GULF POWER COMPANY

2008 Annual Report

GULF POWER
A SOUTHERN COMPANY

CONTENTS
Gulf Power Company 2008 Annual Report

1	SUMMARY
2	LETTER TO INVESTORS
3	MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
4	REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
5	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
27	FINANCIAL STATEMENTS
33	NOTES TO FINANCIAL STATEMENTS
59	SELECTED FINANCIAL AND OPERATING DATA
61	DIRECTORS AND OFFICERS
62	CORPORATE INFORMATION

SUMMARY

	2008	2007	Percent Change
Financial Highlights *(in thousands)*:			
Operating revenues	**1,387,203**	**$1,259,808**	10.1
Operating expenses	**1,194,514**	**$1,083,892**	10.2
Net income after dividends on preference stock	**98,345**	**$84,118**	16.9
Gross property additions	**390,744**	**$239,337**	63.3
Total assets	**2,879,025**	**$2,498,987**	15.2
Operating Data:			
Kilowatt-hour sales *(in thousands)*:			
Retail	**11,543,399**	**11,520,888**	0.2
Sales for resale - non–affiliates	**1,816,839**	**2,227,026**	(18.4)
Sales for resale – affiliates	**1,871,158**	**2,884,440**	(35.1)
Total	**15,231,396**	**16,632,354**	(8.4)
Customers served at year-end	**427,929**	**427,663**	0.1
Peak-hour demand, net *(in megawatts)*	**2,533**	**2,626**	(3.5)
Capitalization Ratios *(percent)*:			
Common stock equity	**46.5**	**46.6**	
Preference stock	**5.5**	**6.2**	
Long-term debt (excluding amounts due within one year)	**48.0**	**47.2**	
Return on Average Common Equity *(percent)*	**12.66**	**12.32**	

LETTER TO INVESTORS
Gulf Power Company 2008 Annual Report

Our commitment to the future

Today, more than ever, it's important that you have a plan for the future. We understand that our plan for the future has a great impact on yours.

We are committed to an energy future that is affordable, reliable, and environmentally responsible. In concert with our customers, we have developed a 3-step plan that includes fuel diversity, renewable energy, and conservation.

In 2008, we partnered with Bay County to produce renewable energy from solid waste incineration. In addition, we're making preliminary plans to convert our Scholz coal-fired power plant near Marianna to biomass. Looking toward the future, we're evaluating the feasibility of solar, wind, and nuclear power — and testing ways to make coal-fired generation cleaner.

Gulf Power expects to continue to keep electricity affordable and reliable by exploring viable fuel sources as we seek to diversify our fuel mix. Fuel diversity helps us avoid fuel shortages and keeps prices down. Nuclear power, natural gas, and clean coal are all important options to maintain reliable generation for the future. New technologies will be a key component to ensuring a clean energy future.

EarthCents, our new energy-efficiency initiative, debuted in 2008. EarthCents programs help our customers save money and energy, and can help Gulf Power delay the need to build new power plants. Over the last 20 years, conservation efforts have saved enough energy to power 100,000 homes and, despite significant growth during that time, Gulf Power has reduced emissions by 70 percent. We continue to research and develop new technologies to protect the environment.

Gulf Power's financial performance in 2008 is a testament to our commitment. Even though kilowatt-hour sales were down 8.4 percent from 2007, net income after dividends on preference stock was the highest ever at $98 million — up 16.9 percent. Our return on average common equity was 12.66 percent and even with a slumping economy we added 266 customers for a total of 427,929 customers in Northwest Florida.

Moving forward, our commitment to you is to light the way with a balanced approach to meet the challenges in our energy future.

Susan N. Story

Susan N. Story,
President and Chief Executive Officer
June 5, 2009

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Gulf Power Company 2008 Annual Report

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

Under management's supervision, an evaluation of the design and effectiveness of the Company's internal control over financial reporting was conducted based on the framework in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2008.

This Annual Report does not include an attestation report of the Company's independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's independent registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this Annual Report.

Susan N. Story
President and Chief Executive Officer

Philip C. Raymond
Vice President and Chief Financial Officer

February 25, 2009

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Gulf Power Company

We have audited the accompanying balance sheets and statements of capitalization of Gulf Power Company (the “Company”) (a wholly owned subsidiary of Southern Company) as of December 31, 2008 and 2007, and the related statements of income, comprehensive income, common stockholder’s equity, and cash flows for each of the three years in the period ended December 31, 2008. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements (pages 27 to 57) present fairly, in all material respects, the financial position of Gulf Power Company at December 31, 2008 and 2007, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2008, in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

Atlanta, Georgia
February 25, 2009

OVERVIEW

Business Activities

Gulf Power Company (the Company) operates as a vertically integrated utility providing electricity to retail customers within its traditional service area located in northwest Florida and to wholesale customers in the Southeast.

Many factors affect the opportunities, challenges, and risks of the Company's business of selling electricity. These factors include the ability to maintain a constructive regulatory environment, to maintain energy sales in the midst of the current economic downturn, and to effectively manage and secure timely recovery of rising costs. These costs include those related to projected long-term demand growth, increasingly stringent environmental standards, fuel prices, and storm restoration costs. Appropriately balancing the need to recover these increasing costs with customer prices will continue to challenge the Company for the foreseeable future.

In July 2006, the Florida Public Service Commission (PSC) extended the storm-recovery surcharge currently being collected by the Company until June 2009. See Notes 1 and 3 to the financial statements under "Property Damage Reserve" and "Retail Regulatory Matters – Storm Damage Cost Recovery," respectively, for additional information.

Key Performance Indicators

In striving to maximize shareholder value while providing cost-effective energy to over 425,000 customers, the Company continues to focus on several key indicators. These indicators include customer satisfaction, plant availability, system reliability, and net income after dividends on preference stock. The Company's financial success is directly tied to the satisfaction of its customers. Key elements of ensuring customer satisfaction include outstanding service, high reliability, and competitive prices. Management uses customer satisfaction surveys and reliability indicators to evaluate the Company's results.

Peak season equivalent forced outage rate (Peak Season EFOR) is an indicator of plant availability and efficient generation fleet operations during the months when generation needs are greatest. The rate is calculated by dividing the number of hours of forced outages by total generation hours. The 2008 Peak Season EFOR of 2.47% was better than the target. Transmission and distribution system reliability performance is measured by the frequency and duration of outages. Performance targets for reliability are set internally based on historical performance, expected weather conditions, and expected capital expenditures. The performance for 2008 was at target for these reliability measures. The performance for net income after dividends on preference stock in 2008 was below target. Net income after dividends on preference stock is the primary component of the Company's contribution to Southern Company's earnings per share goal.

The Company's 2008 results compared with its targets for some of these key indicators are reflected in the following chart:

Key Performance Indicator	2008 Target Performance	2008 Actual Performance
Customer Satisfaction	**Top quartile in customer surveys**	**Top quartile**
Peak Season EFOR	**3.00% or less**	**2.47%**
Net Income	**$102 million**	**$98 million**

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

Earnings

The Company's 2008 net income after dividends on preference stock was $98.3 million, an increase of $14.2 million from the previous year. In 2007, earnings were $84.1 million, an increase of $8.1 million from the previous year. In 2006, earnings were $76.0 million, an increase of $0.8 million from the previous year. The increase in earnings in 2008 was due primarily to higher wholesale revenues from non-affiliates, increased allowance for equity funds used during construction, and a gain on the sale of assets.

The increase in earnings in 2007 was due primarily to increases in retail revenues, earnings on additional investments in environmental controls through the environment cost recovery provision, and related allowance for equity funds used during construction, partially offset by non-fuel operating expenses. The increase in earnings in 2006 was due primarily to higher operating revenues partially offset by higher operating expenses, higher financing costs, and increases in depreciation expense. See FUTURE EARNINGS POTENTIAL – "PSC Matters – Storm Damage Cost Recovery" herein.

RESULTS OF OPERATIONS

A condensed statement of income follows:

	Amount	Increase (Decrease) from Prior Year		
	2008	**2008**	2007	2006
		(in millions)		
Operating revenues	**$ 1,387.2**	**$ 127.4**	$ 55.9	$ 120.3
Fuel	**635.6**	**62.2**	38.5	119.1
Purchased power	**109.4**	**37.9**	(2.3)	(24.6)
Other operations and maintenance	**277.5**	**7.1**	10.9	9.8
Depreciation and amortization	**84.8**	**(0.8)**	(3.6)	4.2
Taxes other than income taxes	**87.2**	**4.2**	3.2	3.4
Total operating expenses	**1,194.5**	**110.6**	46.7	111.9
Operating income	**192.7**	**16.8**	9.2	8.4
Total other income and (expense)	**(34.1)**	**6.7**	1.3	(4.8)
Income taxes	**54.1**	**7.0**	1.8	0.3
Net Income	**104.5**	**16.5**	8.7	3.3
Dividends on Preference Stock	**6.2**	**2.3**	0.6	2.5
Net Income after Dividends on Preference Stock	**$ 98.3**	**$ 14.2**	$ 8.1	$ 0.8

Operating Revenues

Operating revenues increased in 2008 when compared to 2007 and 2006. The following table summarizes the changes in operating revenues for the past three years:

	Amount		
	2008	2007	2006
		(in millions)	
Retail – prior year	**$ 1,006.3**	$ 952.0	$ 864.9
Estimated change in –			
Rates and pricing	**6.3**	2.5	14.2
Sales growth	**(4.6)**	5.8	2.5
Weather	**3.9**	1.2	2.4
Fuel and other cost recovery	**108.9**	44.8	68.0
Retail – current year	**1,120.8**	1,006.3	952.0
Wholesale revenues –			
Non-affiliates	**97.1**	83.5	87.2
Affiliates	**107.0**	113.2	118.1
Total wholesale revenues	**204.1**	196.7	205.3
Other operating revenues	**62.3**	56.8	46.6
Total operating revenues	**$ 1,387.2**	$ 1,259.8	$ 1,203.9
Percent change	**10.1%**	4.6%	11.1%

Retail revenues increased $114.4 million, or 11.4%, in 2008, $54.3 million, or 5.7%, in 2007, and $87.2 million, or 10.1%, in 2006. The significant factors driving these changes are shown in the table above.

Revenues associated with changes in rates and pricing include cost recovery provisions for energy conservation costs and environmental compliance costs. Annually, the Company petitions the Florida PSC for recovery of projected costs, including any true-up amount from prior periods, and approved rates are implemented each January. The recovery provisions include related expenses and a return on average net investment. See Note 3 to the financial statements under "Retail Regulatory Matters – Environmental Cost Recovery" for additional information.

Fuel and other cost recovery provisions include fuel expenses, the energy component of purchased power costs, and purchased power capacity costs. Annually, the Company petitions the Florida PSC for recovery of projected fuel and purchased power costs, including any true-up amount from prior periods, and approved rates are implemented each January. Cost recovery provisions also include revenues related to the recovery of storm damage restoration costs. The recovery provisions generally equal the related expenses and have no material effect on net income. See Note 1 to the financial statements under "Revenues" and "Property Damage Reserve" and Note 3 to the financial statements under "Retail Regulatory Matters – Storm Damage Cost Recovery" and "Retail Regulatory Matters – Fuel Cost Recovery" for additional information.

Total wholesale revenues were $204.1 million in 2008, an increase of $7.4 million, or 3.7%, compared to 2007, primarily due to higher capacity revenues associated with new and existing territorial wholesale contracts with non-affiliated companies. Total wholesale revenues were $196.7 million in 2007, a decrease of $8.5 million, or 4.2%, compared to 2006, primarily due to decreased energy sales to affiliates at a lower cost per kilowatt-hour (KWH) supplied by lower-cost generating resources. Total wholesale revenues were $205.2 million in 2006, an increase of $29.5 million, or 16.8%, compared to 2005, primarily due to increased energy sales to affiliates to serve their territorial energy requirements.

Wholesale revenues from sales to non-affiliates will vary depending on the market cost of available energy compared to the cost of the Company and Southern Company system-owned generation, demand for energy with the Southern Company service territory, and availability of Southern Company system generation.

Wholesale revenues from sales to non-affiliates include unit power sales under long-term contracts to other Florida utilities. Wholesale revenues from contracts have both capacity and energy components. Capacity revenues reflect the recovery of fixed costs and a return on investment. Energy is generally sold at variable cost. The capacity and energy components under these unit power sales contracts were as follows:

	2008	2007	2006
		(in thousands)	
Unit power sales –			
Capacity	**$ 22,028**	$ 18,073	$ 21,477
Energy	**33,767**	36,245	34,597
Total	**55,795**	54,318	56,074
Other power sales –			
Capacity and other	**10,890**	2,397	2,436
Energy	**30,380**	26,799	28,632
Total	**41,270**	29,196	31,068
Total non-affiliated	**$ 97,065**	$ 83,514	$ 87,142

Wholesale revenues from sales to affiliated companies within the Southern Company system will vary from year to year depending on demand and the availability and cost of generating resources at each company. These affiliated sales and purchases are made in accordance with the Intercompany Interchange Contract (IIC), as approved by the Federal Energy Regulatory Commission (FERC). These transactions do not have a significant impact on earnings, since the energy is generally sold at marginal cost and energy purchases are generally offset by revenues through the Company's fuel cost recovery clause.

Other operating revenues increased $5.6 million, or 9.9%, in 2008, primarily due to transmission and distribution network services and other energy services. The increased revenues from other energy services did not have a material impact on earnings since they were generally offset by associated expenses. Other operating revenues increased $10.2 million, or 21.8%, in 2007, primarily due to other energy services and an increase in franchise fees, which were proportional to changes in revenue. Other operating revenues increased $3.6 million, or 8.3%, in 2006, primarily due to an increase in franchise fees, which were proportional to changes in revenue.

Energy Sales

Changes in revenues are influenced heavily by the change in the volume of energy sold from year to year. KWH sales for 2008 and the percent change by year were as follows:

	KWHs	Percent Change		
	2008	**2008**	2007	2006
	(in millions)			
Residential	**5,349**	**(2.3)%**	0.9%	2.0%
Commercial	**3,961**	**(0.3)**	3.3	2.9
Industrial	**2,210**	**7.9**	(4.1)	(1.1)
Other	**23**	**(5.1)**	4.2	5.1
Total retail	**11,543**	**0.2**	0.8	1.7
Wholesale				
Non-affiliates	**1,817**	**(18.4)**	7.1	(9.4)
Affiliates	**1,871**	**(35.1)**	(1.8)	48.6
Total wholesale	**3,688**	**(27.8)**	1.9	17.4
Total energy sales	**15,231**	**(8.4)**	1.1	6.0

Changes in retail energy sales are comprised of changes in electricity usage by customers, changes in weather, and changes in the number of customers.

Residential energy sales decreased 2.3% in 2008, compared to 2007, primarily due to decreased customer usage as a result of a slowing economy, partially offset by more favorable weather. Residential energy sales increased 0.9% in 2007, compared to 2006, primarily due to more favorable weather conditions and customer growth, partially offset by customer response to higher prices. Residential energy sales increased 2.0% in 2006, compared to 2005, primarily due to more favorable weather conditions and customer growth.

The change in commercial energy sales in 2008, compared to 2007, was immaterial. Commercial energy sales increased 3.3% in 2007, compared to 2006, primarily due to more favorable weather conditions and customer growth. Commercial energy sales increased 2.9% in 2006, compared to 2005, primarily due to more favorable weather conditions and customer growth.

Industrial energy sales increased 7.9% in 2008, compared to 2007, primarily due to decreased customer co-generation due to the higher cost of natural gas. Industrial energy sales decreased 4.1% in 2007, compared to 2006, primarily due to a conversion project by a major forest products manufacturer and a production process change by a major petroleum company. Industrial energy sales decreased 1.1% in 2006, compared to 2005, due to reduced demand for and production of building materials and a conversion project by a major paper manufacturer.

Wholesale energy sales to non-affiliates decreased 18.4% in 2008, increased 7.1% in 2007, and decreased 9.4% in 2006, each compared to the prior year primarily as a result of fluctuations in the fuel cost to produce energy sold to non-affiliated utilities under both long-term and short-term contracts. The degree to which oil and natural gas prices, which are the primary fuel sources for these customers, differ from the Company's fuel costs will influence these changes in sales. The fluctuations in sales have a minimal effect on earnings because the energy is generally sold at marginal cost.

Wholesale energy sales to affiliates decreased 35.1% in 2008 and decreased 1.8% in 2007, compared to prior years, primarily due to the availability of lower cost generation resources at affiliated companies. Wholesale energy sales to affiliates increased 48.6% in 2006 compared to 2005, primarily due to increased territorial energy requirements of affiliates.

Fuel and Purchased Power Expenses

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

Details of the Company's electricity generated and purchased were as follows:

	2008	2007	2006
Total generation *(millions of KWHs)*	**14,762**	16,657	16,349
Total purchased power *(millions of KWHs)*	**1,187**	798	876
Sources of generation *(percent)* –			
Coal	**84%**	86%	87%
Gas	**16**	14	13
Cost of fuel, generated *(cents per net KWH)* –			
Coal	**3.58**	2.86	2.68
Gas	**8.02**	6.91	7.24
Average cost of fuel, generated *(cents per net KWH)*	**4.31**	3.44	3.27
Average cost of purchased power *(cents per net KWH)*	**9.21**	8.96	8.43

Total fuel and purchased power expenses were $745.0 million in 2008, an increase of $100.1 million, or 15.5%, above the prior year costs. The net increase in fuel and purchased power expenses was due to a $130.5 million increase in the average cost of fuel and purchased power as well as a $34.9 million increase in KWHs purchased, offset by a $65.3 million decrease in KWHs generated. Total fuel and purchased power expenses were $644.9 million in 2007, an increase of $36.2 million, or 5.9%, above the prior year costs. The net increase in fuel and purchased power expenses was due to a $32.6 million increase in the average cost of fuel and purchased power as well as a $10.1 million increase in KWHs generated, offset by a $6.5 million decrease in KWHs purchased. Total fuel and purchased power expenses were $608.7 million in 2006, an increase of $94.5 million, or 18.4%, above the prior year costs. The net increase in fuel and purchased power expenses was due to an $82.7 million increase in the average cost of fuel and purchased power as well as a $36.7 million increase in KWHs generated, offset by a $24.9 million decrease in KWHs purchased.

Fuel expense was $635.6 million in 2008, an increase of $62.2 million, or 10.9%, above the prior year costs. This increase was the result of a $127.5 million increase in the average cost of fuel, offset by a $65.3 million decrease related to total KWHs generated. Fuel expense was $573.4 million in 2007, an increase of $38.5 million, or 7.2%, above the prior year costs. This increase was the result of a $28.4 million increase in the average cost of fuel and a $10.1 million increase related to total KWHs generated. Fuel expense was $534.9 million in 2006, an increase of $119.1 million, or 28.7%, above the prior year costs. This increase was the result of an $82.4 million increase in the average cost of fuel and a $36.7 million increase related to total KWHs generated.

Purchased power expense was $109.4 million in 2008, an increase of $37.9 million, or 53.0%, above the prior year costs. This increase was the result of a $34.9 million increase in total KWHs purchased and a $3.0 million increase resulting from the higher average cost per net KWH. Purchased power expense was $71.5 million in 2007, a decrease of $2.3 million, or 3.1%, below the prior year costs. This decrease was the result of a $6.5 million decrease in total KWHs purchased, offset by a $4.2 million increase resulting from the higher average cost per net KWH. Purchased power expense was $73.8 million in 2006, a decrease of $24.6 million, or 25.0%, below the prior year costs. This decrease was the result of a $24.9 million decrease in total KWHs purchased, offset by a $0.3 million increase resulting from the higher average cost per net KWH.

Over the last several years, coal prices have been influenced by a worldwide increase in demand from developing countries, as well as increases in mining and fuel transportation costs. In the first half of 2008, coal prices reached unprecedented high levels primarily due to increased demand following more moderate pricing in 2006 and 2007. Despite these fluctuations, fuel inventories have been adequate and fuel supply markets have been sufficient to meet expected fuel requirements. Demand for natural gas in the United States also increased in 2007 and the first half of 2008. However, natural gas supplies increased in the last half of 2008 as a result of increased production and higher storage levels due in part to weak industrial demand. Both coal and natural gas prices moderated in the second half of 2008 as the result of a recessionary economy.

Fuel expenses generally do not affect net income, since they are offset by fuel revenues under the Company's fuel cost recovery provisions. See FUTURE EARNINGS POTENTIAL – "PSC Matters – Fuel Cost Recovery" herein for additional information.

Other Operations and Maintenance Expenses

In 2008, other operations and maintenance expenses increased $7.1 million, or 2.6%, compared to the prior year primarily due to an $8.2 million increase in scheduled and unscheduled maintenance at generation facilities. In 2007, other operations and maintenance expenses increased $10.9 million, or 4.2%, compared to the prior year primarily due to a $5.0 million increase in other energy services and a $4.3 million increase in severance costs associated with a reorganization. The increased expenses from other energy services did not have a material impact on earnings since they were generally offset by associated revenue. In 2007, the Company offered both voluntary and involuntary severance to a number of employees in connection with a reorganization of certain functions. In 2006, other operations and maintenance expenses increased $9.8 million, or 3.9%, compared to the prior year primarily due to a $4.2 million increase in the recovery of incurred costs for storm damage activity as approved by the Florida PSC, a $1.9 million increase in employee benefit expenses, and a $1.1 million increase in property insurance costs. See FUTURE EARNINGS POTENTIAL – "PSC Matters – Storm Damage Cost Recovery" herein and Notes 1 and 3 to the financial statements under "Property Damage Reserve" and "Retail Regulatory Matters – Storm Damage Cost Recovery," respectively, for additional information.

Depreciation and Amortization

Depreciation and amortization expense decreased $0.8 million, or 0.9%, in 2008 compared to the prior year primarily as a result of a $3.8 million gain on the sale of a building. The decrease was partially offset by an increase of $3.0 million in depreciation due to net additions to generation and distribution facilities. Depreciation and amortization expense decreased $3.6 million, or 4.0%, in 2007 compared to the prior year primarily due to new depreciation rates implemented in January 2007. Depreciation and amortization expense increased $4.2 million, or 4.9%, in 2006 compared to the prior year primarily due to the construction of environmental control projects at Plants Crist and Daniel that were placed in service in 2005.

Taxes Other Than Income Taxes

Taxes other than income taxes increased $4.2 million, or 5.1%, in 2008, compared to the prior year primarily due to a $1.9 million decrease in 2007 related to the resolution of a dispute regarding property taxes in Monroe County, Georgia and a $1.9 million increase in franchise and gross receipt taxes, which were directly related to the increase in retail revenues. Taxes other than income taxes increased $3.2 million, or 4.0%, in 2007, and $3.4 million, or 4.5%, in 2006 primarily due to increases in franchise and gross receipts taxes, which were directly related to the increase in retail revenues.

Allowance for Equity Funds Used During Construction

Allowance for equity funds used during construction (AFUDC) increased $7.6 million, or 319.9%, in 2008 compared to the prior year primarily due to construction of environmental control projects at Plant Crist and Plant Scherer. AFUDC increased $2.0 million, or 554.0%, in 2007 compared to the prior year primarily due to construction of an environmental control project at Plant Crist. AFUDC decreased $0.8 million, or 68.9%, in 2006 compared to the prior year primarily due to the completion of an environmental control project at Plant Crist Unit 7 during 2005. See FUTURE EARNINGS POTENTIAL – "Environmental Matters – Environmental Statutes and Regulations" herein and Note 1 to the financial statements under "Allowance for Funds Used During Construction (AFUDC)" for additional information.

Interest Income

Interest income decreased $2.2 million, or 41%, in 2008, primarily as a result of lower variable interest rates charged against the under recovered fuel balance and a decrease in the property damage reserve balance. Interest income increased $0.1 million, or 2.3%, in 2007, and increased $1.4 million, or 37.4%, in 2006 compared to the prior year primarily due to interest received related to the recovery of financing costs associated with the fuel clause and incurred costs for storm damage activity as approved by the Florida PSC. See FUTURE EARNINGS POTENTIAL – "PSC Matters – Storm Damage Cost Recovery" herein and Note 3 to the financial statements under "Retail Regulatory Matters – Storm Damage Cost Recovery" for additional information.

Interest Expense, Net of Amounts Capitalized

Interest expense, net of amounts capitalized decreased $1.6 million, or 3.5%, in 2008 compared to the prior year as the result of an increase in capitalization of AFUDC related to the construction of environmental control projects and the redemption of $41.2 million of long-term debt payable to an affiliated trust in 2007. These decreases were offset by the issuance of a $110 million term loan agreement in 2008. Interest expense, net of amounts capitalized increased $0.5 million, or 1.2%, in 2007 compared to the prior year and was not material. Interest expense, net of amounts capitalized increased $3.8 million, or 9.5%, in 2006 compared to the prior year as the result of higher interest rates on variable rate pollution control bonds, increased levels of short-term borrowings at higher interest rates, and the issuance of $60 million in senior notes in August 2005. These increases were partially offset by the maturity of a $100 million bank note in October 2005 and the extinguishment of $30 million aggregate principal amount of first mortgage bonds in 2005.

Other Income (Expense), Net

Other expense, net increased $0.2 million, or 4.9%, in 2008, and increased $0.3 million, or 9.2%, in 2007, compared to prior years and was not material. Other expense, net increased $1.5 million, or 79.1%, in 2006 compared to the prior year primarily as a result of changes in charitable contributions.

Income Taxes

Income taxes increased $7.0 million, or 14.9%, in 2008, compared to the prior year primarily due to higher earnings before income taxes and a decrease in the federal production activities deduction, partially offset by the tax benefit associated with an increase in AFUDC, which is non-taxable. Income taxes increased $1.8 million, or 4.0%, in 2007, and increased $0.3 million, or 0.7%, in 2006 compared to the prior years primarily as a result of higher earnings before income taxes. See Note 5 to the financial statements under "Effective Tax Rate" for additional information.

Effects of Inflation

The Company is subject to rate regulation based on the recovery of historical costs. When historical costs are included, or when inflation exceeds projected costs used in rate regulation or market-based prices, the effects of inflation can create an economic loss since the recovery of costs could be in dollars that have less purchasing power. In addition, the income tax laws are based on historical costs. While the inflation rate has been relatively low in recent years, it continues to have an adverse effect on the Company because of the large investment in utility plant with long economic lives. Conventional accounting for historical cost does not recognize this economic loss or the partially offsetting gain that arises through financing facilities with fixed-money obligations such as long-term debt, preference stock, and preferred securities. Any recognition of inflation by regulatory authorities is reflected in the rate of return allowed in the Company's approved electric rates.

FUTURE EARNINGS POTENTIAL

General

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

The results of operations for the past three years are not necessarily indicative of future earnings potential. The level of the Company's future earnings depends on numerous factors that affect the opportunities, challenges, and risks of the Company's business of selling electricity. These factors include the Company's ability to maintain a constructive 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 maintaining energy sales during the current economic downturn, 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 or decline in the Company's service area. Recent recessionary conditions have negatively impacted sales growth. The timing and extent of the economic recovery will impact future earnings.

Environmental Matters

Compliance costs related to the Clean Air Act and other environmental statutes and regulations could affect earnings if such costs cannot continue to be fully recovered in rates on a timely basis. Environmental compliance spending over the next several years may exceed amounts estimated. Some of the factors driving the potential for such an increase are higher commodity costs, market demand for labor, and scope additions and clarifications. The timing, specific requirements, and estimated costs could also change as environmental statutes and regulations are adopted or modified. See Note 3 to the financial statements under "Environmental Matters" for additional information.

New Source Review Actions

In November 1999, the Environmental Protection Agency (EPA) brought a civil action in the U.S. District Court for the Northern District of Georgia against certain Southern Company subsidiaries, including Alabama Power Company (Alabama Power) and Georgia Power Company (Georgia Power), alleging that these subsidiaries had violated the New Source Review (NSR) provisions of the Clean Air Act and related state laws at certain coal-fired generating facilities. The EPA concurrently issued notices of violation relating to the Company's Plant Crist and a unit at Georgia Power's Plant Scherer that is partially owned by the Company. In early 2000, the EPA filed a motion to amend its complaint to add the allegations in the notice of violation and to add the Company as a defendant. However, in March 2001, the court denied the motion based on lack of jurisdiction, and the EPA has not refiled. After Alabama Power was dismissed from the original action for jurisdictional reasons, the EPA filed a separate action in January 2001 against Alabama Power in the U.S. District Court for the Northern District of Alabama. In these lawsuits, the EPA alleged that NSR violations occurred at eight coal-fired generating facilities operated by Alabama Power and Georgia Power. The civil actions request penalties and injunctive relief, including an order requiring installation of the best available control technology at the affected units. The action against Georgia Power has been administratively closed since the spring of 2001, and the case has not been reopened.

In June 2006, the U.S. District Court for the Northern District of Alabama entered a consent decree between Alabama Power and the EPA, resolving a portion of the Alabama Power lawsuit relating to the alleged NSR violations at Plant Miller. The consent decree required Alabama Power to pay $100,000 to resolve the government's claim for a civil penalty and to donate $4.9 million of sulfur dioxide emission allowances to a nonprofit charitable organization. It also formalized specific emissions reductions to be accomplished by Alabama Power, consistent with other Clean Air Act programs that require emissions reductions. In August 2006, the district court in Alabama granted Alabama Power's motion for summary judgment and entered final judgment in favor of Alabama Power on the EPA's claims related to all of the remaining plants: Plants Barry, Gaston, Gorgas, and Greene County.

The plaintiffs appealed the district court's decision to the U.S. Court of Appeals for the Eleventh Circuit, where the appeal was stayed, pending the U.S. Supreme Court's decision in a similar case against Duke Energy. The Supreme Court issued its decision in the Duke Energy case in April 2007, and in December 2007, the Eleventh Circuit vacated the district court's decision in the Alabama Power case and remanded the case back to the district court for consideration of the legal issues in light of the Supreme Court's decision in the Duke Energy case. On July 24, 2008, the U.S. District Court for the Northern District of Alabama granted partial summary judgment in favor of Alabama Power regarding the proper legal test for determining whether projects are routine maintenance, repair, and replacement and therefore are excluded from NSR permitting. The decision did not resolve the case and the ultimate outcome of these matters cannot be determined at this time.

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

Carbon Dioxide Litigation

New York Case

In July 2004, three environmental groups and attorneys general from eight states, each outside of Southern Company's service territory, and the corporation counsel for New York City filed complaints in the U.S. District Court for the Southern District of New York against Southern Company and four other electric power companies. The complaints allege that the companies' emissions of carbon dioxide, a greenhouse gas, contribute to global warming, which the plaintiffs assert is a public nuisance. Under common law public and private nuisance theories, the plaintiffs seek a judicial order (1) holding each defendant jointly and severally liable for creating, contributing to, and/or maintaining global warming and (2) requiring each of the defendants to cap its emissions of carbon dioxide and then reduce those emissions by a specified percentage each year for at least a decade. The plaintiffs have not, however, requested that damages be awarded in connection with their claims. Southern Company believes these claims are without merit and notes that the complaint cites no statutory or regulatory basis for the claims. In September 2005, the U.S. District Court for the Southern District of New York granted Southern Company's and the other defendants' motions to dismiss these cases. The plaintiffs filed an appeal to the U.S. Court of Appeals for the Second Circuit in October 2005, but no decision has been issued. The ultimate outcome of these matters cannot be determined at this time.

Kivalina Case

On February 26, 2008, the Native Village of Kivalina and the City of Kivalina filed a suit in the U.S. District Court for the Northern District of California against several electric utilities (including Southern Company), several oil companies, and a coal company. The plaintiffs are the governing bodies of an Inupiat village in Alaska. The plaintiffs contend that the village is being destroyed by erosion allegedly caused by global warming that the plaintiffs attribute to emissions of greenhouse gases by the defendants. The plaintiffs assert claims for public and private nuisance and contend that the defendants have acted in concert and are therefore jointly and severally liable for the plaintiffs' damages. The suit seeks damages for lost property values and for the cost of relocating the village, which is alleged to be $95 million to $400 million. On June 30, 2008, all defendants filed motions to dismiss this case. Southern Company believes that these claims are without merit and notes that the complaint cites no statutory or regulatory basis for the claims. The ultimate outcome of this matter cannot be determined at this time.

Environmental Statutes and Regulations

General

The Company's operations are subject to extensive regulation by state and federal environmental agencies under a variety of statutes and regulations governing environmental media, including air, water, and land resources. Applicable statutes include the Clean Air Act; the Clean Water Act; the Comprehensive Environmental Response, Compensation, and Liability Act; the Resource Conservation and Recovery Act; the Toxic Substances Control Act; the Emergency Planning & Community Right-to-Know Act; the Endangered Species Act; and related federal and state regulations. Compliance with these environmental requirements involves significant capital and operating costs, a major portion of which is expected to be recovered through existing ratemaking provisions. Through 2008, the Company had invested approximately $718 million in capital projects to comply with these requirements, with annual totals of $296 million, $124 million, and $46 million for 2008, 2007, and 2006, respectively. The Company expects that capital expenditures to assure compliance with existing and new statutes and regulations will be an additional $335 million, $164 million, and $233 million for 2009, 2010, and 2011, respectively. The Company's compliance strategy can be affected by changes to existing environmental laws, statutes, and regulations, the cost, availability, and existing inventory of emission allowances, and the Company's fuel mix. Environmental costs that are known and estimable at this time are included in capital expenditures discussed under FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" herein.

The Florida Legislature has adopted legislation that allows a utility to petition the Florida PSC for recovery of prudent environmental compliance costs that are not being recovered through base rates or any other recovery mechanism. The legislation is discussed in Note 3 to the financial statements under "Retail Regulatory Matters – Environmental Cost Recovery." Substantially all of the costs for the Clean Air Act and other new environmental legislation discussed below are expected to be recovered through the environmental cost recovery clause.

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

Air Quality

Compliance with the Clean Air Act and resulting regulations has been and will continue to be a significant focus for the Company. Through 2008, the Company had spent approximately $508 million in reducing sulfur dioxide (SO_2) and nitrogen oxide (NO_x) emissions and in monitoring emissions pursuant to the Clean Air Act. Additional controls are currently being installed at several plants to further reduce air emissions, maintain compliance with existing regulations, and meet new requirements.

In 2004, the EPA designated nonattainment areas under an eight-hour ozone standard. No area within the Company's service area was designated as nonattainment under the eight-hour ozone standard. Macon, Georgia, where Plant Scherer is located, was designated as nonattainment under the eight-hour ozone standard. However, the Macon area has since been redesignated as an attainment area by the EPA, and a maintenance plan to address future exceedances of the standard have been approved. On March 12, 2008, the EPA issued a final rule establishing a more stringent eight-hour ozone standard which could result in designation of new nonattainment areas within the Company's service territory. The EPA is expected to publish those designations in 2010, and require state implementation plans for any nonattainment areas by 2013.

During 2005, the EPA's annual fine particulate matter nonattainment designations became effective for several areas within Georgia. State plans for addressing the nonattainment designations for this standard were due by April 5, 2008 but have not been finalized. These state plans could require further reductions in SO_2 and NO_x emissions from power plants including plants owned in part by the Company.

The EPA issued the final Clean Air Interstate Rule (CAIR) in March 2005. This cap-and-trade rule addresses power plant SO_2 and NO_x emissions that were found to contribute to nonattainment of the eight-hour ozone and fine particulate matter standards in downwind states. Twenty-eight eastern states, including Florida, Georgia, and Mississippi, are subject to the requirements of the rule. The rule calls for additional reductions of NO_x and/or SO_2 to be achieved in two phases, 2009/2010 and 2015. On July 11, 2008, in response to petitions brought by certain states and regulated industries challenging particular aspects of CAIR, the U.S. Court of Appeals for the District of Columbia Circuit issued a decision vacating CAIR in its entirety and remanding it to the EPA for further action consistent with its opinion. On December 23, 2008, however, the U.S. Court of Appeals for the District of Columbia Circuit altered its July decision in response to a rehearing petition and remanded CAIR to the EPA without vacatur, thereby leaving CAIR compliance requirements in place while the EPA develops a revised rule. The State of Florida has an EPA-approved plan to implement this rule. These reductions will be accomplished by the installation of additional emission controls at the Company's coal-fired facilities and/or by the purchase of emission allowances. The State of Georgia has completed plans to implement CAIR, and has approved a "multi-pollutant rule" that requires plant-specific emission controls on all but the smallest generating units in Georgia, to be installed according to a schedule set forth in the rule. The rule is designed to ensure reductions in emissions of SO_2, NO_x, and mercury in Georgia. The full impact of the court's remand and the outcome of the EPA's future rulemaking in response cannot be determined at this time.

The Clean Air Visibility Rule (CAVR) (formerly called the Regional Haze Rule) was finalized in July 2005. The goal of this rule is to restore natural visibility conditions in certain areas (primarily national parks and wilderness areas) by 2064. The rule involves (1) the application of Best Available Retrofit Technology (BART) to certain sources built between 1962 and 1977 and (2) the application of any additional emissions reductions which may be deemed necessary for each designated area to achieve reasonable progress by 2018 toward the natural conditions goal. Thereafter, for each 10-year planning period, additional emissions reductions will be required to continue to demonstrate reasonable progress in each area during that period. For power plants, the CAVR allows states to determine that the CAIR satisfies BART requirements for SO_2 and NO_x. Extensive studies were performed for each of the Company's affected units to demonstrate that additional particulate matter controls are not necessary under BART. States have completed or are currently completing implementation plans that contain strategies for BART and any other measures required to achieve the first phase of reasonable progress.

The impacts of the eight-hour ozone nonattainment designations, the fine particulate matter nonattainment designations, and the CAVR on the Company cannot be determined at this time and will depend on the resolution of any pending legal challenges and the development and implementation of rules at the state level.

The Company has developed and continually updates a comprehensive environmental compliance strategy to assess compliance obligations associated with the continuing and new environmental requirements discussed above. As part of this strategy, the

Company plans to install additional SO_2 and NO_x emission controls within the next several years to ensure continued compliance with applicable air quality requirements.

In March 2005, the EPA published the final Clean Air Mercury Rule (CAMR), a cap-and-trade program for the reduction of mercury emissions from coal-fired power plants. The final CAMR was challenged in the U.S. Court of Appeals for the District of Columbia Circuit. The petitioners alleged that the EPA was not authorized to establish a cap-and-trade program for mercury emissions and instead the EPA must establish maximum achievable control technology standards for coal-fired electric utility steam generating units. On February 8, 2008, the court ruled in favor of the petitioners and vacated the CAMR. The Company's overall environmental compliance strategy relies primarily on a combination of SO_2 and NO_x controls to reduce mercury emissions. Any significant changes in the strategy will depend on the outcome of any appeals and/or future federal and state rulemakings. Future rulemakings necessitated by the court's decision could require emission reductions more stringent than those required by the CAMR.

Water Quality

In July 2004, the EPA published its final technology-based regulations under the Clean Water Act for the purpose of reducing impingement and entrainment of fish, shellfish, and other forms of aquatic life at existing power plant cooling water intake structures. The rules require baseline biological information and, perhaps, installation of fish protection technology near some intake structures at existing power plants. In January 2007, the U.S. Court of Appeals for the Second Circuit overturned and remanded several provisions of the rule, including the use of cost-benefit analysis, to the EPA for revisions. The decision has been appealed to the U.S. Supreme Court. The full impact of these regulations will depend on subsequent legal proceedings, further rulemaking by the EPA, the results of studies and analyses performed as part of the rules' implementation, and the actual requirements established by state regulatory agencies and, therefore, cannot be determined at this time.

Environmental Remediation

The Company must comply with other environmental laws and regulations that cover the handling and disposal of waste and releases of hazardous substances. Under these various laws and regulations, the Company could incur substantial costs to clean up properties. The Company conducts studies to determine the extent of any required cleanup and has recognized in its financial statements the costs to clean up known sites. Included in this amount are costs associated with remediation of the Company's substation sites. These projects have been approved by the Florida PSC for recovery through the environmental cost recovery clause; therefore, there is no impact to the Company's net income as a result of these liabilities. The Company may be liable for some or all required cleanup costs for additional sites that may require environmental remediation. See Note 3 to the financial statements under "Environmental Matters – Environmental Remediation" for additional information.

Global Climate Issues

Federal legislative proposals that would impose mandatory requirements related to greenhouse gas emissions and renewable energy standards continue to be strongly considered in Congress, and the reduction of greenhouse gas emissions has been identified as a high priority by the current Administration. The ultimate outcome of these proposals cannot be determined at this time; however, mandatory restrictions on the Company's greenhouse gas emissions could result in significant additional compliance costs that could affect future unit retirement and replacement decisions and results of operations, cash flows, and financial condition if such costs are not recovered through regulated rates.

In April 2007, the U.S. Supreme Court ruled that the EPA has authority under the Clean Air Act to regulate greenhouse gas emissions from new motor vehicles. The EPA is currently developing its response to this decision. Regulatory decisions that will follow from this response may have implications for both new and existing stationary sources, such as power plants. The ultimate outcome of these rulemaking activities cannot be determined at this time; however, as with the current legislative proposals, mandatory restrictions on the Company's greenhouse gas emissions could result in significant additional compliance costs that could affect future unit retirement and replacement decisions and results of operations, cash flows, and financial condition if such costs are not recovered through regulated rates.

In addition, some states are considering or have undertaken actions to regulate and reduce greenhouse gas emissions. On June 25, 2008, Florida's Governor signed comprehensive energy-related legislation that includes authorization for the Florida Department of Environmental Protection to adopt rules for a cap-and-trade regulatory program to address greenhouse gas emissions from electric utilities, conditioned upon their ratification by the legislature no sooner than the 2010 legislative session. This legislation also authorizes the Florida PSC to adopt a renewable portfolio standard for public utilities, subject to legislative ratification. The impact of this and any similar legislation on the Company will depend on the future development, adoption, legislative ratification, implementation, and potential legal challenges to rules governing greenhouse gas emissions and mandates regarding the use of renewable energy, and the ultimate outcome cannot be determined at this time.

International climate change negotiations under the United Nations Framework Convention on Climate Change also continue. Current efforts focus on a potential successor to the Kyoto Protocol for the post 2012 timeframe, with a conclusion to this round of negotiations targeted for the end of 2009. The outcome and impact of the international negotiations cannot be determined at this time.

The Company continues to evaluate its future energy and emission profiles and is participating in voluntary programs to reduce greenhouse gas emissions and to help develop and advance technology to reduce emissions.

FERC Matters

Market-Based Rate Authority

The Company has authorization from the FERC to sell power to non-affiliates, including short-term opportunity sales, at market-based prices. Specific FERC approval must be obtained with respect to a market-based contract with an affiliate.

In December 2004, the FERC initiated a proceeding to assess Southern Company's generation dominance within its retail service territory. The ability to charge market-based rates in other markets is not an issue in the proceeding. Any new market-based rate sales by the Company in Southern Company's retail service territory entered into during a 15-month refund period that ended in May 2006 could be subject to refund to a cost-based rate level.

In November 2007, the presiding administrative law judge issued an initial decision regarding the methodology to be used in the generation dominance tests. The proceedings are ongoing. The ultimate outcome of this generation dominance proceeding cannot now be determined, but an adverse decision by the FERC in a final order could require the Company to charge cost-based rates for certain wholesale sales in the Southern Company retail service territory, which may be lower than negotiated market-based rates, and could also result in total refunds of up to $0.8 million, plus interest. The Company believes that there is no meritorious basis for an adverse decision in this proceeding and is vigorously defending itself in this matter.

In June 2007, the FERC issued its final rule in Order No. 697 regarding market-based rate authority. The FERC generally retained its current market-based rate standards. Responding to a number of requests for rehearing, the FERC issued Order No. 697-A on April 21, 2008 and Order No. 697-B on December 12, 2008. These orders largely affirmed the FERC's prior revision and codification of the regulations governing market-based rates for public utilities. In accordance with the orders, Southern Company submitted to the FERC an updated market power analysis on September 2, 2008 related to its continued market-based rate authority. The ultimate outcome of this matter cannot now be determined.

On October 17, 2008, Southern Company filed with the FERC a revised market-based rate (MBR) tariff and a new cost-based rate (CBR) tariff. The revised MBR tariff provides for a "must offer" energy auction whereby Southern Company, offers all of its available energy for sale in a day-ahead auction and an hour-ahead auction with reserve prices not to exceed the CBR tariff price, after considering Southern Company's native load requirements, reliability obligations, and sales commitments to third parties. All sales under the energy auction would be at market clearing prices established under the auction rules. The new CBR tariff provides for a cost-based price for wholesale sales of less than a year. On December 18, 2008, the FERC issued an order conditionally accepting the MBR tariff subject to certain revisions to the auction proposal. On January 21, 2009, Southern Company made a compliance filing that accepted all the conditions of the MBR tariff order. When this order becomes final, Southern Company will have 30 days to implement the wholesale auction. On December 31, 2008, the FERC issued an order conditionally accepting the CBR tariff subject to providing additional information concerning one aspect of the tariff. On January 30, 2009, Southern Company filed a response addressing the FERC inquiry to the CBR tariff order. Implementation of the energy auction in accordance with the MBR tariff order is expected to adequately mitigate going forward any presumption of market power that Southern Company may have in the Southern Company retail service territory. The timing of when the FERC may issue the final orders on the MBR and CBR tariffs and the ultimate outcome of these matters cannot be determined at this time.

PSC Matters

Fuel Cost Recovery

The Company petitions for fuel cost recovery rates to be approved by the Florida PSC on an annual basis. At December 31, 2008 and 2007, the under recovered balance was $96.7 million and $56.6 million, respectively, primarily due to lower non-territorial sales, increased costs for coal, and a higher percentage of natural gas fired generation. The Company continuously monitors the over or under recovered fuel cost balance in light of the inherent variability in fuel costs. If the projected fuel cost over or under recovery exceeds 10% of the projected fuel revenue applicable for the period, the Company is required to notify the Florida PSC and indicate if an adjustment to the fuel cost recovery factor is being requested.

On July 29, 2008, the Florida PSC approved a request by the Company to increase the fuel cost recovery factor effective with billings beginning September 2008. The remaining portion of the projected under recovered balance is expected to be recovered in 2009. On September 2, 2008, the Company filed its 2009 projected fuel cost recovery filing with the Florida PSC which includes the fuel factors proposed for January 2009 through December 2009. On October 13, 2008, the Company notified the Florida PSC that the updated projected fuel cost under recovery balance at year-end exceeds the 10% threshold, but no adjustment to the fuel factor was requested.

On November 6, 2008, the Florida PSC approved an increase of approximately 12.9% in the fuel factor for retail customers, effective with billings beginning January 2009. The fuel factors are intended to allow the Company to recover its projected 2009 fuel and purchased power costs as well as the 2008 under recovered amounts in 2009. Fuel cost recovery revenues, as recorded on the financial statements, are adjusted for differences in actual recoverable costs and amounts billed in current regulated rates. Accordingly, changing the billing factor has no significant effect on the Company's revenues or net income, but does impact annual cash flow. See Notes 1 and 3 to the financial statements under "Revenues" and "Retail Regulatory Matters - Fuel Cost Recovery," respectively.

Environmental Cost Recovery

In August 2007, the Florida PSC voted to approve a stipulation among the Company, the Office of Public Counsel, and the Florida Industrial Power Users Group regarding the Company's plan for complying with certain federal and state regulations addressing air quality. The Company's environmental compliance plan as filed in March 2007 contemplated implementation of specific projects identified in the plan from 2007 through 2018. The stipulation covers all elements of the current plan that are scheduled to be implemented in the 2007 through 2011 timeframe. On September 18, 2008, the Company filed an update to the plan, which was approved by the Florida PSC on November 4, 2008. The Florida PSC acknowledged that the costs associated with the Company's CAIR/CAMR/CAVR compliance plan are clearly eligible for recovery through the environmental cost recovery clause. See FINANCIAL CONDITION AND LIQUIDITY - "Capital Requirements and Contractual Obligations" herein, Note 3 to the financial statements under "Retail Regulatory Matters - Environmental Cost Recovery," and Note 7 to the financial statements under "Construction Program" for additional information.

Storm Damage Cost Recovery

Under authority granted by the Florida PSC, the Company maintains a reserve for property damage to cover the cost of uninsured damages from major storms to its transmission and distribution facilities, generation facilities, and other property. Funds collected by the Company related to the storm-recovery costs associated with previous hurricanes had been fully recovered by August 31, 2008. Funds collected by the Company through its storm-recovery surcharge are now being credited to the property reserve and will continue through June 2009 when the approved surcharge ends. As of December 31, 2008, the balance in the Company's property damage reserve totaled approximately $9.8 million, which is included in deferred liabilities in the balance sheets.

See Notes 1 and 3 to the financial statements under "Property Damage Reserve" and "Retail Regulatory Matters – Storm Damage Cost Recovery," respectively, for additional information.

Income Tax Matters

Legislation

On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009 (ARRA). Major tax incentives in the ARRA include an extension of bonus depreciation and multiple renewable energy incentives. These incentives could have a significant impact on the Company's future cash flow and net income. Additionally, the ARRA includes programs for renewable energy, transmission and smart grid enhancement, fossil energy and research, and energy efficiency and conservation. The ultimate impact cannot be determined at this time.

Internal Revenue Code Section 199 Domestic Production Deduction

The American Jobs Creation Act of 2004 created a tax deduction for a portion of income attributable to U.S. production activities as defined in the Section 199 (production activities deduction) of the Internal Revenue Code of 1986, as amended (Internal Revenue Code). The deduction is equal to a stated percentage of qualified production activities net income. 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 thereafter. The Internal Revenue Service (IRS) has not clearly defined a methodology for calculating this deduction. However, Southern Company has agreed with the IRS on a calculation methodology and signed a closing agreement on December 11, 2008. Therefore, the Company reversed the unrecognized tax benefit and adjusted the deduction to conform to the agreement. The net impact of the reversal of the unrecognized tax benefits combined with the application of the new methodology had no material effect on the Company's financial statements. See Note 5 to the financial statements under "Effective Tax Rate" for additional information.

Other Matters

In 2004, Georgia Power and the Company entered into power purchase agreements (PPAs) with Florida Power & Light Company (FP&L) and Progress Energy Florida. Under the agreements, Georgia Power and the Company will provide FP&L and Progress Energy Florida with 165 megawatts and 74 megawatts, respectively, of capacity annually from the jointly owned Plant Scherer Unit 3 for the period from June 2010 through December 2015. The contracts provide for fixed capacity payments and variable energy payments based on actual energy delivered. The Florida PSC approved the contracts in 2005.

Also in 2004, Georgia Power and the Company entered into a PPA with Flint Electric Membership Corporation. Under the agreement, Georgia Power and the Company will provide Flint Electric Membership Corporation with 75 megawatts of capacity annually from the jointly owned Plant Scherer Unit 3 for the period from June 2010 through December 2019. The contract provides for fixed capacity payments and variable energy payments based on actual energy delivered.

The Company is involved in various other matters being litigated and regulatory matters that could affect future earnings. In addition, the Company is subject to certain claims and legal actions arising in the ordinary course of business. The Company's business activities are subject to extensive governmental regulation related to public health and the environment. 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 and water 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 the Company cannot be predicted at this time; however, for current proceedings not specifically reported herein, management does not anticipate that the liabilities, if any, arising from such current proceedings would have a material adverse effect on the Company's financial statements. See Note 3 to the financial statements for information regarding material issues.

ACCOUNTING POLICIES

Application of Critical Accounting Policies and Estimates

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

Electric Utility Regulation

The Company is subject to retail regulation by the Florida PSC and wholesale regulation by the FERC. These regulatory agencies set the rates the Company is permitted to charge customers based on allowable costs. As a result, the Company applies Financial Accounting Standards Board (FASB) Statement No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71), which requires the financial statements to reflect the effects of rate regulation. Through the ratemaking process, the regulators may require the inclusion of costs or revenues in periods different than when they would be recognized by a non-regulated company. This treatment may result in the deferral of expenses and the recording of related regulatory assets based on anticipated future recovery through rates or the deferral of gains or creation of liabilities and the recording of related regulatory liabilities. The application of SFAS No. 71 has a further effect on the Company's financial statements as a result of the estimates of allowable costs used in the ratemaking process. These estimates may differ from those actually incurred by the Company; therefore, the accounting estimates inherent in specific costs such as depreciation and pension and postretirement benefits have less of a direct impact on the Company's results of operations than they would on a non-regulated company.

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

Contingent Obligations

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

- Changes in existing state or federal regulation by governmental authorities having jurisdiction over air quality, water quality, control of toxic substances, hazardous and solid wastes, and other environmental matters.
- Changes in existing income tax regulations or changes in IRS or state revenue department interpretations of existing regulations.
- Identification of additional sites that require environmental remediation or the filing of other complaints in which the Company may be asserted to be a potentially responsible party.
- Identification and evaluation of other potential lawsuits or complaints in which the Company may be named as a defendant.
- Resolution or progression of new or existing matters through the legislative process, the court systems, the IRS, the FERC, or the EPA.

Unbilled Revenues

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

FINANCIAL CONDITION AND LIQUIDITY

Overview

The Company's financial condition remained stable at December 31, 2008. Throughout the recent turmoil in the financial markets, the Company has maintained adequate access to capital without drawing on any of its bank credit arrangements used to support its commercial paper programs and variable rate pollution control revenue bonds. The Company has continued to issue commercial paper at reasonable rates. The Company intends to continue to monitor its access to short-term and long-term capital markets as well as its bank credit arrangements to meet future capital and liquidity needs. No material changes in bank credit arrangements have occurred, although market rates for committed credit have increased and the Company may be subject to higher costs as its existing facilities are replaced or renewed. The Company's interest cost for short-term debt has decreased as market short-term interest rates have declined. The ultimate impact on future financing costs as a result of the financial turmoil cannot be determined at this time. The Company experienced no material counterparty credit losses as a result of the turmoil in the financial markets. See "Sources of Capital" and "Financing Activities" herein for additional information.

The Company's investments in pension trust funds declined in value as of December 31, 2008. The Company expects that the earliest that cash may have to be contributed to the pension trust fund is 2011 and such contribution could be significant; however, projections of the amount vary significantly depending on interpretations of and decisions related to federal legislation passed during 2008 as well as other key variables including future trust fund performance and cannot be determined at this time.

Net cash flow from operating activities totaled $147.9 million, $217.0 million, and $143.4 million for 2008, 2007, and 2006, respectively. The $69.1 million decrease in net cash flows from operating activities in 2008 was due primarily to a $61.0 million increase in cash used for the under recovered regulatory clause related to fuel. The $73.6 million increase in net cash flows from operating activities in 2007 was due primarily to increased cash inflows for fuel cost recovery. The $9.3 million decrease in net cash flows from operating activities in 2006 was due primarily to increased payments related to income taxes and fuel. Net cash flow used by investing activities totaled $348.7 million, $239.3 million, and $164.4 million for 2008, 2007, and 2006, respectively. The increases in cash flows used by investing activities were primarily due to gross property additions to utility plant of $390.7 million, $239.3 million, and $147.1 million for 2008, 2007, and 2006, respectively. Funds for the Company's property additions were provided by operating activities, capital contributions, and other financing activities. Net cash flow from financing activities totaled $198.8 million, $20.2 million, and $24.7 million for 2008, 2007, and 2006, respectively. The $178.6 million increase in net cash flows from financing activities in 2008 was due primarily to the issuance of $110 million in long-term debt and $50 million in short-term debt, and a $49.1 million change in commercial paper cash flows in 2008. The increase was partially offset by the issuance of $85 million in senior notes in 2007. The $4.5 million decrease in net cash flows from financing activities in 2007 was due primarily to a $105.6 million change in commercial paper cash flows and a $25.0 million decrease in senior note proceeds. These decreases were partially offset by the issuance of $80 million in common stock and $45 million in preference stock in 2007. The $77.4 million increase in net cash flows from financing activities in 2006 was due primarily to a $50.0 million increase in senior note proceeds and the redemption of $100.0 million in long-term debt in 2005. These increases were partially offset by the issuance of $55.0 million in preference stock in 2005 and the redemption of $30.9 million of long-term debt payable to affiliated trusts in 2006. See the statements of cash flows for additional information.

Significant balance sheet changes in 2008 included a net increase of $308.2 million in property, plant, and equipment, primarily related to environmental control projects, the issuance of $110 million in long-term debt and $50 million in short-term debt, a $40.1 million increase in under recovered regulatory clause revenues related to fuel, and a $31.0 million change in energy-related derivative contracts. Other significant balance sheet changes which are primarily attributable to the decline in market value of the Company's pension trust fund include a decrease of $107.2 million in prepaid pension costs, an increase of $73.3 million in other deferred regulatory assets, and a decrease of $54.1 million in other deferred regulatory liabilities.

The Company's ratio of common equity to total capitalization, including short-term debt, was 42.9% in 2008, 45.3% in 2007, and 42.1% in 2006. See Note 6 to the financial statements for additional information.

The Company has received investment grade credit ratings from the major rating agencies with respect to its debt and preference stock. See "SELECTED FINANCIAL AND OPERATING DATA" for additional information regarding the Company's security ratings.

Sources of Capital

The Company plans to obtain the funds required for construction and other purposes from sources similar to those used in the past, which were primarily from operating cash flows, securities issuances, term loans, and short-term indebtedness. However, the type and timing of any future financings, if needed, will depend on market conditions, regulatory approval, and other factors.

Security issuances are subject to regulatory approval by the Florida PSC pursuant to its rules and regulations. Additionally, with respect to the public offering of securities, the Company files registration statements with the Securities and Exchange Commission (SEC) under the Securities Act of 1933, as amended (1933 Act). The amounts of securities authorized by the Florida PSC, as well as the amounts, if any, registered under the 1933 Act, are continuously monitored and appropriate filings are made to ensure flexibility in the capital markets.

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

The Company's current liabilities frequently exceed current assets because of the continued use of short-term debt as a funding source to meet cash needs which can fluctuate significantly due to the seasonality of the business. To meet short-term cash needs and contingencies, the Company has various internal and external sources of liquidity. At December 31, 2008, the Company had approximately $3.4 million of cash and cash equivalents, along with $120 million of unused committed lines of credit with banks to meet its short-term cash needs. Of these bank credit arrangements, $120 million will expire in 2009 and $90 million contain provisions allowing one-year term loans executable at expiration. Subsequent to December 31, 2008, the Company obtained an additional $20 million of committed credit, which expires in 2009. The Company plans to renew these lines of credit during 2009 prior to their expiration. In addition, the Company has substantial cash flow from operating activities and access to the capital markets including a commercial paper program to meet liquidity needs. See Note 6 to the financial statements under "Bank Credit Arrangements" for additional information.

The Company 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 the Company and the other traditional operating companies. Proceeds from such issuances for the benefit of the Company are loaned directly to the Company and are not commingled with proceeds from such issuances for the benefit of any other traditional operating company. There is no cross affiliate credit support. At December 31, 2008, the Company had $89.9 million of commercial paper outstanding. In addition, the Company had a $50 million short-term bank loan outstanding and $8.3 million in notes payable outstanding related to other energy services contracts.

Financing Activities

In 2008, the Company borrowed $110 million under a three-year term loan agreement and $50 million under a short-term loan agreement. Proceeds were used to repay a portion of the Company's short-term indebtedness and for other general corporate purposes, including Gulf Power's continuous construction activities. Interest rate hedges of $80 million were settled related to issuance of senior debt at a loss of approximately $5 million.

In the first and second quarters of 2008, the Company converted its entire $141 million of obligations related to auction rate pollution control revenue bonds from auction rate modes to other interest rate modes. Approximately $75 million of the auction rate pollution control revenue bonds were converted to fixed interest rate modes and approximately $66 million were converted to variable rate modes.

During the fourth quarter of 2008, the Company converted $66 million in obligations related to variable rate pollution control revenue bonds to a fixed interest rate mode, eliminating the committed credit backup requirement for these bonds. Of this amount, the Company purchased from investors approximately $37 million of variable rate pollution control revenue bonds that were subject to mandatory tender, all of which were subsequently remarketed at a fixed rate.

On January 22, 2009, the Company issued to Southern Company 1,350,000 shares of the Company's common stock, without par value, and realized proceeds of $135 million. The proceeds were used to repay a portion of the Company's short-term debt and for other general corporate purposes.

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

Credit Rating Risk

The Company does not have any credit arrangements that would require material changes in payment schedules or terminations as a result of a credit rating downgrade. There are certain contracts that could require collateral, but not accelerated payment, in the event of a credit rating change to BBB- and/or Baa3 or below. These contracts are for physical electricity purchases and sales, fuel transportation and storage, emissions allowances and energy price risk management. At December 31, 2008, the maximum potential collateral requirements under these contracts at a BBB- and/or Baa3 rating were approximately $49 million. At December 31, 2008, the maximum potential collateral requirements under these contracts at a rating below BBB- and/or Baa3 were approximately $205 million. Included in these amounts are certain agreements that could require collateral in the event that one or more power pool participants has a credit rating change to below investment grade. Generally, collateral may be provided by a Southern Company guaranty, letter of credit, or cash. Additionally, any credit rating downgrade could impact the Company's ability to access capital markets, particularly the short-term debt market.

Market Price Risk

The Company's market risk exposures relative to interest rate changes have not changed materially compared with the December 31, 2007 reporting period. Since a significant portion of outstanding indebtedness is at fixed rates, the Company is not aware of any facts or circumstances that would significantly affect exposures on existing indebtedness in the near term. However, the impact on future financing costs cannot now be determined.

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

To mitigate residual risks relative to movements in electricity prices, the Company enters into 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 Company has implemented a fuel-hedging program per the guidelines of the Florida PSC.

The weighted average interest rate on $114 million variable rate long-term debt at January 1, 2009 was 1.62%. If the Company sustained a 100 basis point change in interest rates for all variable rate long-term debt, the change would affect annualized interest expense by approximately $1 million at January 1, 2009. See Notes 1 and 6 to the financial statements under "Financial Instruments" for additional information.

The changes in fair value of energy-related derivative contracts were as follows at December 31:

	2008 Changes	2007 Changes
	Fair Value	
	(in millions)	
Contracts outstanding at the beginning of the period, assets (liabilities), net	**$ (0.2)**	$ (7.1)
Contracts realized or settled	**(8.0)**	6.6
Current period changes[(a)]	**(23.0)**	0.3
Contracts outstanding at the end of the period, assets (liabilities), net	**$ (31.2)**	$ (0.2)

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

The decrease in the fair value positions of the energy-related derivative contracts for the year ended December 31, 2008 was $31.0 million, substantially all of which is due to natural gas positions. This change is attributable to both the volume and prices of natural gas. At December 31, 2008, the Company had a net hedge volume of 14.2 billion cubic feet (Bcf) with a weighted average contract cost approximately $2.24 per million British thermal units (mmBtu) above market prices, and 7.5 Bcf at December 31, 2007 with a weighted average contract cost approximately $0.03 per mmBtu above market prices. Natural gas hedges are recovered through the fuel cost recovery clause.

At December 31, the net fair value of energy-related derivative contracts by hedge designation was reflected in the financial statements as assets/ (liabilities) as follows:

	2008	2007
	(in millions)	
Regulatory hedges	**$ (31.2)**	$ (0.2)
Cash flow hedges	**-**	-
Non-accounting hedges	**-**	-
Total fair value	**$ (31.2)**	$ (0.2)

Energy-related derivative contracts designated as regulatory hedges are related to the Company's fuel hedging programs, where gains and losses are initially recorded as regulatory liabilities and assets, respectively, and then are included in fuel expense as they are recovered through the fuel cost recovery clause. Certain other gains and losses on energy-related derivatives, designated as cash flow hedges, are initially deferred in other comprehensive income before being recognized in income in the same period as the hedged transaction. Gains and losses on energy-related derivative contracts that are not designated or fail to qualify as hedges are recognized in the statements of income as incurred.

Unrealized pre-tax gains and losses from energy-related derivative contracts recognized in income were not material for any year presented.

The maturities of the energy-related derivative contracts and the level of the fair value hierarchy in which they fall at December 31, 2008 are as follows:

	December 31, 2008 Fair Value Measurements			
	Total	Maturity		
	Fair Value	Year 1	Years 2&3	Years 4&5
	(in millions)			
Level 1	**$ -**	**$ -**	**$ -**	**$ -**
Level 2	**(31.2)**	**(25.9)**	**(5.3)**	**-**
Level 3	**-**	**-**	**-**	**-**
Fair value of contracts outstanding at end of period	**$ (31.2)**	**$ (25.9)**	**$ (5.3)**	**$ -**

As part of the adoption of FASB Statement No. 157, "Fair Value Measurements" to increase consistency and comparability in fair value measurements and related disclosures, the table above now uses the three-tier fair value hierarchy, as discussed in Note 9 to the financial statements, as opposed to the previously used descriptions "actively quoted," "external sources," and "models and other methods." The three-tier fair value hierarchy focuses on the fair value of the contract itself, whereas the previous descriptions focused on the source of the inputs. Because the Company uses over-the-counter contracts that are not exchange traded but are fair valued using prices which are actively quoted, the valuations of those contracts now appear in Level 2; previously they were shown as "actively quoted."

The Company is exposed to market price risk in the event of nonperformance by counterparties to the derivative energy contracts. The Company's practice is to enter into agreements with counterparties that have investment grade credit ratings by Moody's and Standard & Poor's or with counterparties who have posted collateral to cover potential credit exposure. Therefore, the Company does not anticipate market risk exposure from nonperformance by the counterparties. See Notes 1 and 6 to the financial statements under "Financial Instruments" for additional information.

Capital Requirements and Contractual Obligations

The construction program of the Company is currently estimated to be $478 million in 2009, $337 million in 2010, and $400 million in 2011. Environmental expenditures included in these estimated amounts are $335 million in 2009, $164 million in 2010, and $233 million in 2011. The construction programs are subject to periodic review and revision, and actual construction costs may vary from these estimates because of numerous factors. These factors include: changes in business conditions; revised load growth estimates; storm impacts; changes in environmental statutes and regulations; changes in FERC rules and regulations; Florida PSC approvals; the cost and efficiency of construction labor, equipment, and materials; and the cost of capital. In addition, there can be no assurance that costs related to capital expenditures will be fully recovered.

The Company plans to construct a new landfill gas to energy generation facility. Construction of new transmission and distribution facilities and capital improvements, including those needed to meet environmental standards for the Company's existing generation, transmission, and distribution facilities, is ongoing.

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

Other funding requirements related to obligations associated with scheduled maturities of long-term debt, as well as the related interest, derivative obligations, preference stock dividends, leases, and other purchase commitments are as follows. See Notes 1, 6, and 7 to the financial statements for additional information.

Contractual Obligations

	2009	2010-2011	2012-2013	After 2013	Total
			(in thousands)		
Long-term debt[a] –					
Principal	$ -	$ 110,000	$ 60,000	$ 686,255	$ 856,255
Interest	40,864	81,728	78,110	471,610	672,312
Energy-related derivative obligations[b]	26,928	5,305	-	-	32,233
Preference stock dividends[c]	6,203	12,405	12,405	-	31,013
Operating leases	5,549	9,064	2,352	2,223	19,188
Purchase commitments[d] –					
Capital[e]	477,618	737,292	-	-	1,214,910
Limestone[f]	-	11,540	12,125	40,182	63,847
Coal	282,370	182,486	-	-	464,856
Natural gas[g]	112,618	128,320	40,276	151,016	432,230
Purchased power	23,007	53,672	53,997	3,918	134,594
Long-term service agreements[h]	7,088	14,903	14,552	25,954	62,497
Postretirement benefits trust[i]	34	68	-	-	102
Total	$ 982,279	$ 1,346,783	$ 273,817	$ 1,381,158	$ 3,984,037

(a) All amounts are reflected based on final maturity dates. The Company plans to continue to retire higher-cost securities and replace these obligations with lower-cost capital if market conditions permit. Variable rate interest obligations are estimated based on rates as of January 1, 2009, as reflected in the statements of capitalization.

(b) For additional information, see Notes 1 and 6 to the financial statements.

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

(d) The Company generally does not enter into non-cancelable commitments for other operations and maintenance expenditures. Total other operations and maintenance expenses for the last three years were $277 million, $270 million, and $260 million, respectively.

(e) The Company forecasts capital expenditures over a three-year period. Amounts represent current estimates of total expenditures. At December 31, 2008, significant purchase commitments were outstanding in connection with the construction program.

(f) As part of the Company's program to reduce sulfur dioxide emissions from its coal plants, the Company has begun construction of flue gas desulfurization projects and has entered into various long-term commitments for the procurement of limestone to be used in such equipment.

(g) Natural gas purchase commitments are based on various indices at the time of delivery. Amounts reflected have been estimated based on the New York Mercantile Exchange future prices at December 31, 2008.

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

(i) The Company forecasts postretirement trust contributions over a three-year period. The Company expects that the earliest that cash may have to be contributed to the pension trust fund is 2011 and such contribution could be significant; however, projections of the amount vary significantly depending on interpretations of and decisions related to federal legislation passed during 2008 as well as other key variables including future trust fund performance and cannot be determined at this time. Therefore, no amounts related to the pension trust fund are included in the table. See Note 2 to the financial statements for additional information related to the pension and postretirement plans, including estimated benefit payments. Certain benefit payments will be made through the related trusts. Other benefit payments will be made from the Company's corporate assets.

Cautionary Statement Regarding Forward-Looking Statements

The Company's 2008 Annual Report contains forward-looking statements. Forward-looking statements include, among other things, statements concerning retail sales growth, retail rates, storm damage cost recovery and repairs, fuel cost recovery and other rate actions, environmental regulations and expenditures, earnings growth, access to sources of capital, projections for postretirement benefit trust contributions, financing activities, completion of construction projects, impacts of adoption of new accounting rules, estimated sales and purchases under new power sale and purchase agreements, 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 the negative of these terms or other similar terminology. There are various factors that could cause actual results to differ materially from those suggested by the forward-looking statements; accordingly, there can be no assurance that such indicated results will be realized. These factors include:

- the impact of recent and future federal and state regulatory 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 water quality and 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 the Company is subject, as well as changes in application of existing laws and regulations;
- current and future litigation, regulatory investigations, proceedings or inquiries, including FERC matters and the EPA civil actions against the Company;
- the effects, extent, and timing of the entry of additional competition in the markets in which the Company operates;
- variations in demand for electricity, including those relating to weather, the general economy, population, and business growth (and declines), and the effects of energy conservation measures;
- available sources and costs of fuels;
- effects of inflation;
- ability to control costs;
- investment performance of the 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;
- internal restructuring or other restructuring options that may be pursued;
- potential business strategies, including acquisitions or dispositions of assets or businesses, which cannot be assured to be completed or beneficial to the Company;
- the ability of counterparties of the Company to make payments as and when due and to perform as required;
- the ability to obtain new short- and long-term contracts with neighboring utilities;
- the direct or indirect effect on the 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 the Company's credit ratings;
- the ability of the Company 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 the 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 Company from time to time with the SEC.

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

STATEMENTS OF INCOME

For the Years Ended December 31, 2008, 2007, and 2006

Gulf Power Company 2008 Annual Report

	2008	2007	2006
		(in thousands)	
Operating Revenues:			
Retail revenues	**$1,120,766**	$1,006,329	$952,038
Wholesale revenues --			
Non-affiliates	**97,065**	83,514	87,142
Affiliates	**106,989**	113,178	118,097
Other revenues	**62,383**	56,787	46,637
Total operating revenues	**1,387,203**	1,259,808	1,203,914
Operating Expenses:			
Fuel	**635,634**	573,354	534,921
Purchased power --			
Non-affiliates	**29,590**	11,994	16,288
Affiliates	**79,750**	59,499	57,536
Other operations and maintenance	**277,478**	270,440	259,519
Depreciation and amortization	**84,815**	85,613	89,170
Taxes other than income taxes	**87,247**	82,992	79,808
Total operating expenses	**1,194,514**	1,083,892	1,037,242
Operating Income	**192,689**	175,916	166,672
Other Income and (Expense):			
Allowance for equity funds used during construction	**9,969**	2,374	363
Interest income	**3,155**	5,348	5,228
Interest expense, net of amounts capitalized	**(43,098)**	(44,680)	(44,133)
Other income (expense), net	**(4,064)**	(3,876)	(3,548)
Total other income and (expense)	**(34,038)**	(40,834)	(42,090)
Earnings Before Income Taxes	**158,651**	135,082	124,582
Income taxes	**54,103**	47,083	45,293
Net Income	**104,548**	87,999	79,289
Dividends on Preference Stock	**6,203**	3,881	3,300
Net Income After Dividends on Preference Stock	**$ 98,345**	$ 84,118	$ 75,989

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

STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2008, 2007, and 2006
Gulf Power Company 2008 Annual Report

	2008	2007	2006
		(in thousands)	
Operating Activities:			
Net income	**$104,548**	$ 87,999	$ 79,289
Adjustments to reconcile net income			
to net cash provided from operating activities --			
Depreciation and amortization	**93,606**	90,694	94,466
Deferred income taxes	**23,949**	(10,818)	1,170
Allowance for equity funds used during construction	**(9,969)**	(2,374)	(363)
Pension, postretirement, and other employee benefits	**1,585**	6,062	3,319
Stock based compensation expense	**765**	1,141	1,005
Tax benefit of stock options	**215**	344	211
Hedge settlements	**(5,220)**	3,030	(5,399)
Other, net	**(5,150)**	(7,074)	7,294
Changes in certain current assets and liabilities --			
Receivables	**(49,885)**	10,302	(36,795)
Fossil fuel stock	**(36,765)**	5,025	(31,297)
Materials and supplies	**8,927**	(2,625)	(2,330)
Prepaid income taxes	**(416)**	7,177	(7,060)
Property damage cost recovery	**26,143**	25,103	24,544
Other current assets	**(307)**	(632)	(955)
Accounts payable	**(4,561)**	(555)	13,876
Accrued taxes	**(6,511)**	4,773	(455)
Accrued compensation	**570**	(1,322)	(3,251)
Other current liabilities	**6,418**	732	6,165
Net cash provided from operating activities	**147,942**	216,982	143,434
Investing Activities:			
Property additions	**(377,790)**	(241,538)	(154,377)
Cost of removal net of salvage	**(8,713)**	(9,408)	(4,564)
Construction payables	**37,244**	10,817	3,309
Other	**576**	803	(8,779)
Net cash used for investing activities	**(348,683)**	(239,326)	(164,411)
Financing Activities:			
Increase (decrease) in notes payable, net	**107,438**	(75,821)	30,981
Proceeds --			
Senior notes	**-**	85,000	110,000
Common stock issued to parent	**-**	80,000	-
Preference stock	**-**	45,000	-
Pollution control revenue bonds	**37,000**	-	-
Gross excess tax benefit of stock options	**298**	799	423
Capital contributions from parent company	**75,324**	4,174	26,140
Other long-term debt	**110,000**	-	-
Redemptions --			
Senior notes	**(1,300)**	-	-
Pollution control revenue bonds	**(37,000)**	-	(12,075)
First mortgage bonds	**-**	-	(25,000)
Other long-term debt	-	(41,238)	(30,928)
Payment of preference stock dividends	**(6,057)**	(3,300)	(3,300)
Payment of common stock dividends	**(81,700)**	(74,100)	(70,300)
Other	**(5,167)**	(348)	(1,285)
Net cash provided from financing activities	**198,836**	20,166	24,656
Net Change in Cash and Cash Equivalents	**(1,905)**	(2,178)	3,679
Cash and Cash Equivalents at Beginning of Year	**5,348**	7,526	3,847
Cash and Cash Equivalents at End of Year	**$ 3,443**	$ 5,348	$ 7,526
Supplemental Cash Flow Information:			
Cash paid during the period for --			
Interest (net of $3,973, $1,048, and $160 capitalized, respectively)	**$39,956**	$35,237	$37,297
Income taxes (net of refunds)	**40,176**	39,228	54,533

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

BALANCE SHEETS
At December 31, 2008 and 2007
Gulf Power Company 2008 Annual Report

Assets	**2008**	2007
	(in thousands)	
Current Assets:		
Cash and cash equivalents	**$ 3,443**	$ 5,348
Receivables --		
Customer accounts receivable	**69,531**	63,227
Unbilled revenues	**48,742**	39,000
Under recovered regulatory clause revenues	**98,645**	58,435
Other accounts and notes receivable	**7,201**	7,162
Affiliated companies	**8,516**	19,377
Accumulated provision for uncollectible accounts	**(2,188)**	(1,711)
Fossil fuel stock, at average cost	**108,129**	71,012
Materials and supplies, at average cost	**36,836**	45,763
Property damage cost recovery	**-**	18,585
Other regulatory assets	**38,907**	10,220
Other	**25,655**	14,878
Total current assets	**443,417**	351,296
Property, Plant, and Equipment:		
In service	**2,785,561**	2,678,952
Less accumulated provision for depreciation	**971,464**	931,968
	1,814,097	1,746,984
Construction work in progress	**391,987**	150,870
Total property, plant, and equipment	**2,206,084**	1,897,854
Other Property and Investments	**15,918**	4,563
Deferred Charges and Other Assets:		
Deferred charges related to income taxes	**24,220**	17,847
Prepaid pension costs	**-**	107,151
Other regulatory assets	**170,836**	97,492
Other	**18,550**	22,784
Total deferred charges and other assets	**213,606**	245,274
Total Assets	**$2,879,025**	$2,498,987

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

BALANCE SHEETS

At December 31, 2008 and 2007

Gulf Power Company 2008 Annual Report

Liabilities and Stockholder's Equity	**2008**	2007
	(in thousands)	
Current Liabilities:		
Notes payable	**$148,239**	$ 44,625
Accounts payable --		
Affiliated	**50,304**	39,375
Other	**90,381**	56,823
Customer deposits	**28,017**	24,885
Accrued taxes --		
Income taxes	**39,983**	30,026
Other	**11,855**	10,577
Accrued interest	**8,959**	7,698
Accrued compensation	**15,667**	15,096
Other regulatory liabilities	**4,602**	6,027
Liabilities from risk management activities	**26,928**	4,065
Other	**29,047**	27,958
Total current liabilities	**453,982**	267,155
Long-term Debt (See accompanying statements)	**849,265**	740,050
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	**254,354**	240,101
Accumulated deferred investment tax credits	**11,255**	12,988
Employee benefit obligations	**97,389**	74,021
Other cost of removal obligations	**180,325**	172,876
Other regulatory liabilities	**28,596**	82,741
Other	**83,769**	79,802
Total deferred credits and other liabilities	**655,688**	662,529
Total Liabilities	**1,958,935**	1,669,734
Preference Stock (See accompanying statements)	**97,998**	97,998
Common Stockholder's Equity (See accompanying statements)	**822,092**	731,255
Total Liabilities and Stockholder's Equity	**$2,879,025**	$2,498,987
Commitments and Contingent Matters (See notes)		

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

STATEMENTS OF CAPITALIZATION

At December 31, 2008 and 2007

Gulf Power Company 2008 Annual Report

	2008	2007	**2008**	2007
	(in thousands)		*(percent of total)*	
Long Term Debt:				
Long-term notes payable --				
4.35% due 2013	**$ 60,000**	$ 60,000		
4.90% to 5.90% due 2014-2044	**528,700**	530,000		
Variable rates (1.645% at 1/1/09) due 2011	**110,000**	-		
Total long-term notes payable	**698,700**	590,000		
Other long-term debt --				
Pollution control revenue bonds --				
2.35% to 6.00% due 2022-2037	**153,625**	13,000		
Variable rate (1.05% at 1/1/09) due 2022-2037	**3,930**	144,555		
Total other long-term debt	**157,555**	157,555		
Unamortized debt discount	**(6,990)**	(7,505)		
Total long-term debt (annual interest requirement -- $40.9 million)	**849,265**	740,050	**48.0%**	47.2%
Preferred and Preference Stock:				
Authorized - 20,000,000 shares--preferred stock				
- 10,000,000 shares--preference stock				
Outstanding - $100 par or stated value -- 6% preference stock	**53,886**	53,886		
-- 6.45% preference stock	**44,112**	44,112		
- 1,000,000 shares (non-cumulative)				
Preference stock (annual dividend requirement -- $6.2 million)	**97,998**	97,998	**5.5**	6.2
Common Stockholder's Equity:				
Common stock, without par value --				
Authorized - 20,000,000 shares				
Outstanding - 1,792,717 shares	**118,060**	118,060		
Paid-in capital	**511,547**	435,008		
Retained earnings	**197,417**	181,986		
Accumulated other comprehensive income (loss)	**(4,932)**	(3,799)		
Total common stockholder's equity	**822,092**	731,255	**46.5**	46.6
Total Capitalization	**$1,769,355**	$1,569,303	**100.0%**	100.0%

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

STATEMENTS OF COMMON STOCKHOLDER'S EQUITY

For the Years Ended December 31, 2008, 2007, and 2006

Gulf Power Company 2008 Annual Report

	Common Stock	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
			(in thousands)		
Balance at December 31, 2005	$38,060	$400,815	$166,279	$ (2,810)	$602,344
Net income after dividends on preference stock	-	-	75,989	-	75,989
Capital contributions from parent company	-	27,777	-	-	27,777
Other comprehensive income (loss)	-	-	-	(3,112)	(3,112)
Adjustment to initially apply FASB Statement No. 158, net of tax	-	-	-	1,325	1,325
Cash dividends on common stock	-	-	(70,300)	-	(70,300)
Balance at December 31, 2006	38,060	428,592	171,968	(4,597)	634,023
Net income after dividends on preference stock	-	-	84,118	-	84,118
Issuance of common stock	80,000	-	-	-	80,000
Capital contributions from parent company	-	6,458	-	-	6,458
Other comprehensive income (loss)	-	-	-	798	798
Cash dividends on common stock	-	-	(74,100)	-	(74,100)
Other	-	(42)	-	-	(42)
Balance at December 31, 2007	**118,060**	**435,008**	**181,986**	**(3,799)**	**731,255**
Net income after dividends on preference stock	**-**	**-**	**98,345**	**-**	**98,345**
Capital contributions from parent company	**-**	**76,539**	**-**	**-**	**76,539**
Other comprehensive income (loss)	**-**	**-**	**-**	**(1,133)**	**(1,133)**
Cash dividends on common stock	**-**	**-**	**(81,700)**	**-**	**(81,700)**
Change in benefit plan measurement date	**-**	**-**	**(1,214)**	**-**	**(1,214)**
Balance at December 31, 2008	**$118,060**	**$511,547**	**$197,417**	**$(4,932)**	**$822,092**

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

STATEMENTS OF COMPREHENSIVE INCOME

For the Years Ended December 31, 2008, 2007, and 2006

Gulf Power Company 2008 Annual Report

	2008	2007	2006
		(in thousands)	
Net income after dividends on preference stock	**$98,345**	$84,118	$75,989
Other comprehensive income (loss):			
Qualifying hedges:			
Changes in fair value, net of tax of $(1,077), $232, and $(2,082), respectively	**(1,716)**	371	(3,317)
Reclassification adjustment for amounts included in net income, net of tax of $366, $269, and $140, respectively	**583**	427	224
Pension and other postretirement benefit plans:			
Change in additional minimum pension liability, net of tax of $-, $-, and $(13), respectively	**-**	-	(19)
Total other comprehensive income (loss)	**(1,133)**	798	(3,112)
Comprehensive Income	**$97,212**	$84,916	$72,877

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

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

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

The equity method is used for subsidiaries in which the Company has significant influence but does not control and for variable interest entities where the Company is not the primary beneficiary.

The Company is subject to regulation by the Federal Energy Regulatory Commission (FERC) and the Florida Public Service Commission (PSC). The Company follows accounting principles generally accepted in the United States and complies with the accounting policies and practices prescribed by its regulatory commissions. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the use of estimates, and the actual results may differ from those estimates.

Reclassifications

Certain prior years' data presented in the financial statements have been reclassified to conform to current year presentation. For presentation purposes, the statements of income for the prior periods presented have been modified within the operating expenses section to combine the line items "Other operations" and "Maintenance" into a single line item entitled "Other operations and maintenance." In addition, the statements of income were modified to report a separate line item for "Allowance for equity funds used during construction" previously included in "Other income and expense, net." In conjunction with such modification, the Company modified its statement of cash flows within the operating activities section to present a separate line item for "Allowance for equity funds used during construction" previously included in "Other, net." The balance sheet at December 31, 2007 was modified to present a separate line for "Liabilities for risk management activities" previously included in "Other." These reclassifications had no effect on total assets, net income, or cash flows.

Affiliate Transactions

The Company has an agreement with SCS under which the following services are rendered to the Company at direct or allocated cost: general and design engineering, purchasing, accounting and statistical analysis, finance and treasury, tax, information resources, marketing, auditing, insurance and pension administration, human resources, systems and procedures, digital wireless communications, and other services with respect to business and operations and power pool operations. Costs for these services amounted to $86 million, $73 million, and $59 million during 2008, 2007, and 2006, respectively. Cost allocation methodologies used by SCS were approved by the Securities and Exchange Commission prior to the repeal of the Public Utility Holding Company Act of 1935, as amended, and management believes they are reasonable. The FERC permits services to be rendered at cost by system service companies.

The Company has agreements with Georgia Power and Mississippi Power under which the Company owns a portion of Plant Scherer and Plant Daniel, respectively. Georgia Power operates Plant Scherer and Mississippi Power operates Plant Daniel. The Company reimbursed Georgia Power $8.1 million, $5.1 million, and $8.0 million, and Mississippi Power $22.8 million, $23.1 million, and $19.7 million in 2008, 2007, and 2006, respectively, for its proportionate share of related expenses. See Note 4 and Note 7 under "Operating Leases" for additional information.

The Company entered into a power purchase agreement (PPA), with Southern Power for a total of approximately 292 megawatts annually from June 2009 through May 2014. The PPA was the result of a competitive request for proposal process initiated by the Company in January 2006 to address the anticipated need for additional capacity beginning in 2009. In May 2007, the Florida PSC issued an order approving the PPA for purpose of cost recovery through the Company's purchased power capacity clause. The PPA with Southern Power was approved by the FERC in July 2007.

The Company provides incidental services to and receives such services from other Southern Company subsidiaries which are generally minor in duration and amount. There were no significant services provided or received in 2008, 2007, and 2006.

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

In 2008, the Company sold a turbine rotor assembly and a distance piece component to Southern Power for $9.4 million and $0.7 million, respectively. In 2007, the Company purchased a compressor assembly from Georgia Power and a turbine rotor assembly from Southern Power for $4.0 million and $7.9 million, respectively. The affiliate transactions were made in accordance with FERC and state PSC rules and guidelines. The purchases are included in property, plant, and equipment in the balance sheets.

Regulatory Assets and Liabilities

The Company is subject to the provisions of Financial Accounting Standards Board (FASB) Statement No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71). Regulatory assets represent probable future revenues associated with certain costs that are expected to be recovered from customers through the ratemaking process. Regulatory liabilities represent probable future reductions in revenues associated with amounts that are expected to be credited to customers through the ratemaking process. Regulatory assets and (liabilities) reflected in the balance sheets at December 31 relate to:

	2008	2007	Note
	(in thousands)		
Environmental remediation	**$ 66,812**	$ 66,923	(a)
Loss on reacquired debt	**16,248**	17,378	(b)
Vacation pay	**7,991**	7,411	(c)
Deferred charges related to income taxes	**24,220**	17,847	(d)
Fuel-hedging (realized and unrealized) losses	**35,333**	1,834	(e)
Underfunded retiree benefit plans	**81,912**	14,602	(f)
Other assets	**3,360**	1,371	(g)
Under recovered regulatory clause revenues	**96,731**	56,628	(g)
Property damage reserve	**(9,801)**	18,585	(h)
Asset retirement obligations	**(4,531)**	(4, 570)	(d)
Other cost of removal obligations	**(180,325)**	(172,876)	(d)
Deferred income tax credits	**(12,983)**	(15,331)	(d)
Fuel-hedging (realized and unrealized) gains	**(1,071)**	(1,455)	(e)
Over recovered regulatory clause revenues	**(3,295)**	(5,233)	(g)
Other liabilities	**(1,518)**	(1,715)	(g)
Overfunded retiree benefit plans	**-**	(60,464)	(f)
Total assets (liabilities), net	**$ 119,083**	$ (59,065)	

Note: The recovery and amortization periods for these regulatory assets and (liabilities) are as follows:
(a) Recovered through the environmental cost recovery clause when the remediation is performed.
(b) Recovered over the remaining life of the original issue, which may range up to 40 years.
(c) Recorded as earned by employees and recovered as paid, generally within one year.
(d) Asset retirement and removal liabilities are recovered, deferred charges related to income tax assets are recovered, and deferred charges related to income tax liabilities are amortized over the related property lives, which may range up to 65 years. Asset retirement and removal liabilities will be settled and trued up following completion of the related activities.
(e) Fuel-hedging assets and liabilities are recognized over the life of the underlying hedged purchase contracts, which generally do not exceed four years. Upon final settlement, costs are recovered through the fuel cost recovery clause.
(f) Recovered and amortized over the average remaining service period which may range up to 14 years. See Note 2 under "Retirement Benefits."
(g) Recorded and recovered or amortized as approved by the Florida PSC.
(h) Recorded and recovered or amortized as approved by the Florida PSC. Storm cost recovery surcharge ends in June 2009.

In the event that a portion of the Company's operations is no longer subject to the provisions of SFAS No. 71, the Company would be required to write off or reclassify to accumulated other comprehensive income related regulatory assets and liabilities that are not specifically recoverable through regulated rates. In addition, the Company would be required to determine if any impairment to other assets, including plant assets, exists and write down the assets, if impaired, to their fair values. All regulatory assets and liabilities are reflected in rates.

Revenues

Energy and other revenues are recognized as services are provided. Unbilled revenues related to retail sales are accrued at the end of each fiscal period. Wholesale capacity revenues are generally recognized on a levelized basis over the appropriate contract period. The Company's retail electric rates include provisions to adjust billings for fluctuations in fuel costs, the energy component of purchased power costs, and certain other costs. The Company continuously monitors the over or under recovered fuel cost balance in light of the inherent variability in fuel costs. The Company is required to notify the Florida PSC if the projected fuel cost over or under recovery is expected to exceed 10% of the projected fuel revenue applicable for the period and indicate if an adjustment to the fuel cost recovery factor is being requested. The Company has similar retail cost recovery clauses for energy conservation costs, purchased power capacity costs, and environmental compliance costs. Revenues are adjusted for differences between these actual costs and amounts billed in current regulated rates. Under or over recovered regulatory clause revenues are recorded in the balance sheets and are recovered or returned to customers through adjustments to the billing factors. Annually, the Company petitions for recovery of projected costs including any true-up amount from prior periods, and approved rates are implemented each January. In November 2008, the Florida PSC approved billing factors for 2009 intended to allow the Company to recover projected 2009 costs as well as refund or collect the 2008 over or under recovered amounts in 2009. See Note 3 under "Regulatory Matters – Fuel Cost Recovery" for additional information.

The Company has a diversified base of customers. No single customer or industry comprises 10% or more of revenues. For all periods presented, uncollectible accounts averaged less than 1% of revenues.

Fuel Costs

Fuel costs are expensed as the fuel is used.

Income and Other Taxes

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

In accordance with FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48), the Company recognizes tax positions that are "more likely than not" of being sustained upon examination by the appropriate taxing authorities. See Note 5 under "Unrecognized Tax Benefits" for additional information.

Property, Plant, and Equipment

Property, plant, and equipment is stated at original cost less regulatory disallowances and impairments. Original cost includes: materials; labor; minor items of property; appropriate administrative and general costs; payroll-related costs such as taxes, pensions, and other benefits; and the interest capitalized and/or cost of funds used during construction.

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

	2008	2007
	(in thousands)	
Generation	**$ 1,445,095**	$ 1,390,635
Transmission	**305,097**	282,408
Distribution	**900,793**	873,642
General	**131,269**	128,704
Plant acquisition adjustment	**3,307**	3,563
Total plant in service	**$ 2,785,561**	$ 2,678,952

The cost of replacements of property, exclusive of minor items of property, is capitalized. The cost of maintenance, repairs, and replacement of minor items of property is charged to maintenance expense as incurred or performed.

Depreciation and Amortization

Depreciation of the original cost of utility plant in service is provided primarily by using composite straight-line rates, which approximated 3.4% in 2008, 3.4% in 2007, and 3.7% in 2006. Depreciation studies are conducted periodically to update the composite rates. These studies are approved by the Florida PSC. When property subject to depreciation is retired or otherwise disposed of in the normal course of business, its original cost, together with the cost of removal, less salvage, is charged to accumulated depreciation. For other property dispositions, the applicable cost and accumulated depreciation is removed from the balance sheet accounts and a gain or loss is recognized. Minor items of property included in the original cost of the plant are retired when the related property unit is retired.

Asset Retirement Obligations and Other Costs of Removal

Asset retirement obligations are computed as the present value of the ultimate costs for an asset's future retirement and are recorded in the period in which the liability is incurred. The costs are capitalized as part of the related long-lived asset and depreciated over the asset's useful life. The Company has received an order from the Florida PSC allowing the continued accrual of other future retirement costs for long-lived assets that the Company does not have a legal obligation to retire. Accordingly, the accumulated removal costs for these obligations will continue to be reflected in the balance sheets as a regulatory liability.

The liability recognized to retire long-lived assets primarily relates to the Company's combustion turbines at its Pea Ridge facility, various landfill sites, a barge unloading dock, asbestos removal, ash ponds, and disposal of polychlorinated biphenyls in certain transformers. The Company also has identified retirement obligations related to certain transmission and distribution facilities, certain wireless communication towers, and certain structures authorized by the United States Army Corps of Engineers. However, liabilities for the removal of these assets have not been recorded because the range of time over which the Company may settle these obligations is unknown and cannot be reasonably estimated. The Company will continue to recognize in the statements of income allowed removal costs in accordance with its regulatory treatment. Any differences between costs recognized under FASB Statement No. 143 "Accounting for Asset Retirement Obligations" and FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" and those reflected in rates are recognized as either a regulatory asset or liability, as ordered by the Florida PSC, and are reflected in the balance sheets.

Details of the asset retirement obligations included in the balance sheets are as follows:

	2008	2007
	(in thousands)	
Balance beginning of year	**$ 11,942**	$ 12,718
Liabilities incurred	**-**	503
Liabilities settled	**(354)**	(484)
Accretion	**631**	619
Cash flow revisions	**(177)**	(1,414)
Balance end of year	**$ 12,042**	$ 11,942

Allowance for Funds Used During Construction (AFUDC)

In accordance with regulatory treatment, the Company records AFUDC, which represents the estimated debt and equity costs of capital funds that are necessary to finance the construction of new regulated facilities. While cash is not realized currently from such allowance, it increases the revenue requirement over the service life of the plant through a higher rate base and higher depreciation expense. The equity component of AFUDC is not included in calculating taxable income. The average annual AFUDC rate was 7.65%, 7.48%, and 7.48%, respectively, for the years 2008, 2007, and 2006. AFUDC, net of taxes, as a percentage of net income after dividends on preference stock was 12.62%, 3.59%, and 0.61%, respectively, for 2008, 2007, and 2006.

Impairment of Long-Lived Assets and Intangibles

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

Property Damage Reserve

The Company accrues for the cost of repairing damages from major storms and other uninsured property damages, including uninsured damages to transmission and distribution facilities, generation facilities, and other property. The cost of such damages is charged to the reserve. The Florida PSC approved annual accrual to the property damage reserve is $3.5 million, with a target level for the reserve between $25.1 million and $36.0 million. The Florida PSC also authorized the Company to make additional accruals above the $3.5 million at the Company's discretion. The Company accrued total expenses of $3.5 million in 2008, $3.5 million in 2007, and $6.5 million in 2006. As of December 31, 2008, the balance in the Company's property damage reserve totaled approximately $9.8 million, which is included in deferred liabilities in the balance sheets. See Note 3 under "Retail Regulatory Matters – Storm Damage Cost Recovery" for additional information regarding the surcharge mechanism approved by the Florida PSC to replenish these reserves.

Injuries and Damages Reserve

The Company is subject to claims and suits arising in the ordinary course of business. As permitted by the Florida PSC, the Company accrues for the uninsured costs of injuries and damages by charges to income amounting to $1.6 million annually. The Florida PSC has also given the Company the flexibility to increase its annual accrual above $1.6 million to the extent the balance in the reserve does not exceed $2 million and to defer expense recognition of liabilities greater than the balance in the reserve. The cost of settling claims is charged to the reserve. The injuries and damages reserve was $2.5 million and $2.2 million at December 31, 2008 and 2007, respectively, and is included in Current Liabilities in the balance sheets. Liabilities in excess of the reserve balance of $0.8 million and $0.8 million at December 31, 2008 and 2007, respectively, are included in Deferred Credits and Other Liabilities in the balance sheets. Corresponding regulatory assets of $0.8 million and $0.8 million at December 31, 2008 and 2007, respectively, are included in Current Assets in the balance sheets.

Cash and Cash Equivalents

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

Materials and Supplies

Generally, materials and supplies include the average cost of transmission, distribution, and generating plant materials. Materials are charged to inventory when purchased and then expensed or capitalized to plant, as appropriate, at weighted average cost when installed.

Fuel Inventory

Fuel inventory includes the average costs of oil, coal, natural gas, and emission allowances. Fuel is charged to inventory when purchased and then expensed as used and recovered through fuel cost recovery rates approved by the Florida PSC. Emission allowances granted by the Environmental Protection Agency (EPA) are included in inventory at zero cost.

Financial Instruments

The Company uses derivative financial instruments to limit exposure to fluctuations in interest rates, the prices of certain fuel purchases, and electricity purchases and sales. All derivative financial instruments are recognized as either assets or liabilities (categorized in "Other" or shown separately as "Risk Management Activities") and are measured at fair value. See Note 9 for additional information. Substantially all of the Company's bulk energy purchases and sales contracts that meet the definition of a derivative are exempt from fair value accounting requirements and are accounted for under the accrual method. Other derivative contracts qualify as cash flow hedges of anticipated transactions or are recoverable through the Florida PSC-approved hedging program. This results in the deferral of related gains and losses in other comprehensive income or regulatory assets and liabilities, respectively, until the hedged transactions occur. Any ineffectiveness arising from cash flow hedges is recognized currently in net income. Other derivative contracts are marked to market through current period income and are recorded on a net basis in the statements of income. See Note 6 under "Financial Instruments" for additional information.

The Company does not offset fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a master netting arrangement. Additionally, the Company has no outstanding collateral repayment obligations or rights to reclaim collateral arising from derivative instruments recognized at December 31, 2008.

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

Other financial instruments for which the carrying amounts did not equal fair values at December 31 were as follows:

	Carrying Amount	Fair Value
	(in thousands)	
Long-term debt:		
2008	**$ 849,265**	**$ 831,763**
2007	$ 740,050	$ 725,885

The fair values were based on either closing market prices (Level 1) or closing prices of comparable instruments (Level 2). See Note 9 for all other items recognized at fair value in the financial statements.

Comprehensive Income

The objective of comprehensive income is to report a measure of all changes in common stock equity of an enterprise that result from transactions and other economic events of the period other than transactions with owners. Comprehensive income consists of net income and changes in the fair value of qualifying cash flow hedges, and prior to the adoption of SFAS No.158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS No. 158) the minimum pension liability, less income taxes and reclassifications for amounts included in net income.

Variable Interest Entities

The primary beneficiary of a variable interest entity must consolidate the related assets and liabilities. The Company had established certain wholly-owned trusts to issue preferred securities. The Company is not considered the primary beneficiary of the trusts. Therefore, the investments in these trusts were reflected as Other Investments for the Company, and the related loans from the trusts were included in Long-term Debt in the balance sheets. In November 2007, the Company redeemed $41.2 million of its Series E Junior Subordinated Notes and the related trust preferred and common securities of Gulf Power Capital Trust IV. As of December 31, 2008, the Company no longer had any outstanding trust preferred securities. See Note 6 under "Long-Term Debt Payable to Affiliated Trusts" for additional information.

2. RETIREMENT BENEFITS

The Company has a defined benefit, trusteed, pension plan covering substantially all employees. The plan is funded in accordance with requirements of the Employee Retirement Income Security Act of 1974, as amended (ERISA). No contributions to the plan are expected for the year ending December 31, 2009. The Company also provides a defined benefit pension plan for a selected group of management and highly compensated employees. Benefits under this non-qualified plan are funded on a cash basis. In addition, the Company provides certain medical care and life insurance benefits for retired employees through other postretirement benefit plans. The Company funds related trusts to the extent required by the FERC. For the year ending December 31, 2009, postretirement trust contributions are expected to total approximately $34,000.

The measurement date for plan assets and obligations for 2008 was December 31 while the measurement date for prior years was September 30. Pursuant to SFAS No. 158, the Company was required to change the measurement date for its defined benefit postretirement plans from September 30 to December 31 beginning with the year ending December 31, 2008. As permitted, the Company adopted the measurement date provisions of SFAS No. 158 effective January 1, 2008 resulting in an increase in long-term liabilities of approximately $1.4 million and an increase in prepaid pension costs of approximately $0.6 million.

Pension Plans

The total accumulated benefit obligation for the pension plans was $243 million in 2008 and $230 million in 2007. Changes during the 15-month period ended December 31, 2008 and the 12-month period ended September 30, 2007 in the projected benefit obligations and the fair value of plan assets were as follows:

	2008	2007
	(in thousands)	
Change in benefit obligation		
Benefit obligation at beginning of year	**$ 251,781**	$ 246,569
Service cost	**8,437**	6,835
Interest cost	**19,344**	14,519
Benefits paid	**(15,880)**	(11,625)
Plan amendments	**-**	1,698
Actuarial (gain) loss	**(2,917)**	(6,215)
Balance at end of year	**260,765**	251,781
Change in plan assets		
Fair value of plan assets at beginning of year	**345,398**	305,525
Actual return (loss) on plan assets	**(101,036)**	50,816
Employer contributions	**925**	682
Benefits paid	**(15,880)**	(11,625)
Fair value of plan assets at end of year	**229,407**	345,398
Funded status at end of year	**(31,358)**	93,617
Fourth quarter contributions	**-**	149
(Accrued liability) prepaid pension asset	**$ (31,358)**	$ 93,766

At December 31, 2008, the projected benefit obligations for the qualified and non-qualified pension plans were $247.9 million and $12.9 million, respectively. All pension plan assets are related to the qualified pension plan.

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

The actual composition of the Company's pension plan assets as of the end of the year, along with the targeted mix of assets, is presented below:

	Target	**2008**	2007
Domestic equity	36%	**34%**	38%
International equity	24	**23**	24
Fixed income	15	**14**	15
Real estate	15	**19**	16
Private equity	10	**10**	7
Total	100%	**100%**	100%

Amounts recognized in the balance sheets related to the Company's pension plans consist of:

	2008	2007
	(in thousands)	
Prepaid pension costs	**$ -**	$107,151
Other regulatory assets	**71,990**	6,561
Current liabilities, other	**(863)**	(639)
Other regulatory liabilities	**-**	(60,464)
Employee benefit obligations	**(30,494)**	(12,403)

Presented below are the amounts included in regulatory assets and regulatory liabilities at December 31, 2008 and 2007 related to the defined benefit pension plans that had not yet been recognized in net periodic pension cost along with the estimated amortization of such amounts for 2009.

	Prior Service Cost	**Net (Gain) Loss**
	(in thousands)	
Balance at December 31, 2008:		
Regulatory assets	**$ 9,984**	**$ 62,006**
Regulatory liabilities	**-**	**-**
Total	**$ 9,984**	**$ 62,006**
Balance at December 31, 2007:		
Regulatory assets	$ 1,900	$ 4,661
Regulatory liabilities	9,932	(70,396)
Total	$ 11,832	$ (65,735)
Estimated amortization in net periodic pension cost in 2009:		
Regulatory assets	$ 1,478	$ 224
Regulatory liabilities	-	-
Total	$ 1,478	$ 224

The changes in the balances of regulatory assets and regulatory liabilities related to the defined benefit pension plans for the 15-month period ended December 31, 2008 and the 12-month period ended September 30, 2007 are presented in the following table:

	Regulatory Assets	Regulatory Liabilities
	(in thousands)	
Balance at December 31, 2006	$ 5,091	$ (23,478)
Net (gain) loss	313	(35,765)
Change in prior service costs	1,698	-
Reclassification adjustments:		
Amortization of prior service costs	(199)	(1,221)
Amortization of net gain	(342)	-
Total reclassification adjustments	(541)	(1,221)
Total change	1,470	(36,986)
Balance at December 31, 2007	**$ 6,561**	**$ (60,464)**
Net (gain) loss	**66,170**	**61,989**
Change in prior service costs	**-**	**-**
Reclassification adjustments:		
Amortization of prior service costs	**(323)**	**(1,525)**
Amortization of net gain	**(418)**	**-**
Total reclassification adjustments	**(741)**	**(1,525)**
Total change	**65,429**	**60,464**
Balance at December 31, 2008	**$ 71,990**	**$ -**

Components of net periodic pension cost (income) were as follows:

	2008	2007	2006
		(in thousands)	
Service cost	**$ 6,750**	$ 6,835	$ 6,980
Interest cost	**15,475**	14,519	13,358
Expected return on plan assets	**(23,757)**	(21,934)	(20,727)
Recognized net (gain) loss	**334**	342	463
Net amortization	**1,478**	1,419	1,313
Net periodic pension cost (income)	**$ 280**	$ 1,181	$ 1,387

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

Future benefit payments reflect expected future service and are estimated based on assumptions used to measure the projected benefit obligation for the pension plans. At December 31, 2008, estimated benefit payments were as follows:

	Benefit Payments
	(in thousands)
2009	$ 13,699
2010	14,119
2011	14,662
2012	15,342
2013	16,033
2014 to 2018	95,308

Other Postretirement Benefits

Changes during the 15-month period ended December 31, 2008 and the 12-month period ended September 30, 2007 in the accumulated postretirement benefit obligations (APBO) and in the fair value of plan assets were as follows:

	2008	2007
	(in thousands)	
Change in benefit obligation		
Benefit obligation at beginning of year	**$ 73,909**	$ 73,985
Service cost	**1,766**	1,351
Interest cost	**5,671**	4,330
Benefits paid	**(4,864)**	(3,586)
Actuarial (gain) loss	**(4,522)**	(2,430)
Retiree drug subsidy	**431**	259
Balance at end of year	**72,391**	73,909
Change in plan assets		
Fair value of plan assets at beginning of year	**19,610**	17,640
Actual return (loss) on plan assets	**(5,556)**	2,934
Employer contributions	**3,559**	2,363
Benefits paid	**(4,433)**	(3,327)
Fair value of plan assets at end of year	**13,180**	19,610
Funded status at end of year	**(59,211)**	(54,299)
Fourth quarter contributions	**-**	872
Accrued liability	**$ (59,211)**	$ (53,427)

Other postretirement benefit plan assets are managed and invested in accordance with all applicable requirements, including ERISA and the Internal Revenue Code. The Company's investment policy covers a diversified mix of assets, including equity and fixed income securities, real estate, and private equity. Derivative instruments are used primarily as hedging tools but may also be used to gain efficient exposure to the various asset classes. The Company primarily minimizes the risk of large losses through diversification but also monitors and manages other aspects of risk. The actual composition of the Company's other postretirement benefit plan assets as of the end of the year, along with the targeted mix of assets, is presented below:

	Target	**2008**	2007
Domestic equity	35%	**33%**	37%
International equity	23	**22**	23
Fixed income	18	**17**	17
Real estate	14	**19**	16
Private equity	10	**9**	7
Total	100%	**100%**	100%

Amounts recognized in the balance sheets related to the Company's other postretirement benefit plans consist of:

	2008	2007
	(in thousands)	
Other regulatory assets	**$ 9,922**	$ 8,040
Current liabilities, other	**(500)**	(511)
Employee benefit obligations	**(58,711)**	(52,916)

Presented below are the amounts included in regulatory assets at December 31, 2008 and 2007, related to the other postretirement benefit plans that had not yet been recognized in net periodic postretirement benefit cost along with the estimated amortization of such amounts for 2009.

	Prior Service Cost	Net (Gain) Loss	Transition Obligation
		(in thousands)	
Balance at December 31, 2008:			
Regulatory assets	**$ 3,187**	**$ 5,302**	**$ 1,433**
Balance at December 31, 2007:			
Regulatory assets	$ 3,619	$ 2,544	$ 1,877
Estimated amortization as net periodic postretirement benefit cost in 2009:			
Regulatory assets	$ 346	$ (87)	$ 356

The change in the balance of regulatory assets related to the other postretirement benefit plans for the 15-month period ended December 31, 2008 and the 12-month period ended September 30, 2007 are presented in the following table:

	Regulatory Assets
	(in thousands)
Beginning balance	$ 12,877
Net gain	(4,045)
Change in prior service costs	-
Reclassification adjustments:	
Amortization of transition obligation	(356)
Amortization of prior service costs	(346)
Amortization of net gain	(90)
Total reclassification adjustments	(792)
Total change	(4,837)
Balance at December 31, 2007	**$ 8,040**
Net gain	**2,759**
Change in prior service costs	**-**
Reclassification adjustments:	
Amortization of transition obligation	**(445)**
Amortization of prior service costs	**(432)**
Amortization of net gain	**-**
Total reclassification adjustments	**(877)**
Total change	**1,882**
Balance at December 31, 2008	**$ 9,922**

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

	2008	2007	2006
		(in thousands)	
Service cost	**$ 1,413**	$ 1,351	$ 1,424
Interest cost	**4,536**	4,330	3,940
Expected return on plan assets	**(1,452)**	(1,320)	(1,264)
Net amortization	**702**	792	857
Net postretirement cost	**$ 5,199**	$ 5,153	$ 4,957

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (Medicare Act) provides a 28% prescription drug subsidy for Medicare eligible retirees. The effect of the subsidy reduced the Company's expenses for the years ended December 31, 2008, 2007, and 2006 by approximately $1.4 million, $1.5 million, and $1.7 million, respectively.

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

	Benefit Payments	Subsidy Receipts	Total
		(in thousands)	
2009	$ 4,475	$ (378)	$ 4,097
2010	4,792	(442)	4,350
2011	5,202	(494)	4,708
2012	5,449	(565)	4,884
2013	5,689	(638)	5,051
2014 to 2018	31,319	(4,401)	26,918

Actuarial Assumptions

The weighted average rates assumed in the actuarial calculations used to determine both the benefit obligations as of the measurement date and the net periodic costs for the pension and other postretirement benefit plans for the following year are presented below. Net periodic benefit costs were calculated in 2005 for the 2006 plan year using a discount rate of 5.50%.

	2008	2007	2006
Discount	**6.75%**	6.30%	6.00%
Annual salary increase	**3.75**	3.75	3.50
Long-term return on plan assets	**8.50**	8.50	8.50

The Company determined the long-term rate of return based on historical asset class returns and current market conditions, taking into account the diversification benefits of investing in multiple asset classes.

An additional assumption used in measuring the APBO was a weighted average medical care cost trend rate of 9.15% for 2009, decreasing gradually to 5.50% through the year 2015 and remaining at that level thereafter. An annual increase or decrease in the assumed medical care cost trend rate of 1% would affect the APBO and the service and interest cost components at December 31, 2008 as follows:

	1 Percent Increase	1 Percent Decrease
	(in thousands)	
Benefit obligation	**$ 3,904**	**$ 4,211**
Service and interest costs	**275**	**236**

Employee Savings Plan

The Company also sponsors a 401(k) defined contribution plan covering substantially all employees. The Company provides an 85% matching contribution up to 6% of an employee's base salary. Prior to November 2006, the Company matched employee contributions at a rate of 75% up to 6% of the employee's base salary. Total matching contributions made to the plan for 2008, 2007, and 2006 were $3.5 million, $3.5 million, and $3.0 million, respectively.

3. CONTINGENCIES AND REGULATORY MATTERS

General Litigation Matters

The Company is subject to certain claims and legal actions arising in the ordinary course of business. In addition, the Company's business activities are subject to extensive governmental regulation related to public health and the environment. 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 and water 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 the Company cannot be predicted at this time; however, for current proceedings not specifically reported herein, management does not anticipate that the liabilities, if any, arising from such current proceedings would have a material adverse effect on the Company's financial statements.

Environmental Matters

New Source Review Actions

In November 1999, the EPA brought a civil action in the U.S. District Court for the Northern District of Georgia against certain Southern Company subsidiaries, including Alabama Power and Georgia Power, alleging that these subsidiaries had violated the New Source Review (NSR) provisions of the Clean Air Act and related state laws at certain coal-fired generating facilities. The EPA concurrently issued notices of violation relating to the Company's Plant Crist and a unit at Georgia Power's Plant Scherer that is partially owned by the Company. In early 2000, the EPA filed a motion to amend its complaint to add the allegations in the notice of violation and to add the Company as a defendant. However, in March 2001, the court denied the motion based on lack of jurisdiction, and the EPA has not refiled. After Alabama Power was dismissed from the original action for jurisdictional reasons, the EPA filed a separate action in January 2001 against Alabama Power in the U.S. District Court for the Northern District of Alabama. In these lawsuits, the EPA alleged that NSR violations occurred at eight coal-fired generating facilities operated by Alabama Power and Georgia Power. The civil actions request penalties and injunctive relief, including an order requiring installation of the best available control technology at the affected units. The action against Georgia Power has been administratively closed since the spring of 2001, and the case has not been reopened.

In June 2006, the U.S. District Court for the Northern District of Alabama entered a consent decree between Alabama Power and the EPA, resolving a portion of the Alabama Power lawsuit relating to the alleged NSR violations at Plant Miller. The consent decree required Alabama Power to pay $100,000 to resolve the government's claim for a civil penalty and to donate $4.9 million of sulfur dioxide emission allowances to a nonprofit charitable organization. It also formalized specific emissions reductions to be accomplished by Alabama Power, consistent with other Clean Air Act programs that require emissions reductions. In August 2006, the district court in Alabama granted Alabama Power's motion for summary judgment and entered final judgment in favor of Alabama Power on the EPA's claims related to all of the remaining plants: Plants Barry, Gaston, Gorgas, and Greene County.

The plaintiffs appealed the district court's decision to the U.S. Court of Appeals for the Eleventh Circuit, where it was stayed, pending the U.S. Supreme Court's decision in a similar case against Duke Energy. The Supreme Court issued its decision in the Duke Energy case in April 2007, and in December 2007, the Eleventh Circuit vacated the district court's decision in the Alabama Power case and remanded the case back to the district court for consideration of the legal issues in light of the Supreme Court's decision in the Duke Energy case. On July 24, 2008, the U.S. District Court for the Northern District of Alabama granted partial summary judgment in favor of Alabama Power regarding the proper legal test for determining whether projects are routine maintenance, repair, and replacement and therefore are excluded from NSR permitting. The ultimate outcome of these matters cannot be determined at this time.

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

Carbon Dioxide Litigation

New York Case

In July 2004, three environmental groups and attorneys general from eight states, each outside of Southern Company's service territory, and the corporation counsel for New York City filed complaints in the U.S. District Court for the Southern District of New York against Southern Company and four other electric power companies. The complaints allege that the companies' emissions of carbon dioxide, a greenhouse gas, contribute to global warming, which the plaintiffs assert is a public nuisance. Under common law public and private nuisance theories, the plaintiffs seek a judicial order (1) holding each defendant jointly and severally liable for creating, contributing to, and/or maintaining global warming and (2) requiring each of the defendants to cap its emissions of carbon dioxide and then reduce those emissions by a specified percentage each year for at least a decade. The plaintiffs have not, however, requested that damages be awarded in connection with their claims. Southern Company believes these claims are without merit and notes that the complaint cites no statutory or regulatory basis for the claims. In September 2005, the U.S. District Court for the Southern District of New York granted Southern Company's and the other defendants' motions to dismiss these cases. The plaintiffs filed an appeal to the U.S. Court of Appeals for the Second Circuit in October 2005, but no decision has been issued. The ultimate outcome of these matters cannot be determined at this time.

Kivalina Case

On February 26, 2008, the Native Village of Kivalina and the City of Kivalina filed a suit in the U.S. District Court for the Northern District of California against several electric utilities (including Southern Company), several oil companies, and a coal company. The plaintiffs are the governing bodies of an Inupiat village in Alaska. The plaintiffs contend that the village is being destroyed by erosion allegedly caused by global warming that the plaintiffs attribute to emissions of greenhouse gases by the defendants. The plaintiffs assert claims for public and private nuisance and contend that the defendants have acted in concert and are therefore jointly and severally liable for the plaintiffs' damages. The suit seeks damages for lost property values and for the cost of relocating the village, which is alleged to be $95 million to $400 million. On June 30, 2008, all defendants filed motions to dismiss this case. Southern Company believes that these claims are without merit and notes that the complaint cites no statutory or regulatory basis for the claims. The ultimate outcome of this matter cannot be determined at this time.

Environmental Remediation

The Company must comply with other environmental laws and regulations that cover the handling and disposal of waste and releases of hazardous substances. Under these various laws and regulations, the Company may also incur substantial costs to clean up properties. The Company received authority from the Florida PSC to recover approved environmental compliance costs through the environmental cost recovery clause. The Florida PSC reviews costs and adjusts rates up or down annually.

The Company's environmental remediation liability includes estimated costs of environmental remediation projects of approximately $66.8 million as of December 31, 2008. These estimated costs relate to site closure criteria by the Florida Department of Environmental Protection (FDEP) for potential impacts to soil and groundwater from herbicide applications at the Company's substations. The schedule for completion of the remediation projects will be subject to FDEP approval. The projects have been approved by the Florida PSC for recovery through the Company's environmental cost recovery clause; therefore, there is no impact to net income as a result of these liabilities.

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

FERC Matters

Market-Based Rate Authority

The Company has authorization from the FERC to sell power to non-affiliates, including short-term opportunity sales, at market-based prices. Specific FERC approval must be obtained with respect to a market-based contract with an affiliate.

In December 2004, the FERC initiated a proceeding to assess Southern Company's generation dominance within its retail service territory. The ability to charge market-based rates in other markets is not an issue in the proceeding. Any new market-based rate sales by the Company in Southern Company's retail service territory entered into during a 15-month refund period that ended in May 2006 could be subject to refund to a cost-based rate level.

In November 2007, the presiding administrative law judge issued an initial decision regarding the methodology to be used in the generation dominance tests. The proceedings are ongoing. The ultimate outcome of this generation dominance proceeding cannot now be determined, but an adverse decision by the FERC in a final order could require the Company to charge cost-based rates for certain wholesale sales in the Southern Company retail service territory, which may be lower than negotiated market-based rates, and could also result in total refunds of up to $0.8 million, plus interest. The Company believes that there is no meritorious basis for an adverse decision in this proceeding and is vigorously defending itself in this matter.

In June 2007, the FERC issued its final rule in Order No. 697 regarding market-based rate authority. The FERC generally retained its current market-based rate standards. Responding to a number of requests for rehearing, the FERC issued Order No. 697-A on April 21, 2008 and Order No. 697-B on December 12, 2008. These orders largely affirmed the FERC's prior revision and codification of the regulations governing market-based rates for public utilities. In accordance with the orders, Southern Company submitted to the FERC an updated market power analysis on September 2, 2008 related to its continued market-based rate authority. The ultimate outcome of this matter cannot now be determined.

On October 17, 2008, Southern Company filed with the FERC a revised market-based rate (MBR) tariff and a new cost-based rate (CBR) tariff. The revised MBR tariff provides for a "must offer" energy auction whereby Southern Company, offers all of its available energy for sale in a day-ahead auction and an hour-ahead auction with reserve prices not to exceed the CBR tariff price, after considering Southern Company's native load requirements, reliability obligations, and sales commitments to third parties. All sales under the energy auction would be at market clearing prices established under the auction rules. The new CBR tariff provides for a cost-based price for wholesale sales of less than a year. On December 18, 2008, the FERC issued an order conditionally accepting the MBR tariff subject to certain revisions to the auction proposal. On January 21, 2009, Southern Company made a compliance filing that accepted all the conditions of the MBR tariff order. When this order becomes final, Southern Company will have 30 days to implement the wholesale auction. On December 31, 2008, the FERC issued an order conditionally accepting the CBR tariff subject to providing additional information concerning one aspect of the tariff. On January 30, 2009, Southern Company filed a response addressing the FERC inquiry to the CBR tariff order. Implementation of the energy auction in accordance with the MBR tariff order is expected to adequately mitigate going forward any presumption of market power that Southern Company may have in the Southern Company retail service territory. The timing of when FERC may issue the final orders on the MBR and CBR tariffs and the ultimate outcome of these matters cannot be determined at this time.

Intercompany Interchange Contract

The Company's generation fleet is operated under the Intercompany Interchange Contract (IIC), as approved by the FERC. In May 2005, the FERC initiated a new proceeding to examine (1) the provisions of the IIC among the traditional operating companies (including the Company), Southern Power, and SCS, as agent, under the terms of which the power pool of Southern Company is operated, (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. In connection with the formation of Southern Power, the FERC authorized Southern Power's inclusion in the IIC in 2000. The FERC also previously approved Southern Company's code of conduct.

In October 2006, the FERC issued an order accepting a settlement resolving the proceeding subject to Southern Company's agreement to accept certain modifications to the settlement's terms and Southern Company notified the FERC that it accepted the modifications. The modifications largely involve functional separation and information restrictions related to marketing activities conducted on behalf of Southern Power. In November 2006, Southern Company filed with the FERC a compliance plan in connection with the order. In April 2007, the FERC approved, with certain modifications, the plan submitted by Southern Company. Implementation of the plan did not have a material impact on the Company's financial statements. In November 2007 Southern Company notified the FERC that the plan had been implemented. On December 12, 2008 the FERC division of audits issued for public comment its final audit report pertaining to compliance implementation and related matters. No comments challenging the audits report's findings were submitted. A decision is now pending from the FERC.

Retail Regulatory Matters

Fuel Cost Recovery

The Company petitions for fuel cost recovery rates to be approved by the Florida PSC on an annual basis. The Company continuously monitors the under recovered fuel cost balance in light of the inherent variability in fuel costs. If the projected fuel cost over or under recovery exceeds 10% of the projected fuel revenue applicable for the period, the Company is required to notify the Florida PSC and indicate if an adjustment to the fuel cost recovery is being requested.

On July 29, 2008, the Florida PSC approved a request by the Company to increase the fuel cost recovery factor effective with billings beginning September 2008. The remaining portion of the projected under recovered balance is expected to be recovered in 2009. On September 2, 2008, the Company filed its 2009 projected fuel cost recovery filing with the Florida PSC which includes the fuel factors proposed for January 2009 through December 2009. On October 13, 2008, the Company notified the Florida PSC that the updated projected fuel cost under recovery balance at year-end exceeds the 10% threshold, but no adjustment to the fuel factors were requested.

On November 6, 2008, the Florida PSC approved an increase of approximately 12.9% in the fuel factor for retail customers, effective with billings beginning January 2009. The fuel factors are intended to allow the Company to recover its projected 2009 fuel and purchased power costs as well as the 2008 under recovered amounts in 2009. Fuel cost recovery revenues, as recorded on the financial statements, are adjusted for differences in actual recoverable costs and amounts billed in current regulated rates. Accordingly, changing the billing factor has no significant effect on the Company's revenues or net income, but does impact annual cash flow. As of December 31, 2008, the Company had an under recovered fuel balance of approximately $97 million, which is included in current assets in the balance sheets.

Environmental Cost Recovery

The Florida Legislature adopted legislation for an environmental cost recovery clause, which allows an electric utility to petition the Florida PSC for recovery of prudent environmental compliance costs that are not being recovered through base rates or any other recovery mechanism. Such environmental costs include operation and maintenance expense, emission allowance expense, depreciation, and a return on invested capital. This legislation also allows recovery of costs incurred as a result of an agreement between the Company and the FDEP for the purpose of ensuring compliance with ozone ambient air quality standards adopted by the EPA. In August 2007, the Florida PSC voted to approve a stipulation among the Company, the Office of Public Counsel, and the Florida Industrial Power Users Group regarding the Company's plan for complying with certain federal and state regulations addressing air quality. The Company's environmental compliance plan as filed in March 2007 contemplates implementation of specific projects identified in the plan from 2007 through 2018. The stipulation covers all elements of the current plan that are scheduled to be implemented in the 2007 through 2011 timeframe. On September 18, 2008, the Company filed an update to the plan which was approved by the Florida PSC on November 4, 2008. The Florida PSC acknowledged that the costs associated with the Company's Clean Air Interstate Rule/Clean Air Mercury Rule/Clean Air Visibility Rule compliance plan are eligible for recovery through the environmental cost recovery clause. During 2008, 2007, and 2006, the Company recorded environmental cost recovery clause revenues of $50.0 million, $43.6 million, and $40.9 million, respectively. Annually, the Company seeks recovery of projected costs including any true-up amounts from prior periods. At December 31, 2008, the over recovered balance was approximately $71,000.

Storm Damage Cost Recovery

Under authority granted by the Florida PSC, the Company maintains a reserve for property damage to cover the cost of uninsured damages from major storms to its transmission and distribution facilities, generation facilities, and other property.

In July 2006, the Florida PSC issued an order (2006 Order) approving a stipulation and settlement between the Company and several consumer groups that resolved all matters relating to the Company's request for recovery of incurred costs for storm-recovery activities and the replenishment of the Company's property damage reserve. The 2006 Order provided for an extension of the storm-recovery surcharge then being collected by the Company for an additional 27 months, expiring in June 2009.

Funds collected by the Company related to the storm-recovery costs associated with previous hurricanes had been fully recovered by August 2008. Funds collected by the Company through its storm-recovery surcharge are now being credited to the property damage reserve and will continue through June 2009 when the approved surcharge ends.

According to the 2006 Order, in the case of future storms, if the Company incurs cumulative costs for storm-recovery activities in excess of $10 million during any calendar year, the Company will be permitted to file a streamlined formal request for an interim surcharge. Any interim surcharge would provide for the recovery, subject to refund, of up to 80% of the claimed costs for storm-recovery activities. The Company would then petition the Florida PSC for full recovery through a final or non-interim surcharge or other cost recovery mechanism.

See Note 1 under “Property Damage Reserve” for additional information.

4. JOINT OWNERSHIP AGREEMENTS

The Company and Mississippi Power jointly own Plant Daniel Units 1 and 2, which together represent capacity of 1,000 megawatts. Plant Daniel is a generating plant located in Jackson County, Mississippi. In accordance with the operating agreement, Mississippi Power acts as the Company’s agent with respect to the construction, operation, and maintenance of these units.

The Company and Georgia Power jointly own the 818 megawatts capacity Plant Scherer Unit 3. Plant Scherer is a generating plant located near Forsyth, Georgia. In accordance with the operating agreement, Georgia Power acts as the Company’s agent with respect to the construction, operation, and maintenance of the unit.

The Company’s pro rata share of expenses related to both plants is included in the corresponding operating expense accounts in the statements of income and the Company is responsible for providing its own financing.

At December 31, 2008, the Company’s percentage ownership and its investment in these jointly owned facilities were as follows:

	Plant Scherer Unit 3 (coal)	**Plant Daniel Units 1 & 2 (coal)**
	(in thousands)	
Plant in service	**$ 191,688**[(a)]	**$ 261,078**
Accumulated depreciation	**97,937**	**146,690**
Construction work in progress	**75,760**	**253**
Ownership	**25%**	**50%**

(a) Includes net plant acquisition adjustment of $3.3 million.

5. INCOME TAXES

Southern Company files a consolidated federal income tax return and combined State of Mississippi and State of Georgia income tax returns. Under a joint consolidated income tax allocation agreement, each subsidiary’s current and deferred tax expense is computed on a stand-alone basis and no subsidiary is allocated more expense than would be paid if it filed a separate income tax return. In accordance with Internal Revenue Service (IRS) regulations, each company is jointly and severally liable for the tax liability.

Current and Deferred Income Taxes

Details of income tax provisions are as follows:

	2008	2007	2006
		(in thousands)	
Federal –			
Current	**$ 26,592**	$ 51,321	$ 40,472
Deferred	**21,481**	(9,431)	(470)
	48,073	41,890	40,002
State –			
Current	**3,563**	6,581	3,651
Deferred	**2,467**	(1,388)	1,640
	6,030	5,193	5,291
Total	**$ 54,103**	$ 47,083	$ 45,293

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

	2008	2007
	(in thousands)	
Deferred tax liabilities–		
Accelerated depreciation	**$ 284,653**	$ 260,720
Fuel recovery clause	**39,176**	22,934
Pension and other employee benefits	**15,356**	38,109
Property reserve	**-**	6,624
Regulatory assets associated with employee benefit obligations	**34,787**	9,206
Regulatory assets associated with asset retirement obligations	**4,877**	4,837
Other	**3,747**	3,316
Total	**382,596**	345,746
Deferred tax assets–		
Federal effect of state deferred taxes	**$ 14,039**	$ 13,168
Post retirement benefits	**17,428**	16,371
Pension and other employee benefits	**38,156**	11,880
Property reserve	**4,872**	-
Other comprehensive loss	**3,097**	2,386
Regulatory liabilities associated with employee benefit obligations	**-**	23,192
Asset retirement obligations	**4,877**	4,837
Other	**7,003**	12,126
Total	**89,472**	83,960
Net deferred tax liabilities	**293,124**	261,786
Less current portion, net	**(38,770)**	(21,685)
Accumulated deferred income taxes in the balance sheets	**$ 254,354**	$ 240,101

At December 31, 2008, the tax-related regulatory assets to be recovered from customers were $24.2 million. These assets are attributable to tax benefits flowed through to customers in prior years and to taxes applicable to capitalized allowance for funds used during construction. At December 31, 2008, the tax-related regulatory liabilities to be credited to customers were $13.0 million. These liabilities are attributable to deferred taxes previously recognized at rates higher than the current enacted tax law and to unamortized investment tax credits.

In accordance with regulatory requirements, deferred investment tax credits are amortized over the lives of the related property with such amortization normally applied as a credit to reduce depreciation in the statements of income. Credits amortized in this manner amounted to $1.7 million in 2008, $1.7 million in 2007, and $1.8 million in 2006. At December 31, 2008, all investment tax credits available to reduce federal income taxes payable had been utilized.

Effective Tax Rate

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

	2008	2007	2006
Federal statutory rate	**35.0%**	35.0%	35.0%
State income tax, net of federal deduction	**2.5**	2.5	2.8
Non-deductible book depreciation	**0.0**	0.4	0.5
Difference in prior years' deferred and current tax rate	**(0.5)**	(0.6)	(0.8)
Production activities deduction	**0.1**	(1.4)	(0.3)
Allowance for funds used during construction	**(2.2)**	(0.6)	0.0
Other, net	**(0.8)**	(0.4)	(0.8)
Effective income tax rate	**34.1%**	34.9%	36.4%

The decrease in the 2008 effective tax rate is primarily the result of an increase in nontaxable allowance for equity funds used during construction.

The American Jobs Creation Act of 2004 created a tax deduction for a portion of income attributable to U.S. production activities as defined in Internal Revenue Code Section 199 (production activities deduction). The deduction is equal to a stated percentage of qualified production activities net income. 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 thereafter. The increase from 3% in 2006 to 6% in 2007 was one of several factors that increased the Company's 2007 deduction by $4 million over the 2006 deduction. The resulting additional tax benefit was over $1 million. The IRS has not clearly defined a methodology for calculating this deduction. However, Southern Company has agreed with the IRS on a calculation methodology and signed a closing agreement on December 11, 2008. Therefore, the Company reversed the unrecognized tax benefit and adjusted the deduction for all previous years to conform to the agreement which resulted in a decrease in the 2008 deduction when compared to the 2007 deduction. The net impact of the reversal of unrecognized tax benefits combined with the true-up to the new methodology was immaterial.

Unrecognized Tax Benefits

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. For 2008, the total amount of unrecognized tax benefits decreased by $0.6 million, resulting in a balance of $0.3 million as of December 31, 2008.

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

	2008	2007
	(thousands)	
Unrecognized tax benefits at beginning of year	**$ 887**	$ 211
Tax positions from current periods	**93**	469
Tax positions from prior periods	**11**	207
Reductions due to settlements	**(697)**	-
Reductions due to expired statute of limitations	**-**	-
Balance at end of year	**$ 294**	$ 887

The reduction due to settlements relates to the agreement with the IRS regarding the production activities deduction methodology. See "Effective Tax Rate" above for additional information.

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

	2008	2007	Change
		(thousands)	
Tax positions impacting the effective tax rate	**$ 294**	$ 887	$ 593
Tax positions not impacting the effective tax rate	**-**	-	-
Balance of unrecognized tax benefits	**$ 294**	$ 887	$ 593

Accrued interest for unrecognized tax benefits:

	2008	2007
	(thousands)	
Interest accrued at beginning of year	**$ 58**	$ 5
Interest reclassified due to settlements	**(54)**	-
Interest accrued during the year	**13**	53
Balance at end of year	**$ 17**	$ 58

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

The IRS has audited and closed all tax returns prior to 2004. The audits for the state returns have either been concluded, or the statute of limitations has expired, for years prior to 2002.

It is reasonably possible that the amount of the unrecognized benefit with respect to the majority of the Company's unrecognized tax positions will significantly increase or decrease within the next 12 months. The possible conclusion or settlement of federal or state audits could impact the balances significantly. At this time, an estimate of the range of reasonably possible outcomes cannot be determined.

6. FINANCING

Long-Term Debt Payable to Affiliated Trusts

The Company has formed certain wholly owned trust subsidiaries for the purpose of issuing preferred securities. The proceeds of the related equity investments and preferred security sales were loaned back to the Company through the issuance of junior subordinated notes which constitute substantially all of the assets of these trusts and are reflected in the balance sheets as Long-Term Debt. The Company considers that the mechanisms and obligations relating to the preferred securities issued for its benefit, taken together, constitute a full and unconditional guarantee by it of the trusts' payment obligations with respect to these securities. During 2007, the Company redeemed its last remaining series, which totaled $41.2 million. See Note 1 under "Variable Interest Entities" for additional information on the accounting treatment for these trusts and the related securities.

Bank Term Loans

In 2008, the Company borrowed $110 million under a three-year term loan agreement and $50 million under a short-term loan agreement. The proceeds of these issuances were used for general corporate purposes, including the Company's continuous construction program.

Senior Notes

At December 31, 2008 and 2007, the Company had a total of $588.7 million and $590.0 million of senior notes outstanding, respectively. These senior notes are subordinate to all secured debt of the Company which amounts to approximately $41 million at December 31, 2008.

Pollution Control Revenue Bonds

Pollution control obligations represent loans to the Company from public authorities of funds derived from sales by such authorities of revenue bonds issued to finance pollution control facilities. The Company has $157.6 million of outstanding pollution control revenue bonds and is required to make payments sufficient for the authorities to meet principal and interest requirements of such bonds.

Outstanding Classes of Capital Stock

The Company currently has preferred stock, Class A preferred stock, preference stock, and common stock authorized. The Company's preferred stock and Class A preferred stock, without preference between classes, rank senior to the Company's preference stock and common stock with respect to payment of dividends and voluntary or involuntary dissolution. No shares of preferred stock or Class A preferred stock were outstanding at December 31, 2008. The Company's preference stock ranks senior to the common stock with respect to the payment of dividends and voluntary or involuntary dissolution. Certain series of the preference stock are subject to redemption at the option of the Company on or after a specified date (typically 5 or 10 years after the date of issuance) at a redemption price equal to 100% of the liquidation amount of the preference stock. In addition, one series of the preference stock may be redeemed earlier at a redemption price equal to 100% of the liquidation amount plus a make-whole premium based on the present value of the liquidation amount and future dividends.

In January 2007, the Company issued to Southern Company 800,000 shares of the Company's common stock, without par value, and realized proceeds of $80 million. The proceeds were used to repay a portion of the Company's short-term indebtedness and for other general corporate purposes. Subsequent to December 31, 2008, the Company issued to Southern Company 1,350,000 shares of the Company's common stock, without par value, and realized proceeds of $135 million.

Dividend Restrictions

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

Assets Subject to Lien

In January 2007, the Company's first mortgage bond indenture was discharged. As a result, there are no longer any first mortgage liens on the Company's property and the Company no longer has to comply with the covenants and restrictions of the first mortgage bond indenture. The Company has granted a lien on its property at Plant Daniel in connection with the issuance of two series of pollution control bonds with an outstanding principal amount of $41 million.

There are no agreements or other arrangements among the affiliated companies under which the assets of one company have been pledged or otherwise made available to satisfy obligations of Southern Company or any of its subsidiaries.

Bank Credit Arrangements

At December 31, 2008, the Company had $120 million of lines of credit with banks, all of which remained unused. These bank credit arrangements will expire in 2009 and $90 million contain provisions allowing one-year term loans executable at expiration. Of the $120 million, $116 million provides liquidity support for the Company's commercial paper program and $4 million provides support for variable rate pollution control bonds. Subsequent to December 31, 2008, the Company obtained an additional $20 million of committed credit. Commitment fees average less than 1/4 of 1% for the Company.

Certain credit arrangements contain covenants that limit the level of indebtedness to capitalization to 65%, as defined in the arrangements. At December 31, 2008, the Company was in compliance with these covenants.

In addition, certain credit arrangements contain cross default provisions to other indebtedness that would trigger an event of default if the Company defaulted on indebtedness over a specified threshold. The cross default provisions are restricted only to indebtedness of the Company. The Company is currently in compliance with all such covenants.

The Company borrows primarily through a commercial paper program that has the liquidity support of committed bank credit arrangements. The Company may also borrow through various other arrangements with banks. At December 31, 2008, the Company had $89.9 million of commercial paper and $50 million of bank notes outstanding. At December 31, 2007, the Company had $40.8 million of commercial paper outstanding. During 2008, the peak amount outstanding for short term debt was $141.2 million and the average amount outstanding was $36.9 million. The average annual interest rate on commercial paper was 2.2%.

Financial Instruments

The Company enters into energy-related derivatives to hedge exposures to electricity, gas, and other fuel price changes. However, due to cost-based rate regulations, the Company has limited exposure to market volatility in commodity fuel prices and prices of electricity. The Company has implemented a fuel-hedging program per the guidelines of the Florida PSC. The Company enters into hedges of forward electricity sales.

At December 31, 2008 and 2007, the Company had a net $31.2 million and $0.2 million fair value liability, respectively, of energy-related derivative contracts designated as regulatory hedges in the financial statements.

The gains and losses arising from these regulatory hedges are initially recorded as regulatory liabilities and assets, respectively, and then are included in fuel expense as they are recovered through the fuel cost recovery clause. There was no ineffectiveness recorded in the earnings for any period presented. The Company has energy-related hedges in place up to and including 2011.

The Company also enters into derivatives to hedge exposure to changes in interest rates. Derivatives related to forecasted transactions are accounted for as cash flow hedges and will be terminated at the time the underlying debt is issued. The derivatives employed as hedging instruments are structured to minimize ineffectiveness. As such, no ineffectiveness has been recorded in earnings for any period presented. At December 31, 2008, the Company had no interest rate derivatives outstanding.

The fair value gains or losses for cash flow hedges are recorded in other comprehensive income and are reclassified into earnings at the same time the hedged items affect earnings. In 2008, 2007, and 2006, the Company settled gains/(losses) totaling $(5.2) million,

$3.0 million, and $(5.4) million, respectively, upon termination of certain interest derivatives at the same time it issued debt. The effective portion of these gains/(losses) have been deferred in other comprehensive income and will be amortized to interest expense over the life of the original interest derivative. For the years 2008, 2007, and 2006, approximately $0.9 million, $0.7 million, and $0.4 million, respectively, of pre-tax losses were reclassified from other comprehensive income to interest expense. For 2009, pre-tax losses of approximately $1.1 million are expected to be reclassified from other comprehensive income to interest expense. The Company has deferred realized net losses that are being amortized through 2018.

All derivative financial instruments are recognized as either assets or liabilities and are measured at fair value. See Note 9 for additional information.

7. COMMITMENTS

Construction Program

The Company is engaged in a continuous construction program, the cost of which is currently estimated to total $478 million in 2009, $337 million in 2010, and $400 million in 2011. The construction programs are subject to periodic review and revision, and actual construction costs may vary from these estimates because of numerous factors. These factors include: changes in business conditions; revised load growth estimates; storm impacts; changes in environmental statutes and regulations; changes in FERC rules and regulations; Florida PSC approvals; the cost and efficiency of construction labor, equipment, and materials; and the cost of capital. In addition, there can be no assurance that costs related to capital expenditures will be fully recovered. At December 31, 2008, significant purchase commitments were outstanding in connection with the ongoing construction program.

Included in the amounts above are $335 million in 2009, $164 million in 2010, and $233 million in 2011 for environmental expenditures. The Company does not have any new generating capacity under construction. Construction of new transmission and distribution facilities and other capital improvements, including those needed to meet environmental standards for the Company's existing generation, transmission, and distribution facilities, are ongoing.

Long-Term Service Agreements

The Company has a Long-Term Service Agreement (LTSA) with General Electric (GE) for the purpose of securing maintenance support for a combined cycle generating facility. The LTSA provides that GE will perform all planned inspections on the covered equipment, which generally includes the cost of all labor and materials. GE is also obligated to cover the costs of unplanned maintenance on the covered equipment subject to limits and scope specified in the LTSA.

In general, the LTSA is in effect through two major inspection cycles of the unit. Scheduled payments to GE, which are subject to price escalation, are made at various intervals based on actual operating hours of the unit. Total remaining payments to GE under the LTSA for facilities owned are currently estimated at $62.5 million over the remaining life of the LTSA, which is currently estimated to be up to 9 years. However, the LTSA contains various cancellation provisions at the option of the Company.

Payments made under the LTSA prior to the performance of any planned inspections are recorded as prepayments. These amounts are included in Current Assets and Deferred Charges and Other Assets in the balance sheets, for 2008 and 2007, respectively. Inspection costs are capitalized or charged to expense based on the nature of the work performed.

Limestone Commitments

As part of the Company's program to reduce sulfur dioxide emissions from certain of its coal plants, the Company has begun construction of flue gas desulfurization projects and has entered into various long-term commitments for the procurement of limestone to be used in such equipment. Limestone contracts are structured with tonnage minimums and maximums in order to account for fluctuations in coal burn and sulfur content. The Company has a minimum contractual obligation of 0.8 million tons equating to approximately $63.8 million, through 2019. Estimated expenditures (based on minimum contracted obligated dollars) over the next five years are none in 2009, $5.7 million in 2010, $5.8 million in 2011, $6.0 million in 2012, and $6.1 million in 2013. Limestone costs are expected to be recovered through the environmental cost recovery clause.

Fuel and Purchased Power Commitments

To supply a portion of the fuel requirements of the generating plants, the Company has entered into various long-term commitments for the procurement of fossil fuel. In most cases, these contracts contain provisions for price escalations, minimum purchase levels, and other financial commitments. Coal commitments include forward contract purchases for sulfur dioxide and nitrogen oxide emission allowances. Natural gas purchase commitments contain fixed volumes with prices based on various indices at the time of delivery; amounts included in the chart below represent estimates based on New York Mercantile Exchange future prices at December 31, 2008. Also, the Company has entered into various long-term commitments for the purchase of capacity, electricity, and transmission.

Total estimated minimum long-term obligations at December 31, 2008 were as follows:

	Commitments		
	Purchased Power*	Natural Gas	Coal
		(in thousands)	
2009	$ 23,007	$ 112,618	$ 282,370
2010	26,811	85,713	158,520
2011	26,861	42,607	23,966
2012	26,927	20,149	-
2013	27,070	20,127	-
2014 and thereafter	3,918	151,016	-
Total	$ 134,594	$ 432,230	$ 464,856

*Included above is $81 million in obligations with affiliated companies.

Additional commitments for fuel will be required to supply the Company's future needs.

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

Operating Leases

The Company has operating lease agreements with various terms and expiration dates. Total operating lease expenses were $5.0 million, $4.7 million, and $4.9 million, for 2008, 2007, and 2006, respectively. Included in these lease expenses are railcar lease costs which are charged to fuel inventory and are allocated to fuel expense as the fuel is used. These expenses are then recovered through the Company's fuel cost recovery clause. The Company's share of the lease costs charged to fuel inventories was $4.0 million in 2008, $4.4 million in 2007, and $4.6 million in 2006. The Company includes any step rents, escalations, and lease concessions in its computation of minimum lease payments, which are recognized on a straight-line basis over the minimum lease term.

At December 31, 2008, estimated minimum rental commitments for noncancelable operating leases were as follows:

	Minimum Lease Payments		
	Rail Cars	Other	Total
		(in thousands)	
2009	$ 3,547	$ 2,002	$ 5,549
2010	3,545	1,877	5,422
2011	1,822	1,820	3,642
2012	1,229	219	1,448
2013	904	-	904
2014 and thereafter	2,223	-	2,223
Total	$ 13,270	$ 5,918	$ 19,188

The Company and Mississippi Power jointly entered into operating lease agreements for aluminum railcars for the transportation of coal to Plant Daniel. The Company has the option to purchase the railcars at the greater of lease termination value or fair market value or to renew the leases at the end of each lease term. The Company and Mississippi Power also have separate lease agreements for other railcars that do not include purchase options.

In addition to railcar leases, the Company has other operating leases for fuel handling equipment at Plant Daniel. The Company's share of these leases was charged to fuel handling expense in the amount of $0.3 million in 2008. The Company's annual lease payments for 2009 to 2010 will average approximately $0.1 million.

8. STOCK OPTION PLAN

Southern Company provides non-qualified stock options to a large segment of the Company's employees ranging from line management to executives. As of December 31, 2008, there were 292 current and former employees of the Company participating in the stock option plan, and there were 33.2 million shares of common stock remaining available for awards under this plan. The prices of options granted to date have been at the fair market value of the shares on the dates of grant. Options granted to date become exercisable pro rata over a maximum period of three years from the date of grant. The Company generally recognizes stock option expense on a straight-line basis over the vesting period which equates to the requisite service period; however, for employees who are eligible for retirement the total cost is expensed at the grant date. Options outstanding will expire no later than 10 years after the date of grant, unless terminated earlier by the Southern Company Board of Directors in accordance with the stock option plan. For certain stock option awards a change in control will provide accelerated vesting.

The estimated fair values of stock options granted in 2008, 2007, and 2006 were derived using the Black-Scholes stock option pricing model. Expected volatility was based on historical volatility of Southern Company's stock over a period equal to the expected term. The Company used historical exercise data to estimate the expected term that represents the period of time that options granted to employees are expected to be outstanding. The risk-free rate was based on the U.S. Treasury yield curve in effect at the time of grant that covers the expected term of the stock options. The following table shows the assumptions used in the pricing model and the weighted average grant-date fair value of stock options granted:

Year Ended December 31	**2008**	2007	2006
Expected volatility	**13.1%**	14.8%	16.9%
Expected term *(in years)*	**5.0**	5.0	5.0
Interest rate	**2.8%**	4.6%	4.6%
Dividend yield	**4.5%**	4.3%	4.4%
Weighted average grant-date fair value	**$ 2.37**	$ 4.12	$ 4.15

The Company's activity in the stock option plan for 2008 is summarized below:

	Shares Subject to Option	**Weighted Average Exercise Price**
Outstanding at December 31, 2007	**1,225,355**	**$ 31.01**
Granted	**239,507**	**35.79**
Exercised	**(184,865)**	**28.56**
Cancelled	**(232)**	**35.78**
Outstanding at December 31, 2008	**1,279,765**	**32.25**
Exercisable at December 31, 2008	**818,636**	**$ 30.31**

The number of stock options vested, and expected to vest in the future, as of December 31, 2008 was not significantly different from the number of stock options outstanding at December 31, 2008 as stated above. As of December 31, 2008, the weighted average remaining contractual term for the options outstanding and options exercisable was 6.3 years and 5.1 years, respectively, and the aggregate intrinsic value for the options outstanding and options exercisable was $6.1 million and $5.5 million, respectively.

As of December 31, 2008, there was $0.4 million of total unrecognized compensation cost related to stock option awards not yet vested. That cost is expected to be recognized over a weighted average period of approximately 8 months.

For the years ended December 31, 2008, 2007, and 2006, total compensation cost for stock option awards recognized in income was $0.8 million, $1.1 million, and $1.0 million, respectively, with the related tax benefit also recognized in income of $0.3 million, $0.4 million, and $0.4 million, respectively.

The compensation cost and tax benefits related to the grant and exercise of Southern Company stock options to the Company's employees are recognized in the Company's financial statements with a corresponding credit to equity, representing a capital contribution from Southern Company.

The total intrinsic value of options exercised during the years ended December 31, 2008, 2007, and 2006 was $1.3 million, $3.0 million, and $1.6 million, respectively. The actual tax benefit realized by the Company for the tax deductions from stock option exercises for the years ended December 31, 2008, 2007, and 2006 totaled $0.5 million, $1.1 million, and $0.6 million, respectively.

9. FAIR VALUE MEASUREMENTS

On January 1, 2008, the Company adopted FASB Statement No. 157, "Fair Value Measurements" (SFAS No. 157) which defines fair value, establishes a framework for measuring fair value, and requires additional disclosures about fair value measurements. The criterion that is set forth in SFAS No. 157 is applicable to fair value measurement where it is permitted or required under other accounting pronouncements.

SFAS No. 157 defines fair value as the exit price, which is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on inputs of observable and unobservable market data that a market participant would use in pricing the asset or liability. The use of observable inputs is maximized where available and the use of unobservable inputs is minimized for fair value measurement. As a means to illustrate the inputs used, SFAS No. 157 establishes a three-tier fair value hierarchy that prioritizes inputs to valuation techniques used for fair value measurement.

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

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

The adoption of SFAS No. 157 has not resulted in any significant changes to the methodologies used for fair value measurement. Primarily all the changes in the fair value of assets and liabilities are recorded in other comprehensive income or regulatory assets and liabilities, and thus the impact on earnings is limited to derivatives that do not qualify for hedge accounting.

The fair value measurements performed on a recurring basis and the level of the fair value hierarchy in which they fall at December 31, 2008 are as follows:

At December 31, 2008:	Level 1	Level 2	Level 3	Total
		(in millions)		
Assets:				
Energy-related derivatives total fair value	$ -	$ 1.0	$ -	$ 1.0
Liabilities:				
Energy-related derivatives total fair value	$ -	$ 32.2	$ -	$ 32.2

Energy-related derivatives primarily consist of over-the-counter contracts. See Note 6 under "Financial Instruments" for additional information. These financial instruments and investments are valued primarily using the market approach.

10. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Summarized quarterly financial data for 2008 and 2007 are as follows:

Quarter Ended	Operating Revenues	Operating Income	Net Income After Dividends on Preference Stock
		(in thousands)	
March 2008	**$ 311,535**	**$ 40,708**	**$ 19,530**
June 2008	**349,867**	**52,314**	**26,992**
September 2008	**421,841**	**69,039**	**37,343**
December 2008	**303,960**	**30,628**	**14,480**
March 2007	$ 296,233	$ 40,775	$ 18,863
June 2007	298,394	45,017	21,275
September 2007	376,556	64,999	34,163
December 2007	288,625	25,125	9,817

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

SELECTED FINANCIAL AND OPERATING DATA 2004-2008

Gulf Power Company 2008 Annual Report

	2008	2007	2006	2005	2004
Operating Revenues (in thousands)	**$1,387,203**	$1,259,808	$1,203,914	$1,083,622	$960,131
Net Income after Dividends on Preferred and Preference Stock (in thousands)	**$98,345**	$84,118	$75,989	$75,209	$68,223
Cash Dividends on Common Stock (in thousands)	**$81,700**	$74,100	$70,300	$68,400	$70,000
Return on Average Common Equity (percent)	**12.66**	12.32	12.29	12.59	11.83
Total Assets (in thousands)	**$2,879,025**	$2,498,987	$2,340,489	$2,175,797	$2,111,877
Gross Property Additions (in thousands)	**$390,744**	$239,337	$147,086	$142,583	$161,205
Capitalization (in thousands):					
Common stock equity	**$ 822,092**	$731,255	$634,023	$602,344	$592,172
Preferred and preference stock	**97,998**	97,998	53,887	53,891	4,098
Long-term debt	**849,265**	740,050	696,098	616,554	623,155
Total (excluding amounts due within one year)	**$1,769,355**	$1,569,303	$1,384,008	$1,272,789	$1,219,425
Capitalization Ratios (percent):					
Common stock equity	**46.5**	46.6	45.8	47.3	48.6
Preferred and preference stock	**5.5**	6.2	3.9	4.2	0.3
Long-term debt	**48.0**	47.2	50.3	48.5	51.1
Total (excluding amounts due within one year)	**100.0**	100.0	100.0	100.0	100.0
Security Ratings:					
First Mortgage Bonds -					
Moody's	**-**	-	-	A1	A1
Standard and Poor's	**-**	-	-	A+	A+
Fitch	**-**	-	-	A+	A+
Preferred Stock/ Preference Stock -					
Moody's	**Baa1**	Baa1	Baa1	Baa1	Baa1
Standard and Poor's	**BBB+**	BBB+	BBB+	BBB+	BBB+
Fitch	**A-**	A-	A-	A-	A-
Unsecured Long-Term Debt -					
Moody's	**A2**	A2	A2	A2	A2
Standard and Poor's	**A**	A	A	A	A
Fitch	**A**	A	A	A	A
Customers (year-end):					
Residential	**373,595**	373,036	364,647	354,466	343,151
Commercial	**53,548**	53,838	53,466	53,398	51,865
Industrial	**287**	298	295	298	285
Other	**499**	491	484	479	473
Total	**427,929**	427,663	418,892	408,641	395,774
Employees (year-end)	**1,342**	1,324	1,321	1,335	1,336

SELECTED FINANCIAL AND OPERATING DATA 2004-2008 (continued)
Gulf Power Company 2008 Annual Report

	2008	2007	2006	2005	2004
Operating Revenues (in thousands)**:**					
Residential	**$ 581,723**	$537,668	$510,995	$465,346	$401,382
Commercial	**369,625**	329,651	305,049	273,114	232,928
Industrial	**165,564**	135,179	132,339	123,044	99,420
Other	**3,854**	3,831	3,655	3,355	3,140
Total retail	**1,120,766**	1,006,329	952,038	864,859	736,870
Wholesale - non-affiliates	**97,065**	83,514	87,142	84,346	73,537
Wholesale - affiliates	**106,989**	113,178	118,097	91,352	110,264
Total revenues from sales of electricity	**1,324,820**	1,203,021	1,157,277	1,040,557	920,671
Other revenues	**62,383**	56,787	46,637	43,065	39,460
Total	**$1,387,203**	$1,259,808	$1,203,914	$1,083,622	$960,131
Kilowatt-Hour Sales (in thousands)**:**					
Residential	**5,348,642**	5,477,111	5,425,491	5,319,630	5,215,332
Commercial	**3,960,923**	3,970,892	3,843,064	3,735,776	3,695,471
Industrial	**2,210,597**	2,048,389	2,136,439	2,160,760	2,113,027
Other	**23,237**	24,496	23,886	22,730	22,579
Total retail	**11,543,399**	11,520,888	11,428,880	11,238,896	11,046,409
Sales for resale - non-affiliates	**1,816,839**	2,227,026	2,079,165	2,295,850	2,256,942
Sales for resale - affiliates	**1,871,158**	2,884,440	2,937,735	1,976,368	3,124,788
Total	**15,231,396**	16,632,354	16,445,780	15,511,114	16,428,139
Average Revenue Per Kilowatt-Hour (cents)**:**					
Residential	**10.88**	9.82	9.42	8.75	7.70
Commercial	**9.33**	8.30	7.94	7.31	6.30
Industrial	**7.49**	6.60	6.19	5.69	4.71
Total retail	**9.71**	8.73	8.33	7.70	6.67
Wholesale	**5.53**	3.85	4.09	4.11	3.42
Total sales	**8.70**	7.23	7.04	6.71	5.60
Residential Average Annual Kilowatt-Hour Use Per Customer	**14,274**	14,755	15,032	15,181	15,096
Residential Average Annual Revenue Per Customer	**$1,552**	$1,448	$1,416	$1,328	$1,162
Plant Nameplate Capacity Ratings (year-end) (megawatts)	**2,659**	2,659	2,659	2,712	2,712
Maximum Peak-Hour Demand (megawatts)**:**					
Winter	**2,360**	2,215	2,195	2,124	2,061
Summer	**2,533**	2,626	2,479	2,433	2,421
Annual Load Factor (percent)	**56.7**	55.0	57.9	57.7	57.1
Plant Availability Fossil-Steam (percent)	**88.6**	93.4	91.3	89.7	92.4
Source of Energy Supply (percent)**:**					
Coal	**77.3**	81.8	82.5	79.7	77.9
Gas	**15.3**	13.6	12.4	13.1	14.4
Purchased power -					
From non-affiliates	**2.6**	1.6	1.9	2.8	4.5
From affiliates	**4.8**	3.0	3.2	4.4	3.2
Total	**100.0**	100.0	100.0	100.0	100.0

DIRECTORS AND OFFICERS
Gulf Power Company 2008 Annual Report

DIRECTORS

Susan N. Story
President and Chief Executive Officer
Gulf Power Company
Pensacola, Florida. Elected 2003

C. LeDon Anchors
Attorney at Law
Anchors Smith Grimsley
A Professional Limited Company
Fort Walton Beach, Florida. Elected 2001

William C. Cramer, Jr.
President
Tommy Thomas Chevrolet, Inc.
Panama City, Florida. Elected 2002

Fred C. Donovan, Sr.
Chairman and Chief Executive Officer
Baskerville-Donovan, Inc.
Pensacola, Florida. Elected 1991

William A. Pullum
Broker/President
Bill Pullum Realty, Inc.
Navarre, Florida. Elected 2001

Winston E. Scott
Dean, College of Aeronautics
Florida Institute of Technology
Melbourne, Florida. Elected 2003

OFFICERS

Susan N. Story
President and Chief Executive Officer
26 Years of Service

P. Bernard Jacob
Vice President – Customer Operations
26 Years of Service

Theodore J. McCullough
Vice President – Sr. Production Officer
22 Years of Service

Philip C. Raymond
Vice President and Chief Financial Officer
17 Years of Service

Bentina C. Terry
Vice President – External Affairs and
Corporate Services
8 Years of Service

Connie J. Erickson
Comptroller
6 Years of Service

Susan D. Ritenour
Secretary and Treasurer
27 Years of Service

Terry A. Davis
Assistant Secretary and Assistant Treasurer
22 Years of Service

Marsha S. Johnson
Vice President
23 Years of Service

E. Wayne Boston
Assistant Secretary and Assistant Treasurer
38 Years of Service

CORPORATE INFORMATION
Gulf Power Company 2008 Annual Report

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

Profile
The Company produces and delivers electricity as an integrated utility to both retail and wholesale customers within the State of Florida. The Company sells electricity to approximately 428,000 customers within its service area of approximately 7,500 square miles in the Florida panhandle. In 2008, retail energy sales accounted for 76 percent of the Company's total sales of 15.2 billion kilowatt-hours.

The Company is a wholly owned subsidiary of The Southern Company, which is the parent company of four traditional operating companies, a wholesale generation subsidiary, and other direct and indirect subsidiaries. There is no established public trading market for the Company's common stock.

Registrar, Transfer Agent, and Dividend Paying Agent
Preference Stock
Southern Company Services, Inc.
Stockholder Services
P.O. Box 54250
Atlanta, GA 30308-0250
(800) 554-7626

Trustee, Registrar, and Interest Paying Agent
All series of Senior Notes
The Bank of New York Mellon
Global Corporate Trust
100 Ashford Center North, Suite 520
Atlanta, Georgia 30338

All of the outstanding shares of the Company's preference stock are registered in the name of Cede & Co., as nominee for The Depository Trust Company.

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

Corporate Office
Principal Address & Deliveries:
Gulf Power Company
500 Bayfront Parkway
Pensacola, FL 32520
(850) 444-6111

Mailing Address:
Gulf Power Company
One Energy Place
Pensacola, FL 32520

Auditors
Deloitte & Touche LLP
Suite 1500
191 Peachtree Street, N.E.
Atlanta, GA 30303-1924

Legal Counsel
Beggs & Lane
A Registered Limited Liability Partnership
P.O. Box 12950
Pensacola, FL 32591-2950