SOUTHERN CO
Form 10-Q
November 06, 2007

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2007
OR
o 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	Registrant, State of Incorporation, Address and Telephone Number	I.R.S. Employer Identification No.
1-3526	**The Southern Company** (A Delaware Corporation) 30 Ivan Allen Jr. Boulevard, N.W. Atlanta, Georgia 30308 (404) 506-5000	58-0690070
1-3164	**Alabama Power Company** (An Alabama Corporation) 600 North 18th Street Birmingham, Alabama 35291 (205) 257-1000	63-0004250
1-6468	**Georgia Power Company** (A Georgia Corporation) 241 Ralph McGill Boulevard, N.E. Atlanta, Georgia 30308 (404) 506-6526	58-0257110
0-2429	**Gulf Power Company** (A Florida Corporation) One Energy Place Pensacola, Florida 32520 (850) 444-6111	59-0276810
001-11229	**Mississippi Power Company** (A Mississippi Corporation) 2992 West Beach Gulfport, Mississippi 39501 (228) 864-1211	64-0205820
333-98553	**Southern Power Company** (A Delaware Corporation) 30 Ivan Allen Jr. Boulevard, N.W. Atlanta, Georgia 30308	58-2598670

(404) 506-5000

Table of Contents

Indicate by check mark whether the registrants (1) have 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 registrants were required to file such reports), and (2) have been subject to such filing requirements for the past 90 days. Yes þ *No* o

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

Registrant	**Large Accelerated Filer**	**Accelerated Filer**	**Non-accelerated Filer**
The Southern Company	X		
Alabama Power Company			X
Georgia Power Company			X
Gulf Power Company			X
Mississippi Power Company			X
Southern Power Company			X

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.) Yes o *No* þ (Response applicable to all registrants.)

Registrant	**Description of Common Stock**	**Shares Outstanding at September 30, 2007**
The Southern Company	**Par Value $5 Per Share**	**759,478,801**
Alabama Power Company	**Par Value $40 Per Share**	**15,750,000**
Georgia Power Company	**Without Par Value**	**9,261,500**
Gulf Power Company	**Without Par Value**	**1,792,717**
Mississippi Power Company	**Without Par Value**	**1,121,000**
Southern Power Company	**Par Value $0.01 Per Share**	**1,000**

This combined Form 10-Q is separately filed by The Southern Company, Alabama Power Company, Georgia Power Company, Gulf Power Company, Mississippi Power Company, and Southern Power Company. Information contained herein relating to any individual registrant is filed by such registrant on its own behalf. Each registrant makes no representation as to information relating to the other registrants.

INDEX TO QUARTERLY REPORT ON FORM 10-Q
September 30, 2007

INDEX TO QUARTERLY REPORT ON FORM 10-Q
September 30, 2007

Table of Contents

DEFINITIONS

TERM	MEANING
AFUDC	Allowance for funds used during construction
Alabama Power	Alabama Power Company
ALJ	Administrative law judge
BMA	Bond Market Association
Clean Air Act	Clean Air Act Amendments of 1990
DOE	U.S. Department of Energy
Duke Energy	Duke Energy Corporation
ECO Plan	Environmental Compliance Overview Plan
EPA	U.S. Environmental Protection Agency
ERISA	Employee Retirement Income Security Act of 1974, as amended
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
Form 10-K	Combined Annual Report on Form 10-K of Southern Company, Alabama Power, Georgia Power, Gulf Power, Mississippi Power, and Southern Power for the year ended December 31, 2006 and, with respect to Gulf Power, Amendment No. 1 thereto
Georgia Power	Georgia Power Company
Gulf Power	Gulf Power Company
IGCC	Integrated coal gasification combined cycle
IIC	Intercompany Interchange Contract
IRC	Internal Revenue Code of 1986, as amended
IRS	Internal Revenue Service
KWH	Kilowatt-hour
LIBOR	London Interbank Offered Rate
Mirant	Mirant Corporation
Mississippi Power	Mississippi Power Company
MW	Megawatt
NRC	Nuclear Regulatory Commission
NSR	New Source Review
PEP	Performance Evaluation Plan
Power Pool	The operating arrangement whereby the integrated generating resources of the traditional operating companies and Southern Power 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 certified new plant rate mechanism
Rate ECR	Alabama Power s energy cost recovery rate mechanism
Rate NDR	Alabama Power s natural disaster recovery rate mechanism
Rate RSE	Alabama Power s rate stabilization and equalization rate mechanism
Savannah Electric	Savannah Electric and Power Company (merged into Georgia Power on July 1, 2006)
SCS	Southern Company Services, Inc.
SEC	Securities and Exchange Commission
Southern Company	The Southern Company
Southern Company system	Southern Company, the traditional operating companies, Southern Power, and other subsidiaries

Southern Nuclear	Southern Nuclear Operating Company, Inc.
Southern Power	Southern Power Company
traditional operating companies	Alabama Power, Georgia Power, Gulf Power, and Mississippi Power
wholesale revenues	revenues generated from sales for resale

Table of Contents

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This Quarterly Report on Form 10-Q contains forward-looking statements. Forward-looking statements include, among other things, statements concerning the strategic goals for the wholesale business, retail sales growth, customer growth, storm damage cost recovery and repairs, fuel cost recovery, environmental regulations and expenditures, access to sources of capital, projections for postretirement benefit trust contributions, synthetic fuel investments, financing activities, completion or termination of construction projects, impacts of adoption of new accounting rules, PPA revenues, costs of implementing the IIC settlement with the FERC, and estimated construction and other expenditures. In some cases, forward-looking statements can be identified by terminology such as may, will, could, should, expects, plans, anticipates, believes, estimates, projects, predicts, potential, or continue or 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 change, including legislative and regulatory initiatives regarding deregulation and restructuring of the electric utility industry, implementation of the Energy Policy Act of 2005, environmental laws including regulation of emissions of sulfur, nitrogen, mercury, carbon, soot, or particulate matter 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 the pending EPA civil actions against certain Southern Company subsidiaries, FERC matters, IRS audits, and Mirant matters;
- 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, population and business growth (and declines), and the effects of energy conservation measures;
- available sources and costs of fuels;
- ability to control costs;
- investment performance of Southern Company s employee benefit plans;
- advances in technology;
- state and federal rate regulations and the impact of pending and future rate cases and negotiations, including rate actions relating to fuel and storm restoration cost recovery;
- the performance of projects undertaken by the non-utility businesses and the success of efforts to invest in and develop new opportunities;
- fluctuations in the level of oil prices;
- the level of production by the synthetic fuel operations at Carbontronics Synfuels Investors LP and Alabama Fuel Products, LLC for the remainder of fiscal year 2007;
- 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;
- the ability to obtain new short- and long-term contracts with neighboring utilities;
- the direct or indirect effect on Southern Company s business resulting from terrorist incidents and the threat of terrorist incidents;
- interest rate fluctuations and financial market conditions and the results of financing efforts, including Southern Company s and its subsidiaries credit ratings;
- the ability of Southern Company and its subsidiaries to obtain additional generating capacity at competitive prices;
- catastrophic events such as fires, earthquakes, explosions, floods, hurricanes, droughts, pandemic health events such as an avian influenza, or other similar occurrences;
- the direct or indirect effects on Southern Company s business resulting from incidents similar to the August 2003 power outage in the Northeast;
- the effect of accounting pronouncements issued periodically by standard setting bodies; and

other factors discussed elsewhere herein and in other reports (including the Form 10-K) filed by the registrants from time to time with the SEC.

Each registrant expressly disclaims any obligation to update any forward-looking statements.

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES

7

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2007	2006	**2007**	2006
	(in thousands)		*(in thousands)*	
Operating Revenues:				
Retail revenues	**$ 4,085,704**	$ 3,853,423	**$ 9,934,571**	$ 9,295,223
Wholesale revenues	**563,233**	506,326	**1,530,809**	1,361,097
Other electric revenues	**130,590**	120,001	**381,467**	347,086
Other revenues	**52,516**	69,628	**165,793**	200,735
Total operating revenues	**4,832,043**	4,549,378	**12,012,640**	11,204,141
Operating Expenses:				
Fuel	**1,738,693**	1,625,046	**4,512,718**	3,981,241
Purchased power	**281,489**	239,891	**445,698**	483,145
Other operations	**651,127**	603,346	**1,802,876**	1,753,719
Maintenance	**260,449**	236,647	**831,483**	793,569
Depreciation and amortization	**311,939**	300,104	**928,569**	896,562
Taxes other than income taxes	**206,763**	186,631	**574,329**	540,834
Total operating expenses	**3,450,460**	3,191,665	**9,095,673**	8,449,070
Operating Income	**1,381,583**	1,357,713	**2,916,967**	2,755,071
Other Income and (Expense):				
Allowance for equity funds used during construction	**28,050**	11,847	**71,821**	33,772
Interest income	**11,638**	12,748	**31,853**	25,657
Equity in losses of unconsolidated subsidiaries	**(410)**	(133)	**(20,712)**	(44,985)
Leveraged lease income	**12,359**	16,787	**31,928**	52,489
Impairment loss on equity method investments		(695)		(15,969)
Interest expense, net of amounts capitalized	**(220,090)**	(185,189)	**(614,345)**	(542,259)
Interest expense to affiliate trusts	**(12,696)**	(30,550)	**(58,867)**	(91,819)
Preferred and preference dividends of subsidiaries	**(10,451)**	(9,120)	**(30,709)**	(26,141)
Other income (expense), net	**17,271**	(30,154)	**8,325**	(26,986)
Total other income and (expense)	**(174,329)**	(214,459)	**(580,706)**	(636,241)
Earnings Before Income Taxes	**1,207,254**	1,143,254	**2,336,261**	2,118,830
Income taxes	**445,259**	405,269	**806,424**	734,015
Consolidated Net Income	**$ 761,995**	$ 737,985	**$ 1,529,837**	$ 1,384,815
Common Stock Data:				
Earnings per share-				

Basic	**$ 1.00**	$ 0.99	**$ 2.03**	$ 1.86
Diluted	**$ 1.00**	$ 0.99	**$ 2.02**	$ 1.85
Average number of basic shares of common stock outstanding (in thousands)	**758,308**	742,884	**754,568**	742,532
Average number of diluted shares of common stock outstanding (in thousands)	**762,392**	747,560	**759,182**	746,983
Cash dividends paid per share of common stock	**$ 0.4025**	$ 0.3875	**$ 1.1925**	$ 1.1475

The accompanying notes as they relate to Southern Company are an integral part of these condensed financial statements.

8

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	For the Nine Months Ended September 30,	
	2007	2006
	(in thousands)	
Operating Activities:		
Consolidated net income	**$ 1,529,837**	$ 1,384,815
Adjustments to reconcile consolidated net income to net cash provided from operating activities		
Depreciation and amortization	**1,108,475**	1,059,567
Deferred income taxes and investment tax credits	**102,314**	344,062
Allowance for equity funds used during construction	**(71,821)**	(33,772)
Equity in losses of unconsolidated subsidiaries	**20,712**	44,985
Leveraged lease income	**(31,928)**	(52,489)
Pension, postretirement, and other employee benefits	**75,303**	74,033
Stock option expense	**26,011**	25,045
Hedge settlements	**15,151**	18,006
Hurricane Katrina grant proceeds-property reserve	**60,000**	
Other, net	**10,454**	47,060
Changes in certain current assets and liabilities		
Receivables	**(426,107)**	(460,092)
Fossil fuel stock	**(57,624)**	(136,720)
Materials and supplies	**(55,191)**	(56,559)
Other current assets	**(2,808)**	61,019
Hurricane Katrina grant proceeds	**14,345**	
Accounts payable	**(3,951)**	(319,564)
Accrued taxes	**303,781**	185,626
Accrued compensation	**(148,274)**	(162,455)
Other current liabilities	**(1,342)**	(42,382)
Net cash provided from operating activities	**2,467,337**	1,980,185
Investing Activities:		
Property additions	**(2,469,059)**	(2,112,780)
Investment in restricted cash from pollution control bonds	**(96,052)**	
Distribution of restricted cash from pollution control bonds	**44,550**	
Nuclear decommissioning trust fund purchases	**(538,049)**	(572,932)
Nuclear decommissioning trust fund sales	**531,169**	566,052
Proceeds from property sales	**31,333**	148,427
Investment in unconsolidated subsidiaries	**(34,550)**	(57,116)
Cost of removal, net of salvage	**(65,601)**	(53,605)
Hurricane Katrina capital grant proceeds	**10,869**	
Other	**25,908**	(66,517)
Net cash used for investing activities	**(2,559,482)**	(2,148,471)
Financing Activities:		

Increase (decrease) in notes payable, net	**(656,348)**	788,744
Proceeds		
Long-term debt	**3,081,500**	1,075,845
Common stock	**414,498**	30,804
Preferred and Preference Stock	**150,000**	
Redemptions		
Long-term debt	**(904,270)**	(550,176)
Long-term debt to affiliate trusts	**(695,376)**	(67,457)
Preferred stock		(14,569)
Common stock repurchased		(117)
Payment of common stock dividends	**(898,766)**	(851,991)
Other	**(31,432)**	(26,811)
Net cash provided from financing activities	**459,806**	384,272
Net Change in Cash and Cash Equivalents	**367,661**	215,986
Cash and Cash Equivalents at Beginning of Period	**166,846**	202,111
Cash and Cash Equivalents at End of Period	**$ 534,507**	$ 418,097
Supplemental Cash Flow Information:		
Cash paid during the period for		
Interest (net of $44,229 and $16,604 capitalized for 2007 and 2006, respectively)	**$ 600,634**	$ 638,380
Income taxes (net of refunds)	**$ 388,634**	$ 245,941

The accompanying notes as they relate to Southern Company are an integral part of these condensed financial statements.

9

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

Assets	At September 30, 2007	At December 31, 2006
	(in thousands)	
Current Assets:		
Cash and cash equivalents	**$ 534,507**	$ 166,846
Restricted cash	**51,502**	
Receivables		
Customer accounts receivable	**1,360,586**	942,821
Unbilled revenues	**370,541**	283,275
Under recovered regulatory clause revenues	**919,771**	516,441
Other accounts and notes receivable	**318,377**	329,619
Accumulated provision for uncollectible accounts	**(26,336)**	(34,901)
Fossil fuel stock, at average cost	**732,345**	674,902
Materials and supplies, at average cost	**701,243**	648,127
Vacation pay	**123,505**	121,246
Prepaid expenses	**167,974**	127,908
Other	**181,839**	242,735
Total current assets	**5,435,854**	4,019,019
Property, Plant, and Equipment:		
In service	**46,565,693**	45,484,895
Less accumulated depreciation	**17,213,524**	16,581,886
	29,352,169	28,903,009
Nuclear fuel, at amortized cost	**336,477**	317,429
Construction work in progress	**2,896,405**	1,871,538
Total property, plant, and equipment	**32,585,051**	31,091,976
Other Property and Investments:		
Nuclear decommissioning trusts, at fair value	**1,146,615**	1,057,534
Leveraged leases	**976,928**	1,138,730
Other	**259,147**	296,484
Total other property and investments	**2,382,690**	2,492,748
Deferred Charges and Other Assets:		
Deferred charges related to income taxes	**932,382**	895,446
Prepaid pension costs	**1,577,648**	1,548,983
Unamortized debt issuance expense	**183,947**	171,758
Unamortized loss on reacquired debt	**289,820**	293,016
Deferred under recovered regulatory clause revenues	**354,548**	845,201
Other regulatory assets	**912,102**	935,804

Other	**654,172**	564,498
Total deferred charges and other assets	**4,904,619**	5,254,706
Total Assets	**$ 45,308,214**	$ 42,858,449

The accompanying notes as they relate to Southern Company are an integral part of these condensed financial statements.

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

Liabilities and Stockholders Equity	At September 30, 2007	At December 31, 2006
	(in thousands)	
Current Liabilities:		
Securities due within one year	**$ 1,721,312**	$ 1,416,898
Notes payable	**1,284,453**	1,940,801
Accounts payable	**1,102,793**	1,081,256
Customer deposits	**269,420**	248,781
Accrued taxes		
Income taxes	**363,065**	110,009
Other	**423,928**	390,716
Accrued interest	**199,325**	183,918
Accrued vacation pay	**154,857**	151,113
Accrued compensation	**299,306**	443,610
Other	**298,181**	385,858
Total current liabilities	**6,116,640**	6,352,960
Long-term Debt	**13,095,389**	10,942,025
Long-term Debt Payable to Affiliated Trusts	**721,651**	1,561,358
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	**5,853,662**	5,989,063
Deferred credits related to income taxes	**278,043**	291,474
Accumulated deferred investment tax credits	**485,259**	503,217
Employee benefit obligations	**1,682,419**	1,566,591
Asset retirement obligations	**1,184,590**	1,136,982
Other cost of removal obligations	**1,318,417**	1,300,461
Other regulatory liabilities	**893,507**	793,869
Other	**565,054**	305,255
Total deferred credits and other liabilities	**12,260,951**	11,886,912
Total Liabilities	**32,194,631**	30,743,255
Preferred and Preference Stock of Subsidiaries	**766,302**	744,065
Common Stockholders Equity:		
Common stock, par value $5 per share		
Authorized 1 billion shares		
Issued September 30, 2007: 759,863,967 Shares;		
December 31, 2006: 751,863,854 Shares		
Treasury September 30, 2007: 385,166 Shares;		

December 31, 2006: 5,593,691 Shares			
Par value	**3,799,320**		3,759,319
Paid-in capital	**1,340,344**		1,096,387
Treasury, at cost	**(10,571)**		(192,309)
Retained earnings	**7,256,378**		6,765,219
Accumulated other comprehensive loss	**(38,190)**		(57,487)
Total Common Stockholders Equity	**12,347,281**		11,371,129
Total Liabilities and Stockholders Equity	**$ 45,308,214**	$	42,858,449

The accompanying notes as they relate to Southern Company are an integral part of these condensed financial statements.

11

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2007	2006	**2007**	2006
	(in thousands)		*(in thousands)*	
Consolidated Net Income	**$ 761,995**	$ 737,985	**$ 1,529,837**	$ 1,384,815
Other comprehensive income (loss):				
Qualifying hedges:				
Changes in fair value, net of tax of $(7,342), $(18,019), $6,087, and $(3,634), respectively	**(11,667)**	(28,556)	**9,704**	(5,645)
Reclassification adjustment for amounts included in net income, net of tax of $1,548, $(646), $4,227, and $(340), respectively	**2,369**	1,059	**6,770**	1,347
Marketable securities:				
Change in fair value, net of tax of $1,094, $365, $2,998, and $4,772, respectively	**2,130**	866	**4,757**	7,721
Reclassification adjustment for amounts included in net income, net of tax of $(127), $-, $(488), and $-, respectively	**(201)**		**(774)**	
Pension and other post retirement benefit plans:				
Additional prior service costs from amendment to non-qualified pension plans, net of tax of $-, $-, $(1,510), and $-, respectively			**(2,424)**	
Reclassification adjustment for amounts included in net income, net of tax of $263, $-, $790, and $-, respectively	**422**		**1,264**	
Total other comprehensive income (loss)	**(6,947)**	(26,631)	**19,297**	3,423
COMPREHENSIVE INCOME	**$ 755,048**	$ 711,354	**$ 1,549,134**	$ 1,388,238

The accompanying notes as they relate to Southern Company are an integral part of these condensed financial statements.

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
THIRD QUARTER 2007 vs. THIRD QUARTER 2006
AND
YEAR-TO-DATE 2007 vs. YEAR-TO-DATE 2006

OVERVIEW

Discussion of the results of operations is focused on Southern Company s primary business of electricity sales in the Southeast by the traditional operating companies Alabama Power, Georgia Power, Gulf Power, and Mississippi Power and Southern Power. Southern Power is an electric wholesale generation subsidiary with market-based rate authority. Southern Company s other business activities include investments in synthetic fuels and leveraged lease projects, telecommunications, and energy-related services. For additional information on these businesses, see BUSINESS The Southern Company System Traditional operating companies, Southern Power, and Other Business in Item 1 of the Form 10-K. For information regarding the synthetic fuel investment, see Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Synthetic Fuel Tax Credits herein.

Southern Company continues to focus on several key performance indicators. These indicators include customer satisfaction, plant availability, system reliability, and earnings per share. For additional information on these indicators, see MANAGEMENT S DISCUSSION AND ANALYSIS OVERVIEW Key Performance Indicators of Southern Company in Item 7 of the Form 10-K.

RESULTS OF OPERATIONS

Net Income

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$24.0	3.3	$145.0	10.5

Southern Company s third quarter 2007 earnings were $762.0 million ($1.00 per share) compared to $738.0 million ($0.99 per share) for third quarter 2006. The increase was primarily due to a retail base rate increase at Alabama Power, favorable weather as compared to the same period in 2006, and an increase in contributions from market-based rates to large commercial and industrial customers when compared to the same period in 2006. The third quarter 2007 increase was partially offset by higher other operations and maintenance expenses.

Southern Company s year-to-date 2007 earnings were $1.5 billion ($2.03 per share) compared to $1.4 billion ($1.86 per share) for year-to-date 2006. The increase was primarily due to a retail base rate increase at Alabama Power, favorable weather as compared to the same period in 2006, and customer growth in the Southern Company service area. Higher earnings from the synthetic fuel business also contributed to the increase. The year-to-date 2007 increase was partially offset by higher other operations and maintenance expenses and a decrease in contributions from market-based rates to large commercial and industrial customers.

Retail Revenues

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$232.3	6.0	$639.3	6.9

In the third quarter 2007, retail revenues were $4.1 billion compared to $3.9 billion for the same period in 2006. Year-to-date 2007, retail revenues were $9.9 billion compared to $9.3 billion for the same period in 2006.

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Details of the change to retail revenues follow:

	Third Quarter 2007		Year-to-Date 2007	
	(in millions)	*(% change)*	*(in millions)*	*(% change)*
Retail prior year	$3,853.4		$9,295.2	
Estimated change in				
Rates and pricing	89.6	2.3	121.9	1.3
Sales growth	3.3	0.1	52.2	0.6
Weather	23.5	0.6	54.2	0.6
Fuel and other cost recovery	115.9	3.0	411.1	4.4
Retail current year	$4,085.7	6.0%	$9,934.6	6.9%

Revenues associated with changes in rates and pricing increased for third quarter 2007 when compared to the same period in 2006 primarily as a result of an increase in base rates at Alabama Power, as well as an increase in contributions from market-based rates to large commercial and industrial customers. Revenues associated with changes in rates and pricing increased for year-to-date 2007 when compared to the same period in 2006 primarily as a result of an increase in base rates at Alabama Power, partially offset by a decrease in contributions from market-based rates to large commercial and industrial customers during the first two quarters of 2007.

Revenues attributable to changes in sales growth increased for third quarter and year-to-date 2007 when compared to the same periods in 2006 due to a 1.2% and 1.5% increase in retail KWH sales, respectively, resulting primarily from continued customer growth. The number of retail customers increased by 1.5% as of September 2007 compared to September 2006. For the third quarter and year-to-date 2007, residential KWH sales increased 1.5% and 2.6%, respectively, and commercial KWH sales increased 2.8% and 3.1%, respectively. These increases were partially offset by a 1.0% decrease in KWH sales to industrial customers in both the third quarter and year-to-date 2007 primarily due to reduced demand from the primary metals and textile industries.

Revenues resulting from changes in weather increased because of favorable weather for third quarter and year-to-date 2007 compared to the same periods in 2006.

Fuel and other cost recovery revenues increased $115.9 million in the third quarter of 2007 and $411.1 million for year-to-date 2007 when compared to the same periods in 2006. 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 fuel component of purchased power costs, and do not affect net income.

Wholesale Revenues

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$56.9	11.2	$169.7	12.5

In the third quarter 2007, wholesale revenues were $563.2 million compared to $506.3 million in the same period in 2006. The increase was primarily a result of a rise in fuel revenues due to a 6.4% increase in the average unit cost of fuel per net KWH generated. Also contributing to the increase were generating plant operational performance incentives on existing wholesale contracts.

For year-to-date 2007, wholesale revenues were $1.5 billion compared to $1.3 billion for the same period in 2006. The increase was a result of a rise in fuel revenues due to an 8.6% increase in the average unit cost of fuel per net KWH generated, increased revenues from new and existing contracts, and generating plant operational performance incentives on existing wholesale contracts. Short-term opportunity sales also contributed to the increase due to higher sales margins attributable to favorable weather compared to neighboring territories and a

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

favorable price differential between market prices and Southern Company s marginal cost. Short-term opportunity sales are made at market-based rates that generally provide a margin above Southern Company s variable cost to produce the energy.

Other Electric Revenues

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$10.6	8.8	$34.4	9.9

In the third quarter 2007, other electric revenues were $130.6 million compared to $120.0 million in the same period in 2006. The increase was primarily a result of an increase in transmission revenues of $5.3 million and an increase in outdoor lighting revenues of $2.2 million related to a 3.1% increase in the number of lighting customers.

For year-to-date 2007, other electric revenues were $381.5 million compared to $347.1 million in the same period in 2006. The increase was primarily a result of an increase in transmission revenues of $17.8 million, an increase in outdoor lighting revenues of $5.7 million related to a 3.1% increase in the number of lighting customers, and an increase in customer fees of $4.1 million related primarily to an increase in the number of retail electric customers.

Fuel and Purchased Power Expenses

	Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
	(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
Fuel	$ 113.6	7.0	$ 531.5	13.3
Purchased power	41.6	17.3	(37.4)	(7.8)
Total fuel and purchased power expenses	$ 155.2		$ 494.1	

Fuel and purchased power expenses for the third quarter 2007 were $2.0 billion compared to $1.8 billion for the corresponding period in 2006. The increase in fuel and purchased power expenses was due to a $37.3 million net increase in the average cost of fuel and purchased power, as well as a $117.9 million net increase related to total KWHs generated and purchased when compared to the same period in 2006. The net increase in fuel and purchased power expenses for the third quarter 2007 compared to the corresponding period in 2006 resulted from rising fossil fuel prices and a 0.3% increase in fossil fuel generation by Southern Company-owned facilities, primarily due to a 17.6% decrease in hydro generation from a severe drought.

Fuel and purchased power expenses for year-to-date 2007 were $5.0 billion compared to $4.5 billion for the corresponding period in 2006. The increase in fuel and purchased power expenses was due to a $324.9 million net increase in the average cost of fuel and purchased power, as well as a $169.2 million net increase related to total KWHs generated and purchased when compared to the same period in 2006. The net increase in fuel and purchased power expenses for year-to-date 2007 compared to the corresponding period in 2006 resulted from rising fossil fuel prices and a 5.0% increase in fossil fuel generation by Southern Company-owned facilities, primarily due to a 43.6% decrease in hydro generation from a severe drought.

Increases in fuel and purchased power expenses at the traditional operating companies are generally offset by fuel revenues and do not affect net income. See FUTURE EARNINGS POTENTIAL FERC and State PSC 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 affect net income.

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Details of Southern Company s cost of generation and purchased power are as follows:

Average Cost	Third Quarter 2007	Third Quarter 2006	% change	Year-to-Date 2007	Year-to-Date 2006	% change
	(cents per net KWH)			*(cents per net KWH)*		
Fuel	3.01	2.83	6.4	2.90	2.67	8.6
Purchased power	8.67	10.45	(17.0)	7.75	8.25	(6.1)

Energy purchases will vary depending on demand for energy within the Southern Company service area, the market cost of available energy as compared to the cost of Southern Company system generated-energy, and the availability of Southern Company system generation.

Other Operations and Maintenance Expenses

	Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
	(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
Other operations	$ 47.8	7.9	$ 49.2	2.8
Maintenance	23.8	10.1	37.9	4.8
Total other operations and maintenance expenses	$ 71.6		$ 87.1	

For the third quarter 2007, other operations and maintenance expenses were $911.6 million compared to $840.0 million in the same period in 2006. The increase in other operations and maintenance expenses was primarily a result of a $49.1 million increase related to labor and materials expenses, timing of and expenses incurred for maintenance outages, and increases in expenses associated with new facilities, primarily Plant Rowan acquired by Southern Power in September 2006. Also contributing to the increase in other operations and maintenance expenses was a $20.1 million increase in administrative and general expenses largely related to an increase in shared service expenses and accrued litigation expenses.

For year-to-date 2007, other operations and maintenance expenses were $2.6 billion compared to $2.5 billion for the same period in 2006. The increase in other operations and maintenance expenses was primarily a result of a $79.8 million increase related to labor and materials expenses, timing of and expenses incurred for maintenance outages, and increases in expenses associated with new facilities, primarily Plants DeSoto and Rowan acquired by Southern Power in June 2006 and September 2006, respectively.

Depreciation and Amortization

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$11.8	3.9	$32.0	3.6

In the third quarter 2007, depreciation and amortization was $311.9 million compared to $300.1 million in the same period in 2006.

For year-to-date 2007, depreciation and amortization was $928.6 million compared to $896.6 million in the same period in 2006.

The third quarter and year-to-date 2007 increases in depreciation and amortization were a result of additional investments in environmental, transmission, and distribution projects, as well as an increase in amortization related to a regulatory liability recorded in 2003 in connection with the Mississippi PSC s accounting order on

16

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Plant Daniel capacity. See Note 3 to the financial statements of Mississippi Power under Retail Regulatory Matters in Item 8 of the Form 10-K for additional information. Also contributing to the increases was the acquisition of Plant Rowan by Southern Power in September 2006.

Taxes Other than Income Taxes

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$20.2	10.8	$33.5	6.2

In the third quarter 2007, taxes other than income taxes were $206.8 million compared to $186.6 million in the same period in 2006.

For year-to-date 2007, taxes other than income taxes were $574.3 million compared to $540.8 million in the same period in 2006.

The third quarter and year-to-date 2007 increases in taxes other than income taxes were primarily a result of increases in franchise taxes which are directly related to increases in revenues.

Allowance for Equity Funds Used During Construction

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$16.3	136.8	$38.0	112.7

In the third quarter 2007, allowance for equity funds used during construction was $28.1 million compared to $11.8 million in the same period in 2006.

For year-to-date 2007, allowance for equity funds used during construction was $71.8 million compared to $33.8 million in the same period in 2006.

The third quarter and year-to-date 2007 increases were primarily a result of additional investments in environmental, transmission, and distribution projects mainly at Alabama Power and Georgia Power.

Equity in Losses of Unconsolidated Subsidiaries

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$0.3	208.3	$(24.3)	(54.0)

The third quarter 2007 variance when compared to the third quarter 2006 is not material.

For year-to-date 2007, equity in losses of unconsolidated subsidiaries was $20.7 million compared to $45.0 million for the same period in 2006. Southern Company made investments in two synthetic fuel production facilities that generate operating losses. These investments also allow Southern Company to claim federal income tax credits that offset these operating losses and make the projects profitable. The decrease in equity in losses of unconsolidated subsidiaries for year-to-date 2007 when compared with the same period in 2006 was primarily the result of terminating Southern Company s membership interest in one synthetic fuel entity in 2006 which eliminated the funding obligation and Southern Company s share of losses for year-to-date 2007, partially offset by higher operating expenses at the other synthetic fuel entity due to idled production for a portion of second quarter and most of third quarter 2006. See FUTURE EARNINGS POTENTIAL Income

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Tax Matters Synthetic Fuel Tax Credits and Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Synthetic Fuel Tax Credits herein for further information.

Leveraged Lease Income

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$(4.4)	(26.4)	$(20.6)	(39.2)

Leveraged lease income for the third quarter 2007 was $12.4 million compared to $16.8 million for the corresponding period in 2006.

Leveraged lease income for year-to-date 2007 was $31.9 million compared to $52.5 million for the corresponding period in 2006.

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. The adoption of FASB Staff Position No. FAS 13-2 (FSP 13-2), Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction resulted in decreases to leveraged lease pre-tax income of $6.4 million and $19.3 million for the third quarter and year-to-date 2007, respectively, when compared to the same periods in 2006. See FUTURE EARNINGS POTENTIAL Income Tax Matters Leveraged Lease Transactions and Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Leveraged Lease Transactions herein for further information.

Impairment Loss on Equity Method Investments

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$(0.7)	N/M	$(16.0)	N/M

N/M Not meaningful

The third quarter 2007 variance when compared to the third quarter 2006 is not material.

For year-to-date 2007, impairment loss on equity method investments was $0.0 compared to $16.0 million for the same period in 2006. The decrease in impairment loss on equity method investments was primarily a result of impairment losses of $15.9 million recognized during the second quarter 2006 related to Southern Company s investments in two synthetic fuel production facilities. See FUTURE EARNINGS POTENTIAL Income Tax Matters Synthetic Fuel Tax Credits and Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Synthetic Fuel Tax Credits herein for further information.

Interest Expense, Net of Amounts Capitalized

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$34.9	18.8	$72.0	13.3

Interest expense, net of amounts capitalized for the third quarter 2007 was $220.1 million compared to $185.2 million for the corresponding period in 2006. The increase was a result of $42.8 million increase associated with $1.6 billion in additional debt outstanding at September 30, 2007 compared to September 30, 2006 and higher interest rates associated with the issuance of new long-term debt. Also contributing to the increase was $2.0 million related to an increase in average interest rates on existing variable rate debt. These increases were

18

partially offset by $9.9 million in higher capitalized interest as compared to the same period in 2006. See MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Financing Activities of Southern Company in Item 7 of the Form 10-K and herein for additional information.

Interest expense, net of amounts capitalized for year-to-date 2007 was $614.3 million compared to $542.3 million for the corresponding period in 2006. The increase was a result of an $87.4 million increase associated with $1.6 billion in additional debt outstanding at September 30, 2007 compared to September 30, 2006 and higher interest rates associated with the issuance of new long-term debt. Also contributing to the increase was $12.3 million related to an increase in average interest rates on existing variable rate debt. These increases were partially offset by $27.6 million in higher capitalized interest as compared to the same period in 2006.

Interest Expense to Affiliate Trusts

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$(17.9)	(58.4)	$(32.9)	(35.9)

Interest expense to affiliate trusts for the third quarter 2007 was $12.7 million compared to $30.6 million for the corresponding period in 2006.

Interest expense to affiliate trusts for year-to-date 2007 was $58.9 million compared to $91.8 million for the corresponding period in 2006.

The third quarter and year-to-date 2007 decreases in interest expense to affiliate trusts were primarily a result of the redemption of approximately $1.0 billion of long-term debt payable to affiliated trusts since September 30, 2006.

Other Income (Expense), Net

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$47.5	157.3	$35.3	130.8

In the third quarter 2007, other income (expense), net was $17.3 million compared to $(30.2) million for the same period in 2006 primarily as a result of a $47.0 million increase related to changes in the value of derivative transactions in the synthetic fuel business. These derivative transactions were entered into to reduce Southern Company s exposure to changes in the value of synthetic fuel tax credits, which are impacted by changes in oil prices. See FUTURE EARNINGS POTENTIAL Income Tax Matters Synthetic Fuel Tax Credits and Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Synthetic Fuel Tax Credits herein for further information.

For year-to-date 2007, other income (expense), net was $8.3 million compared to $(27.0) million for the same period in 2006 primarily as a result of a $42.8 million increase related to changes in the value of derivative transactions in the synthetic fuel business, partially offset by the release of $6.3 million in certain obligations associated with one of Southern Company s synthetic fuel investments which was terminated effective July 1, 2006.

Income Taxes

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$40.0	9.9	$72.4	9.9

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Income taxes for the third quarter 2007 were $445.3 million compared to $405.3 million for the corresponding period in 2006. The increase in income taxes was primarily a result of higher pre-tax earnings and a decrease in net synthetic fuel tax credits in third quarter 2007 compared to the same period in 2006. See FUTURE EARNINGS POTENTIAL Income Tax Matters Synthetic Fuel Tax Credits and Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Synthetic Fuel Tax Credits herein for further information. The increase in income taxes was partially offset by the tax benefit associated with an increase in allowance for equity funds used during construction and an increase in the IRC Section 199 domestic production deduction. See FUTURE EARNINGS POTENTIAL Income Tax Matters IRC Section 199 Domestic Production Deduction and Note (H) to the Condensed Financial Statements herein for further information.

Income taxes for year-to-date 2007 were $806.4 million compared to $734.0 million for the corresponding period in 2006. The increase was primarily a result of higher pre-tax earnings. The increase in income taxes was partially offset by the tax benefit associated with an increase in reference to a heading where capitalized allowance for equity funds used during construction and an increase in the IRC Section 199 domestic production deduction.

FUTURE EARNINGS POTENTIAL

The results of operations discussed above are not necessarily indicative of Southern Company s future earnings potential. The level of Southern Company s future earnings depends on numerous factors that affect the opportunities, challenges, and risks of Southern Company s primary business of selling electricity. These factors include the traditional operating companies ability to maintain a stable regulatory environment that continues to allow for the recovery of all prudently incurred costs during a time of increasing costs. Another major factor is the profitability of the competitive market-based wholesale generating business and federal regulatory policy, which may impact Southern Company s level of participation in this market. Future earnings for the electricity business in the near term will depend, in part, upon growth in energy sales, which is subject to a number of factors. These factors include weather, competition, new energy contracts with neighboring utilities, energy conservation practiced by customers, the price of electricity, the price elasticity of demand, and the rate of economic growth in the service area. For additional information relating to these issues, see RISK FACTORS in Item 1A and MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL of Southern Company in Item 7 of the Form 10-K.

Environmental Matters

Compliance costs related to the Clean Air Act and other environmental regulations could affect earnings if such costs cannot be fully recovered in rates on a timely basis. See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under Environmental Matters in Item 8 of the Form 10-K for additional information.

New Source Review Litigation

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters New Source Review Actions of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under Environmental Matters New Source Review Actions in Item 8 of the Form 10-K for additional information regarding a civil action brought by the EPA alleging that Alabama Power had violated the NSR provisions of the Clean Air Act and related state laws with respect to certain of its coal-fired generating facilities. The plaintiffs appeal against Alabama Power was stayed by the U.S. Court of Appeals for the Eleventh Circuit pending the U.S. Supreme Court s decision in a similar case against Duke Energy. On April 2, 2007, the U.S. Supreme Court issued an opinion in the Duke Energy case. The U.S. District Court for the Northern District of Alabama has issued an order indicating a willingness to re-

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

evaluate its previous decision in light of the Supreme Court s Duke Energy opinion. The Eleventh Circuit is now considering whether to proceed with the appeal or remand the case to the District Court for further proceedings, and if so, whether to vacate the District Court s original judgment in favor of Alabama Power. The final resolution of these claims cannot be determined at this time.

Eight-Hour Ozone Regulations

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters Environmental Statutes and Regulations Air Quality of Southern Company in Item 7 of the Form 10-K for additional information regarding revisions to the eight-hour ozone air quality standard. On June 20, 2007, the EPA proposed additional revisions to the current eight-hour ozone standard which, if enacted, could result in designation of new nonattainment areas within Southern Company s service territory. The EPA has requested comment and is expected to make a determination regarding finalization of a revised standard in 2008. The ultimate outcome of this matter cannot be determined at this time.

Fine Particulate Matter Regulations

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters Environmental Statutes and Regulations Air Quality of Southern Company in Item 7 of the Form 10-K for additional information regarding nonattainment designations for the fine particulate matter air quality standard. In March 2007, the EPA finalized its fine particulate matter implementation rule, requiring submittal of state plans for addressing the nonattainment designations by April 2008. The ultimate outcome of this matter depends on the development and submittal of those state plans and the resolution of pending legal challenges and, therefore, cannot be determined at this time.

Georgia Multi-Pollutant Rule

On June 27, 2007, the State of Georgia approved a new multi-pollutant rule for certain existing coal-fired electric utility steam generating units in Georgia. The rule is designed to reduce emissions of mercury, sulfur dioxide, nitrogen oxide, and fine particulates state-wide by requiring installation of specified control technologies at each affected unit by a date certain between December 31, 2008 and June 1, 2015. This rule will require the installation of controls on the majority of Georgia Power s coal-fired units. See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters Environmental Statutes and Regulations General in Item 7 of the Form 10-K for a discussion of estimated compliance costs for 2007 through 2009. If compliance costs cannot be fully recovered in rates on a timely basis, Southern Company s financial statements would be adversely impacted. See FERC and State PSC Matters Georgia Power Retail Base Rate Recovery for information on Georgia Power s request to increase retail rates effective January 1, 2008.

Plant Wansley Environmental Litigation

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters Plant Wansley Environmental Litigation of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under Environmental Matters Plant Wansley Environmental Litigation in Item 8 of the Form 10-K for additional information on litigation involving alleged violations of the Clean Air Act at four of the units at Plant Wansley. On June 18, 2007, the U.S. District Court for the Northern District of Georgia approved a settlement between the parties resolving all remaining issues and dismissed the case. There was no material impact on Southern Company s financial statements.

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Florida Greenhouse Gas Executive Orders

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters - Global Climate Issues of Southern Company in Item 7 of the Form 10-K for additional information regarding domestic efforts to reduce greenhouse gases. On July 13, 2007, the Governor of the State of Florida signed three executive orders addressing reduction of greenhouse gas emissions within the state, including statewide emission reduction targets beginning in 2017. Included in the orders is a directive to the Secretary of Environmental Protection to develop rules adopting maximum allowable emissions levels of greenhouse gases for electric utilities, consistent with the statewide emission reduction targets, and a request to the Florida PSC to initiate rulemaking requiring utilities to produce at least 20% of their electricity from renewable sources. The impact of these orders on Southern Company will depend on the development, adoption, and implementation of any rules governing greenhouse gas emissions, and the ultimate outcome cannot be determined at this time.

FERC and State PSC Matters

Market-Based Rate Authority

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL FERC Matters Market-Based Rate Authority of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under FERC Matters Market-Based Rate Authority in Item 8 of the Form 10-K for information regarding the proceedings initiated by the FERC in December 2004 to assess Southern Company s generation dominance within its retail service territory and in May 2005 to determine whether Southern Company satisfies the other three parts of the FERC s market-based rate analysis: transmission market power, barriers to entry, and affiliate abuse or reciprocal dealing.

In late June and July 2007, hearings were held in the December 2004 proceeding and briefs to the presiding ALJ were filed in August and September 2007. Southern Company anticipates an initial decision from the ALJ in November 2007 on the issues that were set for hearing. The ultimate outcome of this generation dominance proceeding cannot now be determined, but an adverse decision by the FERC in a final order could result in refunds of approximately $19.7 million, plus interest.

On June 21, 2007, the FERC issued an order terminating the May 2005 proceeding pertaining to the other three parts of the market-based rate analysis. In addition, on June 21, 2007, the FERC issued its final rule regarding market-based rate authority. The FERC generally retained its current market-based rate standards. The impact of this order and its effect on the generation dominance proceeding cannot now be determined.

Intercompany Interchange Contract

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL FERC Matters Intercompany Interchange Contract of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under FERC Matters Intercompany Interchange Contract in Item 8 of the Form 10-K for information regarding the proceeding initiated by the FERC in May 2005 to examine (1) the provisions of the IIC among Alabama Power, Georgia Power, Gulf Power, Mississippi Power, Savannah Electric, Southern Power, and SCS, as agent, under the terms of which the Power Pool is operated, and, in particular, the propriety of the continued inclusion of Southern Power as a party to the IIC, (2) whether any parties to the IIC have violated the FERC s standards of conduct applicable to utility companies that are transmission providers, and (3) whether Southern Company s code of conduct defining Southern Power as a system company rather than a marketing affiliate is just and reasonable.

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

On April 19, 2007, the FERC approved, with certain modifications, the compliance filing submitted by Southern Company on November 6, 2006. The compliance plan largely involves functional separation and information restrictions related to marketing activities conducted on behalf of Southern Power. Implementation of the plan is not expected to have a material impact on Southern Company s financial statements.

Retail Fuel Cost Recovery

The traditional operating companies each have established fuel cost recovery rates approved by their respective state PSCs. Over the past several years, the traditional operating companies have experienced higher than expected fuel costs for coal, natural gas, and uranium. These higher fuel costs have resulted in under recovered fuel costs included in the balance sheets of approximately $1.2 billion at September 30, 2007. Gulf Power and Mississippi Power were granted increased fuel billing factors effective January 1, 2007. Georgia Power was granted an increase effective March 2007. Alabama Power was ordered to increase its fuel billing factor effective July 2007. Operating revenues are adjusted for differences in actual recoverable fuel costs and amounts billed in current regulated rates. Accordingly, changes to the billing factors will have no significant effect on Southern Company s revenues or net income but will affect cash flow. The traditional operating companies will continue to monitor the under recovered fuel cost balance in light of these higher fuel costs. See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL PSC Matters Fuel Cost Recovery of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under Alabama Power Retail Regulatory Matters and Georgia Power Retail Regulatory Matters in Item 8 of the Form 10-K for additional information.

Georgia Power Retail Base Rate Filing

Georgia Power is currently operating under a three-year retail rate order that expires December 31, 2007. Under the terms of the existing order, earnings are evaluated annually against a retail return on common equity range of 10.25% to 12.25%. Two-thirds of any earnings above the 12.25% return are applied to rate refunds, with the remaining one-third retained by Georgia Power. The order required Georgia Power to file a general rate case by July 1, 2007.

On June 29, 2007, Georgia Power filed a request to increase retail base rates with the Georgia PSC. The request includes an increase effective January 1, 2008 of approximately $406 million, or 5.98%, in retail revenues, based on a future test year ending July 31, 2008 and a proposed retail return on common equity of 12.5%. The majority of the increase in retail revenues is being requested to cover the costs of environmental compliance and continued investment in new generation, transmission, and distribution facilities to support growth and ensure reliability. The remainder of the increase would include recovery of higher operation, maintenance, and other investment costs to meet the rising demand for electricity. Hearings on Georgia Power s direct testimony were held in early October. In direct testimony filed on October 22, 2007, the Georgia PSC staff proposed certain adjustments to Georgia Power s general rate case that indicates a $21 million revenue surplus. Georgia Power disagrees with the majority of the staff s proposed adjustments. Hearings on Georgia PSC staff s and intervenors direct testimony will be held in early November. Georgia Power s rebuttal hearings will occur later the same month. Georgia Power expects the Georgia PSC to issue a final order in this matter on December 20, 2007. In addition to the traditional test period request, Georgia Power filed information for a three-year rate plan option that includes additional increases of approximately $189 million, or 2.62%, and $41 million, or 0.56%, in retail revenues effective January 1, 2009 and 2010, respectively, to cover the costs of additional environmental controls and certified PPAs. The final outcome of this matter cannot now be determined. See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL PSC Matters Georgia Power of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under Georgia Power Retail Regulatory Matters in Item 8 of the Form 10-K and Note (K) to the Condensed Financial Statements herein for additional information.

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Mississippi Power Storm Damage Cost Recovery

See Note 3 to the financial statements of Southern Company under PSC Matters Storm Damage Cost Recovery in Item 8 of the Form 10-K for information regarding storm restoration costs in connection with Hurricane Katrina and a financing order issued by the Mississippi PSC that authorized the issuance of $121.2 million of storm restoration bonds under a state bond program. The storm restoration bonds were issued by the Mississippi Development Bank on June 1, 2007 on behalf of the State of Mississippi. On June 1, 2007, Mississippi Power received a grant payment of $85.2 million from the State of Mississippi representing recovery of $25.2 million in retail storm restoration costs incurred or to be incurred and $60.0 million to increase Mississippi Power s property damage reserve. On October 9, 2007, Mississippi Power received an additional grant payment of $17.6 million for expenditures incurred to date for construction of a new storm operations center. The funds received related to previously incurred storm restoration expenditures have been accounted for as a government grant and have been recorded as a reduction to the regulatory asset that was recorded as the storm restoration expenditures were incurred, in accordance with FASB Statement No. 71, Accounting for the Effects of Certain Types of Regulation. The funds received for storm restoration expenditures to be incurred were recorded as a regulatory liability. Mississippi Power will receive further grant payments of up to $18.4 million as expenditures are incurred to construct a new storm operations center. See Note (D) to the Condensed Financial statements herein for additional information.

Mirant Matters

Mirant was an energy company with businesses that included independent power projects and energy trading and risk management companies in the U.S. and selected other countries. It was a wholly-owned subsidiary of Southern Company until its initial public offering in October 2000. In April 2001, Southern Company completed a spin-off to its shareholders of its remaining ownership, and Mirant became an independent corporate entity. In July 2003, Mirant filed for voluntary reorganization under Chapter 11 of the U.S. Bankruptcy Code. See Note 3 to the financial statements of Southern Company under Mirant Matters Mirant Bankruptcy in Item 8 of the Form 10-K for information regarding Southern Company s contingent liabilities associated with Mirant, including guarantees of contractual commitments, litigation, and joint and several liabilities in connection with the consolidated federal income tax return.

MC Asset Recovery Litigation

See Note 3 to the financial statements of Southern Company under Mirant Matters MC Asset Recovery Litigation in Item 8 of the Form 10-K for information regarding a suit between MC Asset Recovery, a special purpose subsidiary of the post-bankruptcy corporation that adopted the name Mirant Corporation, and Southern Company. On March 28, 2007, MC Asset Recovery filed a Fourth Amended Complaint. Among other things, the Fourth Amended Complaint adds a claim under the Federal Debt Collection Procedure Act (FDCPA) to avoid certain transfers from Mirant to Southern Company and withdraws the breach of fiduciary duty claim the court struck as a result of Southern Company s motion for summary judgment. MC Asset Recovery claims to have standing to assert violations of the FDCPA and to recover property on behalf of the Mirant debtors estates. The ultimate outcome of this matter cannot be determined at this time.

Mirant Securities Litigation

See Note 3 to the financial statements of Southern Company under Mirant Matters Mirant Securities Litigation in Item 8 of the Form 10-K for information regarding a class action lawsuit that several Mirant shareholders (plaintiffs) originally filed against Mirant and certain Mirant officers in May 2002. In November 2002, Southern Company, certain former and current senior officers of Southern Company, and 12 underwriters of Mirant s initial public offering were added as defendants. On March 24, 2006, the plaintiffs filed a motion for reconsideration requesting that the court vacate that portion of its July 14, 2003 order dismissing the

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

plaintiffs claims based upon Mirant s alleged improper energy trading and marketing activities involving the California energy market. On March 6, 2007, the court granted plaintiffs motion for reconsideration, reinstated the California energy market claims, and granted in part and denied in part defendants motion to compel certain class certification discovery. On March 21, 2007, defendants filed renewed motions to dismiss the California energy claims on grounds originally set forth in their 2003 motions to dismiss, but which were not addressed by the court. On July 27, 2007, certain defendants, including Southern Company, filed motions for reconsideration of the court s denial of a motion seeking dismissal of certain federal securities laws claims based upon, among other things, certain alleged errors included in financial statements issued by Mirant. The ultimate outcome of this matter cannot be determined at this time.

Southern Company Employee Savings Plan Litigation

See Note 3 to the financial statements of Southern Company under Mirant Matters Southern Company Employee Savings Plan Litigation in Item 8 of the Form 10-K for information related to the pending settlement of a class action complaint filed under ERISA in June 2004, and amended in December 2004 and November 2005, on behalf of a purported class of participants in or beneficiaries of The Southern Company Employee Savings Plan at any time since April 2, 2001 and whose plan accounts included investments in Mirant common stock. On August 14, 2007, the U.S. District Court for the Northern District of Georgia issued a final order and judgment approving the December 2006 settlement agreement. The deadline for the appeal expired with no appeal filed. There was no material impact on the financial statements of Southern Company. This matter is now concluded.

Income Tax Matters

Leveraged Lease Transactions

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Income Tax Matters Leveraged Lease Transactions of Southern Company in Item 7 and Note 3 to the financial statements of Southern Company under Income Tax Matters in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Leveraged Lease Transactions herein for information regarding IRS challenges to Southern Company s transactions related to international leveraged leases that could have material impacts on Southern Company s financial statements. Effective January 1, 2007, Southern Company adopted FSP 13-2, which amends FASB Statement No. 13, Accounting for Leases requiring recalculation of the rate of return and the allocation of income whenever the projected timing of the income tax cash flows generated by a leveraged lease is revised with recognition of the resulting gain or loss in the year of the revision. FSP 13-2 also requires that all recognized tax positions in a leveraged lease must be measured in accordance with the criteria in FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes, and any changes resulting from FIN 48 must be reflected as a change in important lease assumptions as of the date of adoption. The cumulative effect of initially adopting FSP 13-2 was recorded as an adjustment to beginning retained earnings. For the lease-in-lease-out (LILO) transaction settled with the IRS in February 2005, the cumulative effect of adopting FSP 13-2 was a $17 million reduction in retained earnings. With respect to Southern Company s sale-in-lease-out (SILO) transactions, the adoption of FSP 13-2 reduced retained earnings by $108 million and the adoption of FIN 48 reduced beginning retained earnings by an additional $15 million. The adjustments to retained earnings are non-cash charges and will be recognized as income over the remaining terms of the affected leases. Any future changes in the timing of projected or actual income tax cash flows will result in an additional recalculation of the net investment in the leases and will be recorded currently in income. Southern Company is continuing to pursue resolution of these matters through litigation. Southern Company believes these transactions are valid leases for U.S. tax purposes and the related deductions are allowable. In addition, the U.S. Senate is currently considering legislation that would disallow tax benefits after December 31, 2007 for SILO losses and other international leveraged lease transactions (such as LILO transactions). The

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

ultimate impact on Southern Company s net income will be dependent on the outcome of pending litigation and the proposed legislation. The impact could be significant, and potentially material, but cannot now be determined.

Synthetic Fuel Tax Credits

As discussed in MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Income Tax Matters Synthetic Fuel Tax Credits of Southern Company in Item 7 of the Form 10-K, Southern Company has an investment in an entity that produces synthetic fuel and receives tax credits under Section 45K (formerly Section 29) of the IRC. In accordance with Section 45K of the IRC, these tax credits are subject to limitation as the annual average price of oil (as determined by the DOE) increases over a specified, inflation-adjusted dollar amount published in the spring of the subsequent year. Southern Company, along with its partners in this investment, has continued to monitor oil prices. Reserves against tax credits earned in 2007 of $37.6 million have been recorded in the first nine months of 2007 due to projected phase-outs of the credits in 2007 as a result of current and projected future oil prices. Additionally, the synthetic fuel tax credits are not allowed under IRC Section 45K for any production after December 31, 2007.

Georgia State Income Tax Credits

In September 2007, 2006, and 2005, Georgia Power filed its 2006, 2005, and 2004 income tax returns, respectively, which included state income tax credits for activity through Georgia ports. Georgia Power has also filed additional similar claims for the years 2002 through 2004. The Georgia Department of Revenue has not responded to these claims. On July 24, 2007, Georgia Power filed a complaint in the Superior Court of Fulton County to recover the credits claimed for the years 2002 through 2004. If Georgia Power prevails, these claims could have a significant, and possibly material, positive effect on Southern Company s net income. If Georgia Power is not successful, payment of the related state tax could have a significant, and possibly material, negative effect on Southern Company s cash flow. The ultimate outcome of this matter cannot now be determined.

IRC Section 199 Domestic Production Deduction

The American Jobs Creation Act of 2004 created a tax deduction for the portion of income attributable to United States production activities as defined in IRC Section 199. The deduction is equal to a stated percentage of the taxpayer s qualified production activities. The percentage is phased in over the years 2005 through 2010 with a 3% rate applicable to the years 2005 and 2006, a 6% rate applicable for years 2007 through 2009, and a 9% rate applicable for all years after 2009. The tax benefit of this deduction is estimated to be approximately $15 $20 million per year in years 2008 and 2009, and approximately 50% higher in 2010.

Construction Projects

Integrated Gasification Combined Cycle (IGCC) Project

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Construction Projects Integrated Gasification Combined Cycle of Southern Company in Item 7 of the Form 10-K for information regarding the development by Southern Power and the Orlando Utilities Commission (OUC) of an IGCC project in Orlando, Florida at OUC s Stanton Energy site. Since the definitive agreements relating to the development of the project were executed in December 2005, the estimated costs of the gasifier portion have increased due primarily to increases in commodity costs and increased market demand for labor. Southern Power had the option under the original agreements to end its participation in the gasifier portion of the project at the end of the project definition phase, which has been completed. On March 29, 2007, Southern Power s Board of Directors approved the continuation and the completion of the design, engineering, and construction of the gasifier portion of the project. Southern Power and OUC will share 65% and 35% of the

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

estimated cost increase, respectively, under the proposed amended agreements. In April 2007, OUC approved its portion of the cost increase, subject to the DOE s approval of the additional funding. On May 8, 2007, SCS, as agent for Southern Power, and the DOE entered into an amendment to the February 2006 cooperative agreement to increase the DOE s funding for the gasifier portion of the project by $58.75 million.

Southern Power is evaluating the potential impacts of proposed federal and state legislation and regulations on the gasifier portion of the IGCC project. Specifically, there is an ongoing assessment of the State of Florida s governor s executive orders concerning future emissions restrictions and the rules and regulations necessary for implementation of such orders. For additional information on the governor s orders, see Environmental Matters Florida Greenhouse Gas Executive Orders herein. As of October 31, 2007, Southern Power s share of actual and committed costs related to the gasifier portion of the IGCC project was approximately $45 million. These costs will increase as the project continues. The ultimate impact on Southern Company s financial statements will be dependent on the evaluation and application of the State of Florida s governor s executive orders and any other legislation or regulations, but could be significant and possibly material. The ultimate outcome of this matter cannot now be determined.

Nuclear

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Construction Projects Nuclear of Southern Company in Item 7 of the Form 10-K for information regarding a development agreement between Southern Nuclear and Duke Energy to evaluate the potential construction of a new two-unit nuclear plant at a jointly owned site in Cherokee County, South Carolina. In March 2007, the Southern Nuclear Board of Directors voted to withdraw from any further development of this project and a notice of withdrawal from the project was provided to Duke Energy. Adjustments to the carrying value of the related assets were recorded in the first quarter 2007 and were not material to the financial statements. During the second quarter 2007, Duke Energy chose to independently continue with the project and purchased Southern Company s interest in the project with no material effect on Southern Company s financial statements. This matter is now concluded.

Other Matters

Georgia Power proposed a donation of approximately 2,200 acres in Tallulah Gorge State Park to the State of Georgia which the Georgia Department of Natural Resources voted to accept on October 24, 2007. The donation is expected to be effective in the fourth quarter 2007. The impact of this donation to Southern Company s net income could possibly be significant but cannot be determined at this time.

Southern Company is subject to certain claims and legal actions arising in the ordinary course of business. In addition, Southern Company s business activities are subject to extensive governmental regulation related to public health and the environment. 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 opacity and air quality standards, has increased generally throughout the United States. In particular, personal injury claims for damages caused by alleged exposure to hazardous materials have become more frequent. 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 of Southern Company in Item 8 of the Form 10-K, management does not anticipate that the liabilities, if any, arising from such current proceedings would have a material adverse effect on Southern Company s financial statements.

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

See the Notes to the Condensed Financial Statements herein for 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 accounting principles generally accepted in the United States. Significant accounting policies are described in Note 1 to the financial statements of Southern Company in Item 8 of the Form 10-K. 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. See MANAGEMENT S DISCUSSION AND ANALYSIS ACCOUNTING POLICIES - Application of Critical Accounting Policies and Estimates of Southern Company in Item 7 of the Form 10-K for a complete discussion of Southern Company s critical accounting policies and estimates related to Electric Utility Regulation, Contingent Obligations, and Unbilled Revenues.

New Accounting Standards

Income Taxes

On January 1, 2007, Southern Company adopted FIN 48, which requires companies to determine whether it is more likely than not that a tax position will be sustained upon examination by the appropriate taxing authorities before any part of the benefit can be recorded in the financial statements. It also provides guidance on the recognition, measurement, and classification of income tax uncertainties, along with any related interest and penalties. The provisions of FIN 48 were applied to all tax positions beginning January 1, 2007. The impact on Southern Company s financial statements was a reduction to beginning 2007 retained earnings of approximately $15 million related to Southern Company s SILO transactions. See Note (I) to the Condensed Financial Statements herein for details regarding the financial statement impact of the adoption.

Leveraged Leases

Effective January 1, 2007, Southern Company adopted FSP 13-2. The cumulative effect of initially adopting FSP 13-2 was recorded as an adjustment to beginning retained earnings. For the LILO transaction settled with the IRS in February 2005, the cumulative effect of adopting FSP 13-2 was a $17 million reduction in retained earnings. With respect to Southern Company s SILO transactions, the adoption of FSP 13-2 reduced retained earnings by $108 million. The adjustments to retained earnings are non-cash charges and will be recognized as income over the remaining terms of the affected leases. Any future changes in the projected or actual income tax cash flows will result in an additional recalculation of the net investment in the leases and will be recorded currently in income. See FUTURE EARNINGS POTENTIAL Income Tax Matters Leveraged Lease Transactions and Note (B) to the Condensed Financial Statements under INCOME TAX MATTERS Leveraged Lease Transactions herein for further details about the effect of FSP 13-2.

Fair Value Measurement

The FASB issued FASB Statement No. 157 (SFAS No. 157), Fair Value Measurements in September 2006. This standard provides guidance on how to measure fair value where it is permitted or required under other accounting pronouncements. SFAS No. 157 also requires additional disclosures about fair value measurements. Southern Company plans to adopt SFAS No. 157 on January 1, 2008 and is currently assessing the impact of this standard.

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Fair Value Option

In February 2007, the FASB issued FASB Statement No. 159 (SFAS No. 159), Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115. This standard permits an entity to choose to measure many financial instruments and certain other items at fair value. Southern Company plans to adopt SFAS No. 159 on January 1, 2008 and is currently assessing its impact to the extent the fair value option is elected.

FINANCIAL CONDITION AND LIQUIDITY

Overview

Southern Company s financial condition and liquidity position remained stable at September 30, 2007. Net cash provided from operating activities totaled $2.5 billion for the first nine months of 2007, compared to $2.0 billion for the corresponding period in 2006. The $487 million increase is primarily due to the increase in net income as previously discussed and a reduction in the outflow of cash for accounts payable, primarily related to gas purchases. Net cash used for investing activities totaled $2.6 billion primarily due to gross property additions to utility plant of $2.5 billion. Net cash provided from financing activities totaled $460 million for the first nine months of 2007, compared to $384 million for the corresponding period in 2006. The increase was primarily the result of additional common stock and long-term debt issuances.

Significant balance sheet changes for the first nine months of the year include a $1.3 billion increase in long-term debt, which was used primarily for the repayment of short-term debt, redemptions of long-term debt payable to affiliated trusts, construction expenditures, and general corporate purposes. Total property, plant, and equipment, net of depreciation, increased $1.5 billion during the first nine months of 2007 primarily from the installation of additional environmental equipment and transmission and distribution construction.

The market price of Southern Company s common stock at September 30, 2007 was $36.28 per share (based on the closing price as reported on the New York Stock Exchange) and the book value was $16.26 per share, representing a market-to-book ratio of 223%, compared to $36.86, $15.24, and 242%, respectively, at the end of 2006. The dividend for the third quarter 2007 was $0.4025 per share compared to $0.3875 per share in the third quarter 2006.

Capital Requirements and Contractual Obligations

See MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Capital Requirements and Contractual Obligations of Southern Company in Item 7 of the Form 10-K for a description of Southern Company s capital requirements for its construction program and other funding requirements associated with scheduled maturities of long-term debt, as well as the related interest, preferred and preference stock dividends, leases, trust funding requirements, and other purchase commitments. Approximately $1.7 billion will be required by September 30, 2008 for redemptions and maturities of long-term debt.

Sources of Capital

Southern Company intends to meet its future capital needs through internal cash flow and external security issuances. Equity capital can be provided from any combination of Southern Company s stock plans, private placements, or public offerings. The amount and timing of additional equity capital to be raised will be contingent on Southern Company s investment opportunities. Southern Company does not currently anticipate any equity offerings in 2007 outside of its existing stock option plan, the employee savings plan, and the Southern Investment Plan. The traditional operating companies and Southern Power plan to obtain the funds required for construction and other purposes from sources similar to those used in the past, which were primarily

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

from operating cash flows, security issuances, term loans, short-term borrowings, and equity contributions from Southern Company. However, the amount, type, and timing of any financings, if needed, will depend upon prevailing market conditions, regulatory approval, and other factors. See MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Sources of Capital of Southern Company in Item 7 of the Form 10-K for additional information.

Southern Company s current liabilities frequently exceed current assets because of the continued use of short-term debt as a funding source to meet scheduled maturities of long-term debt as well as cash needs which can fluctuate significantly due to the seasonality of the business. To meet short-term cash needs and contingencies, Southern Company has substantial cash flow from operating activities and access to capital markets, including commercial paper programs. At September 30, 2007, Southern Company and its subsidiaries had approximately $534 million of cash and cash equivalents, $52 million of restricted cash related to the sale of pollution control bonds which may be used only for future project costs, and approximately $3.6 billion of unused credit arrangements with banks, of which $74 million expire in 2007 and $3.5 billion expire in 2008 and beyond. Approximately $79 million of the credit facilities expiring in 2007 and 2008 allow for the execution of term loans for an additional two-year period, and approximately $443 million contain provisions allowing one-year term loans. See Note 6 to the financial statements of Southern Company under Bank Credit Arrangements in Item 8 of the Form 10-K for additional information. The traditional operating companies may also meet short-term cash needs through a Southern Company subsidiary organized to issue and sell commercial paper and extendible commercial notes at the request and for the benefit of each of the traditional operating companies. At September 30, 2007, the Southern Company system had outstanding commercial paper of $1.2 billion, outstanding bank notes of $60 million, and no extendible commercial notes outstanding. Management believes that the need for working capital can be adequately met by utilizing commercial paper programs and lines of credit without maintaining large cash balances.

Off-Balance Sheet Financing Arrangements

See MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Off-Balance Sheet Financing Arrangements of Southern Company in Item 7 and Note 7 to the financial statements of Southern Company under Operating Leases in Item 8 of the Form 10-K for information related to Mississippi Power s lease of a combined cycle generating facility at Plant Daniel.

Credit Rating Risk

Southern Company does not have any credit arrangements that would require material changes in payment schedules or terminations as a result of a credit rating downgrade. There are certain contracts that could require collateral, but not accelerated payment, in the event of a credit rating change to BBB and Baa2, or BBB- or Baa3 or below. These contracts are primarily for physical electricity purchases and sales. At September 30, 2007, the maximum potential collateral requirements at a BBB and Baa2 rating were approximately $8.6 million and at a BBB- or Baa3 rating were approximately $293.3 million. The maximum potential collateral requirements at a rating below BBB- or Baa3 were approximately $883.5 million. Generally, collateral may be provided by a Southern Company guaranty, letter of credit, or cash.

Southern Company s operating subsidiaries are also party to certain agreements that could require collateral and/or accelerated payment in the event of a credit rating change to below investment grade for Alabama Power and/or Georgia Power. These agreements are primarily for natural gas and power price risk management activities. At September 30, 2007, Southern Company s total exposure to these types of agreements was $26.7 million.

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Market Price Risk

Southern Company s market risk exposures relative to interest rate changes have not changed materially compared with the December 31, 2006 reporting period. In addition, Southern Company is not aware of any facts or circumstances that would significantly affect such exposures in the near term.

Due to cost-based rate regulation, the traditional operating companies have limited exposure to market volatility in interest rates, 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. To mitigate residual risks relative to movements in electricity prices, the traditional operating companies and Southern Power enter into physical fixed-price contracts for the purchase and sale of electricity through the wholesale electricity market and, to a lesser extent, into financial hedge contracts for natural gas purchases. The traditional operating companies have implemented fuel-hedging programs at the instruction of their respective state PSCs.

The fair value of derivative energy contracts at September 30, 2007 was as follows:

	Third Quarter 2007 Changes	**Year-to-Date 2007 Changes**
	Fair Value *(in millions)*	
Contracts beginning of period	$(32)	$ (82)
Contracts realized or settled	32	62
New contracts at inception		
Changes in valuation techniques		
Current period changes (a)	(22)	(2)
Contracts at September 30, 2007	$(22)	$ (22)

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

	Source of September 30, 2007 Valuation Prices		
	Total Fair Value	Maturity	
		Year 1	1-3 Years
	(in millions)		
Actively quoted	$(22)	$(25)	$ 3
External sources		1	(1)
Models and other methods -			
Contracts at September 30, 2007	$(22)	$(24)	$ 2

Unrealized gains and losses from mark-to-market adjustments on derivative contracts related to the traditional operating companies fuel hedging programs are recorded as regulatory assets and liabilities. Realized gains and losses from these programs are included in fuel expense and are recovered through the traditional operating companies fuel cost recovery clauses. In addition, unrealized gains and losses on energy-related derivatives used by Southern Power to hedge anticipated purchases and sales are deferred in other comprehensive income. Gains and losses on derivative contracts that are not designated as hedges are recognized in the statements of income as incurred.

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

At September 30, 2007, the fair value gain/(loss) of derivative energy contracts was reflected in the financial statements as follows:

	Amounts
	(in millions)
Regulatory assets, net	$(21.7)
Accumulated other comprehensive income	0.5
Net income	(0.4)
Total fair value	$(21.6)

Unrealized pre-tax losses recognized in income for the three months and nine months ended September 30, 2007 for derivative energy contracts that are not hedges were $2.2 million and $0.7 million, respectively.

To reduce Southern Company s exposure to changes in the value of synthetic fuel tax credits, which are impacted by changes in oil prices, Southern Company has entered into derivative transactions indexed to annual average oil prices. Because these transactions are not designated as hedges, the gains and losses are recognized in the statements of income as incurred. For the three months and nine months ended September 30, 2007, the fair value gains recognized in income to mark the transactions to market were $23.6 million and $23.4 million, respectively.

For additional information, see MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Market Price Risk of Southern Company in Item 7 and Notes 1 and 6 to the financial statements of Southern Company under Financial Instruments in Item 8 of the Form 10-K and Note (F) to the Condensed Financial Statements herein.

Financing Activities

In the first nine months of 2007, Southern Company and its subsidiaries issued $2.8 billion of senior notes, incurred obligations related to the issuance of $246.5 million of pollution control revenue bonds, issued $150 million of preference stock, and issued $414 million of common stock, including treasury stock, through employee, director, and other stock plans. The proceeds were primarily used to repay short-term indebtedness, to redeem higher cost securities, and to fund ongoing construction projects. See Southern Company s Condensed Consolidated Statements of Cash Flows herein for further details on financing activities during the first nine months of 2007. Southern Company and its subsidiaries also terminated interest rate derivatives related to these transactions at a gain of $15 million. These gains were deferred in other comprehensive income, of which $9 million will be amortized to income over a 10-year period and $6 million will be amortized over a 30-year period. During the first nine months of 2007, Southern Company and its subsidiaries redeemed or paid at maturity $1.6 billion in senior notes and other long-term debt.

In September 2007, holders of $225 million aggregate principal amount of Southern Company s Series 2007B Floating Rate Extendible Senior Notes and holders of $75 million aggregate principal amount of Georgia Power s Series 2007C Floating Rate Senior Notes elected not to extend the then current maturity dates in September 2008.

During the first nine months of 2007, Southern Company and its subsidiaries entered into additional derivative transactions designed to hedge interest rate risk of future debt issuances. See Note (F) to the Condensed Financial Statements herein for further details.

Subsequent to September 30, 2007, Alabama Power issued $200 million of Series 2007C 6.00% Senior Insured Monthly Notes due October 15, 2037 and issued $50 million of 6.50% Preference Stock. The proceeds from both issuances were used for general corporate purposes and to fund its continuous construction program. Alabama Power also terminated interest rate derivatives related to the senior note issuance at a loss of less than $1 million. Georgia Power issued $225 million of 6.50% Preference Stock. The proceeds along with other

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

monies of Georgia Power were applied to the redemption in November of $309 million aggregate principal amount of its Series F 4.875% Junior Subordinated Notes due November 1, 2042 and the related flexible trust preferred and common securities of Georgia Power Capital Trust VI. Also subsequent to September 30, 2007, Gulf Power issued $45 million of 6.45% Preference Stock. Proceeds were used to repay a portion of short-term indebtedness and for other corporate purposes including its continuous construction program. In addition, Alabama Power announced the planned redemption of 1,250 shares of Alabama Power Company Flexible Money Market Class A Preferred Stock (Series 2003A), Par Value $100,000 Per Share ($125 million aggregate value) in January 2008. In October 2007, Gulf Power issued a notice of redemption to the holders of the $41.2 million of Gulf Power Series E Junior Subordinated Notes due November 30, 2042 and the related trust preferred and common securities of Gulf Power Capital Trust IV. All securities in this series will be redeemed in November 2007.

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.

Table of Contents

PART I

Item 3. Quantitative And Qualitative Disclosures About Market Risk.

See MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Market Price Risk herein for each registrant and Notes 1 and 6 to the financial statements of Southern Company, Alabama Power, Georgia Power, Gulf Power, Mississippi Power, and Southern Power under Financial Instruments in Item 8 of the Form 10-K. Also, see Note (F) to the Condensed Financial Statements herein for information relating to derivative instruments.

Item 4. Controls and Procedures.

(a) Evaluation of disclosure controls and procedures.

As of the end of the period covered by this quarterly report, Southern Company, Alabama Power, Georgia Power, Gulf Power, Mississippi Power, and Southern Power conducted separate evaluations under the supervision and with the participation of each company s management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the disclosure controls and procedures (as defined in Sections 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). Based upon these evaluations, the Chief Executive Officer and the Chief Financial Officer, in each case, concluded that the disclosure controls and procedures are effective in alerting them in a timely manner to information relating to their company (including its consolidated subsidiaries, if any) required to be included in periodic filings with the SEC.

(b) Changes in internal controls.

There have been no changes in Southern Company s, Alabama Power s, Georgia Power s, Gulf Power s, Mississippi Power s, or Southern Power s internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) during the third quarter of 2007 that have materially affected or are reasonably likely to materially affect Southern Company s, Alabama Power s, Georgia Power s, Gulf Power s, Mississippi Power s, or Southern Power s internal control over financial reporting.

ALABAMA POWER COMPANY

Table of Contents

ALABAMA POWER COMPANY
CONDENSED STATEMENTS OF INCOME (UNAUDITED)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2007	2006	**2007**	2006
	(in thousands)		*(in thousands)*	
Operating Revenues:				
Retail revenues	**$ 1,394,539**	$ 1,333,021	**$ 3,444,282**	$ 3,161,873
Wholesale revenues				
Non-affiliates	**160,832**	167,066	**472,015**	469,748
Affiliates	**35,400**	29,138	**116,626**	134,551
Other revenues	**44,427**	43,182	**135,569**	128,366
Total operating revenues	**1,635,198**	1,572,407	**4,168,492**	3,894,538
Operating Expenses:				
Fuel	**506,933**	521,507	**1,353,914**	1,282,450
Purchased power				
Non-affiliates	**71,622**	66,690	**94,330**	121,394
Affiliates	**100,054**	88,407	**249,261**	234,145
Other operations	**201,495**	182,508	**556,639**	527,580
Maintenance	**88,135**	81,287	**303,989**	287,734
Depreciation and amortization	**118,403**	114,052	**351,514**	336,209
Taxes other than income taxes	**72,503**	59,692	**216,752**	190,635
Total operating expenses	**1,159,145**	1,114,143	**3,126,399**	2,980,147
Operating Income	**476,053**	458,264	**1,042,093**	914,391
Other Income and (Expense):				
Allowance for equity funds used during construction	**9,600**	3,921	**24,562**	13,285
Interest income	**4,935**	4,931	**12,942**	12,973
Interest expense, net of amounts capitalized	**(65,918)**	(61,786)	**(194,565)**	(174,079)
Interest expense to affiliate trusts	**(4,059)**	(4,059)	**(12,178)**	(12,178)
Other income (expense), net	**(13,067)**	(7,866)	**(19,957)**	(17,599)
Total other income and (expense)	**(68,509)**	(64,859)	**(189,196)**	(177,598)
Earnings Before Income Taxes	**407,544**	393,405	**852,897**	736,793
Income taxes	**152,956**	149,379	**319,840**	280,376
Net Income	**254,588**	244,026	**533,057**	456,417
Dividends on Preferred and Preference Stock	**8,504**	6,072	**24,867**	18,216
Net Income After Dividends on Preferred and Preference Stock	**$ 246,084**	$ 237,954	**$ 508,190**	$ 438,201

CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2007	2006	**2007**	2006
	(in thousands)		*(in thousands)*	
Net Income After Dividends on Preferred and Preference Stock	**$ 246,084**	$ 237,954	**$ 508,190**	$ 438,201
Other comprehensive income (loss):				
Qualifying hedges:				
Changes in fair value, net of tax of $(932), $(2,049), $256, and $334, respectively	**(1,533)**	(3,369)	**420**	551
Reclassification adjustment for amounts included in net income, net of tax of $74, $(854), $206, and $(2,869), respectively	**121**	(1,406)	**339**	(4,720)
Total other comprehensive income (loss)	**(1,412)**	(4,775)	**759**	(4,169)
COMPREHENSIVE INCOME	**$ 244,672**	$ 233,179	**$ 508,949**	$ 434,032

The accompanying notes as they relate to Alabama Power are an integral part of these condensed financial statements.

Table of Contents

ALABAMA POWER COMPANY
CONDENSED STATEMENTS OF CASH FLOWS (UNAUDITED)

	For the Nine Months Ended September 30,	
	2007	2006
	(in thousands)	
Operating Activities:		
Net income	**$ 533,057**	$ 456,417
Adjustments to reconcile net income to net cash provided from operating activities		
Depreciation and amortization	**410,695**	391,422
Deferred income taxes and investment tax credits, net	**10,545**	17,157
Allowance for equity funds used during construction	**(24,562)**	(13,285)
Pension, postretirement, and other employee benefits	**6,941**	8,795
Stock option expense	**4,533**	4,518
Tax benefit of stock options	**1,051**	267
Hedge settlements		18,006
Other, net	**11,465**	(8,383)
Changes in certain current assets and liabilities		
Receivables	**(168,447)**	(144,475)
Fossil fuel stock	**(17,123)**	(37,858)
Materials and supplies	**(30,412)**	(13,683)
Other current assets	**7,624**	33,980
Accounts payable	**(53,611)**	(152,179)
Accrued taxes	**213,510**	134,349
Accrued compensation	**(23,986)**	(34,658)
Other current liabilities	**17,130**	32,894
Net cash provided from operating activities	**898,410**	693,284
Investing Activities:		
Property additions	**(822,818)**	(618,568)
Investment in restricted cash from pollution control bonds	**(96,049)**	
Distribution of restricted cash from pollution control bonds	**44,550**	
Nuclear decommissioning trust fund purchases	**(201,523)**	(206,480)
Nuclear decommissioning trust fund sales	**201,523**	206,480
Cost of removal, net of salvage	**(33,194)**	(28,089)
Other	**(12,930)**	(19,054)
Net cash used for investing activities	**(920,441)**	(665,711)
Financing Activities:		
Decrease in notes payable, net	**(119,670)**	(315,278)
Proceeds		
Common stock issued to parent	**140,000**	40,000
Senior notes	**450,000**	950,000
Pollution control bonds	**246,500**	
Preference Stock	**150,000**	
Gross excess tax benefit of stock options	**2,324**	530

Redemptions		
Pollution control bonds		(2,950)
Senior notes	**(168,500)**	(196,500)
Payment of preferred and preference stock dividends	**(22,875)**	(18,210)
Payment of common stock dividends	**(348,750)**	(330,450)
Other	**(14,822)**	(21,469)
Net cash provided from financing activities	**314,207**	105,673
Net Change in Cash and Cash Equivalents	**292,176**	133,246
Cash and Cash Equivalents at Beginning of Period	**15,539**	22,472
Cash and Cash Equivalents at End of Period	**$ 307,715**	$ 155,718
Supplemental Cash Flow Information:		
Cash paid during the period for		
Interest (net of $12,455 and $5,652 capitalized for 2007 and 2006, respectively)	**$ 176,842**	$ 174,568
Income taxes (net of refunds)	**$ 157,501**	$ 165,266

The accompanying notes as they relate to Alabama Power are an integral part of these condensed financial statements.

Table of Contents

ALABAMA POWER COMPANY
CONDENSED BALANCE SHEETS (UNAUDITED)

Assets	At September 30, 2007	At December 31, 2006
	(in thousands)	
Current Assets:		
Cash and cash equivalents	$ 307,715	$ 15,539
Restricted cash	51,499	
Receivables		
Customer accounts receivable	488,928	323,202
Unbilled revenues	109,336	90,596
Under recovered regulatory clause revenues	278,288	32,451
Other accounts and notes receivable	57,179	49,708
Affiliated companies	30,128	70,836
Accumulated provision for uncollectible accounts	(8,721)	(7,091)
Fossil fuel stock, at average cost	170,063	153,120
Materials and supplies, at average cost	285,863	255,664
Vacation pay	46,642	46,465
Prepaid expenses	41,236	76,265
Other	21,988	66,663
Total current assets	1,880,144	1,173,418
Property, Plant, and Equipment:		
In service	16,444,682	15,997,793
Less accumulated provision for depreciation	5,869,903	5,636,475
	10,574,779	10,361,318
Nuclear fuel, at amortized cost	145,290	137,300
Construction work in progress	838,421	562,119
Total property, plant, and equipment	11,558,490	11,060,737
Other Property and Investments:		
Equity investments in unconsolidated subsidiaries	50,325	47,486
Nuclear decommissioning trusts, at fair value	549,526	513,521
Other	29,780	35,980
Total other property and investments	629,631	596,987
Deferred Charges and Other Assets:		
Deferred charges related to income taxes	378,893	354,225
Prepaid pension costs	749,158	722,287
Deferred under recovered regulatory clause revenues	69,168	301,048
Other regulatory assets	270,877	279,661
Other	207,923	166,927

Total deferred charges and other assets	**1,676,019**	1,824,148
Total Assets	**$ 15,744,284**	$ 14,655,290

The accompanying notes as they relate to Alabama Power are an integral part of these condensed financial statements.

38

Table of Contents

ALABAMA POWER COMPANY
CONDENSED BALANCE SHEETS (UNAUDITED)

Liabilities and Stockholder s Equity	At September 30, 2007	At December 31, 2006
	(in thousands)	
Current Liabilities:		
Securities due within one year	**$ 978,244**	$ 668,646
Notes payable		119,670
Accounts payable		
Affiliated	**172,113**	162,951
Other	**207,241**	263,506
Customer deposits	**65,941**	62,978
Accrued taxes		
Income taxes	**195,292**	3,120
Other	**96,926**	29,696
Accrued interest	**65,770**	53,573
Accrued vacation pay	**38,645**	38,767
Accrued compensation	**62,993**	87,194
Other	**60,003**	79,907
Total current liabilities	**1,943,168**	1,570,008
Long-term Debt	**4,285,242**	3,838,906
Long-term Debt Payable to Affiliated Trusts	**206,186**	309,279
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	**2,056,588**	2,116,575
Deferred credits related to income taxes	**96,114**	98,941
Accumulated deferred investment tax credits	**182,579**	188,582
Employee benefit obligations	**411,073**	375,940
Asset retirement obligations	**499,197**	476,460
Other cost of removal obligations	**612,755**	600,278
Other regulatory liabilities	**439,806**	399,822
Other	**36,769**	35,805
Total deferred credits and other liabilities	**4,334,881**	4,292,403
Total Liabilities	**10,769,477**	10,010,596
Preferred and Preference Stock	**634,646**	612,407
Common Stockholder s Equity:		
Common stock, par value $40 per share		
Authorized 25,000,000 shares		
Outstanding September 30, 2007: 15,750,000 shares		

December 31, 2006: 12,250,000 shares	**630,000**	490,000
Paid-in capital	**2,036,633**	2,028,963
Retained earnings	**1,675,690**	1,516,245
Accumulated other comprehensive loss	**(2,162)**	(2,921)
Total common stockholder s equity	**4,340,161**	4,032,287
Total Liabilities and Stockholder s Equity	**$ 15,744,284**	$ 14,655,290

The accompanying notes as they relate to Alabama Power are an integral part of these condensed financial statements.

39

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
THIRD QUARTER 2007 vs. THIRD QUARTER 2006
AND
YEAR-TO-DATE 2007 vs. YEAR-TO-DATE 2006

OVERVIEW

Alabama Power operates as a vertically integrated utility providing electricity to retail customers within its traditional service area located within the State of Alabama and to wholesale customers in the Southeast. Many factors affect the opportunities, challenges, and risks of Alabama Power s primary business of selling electricity. These factors include the ability to maintain a stable regulatory environment, to achieve energy sales growth, and to effectively manage and secure timely recovery of rising costs. These costs include those related to growing demand, increasingly stringent environmental standards, fuel prices, and restoration following major storms.

Alabama Power continues to focus on several key performance indicators. These indicators include customer satisfaction, plant availability, system reliability, and net income. For additional information on these indicators, see MANAGEMENT S DISCUSSION AND ANALYSIS OVERVIEW Key Performance Indicators of Alabama Power in Item 7 of the Form 10-K.

RESULTS OF OPERATIONS

Net Income

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$8.1	3.4	$70.0	16.0

Alabama Power s net income after dividends on preferred and preference stock for the third quarter 2007 was $246.1 million compared to $238.0 million for the corresponding period of 2006. Net income after dividends on preferred and preference stock for year-to-date 2007 was $508.2 million compared to $438.2 million for the corresponding period of 2006. The increase in earnings for the third quarter and year-to-date 2007 were primarily due to retail base rate revenue increases resulting from an increase in rates under Rate RSE and Rate CNP for environmental costs (Rate CNP Environmental) that took effect January 1, 2007, as well as favorable weather conditions. See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL PSC Matters Retail Rate Adjustments of Alabama Power in Item 7 and Note 3 to the financial statements of Alabama Power under Retail Regulatory Matters in Item 8 of the Form 10-K for additional information on Alabama Power s rates. The increases in revenues for the third quarter and year-to-date 2007 were partially offset by increases in other operations expense mainly related to administrative and general expense, maintenance expense primarily associated with distribution, steam power, and nuclear power, taxes other than income taxes related to state and municipal public utility license tax, and interest expense due to additional debt outstanding and higher interest rates associated with the issuance of new long-term debt.

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Retail Revenues

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$61.5	4.6	$282.4	8.9

In the third quarter 2007, retail revenues were $1.39 billion compared to $1.33 billion in the same period in 2006. For year-to-date 2007, retail revenues were $3.44 billion compared to $3.16 billion in the same period in 2006. Details of retail revenues are as follows:

	Third Quarter 2007		Year-to-Date 2007	
	(in millions)	*(% change)*	*(in millions)*	*(% change)*
Retail prior year	$1,333.0		$3,161.9	
Estimated change in				
Rates and pricing	61.5	4.6	171.0	5.4
Sales growth	(2.6)	(0.2)	(0.5)	0.0
Weather	10.8	0.8	34.2	1.0
Fuel and other cost recovery	(8.2)	(0.6)	77.7	2.5
Retail current year	$1,394.5	4.6%	$3,444.3	8.9%

Revenues associated with changes in rates and pricing increased in the third quarter and year-to-date 2007 when compared to the same periods in 2006 primarily due to the Rate RSE and Rate CNP Environmental increases effective in January 2007. See MANAGEMENT S DISCUSSION AND ANALYSIS - FUTURE EARNINGS POTENTIAL PSC Matters Retail Rate Adjustments of Alabama Power in Item 7 and Note 3 to the financial statements of Alabama Power under Retail Regulatory Matters in Item 8 of the Form 10-K.

Revenues attributable to changes in sales growth were relatively flat in the third quarter of 2007 when compared to the same period in 2006. Commercial KWH energy sales increased due to continued customer and demand growth. This increase was offset by a decrease in industrial KWH energy sales as a result of decreased sales demand in the chemicals and textiles sectors. Residential KWH energy sales during the third quarter 2007 were relatively flat.

For year-to-date 2007, revenues attributable to changes in sales growth were relatively flat when compared to the same period in 2006. Commercial KWH energy sales increased 1.5% due to continued customer and demand growth. This increase was offset by a 0.9% decrease in KWH energy sales to residential customers primarily as a result of a decrease in average residential customer usage and a 2.0% decrease in KWH energy sales to industrial customers primarily as a result of decreased sales demand in the primary metals and textiles sectors.

Revenues increased as a result of favorable weather in the third quarter of 2007 when compared to same period in 2006. The favorable weather, which primarily impacts residential and commercial customers, resulted in increased KWH energy sales to these customers of 1.5% each.

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

For year-to-date 2007, revenues increased as a result of favorable weather when compared to same period in 2006 which resulted in increased KWH energy sales to residential and commercial customers of 3.1% and 1.2%, respectively.

Fuel and other cost recovery revenues decreased in the third quarter of 2007 when compared to the same period in 2006 due to the reduction in the Rate NDR customer billing rate as a result of Alabama Power fully recovering the balance in the deferred natural disaster reserve account in June 2007. See FUTURE EARNINGS POTENTIAL FERC and Alabama Power PSC Matters Natural Disaster Cost Recovery herein for additional information.

For year-to-date 2007, fuel and other cost recovery revenues increased when compared to the same period in 2006 due to an increase in fuel costs, purchased power costs, and cost associated with PPAs certificated by the Alabama PSC, offset by a reduction in the Rate NDR customer billing rate. Electric rates for Alabama Power include provisions to recognize the full recovery of fuel costs, purchased power costs, PPAs certificated by the Alabama PSC, and costs associated with Alabama Power s natural disaster reserve. Under these provisions, fuel and other cost recovery revenues generally equal fuel and other cost recovery expenses and do not affect net income.

Wholesale Revenues Affiliates

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$6.3	21.5	$(17.9)	(13.3)

In the third quarter 2007, revenues from wholesale energy sales to affiliates were $35.4 million compared to $29.1 million in the same period in 2006. This increase was primarily due to a 44.1% increase in price offset by a 15.7% decrease in KWH sales.

For year-to-date 2007, revenues from wholesale energy sales to affiliates were $116.6 million compared to $134.5 million for the same period in 2006. This decrease was primarily due to an 8.3% decrease in price as well as a 5.5% decrease in KWH sales.

Wholesale energy sales to affiliated companies within the Southern Company system vary from period to period depending on demand and the availability and cost of generating resources at each company. These sales are made in accordance with the IIC, as approved by the FERC. These transactions do not have a significant impact on earnings since the energy is generally sold at marginal cost.

Other Revenues

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$1.2	2.9	$7.2	5.6

The third quarter 2007 variance when compared to the third quarter 2006 is not material.

For year-to-date 2007, other revenues were $135.6 million compared to $128.4 million for the same period in 2006. This increase was mainly due to a $4.2 million increase in revenues from co-generation steam facilities resulting from higher gas prices and facilities service contracts and a $2.1 million increase in revenues associated with rent from electric property related to pole attachments and microwave tower rentals.

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Fuel and Purchased Power Expenses

	Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
	(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
Fuel	$ (14.6)	(2.8)	$ 71.5	5.6
Purchased power-non-affiliates	4.9	7.4	(27.1)	(22.3)
Purchased power-affiliates	11.7	13.2	15.1	6.5
Total fuel and purchased power expenses	$ 2.0		$ 59.5	

In the third quarter 2007, total fuel and purchased power expenses were $678.6 million compared to $676.6 million in the same period in 2006. This increase was primarily due to a $10.6 million increase related to greater KWHs purchased offset by an $8.6 million decrease in the cost of energy resulting from a decrease in the average cost of fuel. For year-to-date 2007, total fuel and purchased power expenses were $1.70 billion compared to $1.64 billion for the same period in 2006. This increase is primarily due to a $60.4 million increase related to greater KWHs generated and purchased.

Fuel and purchased power transactions do not have a significant impact on earnings since energy expenses are generally offset by energy revenues through Alabama Power s energy cost recovery clause.

Details of Alabama Power s cost of generation and purchased power are as follows:

Average Cost	Third Quarter 2007	Third Quarter 2006	% change	Year-to-Date 2007	Year-to-Date 2006	% change
	(cents per net KWH)			*(cents per net KWH)*		
Fuel	2.35	2.41	(2.5)	2.35	2.34	0.4
Purchased power	7.57	7.43	1.9	6.30	6.41	(1.7)

In the third quarter 2007, fuel expense was $506.9 million compared to $521.5 million in the same period in 2006. This decrease was due to a 1.4% decrease in generation from Alabama Power-owned coal and gas-fired facilities and a 5.0% decrease in natural gas prices. These decreases were partially offset by a 1.4% increase in the average cost of coal.

For year-to-date 2007, fuel expense was $1.35 billion compared to $1.28 billion for the same period in 2006. This increase was due to a 1.4% increase in the average cost of coal and a 3.2% increase in generation from Alabama Power-owned coal and gas-fired facilities due to a 47.3% decrease in hydro generation from a severe drought. These increases were partially offset by a 4.6% decrease in natural gas prices.

Non-affiliates

In the third quarter 2007, purchased power non-affiliates was $71.6 million compared to $66.7 million in the same period in 2006. This increase was primarily due to a 65.5% increase in the amount of energy purchased due to the use of available lower price market purchases from non-affiliates to meet the increase in weather related system demand requirements partially offset by a 33.6% decrease in price.

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

For year-to-date 2007, purchased power non-affiliates was $94.3 million compared to $121.4 million for the same period in 2006. This decrease was primarily due to a 12.9% decrease in price while the amount of energy purchased declined slightly.

Energy purchases from non-affiliates will vary depending on market cost of available energy being lower than Southern Company system-generated energy, demand for energy within the system service territory, and availability of Southern Company system generation.

Affiliates

In the third quarter 2007, purchased power affiliates was $100.1 million compared to $88.4 million in the same period in 2006. This increase was due to a 13.1% increase in price offset by a 2.5% decrease in energy purchased.

For year-to-date 2007, purchased power affiliates was $249.3 million compared to $234.2 million in the same period in 2006. This increase was due to a 6.4% increase in energy purchased and a 5.4% increase in price.

Energy purchases from affiliates will vary depending on demand and the availability and cost of generating resources at each company within the Southern Company system. These purchases are made in accordance with the IIC, as approved by the FERC.

Other Operations and Maintenance Expenses

	Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
	(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
Other operations	$ 19.0	10.4	$ 29.0	5.5
Maintenance	6.8	8.4	16.3	5.6
Total other operations and maintenance expenses	$ 25.8		$ 45.3	

In the third quarter 2007, other operations and maintenance expenses were $289.6 million compared to $263.8 million in the same period in 2006. This was primarily a result of a $9.6 million increase in administrative and general expenses related to an increase in the accrued expenses for liability insurance, litigation and workers compensation reserve, and an increase in nuclear services expense and a $6.7 million increase in steam power expense associated with scheduled outage maintenance cost, environmental-related expense at various coal-fired facilities, and the cost of labor and materials. Also contributing to the increase was a $4.6 million increase in nuclear expense related to outage cost and a $2.9 million increase in distribution expenses related to scheduled overhead line clearance.

For year-to-date 2007, other operations and maintenance expenses were $860.6 million compared to $815.3 million in the same period in 2006. This increase is primarily due to a $12.6 million increase in distribution expenses related to scheduled overhead line clearance and meter expenses and an $8.8 million increase in administrative and general expenses related to an increase in the accrued expenses for liability insurance, litigation and workers compensation reserve, and an increase in employee group insurance. Also contributing to the increase was a $7.2 million increase in steam power expense associated with increases in environmental-related expenses as well as the cost of labor and materials, a $6.3 million increase in nuclear expense related to

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

outage cost, a $3.3 million increase in transmission expenses related to load dispatching and external electric purchases, and a $2.6 million increase in customer accounts related to uncollectible accounts and meter reading expense.

Taxes Other than Income Taxes

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$12.8	21.5	$26.1	13.7

In the third quarter 2007, taxes other than income taxes were $72.5 million compared to $59.7 million in the same period in 2006. For year-to-date 2007, taxes other than income taxes were $216.7 million compared to $190.6 million for the same period in 2006. These increases were primarily due to increases in state and municipal public utility license taxes which are directly related to increased retail revenues.

Allowance for Equity Funds Used During Construction

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$5.7	144.8	$11.3	84.9

Allowance for equity funds used during construction (AFUDC) in the third quarter 2007 was $9.6 million compared to $3.9 million in the same period in 2006. For year-to-date 2007, AFUDC was $24.6 million compared to $13.3 million for the same period in 2006. These increases were primarily due to increases in the amount of construction work in progress related to environmental, transmission, and distribution projects compared to the same periods in 2006.

Interest Expense, Net of Amounts Capitalized

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$4.1	6.7	$20.5	11.8

In the third quarter 2007, interest expense, net of amounts capitalized was $65.9 million compared to $61.8 million in the same period in 2006. For year-to-date 2007, interest expense, net of amounts capitalized was $194.6 million compared to $174.1 million for the same period in 2006. These increases were mainly due to additional debt outstanding and higher interest rates associated with the issuance of new long-term debt. For additional information, see MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Financing Activities of Alabama Power in Item 7 of the Form 10-K and FINANCIAL CONDITION AND LIQUIDITY Financing Activities herein.

Other Income (Expense), Net

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$5.2	66.1	$2.4	13.4

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In the third quarter 2007, other income (expense), net was $13.1 million compared to $7.9 million in the same period in 2006. This increase in other income (expense), net was mainly attributed to the write off of the net book value of certain equipment due to the discontinuation of a non-utility marketing program. Neither the write off of the assets, the revenue, nor the net profit(loss) associated with this marketing program were material to the results of operations.

For year-to-date 2007, other income (expense), net was $20.0 million compared to $17.6 million for the same period in 2006. The increase in other expense, net was mainly attributed to the write off of the net book value of certain equipment due to the discontinuation of a non-utility marketing program during the third quarter. This increase was partially offset due to the recording of the settlement with the EPA in the NSR litigation in the first quarter of 2006. For additional information, see MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL - Environmental Matters New Source Review Actions of Alabama Power in Item 7 of the Form 10-K.

Dividends on Preferred and Preference Stock

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$2.4	40.1	$6.7	36.5

Dividends on preferred and preference stock in the third quarter 2007 were $8.5 million compared to $6.1 million in the same period in 2006. For year-to-date 2007, dividends on preferred and preference stock were $24.9 million compared to $18.2 million for the same period in 2006. These increases were due to the additional dividends associated with the issuance of six million shares of preference stock ($150 million stated capital) in December 2006 and the issuance of six million shares of preference stock ($150 million stated capital) in September 2007. For additional information, see MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Financing Activities of Alabama Power in Item 7 of the Form 10-K.

Income Taxes

Third Quarter 2007 vs. Third Quarter 2006		Year-to-Date 2007 vs. Year-to-Date 2006	
(change in millions)	*(% change)*	*(change in millions)*	*(% change)*
$3.6	2.4	$39.5	14.1

The third quarter 2007 variance when compared to the third quarter 2006 is not material.

For year-to-date 2007, income tax expense was $319.8 million compared to $280.3 million in the same period in 2006. This increase was primarily a result of higher earnings before income taxes.

FUTURE EARNINGS POTENTIAL

The results of operations discussed above are not necessarily indicative of Alabama Power s future earnings potential. The level of Alabama Power s future earnings depends on numerous factors that affect the opportunities, challenges, and risks of Alabama Power s primary business of selling electricity. These factors include Alabama Power s ability to maintain a stable regulatory environment that continues to allow for the recovery of all prudently incurred costs during a time of increasing costs. Future earnings in the near term will depend, in part, upon growth in energy sales, which is subject to a number of factors. These factors include

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

weather, competition, new energy contracts with neighboring utilities, energy conservation practiced by customers, the price of electricity, the price elasticity of demand, and the rate of economic growth in Alabama Power s service area. For additional information relating to these issues, see RISK FACTORS in Item 1A and MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL of Alabama Power in Item 7 of the Form 10-K.

Environmental Matters

Compliance costs related to the Clean Air Act and other environmental regulations could affect earnings if such costs cannot be fully recovered in rates on a timely basis. See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters of Alabama Power in Item 7 and Note 3 to the financial statements of Alabama Power under Environmental Matters in Item 8 of the Form 10-K for additional information.

New Source Review Litigation

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters New Source Review Actions of Alabama Power in Item 7 and Note 3 to the financial statements of Alabama Power under Environmental Matters New Source Review Actions in Item 8 of the Form 10-K for additional information regarding a civil action brought by the EPA alleging that Alabama Power had violated the NSR provisions of the Clean Air Act and related state laws with respect to certain of its coal-fired generating facilities. The plaintiffs appeal against Alabama Power was stayed by the U.S. Court of Appeals for the Eleventh Circuit pending the U.S. Supreme Court s decision in a similar case against Duke Energy. On April 2, 2007, the U.S. Supreme Court issued an opinion in the Duke Energy case. The U.S. District Court for the Northern District of Alabama has issued an order indicating a willingness to re-evaluate its previous decision in light of the Supreme Court s Duke Energy opinion. The Eleventh Circuit is now considering whether to proceed with the appeal or remand the case to the District Court for further proceedings, and if so, whether to vacate the District Court s original judgment in favor of Alabama Power. The final resolution of these claims cannot be determined at this time.

Eight-Hour Ozone Regulations

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters - Environmental Statutes and Regulations Air Quality of Alabama Power in Item 7 of the Form 10-K for additional information regarding revisions to the eight-hour ozone air quality standard. On June 20, 2007, the EPA proposed additional revisions to the current eight-hour ozone standard which, if enacted, could result in designation of new nonattainment areas within Alabama Power s service territory. The EPA has requested comment and is expected to make a determination regarding finalization of a revised standard in 2008. The ultimate outcome of this matter cannot be determined at this time.

Fine Particulate Matter Regulations

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL Environmental Matters - Environmental Statutes and Regulations Air Quality of Alabama Power in Item 7 of the Form 10-K for additional information regarding nonattainment designations for the fine particulate matter air quality standard. In March 2007, the EPA finalized its fine particulate matter implementation rule, requiring submittal of state plans for addressing the nonattainment designations by April 2008. The ultimate outcome of this matter depends on the development and submittal of those state plans and the resolution of pending legal challenges and, therefore, cannot be determined at this time.

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FERC and Alabama PSC Matters

Market-Based Rate Authority

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL FERC Matters - Market-Based Rate Authority of Alabama Power in Item 7 and Note 3 to the financial statements of Alabama Power under FERC Matters Market-Based Rate Authority in Item 8 of the Form 10-K for information regarding the proceedings initiated by the FERC in December 2004 to assess Southern Company s generation dominance within its retail service territory and in May 2005 to determine whether Southern Company satisfies the other three parts of the FERC s market-based rate analysis: transmission market power, barriers to entry, and affiliate abuse or reciprocal dealing.

In late June and July 2007, hearings were held in the December 2004 proceeding and briefs to the presiding ALJ were filed in August and September. Alabama Power anticipates an initial decision from the ALJ in November 2007 on the issues that were set for hearing. The ultimate outcome of this generation dominance proceeding cannot now be determined, but an adverse decision by the FERC in a final order could result in refunds of approximately $3.9 million, plus interest.

On June 21, 2007, the FERC issued an order terminating the May 2005 proceeding pertaining to the other three parts of the market-based rate analysis. In addition, on June 21, 2007, the FERC issued its final rule regarding market-based rate authority. The FERC generally retained its current market-based rate standards. The impact of this order and its effect on the generation dominance proceeding cannot now be determined.

Intercompany Interchange Contract

See MANAGEMENT S DISCUSSION AND ANALYSIS - FUTURE EARNINGS POTENTIAL FERC Matters - Intercompany Interchange Contract of Alabama Power in Item 7 and Note 3 to the financial statements of Alabama Power under FERC Matters Intercompany Interchange Contract in Item 8 of the Form 10-K for information regarding the proceeding initiated by the FERC in May 2005 to examine (1) the provisions of the IIC among Alabama Power, Georgia Power, Gulf Power, Mississippi Power, Savannah Electric, Southern Power, and SCS, as agent, under the terms of which the Power Pool is operated, and, in particular, the propriety of the continued inclusion of Southern Power as a party to the IIC, (2) whether any parties to the IIC have violated the FERC s standards of conduct applicable to utility companies that are transmission providers, and (3) whether Southern Company s code of conduct defining Southern Power as a system company rather than a marketing affiliate is just and reasonable.

On April 19, 2007, the FERC approved, with certain modifications, the compliance filing submitted by Southern Company on November 6, 2006. The compliance plan largely involves functional separation and information restrictions related to marketing activities conducted on behalf of Southern Power. Implementation of the plan is not expected to have a material impact on Alabama Power s financial statements.

Retail Fuel Cost Recovery

Alabama Power has established fuel cost recovery rates approved by the Alabama PSC. Alabama Power s under recovered fuel costs as of September 30, 2007 totaled $307 million as compared to $301 million at December 31, 2006. As a result of the increasing level of under recovered fuel costs, in June 2007, the Alabama PSC ordered Alabama Power to increase its Rate ECR factor to 3.1 cents per KWH from 2.4 cents per KWH,

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

effective with billings beginning July 2007 for the 30-month period ending December 2009. This change represents on average an increase of approximately $7.37 per month for a customer billing of 1,000 KWH. This increase is intended to permit the recovery of energy costs based on an estimate of future energy costs, as well as the collection of the existing under recovered energy costs by the end of 2009. During the 30-month period, Alabama Power will be allowed to include a carrying charge associated with the under recovered fuel costs in the fuel expense calculation. In the event the application of this increased Rate ECR factor results in an over recovered position during this period, Alabama Power will pay interest on any such over recovered balance at the same rate used to derive the carrying costs. As a result of the order, Alabama Power classified $69 million of the under recovered regulatory clause receivable as deferred charges and other assets in the Condensed Balance Sheet as of September 30, 2007 herein.

Natural Disaster Cost Recovery

See MANAGEMENT S DISCUSSION AND ANALYSIS FUTURE EARNINGS POTENTIAL PSC Matters Natural Disaster Cost Recovery of Alabama Power in Item 7 and Note 3 to the financial statements of Alabama Power under Retail Regulatory Matters Natural Disaster Cost Recovery in Item 8 of the Form 10-K for information regarding natural disaster cost recovery. As of December 31, 2006, Alabama Power had a deficit balance in the deferred natural disaster reserve account of approximately $16.8 million. In June 2007, Alabama Power fully recovered its prior storm costs related to Hurricanes Dennis and Katrina. As a result customer rates decreased by $1.73 per month per residential customer account and $4.29 per month per non-residential customer account beginning with July 2007 billings. Alabama Power continues to collect a monthly Rate NDR charge to establish and maintain a target reserve balance of $75 million for future storms. At September 30, 2007, Alabama Power had accumulated a balance of $23.1 million in the target reserve for future storms, which is included in the Condensed Balance Sheet herein under Other Regulatory Liabilities.

Other Matters

Alabama Power is subject to certain claims and legal actions arising in the ordinary course of business. In addition, Alabama Power s business activities are subject to extensive governmental regulation related to public health and the environment. 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 opacity and air quality standards, has increased generally throughout the United States. In particular, personal injury claims for damages caused by alleged exposure to hazardous materials have become more frequent. The ultimate outcome of such pending or potential litigation against Alabama Power cannot be predicted at this time; however, for current proceedings not specifically reported herein or in Note 3 to the financial statements of Alabama Power in Item 8 of the Form 10-K, management does not anticipate that the liabilities, if any, arising from such current proceedings would have a material adverse effect on Alabama Power s financial statements.

See the Notes to the Condensed Financial Statements herein for 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

Alabama Power prepares its financial statements in accordance with accounting principles generally accepted in

Table of Contents

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

the United States. Significant accounting policies are described in Note 1 to the financial statements of Alabama Power in Item 8 of the Form 10-K. In the application of these policies, certain estimates are made that may have a material impact on Alabama Power 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. See MANAGEMENT S DISCUSSION AND ANALYSIS ACCOUNTING POLICIES Application of Critical Accounting Policies and Estimates of Alabama Power in Item 7 of the Form 10-K for a complete discussion of Alabama Power s critical accounting policies and estimates related to Electric Utility Regulation, Contingent Obligations, and Unbilled Revenues.

New Accounting Standards

Income Taxes

On January 1, 2007, Alabama Power adopted FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes. FIN 48 requires companies to determine whether it is more likely than not that a tax position will be sustained upon examination by the appropriate taxing authorities before any part of the benefit can be recorded in the financial statements. It also provides guidance on the recognition, measurement, and classification of income tax uncertainties, along with any related interest and penalties. The provisions of FIN 48 were applied to all tax positions beginning January 1, 2007. The adoption of FIN 48 did not have a material impact on Alabama Power s financial statements.

Fair Value Measurement

The FASB issued FASB Statement No. 157 (SFAS No. 157), Fair Value Measurements in September 2006. This standard provides guidance on how to measure fair value where it is permitted or required under other accounting pronouncements. SFAS No. 157 also requires additional disclosures about fair value measurements. Alabama Power plans to adopt SFAS No. 157 on January 1, 2008 and is currently assessing the impact of this standard.

Fair Value Option

In February 2007, the FASB issued FASB Statement No. 159 (SFAS No. 159), Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115. This standard permits an entity to choose to measure many financial instruments and certain other items at fair value. Alabama Power plans to adopt SFAS No. 159 on January 1, 2008 and is currently assessing its impact to the extent the fair value option is elected.

FINANCIAL CONDITION AND LIQUIDITY

Overview

Alabama Power s financial condition and liquidity position remained stable at September 30, 2007. Net cash provided from operating activities totaled $898.4 million for the first nine months of 2007, compared to $693.3 million for the corresponding period in 2006. The $205.1 million increase in cash provided from operating activities in the first nine months of 2007 is primarily due to the increase in net income as previously discussed, lower cash outflow for accounts payable, and an increase in the accrued tax liability. Net cash used for investing activities totaled $920.4 million primarily due to gross property additions to utility plant of $822.8 million in the first nine months of 2007. These additions were primarily related to construction of transmission and distribution facilities, replacement of steam equipment, purchases of nuclear fuel, and installation of

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

equipment to comply with environmental standards. Net cash provided from financing activities totaled $314.2 million for the first nine months of 2007, compared to $105.7 million for the corresponding period in 2006. The increase was primarily the result of a decrease in cash outflow for the repayment of outstanding notes payable.

Capital Requirements and Contractual Obligations

See MANAGEMENT S DISCUSSION AND ANALYSIS - FINANCIAL CONDITION AND LIQUIDITY Capital Requirements and Contractual Obligations of Alabama Power in Item 7 of the Form 10-K for a description of Alabama Power s capital requirements for its construction program, scheduled maturities of long-term debt, as well as the related interest, preferred and preference stock dividends, lease obligations, purchase commitments, and trust funding requirements. Approximately $978 million will be required through September 30, 2008 for maturities of long-term debt.

In October 2007, Alabama Power s Board of Directors approved a new capital budget for 2008 and 2009. The construction program budget for Alabama Power is $1.57 billion for 2008 and $1.58 billion for 2009. Through 2009, Alabama Power estimates spending $1.26 billion on environmental related additions, $354 million on Plant Farley (including $272 million for nuclear fuel), $752 million on distribution facilities and $281 million on transmission facilities. The Southern Company s system financial plan, including its capital budget, is expected to be reviewed by the Southern Company Board of Directors in early 2008. See Note 7 to the financial statements of Alabama Power under Construction Program in Item 8 of the Form 10-K for additional details.

Sources of Capital

Alabama Power plans to obtain the funds required for construction and other purposes from sources similar to those utilized in the past. Recently, Alabama Power has primarily utilized funds from operating cash flows, short-term debt, external security offerings, and equity contributions from Southern Company. However, the amount, type, and timing of any future financings, if needed, will depend upon regulatory approval, prevailing market conditions, and other factors. See MANAGEMENT S DISCUSSION AND ANALYSIS FINANCIAL CONDITION AND LIQUIDITY Sources of Capital of Alabama Power in Item 7 of the Form 10-K for additional information.

Alabama Power s current liabilities frequently exceed current assets because of the continued use of short-term debt as a funding source to meet scheduled maturities of long-term debt as well as cash needs which can fluctuate significantly due to the seasonality of the business. To meet short-term cash needs and contingencies, Alabama Power had at September 30, 2007 approximately $308 million of cash and cash equivalents, $51.5 million of restricted cash related to the sale of pollution control bonds which may be used only for future project costs, unused committed lines of credit of approximately $978 million (including $563 million of such lines which are dedicated to funding purchase obligations related to variable rate pollution control bonds), and an extendible commercial note program. Of the unused credit facilities, $378 million will expire at various times in 2008 (of which $298 million allow for one-year term loans). The remaining $600 million credit facility expires in 2012. Alabama Power expects to renew its credit facilities, as needed, prior to expiration. See Note 6 to the financial statements of Alabama Power under Bank Credit Arrangements in Item 8 of the Form 10-K for additional information. Alabama Power may also meet short-term cash needs through a Southern Company subsidiary organized to issue and sell commercial paper and extendible commercial notes at the request and for the benefit of Alabama Power and other Southern Company subsidiaries. Alabama Power has regulatory authority for up to $1.4 billion of short-term borrowings. At September 30, 2007, Alabama Power had no commercial paper or extendible commercial notes outstanding. Management believes that the need for working capital can be adequately met by issuing commercial paper or utilizing lines of credit without maintaining large cash balances.

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Credit Rating Risk

Alabama Power does not have any credit arrangements that would require material changes in payment schedules or terminations as a result of a credit rating downgrade. However, Alabama Power, along with all members of the Power Pool, is party to certain agreements that could require collateral and/or accelerated payment in the event of a credit rating change to below investment grade for it and/or Georgia Power. These agreements are primarily for natural gas and power price risk management activities. At September 30, 2007, Alabama Power s total exposure to these types of agreements was $26.7 million.

Market Price Risk

Alabama Power s market risk exposures relative to interest rate changes have not changed materially compared with the December 31, 2006 reporting period. In addition, Alabama Power is not aware of any facts or circumstances that would significantly affect such exposures in the near term.

Due to cost-based rate regulation, Alabama Power has limited exposure to market volatility in interest rates, commodity fuel prices, and prices of electricity. To mitigate residual risks relative to movements in electricity prices, Alabama Power enters into physical fixed-price contracts for the purchase and sale of electricity through the wholesale electricity market. Alabama Power has also implemented a retail fuel hedging program at the instruction of the Alabama PSC.

The fair value of derivative energy contracts at September 30, 2007 was as follows:

	Third Quarter 2007 Changes	**Year-to-Date 2007 Changes**
	Fair Value *(in thousands)*	
Contracts beginning of period	$ (12,670)	$ (32,628)
Contracts realized or settled	10,510	25,245
New contracts at inception		
Changes in valuation techniques		
Current period changes (a)	(5,795)	(572)
Contracts at September 30, 2007	$ (7,955)	$ (7,955)

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

	Source of September 30, 2007 Valuation Prices		
	Total Fair Value	Maturity	
		Year 1	1-3 Years
		(in thousands)	
Actively quoted	$ (7,956)	$ (8,921)	$ 965
External sources	1	1	
Models and other methods			

Contracts at September 30, 2007	$ (7,955)	$ (8,920)	$ 965

ALABAMA POWER COMPANY
MANAGEMENT S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Unrealized gains and losses from mark-to-market adjustments on derivative contracts related to Alabama Power s fuel hedging programs are recorded as regulatory assets and liabilities. Realized gains and losses from these programs are included in fuel expense and are recovered through Alabama Power s fuel cost recovery clause. Certain other energy related derivatives, designated as hedges, are deferred in other comprehensive income. Gains and losses on derivative contracts that are not designated as hedges are recognized in the statements of income as incurred.

At September 30, 2007, the fair value gain/(loss) of derivative energy contracts was reflected in the financial statements as follows:

	Amounts *(in thousands)*
Regulatory assets, net	$ (7,956)
Accumulated other comprehensive income	
Net income	1
Total fair value	$ (7,955)

Unrealized pre-tax gains and losses on energy contracts recognized in income were not material for any period presented. For additional information, see MANAGEMENT S DISCUSSION AND ANALYSIS - FINANCIAL CONDITION AND LIQUIDITY - Market Price Risk of Alabama Power in Item 7 and Notes 1 and 6 to the financial statements of Alabama Power under Financial Instruments in Item 8 of the Form 10-K and Note (F) to the Condensed Financial Statements herein.

Financing Activities

Alabama Power issued $200 million of senior notes in the first quarter of 2007. The proceeds were used to repay a portion of Alabama Power s outstanding short-term indebtedness and for other general corporate purposes, including Alabama Power s continuing construction activities. Also in the first quarter of 2007, Alabama Power issued 1,750,000 shares of common stock to Southern Company at $40.00 a share ($70 million aggregate purchase price). The proceeds from the sale were used by Alabama Power for general corporate purposes.

In the second quarter 2007, Alabama Power paid at maturity $168.5 million in aggregate principal amount of Series W Floating Rate Extendible Senior Notes. In addition, Alabama Power issued $250 million of senior notes. The proceeds were used to repay a portion of Alabama Power s outstanding short-term indebtedness and for other general corporate purposes, including Alabama Power s continuing construction activities. Also in the second quarter of 2007, Alabama Power issued 1,750,000 shares of common stock to Southern Company at