recorded over the life of the underlying hedged purchase contracts, which generally do not exceed five years. Upon final settlement, actual costs incurred are recovered through the energy cost recovery clause.

(e) Recovered over the life of the PPA for periods up to nine years.

(f) Recorded as earned by employees and recovered as paid, generally within one year. This includes both vacation and banked holiday pay.

(g) Recorded and recovered or amortized as approved or accepted by the appropriate state PSCs over periods not exceeding 10 years.

(h) For additional information, see Note 3 under Integrated Coal Gasification Combined Cycle Rate Recovery of Kemper IGCC Costs Regulatory Assets and Liabilities.

(i) Recorded and recovered or amortized as approved or accepted by the appropriate state PSCs over periods generally not exceeding eight years.

(j) Costs associated with construction of environmental controls that will not be completed as a result of unit retirements being amortized as approved by the Georgia PSC over periods not exceeding nine years or through 2022.

(k) Recovered through the environmental cost recovery clause when the remediation is performed.

(l) Recovered and amortized as approved by the appropriate state PSCs over periods not exceeding 15 years.

(m) Comprised of numerous immaterial components including property taxes, generation site selection/evaluation costs, demand side management cost deferrals, regulatory deferrals, building leases, net book value of retired generating units, Plant Daniel Units 3 and 4

NOTES (continued)

regulatory assets, and other miscellaneous assets. These costs are recorded and recovered or amortized as approved by the appropriate state PSC over periods generally not exceeding 10 years or, as applicable, over the remaining life of the asset but not beyond 2031.

(n) Recovered as storm restoration and potential reliability-related expenses are incurred as approved by the appropriate state PSCs.

(o) Comprised of numerous immaterial components including over-recovered regulatory clause revenues, fuel-hedging liabilities, mine reclamation and remediation liabilities, PPA credits, nuclear disposal fees, and other liabilities that are recorded and recovered or amortized as approved by the appropriate state PSCs generally over periods not exceeding 10 years.

(p) Not earning a return as offset in rate base by a corresponding asset or liability.

In the event that a portion of a traditional operating company s operations is no longer subject to applicable accounting rules for rate regulation, such company would be required to write off to income or reclassify to accumulated OCI related regulatory assets and liabilities that are not specifically recoverable through regulated rates. In addition, the traditional operating company would be required to determine if any impairment to other assets, including plant, exists and write down the assets, if impaired, to their fair values. All regulatory assets and liabilities are to be reflected in rates. See Note 3 under Retail Regulatory Matters Alabama Power, Retail Regulatory Matters Georgia Power, and Integrated Coal Gasification Combined Cycle for additional information.

Revenues

Wholesale capacity revenues from PPAs are recognized either on a levelized basis over the appropriate contract period or the amount billable under the contract terms. Energy and other revenues are recognized as services are provided. Unbilled revenues related to retail sales are accrued at the end of each fiscal period. Electric rates for the traditional operating companies include provisions to adjust billings for fluctuations in fuel costs, fuel hedging, the energy component of purchased power costs, and certain other costs. Revenues are adjusted for differences between these actual costs and 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.

Southern Company s electric utility subsidiaries have 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.

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 expense also includes the amortization of the cost of nuclear fuel and a charge, based on nuclear generation, for the permanent disposal of spent nuclear fuel.

Income and Other Taxes

Southern Company uses the liability method of accounting for deferred income taxes and provides deferred income taxes for all significant income tax temporary differences. Taxes that are collected from customers on behalf of governmental agencies to be remitted to these agencies are presented net on the statements of income.

In accordance with regulatory requirements, deferred federal ITCs for the traditional operating companies are amortized over the average lives of the related property with such amortization normally applied as a credit to reduce depreciation in the statements of income. Credits amortized in this manner amounted to $22 million in 2014, $16 million in 2013, and $23 million in 2012. At December 31, 2014, all ITCs available to reduce federal income taxes payable had not been utilized. The remaining ITCs will be carried forward and utilized in future years. Additionally, several subsidiaries have state ITCs, which are recognized in the period in which the credit is claimed on the state income tax return. A portion of the state ITCs available to reduce state income taxes payable was not utilized currently and will be carried forward and utilized in future years.

Under the American Recovery and Reinvestment Act of 2009 and the American Taxpayer Relief Act of 2012 (ATRA), certain projects at Southern Power are eligible for federal ITCs or cash grants. Southern Power has elected to receive ITCs. The credits are recorded as a deferred credit and are amortized to income tax expense over the life of the asset. Credits amortized in this manner amounted to $11.4 million in 2014, $5.5 million in 2013, and $2.6 million in 2012. Also, Southern Power received cash related to federal ITCs under the renewable energy incentives of $74 million, $158 million, and $45 million for the years ended December 31, 2014, 2013, and 2012, respectively, which had a material impact on cash flows. Furthermore, the tax basis of the asset is reduced by 50% of the credits received, resulting in a net deferred tax asset. Southern Power has elected to recognize the tax benefit of this basis difference as a reduction to income tax expense in the year in which the plant reaches commercial operation. The tax benefit of the related basis differences reduced income tax expense by $48 million in 2014, $31 million in 2013, and $8 million in 2012.

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

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NOTES (continued)

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.

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

	2014	2013
	(in millions)	
Generation	**$ 37,892**	$ 35,360
Transmission	**9,884**	9,289
Distribution	**17,123**	16,499
General	**4,198**	3,958
Plant acquisition adjustment	**123**	123
Utility plant in service	**69,220**	65,229
Information technology equipment and software	**244**	242
Communications equipment	**439**	437
Other	**110**	113
Other plant in service	**793**	792
Total plant in service	**$ 70,013**	$ 66,021

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 as incurred or performed with the exception of nuclear refueling costs, which are recorded in accordance with specific state PSC orders. Alabama Power and Georgia Power defer and amortize nuclear refueling costs over the unit s operating cycle. The refueling cycles for Alabama Power s Plant Farley and Georgia Power s Plants Hatch and Vogtle Units 1 and 2 range from 18 to 24 months, depending on the unit.

Assets acquired under a capital lease are included in property, plant, and equipment and are further detailed in the table below:

	Asset Balances at December 31,	
	2014	2013
	(in millions)	
Office building	**$ 61**	$ 61
Nitrogen plant	**83**	83

Computer-related equipment	**60**	62
Gas pipeline	**6**	6
Less: Accumulated amortization	**(49)**	(48)
Balance, net of amortization	**$ 161**	$ 164

The amount of non-cash property additions recognized for the years ended December 31, 2014, 2013, and 2012 was $528 million, $411 million, and $524 million, respectively. These amounts are comprised of construction-related accounts payable outstanding at each year end. Also, the amount of non-cash property additions associated with capitalized leases for the years ended December 31, 2014, 2013, and 2012 was $25 million, $107 million, and $14 million, respectively.

Acquisitions

Southern Power acquires generation assets as part of its overall growth strategy. Southern Power accounts for business acquisitions from non-affiliates as business combinations. Accordingly, Southern Power has included these operations in the consolidated financial statements from the respective date of acquisition. The purchase price, including contingent consideration, if any, of each acquisition was allocated based on the fair value of the identifiable assets and liabilities. Assets acquired that do not meet the definition of a business in accordance with GAAP are accounted for as asset acquisitions. The purchase price of each asset acquisition was allocated based on the relative fair value of assets acquired. Any due diligence or transition costs incurred by Southern Power for successful or potential acquisitions have been expensed as incurred.

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NOTES (continued)

Acquisitions entered into or made by Southern Power during 2014 and 2013 are detailed in the table below:

	MW Capacity	Percentage Ownership	Year of Operation	Party Under PPA Contract for Plant Output	PPA Contract Period	Purchase Price *(millions)*
SG2 Imperial Valley, LLC [(a)]	150	51%	2014	San Diego Gas & Electric Company	25 years	$ 504.7[(c)]
Macho Springs Solar LLC [(b)]	50	90	2014	El Paso Electric Company	20 years	$ 130.0[(d)]
Adobe Solar, LLC [(b)]	20	90	2014	Southern California Edison Company	20 years	$ 96.2[(d)]
Campo Verde Solar, LLC [(b)(e)]	139	90	2013	San Diego Gas & Electric Company	20 years	$ 136.6[(d)]

(a) This acquisition was made by Southern Power through its subsidiaries Southern Renewable Partnerships, LLC and SG2 Holdings, LLC. SG2 Holdings, LLC is jointly-owned by Southern Power and First Solar, Inc.

(b) This acquisition was made by Southern Power and Turner Renewable Energy, LLC through Southern Turner Renewable Energy, LLC.

(c) Reflects Southern Power s portion of the purchase price.

(d) Reflects 100% of the purchase price, including Turner Renewable Energy, LLC s 10% equity contribution.

(e) Under an engineering, procurement, and construction agreement, an additional $355.5 million was paid to a subsidiary of First Solar, Inc. to complete the construction of the solar facility.

Depreciation and Amortization

Depreciation of the original cost of utility plant in service is provided primarily by using composite straight-line rates, which approximated 3.1% in 2014, 3.3% in 2013, and 3.2% in 2012. Depreciation studies are conducted periodically to update the composite rates. These studies are filed with the respective state PSC and the FERC for the traditional operating companies. Accumulated depreciation for utility plant in service totaled $23.5 billion and $22.5 billion at December 31, 2014 and 2013, respectively. When property subject to composite 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. For other property dispositions, the applicable cost and accumulated depreciation are removed from the balance sheet accounts, and a gain or loss is recognized. Minor items of property included in the original cost of the plant are retired when the related property unit is retired. Certain of Southern Power s generation assets are now depreciated on a units-of-production basis, using hours or starts, to better match outage and maintenance costs to the usage of and revenues from these assets. Cost, net of salvage value, of these assets is depreciated on an hours or starts units-of-production basis. The book value of plant-in-service as of December 31, 2014 that is depreciated on a units-of-production basis was approximately $470.2 million.

In 2009, the Georgia PSC approved an accounting order allowing Georgia Power to amortize a portion of its regulatory liability related to other cost of removal obligations. Under the terms of Georgia Power s Alternate Rate Plan for the years 2011 through 2013 (2010 ARP), Georgia Power amortized approximately $31 million annually of the remaining regulatory liability related to other cost of removal obligations over the three years ended December 31, 2013. Under the terms of the 2013 ARP, an additional $14 million is being amortized annually by Georgia Power over the three years ending December 31, 2016. See Note 3 under Retail Regulatory Matters Georgia Power Rate Plans for additional information.

Depreciation of the original cost of other plant in service is provided primarily on a straight-line basis over estimated useful lives ranging from three to 25 years. Accumulated depreciation for other plant in service totaled $533 million and $513 million at December 31, 2014 and 2013, respectively.

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. Each traditional operating company has received accounting guidance from the various state PSCs allowing the continued accrual of other future retirement costs for long-lived assets that it does not have a legal obligation to retire. Accordingly, the accumulated removal costs for these obligations are reflected in the balance sheets as a regulatory liability.

The liability for AROs primarily relates to the decommissioning of the Southern Company system s nuclear facilities, Plants Farley, Hatch, and Vogtle. In addition, the Southern Company system has retirement obligations related to various landfill sites, ash ponds, asbestos removal, mine reclamation, and disposal of polychlorinated biphenyls in certain transformers. The Southern Company system also has identified retirement obligations related to certain transmission and distribution facilities, certain wireless communication towers, property associated with the Southern Company system s rail lines and natural gas pipelines, and certain structures authorized by the U.S. Army Corps of Engineers. However, liabilities for the removal of these

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NOTES (continued)

assets have not been recorded because the settlement timing for the retirement obligations related to these assets is indeterminable and, therefore, the fair value of the retirement obligations cannot be reasonably estimated. A liability for these AROs will be recognized when sufficient information becomes available to support a reasonable estimation of the ARO. The Company will continue to recognize in the statements of income allowed removal costs in accordance with regulatory treatment. Any differences between costs recognized in accordance with accounting standards related to asset retirement and environmental obligations and those reflected in rates are recognized as either a regulatory asset or liability, as ordered by the various state PSCs, and are reflected in the balance sheets. See Nuclear Decommissioning herein for additional information on amounts included in rates.

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

	2014	2013
	(in millions)	
Balance at beginning of year	**$ 2,018**	$ 1,757
Liabilities incurred	**18**	6
Liabilities settled	**(17)**	(16)
Accretion	**102**	97
Cash flow revisions	**80**	174
Balance at end of year	**$ 2,201**	$ 2,018

The cash flow revisions in 2014 are primarily related to Alabama Power s and SEGCO s AROs associated with asbestos at their steam generation facilities. The cash flow revisions in 2013 are primarily related to revisions to the nuclear decommissioning ARO based on Alabama Power s updated decommissioning study and Georgia Power s updated estimates for ash ponds in connection with the retirement of certain coal-fired generating units.

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 traditional operating companies 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, Southern Company has developed a preliminary nominal dollar estimate of costs associated with closure and groundwater monitoring of ash ponds in place of approximately $860 million and ongoing post-closure care of approximately $140 million. Certain of the traditional operating companies have previously recorded AROs associated with ash ponds of $506 million, or $468 million on a nominal dollar basis, based on existing state requirements. During 2015, the traditional operating companies will record AROs for any incremental estimated closure costs resulting from acceleration in the timing of any currently planned closures and for differences between existing state requirements and the requirements of the CCR Rule. Southern Company s results of operations, cash flows, and financial condition could be significantly impacted if such costs are not recovered through regulated rates.

Nuclear Decommissioning

The NRC requires licensees of commercial nuclear power reactors to establish a plan for providing reasonable assurance of funds for future decommissioning. Alabama Power and Georgia Power have external trust funds (Funds) to comply with the NRC s regulations. Use of the Funds is restricted to nuclear decommissioning activities. The Funds are managed and invested in accordance with applicable requirements of various regulatory bodies, including the NRC, the FERC, and state PSCs, as well as the IRS. While Alabama Power and Georgia Power are allowed to prescribe an overall investment policy to the Funds managers, neither Southern Company nor its subsidiaries or affiliates are allowed to engage in the day-to-day management of the Funds or to mandate individual investment decisions. Day-to-day management of the investments in the Funds is delegated to unrelated third party managers with oversight by the management of Southern Company, Alabama Power, and Georgia Power. The Funds managers are authorized, within certain investment guidelines, to actively buy and sell securities at their own discretion in order to maximize the return on the Funds investments. The Funds are invested in a tax-efficient manner in a diversified mix of equity and fixed income securities and are reported as trading securities.

Southern Company records the investment securities held in the Funds at fair value, as disclosed in Note 10, as management believes that fair value best represents the nature of the Funds. Gains and losses, whether realized or unrealized, are recorded in the regulatory liability for AROs in the balance sheets and are not included in net income or OCI. Fair value adjustments and realized gains and losses are determined on a specific identification basis.

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NOTES (continued)

The Funds at Georgia Power participate in a securities lending program through the managers of the Funds. Under this program, the Funds investment securities are loaned to institutional investors for a fee. Securities loaned are fully collateralized by cash, letters of credit, and/or securities issued or guaranteed by the U.S. government or its agencies or instrumentalities. As of December 31, 2014 and 2013, approximately $51 million and $32 million, respectively, of the fair market value of the Funds securities were on loan and pledged to creditors under the Funds managers securities lending program. The fair value of the collateral received was approximately $52 million and $33 million at December 31, 2014 and 2013, respectively, and can only be sold by the borrower upon the return of the loaned securities. The collateral received is treated as a non-cash item in the statements of cash flows.

At December 31, 2014, investment securities in the Funds totaled $1.5 billion, consisting of equity securities of $886 million, debt securities of $638 million, and $19 million of other securities. At December 31, 2013, investment securities in the Funds totaled $1.5 billion, consisting of equity securities of $896 million, debt securities of $528 million, and $40 million of other securities. These amounts include the investment securities pledged to creditors and collateral received and exclude receivables related to investment income and pending investment sales and payables related to pending investment purchases and the lending pool.

Sales of the securities held in the Funds resulted in cash proceeds of $913 million, $1.0 billion, and $1.0 billion in 2014, 2013, and 2012, respectively, all of which were reinvested. For 2014, fair value increases, including reinvested interest and dividends and excluding the Funds expenses, were $98 million, of which $2 million related to realized gains and $19 million related to unrealized gains and losses related to securities held in the Funds at December 31, 2014. For 2013, fair value increases, including reinvested interest and dividends and excluding the Funds expenses, were $181 million, of which $5 million related to realized gains and $119 million related to unrealized gains related to securities held in the Funds at December 31, 2013. For 2012, fair value increases, including reinvested interest and dividends and excluding the Funds expenses, were $137 million, of which $4 million related to realized gains and $75 million related to unrealized gains related to securities held in the Funds at December 31, 2012. While the investment securities held in the Funds are reported as trading securities, the Funds continue to be managed with a long-term focus. Accordingly, all purchases and sales within the Funds are presented separately in the statements of cash flows as investing cash flows, consistent with the nature of the securities and purpose for which the securities were acquired.

For Alabama Power, amounts previously recorded in internal reserves are being transferred into the Funds over periods approved by the Alabama PSC. The NRC s minimum external funding requirements are based on a generic estimate of the cost to decommission only the radioactive portions of a nuclear unit based on the size and type of reactor. Alabama Power and Georgia Power have filed plans with the NRC designed to ensure that, over time, the deposits and earnings of the Funds will provide the minimum funding amounts prescribed by the NRC.

At December 31, 2014 and 2013, the accumulated provisions for decommissioning were as follows:

	External Trust Funds		**Internal Reserves**		**Total**	
	2014	2013	**2014**	2013	**2014**	2013
			(in millions)			
	$ 754	$ 713	**$ 21**	$ 21	**$ 775**	$ 734

Plant Farley				
Plant Hatch	**496**	469	**496**	469
Plant Vogtle Units 1 and 2	**293**	277	**293**	277

Site study cost is the estimate to decommission a specific facility as of the site study year. The decommissioning cost estimates are based on prompt dismantlement and removal of the plant from service. The actual decommissioning costs may vary from these estimates because of changes in the assumed date of decommissioning, changes in NRC requirements, or changes in the assumptions used in making these estimates. The estimated costs of decommissioning as of December 31, 2014 based on the most current studies, which were performed in 2013 for Alabama Power s Plant Farley and in 2012 for the Georgia Power plants, were as follows for Alabama Power s Plant Farley and Georgia Power s ownership interests in Plant Hatch and Plant Vogtle Units 1 and 2:

	Plant Farley	Plant Hatch	Plant Vogtle Units 1 and 2
Decommissioning periods:			
Beginning year	2037	2034	2047
Completion year	2076	2068	2072
		(in millions)	
Site study costs:			
Radiated structures	$ 1,362	$ 549	$ 453
Spent fuel management		131	115
Non-radiated structures	80	51	76
Total site study costs	$ 1,442	$ 731	$ 644

NOTES (continued)

For ratemaking purposes, Alabama Power s decommissioning costs are based on the site study, and Georgia Power s decommissioning costs are based on the NRC generic estimate to decommission the radioactive portion of the facilities and the site study estimate for spent fuel management as of 2012. Under the 2013 ARP, the Georgia PSC approved Georgia Power s annual decommissioning cost through 2016 for ratemaking of $4 million and $2 million for Plant Hatch and Plant Vogtle Units 1 and 2, respectively. Georgia Power expects the Georgia PSC to periodically review and adjust, if necessary, the amounts collected in rates for nuclear decommissioning costs. Significant assumptions used to determine these costs for ratemaking were an inflation rate of 4.5% and 2.4% for Alabama Power and Georgia Power, respectively, and a trust earnings rate of 7.0% and 4.4% for Alabama Power and Georgia Power, respectively.

Amounts previously contributed to the Funds for Plant Farley are currently projected to be adequate to meet the decommissioning obligations. Alabama Power will continue to provide site-specific estimates of the decommissioning costs and related projections of funds in the external trust to the Alabama PSC and, if necessary, would seek the Alabama PSC s approval to address any changes in a manner consistent with NRC and other applicable requirements.

Allowance for Funds Used During Construction and Interest Capitalized

In accordance with regulatory treatment, the traditional operating companies record 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 calculating taxable income. Interest related to the construction of new facilities not included in the traditional operating companies regulated rates is capitalized in accordance with standard interest capitalization requirements. AFUDC and interest capitalized, net of income taxes were 16.0%, 15.0%, and 8.2% of net income for 2014, 2013, and 2012, respectively.

Cash payments for interest totaled $732 million, $759 million, and $803 million in 2014, 2013, and 2012, respectively, net of amounts capitalized of $111 million, $92 million, and $83 million, respectively.

Impairment of Long-Lived Assets and Intangibles

Southern 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.

Storm Damage Reserves

Each traditional operating company maintains a reserve to cover or is allowed to defer and recover the cost of damages from major storms to its transmission and distribution lines and generally the cost of uninsured damages to its generation facilities and other property. In accordance with their respective state PSC orders, the traditional operating companies accrued $40 million in 2014 and $28 million in 2013. Alabama Power, Gulf Power, and Mississippi Power also have authority based on orders from their state PSCs to accrue certain additional amounts as circumstances warrant. In 2014 and 2013, there were no such additional accruals. See Note 3 under Retail Regulatory Matters Alabama Power Natural Disaster Reserve and Retail Regulatory Matters Georgia Power Storm Damage Recovery for additional information regarding Alabama Power s NDR and Georgia Power s deferred storm costs, respectively.

Leveraged Leases

Southern Company has several leveraged lease agreements, with original terms ranging up to 45 years, which relate to international and domestic energy generation, distribution, and transportation assets. Southern Company receives federal income tax deductions for depreciation and amortization, as well as interest on long-term debt related to these investments. The Company reviews all important lease assumptions at least annually, or more frequently if events or changes in circumstances indicate that a change in assumptions has occurred or may occur. These assumptions include the effective tax rate, the residual value, the credit quality of the lessees, and the timing of expected tax cash flows.

Southern Company s net investment in domestic and international leveraged leases consists of the following at December 31:

	2014	2013
	(in millions)	
Net rentals receivable	**$ 1,495**	$ 1,440
Unearned income	**(752)**	(775)
Investment in leveraged leases	**743**	665
Deferred taxes from leveraged leases	**(299)**	(287)
Net investment in leveraged leases	**$ 444**	$ 378

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NOTES (continued)

A summary of the components of income from the leveraged leases follows:

	2014	2013	2012
		(in millions)	
Pretax leveraged lease income (loss)	**$ 24**	$ (5)	$ 21
Income tax expense	**(9)**	2	(8)
Net leveraged lease income (loss)	**$ 15**	$ (3)	$ 13

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, and generating plant materials. Materials are charged to inventory when purchased and then expensed or capitalized to plant, as appropriate, at weighted average cost when installed.

Fuel Inventory

Fuel inventory includes the average cost of coal, natural gas, oil, transportation, and emissions allowances. Fuel is charged to inventory when purchased and then expensed, at weighted average cost, as used and recovered by the traditional operating companies through fuel cost recovery rates approved by each state PSC. Emissions allowances granted by the EPA are included in inventory at zero cost.

Financial Instruments

Southern Company and its subsidiaries use 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 10 for additional information regarding fair value. Substantially all of the Southern Company system s bulk energy purchases and sales contracts that meet the definition of a derivative are excluded from fair value accounting requirements because they qualify for the normal scope exception, and are accounted for under the accrual method. Derivative contracts that qualify as cash flow hedges of anticipated transactions or are recoverable through the traditional operating companies fuel-hedging programs result in the deferral of related gains and losses in OCI or regulatory assets and liabilities, respectively, until the hedged transactions occur. Any ineffectiveness arising from cash flow hedges is recognized currently in net income. 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 income. See Note 11 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. At December 31, 2014, the amount included in accounts payable in the balance sheets that the Company has recognized for the obligation to return cash collateral arising from derivative instruments was immaterial.

Southern 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 and marketable securities, certain changes in pension and other postretirement benefit plans, reclassifications for amounts included in net income, and dividends on preferred and preference stock of subsidiaries.

Accumulated OCI (loss) balances, net of tax effects, were as follows:

	Qualifying Hedges	Marketable Securities	Pension and Other Postretirement Benefit Plans	Accumulated Other Comprehensive Income (Loss)
		(in millions)		
Balance at December 31, 2013	$ (36)	$	$ (39)	$ (75)
Current period change	(5)		(48)	(53)
Balance at December 31, 2014	**$ (41)**	**$**	**$ (87)**	**$ (128)**

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NOTES (continued)

2. RETIREMENT BENEFITS

Southern 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, certain of the traditional operating companies and other subsidiaries voluntarily contributed an aggregate of $500 million to the qualified pension plan. No mandatory contributions to the qualified pension plan are anticipated for the year ending December 31, 2015. Southern 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, Southern Company provides certain medical care and life insurance benefits for retired employees through other postretirement benefit plans. The traditional operating companies fund related other postretirement trusts to the extent required by their respective regulatory commissions. For the year ending December 31, 2015, other postretirement trust contributions are expected to total approximately $19 million.

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 4.88%, respectively, and an annual salary increase of 3.84%.

	2014	2013	2012
Discount rate:			
Pension plans	**4.17%**	5.02%	4.26%
Other postretirement benefit plans	**4.04**	4.85	4.05
Annual salary increase	**3.59**	3.59	3.59
Long-term return on plan assets:			
Pension plans	**8.20**	8.20	8.20
	7.15	7.13	7.29

Other postretirement benefit plans

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 $636 million and $92 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**
	(in millions)	
Benefit obligation	$ 140	$ (117)
Service and interest costs	6	(5)

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NOTES (continued)

Pension Plans

The total accumulated benefit obligation for the pension plans was $10.0 billion at December 31, 2014 and $8.1 billion 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
	(in millions)	
Change in benefit obligation		
Benefit obligation at beginning of year	**$ 8,863**	$ 9,302
Service cost	**213**	232
Interest cost	**435**	389
Benefits paid	**(382)**	(357)
Actuarial (gain) loss	**1,780**	(703)
Balance at end of year	**10,909**	8,863
Change in plan assets		
Fair value of plan assets at beginning of year	**8,733**	7,953
Actual return on plan assets	**797**	1,098
Employer contributions	**542**	39
Benefits paid	**(382)**	(357)
Fair value of plan assets at end of year	**9,690**	8,733
Accrued liability	**$ (1,219)**	$ (130)

At December 31, 2014, the projected benefit obligations for the qualified and non-qualified pension plans were $10.3 billion and $617 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
	(in millions)	
Prepaid pension costs	**$**	$ 419
Other regulatory assets, deferred	**3,073**	1,651
Other current liabilities	**(42)**	(40)

Employee benefit obligations	**(1,177)**	(509)
Accumulated OCI	**134**	64

Presented below are the amounts included in accumulated OCI and 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.

	Prior Service Cost	**Net (Gain) Loss**
	(in millions)	
Balance at December 31, 2014:		
Accumulated OCI	**$ 4**	**$ 130**
Regulatory assets	**51**	**3,022**
Total	**$ 55**	**$ 3,152**
Balance at December 31, 2013:		
Accumulated OCI	$ 5	$ 59
Regulatory assets	75	1,575
Total	$ 80	$ 1,634
Estimated amortization in net periodic pension cost in 2015:		
Accumulated OCI	$ 1	$ 9
Regulatory assets	24	206
Total	$ 25	$ 215

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NOTES (continued)

The components of OCI and 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:

	Accumulated OCI	Regulatory Assets
	(in millions)	
Balance at December 31, 2012	$ 125	$ 3,013
Net gain	(52)	(1,145)
Change in prior service costs		1
Reclassification adjustments:		
Amortization of prior service costs	(1)	(26)
Amortization of net gain (loss)	(8)	(192)
Total reclassification adjustments	(9)	(218)
Total change	(61)	(1,362)
Balance at December 31, 2013	$ 64	$ 1,651
Net gain	**75**	**1,552**
Change in prior service costs		**1**
Reclassification adjustments:		
Amortization of prior service costs	**(1)**	**(25)**
Amortization of net gain (loss)	**(4)**	**(106)**
Total reclassification adjustments	**(5)**	**(131)**
Total change	**70**	**1,422**
Balance at December 31, 2014	**$ 134**	**$ 3,073**

Components of net periodic pension cost were as follows:

	2014	2013	2012
		(in millions)	
Service cost	**$ 213**	$ 232	$ 198
Interest cost	**435**	389	393
Expected return on plan assets	**(645)**	(603)	(581)

Recognized net loss		**110**		200		95
Net amortization		**26**		27		30
Net periodic pension cost	**$**	**139**	$	245	$	135

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 *(in millions)*
2015	$	522
2016		450
2017		478
2018		499
2019		524
2020 to 2024		2,962

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NOTES (continued)

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
	(in millions)	
Change in benefit obligation		
Benefit obligation at beginning of year	**$ 1,682**	$ 1,872
Service cost	**21**	24
Interest cost	**79**	74
Benefits paid	**(102)**	(94)
Actuarial (gain) loss	**300**	(200)
Plan amendments	**(2)**	
Retiree drug subsidy	**8**	6
Balance at end of year	**1,986**	1,682
Change in plan assets		
Fair value of plan assets at beginning of year	**901**	821
Actual return on plan assets	**54**	129

Employer contributions		**39**		39
Benefits paid		**(94)**		(88)
Fair value of plan assets at end of year		**900**		901
Accrued liability	**$**	**(1,086)**	$	(781)

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**
		(in millions)		
Other regulatory assets, deferred	**$**	**387**	$	109
Other current liabilities		**(4)**		(4)
Employee benefit obligations		**(1,082)**		(777)
Other regulatory liabilities, deferred		**(21)**		(36)
Accumulated OCI		**8**		1

Presented below are the amounts included in accumulated OCI and 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.

		Prior Service Cost		**Net (Gain) Loss**
		(in millions)		
Balance at December 31, 2014:				
Accumulated OCI	**$**		**$**	**8**

Net regulatory assets (liabilities)		**2**		**364**
Total	**$**	**2**	**$**	**372**
Balance at December 31, 2013:				
Accumulated OCI	$		$	1
Net regulatory assets (liabilities)		9		64
Total	$	9	$	65
Estimated amortization as net periodic postretirement benefit cost in 2015:				
Accumulated OCI	$		$	
Net regulatory assets (liabilities)		4		17
Total	$	4	$	17

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NOTES (continued)

The components of OCI, along with 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:

	Accumulated OCI	Net Regulatory Assets (Liabilities)
	(in millions)	
Balance at December 31, 2012	$ 7	$ 360
Net loss	(6)	(266)
Reclassification adjustments:		
Amortization of transition obligation		(5)
Amortization of prior service costs		(4)
Amortization of net gain (loss)		(12)
Total reclassification adjustments		(21)
Total change	(6)	(287)
Balance at December 31, 2013	$ 1	$ 73
Net gain	**7**	**301**

Change in prior service costs		**(2)**
Reclassification adjustments:		
Amortization of prior service costs		**(4)**
Amortization of net gain (loss)		**(2)**
Total reclassification adjustments		**(6)**
Total change	**7**	**293**
Balance at December 31, 2014	**$ 8**	**$ 366**

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

	2014	2013	2012
		(in millions)	
Service cost	**$ 21**	$ 24	$ 21
Interest cost	**79**	74	85
Expected return on plan assets	**(59)**	(56)	(60)
Net amortization	**6**	21	20
Net periodic postretirement benefit cost	**$ 47**	$ 63	$ 66

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	**Subsidy**	**Total**

	Payments	Receipts	
		(in millions)	
2015	$ 118	$ (10)	$ 108
2016	124	(11)	113
2017	129	(12)	117
2018	132	(13)	119
2019	134	(15)	119
2020 to 2024	670	(79)	591

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NOTES (continued)

Benefit Plan Assets

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

The composition of the Company s pension plan and other postretirement benefit plan assets as of December 31, 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	42%	**41%**	40%
International equity	21	**23**	25
Domestic fixed income	24	**26**	24
Global fixed income	4	**3**	4
Special situations	1		
Real estate investments	5	**5**	5
Private equity	3	**2**	2
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.

Trust-owned life insurance (TOLI). Investments of the Company s taxable trusts aimed at minimizing the impact of taxes on the portfolio.

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.

NOTES (continued)

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 relies on information provided by the plan s trustee. This information is reviewed and evaluated by management with changes made to the trustee information as appropriate.

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

Domestic and international equity. Investments in equity securities such as common stocks, American depositary receipts, and real estate investment trusts that trade on a public exchange are classified as Level 1 investments and are valued at the closing price in the active market. Equity investments with unpublished prices (i.e. pooled funds) are valued as Level 2, when the underlying holdings used to value the investment are comprised of Level 1 or Level 2 equity securities.

Fixed income. Investments in fixed income securities are generally classified as Level 2 investments and are valued based on prices reported in the market place. Additionally, the value of fixed income securities takes into consideration certain items such as broker quotes, spreads, yield curves, interest rates, and discount rates that apply to the term of a specific instrument.

TOLI. Investments in TOLI policies are classified as Level 2 investments and are valued based on the underlying investments held in the policy s separate account. The underlying assets are equity and fixed income pooled funds that are comprised of Level 1 and Level 2 securities.

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.

	Fair Value Measurements Using			
As of December 31, 2014:	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total**
		(in millions)		
Assets:				
Domestic equity*	$ 1,704	$ 704	$	$ 2,408
International equity*	1,070	986		2,056
Fixed income:				
U.S. Treasury, government, and agency bonds		699		699
Mortgage- and asset-backed securities		188		188
Corporate bonds		1,135		1,135
Pooled funds		514		514
Cash equivalents and other	3	660		663
Real estate investments	293		1,121	1,414
Private equity			570	570

Total	$	3,070	$	4,886	$	1,691	$	9,647
Liabilities:								
Derivatives	$	(2)	$		$		$	(2)
Total	$	3,068	$	4,886	$	1,691	$	9,645

* 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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NOTES (continued)

As of December 31, 2013:	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
		(in millions)		
Assets:				
Domestic equity*	$ 1,433	$ 839	$	$ 2,272
International equity*	1,101	1,018		2,119
Fixed income:				
U.S. Treasury, government, and agency bonds		599		599
Mortgage- and asset-backed securities		156		156
Corporate bonds		978		978
Pooled funds		471		471
Cash equivalents and other	1	223		224
Real estate investments	260		1,000	1,260

Private equity						571		571
Total	$	2,795	$	4,284	$	1,571	$	8,650
Liabilities:								
Derivatives	$		$	(3)	$		$	(3)
Total	$	2,795	$	4,281	$	1,571	$	8,647

* 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**	
			(in millions)					
Beginning balance	**$**	**1,000**	**$**	**571**	$	841	$	593
Actual return on investments:								
Related to investments held at year end		**79**		**51**		74		8
Related to investments sold during the year		**33**		**(16)**		30		51
Total return on investments		**112**		**35**		104		59
Purchases, sales, and settlements		**9**		**(36)**		55		(81)
Ending balance	**$**	**1,121**	**$**	**570**	$	1,000	$	571

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.

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NOTES (continued)

As of December 31, 2014:	Quoted Prices in Active Markets for Identical Assets (Level 1)	Fair Value Measurements Using Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
		(in millions)		
Assets:				
Domestic equity*	$ 147	$ 56	$	$ 203
International equity*	36	67		103
Fixed income:				
U.S. Treasury, government, and agency bonds		29		29
Mortgage- and asset-backed securities		6		6
Corporate bonds		39		39
Pooled funds		41		41
Cash equivalents and other	9	27		36
Trust-owned life insurance		381		381

Real estate investments	11		37	48
Private equity			19	19
Total	$ 203	$ 646	$ 56	$ 905

* 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.

	Fair Value Measurements Using Significant			
	Quoted Prices in Active Markets for Identical Assets	Other Observable Inputs	Significant Unobservable Inputs	
As of December 31, 2013:	**(Level 1)**	**(Level 2)**	**(Level 3)**	**Total**
		(in millions)		
Assets:				
Domestic equity*	$ 157	$ 45	$	$ 202
International equity*	39	82		121
Fixed income:				
U.S. Treasury, government, and agency bonds		34		34
Mortgage- and asset-backed securities		6		6
Corporate bonds		35		35

Pooled funds				46				46
Cash equivalents and other				19				19
Trust-owned life insurance				369				369
Real estate investments		10				36		46
Private equity						20		20
Total	$	206	$	636	$	56	$	898

* 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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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**
		(in millions)		
Beginning balance	**$ 36**	**$ 20**	$ 30	$ 21
Actual return on investments:				
Related to investments held at year end	**1**	**1**	3	
Related to investments sold during the year		**(1)**	1	2
Total return on investments	**1**		4	2
Purchases, sales, and settlements		**(1)**	2	(3)
Ending balance	**$ 37**	**$ 19**	$ 36	$ 20

Employee Savings Plan

Southern 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 $87 million, $84 million, and $82 million, respectively.

3. CONTINGENCIES AND REGULATORY MATTERS

General Litigation Matters

Southern Company and its subsidiaries are subject to certain claims and legal actions arising in the ordinary course of business. In addition, the business activities of Southern Company s subsidiaries 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 CO_2 and other emissions, CCR, and alleged exposure to hazardous materials, and/or requests for injunctive relief in connection with such matters. The ultimate outcome of such pending or potential litigation against Southern Company and its subsidiaries 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 Southern Company s financial statements.

Insurance Recovery

Mirant Corporation (Mirant) was an energy company with businesses that included independent power projects and energy trading and risk management companies in the U.S. and other countries. Mirant was a wholly-owned subsidiary of Southern Company until its initial public offering in 2000. In 2001, Southern Company completed a spin-off to its stockholders of its remaining ownership, and Mirant became an independent corporate entity.

In 2003, Mirant and certain of its affiliates filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code. In 2005, Mirant, as a debtor in possession, and the unsecured creditors committee filed a complaint against Southern Company. Later in 2005, this complaint was transferred to MC Asset Recovery, LLC (MC Asset Recovery) as part of Mirant s plan of reorganization. In 2009, Southern Company entered into a settlement agreement with MC Asset Recovery to resolve this action. The settlement included an agreement where Southern Company paid MC Asset Recovery $202 million. Southern Company filed an insurance claim in 2009 to recover a portion of this settlement and received payments from its insurance provider of $25 million in June 2012 and $15 million in December 2013. Additionally, legal fees related to these insurance settlements totaled approximately $6 million in 2012 and $4 million in 2013. As a result, the net reduction to expense presented as MC Asset Recovery insurance settlement in the statement of income was approximately $19 million in 2012 and $11 million in 2013.

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 and Georgia Power alleging violations of the New Source Review (NSR) provisions of the Clean Air Act at certain coal-fired electric generating units, including units co-owned by Gulf Power and Mississippi Power. These civil actions seek penalties and injunctive relief, including orders requiring installation of the best available control technologies at the affected units. The case against Georgia Power (including claims related to a unit

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co-owned by Gulf Power) has been administratively closed in the U.S. District Court for the Northern District of Georgia since 2001. The case against Alabama Power (including claims involving a unit co-owned by Mississippi Power) 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.

Southern Company believes the traditional operating companies 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 these matters cannot be determined at this time.

Environmental Remediation

The Southern Company system 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 Southern Company system could incur substantial costs to clean up properties. The traditional operating companies have each received authority from their respective state PSCs to recover approved environmental compliance costs through regulatory mechanisms. These rates are adjusted annually or as necessary within limits approved by the state PSCs.

Georgia Power s environmental remediation liability as of December 31, 2014 was $22 million. Georgia Power has been designated or identified as a potentially responsible party (PRP) at sites governed by the Georgia Hazardous Site Response Act and/or by the federal Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), including a site in Brunswick, Georgia on the CERCLA National Priorities List. The parties have completed the removal of wastes from the Brunswick site as ordered by the EPA. Additional cleanup and claims for recovery of natural resource damages at this site or for the assessment and potential cleanup of other sites are anticipated.

Georgia Power and numerous other entities have been designated by the EPA as PRPs at the Ward Transformer Superfund site located in Raleigh, North Carolina. In 2011, the EPA issued a Unilateral Administrative Order (UAO) to Georgia Power and 22 other parties, ordering specific remedial action of certain areas at the site. Later in 2011, Georgia Power filed a response with the EPA stating it has sufficient cause to believe it is not a liable party under CERCLA. The EPA notified Georgia Power in 2011 that it is considering enforcement options against Georgia Power and other non-complying UAO recipients. If the EPA pursues enforcement actions and the court determines that a respondent failed to comply with the UAO without sufficient cause, the EPA may also seek civil penalties of up to $37,500 per day for the violation and punitive damages of up to three times the costs incurred by the EPA as a result of the party s failure to comply with the UAO.

In addition to the EPA s action at this site, Georgia Power, along with many other parties, was sued in a private action by several existing PRPs for cost recovery related to the removal action. In February 2013, the U.S. District Court for the Eastern District of North Carolina Western Division granted Georgia Power s summary judgment motion, ruling that Georgia Power has no liability in the private action. In May 2013, the plaintiffs appealed the U.S. District Court for the Eastern District of North Carolina Western Division s order to the U.S. Court of Appeals for the Fourth Circuit.

The ultimate outcome of these matters will depend upon the success of defenses asserted, the ultimate number of PRPs participating in the cleanup, and numerous other factors and cannot be determined at this time; however, as a result of Georgia Power s regulatory treatment for environmental remediation expenses, these matters are not expected to have a material impact on Southern Company s financial statements.

Gulf Power s environmental remediation liability includes estimated costs of environmental remediation projects of approximately $48 million as of December 31, 2014. These estimated costs relate to site closure criteria by the Florida Department of Environmental Protection (FDEP) for potential impacts to soil and groundwater from herbicide applications at Gulf Power substations. The schedule for completion of the remediation projects is subject to FDEP approval. The projects have been approved by the Florida PSC for recovery through Gulf Power s environmental cost recovery clause; therefore, these liabilities have no impact on net income.

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

Nuclear Fuel Disposal Costs

Acting through the DOE and pursuant to the Nuclear Waste Policy Act of 1982, the U.S. government entered into contracts with Alabama Power and Georgia Power that require the DOE to dispose of spent nuclear fuel and high level radioactive waste generated at Plants Hatch and Farley and Plant Vogtle Units 1 and 2 beginning no later than January 31, 1998. The DOE has yet

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to commence the performance of its contractual and statutory obligation to dispose of spent nuclear fuel. Consequently, Alabama Power and Georgia Power pursued and continue to pursue legal remedies against the U.S. government for its partial breach of contract.

As a result of the first lawsuit, Georgia Power recovered approximately $27 million, based on its ownership interests, and Alabama Power recovered approximately $17 million, representing the vast majority of the Southern Company system s direct costs of the expansion of spent nuclear fuel storage facilities at Plants Farley and Hatch and Plant Vogtle Units 1 and 2 from 1998 through 2004. In 2012, Alabama Power credited the award to cost of service for the benefit of customers. Also in 2012, Georgia Power credited the award to accounts where the original costs were charged and used it to reduce rate base, fuel, and cost of service for the benefit of customers.

On December 12, 2014, the Court of Federal Claims entered a judgment in favor of Georgia Power and Alabama Power in the second spent nuclear fuel lawsuit seeking damages for the period from January 1, 2005 through December 31, 2010. Georgia Power was awarded approximately $18 million, based on its ownership interests, and Alabama Power was awarded approximately $26 million. No amounts have been recognized in the financial statements as of December 31, 2014. The final outcome of this matter cannot be determined at this time; however, no material impact on Southern Company s net income is expected.

On March 4, 2014, Alabama Power and Georgia Power filed additional lawsuits against the U.S. government for the costs of continuing to store spent nuclear fuel at Plants Farley and Hatch and Plant Vogtle Units 1 and 2 for the period from January 1, 2011 through December 31, 2013. Damages will continue to accumulate until the issue is resolved or storage is provided. No amounts have been recognized in the financial statements as of December 31, 2014 for any potential recoveries from the additional lawsuits. The final outcome of these matters cannot be determined at this time; however, no material impact on Southern Company s net income is expected.

On-site dry spent fuel storage facilities are operational at all three plants and can be expanded to accommodate spent fuel through the expected life of each plant.

Retail Regulatory Matters

Alabama Power

Rate RSE

Alabama Power s Rate RSE adjustments are based on forward-looking information for the applicable upcoming calendar year. Rate adjustments for any two-year period, when averaged together, cannot exceed 4.0% and any annual adjustment is limited to 5.0%. If Alabama Power s actual retail return is above the allowed weighted cost of equity (WCE) range, customer refunds will be required; however, there is no provision for additional customer billings should the actual retail return fall below the WCE range. Prior to 2014, retail rates remained unchanged when the retail ROE was projected to be between 13.0% and 14.5%.

During 2013, the Alabama PSC held public proceedings regarding the operation and utilization of Rate RSE. In August 2013, the Alabama PSC voted to issue a report on Rate RSE that found that Alabama Power s Rate RSE mechanism continues to be just and reasonable to customers and Alabama Power, but recommended Alabama Power modify Rate RSE as follows:

- Eliminate the provision of Rate RSE establishing an allowed range of ROE.
- Eliminate the provision of Rate RSE limiting Alabama Power s capital structure to an allowed equity ratio of 45%.
- Replace these two provisions with a provision that establishes rates based upon the WCE range of 5.75% to 6.21%, with an adjusting point of 5.98%. If calculated under the previous Rate RSE provisions, the resulting WCE would range from 5.85% to 6.53%, with an adjusting point of 6.19%.
- Provide eligibility for a performance-based adder of seven basis points, or 0.07%, to the WCE adjusting point if Alabama Power (i) has an A credit rating equivalent with at least one of the recognized rating agencies or (ii) is in the top one-third of a designated customer value benchmark survey.

Substantially all other provisions of Rate RSE were unchanged.

In August 2013, Alabama Power filed its consent to these recommendations with the Alabama PSC. The changes became effective for calendar year 2014. In November 2013, Alabama Power made its Rate RSE submission to the Alabama PSC of projected data for calendar year 2014; projected earnings were within the specified WCE range and, therefore, retail rates under Rate RSE remained unchanged for 2014. In 2012 and 2013, retail rates under Rate RSE remained unchanged from 2011. Under the terms of Rate RSE, the maxi