AMERICAN INTERNATIONAL GROUP INC
Form 10-Q
November 07, 2007

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

Form 10-Q

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2007

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.
(Exact name of registrant as specified in its charter)

Delaware	**13-2592361**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
70 Pine Street, New York, New York	**10270**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (212) 770-7000
Former name, former address and former fiscal year, if changed since last report: None

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

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

As of October 31, 2007, there were 2,536,238,141 shares outstanding of the registrant s common stock.

TABLE OF CONTENTS

Table of Contents

American International Group, Inc. and Subsidiaries

Part I FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	September 30, 2007	December 31, 2006
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at fair value (amortized cost: 2007 $391,497; 2006 $377,698) (includes hybrid financial instruments: 2007 $566; 2006 $522)	**$ 394,810**	$ 387,391
Bonds held to maturity, at amortized cost (fair value: 2007 $22,053; 2006 $22,154)	**21,576**	21,437
Bond trading securities, at fair value (cost: 2007 $9,604; 2006 $10,292)	**9,459**	10,314
Equity securities:		
Common stocks available for sale, at fair value (cost: 2007 $12,852; 2006 $10,662)	**18,649**	13,256
Common and preferred stocks trading, at fair value (cost: 2007 $17,269; 2006 $13,079)	**19,219**	14,855
Preferred stocks available for sale, at fair value (cost: 2007 $2,620; 2006 $2,485)	**2,606**	2,539
Mortgage loans on real estate, net of allowance (2007 $52; 2006 $55)	**18,854**	17,067
Policy loans	**7,822**	7,501
Collateral and guaranteed loans, net of allowance (2007 $4; 2006 $9)	**4,385**	3,850
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2007 $10,105; 2006 $8,835)	**41,804**	39,875
Securities available for sale, at fair value (cost: 2007 $46,892; 2006 $45,912)	**47,805**	47,205
Trading securities, at fair value	**4,874**	5,031
Spot commodities	**115**	220
Unrealized gain on swaps, options and forward transactions	**18,608**	19,252
Trade receivables	**6,548**	4,317
Securities purchased under agreements to resell, at contract value	**37,189**	30,291
Finance receivables, net of allowance (2007 $775; 2006 $737) (includes finance receivables held for sale: 2007 $406; 2006 $1,124)	**30,640**	29,573
Securities lending collateral, at fair value (cost: 2007 $87,956; 2006 $69,306)	**86,108**	69,306
Other invested assets	**51,783**	42,111
Short-term investments, at cost (approximates fair value)	**38,998**	27,483
Total investments and financial services assets	**861,852**	792,874

Cash		**2,249**		1,590
Investment income due and accrued		**6,635**		6,091
Premiums and insurance balances receivable, net of allowance (2007 $746; 2006 $756)		**18,199**		17,789
Reinsurance assets, net of allowance (2007 $658; 2006 $536)		**23,426**		23,355
Deferred policy acquisition costs		**40,878**		37,235
Investments in partially owned companies		**1,277**		1,101
Real estate and other fixed assets, net of accumulated depreciation (2007 $5,807; 2006 $5,525)		**6,093**		4,381
Separate and variable accounts		**78,701**		70,277
Goodwill		**8,909**		8,628
Other assets		**23,886**		16,089
Total assets	**$**	**1,072,105**	$	979,410

See Accompanying Notes to Consolidated Financial Statements.

Table of Contents

American International Group, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEET *(continued)*
(in millions, except share data) (unaudited)

	September 30, 2007	December 31, 2006
Liabilities:		
Reserve for losses and loss expenses	**$ 83,608**	$ 79,999
Unearned premiums	**27,909**	26,271
Future policy benefits for life and accident and health insurance contracts	**130,759**	122,230
Policyholders contract deposits	**254,109**	248,994
Other policyholders funds	**8,196**	8,281
Commissions, expenses and taxes payable	**6,523**	5,305
Insurance balances payable	**5,304**	3,789
Funds held by companies under reinsurance treaties	**2,456**	2,602
Income taxes payable	**9,288**	9,546
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**19,495**	20,664
Securities sold under agreements to repurchase, at contract value	**23,368**	19,677
Trade payables	**10,137**	6,174
Hybrid financial instrument liabilities, at fair value	**7,692**	8,856
Securities and spot commodities sold but not yet purchased, at market value	**4,736**	4,076
Unrealized loss on swaps, options and forward transactions	**12,512**	11,401
Trust deposits and deposits due to banks and other depositors	**4,737**	5,249
Commercial paper	**10,120**	8,208
Notes, bonds, loans and mortgages payable	**101,747**	87,816
Commercial paper and extendible commercial notes	**5,845**	4,821
Notes, bonds, loans and mortgages payable	**25,165**	16,874
Junior subordinated debt	**4,681**	
Liabilities connected to trust preferred stock	**1,440**	1,440
Separate and variable accounts	**78,701**	70,277
Securities lending payable	**88,360**	70,198
Minority interest	**10,395**	7,778
Other liabilities (includes hybrid financial instruments: 2007 $99; 2006 $111)	**30,655**	27,016
Total liabilities	**967,938**	877,542
Preferred shareholders equity in subsidiary companies	**100**	191
Commitments and Contingent Liabilities (See Note 6)		
Shareholders equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2007 and 2006 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,818**	2,590
Payments advanced to purchase shares	**(1,275)**	

Retained earnings		**94,830**		84,996
Accumulated other comprehensive income (loss)		**6,194**		9,110
Treasury stock, at cost; 2007 201,311,212; 2006 150,131,273 shares of common stock		**(5,378)**		(1,897)
Total shareholders equity		**104,067**		101,677
Total liabilities, preferred shareholders equity in subsidiary companies and shareholders equity	**$**	**1,072,105**	$	979,410

See Accompanying Notes to Consolidated Financial Statements.

2

Table of Contents

American International Group, Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF INCOME

(in millions, except per share data) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Revenues:				
Premiums and other considerations	**$ 19,733**	$ 18,890	**$ 58,908**	$ 55,486
Net investment income	**6,172**	6,463	**21,149**	18,579
Net realized capital gains (losses)	**(864)**	(87)	**(962)**	(132)
Other income	**4,795**	3,981	**12,536**	9,446
Total revenues	**29,836**	29,247	**91,631**	83,379
Benefits and expenses:				
Incurred policy losses and benefits	**15,595**	14,963	**47,962**	44,118
Insurance acquisition and other operating expenses	**9,362**	7,983	**26,290**	22,926
Total benefits and expenses	**24,957**	22,946	**74,252**	67,044
Income before income taxes, minority interest and cumulative effect of an accounting change	**4,879**	6,301	**17,379**	16,335
Income taxes	**1,463**	1,943	**4,868**	5,066
Income before minority interest and cumulative effect of an accounting change	**3,416**	4,358	**12,511**	11,269
Minority interest	**(331)**	(134)	**(1,019)**	(694)
Income before cumulative effect of an accounting change	**3,085**	4,224	**11,492**	10,575
Cumulative effect of an accounting change, net of tax				34
Net income	**$ 3,085**	$ 4,224	**$ 11,492**	$ 10,609
Earnings per common share:				
Basic				
Income before cumulative effect of an accounting change	**$ 1.20**	$ 1.62	**$ 4.43**	$ 4.06
Cumulative effect of an accounting change, net of tax				0.01
Net income	**$ 1.20**	$ 1.62	**$ 4.43**	$ 4.07
Diluted				

Income before cumulative effect of an accounting change	**$ 1.19**	$ 1.61	**$ 4.40**	$ 4.03
Cumulative effect of an accounting change, net of tax				0.01
Net income	**$ 1.19**	$ 1.61	**$ 4.40**	$ 4.04
Dividends declared per common share	**$ 0.200**	$ 0.165	**$ 0.565**	$ 0.480
Average shares outstanding:				
Basic	**2,576**	2,607	**2,596**	2,607
Diluted	**2,589**	2,626	**2,609**	2,625

See Accompanying Notes to Consolidated Financial Statements.

Table of Contents

American International Group, Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Nine Months Ended September 30, 2007	2006
Summary:		
Net cash provided by operating activities	**$ 27,056**	$ 4,037
Net cash used in investing activities	**(65,929)**	(52,144)
Net cash provided by financing activities	**39,524**	47,576
Effect of exchange rate changes on cash	**8**	59
Change in cash	**659**	(472)
Cash at beginning of period	**1,590**	1,897
Cash at end of period	**$ 2,249**	$ 1,425
Cash flows from operating activities:		
Net income	**$ 11,492**	$ 10,609
Adjustments to reconcile net income to net cash provided by operating activities:		
Noncash revenues, expenses, gains and losses included in income:		
Net gains on sales of securities available for sale and other assets	**(1,110)**	(407)
Foreign exchange transaction (gains) losses	**1,214**	845
Net unrealized (gains) losses on non-AIGFP derivative assets and liabilities	**(103)**	(441)
Equity in income of partially owned companies and other invested assets	**(3,336)**	(2,655)
Amortization of deferred policy acquisition costs	**9,242**	8,785
Amortization of premium and discount on securities	**491**	100
Depreciation expenses, principally flight equipment	**2,072**	1,743
Provision for finance receivable losses	**391**	329
Impairment losses	**1,413**	766
Changes in operating assets and liabilities:		
General and life insurance reserves	**12,131**	10,507
Premiums and insurance balances receivable and payable net	**515**	(173)
Reinsurance assets	**561**	614
Capitalization of deferred policy acquisition costs	**(11,897)**	(11,949)
Investment income due and accrued	**(538)**	(486)
Funds held under reinsurance treaties	**(166)**	(1,732)
Other policyholders funds	**(85)**	(840)
Income taxes payable	**707**	1,905
Commissions, expenses and taxes payable	**1,110**	356
Other assets and liabilities net	**2,181**	(842)
Bonds, common and preferred stocks trading, at fair value	**(2,546)**	(5,535)

Trade receivables and payables net		**1,844**		(163)
Trading securities, at fair value		**158**		677
Spot commodities		**105**		(26)
Net unrealized (gain) loss on swaps, options and forward transactions		**2,059**		(966)
Securities purchased under agreements to resell		**(6,898)**		(10,638)
Securities sold under agreements to repurchase		**3,686**		2,384
Securities and spot commodities sold but not yet purchased, at market value		**660**		(330)
Finance receivables held for sale originations and purchases		**(4,377)**		(7,965)
Sales of finance receivables held for sale		**5,095**		7,888
Other, net		**985**		1,677
Total adjustments		**15,564**		(6,572)
Net cash provided by operating activities	**$**	**27,056**	$	4,037

See Accompanying Notes to Consolidated Financial Statements.

4

Table of Contents

American International Group, Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

	Nine Months Ended September 30, 2007	2006
Cash flows from investing activities:		
Proceeds from (payments for)		
Sales and maturities of fixed maturity securities available for sale	**$ 97,068**	$ 86,579
Sales of equity securities available for sale	**6,700**	9,394
Proceeds from fixed maturity securities held to maturity	**175**	265
Sales of flight equipment	**95**	380
Sales or distributions of other invested assets	**9,298**	11,880
Payments received on mortgage, policy, collateral and guaranteed loans	**3,863**	3,081
Principal payments received on finance receivables held for investment	**9,554**	9,131
Purchases of fixed maturity securities available for sale	**(110,037)**	(106,750)
Purchases of equity securities available for sale	**(8,438)**	(11,032)
Purchases of fixed maturity securities held to maturity	**(154)**	(264)
Purchases of flight equipment	**(3,925)**	(4,860)
Purchases of other invested assets and warehoused investments	**(20,677)**	(12,865)
Mortgage, policy, collateral and guaranteed loans issued	**(6,554)**	(5,793)
Finance receivables held for investment originations and purchases	**(11,394)**	(9,947)
Change in securities lending collateral	**(18,723)**	(11,917)
Net additions to real estate, fixed assets, and other assets	**(1,004)**	(620)
Net change in short-term investments	**(11,764)**	(8,787)
Net change in non-AIGFP derivative assets and liabilities	**(12)**	(19)
Net cash used in investing activities	**$ (65,929)**	$ (52,144)
Cash flows from financing activities:		
Proceeds from (payments for)		
Policyholders contract deposits	**$ 46,239**	$ 40,226
Policyholders contract withdrawals	**(43,220)**	(31,201)
Change in other deposits	**(713)**	753
Change in commercial paper	**2,526**	3,216
Notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities issued	**61,119**	40,345
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(42,098)**	(16,851)
Issuance of junior subordinated debt	**4,490**	
Issuance of guaranteed investment agreements	**6,430**	9,411
Maturities of guaranteed investment agreements	**(7,545)**	(9,480)
Change in securities lending payable	**18,156**	11,855

Issuance of treasury stock		**204**		94
Payments advanced to purchase shares		**(5,000)**		
Acquisition of treasury stock		**(16)**		(7)
Cash dividends paid to shareholders		**(1,372)**		(1,209)
Other, net		**324**		424
Net cash provided by financing activities	**$**	**39,524**	$	47,576
Supplementary disclosure of cash flow information:				
Cash paid during the period for:				
Interest	**$**	**6,190**	$	4,202
Taxes	**$**	**4,044**	$	3,252
Non-cash financing activities:				
Interest credited to policyholder accounts	**$**	**7,553**	$	7,253
Treasury stock acquired using payments advanced to purchase shares	**$**	**3,725**		
Non-cash investing activities:				
Debt assumed on acquisitions and warehoused investments	**$**	**358**	$	
Liability related to purchase of additional interest in 21st Century	**$**	**759**	$	

See Accompanying Notes to Consolidated Financial Statements.

Table of Contents

American International Group, Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Net income	**$ 3,085**	$ 4,224	**$ 11,492**	$ 10,609
Other comprehensive income (loss):				
Unrealized (depreciation) appreciation of investments net of reclassification adjustments	**(3,394)**	7,200	**(4,246)**	(1,133)
Deferred income tax benefit (expense) on above changes	**941**	(2,562)	**1,081**	281
Foreign currency translation adjustments	**619**	(115)	**290**	955
Deferred income tax benefit (expense) on above changes	**(109)**	17	**(74)**	(332)
Net derivative gains arising from cash flow hedging activities net of reclassification adjustments	**(93)**	4	**(31)**	12
Deferred income tax benefit (expense) on above changes	**34**	(1)	**39**	(4)
Change in pension and postretirement unrecognized periodic benefit (cost)	**17**		**35**	(3)
Deferred income tax benefit (expense) on above changes	**(8)**		**(10)**	1
Other comprehensive income (loss)	**(1,993)**	4,543	**(2,916)**	(223)
Comprehensive income (loss)	**$ 1,092**	$ 8,767	**$ 8,576**	$ 10,386

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Summary of Significant Accounting Policies

Basis of Presentation

These unaudited condensed consolidated financial statements do not include certain financial information required by U.S. generally accepted accounting principles (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2006 (2006 Annual Report on Form 10-K).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated.

Revisions and Reclassifications

In the third quarter of 2007, AIG determined that certain products that were historically reported as separate account assets under Statement of Position 03-1, Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts (SOP 03-1) should have been reported as general account assets. Accordingly, the December 31, 2006 consolidated balance sheet has been revised to transfer $2.4 billion of assets from separate account assets to general account assets, and the same amount of liabilities from separate account liabilities to policyholders contract deposits. This revision did not have any effect on consolidated income before income taxes, net income, or shareholders equity for any period presented.

Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Out of period adjustments

During the three and nine-month periods ended September 30, 2007, AIG recorded the effects of certain out of period adjustments, which reduced net income by $35 million and $408 million, respectively, and diluted earnings per share by $0.01 per share and $0.16 per share, respectively.

During the three and nine-month periods ended September 30, 2006, AIG recorded the effects of certain out of period adjustments which increased (decreased) net income by $73 million and $(135) million, respectively, and diluted earnings per share by $0.03 per share and $(0.05) per share, respectively.

Recent Accounting Standards

Accounting Changes

SOP 05-1

On September 19, 2005, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position 05-1, Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts (SOP 05-1). SOP 05-1 provides guidance on accounting for internal replacements of insurance and investment contracts other than those specifically described in Statement of Financial Accounting Standards (FAS) No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments (FAS 97). SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. Internal replacements that result in a substantially changed contract are accounted for as a termination and a replacement contract.

The provisions of SOP 05-1 became effective as of January 1, 2007. On the date of adoption, AIG recorded a cumulative effect reduction of $82 million, net of tax, to the opening balance of retained earnings to reflect changes in unamortized deferred policy acquisition costs (DAC), value of business acquired, deferred sales inducement assets, unearned revenue liabilities and future policy benefits for life and accident and health insurance contracts. This adjustment primarily reflects a shorter expected life related to certain group life and health insurance contracts and the effect on the gross profits of investment-oriented products related to previously anticipated future internal replacements. This cumulative effect adjustment affected only the Life Insurance & Retirement Services segment.

FIN 48

On July 13, 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48), which clarifies the accounting for uncertainty in income tax positions. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. AIG adopted the provisions of FIN 48 on January 1, 2007. As a result of the adoption of FIN 48, AIG recognized a $71 million increase in the liability for unrecognized tax benefits, which was accounted for as a decrease to opening retained earnings as of January 1, 2007.

As of the date of adoption and after recognizing the effect of the increase in the liability noted above, the total amount of AIG s unrecognized tax benefit, excluding interest and penalties, was $1.138 billion. Included in this balance are $407 million related to tax positions, the disallowance of which would not

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

1. Summary of Significant Accounting Policies *(continued)*

affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefit that, if recognized, would favorably affect the effective tax rate is $731 million.

At September 30, 2007, AIG s unrecognized tax benefit, excluding interest and penalties, was $1.139 billion, which includes $447 million related to tax positions the disallowance of which would not affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefit that, if recognized, would favorably affect the effective tax rate was $692 million.

Interest and penalties related to unrecognized tax benefits are recognized in income tax expense. At January 1, 2007 and September 30, 2007, AIG had accrued $176 million and $207 million, respectively, for the payment of interest (net of tax benefits) and penalties.

Neither reserves for uncertain tax positions attributable to prior restatements (including various other remediation-related adjustments) nor the corresponding interest income have been recognized because such amounts are not currently estimable. In addition, certain tax benefits from compensation deductions have not been recognized because of existing uncertainty with respect to documentation supporting these tax benefits.

AIG continually evaluates proposed adjustments by taxing authorities. At September 30, 2007, such proposed adjustments would not result in a material change to AIG s consolidated financial condition. However, AIG believes that it is reasonably possible that the balance of the unrecognized tax benefits could decrease by $0 to $100 million within the next twelve months due to settlements or expiration of statutes.

Listed below are the tax years that remain subject to examination by major tax jurisdiction:

Major Tax Jurisdictions	Open Tax Years
United States	1991-2006
Hong Kong	1997-2006
Malaysia	1999-2006
Singapore	1993-2006
Thailand	2001-2006
Taiwan	2000-2006
Japan	2000-2006
United Kingdom	2003-2006
France	2003-2006
Korea	2001-2006

FSP 13-2

On July 13, 2006, the FASB issued FASB Staff Position (FSP) No. 13-2, Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction (FSP 13-2). FSP 13-2 addresses how a change or projected change in the timing of cash flows relating to income taxes generated by a leveraged lease transaction affects the accounting for the lease by the lessor, and directs that the tax assumptions be consistent with any FIN 48 uncertain tax position related to the lease. FSP 13-2 is effective for fiscal years beginning after December 15, 2006. Upon adoption, AIG recorded a $50 million decrease in the opening balance of retained earnings, net of tax, as of January 1, 2007 to reflect the cumulative effect of this change in accounting. The adoption of this guidance is not expected to have a material effect on AIG s results of operations in 2007.

As a result of the adoptions of SOP 05-1, FIN 48 and FSP 13-2, AIG recorded a total decrease to opening retained earnings of $203 million as of January 1, 2007.

Future Application of Accounting Standards

FAS 157

In September 2006, the FASB issued FAS No. 157, Fair Value Measurements (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements. FAS 157 will be effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance.

FAS 159

In February 2007, the FASB issued FAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 will be effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance, which depends on the nature and extent of items elected to be measured at fair value upon initial application of the standard on January 1, 2008.

SOP 07-1

In June 2007, the AICPA issued Statement of Position No. 07-1 (SOP 07-1), Clarification of the Scope of the Audit and Accounting Guide Audits of Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies. SOP 07-1 amends the guidance for whether an entity may apply the provisions of the Audit and Accounting Guide, Audits of Investment Companies (the Guide). Investment companies that are subject to the Guide must report all investments at fair value regardless of the nature of the investment or the level of ownership. SOP 07-1 also establishes new requirements for whether a parent company can retain specialized investment company accounting in its consolidated financial statements for subsidiaries and equity method investees that are covered by the Guide. At the October 17, 2007 Board

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

1. Summary of Significant Accounting Policies *(continued)*
meeting, the FASB decided it would indefinitely defer the effective date of SOP 07-1. AIG understands that a FASB Staff Position will be issued shortly. AIG is currently monitoring any changes to the existing guidance.

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management.

In order to better align financial reporting with the manner in which AIG s chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, AIG realigned certain products among reportable segments and major internal reporting units. AIG also began reporting net realized capital gains and losses for the Financial Services and Asset Management segments in the results of these segments. Historically, net realized capital gains and losses were included in the Other category. There has been no change in AIG s management structure or in its reportable segments. All prior period amounts presented in the tables below have been revised to conform to the current year s presentation of these items.

The following table summarizes AIG s operations by major operating segment:

Operating Segments *(in millions)*	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Revenues[a]:				
General Insurance[b]	**$ 12,758**	$ 12,615	**$ 38,589**	$ 36,438
Life Insurance & Retirement Services[b]	**12,632**	12,542	**40,337**	37,303
Financial Services[c][d]	**2,785**	3,011	**7,109**	5,923
Asset Management	**1,824**	993	**5,721**	3,647
Other	**13**	215	**407**	443
Consolidation and eliminations	**(176)**	(129)	**(532)**	(375)
Consolidated	**$ 29,836**	$ 29,247	**$ 91,631**	$ 83,379
Operating income (loss)[a]:				
General Insurance[b]	**$ 2,439**	$ 2,625	**$ 8,511**	$ 7,819
Life Insurance & Retirement Services[b]	**1,999**	2,472	**6,900**	7,483
Financial Services[c][d]	**669**	1,179	**1,008**	541
Asset Management	**419**	211	**2,541**	1,445
Other[e]	**(627)**	(186)	**(1,557)**	(953)
Consolidation and eliminations	**(20)**		**(24)**	
Consolidated	**$ 4,879**	$ 6,301	**$ 17,379**	$ 16,335

(a) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS No. 133, Accounting for Derivative Instruments and Hedging Activities (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the effect was $(178) million and $165 million in both revenues and operating income. For the nine-month periods ended September 30, 2007 and 2006, respectively, the effect was $(1.06) billion and $(1.13) billion in both

revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings. These gains (losses) for the three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP). The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133.

(b) *Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts (UCITS). For the three and nine- month periods ended September 30, 2006, the effect was an increase of $92 million and $472 million, respectively, in both revenues and operating income for General Insurance and an increase of $24 million and $240 million, respectively, in revenues and $24 million and $169 million, respectively, in operating income for Life Insurance & Retirement Services.*

(c) *Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the effect was $353 million, and $581 million in both revenues and operating income. For the nine-month periods ended September 30, 2007 and 2006, respectively, the effect was $(250) million and $(1.2) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, as discussed above. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million as discussed above. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, American General Finance, Inc. (AGF) and International Lease Finance Corporation (ILFC) began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.*

(d) *For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP s super senior credit default swap portfolio.*

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

2. Segment Information *(continued)*

(e) Includes AIG parent and other operations which are not required to be reported separately. The following table presents the operating loss for AIG s Other category:

(in millions)	Three Months Ended September 30, 2007	2006	Nine Months Ended September 30, 2007	2006
Other operating income (loss):				
Equity earnings in unconsolidated entities	**$ 37**	$ 48	**$ 128**	$ 178
Interest expense	**(315)**	(227)	**(869)**	(633)
Unallocated corporate expenses	**(157)**	(89)	**(519)**	(337)
Compensation expense SICO Plans	**(9)**	(14)	**(29)**	(104)
Compensation expense Starr tender offer				(54)
Net realized capital gains (losses)	**(199)**	85	**(226)**	31
Other miscellaneous, net	**16**	11	**(42)**	(34)
Total Other	**$ (627)**	$ (186)	**$ (1,557)**	$ (953)

The following table summarizes AIG s General Insurance operations by major internal reporting unit:

General Insurance *(in millions)*	Three Months Ended September 30, 2007	2006	Nine Months Ended September 30, 2007	2006
Revenues:				
Domestic Brokerage Group	**$ 6,736**	$ 7,182	**$ 20,731**	$ 20,330
Transatlantic	**1,088**	1,004	**3,253**	3,035
Personal Lines	**1,252**	1,214	**3,688**	3,652
Mortgage Guaranty	**267**	226	**772**	636
Foreign General*	**3,413**	2,989	**10,150**	8,783
Reclassifications and eliminations	**2**		**(5)**	2
Total General Insurance	**$ 12,758**	$ 12,615	**$ 38,589**	$ 36,438
Operating Income (loss):				
Domestic Brokerage Group	**$ 1,829**	$ 1,543	**$ 5,662**	$ 4,322
Transatlantic	**189**	143	**508**	427
Personal Lines	**28**	133	**252**	352
Mortgage Guaranty	**(216)**	85	**(289)**	301
Foreign General*	**607**	721	**2,383**	2,415
Reclassifications and eliminations	**2**		**(5)**	2

Total General Insurance	**$ 2,439**	$ 2,625	**$ 8,511**	$ 7,819

**Includes the effect of an out of period UCITS adjustment which increased both revenues and operating income by $22 million and $406 million for the three and nine-month periods ended September 30, 2006, respectively.*

The following table summarizes AIG s Life Insurance & Retirement Services operations by major internal reporting unit:

Life Insurance & Retirement Services *(in millions)*	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Revenues:				
Foreign:				
Japan and Other	**$ 4,315**	$ 4,339	**$ 13,948**	$ 12,415
Asia*	**4,695**	4,109	**14,205**	12,872
Domestic:				
Domestic Life Insurance	**2,185**	2,259	**7,065**	6,848
Domestic Retirement Services	**1,437**	1,835	**5,119**	5,168
Total Life Insurance & Retirement Services	**$ 12,632**	$ 12,542	**$ 40,337**	$ 37,303
Operating Income:				
Foreign:				
Japan and Other	**$ 1,030**	$ 993	**$ 2,753**	$ 2,946
Asia*	**706**	615	**1,921**	2,087
Domestic:				
Domestic Life Insurance	**61**	261	**774**	862
Domestic Retirement Services	**202**	603	**1,452**	1,588
Total Life Insurance & Retirement Services	**$ 1,999**	$ 2,472	**$ 6,900**	$ 7,483

**Includes the effect of an out of period UCITS adjustment, which increased revenues by $9 million and $208 million and operating income by $9 million and $137 million, respectively, for the three and nine-month periods ended September 30, 2006, respectively.*

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

2. Segment Information *(continued)*

The following table summarizes AIG s Financial Services operations by major internal reporting unit:

Financial Services *(in millions)*	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Revenues:				
Aircraft Leasing*(a)*	**$ 1,237**	$ 950	**$ 3,468**	$ 3,013
Capital Markets*(b)(c)*	**540**	1,118	**701**	30
Consumer Finance*(d)(e)*	**992**	901	**2,824**	2,768
Other, including intercompany adjustments	**16**	42	**116**	112
Total Financial Services	**$ 2,785**	$ 3,011	**$ 7,109**	$ 5,923
Operating income (loss):				
Aircraft Leasing*(a)*	**$ 254**	$ 47	**$ 625**	$ 421
Capital Markets*(b)(c)*	**370**	965	**183**	(457)
Consumer Finance*(d)(e)*	**69**	151	**180**	529
Other, including intercompany adjustments	**(24)**	16	**20**	48
Total Financial Services	**$ 669**	$ 1,179	**$ 1,008**	$ 541

(a) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(19) million and $(111) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(32) million and $(56) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Revenues, shown net of interest expense of $1.4 billion and $802 million for the three-month periods ended September 30, 2007 and 2006, respectively, and $3.3 billion and $2.1 billion for the nine-month periods ended September 30, 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $428 million and $783 million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(185) million and $(1.1) billion, respectively. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million, respectively, related to the

remediation of the material weakness in accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain transactions.

(c) For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP s super senior credit default swap portfolio.

(d) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(6) million and $(73) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(21) million and $(65) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(e) The nine-month period ended September 30, 2007 includes a pre-tax charge of $178 million in connection with domestic consumer finance s mortgage banking activities.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

3. Shareholders Equity and Earnings Per Share

Earnings Per Share (EPS)

Basic EPS of AIG is calculated using the weighted average number of common shares outstanding. Diluted EPS is based on those shares used in basic EPS plus shares that would have been outstanding assuming issuance of common shares for all potentially dilutive common shares outstanding.

The following table presents the computation of basic and diluted EPS:

	Three Months Ended **September 30,**		Nine Months Ended **September 30,**	
(in millions, except per share data)	**2007**	2006	**2007**	2006
Numerator for earnings per share:				
Income before cumulative effect of an accounting change	**$ 3,085**	$ 4,224	**$ 11,492**	$ 10,575
Cumulative effect of an accounting change, net of tax				34
Net income applicable to common stock for basic EPS	**$ 3,085**	$ 4,224	**$ 11,492**	$ 10,609
Interest on contingently convertible bonds, net of tax [(a)]		2		8
Net income applicable to common stock for diluted EPS	**$ 3,085**	$ 4,226	**$ 11,492**	$ 10,617
Cumulative effect of an accounting change, net of tax				(34)
Income before cumulative effect of an accounting change applicable to common stock for diluted EPS	**$ 3,085**	$ 4,226	**$ 11,492**	$ 10,583
Denominator for earnings per share:				
Weighted average shares outstanding used in the computation of EPS:				
Common stock issued	**2,751**	2,751	**2,751**	2,751
Common stock in treasury	**(189)**	(153)	**(168)**	(153)
Deferred shares	**14**	9	**13**	9
Weighted average shares outstanding basic	**2,576**	2,607	**2,596**	2,607
Incremental shares from potential common stock:				
Weighted average number of shares arising from outstanding employee stock plans (treasury stock method) [(b)]	**13**	10	**13**	9
Contingently convertible bonds[(a)]		9		9
Weighted average shares outstanding diluted[(b)]	**2,589**	2,626	**2,609**	2,625
Earnings per share:				
Basic:				
Income before cumulative effect of an accounting change	**$ 1.20**	$ 1.62	**$ 4.43**	$ 4.06

Cumulative effect of an accounting change, net of tax								0.01
Net income	**$**	**1.20**	$	1.62	**$**	**4.43**	$	4.07
Diluted:								
Income before cumulative effect of an accounting change	**$**	**1.19**	$	1.61	**$**	**4.40**	$	4.03
Cumulative effect of an accounting change, net of tax								0.01
Net income	**$**	**1.19**	$	1.61	**$**	**4.40**	$	4.04

(a) Assumes conversion of contingently convertible bonds due to the adoption of Emerging Issues Task Force Issue No. 04-8 Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share.

(b) Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price for the period and would have been antidilutive. The number of shares excluded was 7 million and 14 million for the nine-month periods ended September 30, 2007 and 2006, respectively.

Shareholders Equity

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG s Board of Directors increased AIG s share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. In March 2007, AIG entered into a $3 billion structured share repurchase arrangement and AIG entered into additional $1 billion structured share repurchase arrangements in each of May and September 2007. A total of 55,103,845 shares were repurchased during the first nine months of 2007. The portion of the payments advanced by AIG under the structured share repurchase arrangements that had not yet been utilized to repurchase shares at September 30, 2007, amounting to $1.28 billion, has been recorded as a component of shareholders equity under the caption Payments advanced to purchase shares. Purchases have continued subsequent to September 30, 2007, with an additional 13,964,098 shares purchased from October 1 through November 5, 2007. All shares repurchased are recorded as treasury stock at cost.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

3. Shareholders Equity and Earnings Per Share (EPS) *(continued)*

The quarterly dividend per common share, commencing with the dividend declared in May 2007 and paid on September 21, 2007, was $0.20.

The following table summarizes the changes in retained earnings during the first nine months of 2007:

(in millions)		September 30, 2007
Retained earnings:		
Balance at beginning of year	$	84,996
Cumulative effect of accounting changes, net of tax		(203)
Adjusted balance, beginning of year		84,793
Net income		11,492
Dividends to shareholders		(1,455)
Balance, end of period	$	94,830

4. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

Starr International Company, Inc. (SICO) has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant s voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO s Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO s notice to participants in the SICO Plans. See also Note 6(b) Commitments herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG s adoption of FAS No. 123R Share-Based Payments (FAS 123R), Starr is considered to be an economic interest holder in AIG. As a result, compensation expense of $54 million was included in the first nine months of 2006 with respect to the Starr tender offer.

Compensation expense with respect to the SICO Plans aggregated $9 million and $14 million for the three-month periods ended September 30, 2007 and 2006, respectively, and $29 million and $104 million for the nine-month periods ended September 30, 2007 and 2006, respectively. Compensation expense for the first nine months of 2006 included various out of period adjustments totaling $61 million, primarily relating to stock splits and other miscellaneous items for the SICO plans.

5. Ownership

According to the Schedule 13D filed on March 20, 2007 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be deemed to beneficially own 354,987,261 shares of AIG s common stock at that date. Based on the shares of AIG s common stock outstanding as of October 31, 2007, this ownership would represent approximately 14 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Securities Exchange Act of 1934 (Exchange Act), reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to March 20, 2007.

6. Commitments, Contingencies and Guarantees

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

6. Commitments, Contingencies and Guarantees *(continued)*

subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) Litigation and Investigations

Litigation Arising from Operations. AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. In AIG s insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG s reserve for losses and loss expenses. However, in certain circumstances, AIG provides disclosure because of the size or nature of the potential liability to AIG. The potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Litigation Arising from Insurance Operations Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia,* that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. The trial court is currently considering, under standards mandated by the Alabama Supreme Court, whether a class action can be certified and whether the defendants in the case brought by the intervenors should be dismissed. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Litigation Arising from Insurance Operations Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants motion for summary judgment and granted plaintiffs partial motion for summary judgment, holding that the AIG subsidiary was a group purchaser and, therefore, potentially subject to liability under the Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary is appealing the class certification ruling and is seeking an appeal from the jurisdictional ruling. AIG believes that it has meritorious defenses to plaintiffs claims and expects that the ultimate resolution of this matter will not have a material adverse effect on AIG s consolidated financial condition or results of operations for any period.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

6. Commitments, Contingencies and Guarantees *(continued)*

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $344 million, including interest thereon, are included in other assets at September 30, 2007. At that date, approximately $326 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation. The National Workers Compensation Reinsurance Pool, on behalf of its participant members, has filed a lawsuit against AIG with respect to the underpayment of such assessments. The National Association of Insurance Commissioners has formed a Settlement Review Working Group directed by the State of Indiana, which has commenced its own investigation into the underreporting of workers compensation premium. In addition, similar lawsuits filed by the Attorney General of the State of Minnesota, the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association are pending. AIG cannot currently estimate whether the amount ultimately required to settle these claims will exceed the funds escrowed or otherwise accrued for this purpose.

The remaining escrowed funds, which amounted to $18 million at September 30, 2007, are set aside for settlements for certain specified AIG policyholders. During the first nine months of 2007, approximately $367 million was paid out from escrow in exchange for releasing AIG and its subsidiaries from any alleged liability relating to, among other things, brokerage practices alleged in the NYAG settlement. Any funds remaining at the end of the escrow period can be used to resolve claims asserted by policyholders relating to such insurance brokerage practices, including those described in Private Litigation below.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors, including the shareholder lawsuits described herein.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG s internal control over financial reporting, the policies, procedures and effectiveness of AIG s regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Other than as described above, at the current time, AIG cannot predict the outcome of the matters described above, or estimate any potential additional costs related to these matters.

Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc. Securities Litigation.* Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG s publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used income smoothing products and other techniques to inflate its earnings; (3) concealed that it marketed and sold income smoothing insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG s former Chief Executive Officer manipulated AIG s stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing.

ERISA Action. Between November 30, 2004 and July 1, 2005, several Employee Retirement Income Security Act of 1974 (ERISA) actions were filed on behalf of purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG s Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG s Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. Plaintiffs allege that defendants violated duties under ERISA by allowing the plans to offer AIG stock as a permitted investment, when defendants allegedly knew it was not a prudent investment, and by failing to provide participants with accurate information about AIG stock. AIG s motion to dismiss was denied by

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

6. Commitments, Contingencies and Guarantees *(continued)*
order dated December 12, 2006. AIG filed an answer on February 12, 2007, denying plaintiffs allegations of wrongdoing and asserting affirmative defenses to plaintiffs claims. AIG expects that the ultimate resolution of this matter will not have a material adverse effect on AIG s consolidated financial condition or results of operations for any period.

Derivative Actions Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG s former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG s Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has entered an order staying the derivative case in the Southern District of New York pending resolution of the consolidated derivative action in the Delaware Chancery Court (discussed below). The court also has entered an order that termination of certain named defendants from the Delaware derivative action applies to the New York derivative action without further order of the court. On October 17, 2007, plaintiffs and those AIG officer and director defendants against whom the shareholder plaintiffs in the Delaware action are no longer pursuing claims filed a stipulation providing for all claims in the New York action against such defendants to be dismissed with prejudice. Former directors and officers Maurice R. Greenberg and Howard I. Smith have asked the court to refrain from so ordering this stipulation.

Derivative Actions Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits have been consolidated into a single action. The amended consolidated complaint named 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, were current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. Earlier in 2007, the Court approved an agreement that AIG be realigned as plaintiff, and, on June 13, 2007, acting on the direction of the special committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the special committee filed a motion to terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG s complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. Certain defendants have subsequently filed motions to dismiss plaintiffs complaint, as well as defendants Greenberg and Smith s third-party complaints. On September 28, 2007, AIG and the shareholder plaintiffs filed a combined amended complaint in which AIG continued to assert claims against defendants Greenberg and Smith and took no position as to the claims asserted by the shareholder plaintiffs in the remainder of the combined amended complaint. In that pleading, the shareholder plaintiffs are no longer pursuing claims against certain AIG officers and directors. The factual allegations, legal claims and relief sought in the Delaware action are similar to those alleged in the New York derivative actions, except that shareholder plaintiffs in the Delaware derivative action assert claims only under state law. Certain defendants have filed motions to dismiss the shareholder plaintiffs claims. The shareholder plaintiffs have moved to sever their claims to a separate action. AIG has joined that motion to the extent that, among other things, the claims brought by AIG against defendants Greenberg and Smith remain for prosecution in the pending action. AIG also has moved to stay discovery in the Delaware derivative action pending the resolution of the claims against AIG in the New York consolidated securities action. That motion, together with the motion to sever, is currently pending before the court.

In December 2002, a derivative lawsuit was filed in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG s corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr s owners. The complaint also alleged that the service fees and rental

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

6. Commitments, Contingencies and Guarantees *(continued)*
payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Messrs. Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants motion to dismiss, except with respect to plaintiff s challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG s corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On April 20, 2007, the individual defendants and Starr filed a motion seeking leave of the Court to assert a cross-claim against AIG and a third-party complaint against PwC and the directors previously dismissed from the action, as well as certain other AIG officers and employees. On June 13, 2007, the Court denied the individual defendants motion to file a third-party complaint, but granted the proposed cross-claim against AIG. On June 27, 2007, Starr filed its cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and setoff. AIG has filed an answer and moved to dismiss Starr s cross-claim to the extent it seeks affirmative relief, as opposed to a reduction in the judgment amount. Starr has agreed to withdraw its claim for contribution and clarified that it is not seeking any relief on behalf of the individual defendants. AIG s motion to dismiss Starr s claim for affirmative relief is currently pending before the Court. Document discovery and depositions are currently ongoing.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 24 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated or will be consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *First Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *First Employee Benefits Complaint,* and, together with the *First Commercial Complaint*, the multi-district litigation).

The plaintiffs in the *First Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *First Commercial Complaint* also named ten brokers and fourteen other insurers as defendants (two of which have since settled). The *First Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through bid-rigging and steering practices. The *First Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *First Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the *First Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *First Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *First Employee Benefits Complaint*, with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *First Commercial Complaint.*

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

6. Commitments, Contingencies and Guarantees *(continued)*

broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. On February 16, 2007, the case was transferred to Judge Garrett E. Brown, Chief Judge of the District of New Jersey. On April 5, 2007, Chief Judge Brown granted the defendants renewed motions to dismiss the *First Commercial Complaint* and *First Employee Benefits Complaint* with respect to the antitrust and RICO claims. The claims were dismissed without prejudice and the plaintiffs were given 30 days, later extended to 45 days, to file amended complaints. On April 11, 2007, the Court stayed all proceedings, including all discovery, that are part of the multi-district litigation until any renewed motions to dismiss the amended complaints are resolved.

A number of complaints making allegations similar to those in the *First Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation and have petitioned to have a recently filed action transferred to the District of New Jersey for consolidation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed. Defendants filed their motions to dismiss, and on September 24, 2007, the court denied the motions with respect to the state antitrust, RICO, and common law claims and granted the motions with respect to both the Florida insurance bad faith claim against AIG (with prejudice) and the punitive damages claim (without prejudice). Discovery in this action is ongoing.

Plaintiffs filed amended complaints in both *In re Insurance Brokerage Antitrust Litigation* (the *Second Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Second Employee Benefits Complaint*) along with revised particularized statements in both actions on May 22, 2007. The allegations in the *Second Commercial Complaint* and the *Second Employee Benefits Complaint* are substantially similar to the allegations in the *First Commercial Complaint and First Employee Benefits Complaint*, respectively. The complaints also attempt to add several new parties and delete others; the *Second Commercial Complaint* adds two new plaintiffs and twenty seven new defendants (including three new AIG defendants), and the *Second Employee Benefits Complaint* adds eight new plaintiffs and nine new defendants (including two new AIG defendants). The defendants filed motions to dismiss the amended complaints and to strike the newly added parties. The Court granted (without leave to amend) defendants motions to dismiss the federal antitrust and RICO claims on August 31, 2007 and September 28, 2007, respectively. The Court declined to exercise supplemental jurisdiction over the state law claims in the *Second Commercial Complaint* and therefore dismissed it in its entirety. The *Second Employee Benefits Complaint* is still before the Court, pending a decision on defendants motion for summary judgment on the ERISA claims.

On August 24, 2007, the Ohio Attorney General filed a complaint in the Ohio Court of Common Pleas against AIG and a number of its subsidiaries, as well as several other broker and insurer defendants, asserting violation of Ohio s antitrust laws. The complaint, which is similar to the *Second Commercial Complaint*, alleges that AIG and the other broker and insurer defendants conspired to allocate customers, divide markets, and restrain competition in commercial lines of casualty insurance sold through the broker defendant. The complaint seeks treble damages on behalf of Ohio public purchasers of commercial casualty insurance, disgorgement on behalf of both public and private purchasers of commercial casualty insurance, as well as a $500 per day penalty for each day of conspiratorial conduct.

Litigation Relating to 21st Century. Shortly after the announcement in late January 2007 of AIG s offer to acquire the outstanding shares of 21st Century Insurance Group (21st Century) not already owned by AIG and its subsidiaries, two related class actions were filed in the Superior Court of California, Los Angeles County, against AIG, 21st Century, and the individual members of 21st Century s Board of Directors, two of whom are current executive officers of AIG. The actions were filed purportedly on behalf of the minority shareholders of 21st Century and assert breaches of fiduciary duty in connection with the AIG proposal. The complaints alleged that the proposed per share price was unfair and sought preliminary and permanent injunctive relief to enjoin the consummation of the proposed transaction. On May 23, 2007, a third action was filed alleging breaches of fiduciary duty by the same defendants based upon their entering into the merger agreement and taking steps to complete the contemplated merger, and seeking injunctive relief comparable to that sought in the first two complaints. All three actions were consolidated under the caption *In re 21st Century Shareholder Litigation.* On August 14, 2007, the court dismissed the action at the request of the plaintiffs.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO s allegations and setting forth defenses to SICO s claims. In addition, AIG filed counterclaims asserting breach of contract, unjust en-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

6. Commitments, Contingencies and Guarantees *(continued)*
richment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO s breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been substantially concluded and SICO s motion for summary judgment is pending.

Regulatory Investigations. Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry-wide practices as well as other broker-related conduct, such as alleged bid-rigging. In addition, various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG s transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG s ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG s consolidated financial condition, although it is possible that the effect would be material to AIG s consolidated results of operations for an individual reporting period.

(b) Commitments

Flight Equipment

At September 30, 2007, ILFC had committed to purchase 245 new aircraft deliverable from 2007 through 2017 at an estimated aggregate purchase price of $21.0 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

Other Commitments

In the normal course of business, AIG enters into commitments to invest in limited partnerships, private equities, hedge funds and mutual funds and to purchase and develop real estate in the U.S. and abroad. These commitments totaled $5.98 billion at September 30, 2007.

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed in Note 4 herein).

(c) Contingencies

Loss Reserves. Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG s ultimate loss reserves will not develop adversely and materially exceed AIG s current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Synthetic Fuel Tax Credits. AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. AIG evaluates the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of fluctuating domestic crude oil prices, AIG evaluates and adjusts production levels when appropriate in light of this risk. Recent increases in oil prices have reduced the current estimate of 2007

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

tax credits. Under current legislation, the opportunity to generate additional tax credits from the production and sale of synthetic fuel expires on December 31, 2007.

Lease Transactions. In June and August, 2007, field agents at the Internal Revenue Service issued Notices of Proposed Adjustment (NOPAs) relating to a series of lease transactions by an AIG subsidiary. In the NOPAs, the field agents asserted that the leasing transactions were lease-in lease-out transactions described in Revenue Ruling 2002-69 and proposed adjustments to taxable income of approximately $203 million in the aggregate for the years 1998, 1999, 2001 and 2002.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG s derivative activity is transacted by AIGFP. See Note 9 below and see Note 19 to the consolidated financial statements in the 2006 Annual Report on Form 10-K.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

7. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and other postretirement benefits:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended September 30, 2007						
Components of net periodic benefit cost:						
Service cost	**$ 22**	**$ 30**	**$ 52**	**$ 1**	**$ 3**	**$ 4**
Interest cost	**12**	**45**	**57**	**1**	**3**	**4**
Expected return on assets	**(9)**	**(53)**	**(62)**			
Amortization of prior service cost	**(2)**	**(1)**	**(3)**			
Amortization of net loss	**2**	**9**	**11**			
Amortization of initial net obligation	**1**		**1**			
Settlement loss		**3**	**3**			
Net periodic benefit cost	**$ 26**	**$ 33**	**$ 59**	**$ 2**	**$ 6**	**$ 8**
Three Months Ended September 30, 2006						
Components of net periodic benefit cost:						
Service cost	$ 18	$ 32	$ 50	$ 1	$ 1	$ 2
Interest cost	9	41	50	1	3	4
Expected return on assets	(7)	(48)	(55)			
Amortization of prior service cost	(3)	(1)	(4)		(2)	(2)
Amortization of transitional liability	1		1			
Recognized actuarial loss	4	18	22			
Net periodic benefit cost	$ 22	$ 42	$ 64	$ 2	$ 2	$ 4
Nine Months Ended September 30, 2007						
Components of net periodic benefit cost:						
Service cost	**$ 66**	**$ 90**	**$ 156**	**$ 4**	**$ 8**	**$ 12**
Interest cost	**36**	**134**	**170**	**2**	**11**	**13**
Expected return on assets	**(27)**	**(160)**	**(187)**			
Amortization of prior service cost	**(7)**	**(2)**	**(9)**		**(1)**	**(1)**
Amortization of net loss	**7**	**27**	**34**			
Amortization of initial net obligation	**1**		**1**			
Settlement loss	**1**	**3**	**4**			
Net periodic benefit cost	**$ 77**	**$ 92**	**$ 169**	**$ 6**	**$ 18**	**$ 24**
Nine Months Ended September 30, 2006						
Components of net periodic benefit cost:						

Service cost	$ 55	$ 94	$ 149	$ 3	$ 4	$ 7
Interest cost	26	122	148	2	8	10
Expected return on assets	(21)	(145)	(166)			
Amortization of prior service cost	(7)	(2)	(9)		(5)	(5)
Amortization of transitional liability	1		1			
Recognized actuarial loss	12	56	68			
Net periodic benefit cost	$ 66	$ 125	$ 191	$ 5	$ 7	$ 12

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

8. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

AIG Life Holdings (US), Inc. (AIGLH), formerly known as American General Corporation, is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AIGLH.

AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp.

AIG Program Funding, Inc. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Program Funding, Inc., which was established in 2007.

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
September 30, 2007							
Assets:							
Investments and financial services assets	$ 15,718	$ 40	$	$	$ 865,584	$ (19,490)	$ 861,852
Cash	25	1			2,223		2,249
Carrying value of subsidiaries and partially owned companies, at equity	118,252	24,378			11,451	(152,804)	1,277
Other assets	4,693	2,650			199,420	(36)	206,727
Total assets	$ 138,688	$ 27,069	$	$	$ 1,078,678	$ (172,330)	$ 1,072,105
Liabilities:							
Insurance liabilities	$ 48	$	$	$	$ 518,879	$ (63)	$ 518,864
Debt	28,758	2,136			163,878	(18,587)	176,185
Other liabilities	5,815	3,191			264,348	(465)	272,889

Total liabilities	**34,621**	**5,327**			**947,105**	**(19,115)**	**967,938**
Preferred shareholders equity in subsidiary companies					**100**		**100**
Total shareholders equity	**104,067**	**21,742**			**131,473**	**(153,215)**	**104,067**
Total liabilities, preferred shareholders equity in subsidiary companies and shareholders equity	**$ 138,688**	**$ 27,069**	**$**	**$**	**$ 1,078,678**	**$ (172,330)**	**$ 1,072,105**

22

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
December 31, 2006							
Assets:							
Investments and financial services assets	$ 7,346	$	$ *	$	$ 800,350	$ (14,822)	$ 792,874
Cash	76		*		1,514		1,590
Carrying value of subsidiaries and partially owned companies, at equity	109,125	27,967			8,436	(144,427)	1,101
Other assets	3,989	2,622	*		179,183	(1,949)	183,845
Total assets	$ 120,536	$ 30,589	$ *	$	$ 989,483	$ (161,198)	$ 979,410
Liabilities:							
Insurance liabilities	$ 21	$	$	$	$ 497,514	$ (64)	$ 497,471
Debt	15,157	2,136	*		146,206	(14,820)	148,679
Other liabilities	3,681	3,508	*		225,685	(1,482)	231,392
Total liabilities	18,859	5,644	*	$	869,405	(16,366)	877,542
Preferred shareholders equity in subsidiary companies					191		191
Total shareholders equity	101,677	24,945	*		119,887	(144,832)	101,677
Total liabilities, preferred shareholders equity in subsidiary companies and	$ 120,536	$ 30,589	$ *	$	$ 989,483	$ (161,198)	$ 979,410

shareholders equity

**Less than $1 million.*

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

American International Group, Inc. and Subsidiaries

8. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended September 30, 2007							
Operating income (loss)	**$ (587)**	**$ (37)**	**$ ***	**$**	**$ 5,503**	**$**	**$ 4,879**
Equity in undistributed net income of consolidated subsidiaries	**2,343**	**55**				**(2,398)**	
Dividend income from consolidated subsidiaries	**1,109**	**320**				**(1,429)**	
Income taxes	**(220)**	**256**	*****		**1,427**		**1,463**
Minority interest					**(331)**		**(331)**
Net income (loss)	**$ 3,085**	**$ 82**	**$ ***	**$**	**$ 3,745**	**$ (3,827)**	**$ 3,085**
Three Months Ended September 30, 2006							
Operating income (loss)	$ (215)	$ (49)	$ *	$	$ 6,565	$	$ 6,301
Equity in undistributed net income of consolidated subsidiaries	4,223	420				(4,643)	
Dividend income from consolidated subsidiaries	287	134				(421)	
Income taxes (benefits)	71	(17)	*		1,889		1,943
Minority interest					(134)		(134)

Net income (loss)	$ 4,224	$ 522	$ *	$	$ 4,542	$ (5,064)	$ 4,224
Nine Months Ended September 30, 2007							
Operating income (loss)	**$ (1,130)**	**$ (123)**	**$ ***	**$**	**$ 18,632**	**$**	**$ 17,379**
Equity in undistributed net income of consolidated subsidiaries	**9,192**	**546**				**(9,738)**	
Dividend income from consolidated subsidiaries	**3,274**	**978**				**(4,252)**	
Income taxes	**(156)**	**249**	*****		**4,775**		**4,868**
Minority interest					**(1,019)**		**(1,019)**
Net income (loss)	**$ 11,492**	**$ 1,152**	**$ ***	**$**	**$ 12,838**	**$ (13,990)**	**$ 11,492**
Nine Months Ended September 30, 2006							
Operating income (loss)	$ (937)	$ (135)	$ *	$	$ 17,407	$	$ 16,335
Equity in undistributed net income of consolidated subsidiaries	10,990	1,088				(12,078)	
Dividend income from consolidated subsidiaries	854	592				(1,446)	
Income taxes (benefits)	332	(47)	*		4,781		5,066
Minority interest					(694)		(694)
Cumulative effect of an accounting change, net of tax	34						34
Net income (loss)	$ 10,609	$ 1,592	$ *	$	$ 11,932	$ (13,524)	$ 10,609

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

8. Information Provided in Connection with Outstanding Debt *(continued)*
Condensed Consolidating Statement of Cash Flows

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Consolidated AIG
Nine Months Ended September 30, 2007						
Net cash provided by operating activities	$ 1,627	$ 375	$ *	$	$ 25,054	$ 27,056
Cash flows from investing:						
Invested assets disposed	782				125,971	126,753
Invested assets acquired	(8,767)				(182,911)	(191,678)
Other	186	(220)	*		(970)	(1,004)
Net cash used in investing activities	(7,799)	(220)	*		(57,910)	(65,929)
Cash flows from financing activities:						
Issuance of debt	13,540				61,025	74,565
Repayments of debt	(1,143)				(48,500)	(49,643)
Payments advanced to purchase shares	(2,955)				(2,045)	(5,000)
Cash dividends paid to shareholders	(1,372)					(1,372)
Other	(1,949)	(154)	*		23,077	20,974
Net cash provided by (used in) financing activities	6,121	(154)	*		33,557	39,524
Effect of exchange rate changes on cash					8	8
Change in cash	(51)	1	*		709	659
Cash at beginning of period	76				1,514	1,590
Cash at end of period	$ 25	$ 1	$ *	$	$ 2,223	$ 2,249

Nine Months Ended September 30, 2006						
Net cash (used in) provided by operating activities	$ (2,526)	$ 160	$ *	$	$ 6,403	$ 4,037
Cash flows from investing:						
Invested assets disposed	2,147				118,563	120,710
Invested assets acquired	(5,555)				(166,679)	(172,234)
Other	790	(17)	*		(1,393)	(620)
Net cash used in investing activities	(2,618)	(17)	*		(49,509)	(52,144)
Cash flows from financing activities:						
Issuance of debt	7,445				45,527	52,972
Repayments of debt	(1,345)				(24,986)	(26,331)
Cash dividends paid to shareholders	(1,209)					(1,209)
Other	91	(143)	*		22,196	22,144
Net cash provided by (used in) financing activities	4,982	(143)	*		42,737	47,576
Effect of exchange rate changes on cash					59	59
Change in cash	(162)		*		(310)	(472)
Cash at beginning of period	190				1,707	1,897
Cash at end of period	$ 28	$	$ *	$	$ 1,397	$ 1,425

**Less than $1 million.*

25

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

9. Derivatives and Hedge Accounting

AIG uses derivatives and other financial instruments as part of its financial risk management programs and as part of its investment operations. AIGFP also transacts in derivatives as a dealer.

Derivatives, as defined in FAS 133, are financial arrangements among two or more parties with returns linked to or derived from some underlying equity, debt, commodity or other asset, liability, or foreign exchange rate or other index or the occurrence of a specified payment event. Derivative payments may be based on interest rates, exchange rates, prices of certain securities, commodities, or financial or commodity indices or other variables.

Unless subject to a scope exclusion, AIG carries all derivatives on the consolidated balance sheet at fair value. The changes in fair value of the derivative transactions of AIGFP are presented as a component of AIG s operating income.

AIGFP

AIGFP, in the ordinary course of operations and as principal, structures and enters into derivative transactions to meet the needs of counterparties who may be seeking to hedge certain aspects of such counterparties operations or obtain a desired financial exposure. AIGFP also enters into derivative transactions to mitigate risk in its exposures (interest rates, currencies, commodities, credit and equities) arising from such transactions. Such instruments are carried at market or fair value, whichever is appropriate, and are reflected on the balance sheet in Unrealized gain on swaps, options and forward transactions and Unrealized loss on swaps, options and forward contracts.

Beginning in the first quarter of 2007, AIGFP designated certain interest rate swaps as fair value hedges of the benchmark interest rate risk on certain of its interest bearing financial assets and liabilities. In these hedging relationships, AIG is hedging its fixed rate available for sale securities and fixed rate borrowings. AIGFP also designated foreign currency forward contracts as fair value hedges for changes in spot foreign exchange rates of the non-U.S. dollar denominated available for sale debt securities. Under these strategies, all or portions of individual or multiple derivatives may be designated against a single hedged item.

At inception of each hedging relationship, AIGFP performs and documents its prospective assessments of hedge effectiveness to demonstrate that the hedge is expected to be highly effective. For hedges of interest rate risk, AIGFP uses regression to demonstrate the hedge is highly effective, while it uses the periodic dollar offset method for its foreign currency hedges. AIGFP uses the periodic dollar offset method to assess whether its hedging relationships were highly effective on a retrospective basis. The prospective and retrospective assessments are updated on a daily basis. The passage of time component of the hedging instruments and the forward points on foreign currency hedges are excluded from the assessment of hedge effectiveness and measurement of hedge ineffectiveness. AIGFP does not utilize the shortcut, matched terms or equivalent methods.

The change in fair value of the derivative that qualifies under the requirements of FAS 133 as a fair value hedge is recorded in current period earnings along with the gain or loss on the hedged item for the hedged risk. For interest rate hedges, the adjustments to the carrying value of the hedged items are amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings.

For the three and nine months ended September 30, 2007, AIGFP recognized net losses of $5 million and $3 million in earnings, respectively, representing hedge ineffectiveness, and also recognized net losses of $152 million and $363 million, respectively, related to the portion of the hedging instruments excluded from the assessment of hedge effectiveness. All these amounts are reflected in Other income. AIGFP did not apply hedge accounting in 2006.

Other Derivative Users

AIG and its subsidiaries (other than AIGFP) also use derivatives and other instruments as part of their financial risk management programs. Interest rate derivatives (such as interest rate swaps) are used to manage interest rate risk associated with investments in fixed income securities, commercial paper issuances, medium and long-term note offerings, and other interest rate sensitive assets and liabilities. In addition, foreign exchange derivatives (principally cross currency swaps, forwards and options) are used to economically mitigate risk associated with non-U.S. dollar denominated debt, net capital exposures and foreign exchange transactions. The derivatives are effective economic hedges of the exposures they are meant to offset.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*
American International Group, Inc. and Subsidiaries

9. Derivatives and Hedge Accounting *(continued)*

In 2007, AIG and its subsidiaries other than AIGFP designated certain derivatives as either fair value or cash flow hedges of their debt. The fair value hedges included (i) interest rate swaps that were designated as hedges of the change in the fair value of fixed rate debt attributable to changes in the benchmark interest rate and (ii) foreign currency swaps designated as hedges of the change in fair value of foreign currency denominated debt attributable to changes in foreign exchange rates and/or the benchmark interest rate. With respect to the cash flow hedges, (i) interest rate swaps were designated as hedges of the changes in cash flows on floating rate debt attributable to changes in the benchmark interest rate, and (ii) foreign currency swaps were designated as hedges of changes in cash flows on foreign currency denominated debt attributable to changes in the benchmark interest rate and foreign exchange rates.

AIG assesses, both at the hedge s inception and on an ongoing basis, whether the derivatives used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. Regression analysis is employed to assess the effectiveness of these hedges both on a prospective and retrospective basis. AIG does not utilize the shortcut, matched terms or equivalent methods.

The change in fair value of derivatives designated and effective as fair value hedges along with the gain or loss on the hedged item are recorded in net realized capital gains (losses). Upon discontinuation of hedge accounting, the cumulative adjustment to the carrying value of the hedged item resulting from changes in the benchmark interest rate is amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings. During both the three and nine months ended September 30, 2007, AIG recognized a loss of less than $1 million in earnings related to the ineffective portion of the hedging instruments. During the three and nine months ended September 30, 2007, AIG also recognized losses of $45 million and $53 million, respectively, related to the change in the hedging instruments forward points excluded from the assessment of hedge effectiveness.

The effective portion of the change in fair value of a derivative qualifying as a cash flow hedge is recorded in Accumulated other comprehensive income (loss), until earnings are affected by the variability of cash flows in the hedged item. The ineffective portion of these hedges is recorded in net realized capital gains (losses). During both the three and nine months ended September 30, 2007, AIG recognized losses of $1 million in earnings representing hedge ineffectiveness. At September 30, 2007, $10 million of the deferred net loss in Accumulated other comprehensive income is expected to be recognized in earnings during the next 12 months. All components of the derivatives gains and losses were included in the assessment of hedge effectiveness. There were no instances of the discontinuation of hedge accounting in 2007.

10. Cash Flows

As part of its ongoing remediation activities, AIG has made certain revisions to the Consolidated Statement of Cash Flows, primarily relating to certain elements of net realized capital gains, the effect of reclassifying certain policyholders account balances from Other policyholder funds to Policyholders contract deposits, the elimination of certain intercompany balances and revisions related to separate account assets. Accordingly, AIG revised the previous periods presented to conform to the revised presentation.

The revisions and their effect on the Consolidated Statement of Cash Flows for the nine months ended September 30, 2006 are presented below:

(in millions)	**Originally Reported September 30, 2006**	**Revisions**	**As Revised**
Cash flows from operating activities	$ 6,004	$ (1,967)	$ 4,037
Cash flows from investing activities	(51,400)	(744)	(52,144)

Cash flows from financing activities	44,865	2,711	47,576
Effect of exchange rate changes on cash	59		59
Change in cash	(472)		(472)

27

ITEM 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Management s Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG s operations, financial condition and liquidity and certain other significant matters.

INDEX

Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report on Form 10-Q and other publicly available documents may include, and AIG s officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG s belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG s control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG s businesses, financial position, results of operations, cash flows and liquidity, the effect of credit rating changes on AIG s businesses and competitive position, the unwinding and resolving of various relationships between AIG and SICO and AIG s strategy for growth, product development, market position, financial results and reserves. It is possible that AIG s actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG s actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management s Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of AIG s Annual Report on Form 10-K for the year ended December 31, 2006 (2006 Annual Report on Form 10-K). AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

In addition to reviewing AIG s results for the first nine months of 2007, this Management s Discussion and Analysis of Financial Condition and Results of Operations supplements and updates the information and discussion included in the 2006 Annual Report on Form 10-K. Throughout this Management s Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG s insurance competitors. AIG has also incorporated into this discussion cross-references to additional information included in this Quarterly Report on Form 10-Q and in the 2006 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product or service line, consistent with its management structure. AIG s segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG s operations in 2007 and 2006 were conducted by its subsidiaries through these segments. Through these segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG s major strengths and sets it apart from its competitors. AIG s Other category consists of items not allocated to AIG s operating segments.

AIG s subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG s Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its spread-based business activities, AIG issues various debt instruments in the public and private markets.

Outlook

The following paragraphs supplement and update the information and discussion included in Management s Discussion and Analysis of Financial Condition and Results of Operations Outlook, in the 2006 Annual Report on Form 10-K to reflect developments in or affecting AIG s business during 2007.

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophes or other significant losses that affect the overall capacity of the industry to provide coverage. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG s broad product line and extensive distribution networks in the U.S. and abroad. In October 2007, for example, AIG expanded its Foreign General insurance operations in Germany through the acquisition of Württembergische and Badische Versicherungs-Aktiengesellschaft.

Workers compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for aviation, excess casualty, D&O and certain other lines of insurance also continue to decline due to competitive pressures. AIG also expects further price erosion for its foreign commercial lines during 2008. There can be no assurance that price erosion will not become more widespread or that AIG s profitability will not deteriorate from current levels in major commercial lines; however, AIG seeks to mitigate this risk by constantly seeking out profitable opportunities across its diverse product lines and distribution networks.

AIG has commenced a realignment of its Foreign General insurance operations, many of which were historically conducted through branches of U.S. companies. On December 1, 2007, Landmark Insurance Company Limited, a U.K. subsidiary, will assume all of the insurance liabilities of the U.K. branch of New Hampshire Insurance Company and will change its name to AIG U.K. Ltd.

In AIG s Foreign Retirement Services business, the continued weak yen has resulted in higher than normal surrenders and that trend, if prolonged, could further accelerate the amortization of deferred acquisition costs (DAC). Similarly, in the Domestic Retirement Services business, the competitive environment and the age of the in-force blocks of individual fixed annuities could result in ongoing heightened surrender activity.

In Japan, the National Tax Authority in cooperation with the Life Insurance Association of Japan is reviewing the tax treatment for increasing term life insurance, which may affect the amount of premiums that qualify as tax deductions for business owners. As a result of this review, AIG s life insurance companies in Japan suspended the sale of increasing term life insurance from early April 2007. This action had an adverse effect on life insurance sales in the third quarter of 2007 and AIG expects that trend to continue for the remainder of the year. AIG companies in Japan have taken several measures aimed at increasing sales of other products in the Japanese market, in particular sales of U.S. dollar life insurance products.

In Japan, full deregulation of banks with respect to insurance product sales will become effective in December 2007. AIG expects that it will be able to leverage its existing bank relationships and innovative product expertise to expand sales of both life and accident and health products beginning in 2008.

During the third quarter of 2007, the Internal Revenue Service proposed to change the treatment of the dividends-received deduction on separate account assets held in connection with variable annuity contracts. This proposal was withdrawn later in the quarter for additional study. Should this change be adopted, AIG does not expect it would have a material effect on AIG s consolidated financial position or results of operations for any period.

In March 2007, the U.S. Treasury Department published proposed new regulations that, if adopted in their current form, would limit the ability of U.S. taxpayers to claim foreign tax credits in certain circumstances under the Internal Revenue Code. Should the proposed regulations be adopted in their current form, they would limit AIG s ability to claim foreign tax credits in connection with certain structured transactions entered into by AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP), resulting in a material adverse effect on AIGFP s operating results.

The ongoing disruption in the structured finance markets and the recent downgrades by rating agencies continue to adversely affect AIG s estimates of the fair value of the super senior credit derivatives written by AIGFP. Although it remains difficult to estimate the fair value of these derivatives due to continuing limitations on the availability of market observable data, AIG s best estimate of the further decline in the fair value of AIGFP s super senior credit derivatives since September 30, 2007 is approximately $550 million as of October 31, 2007. The fair value of these derivatives is expected to fluctuate, perhaps materially, in response to changing market conditions, and AIG s estimates of the value of AIGFP s super senior credit derivative portfolio at future dates could therefore be materially different from current estimates. AIG continues to believe that it is highly unlikely that AIGFP will be required to make payments with respect to these derivatives.

The U.S. residential mortgage market is experiencing serious disruption due to credit quality deterioration in a significant portion of loans originated, particularly to non-prime and subprime borrowers, evolving changes in the regulatory environment, a slower residential housing market, increased cost of borrowings for mortgage participants and illiquid credit markets. AIG participates in the U.S. residential mortgage market in several ways: American General Finance, Inc. (AGF) originates principally first-lien mortgage loans and to a lesser extent second-lien mortgage loans to buyers and owners of residential housing; United Guaranty Corporation (UGC) provides first loss mortgage guaranty insurance for high loan-to-value first and second-lien residential mortgages; AIG insurance and financial services subsidiaries invest in mortgage-backed securities and collateralized debt obligations (CDOs) in which the underlying collateral is composed in whole or in part of residential mortgage loans; and AIGFP provides credit protection through credit default swaps on certain super senior tranches of CDOs that have AAA underlying or subordinate layers. The operating results of AIG s consumer finance and mortgage guaranty operations in the United States have been and are likely to continue to be adversely affected by the factors referred to above. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level and the mortgage credit market stabilizes. AIG expects that this downward cycle will continue to adversely affect UGC s operating results for the foreseeable future and will result in a significant operating loss for UGC in 2008. The effect of the downward cycle in the U.S. housing market on AIG s other operations, investment portfolio and overall consolidated financial position could be material if the market disruption continues and expands beyond the U.S. residential mortgage markets, although AIG seeks to mitigate the risks to its business by disciplined underwriting and active risk management.

In recent quarters, AIG s returns from partnerships and other alternative investments were particularly strong, driven by favorable equity market performance and credit conditions. These returns may vary from period to period and declined significantly in the most recent quarter. AIG believes that the particularly strong performance in certain prior periods is not indicative of the returns to be expected from this asset class in future periods.

As part of an ongoing project to increase the standardization of AIG actuarial systems and processes throughout the world, adjustments reflecting certain changes in actuarial estimates for future policy benefits and DAC have been recognized in the Life Insurance & Retirement Services segment results during 2006 and 2007. AIG expects further adjustments over time as these new systems and processes are implemented.

AIG has recorded out of period quarterly adjustments in the last two years due to the remediation of control deficiencies. As AIG continues its remediation activities, AIG expects to record additional out of period adjustments.

Table of Contents

American International Group, Inc. and Subsidiaries

Consolidated Results

The following table summarizes AIG s consolidated revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income:

	Three Months Ended September 30,		Percentage	Nine Months Ended September 30,		Percentage
(in millions)	**2007**	2006	Increase/ (Decrease)	**2007**	2006	Increase/ (Decrease)
Total revenues	**$ 29,836**	$ 29,247	2%	**$ 91,631**	$ 83,379	10%
Income before income taxes, minority interest and cumulative effect of an accounting change	**4,879**	6,301	(23)	**17,379**	16,335	6
Net income	**$ 3,085**	$ 4,224	(27)%	**$ 11,492**	$ 10,609	8%

AIG s consolidated revenues increased slightly for the three months ended September 30, 2007 compared to the same period in 2006. AIG s consolidated income before income taxes, minority interest and cumulative effect of an accounting change decreased for the three-month period ended September 30, 2007 compared to the same period in 2006 primarily due to higher Net realized capital losses and the operating loss in the Mortgage Guaranty business. Net realized capital losses included other-than-temporary declines of $529 million and foreign currency related losses of $361 million.

AIG s consolidated revenues increased for the nine-month period ended September 30, 2007 compared to the same period in 2006 as revenues increased in each of the operating segments. Operating income increased in all segments with the exception of Life Insurance & Retirement Services, which declined due to an increase in Net realized capital losses compared to the same period in 2006.

Operating income for the three and nine-month periods ended September 30, 2007 was significantly affected by the change in accounting treatment for hedging activities. In the first nine months of 2007, AIGFP applied hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks, offsetting the gains and losses on the derivatives designated as hedges. In 2006, AIGFP did not apply hedge accounting under FAS 133 to any of its assets and liabilities.

During the three months ended September 30, 2007, AIG recorded certain out of period adjustments. These adjustments collectively decreased pre-tax operating income in that quarter by $33 million and net income by $35 million. The adjustments were primarily comprised of a net charge of $49 million ($32 million after tax) in Capital Markets, a $14 million increase in income tax expense related to the remediation of the material weakness in controls over income tax accounting and an increase to operating income of $16 million ($11 million after tax) primarily related to other remediation activities.

For the nine months ended September 30, 2007, out of period adjustments collectively decreased pre-tax operating income by $536 million ($408 million after tax). The adjustments were comprised of a charge of $380 million ($247 million after tax) to reverse net gains on transfers of investment securities among legal entities consolidated within AIGFP and a corresponding increase to Accumulated other comprehensive income; $58 million of additional income tax expense related to the aforementioned remediation activities; $71 million ($46 million after tax) of net realized capital gains related to foreign exchange; and $227 million ($149 million after tax) of additional expense, primarily relating to other remediation activities.

During the three months ended September 30, 2006, out of period adjustments collectively increased pre-tax operating income by $293 million and net income by $73 million. The adjustments were comprised of an increase in income primarily related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133 totalling $151 million ($23 million after tax); increases in bad debt expense of $225 million ($146 million after tax) and earned premiums of $99 million ($65 million after tax), both of which relate to balance sheet reconciliations; an increase in partnership income of $121 million ($79 million after tax), which relates to improved valuation information; a further increase in income from certain investments in unit investment trusts (UCITS) of $116 million ($75 million after tax), as described below; other favorable remediation adjustments of $31 million ($16 million after tax) and an increase in income tax expense of $39 million relating to AIG s ongoing remediation of internal controls over income tax accounting. See also the discussion of AIG s reportable segments in Management s Discussion & Analysis of Financial Condition and Results of Operations.

For the nine months ended September 30, 2006, out of period adjustments collectively increased pre-tax operating income by $173 million and reduced net income by $135 million. The adjustments were comprised of $642 million ($417 million after tax) of additional investment income related to the accounting for UCITS; $194 million ($127 million after tax) of charges primarily related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133; $239 million of additional income tax expense related to the aforementioned remediation activities; $85 million ($55 million after tax) of interest income related to interest earned on deposit contracts; $61 million (before and after tax) of expenses related to the Starr International Company, Inc. (SICO) Deferred Compensation Profit Participation Plans (SICO Plans); $59 million ($38 million after tax) of expenses related to deferred advertising costs; and $240 million ($142 million after tax) of additional expense, primarily related to other remediation activities.

Results for the first nine months of 2006 were also negatively affected by a one-time charge relating to the C.V. Starr & Co., Inc. (Starr) tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before and after tax), both of which were recorded in first quarter of 2006.

AIG s effective income tax rates for the year ended December 31, 2006 and the three-month period ended September 30, 2007 were 30.1 percent and 30.0 percent, respectively. For the nine-month period ended September 30, 2007, the effective income tax rate declined to 28.0 percent, primarily due to recognition of tax benefits associated with the SICO Plans for which the compensation expense had been recognized in prior years. Such tax benefits amounted to $194 million for the nine-month period ended September 30, 2007.

Segment Results

The following table summarizes AIG s operations by major operating segment. (See also Note 2 of Notes to Consolidated Financial Statements.)

	Three Months Ended September 30,		Percentage Increase/	Nine Months Ended September 30,		Percentage Increase/
(in millions)	**2007**	2006	(Decrease)	**2007**	2006	(Decrease)
Revenues[(a)]:						
General Insurance[(b)]	**$ 12,758**	$ 12,615	1%	**$ 38,589**	$ 36,438	6%
Life Insurance & Retirement Services[(b)]	**12,632**	12,542	1	**40,337**	37,303	8
Financial Services[(c)(d)]	**2,785**	3,011	(8)	**7,109**	5,923	20
Asset Management	**1,824**	993	84	**5,721**	3,647	57
Other	**13**	215	(94)	**407**	443	(8)
Consolidation and eliminations	**(176)**	(129)	36	**(532)**	(375)	42
Consolidated	**$ 29,836**	$ 29,247	2%	**$ 91,631**	$ 83,379	10%
Operating income (loss)[(a)]:						
General Insurance[(b)]	**$ 2,439**	$ 2,625	(7)%	**$ 8,511**	$ 7,819	9%
Life Insurance & Retirement Services[(b)]	**1,999**	2,472	(19)	**6,900**	7,483	(8)
Financial Services[(c)(d)]	**669**	1,179	(43)	**1,008**	541	86
Asset Management	**419**	211	99	**2,541**	1,445	76
Other	**(627)**	(186)	237	**(1,557)**	(953)	63
Consolidation and eliminations	**(20)**			**(24)**		
Consolidated	**$ 4,879**	$ 6,301	(23)%	**$ 17,379**	$ 16,335	6%

(a) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, Accounting for Derivative Instruments and Hedging Activities (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the

effect was $(178) million and $165 million in both revenues and operating income. For the nine- month periods ended September 30, 2007 and 2006, respectively, the effect was $(1.06) billion and $(1.13) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings. These gains (losses) for the three and nine months ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133.

(b) Includes the effect of out of period UCITS adjustments. For the three and nine-month periods ended September 30, 2006, the effect was an increase of $92 million and $472 million, respectively, in both revenues and operating income for General Insurance and an increase of $24 million and $240 million, respectively, in revenues and $24 million and $169 million, respectively, in operating income for Life Insurance & Retirement Services.

(c) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the effect was $353 million, and $581 million in both revenues and operating income. For the nine-month periods ended September 30, 2007 and 2006, respectively, the effect was $(250) million and $(1.2) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, as discussed above. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million as discussed above. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.

(d) For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP s super senior credit default swap portfolio.

General Insurance

AIG s General Insurance operations provide property and casualty products and services throughout the world. Foreign operations provided approximately 25 percent and 27 percent of General Insurance operating income for the three months ended September 30, 2007 and 2006, respectively, and approximately 28 percent and 31 percent for the nine months ended September 30, 2007 and 2006, respectively. The decrease in General Insurance operating income in the three-month period ended September 30, 2007 compared to the same period in 2006 was primarily attributable to operating losses from the Mortgage Guaranty business and a decline in operating income in the Foreign

32

General and Personal Lines businesses, partially offset by improved underwriting results for the Domestic Brokerage Group (DBG) and higher net investment income.

Operating income grew in the nine-month period ended September 30, 2007 compared to the same period of 2006, driven by strength in DBG, partially offset by operating losses from the Mortgage Guaranty business.

Life Insurance & Retirement Services

AIG s Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 87 percent and 65 percent of Life Insurance & Retirement Services operating income for the three months ended September 30, 2007 and 2006, respectively, and approximately 68 percent and 67 percent for the nine months ended September 30, 2007 and 2006, respectively. Operating income for the three months ended September 30, 2007 declined compared to the same period in 2006, primarily due to the securities market volatility which resulted in lower investment income and higher net realized capital losses compared to the same period in 2006. For the nine months ended September 30, 2007, operating income declined 8 percent compared to the same period in 2006 due to charges related to balance sheet reconciliation remediation, an industry-wide claims review in Japan, the effect of SOP 05-1, trading account losses and realized capital losses.

Financial Services

AIG s Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services operating income decreased in the three-month period and increased in the nine-month period ended September 30, 2007 compared to the same periods in 2006 due, in large part, to differences in the accounting treatment for hedging activities. In the first quarter of 2007, AIGFP began applying hedge accounting to certain of its interest rate swaps and foreign currency forward contracts that hedge its investments and borrowings. In the second quarter of 2007, AGF and International Lease Finance Corporation (ILFC) began applying hedge accounting to most of their derivatives that hedge interest rate and foreign currency denominated borrowings. Prior to 2007, hedge accounting under FAS 133 was not being applied to any of AIG s derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities. During the three and nine-month periods ended September 30, 2007 operating income was also adversely affected by an unrealized market valuation loss of $352 million on AIGFP s super senior credit default swap portfolio.

ILFC generated strong operating income growth for the three and nine-month periods ended September 30, 2007 compared to the same periods in 2006, driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization.

AGF s operating income decreased in the three and nine months ended September 30, 2007, in large part due to the reduced residential mortgage origination volumes and lower revenues from its mortgage banking activities. Further, in the first nine months of 2007, AGF s mortgage banking operations recorded pre-tax charges of $178 million, representing the estimated cost of implementing the Supervisory Agreement entered into with the Office of Thrift Supervision (OTS), which are discussed in the Consumer Finance results of operations section.

Asset Management

AIG s Asset Management operations include institutional and retail asset management, broker-dealer services and institutional spread-based investment businesses. The Matched Investment Program (MIP) has replaced the GIC program as AIG s principal institutional spread-based investment activity.

Asset Management operating income increased for the three and nine-month periods ended September 30, 2007 compared to the same periods in 2006, primarily due to higher income from consolidated managed partnerships and funds that is entirely offset in Minority interest expense, which is not a component of operating income. Realized capital losses, principally relating to economically effective hedges not qualifying for hedge accounting, also increased for the three months ended September 30, 2007 compared to the same period in 2006. Asset Management operating income also increased for the nine-month period ended September 30, 2007 compared to the same period in 2006 due to increased investment income from consolidated managed partnerships and funds, and a realized capital gain of $398 million on the sale of a portion of AIG s investment in Blackstone Group, LP in connection with its initial public offering, as well as growth in both the Spread-Based Investment business and the Institutional Asset Management business.

Capital Resources

In the first nine months of 2007, AIG issued an aggregate of $4.49 billion of junior subordinated debentures in four series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to repurchase shares of AIG s common stock.

At September 30, 2007, AIG had total consolidated shareholders equity of $104.1 billion and total consolidated borrowings of $176.2 billion, of which $20.3 billion represented AIG s net borrowings. At that date, $155.9 billion of total borrowings represented obligations of

AIG s subsidiaries not guaranteed by AIG, matched borrowings by AIG parent or AIGFP, obligations of guaranteed investment agreements, junior subordinated debt, liabilities connected to trust preferred stock and hybrid financial instrument liabilities.

In February 2007, AIG s Board of Directors increased AIG s share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. Share repurchases during 2007 are described under Capital Resources and Liquidity Share Repurchases and in Item 2. of Part II of this Quarterly Report on Form 10-Q.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At September 30, 2007, AIG s consolidated invested assets, primarily held by its subsidiaries, included $41.2 billion in cash and short-term investments. The increase in cash and short-term investments during the quarter was primarily the result of the steps AIG took to enhance the liquidity of its portfolios in light of the market disruption during the quarter. Consolidated net cash provided from operating activities in the first nine months of 2007 amounted to $27.1 billion. Management believes that AIG s liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG s new dividend policy and repurchases of common stock.

Critical Accounting Estimates

AIG considers its most critical accounting estimates to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG s results of operations would be directly affected.

Throughout this Management s Discussion and Analysis of Financial Condition and Results of Operations, AIG s critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses
(General Insurance):

Loss trend factors: used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.

Expected loss ratios for the latest accident year: in this case, accident year 2007 for the loss reserve analyses updated through September 30, 2007. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.

Loss development factors: used to project the reported losses for each accident year to an ultimate amount.

Reinsurance recoverable on unpaid losses: the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

Interest rates: which vary by geographical region, year of issuance and products.

Mortality, morbidity and surrender rates: based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Estimated Gross Profits (Life Insurance & Retirement Services):

Estimated gross profits: to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability and associated amortization patterns under FAS 97 and Sales Inducement Assets under SOP 03-1. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

Recoverability: based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

Recoverability and eligibility: based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations Of Certain Assets And Liabilities:

Market price data: AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as IDC, Bloomberg or Reuters or third-party broker/dealer quotes for use in its models. When such data is not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable recent prices.

Valuation models: utilizing factors, such as market prices, liquidity, commodity prices, credit spreads, and current interest, foreign exchange and volatility rates.

Other-Than-Temporary Declines In The Value Of Investments:

A security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);

The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization; or

The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in the creditworthiness of the obligor, unanticipated changes in interest rates, tax laws, statutory capital positions and unforeseen liquidity events, among others, AIG revisits its intent. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these unexpected changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

In periods subsequent to the recognition of an other-than-temporary impairment loss for debt securities, AIG amortizes the discount or reduced premium over the remaining life of the security in a prospective manner based on the amount and timing of estimated future cash flows.

Flight Equipment Recoverability (Financial Services):

Expected undiscounted future net cash flows: based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Allowance for Finance Receivable Losses (Financial Services):

Historical defaults and delinquency experience: utilizing factors, such as delinquency ratio, allowance ratio, charge-off ratio, and charge-off coverage.

Portfolio characteristics: portfolio composition and consideration of the recent changes to underwriting criteria and portfolio seasoning.

External factors: consideration of current economic conditions, including levels of unemployment and personal bankruptcies.

Migration analysis: empirical technique measuring historical movement of like finance receivables through various levels of repayment, delinquency, and loss categories to existing finance receivable pools.

Operating Review

General Insurance Operations

AIG s General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance and various personal lines both domestically and abroad.

Domestic General Insurance operations are comprised of DBG, Reinsurance, Personal Lines and Mortgage Guaranty businesses.

DBG writes substantially all classes of business insurance, accepting such business mainly from insurance brokers. This provides DBG the opportunity to select specialized markets and retain underwriting control. Any licensed broker is able to submit business to DBG without the traditional agent-company contractual relationship, but such broker usually has no authority to commit DBG to accept a risk.

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG s Personal Lines operations provide automobile insurance through aigdirect.com, the newly formed operation resulting from the merger of AIG Direct and 21st Century, and the Agency Auto Division, as well as a broad range of coverages for high net worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance that covers the first loss for credit defaults on high loan-to-value conventional first-lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second-lien and private student loan guaranty insurance.

AIG s Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG s foreign-based insurance subsidiaries.

Table of Contents

American International Group, Inc. and Subsidiaries

General Insurance Results

General Insurance operating income is comprised of statutory underwriting results, changes in DAC, net investment income and net realized capital gains and losses.

Operating income, as well as net premiums written, net premiums earned, net investment income and net realized capital gains (losses) and statutory ratios were as follows:

	Three Months Ended September 30,		Percentage Increase/	Nine Months Ended September 30,		Percentage Increase/
(in millions, except ratios)	**2007**	2006	**(Decrease)**	**2007**	2006	**(Decrease)**
Net premiums written:						
Domestic General						
DBG	**$ 6,012**	$ 6,071	(1)%	**$18,460**	$18,407	-%
Transatlantic	**985**	895	10	**2,952**	2,723	8
Personal Lines	**1,253**	1,162	8	**3,685**	3,540	4
Mortgage Guaranty	**303**	232	31	**841**	622	35
Foreign General	**3,270**	2,864	14	**10,130**	8,821	15
Total	**$11,823**	$11,224	5%	**$36,068**	$34,113	6%
Net premiums earned:						
Domestic General						
DBG	**$ 5,942**	$ 6,276	(5)%	**$17,919**	$17,863	-%
Transatlantic	**960**	895	7	**2,873**	2,712	6
Personal Lines	**1,193**	1,158	3	**3,516**	3,484	1
Mortgage Guaranty	**226**	191	18	**657**	536	23
Foreign General	**3,112**	2,697	15	**9,050**	7,770	16
Total	**$11,433**	$11,217	2%	**$34,015**	$32,365	5%
Net investment income:						
Domestic General						
DBG	**$ 854**	$ 880	(3)%	**$ 2,871**	$ 2,438	18%
Transatlantic	**113**	107	6	**348**	317	10
Personal Lines	**59**	56	5	**173**	168	3
Mortgage Guaranty	**42**	35	20	**118**	103	15
Foreign General[(a)]	**325**	291	12	**1,071**	1,075	-
Reclassifications and Eliminations	**1**	1	-	**4**	1	-
Total	**$ 1,394**	$ 1,370	2%	**$ 4,585**	$ 4,102	12%
Net realized capital gains (losses)	**$ (69)**	$ 28	-%	**$ (11)**	$ (29)	(62)%
Operating Income (loss):						
Domestic General						

DBG	**$ 1,829**	$ 1,543	19%	**$ 5,662**	$ 4,322	31%
Transatlantic	**189**	143	32	**508**	427	19
Personal Lines	**28**	133	(79)	**252**	352	(28)
Mortgage Guaranty	**(216)**	85	-	**(289)**	301	-
Foreign General[(a)]	**607**	721	(16)	**2,383**	2,415	(1)
Reclassifications and Eliminations	**2**	-	-	**(5)**	2	-
Total	**$ 2,439**	$ 2,625	(7)%	**$ 8,511**	$ 7,819	9%
Statutory underwriting profit (loss)[(b)] :						
Domestic General						
DBG	**$ 1,014**	$ 666	52%	**$ 2,744**	$ 1,791	53%
Transatlantic	**53**	34	56	**106**	97	9
Personal Lines	**(40)**	83	-	**49**	176	(72)
Mortgage Guaranty	**(270)**	48	-	**(438)**	191	-
Foreign General	**266**	391	(32)	**1,039**	1,147	(9)
Total	**$ 1,023**	$ 1,222	(16)%	**$ 3,500**	$ 3,402	3%
Domestic General:						
Loss Ratio	**69.2**	67.0		**68.8**	69.0	
Expense Ratio	**21.1**	23.7		**20.5**	21.2	
Combined Ratio	**90.3**	90.7		**89.3**	90.2	
Foreign General:						
Loss Ratio	**52.4**	48.4		**51.7**	48.7	
Expense Ratio	**37.1**	35.0		**32.9**	32.2	
Combined ratio	**89.5**	83.4		**84.6**	80.9	
Consolidated:						
Loss Ratio	**64.7**	62.6		**64.3**	64.1	
Expense Ratio	**25.5**	26.5		**24.0**	24.1	
Combined Ratio	**90.2**	89.1		**88.3**	88.2	

(a) The three and nine-month periods ended September 30, 2006 include increases of $22 million and $406 million, respectively, relating to an out of period UCITS adjustment.

Table of Contents

American International Group, Inc. and Subsidiaries

(b) *Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance:*

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
Three Months Ended September 30, 2007:							
Statutory underwriting profit (loss)	**$ 1,014**	**$ 53**	**$ (40)**	**$ (270)**	**266**	**$**	**$ 1,023**
Increase (decrease) in DAC	**21**	**8**	**9**	**13**	**40**		**91**
Net investment income	**854**	**113**	**59**	**42**	**325**	**1**	**1,394**
Net realized capital gains (losses)	**(60)**	**15**		**(1)**	**(24)**	**1**	**(69)**
Operating income (loss)	**$ 1,829**	**$ 189**	**$ 28**	**$ (216)**	**607**	**$ 2**	**$ 2,439**
Three Months Ended September 30, 2006:							
Statutory underwriting profit (loss)	$ 666	$ 34	$ 83	$ 48	$ 391	$	$ 1,222
Increase (decrease) in DAC	(29)		(6)	2	38		5
Net investment income	880	107	56	35	291	1	1,370
Net realized capital gains (losses)	26	2			1	(1)	28
Operating income (loss)	$ 1,543	$ 143	$ 133	$ 85	$ 721	$	$ 2,625
Nine Months Ended September 30, 2007:							
Statutory underwriting profit (loss)	**$ 2,744**	**$ 106**	**$ 49**	**$ (438)**	**1,039**	**$**	**$ 3,500**
Increase (decrease) in DAC	**106**	**22**	**31**	**34**	**244**		**437**

Net investment income	**2,871**	**348**	**173**	**118**	**1,071**	**4**	**4,585**
Net realized capital gains (losses)	**(59)**	**32**	**(1)**	**(3)**	**29**	**(9)**	**(11)**
Operating income (loss)	**$ 5,662**	**$ 508**	**$ 252**	**$ (289)**	**2,383**	**$ (5)**	**$ 8,511**
Nine Months Ended September 30, 2006:							
Statutory underwriting profit (loss)	$ 1,791	$ 97	$ 176	$ 191	$ 1,147	$	$ 3,402
Increase (decrease) in DAC	64	7	8	10	255		344
Net investment income	2,438	317	168	103	1,075	1	4,102
Net realized capital gains (losses)	29	6		(3)	(62)	1	(29)
Operating income (loss)	$ 4,322	$ 427	$ 352	$ 301	$ 2,415	$ 2	$ 7,819

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of General Insurance net premiums written:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Growth in original currency*	**4.3%**	8.5%	**4.6%**	8.1%
Foreign exchange effect	**1.0**	0.3	**1.1**	(0.6)
Growth as reported in U.S. dollars	**5.3%**	8.8%	**5.7%**	7.5%

* *Computed using a constant exchange rate throughout each period.*

Quarterly General Insurance Results

General Insurance operating income decreased in the three months ended September 30, 2007 compared to the same period in 2006. The 2007 combined ratio increased to 90.2, an increase of 1.1 points over 2006, including an increase in the loss ratio of 2.1 points. The loss ratio for accident year 2007 recorded in the three months ended September 30, 2007 was 4.5 points higher than the loss ratio recorded in the three months ended September 30, 2006 for accident year 2006. Increases in Mortgage Guaranty losses accounted for 3.1 points of the higher accident year loss ratio. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect UGC s loss ratios for the foreseeable future.

The higher accident year loss ratio was partially offset by favorable development on prior years and increases in the loss reserve discount, reducing losses by $377 million and $41 million for three months ended September 30, 2007 and 2006, respectively. The three months ended September 30, 2006, included an increase to Other expenses of $225 million in connection with balance sheet reconciliation remediation activities which accounted for 2.0 points of the decrease in the expense ratio in the three months ended September 30, 2007 compared to the same period in 2006. Net premiums written increased for the three months ended September 30, 2007 compared to the same period in 2006, driven by Foreign General growth from both established and new distribution channels and the effect of changes in foreign currency exchange rates.

General Insurance net investment income was essentially unchanged for the three months ended September 30, 2007 compared to the same period in 2006, which included an out of period increase to Net investment income of $213 million related to the accounting for UCITS and additional partnership income arising from improved valuations. Interest and dividend income increased $244 million for the third quarter of 2007 compared to the same period in 2006 as investment in fixed maturities and equity securities increased by $12.0 billion from the investment of operating cash flow and the yield on interest earning investments increased 30 basis points to 4.8 percent. Income from partnership investments increased $10 million for the three months ended September 30, 2007 compared to the same period in 2006, primarily due to improved returns on underlying investments. Other investment income decreased $290 million, primarily due to declining returns on investments in mutual funds and the effect of the $92 million out of period adjustment related to the accounting for UCITS recorded in 2006.

Year-to-Date General Insurance Results

General Insurance operating income increased for the first nine months of 2007 compared to the same period in 2006 due to growth in net investment income and an increase in underwriting profit, driven by an increase in earned premiums as the combined ratio was substantially the same for both periods. The loss ratio for accident year 2007 recorded in the first nine months of 2007 was 1.2 points higher than the loss ratio recorded in the first nine months of 2006 for accident year 2006, primarily due to an increase in Mortgage Guaranty losses in the 2007 period. The higher accident year loss ratio was substantially offset by favorable development on prior years and increases in the loss reserve discount, which combined to reduce losses by $720 million and $255 million in the first nine months of 2007 and 2006, respectively.

General Insurance net premiums written increased in the first nine months of 2007 compared to the same period in 2006, reflecting growth in Foreign General from both established and new distribution channels, the effect of changes in foreign currency exchange rates, and growth in Mortgage Guaranty, primarily from international business.

General Insurance net investment income increased in the first nine months of 2007 to $4.6 billion. Interest and dividend income increased $577 million for the first nine months of 2007 compared to the same period of 2006 as fixed maturities and equity securities increased by $15.3 billion and the yield increased 20 basis points to 4.7 percent. Income from partnership investments increased $312 million for the first nine months of 2007 compared to the same period in 2006, primarily due to improved returns on underlying investments and higher levels of invested assets, which increased by $1.2 billion. Other investment income decreased by $444 million, which reflects the effect of the $472 million out of period UCITS adjustment recorded in 2006. See also Capital Resources and Liquidity and Invested Assets herein.

In order to better align financial reporting with the manner in which AIG s chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, the foreign aviation business, which was historically reported in DBG, is now being reported as part of Foreign General, and the oil rig and marine businesses, which were historically reported in Foreign General, are now being reported as part of DBG. Prior period amounts have been revised to conform to the current presentation.

Quarterly DBG Results

DBG s operating income increased in the three months ended September 30, 2007 compared to the same period of 2006. The improvement is also reflected in the combined ratio, which declined 7.4 points in the three months ended September 30, 2007 compared to the same period of 2006 due to an improvement in the loss ratio of 3.7 points and an improvement in the expense ratio of 3.7 points. Favorable prior year development and increases in the loss reserve discount reduced incurred losses by $353 million and increased incurred losses by $67 million for the three months ended September 30, 2007 and 2006, respectively, accounting for 7.0 points of the improvement. The loss ratio for accident year 2007 recorded in the three months ended September 30, 2007 was 1.6 points higher than the loss ratio recorded in the same period of 2006 for accident year 2006. The expected loss ratios for accident year 2006 were reduced for a number of casualty classes of business in the three-month period ended September 30, 2006, accounting for most of the change in the accident year loss ratio compared to the same period in 2006. Net premiums earned in the three months ended September 30, 2006 included a favorable out of period adjustment of $155 million which reduced the loss ratio by 1.7 points.

DBG s net premiums written declined for the three months ended September 30, 2007 compared to the same period in 2006 due to an increase in ceded premiums and declines in premium rates in casualty lines of business. Ceded premiums as a percentage of gross written premiums increased to 24 percent for the three months ended September 30, 2007 compared to 23 percent in the same period in 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG s expense ratio decreased to 19.2 for the three months ended September 30, 2007 compared to 23.0 in the same period in 2006, primarily due to a decrease in charges related to remediation of the material weakness in balance sheet reconciliations which included a $225 million out of period charge in the third quarter of 2006.

DBG s net investment income decreased for the three months ended September 30, 2007 compared to the same period in 2006, which included out of period increases in partnership and other investment income of $121 million and $70 million, respectively. Interest income increased $139 million for the three months ended September 30, 2007, on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Income from partnership investments increased $16 million for the three months ended September 30, 2007 compared to the same period in 2006, primarily due to improved returns on the underlying investments.

*Year-to-*date DBG Results

DBG s operating income increased for the first nine months of 2007 compared to the same period in 2006 due to growth in both net investment income and underwriting profit. The improvement is also reflected in the combined ratio, which declined 5.2 points in the first nine months of 2007 compared to the same period in 2006, primarily due to an improvement in the loss ratio of 4.2 points. The loss ratio for accident year 2007 recorded for the first nine months of 2007 was 0.5 points lower than the loss ratio recorded in the same period of 2006 for accident year 2006. The loss ratio for accident year 2006 has subsequently improved in each quarter since September 30, 2006. Prior year development and increases in the loss reserve discount reduced incurred losses by $630 million for the nine months ended September 30, 2007 and increased incurred losses by $35 million for the same period in 2006, accounting for 3.7 points of the improvement.

DBG s net premiums written was essentially unchanged in the first nine months of 2007 compared to the same period of 2006. Ceded premiums as a percentage of gross written premiums increased to 25 percent in the first nine months of 2007 compared to 23 percent for the same period in 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG s expense ratio decreased to 18.6 for the first nine months in 2007 compared to 19.7 in the same period of 2006, primarily due to the 2006 charge related to the remediation of the material weakness in internal control over certain balance sheet reconciliations that accounted for 1.6 points of the decline. The decline was partially offset by increases in operating expenses for marketing initiatives and operations as well as changes in the mix of business towards products with lower loss ratios and higher expense ratios.

DBG s net investment income increased for the first nine months of 2007 compared to the same period in 2006, as interest income increased $334 million for the nine months ended September 30, 2007, on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Income from partnership investments increased $215 million for the first nine months of 2007 compared to the same period in 2006, primarily due to improved returns on the underlying investments. Other investment income declined $133 million in the first nine months of 2007 compared to the same period in 2006, primarily due to the out of period adjustment of $151 million recorded in the 2006 period.

Quarterly Transatlantic Results

Transatlantic s net premiums written and net premiums earned increased for the three months ended September 30, 2007 compared to the same period in 2006 due primarily to increased writings in domestic and international operations and the strengthening of certain foreign currencies against the U.S. dollar. Statutory underwriting profit increased due to improved underwriting results from domestic operations for the three months ended September 30, 2007 compared to the same period in 2006. Operating income increased for the three months ended September 30, 2007 compared to the same period in 2006 due primarily to increased net investment income, improved underwriting results and increased net realized capital gains.

*Year-to-*date Transatlantic Results

Transatlantic s net premiums written and net premiums earned increased for the first nine months of 2007 compared to the same period in 2006 due primarily to increased writings in domestic operations. The increase in statutory underwriting profit in the nine months ended September 30, 2007 compared to the same period in 2006 reflects improved underwriting results in Domestic and European operations. Overall, costs from European windstorms and floods and storms in Australia in the nine months ended September 30, 2007 were largely offset by lower estimated net adverse development, related to losses occurring in prior years, compared to the same period of 2006. Operating income increased for the first nine months of 2007 compared to the same period in 2006 due principally to increased net investment income, improved underwriting results and net realized capital gains.

Quarterly Personal Lines Results

Personal Lines operating income for the three months ended September 30, 2007 was $28 million, a decrease of $105 million compared to the same period in 2006, primarily due to a $53 million increase in incurred losses resulting from a change in prior year reserve development, mainly from discontinued businesses, and $28 million of transaction and integration costs related to the acquisition of the minority interest in 21st Century Insurance Group (21st Century), as discussed below. The loss ratio for accident year 2007 recorded for the three months ended September 30, 2007 was 3.21 points higher than the loss ratio for the same period in 2006 primarily due to increasing accident frequency trends in the direct businesses coupled with a decline in average premium, and increasing loss frequencies in the homeowners line of the Private Client Group segment. Prior year development increased incurred losses by $32 million for the three months ended September 30, 2007 and decreased incurred losses by $21 million for the three months ended September 30, 2006, thereby increasing the 2007 loss ratio by 4.52 points relative to the 2006 loss ratio. The transaction and integration costs related to the 21st Century acquisition increased the expense ratio in the third quarter of 2007 by 2.2 points compared to the same period of 2006.

Net premiums written increased 7.8 percent for the three months ended September 30, 2007 compared to the same period of 2006, which represents the highest growth rate since the third quarter of 2005. This increase resulted from continued growth in the Private Client Group, as well as growth in Agency Auto and the Direct segment.

On September 27, 2007, AIG completed its previously announced acquisition of 21st Century. AIG paid $759 million to acquire the remaining 39.2 percent of the shares of 21st Century that it did not previously own. As a result of the acquisition, the AIG Direct and 21st Century operations will be combined as aigdirect.com. Duplicate positions which exist in both the home office and corporate functions and in the field organization will be eliminated. These positions, as well as the locations scheduled for closing over the next two years, have been identified and will affect about 11 percent of the combined workforce.

Under the purchase method of accounting, the assets and liabilities of 21st Century that were acquired were adjusted to their estimated fair values as of the date of the acquisition, and goodwill of $233 million was recorded. A customer relationship intangible asset, initially valued at $290 million, was also established.

*Year-to-*date Personal Lines Results

Personal Lines operating income for the nine months of 2007 was $252 million, a decrease of $100 million compared to the same period in 2006, primarily due to $55 million of less favorable reserve development and $31 million of transaction and integration costs related to the 21st Century acquisition. The loss ratio for accident year 2007 recorded for the first nine months of 2007 increased by 0.36 points compared to the same period in 2006 for accident year 2006. Favorable prior year development reduced incurred losses by $29 million and $84 million for the nine months ended September 30, 2007 and 2006, respectively, resulting in a 1.57 point increase in the loss ratio for the first nine months of 2007 compared to the same period of 2006. The 0.9 point increase in the expense ratio was primarily due to the transaction and integration costs associated with the 21st Century acquisition.

Net premiums written increased 4.1 percent for the first nine months of 2007 compared to the same period in 2006 due to continued growth in the Private Client Group and an increase in the aigdirect.com business, partially offset by a reduction in the Agency Auto segment.

Quarterly Mortgage Guaranty Results

Mortgage Guaranty reported an operating loss of $216 million for the three months ended September 30, 2007 compared to operating income of $85 million in the same period in 2006 due to the unfavorable loss experience in both the domestic first and second-lien businesses as continued deterioration in the U.S. housing market increased the frequency and severity of claims. The second-lien product was the major contributor to the operating loss, comprising $206 million of the third quarter 2007 operating loss. UGC s consolidated loss ratio for the third quarter of 2007 was 197.0 compared to a loss ratio of 47.5 in the same period of 2006. Prior year development reduced incurred losses by $27 million and $22 million for the three months ended September 30, 2007 and 2006, respectively, decreasing the 2007 loss ratio by 0.4 points relative to the 2006 loss ratio.

Net premiums written increased 31 percent in the three months ended September 30, 2007 compared to the same period in 2006 as strong growth in the European markets, Canada and Australia led to higher International premiums of $55 million. The increased use of mortgage insurance for credit enhancement, along with improved persistency, led to higher domestic first-lien premiums of $32 million, an increase of 27 percent compared to the 2006 quarter. Although UGC discontinued accepting new business for the poorly performing third-party originated second-lien product in the fourth quarter of 2006, UGC will continue to receive renewal premiums on the existing portfolio for the life of the loans, estimated to be three to five years. The expense ratio of 16.8 points in the three months ended September 30, 2007 declined from 22.5 points in the same period of 2006 as premium growth offset the effect of increased expenses related to UGC s international expansion and the employment of additional operational resources in the second-lien business.

UGC s domestic mortgage risk in force totaled $28.2 billion as of September 30, 2007 and the 60-day delinquency ratio was 3.0 percent (based on number of policies, consistent with mortgage industry practice) compared to domestic mortgage risk in force of $24.2 billion and a delinquency ratio of 2.0 percent at September 30, 2006. Approximately 81 percent of the domestic mortgage risk is secured by first-lien, owner-occupied properties.

Year-to-date Mortgage Guaranty Results

Mortgage Guaranty s operating loss for the first nine months of 2007 was $289 million compared to operating income of

$301 million for the same period in 2006 as the deteriorating U.S. residential housing market adversely affected losses incurred for both the domestic first-lien and second-lien businesses. Domestic first and second-lien losses incurred increased 254 percent and 611 percent respectively, compared to the first nine months of 2006, resulting in year-to-date loss ratios of 87.6 and 343.1, respectively, for the first nine months of 2007. Increases in domestic losses incurred resulted in a consolidated UGC loss ratio of 140.9 for the first nine months of 2007 compared to 37.4 for the same period in 2006. Prior year development had minimal effect on incurred losses in the first nine months of 2007 compared to a reduction of $86 million for the same period in 2006, which accounted for 16 points of the increase in the loss ratio.

Net premiums written increased 35 percent in the nine months ended September 30, 2007 compared to the same period in 2006 primarily due to growth in the International markets, accounting for 22 percent of the increase in net written premiums. In addition the increased use of mortgage insurance for credit enhancement as well as better persistency resulted in an increase in domestic first-lien premiums. The expense ratio for the first nine months of 2007 was 20.2, down from 23.3 in the same period in 2006 as premium growth offset the effect of increased expenses related to UGC s international expansion.

Quarterly Foreign General Insurance Results

Foreign General s operating income decreased in the three months ended September 30, 2007 compared to the same period in 2006 due to decreases in statutory underwriting profit, partially offset by increases in net investment income and the effect of changes in the currency exchange rates of the Euro and the British Pound. Statutory underwriting profit decreased due to lower favorable loss development on prior accident years of $49 million, additional losses from the June 2007 U.K. floods of $23 million and an increase over the 2006 quarter in severe but non-catastrophic losses of $20 million.

Net premiums written increased 14 percent (11 percent in original currency) for the three months ended September 30, 2007 compared to the same period in 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including Central Insurance Co. Ltd. in Taiwan. Net premiums written for commercial lines in the U.K. and Europe increased due to new business and decreases in the use of reinsurance, partially offset by declines in premium rates. Growth in consumer lines in Latin America, Asia and Europe also contributed to the increase. Net premiums written also increased by one percent compared to the same period in 2006 due to decreases in the use of reinsurance. Net premiums for the Lloyd s syndicate Ascot and Aviation declined due to rate decreases resulting from increased market competition.

The loss ratio increased 4.0 points for the three months ended September 30, 2007 compared to the same period in 2006. The 2007 loss ratio increased a total of 3.3 points due to the losses described above. The lower favorable loss development on prior accident years was primarily due to increases in the allowance for reinsurance. Also, the loss ratio increased due to higher loss frequency for personal accident businesses in Japan.

The expense ratio increased 2.1 points for the three months ended September 30, 2007 compared to the same period in 2006 due to higher operating expenses relating to new business initiatives. In addition, the 2007 expense ratio increased 1.2 points due to accelerated amortization of advertising costs, the cost of realigning certain legal entities through which Foreign General operates and the increased significance of consumer lines of business, which have higher acquisition costs. AIG expects the expense ratio to increase in the fourth quarter of 2007 as a result of expected decreases in net premiums written due to continuing rate pressures in the commercial lines business, the underlying seasonality of renewals and the growth of the consumer lines of business.

Net investment income increased for the three months ended September 30, 2007 compared to the same period of 2006 reflecting higher interest rates and strong cash flows, partially offset by reductions in mutual fund income. Mutual fund income was $61 million lower than the same quarter in 2006 reflecting a weaker performance in the equity markets and income of $22 million from an out of period UCITS adjustment in the year ago quarter.

Year-to-date Foreign General Insurance Results

Foreign General s operating income decreased in the first nine months of 2007 compared to the same period in 2006, due primarily to decreases in statutory underwriting profits. Statutory underwriting profit decreased due to lower favorable loss development on prior accident years of $101 million, losses from the June 2007 U.K. floods of

$91 million, and an increase in severe but non-catastrophic losses of $48 million compared to the same period in 2006. Net investment income in the nine months ended September 30, 2006 included income of $406 million from out of period UCITS adjustments.

Net premiums written increased 15 percent (11 percent in original currency) for the nine months ended September 30, 2007 compared to the same period in 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels.

The loss ratio increased 3.0 points for the nine months ended September 30, 2007 compared to the same period in 2006. The 2007 loss ratio increased 2.6 points, due to the losses described above.

The expense ratio increased 0.7 points for the nine months ended September 30, 2007 compared to the same period in 2006 due to higher commission costs and higher operating expenses resulting from new business initiatives and the costs to realign certain legal entities.

Net investment income was essentially unchanged in the nine months ended September 30, 2007 compared to the same period of 2006 as the 2006 period included the out of period UCITS adjustments, which more than offset increased investment income of $402 million reflecting higher interest rates, strong cash flows and increased partnership and mutual fund income. Partnership income was $97 million higher than prior year due to strong infrastructure fund performance in Africa, Europe and Latin America. Mutual fund income was $117 million higher than the same period of the prior year reflecting strong performance in the equity markets for the nine month period.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) as of September 30, 2007 and December 31, 2006 by major line of business on a statutory Annual Statement basis[(a)]:

(in millions)	**September 30, 2007**	December 31, 2006[(b)]
Other liability occurrence	**$ 20,296**	$ 19,327
Workers compensation	**14,994**	13,612
Other liability claims made	**13,546**	12,513
Auto liability	**6,208**	6,070
International	**6,173**	6,006
Property	**4,431**	5,499
Reinsurance	**3,371**	2,979
Medical malpractice	**2,349**	2,347
Products liability	**2,181**	2,239
Accident and health	**1,901**	1,693
Commercial multiple peril	**1,744**	1,651
Aircraft	**1,715**	1,629
Fidelity/surety	**1,248**	1,148
Other	**3,451**	3,286
Total	**$ 83,608**	$ 79,999

(a) *Presented by lines of business pursuant to statutory reporting requirements as prescribed by the National Association of Insurance Commissioners.*

(b) *Allocations among various lines were revised from the previous presentation.*

AIG s gross reserve for losses and loss expenses represents the accumulation of estimates of ultimate losses, including provisions for losses incurred but not reported (IBNR) and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated by management. Any adjustments resulting therefrom are reflected in operating income currently. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable or adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

Estimates for mortgage guaranty insurance losses and loss adjustment expense reserves are based on notices of mortgage loan delinquencies and estimates of delinquencies that have been incurred but have not been reported by loan servicers, based upon historical reporting trends. UGC establishes reserves using a percentage of the contractual liability (for each delinquent loan reported) that is based upon past experience regarding certain loan factors such as age of the delinquency, dollar amount of the loan and type of mortgage loan. Because mortgage delinquencies and claims payments are affected primarily by macroeconomic events, such as changes in home price appreciation, interest rates and unemployment, the determination of the ultimate loss cost requires a high degree of judgment. AIG believes it has provided appropriate reserves for currently delinquent loans. Consistent with industry practice, AIG does not establish a reserve for loans that are not currently delinquent, but that may become delinquent in future periods.

At September 30, 2007, General Insurance net loss reserves were $66.94 billion, an increase of $4.31 billion from the prior year-end. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserves by business unit:

(in millions)		**September 30, 2007**		December 31, 2006
DBG[(a)]	**$**	**46,511**	$	44,119
Transatlantic		**6,669**		6,207
Personal Lines[(b)]		**2,313**		2,440
Mortgage Guaranty		**1,016**		460
Foreign General[(c)]		**10,428**		9,404
Total Net Loss Reserve	**$**	**66,937**	$	62,630

(a) *At September 30, 2007 and December 31, 2006, respectively, DBG loss reserves include approximately $3.16 billion and $3.33 billion ($3.40 billion and $3.66 billion, respectively, before discount), related to business written by DBG but ceded to American International Reinsurance Company Limited (AIRCO) and reported in AIRCO s statutory filings. DBG loss reserves also include approximately $573 million and $535 million related to business included in American International Underwriters Overseas, Ltd. s (AIUO) statutory filings at September 30, 2007 and December 31, 2006, respectively.*

(b) *At September 30, 2007 and December 31, 2006, respectively, Personal Lines loss reserves include $844 million and $861 million related to business ceded to DBG and reported in DBG s statutory filings.*

(c) *At September 30, 2007 and December 31, 2006, respectively, Foreign General loss reserves include approximately $3.05 billion and $2.75 billion related to business reported in DBG s statutory filings.*

The DBG net loss reserve of $46.5 billion is comprised principally of the business of AIG subsidiaries participating in

42

the American Home Assurance Company (American Home)/ National Union Fire Insurance Company of Pittsburgh, Pa. (National Union) pool (10 companies) and the surplus lines pool (Lexington, AIG Excess Liability Insurance Company and Landmark Insurance Company).

DBG cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 15 percent for the nine months ended September 30, 2007 and 20 percent for the year 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. AIRCO s loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of September 30, 2007, AIRCO carried a discount of approximately $240 million applicable to the $3.40 billion in undiscounted reserves it assumed from the American Home/ National Union pool via this quota share cession. AIRCO also carries approximately $523 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of September 30, 2007, these AIU reserves carried by participants in the American Home/ National Union pool totaled approximately $3.05 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at September 30, 2007 by AIUO and AIRCO were approximately $5.04 billion and $3.69 billion, respectively. AIRCO s $3.69 billion in total general insurance reserves consist of approximately $3.16 billion from business assumed from the American Home/National Union pool and an additional $523 million relating to Foreign General Insurance business.

Discounting of Reserves

At September 30, 2007, AIG s overall General Insurance net loss reserves reflect a loss reserve discount of $2.43 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company s own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $726 million tabular discount for workers compensation in DBG; $1.46 billion non-tabular discount for workers compensation in DBG; and, $240 million non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $12.7 billion as of September 30, 2007. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.40 billion at September 30, 2007.

Quarterly Reserving Process

Management believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of September 30, 2007. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG s ultimate loss reserves will not develop adversely and materially exceed AIG s loss reserves as of September 30, 2007. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG s consolidated financial condition, although it could have a material adverse effect on AIG s consolidated results of operations for an individual reporting period.

The following table presents the reconciliation of net loss reserves:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2007**	2006	**2007**	2006
Net reserve for losses and loss expenses at beginning of period	**$ 65,197**	$ 60,214	**$ 62,630**	$ 57,476
Foreign exchange effect	**224**	34	**438**	521
Acquisition*		55		55
Losses and loss expenses incurred:				
Current year	**7,636**	6,957	**22,185**	20,710
Prior years, other than accretion of discount	**(337)**	(41)	**(605)**	(255)
Prior years, accretion of discount	**92**	101	**220**	303
Losses and loss expenses incurred	**7,391**	7,017	**21,800**	20,758
Losses and loss expenses paid	**5,875**	5,807	**17,931**	17,297
Net reserve for losses and loss expenses at end of period	**$ 66,937**	$ 61,513	**$ 66,937**	$ 61,513

* *Reflects the opening balance with respect to the acquisition of the Central Insurance Co., Ltd. in the third quarter of 2006*

The following tables summarize development, (favorable) or unfavorable, of incurred losses and loss expenses for prior years (other than accretion of discount):

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2007**	2006	**2007**	2006
Prior Accident Year Development by Reporting Unit:				
DBG	**$ (313)**	$ 67	**$ (465)**	$ 35
Personal Lines	**32**	(21)	**(29)**	(84)
Mortgage Guaranty	**(27)**	(22)		(86)

Foreign General	**(40)**	(89)	**(108)**	(209)
Subtotal	**(348)**	(65)	**(602)**	(344)
Transatlantic	**11**	24	**47**	89
Asbestos settlements*			**(50)**	
Prior years, other than accretion of discount	**$ (337)**	$ (41)	**$ (605)**	$ (255)

** Represents the effect of settlements of certain asbestos liabilities.*

	Calendar Year	
(in millions)	**2007**	2006
Prior Accident Year Development by Accident Year:		
2006	**$ (898)**	
2005	**(373)**	$ (638)
2004	**(248)**	(416)
2003	**143**	(233)
2002	**200**	156
2001 & prior	**571**	876
Prior years, other than accretion of discount	**$ (605)**	$ (255)

In determining the quarterly loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center s reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the third quarter of 2007 to determine the loss development from prior accident years for the third quarter of 2007. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to the U.S. mortgage and housing market. Also as part of the quarterly reserving process, beginning with the second quarter of 2007, AIG updated its analysis of the loss reserve discount pertaining to workers compensation reserves. Historically, this review was only performed at year end. As a result of the updated analysis in the third quarter of 2007, AIG increased its loss reserve discount for workers compensation by approximately $70 million in the third quarter of 2007, bringing the total increase in loss reserve discount for workers compensation for the first nine months of 2007 to approximately $255 million.

2007 Net Loss Development

In the three months ended September 30, 2007, net loss development from prior accident years was favorable by approximately $337 million, including approximately $11 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $92 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the three months ended September 30, 2007 from prior accident years was favorable by approximately $348 million. The overall favorable development of $337 million consisted of approximately $764 million of favorable development from accident years 2004 through 2006, partially offset by approximately $299 million of adverse development from accident years 2002 and prior and $128 million of adverse development from accident year 2003. For the three months ended September 30, 2007, most classes of AIG s business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to developments from excess casualty business within DBG and from Transatlantic. The adverse development from accident year 2003 was primarily related to developments from excess casualty business within DBG, which represented less than a 1 percent change in the ultimate loss estimate for accident year 2003. In the three months ended September 30, 2007, AIG completed an update of its ground up projections of claims exposure for the D&O and related management liability classes of business. AIG utilizes the ultimate loss estimates resulting from these claims projections as a benchmark in determining the appropriate loss reserves for this business. As a result of the updated claims projections, in addition to the quarterly review of reported loss experience as of September 30, 2007 and other relevant factors, AIG recognized approximately $150 million in favorable loss development from prior accident years for the D&O and related management liability classes of business in the three months ended September 30, 2007. This consisted of approximately $200 million of favorable development from accident years 2004 through 2006, partially offset by approximately $50 million of adverse development from accident years 2002 and prior. The overall favorable development of $337 million reflects this $150 million from the D&O and related management liability classes of business within DBG.

In the first nine months of 2007, net loss development from prior accident years was favorable by approximately $605 million, including approximately $47 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $220 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the first nine months of 2007 from prior accident years was favorable by approximately $652 million. The overall favorable development of $605 million consisted of approximately $1.52 billion of favorable development from accident years 2004 through 2006, partially offset by approximately $771 million of adverse development from accident years 2002 and prior and $143 million of adverse development from accident year 2003. For the first nine months of 2007, most classes of AIG s business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to development from excess casualty business within DBG and from Transatlantic. The adverse development from accident year 2003 was primarily related to developments from excess casualty business within DBG. The overall favorable development of $605 million includes approximately $200 million pertaining to the D&O and related management liability classes of business within DBG, consisting of approximately $235 million of favorable development from accident years 2004 through 2006, partially offset by approximately $35 million of adverse development from accident years 2002 and prior.

2006 Net Loss Development

In the three months ended September 30, 2006, net loss development from prior accident years was favorable by approximately $41 million, including approximately $43 million of adverse development pertaining to the major hurricanes in 2005 and 2004 and $24 million of adverse development pertaining to the general reinsurance operations of Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $101 million, net loss development from prior accident years in the three months ended September 30, 2006 was favorable by approximately $108 million. This overall favorable development of $41 million consisted of approximately $511 million of favorable development from accident years 2003 through 2005, partially offset by approximately $470 million of adverse development from accident years 2002 and prior. For the three months ended September 30, 2006, most classes of business throughout AIG experienced favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected developments from excess casualty, workers compensation, and post-1986 environmental liability classes of business, all within DBG, and from Transatlantic.

In the first nine months of 2006, net loss development from prior accident years was favorable by approximately $255 million, including approximately $80 million of adverse development pertaining to the major hurricanes in 2004 and 2005 and $89 million of adverse development from the general reinsurance operations of Transatlantic, and excluding approximately $303 million from accretion of loss reserve discount. Excluding catastrophes and Transatlantic, as well as accretion of discount, net loss development from prior accident years in the first nine months of 2006 was favorable by approximately $424 million. The overall favorable development of $255 million consisted of approximately $1.29 billion of favorable development from accident years 2003 through 2005, partially offset by approximately $1.03 billion of adverse development from accident years 2002 and prior. For the first nine months of 2006, most classes of business throughout AIG experienced favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected developments from excess casualty, workers compensation, excess workers compensation, and post-1986 environmental liability classes of business, all within DBG, and from Transatlantic.

As a result of the continued favorable experience for accident years 2003 through 2005, the expected loss ratios for accident year 2006 were improved for a number of casualty classes of business in the three months ended September 30, 2006. For those classes of business where the expected loss ratio for accident year 2006 was adjusted in the three months ended September 30, 2006, the revised loss ratio was generally applied to the cumulative 2006 net earned premium for the class. The overall effect on the results for the three months ended September 30, 2006, was approximately a $100 million improvement. This amount represents the application of the revised expected loss ratios to the net premiums earned reported for the first six months of 2006.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2006 Annual Report on Form 10-K, AIG s reserves relating to asbestos and environmental claims reflect a comprehensive ground up analysis. In the first nine months of 2007, one large asbestos settlement, as well as a reduction in estimated reinsurance recoverable, resulted in a minor amount of adverse incurred loss development, which was partially offset, on a net basis, by the favorable $50 million effect of several other settlements.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined:

	Nine Months Ended September 30,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$ 4,464**	**$ 1,889**	$ 4,441	$ 1,840
Losses and loss expenses incurred*	**19**	**7**	2	7
Losses and loss expenses paid*	**(614)**	**(363)**	(404)	(151)
Reserve for losses and loss expenses at end of period	**$ 3,869**	**$ 1,533**	$ 4,039	$ 1,696

Environmental:

Reserve for losses and loss expenses at beginning of year	**$ 588**	**$ 290**	$ 926	$ 410
Losses and loss expenses incurred*	**2**	**(1)**	(3)	
Losses and loss expenses paid*	**(89)**	**(46)**	(80)	(43)
Reserve for losses and loss expenses at end of period	**$ 501**	**$ 243**	$ 843	$ 367
Combined:				
Reserve for losses and loss expenses at beginning of year	**$ 5,052**	**$ 2,179**	$ 5,367	$ 2,250
Losses and loss expenses incurred*	**21**	**6**	(1)	7
Losses and loss expenses paid*	**(703)**	**(409)**	(484)	(194)
Reserve for losses and loss expenses at end of period	**$ 4,370**	**$ 1,776**	$ 4,882	$ 2,063

** All amounts pertain to policies underwritten in prior years, primarily to policies issued in 1984 and prior.*

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, were estimated as follows:

	Nine Months Ended September 30,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos	**$ 2,743**	**$ 1,261**	$ 2,863	$ 1,312
Environmental	**289**	**127**	567	242
Combined	**$ 3,032**	**$ 1,388**	$ 3,430	$ 1,554

A summary of asbestos and environmental claims count activity was as follows:

	Nine Months Ended September 30,					
	2007			2006		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined
Claims at beginning of year	**6,878**	**9,442**	**16,320**	7,293	9,873	17,166
Claims during year:						
Opened	**321**	**850**	**1,171**	538	1,032	1,570
Settled	**(113)**	**(101)**	**(214)**	(126)	(120)	(246)
Dismissed or otherwise resolved	**(745)**	**(2,138)**	**(2,883)**	(678)	(1,295)	(1,973)
Claims at end of period	**6,341**	**8,053**	**14,394**	7,027	9,490	16,517

Survival Ratios   Asbestos and Environmental

The table below presents AIG s survival ratios for asbestos and environmental claims at September 30, 2007 and 2006. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The September 30, 2007 survival ratio is lower than the ratio at September 30, 2006 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG s survival ratio for asbestos claims was negatively affected by the favorable settlements described above, which reduced gross and net asbestos survival ratios at September 30, 2007 by approximately 1.4 years and 3.2 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG s survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at September 30, 2007 and 2006 were as follows:

(number of years)	**Gross**	**Net**
2007		
Survival ratios:		
Asbestos	7.6	6.4
Environmental	4.8	3.8
Combined	7.1	5.8
2006		
Survival ratios:		
Asbestos	11.9	13.6
Environmental	6.5	5.3
Combined	10.4	10.7

Life Insurance & Retirement Services Operations

AIG s Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad.

Overseas, AIG s Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

Domestically, AIG s Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance and group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold primarily through career agents. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker-dealers and exclusive sales representatives, and annuity runoff operations, which include previously acquired closed blocks and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

AIG s Life Insurance & Retirement Services subsidiaries report their operations through the following major internal reporting units and business units:

Foreign Life Insurance & Retirement Services

Japan and Other

American Life Insurance Company (ALICO)

AIG Star Life Insurance Co., Ltd. (AIG Star Life)

AIG Edison Life Insurance Company (AIG Edison Life)

Asia

American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA)

Nan Shan Life Insurance Company, Ltd. (Nan Shan)

American International Reinsurance Company Limited (AIRCO)

The Philippine American Life and General Insurance Company (Philamlife)

Domestic Life Insurance

American General Life Insurance Company (AIG American General)

The United States Life Insurance Company in the City of New York (USLIFE)

American General Life and Accident Insurance Company (AGLA)

Domestic Retirement Services

The Variable Annuity Life Insurance Company (VALIC)

AIG Annuity Insurance Company (AIG Annuity)

AIG SunAmerica Life Assurance Company (AIG SunAmerica)

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Foreign Life Insurance & Retirement Services	**$ 6,505**	**$ 2,367**	**$ 138**	**$ 9,010**	**$ 1,736**
Domestic Life Insurance	**1,495**	**985**	**(295)**	**2,185**	**61**
Domestic Retirement Services	**300**	**1,471**	**(334)**	**1,437**	**202**
Total	**$ 8,300**	**$ 4,823**	**$ (491)**	**$ 12,632**	**$ 1,999**
Three Months Ended September 30, 2006					
Foreign Life Insurance & Retirement Services*	$ 5,987	$ 2,490	$ (29)	$ 8,448	$ 1,608
Domestic Life Insurance	1,424	958	(123)	2,259	261
Domestic Retirement Services	262	1,597	(24)	1,835	603
Total	$ 7,673	$ 5,045	$ (176)	$ 12,542	$ 2,472
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	9%	(5)%	%	7%	8%
Domestic Life Insurance	5	3		(3)	(77)
Domestic Retirement Services	15	(8)		(22)	(67)
Total	8%	(4)%	%	1%	(19)%
Nine Months Ended September 30, 2007					
Foreign Life Insurance & Retirement Services	**$ 19,621**	**$ 8,611**	**$ (79)**	**$ 28,153**	**$ 4,674**
Domestic Life Insurance	**4,392**	**2,996**	**(323)**	**7,065**	**774**
Domestic Retirement Services	**882**	**4,861**	**(624)**	**5,119**	**1,452**
Total	**$ 24,895**	**$ 16,468**	**$ (1,026)**	**$ 40,337**	**$ 6,900**
Nine Months Ended September 30, 2006					

Foreign Life Insurance & Retirement Services*	$ 18,085	$ 6,715	$ 487	$ 25,287	$ 5,033
Domestic Life Insurance	4,254	2,784	(190)	6,848	862
Domestic Retirement Services	782	4,800	(414)	5,168	1,588
Total	$ 23,121	$ 14,299	$ (117)	$ 37,303	$ 7,483
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	8%	28%	%	11%	(7)%
Domestic Life Insurance	3	8		3	(10)
Domestic Retirement Services	13	1		(1)	(9)
Total	8%	15%	%	8%	(8)%

* *Includes the effect of an out of period UCITS adjustment in 2006. For the three and nine-month periods ended September 30, 2006, the effect was increases of $24 million and $240 million, respectively, in net investment income and $24 million and $169 million, respectively, in operating income.*

The following table presents the Insurance In force for Life Insurance & Retirement Services:

(in millions)	**September 30, 2007**	December 31, 2006
Foreign	**$ 1,237,507**	$1,162,699
Domestic	**964,515**	907,901
Total	**$ 2,202,022**	$2,070,600

Volatility in the securities markets had a negative effect on Life Insurance & Retirement Services results for the three months ended September 30, 2007, and resulted in lower investment income from partnerships and UCITS and higher net realized capital losses for the quarter compared to last year. This negative effect was partially offset by strong life insurance production in Asia, improved universal life and variable universal life sales in the Domestic Life operations, and improved deposit flows for group retirement products and individual variable annuities in the Domestic Retirement Services business. The fixed annuity business environment remained challenging both domestically and in Japan reflecting a continuation of trends seen throughout the year. Investment income for the three months ended September 30, 2007 reflects a decline of $163 million in income from partnerships, UCITS, mutual funds and hedge funds, particularly in the Domestic Retirement Services business, and $74 million of trading account losses in the U.K. related to variable annuity products. In addition, the decline in Japanese equity markets resulted in higher incurred benefits of $36 million on a closed block of business having guaranteed benefits. The nine-month period ended September 30, 2007 included an increase of $176 million in income from partnerships, UCITS, mutual funds and hedge funds and $88 million of trading account losses in the U.K. associated with the variable annuity products.

Life Insurance & Retirement Services total revenues for the three and nine-month periods ended September 30, 2007 reflect growth in premiums and other considerations and higher realized capital losses. Net investment income grew for the nine months ended September 30, 2007 but declined for three months then ended compared to the same period in 2006. Net realized capital losses reduced revenues by $491 million and $1.0 billion in the three and nine-month periods ended September 30, 2007, respectively, while net realized capital losses decreased revenues by $176 million and $117 million in the three and nine-month periods ended September 30, 2006, respectively. Net realized capital losses in 2007 were primarily related to the other-than-temporary decline in value of securities that AIG no longer intends to hold to recovery. Net investment income includes policyholder investment income and trading gains and losses (collectively, policyholder trading gains), which are offset by an equal charge to incurred policy losses and benefits expense, as these investment returns accrue to the benefit of the policyholder. Policyholder trading gains generally reflect the trend in equity markets. Policyholder trading gains were $150 million and $2 billion for the three and nine-month periods ended September 30, 2007, respectively, compared to $485 million and $969 million for the three and nine-month periods ended September 30, 2006, respectively. Net investment income for the three and nine-month periods ended September 30, 2006 included an increase of $24 million and $240 million, respectively, for an out of period adjustment related to the accounting for UCITS.

In order to better align financial reporting with the manner in which AIG s chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, revenues and operating income related to foreign investment contracts, which were historically reported as a component of the Asset Management segment, are now being reported as part of Foreign Life Insurance & Retirement Services. Prior period amounts have been revised to conform to the current presentation.

Operating income for the first nine months of 2007 includes the adverse effect of $62 million related to SOP 05-1, a $62 million charge for additional benefits expense and a $50 million charge related to balance sheet reconciliation remediation activities. SOP 05-1 generally requires DAC related to group contracts to be amortized over a shorter duration than in prior periods and also requires that DAC be expensed at the time a policy is terminated. The effect of SOP 05-1 was most significant to the group products line in the Domestic Life operations. The additional benefit expense resulted from a continuing industry-wide review of claims in Japan. In addition, increased charges for DAC related to the conversion of actuarial systems to a common global standard within AIG decreased operating income by $32 million for both the three and nine-month periods ended September 30, 2007, respectively. Operating income for the three and nine-month periods ended September 30, 2006 included an increase of $24 million and $169 million, respectively, for an out of period adjustment related to the accounting for UCITS. Operating income for the three-month period ended September 30, 2007 declined compared to the same period in 2006 due to higher net realized capital losses, lower income from partnerships, UCITS, mutual funds and hedge funds as discussed above, trading account losses in the U.K. and a $14 million charge related to SOP 05-1.

Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Life insurance	**$ 3,992**	**$ 1,598**	**$ 74**	**$ 5,664**	**$ 1,048**
Personal accident	**1,519**	**91**	**12**	**1,622**	**353**
Group products	**744**	**162**	**(37)**	**869**	**81**
Individual fixed annuities	**141**	**533**	**89**	**763**	**286**
Individual variable annuities	**109**	**(17)**		**92**	**(32)**
Total	**$ 6,505**	**$ 2,367**	**$ 138**	**$ 9,010**	**$ 1,736**
Three Months Ended September 30, 2006					
Life insurance*	$ 3,837	$ 1,404	$ (25)	$ 5,216	$ 920
Personal accident	1,398	78	(16)	1,460	362
Group products	589	171	8	768	106
Individual fixed annuities	84	516	4	604	178
Individual variable annuities	79	321		400	42
Total	$ 5,987	$ 2,490	$ (29)	$ 8,448	$ 1,608
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	4%	14%	%	9%	14%
Personal accident	9	17		11	(2)
Group products	26	(5)		13	(24)
Individual fixed annuities	68	3		26	61
Individual variable annuities	38			(77)	
Total	9%	(5)%	%	7%	8%
Nine Months Ended September 30, 2007					
Life insurance	**$ 12,264**	**$ 5,247**	**$ 47**	**$ 17,558**	**$ 2,855**
Personal accident	**4,479**	**261**	**6**	**4,746**	**1,046**
Group products	**2,187**	**558**	**(64)**	**2,681**	**233**
Individual fixed annuities	**387**	**1,681**	**(68)**	**2,000**	**487**
Individual variable annuities	**304**	**864**		**1,168**	**53**

Total	**$**	**19,621**	**$**	**8,611**	**$**	**(79)**	**$ 28,153**	**$**	**4,674**
Nine Months Ended September 30, 2006									
Life insurance*	$	11,857	$	3,997	$	395	$ 16,249	$	3,072
Personal accident		4,084		213		36	4,333		1,080
Group products		1,669		463		20	2,152		303
Individual fixed annuities		273		1,470		36	1,779		475
Individual variable annuities		202		572			774		103
Total	$	18,085	$	6,715	$	487	$ 25,287	$	5,033
Percentage Increase/(Decrease) from Prior Year:									
Life insurance		3%		31%		(88)%	8%		(7)%
Personal accident		10		23		(83)	10		(3)
Group products		31		21			25		(23)
Individual fixed annuities		42		14			12		3
Individual variable annuities		50		51			51		(49)
Total		8%		28%		%	11%		(7)%

* *Includes the effect of an out of period UCITS adjustment in 2006. For the three and nine-month periods ended September 30, 2006, the effect was an increase of $22 million and $237 million, respectively, in net investment income and $22 million and $166 million, respectively, in operating income.*

Foreign Life Insurance & Retirement Services Results (continued)

American International Group, Inc. and Subsidiaries

AIG transacts business in most major foreign currencies and therefore premiums reported in U.S. dollars vary both by volume and as a result of changes in foreign currency translation rates. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of the Foreign Life Insurance & Retirement Services premiums and other considerations:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Growth in original currency*	**7.5%**	8.8%	**6.8%**	7.8%
Foreign exchange effect	**1.2**	(0.6)	**1.7**	(3.0)
Growth as reported in U.S. dollars	**8.7%**	8.2%	**8.5%**	4.8%

** Computed using a constant exchange rate throughout each period.*

Quarterly Japan and Other Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Life insurance	**$ 1,219**	**$ 393**	**$ 81**	**$ 1,693**	**$ 429**
Personal accident	**1,049**	**48**	**5**	**1,102**	**267**
Group products	**563**	**131**	**(2)**	**692**	**76**
Individual fixed annuities	**137**	**499**	**101**	**737**	**290**
Individual variable annuities	**109**	**(18)**		**91**	**(32)**
Total	**$ 3,077**	**$ 1,053**	**$ 185**	**$ 4,315**	**$ 1,030**
Three Months Ended September 30, 2006					
Life insurance*	$ 1,199	$ 470	$ 66	$ 1,735	$ 428
Personal accident	1,004	42	(4)	1,042	292
Group products	449	147	1	597	61
Individual fixed annuities	72	490	4	566	171
Individual variable annuities	78	321		399	41
Total	$ 2,802	$ 1,470	$ 67	$ 4,339	$ 993

Percentage Increase/(Decrease) from Prior Year:					
Life insurance	2%	(16)%	23%	(2)%	%
Personal accident	4	14		6	(9)
Group products	25	(11)		16	25
Individual fixed annuities	90	2		30	70
Individual variable annuities	40			(77)	
Total	10%	(28)%	176%	(1)%	4%

* *Includes the effect of an out of period UCITS adjustment in 2006. For the three-month period ended September 30, 2006, the effect was an increase of $13 million for both net investment income and operating income.*

52

Total revenues for the three-month period ended September 30, 2007 declined slightly compared to the same period in 2006, primarily due to securities markets volatility which resulted in lower policyholder trading gains and partnership and mutual fund income. Operating income increased for the three months ended September 30, 2007 compared to the same period in 2006 primarily due to net realized capital gains which more than offset the negative effect of securities markets volatility. The volatility in the securities markets reduced partnership and mutual fund revenues by $89 million, increased incurred policyholder benefits by $36 million related to a closed block of business with guaranteed benefits and resulted in trading account losses of $74 million in the U.K. associated with the variable annuity product.

Life insurance premiums and other considerations increased moderately in the three months ended September 30, 2007 compared to the same period in 2006 reflecting a continuing shift to interest sensitive whole life products in Japan. In addition, first year premium sales in Japan declined due to the suspension of increasing term products pending completion of an industry-wide review by the National Tax Authority. Single premium sales of interest sensitive whole life products in Japan and investment linked products in Europe remained strong. Net investment income declined due to lower policyholder trading gains. Both net investment income and operating income for the three months ended September 30, 2006 included out of period income related to UCITS of $13 million. Life insurance operating income for the three months ended September 30, 2007 was essentially unchanged compared to the same period in 2006 as higher realized capital gains and earnings from growth in new business were offset by the effects of securities market volatility which resulted in a decline in partnership and mutual fund income, and higher incurred benefits of $36 million on a closed block of business with guaranteed benefits.

Personal accident premiums and other considerations continue to grow at a modest rate. Strong growth in Europe was offset by declines in Japan, which has been adversely affected by increased competition and market saturation. When compared to the same period in 2006, net investment income increased due to higher invested assets. Operating income declined for the three months ended September 30, 2007 compared to the same period in 2006 due to changes in actuarial estimates, which decreased operating income in 2007 by $14 million and increased operating income in 2006 by $29 million.

Group products premiums and other considerations increased for the three months ended September 30, 2007 compared to the same period in 2006 primarily due to rapidly growing credit business in Europe and higher fee income from pension business in Brazil. Net investment income declined over the same period last year as policyholder trading gains were negatively affected by the volatile securities market. Operating income increased compared to the same period in 2006 reflecting higher premium revenues.

Individual fixed annuities premiums and other considerations growth reflects higher surrender charges from U.S. dollar contracts in Japan where a weak yen makes it attractive for certain policyholders to lock in foreign exchange gains in excess of surrender charges. Surrender charges were $46 million and $22 million for the three months ended September 30, 2007 and 2006, respectively. Operating income also reflected higher net realized capital gains.

Individual variable annuity deposits declined in Europe due to a change in consumer tax benefits for certain off-shore products, but increased in Japan as the bank distribution base for new products with guarantees is steadily expanding. New on-shore products are being launched in the U.K. to replace declining sales of off-shore products. Net investment income for the three months ended September 30, 2007 declined compared to the same period in 2006 due to lower policyholder trading gains as a result of the volatility in the securities markets. Net investment income in 2007 also included trading account losses of $74 million, offset partially by higher fees generated from the growth in assets under management compared to the same period in 2006.

Year-to-date Japan and Other Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Nine Months Ended September 30, 2007					
Life insurance	**$ 3,785**	**$ 1,584**	**$ 96**	**$ 5,465**	**$ 1,219**
Personal accident	**3,118**	**150**	**7**	**3,275**	**799**
Group products	**1,677**	**482**	**4**	**2,163**	**212**
Individual fixed annuities	**354**	**1,591**	**(63)**	**1,882**	**471**
Individual variable annuities	**302**	**861**		**1,163**	**52**
Total	**$ 9,236**	**$ 4,668**	**$ 44**	**$ 13,948**	**$ 2,753**
Nine Months Ended September 30, 2006					
Life insurance *	$ 3,608	$ 1,269	$ 300	$ 5,177	$ 1,330
Personal accident	2,954	122	36	3,112	858
Group products	1,289	393	12	1,694	201
Individual fixed annuities	229	1,398	34	1,661	457
Individual variable annuities	201	570		771	100
Total	$ 8,281	$ 3,752	$ 382	$ 12,415	$ 2,946
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	5%	25%	(68)%	6%	(8)%
Personal accident	6	23	(81)	5	(7)
Group products	30	23	(67)	28	5
Individual fixed annuities	55	14		13	3
Individual variable annuities	50	51		51	(48)
Total	12%	24%	(88)%	12%	(7)%

* *Includes the effect of an out of period UCITS adjustment in 2006. For the nine-month period ended September 30, 2006, the effect was an increase of $29 million for both net investment income and operating income.*

Revenues for the first nine months of 2007 increased compared to the same period in 2006, primarily due to higher premiums and other considerations and net investment income partially offset by lower net realized capital gains. Investment income increased due to growth in assets under management and higher policyholder trading gains partially offset by lower partnership and mutual fund income for the nine months ended September 30, 2007. Operating income decreased in the first nine months of 2007 compared to the same period in 2006 due to lower net realized capital gains, trading account losses of $88 million in the U.K. associated with the variable annuity products and $62 million of additional reserve provisions related to the claims review in Japan.

Life insurance premiums and other considerations increased in the first nine months of 2007 compared to the same period in 2006. In Japan, increased fees and policy charges related to interest sensitive whole life and U.S. dollar life insurance products, as well as strong sales of increasing term products earlier in the year, were partially offset by the runoff of the acquired blocks of business in AIG Star Life and AIG Edison Life. In Europe, growth in premiums and other considerations was driven by the growing block of single premium investment-linked products and the positive effect of foreign exchange rates. The growth in net investment income was due to higher partnership income and other yield enhancement income, income from UCITS, higher policyholder trading gains and growth in underlying invested assets. Life insurance operating income declined in the first nine months of 2007 compared to the same period in 2006 due to lower net realized capital gains.

Personal accident premiums and other considerations grew modestly as strong growth in Europe was offset by slower growth in Japan. Net investment income increased in the first nine months of 2007 compared to the same period in 2006 primarily due to higher invested assets and increased partnership income. Operating income in the first nine months of 2007 was affected by lower realized capital gains, a $46 million provision related to the Japan claims review, and $17 million of additional expenses related to the effect of SOP 05-1. The effect of the termination of certain tax-related accident and health products in Japan diminished in the third quarter of 2007 as the renewal cycle of these policies has been completed. Loss ratios remained stable for this business.

Group products premiums and other considerations increased for the first nine months in 2007 compared to the same period in 2006 primarily due to the growing credit business in Europe. Net investment income increased from the first nine months of 2006 primarily due to higher assets under management related to the Brazil pension business. Operating income for the first nine months of 2007 improved over the same period in 2006 primarily due to revenue growth, which was partially offset by a $16 million adverse effect related to SOP 05-1.

Individual fixed annuity deposits declined in the first nine months of 2007 due to the effect of a weak Yen on sales in Japan as well as the market shift to variable annuity products in Japan. Assets under management however continued to grow. Individual fixed annuities premiums and other considerations growth reflects a shift to front-end load products and higher surrender charges from U.S. dollar contracts in Japan where a weak yen makes it attractive for certain policyholders to lock in foreign exchange gains in excess of surrender charges. Surrender charges were $132 million and $64 million for the nine months ended September 30, 2007 and 2006, respectively. Net investment income increased due to higher average investment yields and growth in assets under management, partially offset by lower partnership income. Operating income declined in 2007 due to realized capital losses in 2007 versus realized capital gains in 2006.

Individual variable annuity deposits declined due to the effect of tax law changes in Europe that reduced tax benefits to policyholders and lower sales in Japan. The fees generated from the growth in assets under management increased premiums and other considerations for the first nine months of 2007 compared to the same period in 2006. Net investment income increased due to higher policyholder trading gains in the first nine months of 2007 compared to the same period in 2006. Operating income declined for the first nine months of 2007 compared to the same period in 2006 primarily due to $88 million of trading account losses.

Quarterly Asia Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Life insurance	**$ 2,773**	**$ 1,205**	**$ (7)**	**$ 3,971**	**$ 619**
Personal accident	**470**	**43**	**7**	**520**	**86**
Group products	**181**	**31**	**(35)**	**177**	**5**
Individual fixed annuities	**4**	**34**	**(12)**	**26**	**(4)**
Individual variable annuities		**1**		**1**	
Total	**$ 3,428**	**$ 1,314**	**$ (47)**	**$ 4,695**	**$ 706**
Three Months Ended September 30, 2006					
Life insurance *	$ 2,638	$ 934	$ (91)	$ 3,481	$ 492
Personal accident	394	36	(12)	418	70
Group products	140	24	7	171	45
Individual fixed annuities	12	26		38	7
Individual variable annuities	1			1	1
Total	$ 3,185	$ 1,020	$ (96)	$ 4,109	$ 615
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	5%	29%	%	14%	26%
Personal accident	19	19		24	23
Group products	29	29		4	(89)

Individual fixed annuities	(67)	31		(32)	
Individual variable annuities					
Total	8%	29%	%	14%	15%

* *Includes the effect of an out of period UCITS adjustment in 2006. For the three-month period ended September 30, 2006, the effect was an increase of $9 million for both net investment income and operating income.*

Total revenues for the three months ended September 30, 2007 increased from the same period in 2006. Premiums and other considerations growth reflects a continued trend toward investment-oriented products where only a portion of policy charges are reported as premiums. Net investment income increased due to growth in assets under management, higher equity dividends in Taiwan and higher policyholder trading gains. In Taiwan, it is customary for most companies to declare and distribute dividends in the third quarter of the calendar year. Dividend income for Taiwan was $129 million and $90 million for the three-month periods ended September 30, 2007 and 2006, respectively. Both net investment income and operating income for the three months ended September 30, 2006 included out of period income related to UCITS of $9 million. Operating income for the three months ended September 30, 2007 improved over the same period in 2006 primarily due to growth in premiums and other considerations, higher investment returns and lower net realized capital losses.

Life insurance premiums and other considerations grew modestly in the three months ended September 30, 2007 compared to the same period in 2006, despite strong growth in both first year and single premium business in the quarter. The strong sales growth, principally in Taiwan, Hong Kong, Thailand and Singapore, was primarily from investment- linked products. In Taiwan, the strong sales growth in the third quarter was due to a combination of sales campaigns and anticipation of regulatory changes related to investment-linked products that will be effective in the fourth quarter of 2007. The shift in product mix from traditional life insurance products to investment-oriented products as mentioned above dampens the growth rate of premiums and other considerations. Net investment income increased in the current period compared to the same period in 2006, due primarily to the growth in the underlying invested assets, higher equity dividends in Taiwan and higher policyholder trading gains. Both net investment income and operating income for the three months ended September 30, 2006 included out of period income related to UCITS of $9 million. Operating income increased for the three months ended September 30, 2007 compared to the same period in 2006 as a result of growth in revenues and lower net realized capital losses.

Personal accident premiums and other considerations increased primarily due to growth in Korea. Operating earnings reflect the combined effect of premium growth and stable loss ratios and include a benefit of $4 million resulting from SOP 05-1.

Group products premiums and other considerations grew in the three months ended September 30, 2007 compared to the same period in 2006, reflecting higher pension management fees and growth in Australia. Operating income declined from the prior year due to realized capital losses, primarily related to hedging activities.

Individual fixed annuities total revenues and operating income were lower for the three months ended September 30, 2007 compared to the same period in 2006 resulting from net realized capital losses. New production for the three months ended September 30, 2007 increased compared to the same period in 2006, primarily due to new products in Korea, although market demand is shifting to variable annuities.

Year-to-date Asia Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Nine Months Ended September 30, 2007					
Life insurance	**$ 8,479**	**$ 3,663**	**$ (49)**	**$ 12,093**	**$ 1,636**
Personal accident	**1,361**	**111**	**(1)**	**1,471**	**247**
Group products	**510**	**76**	**(68)**	**518**	**21**
Individual fixed annuities	**33**	**90**	**(5)**	**118**	**16**
Individual variable annuities	**2**	**3**		**5**	**1**
Total	**$ 10,385**	**$ 3,943**	**$ (123)**	**$ 14,205**	**$ 1,921**
Nine Months Ended September 30, 2006					
Life insurance*	$ 8,249	$ 2,728	$ 95	$ 11,072	$ 1,742
Personal accident	1,130	91		1,221	222
Group products	380	70	8	458	102
Individual fixed annuities	44	72	2	118	18
Individual variable annuities	1	2		3	3
Total	$ 9,804	$ 2,963	$ 105	$ 12,872	$ 2,087
Percentage Increase/(Decrease) from Prior Year:					

Life insurance	3%	34%	%	9%	(6)%
Personal accident	20	22		20	11
Group products	34	9		13	(79)
Individual fixed annuities	(25)	25			(11)
Individual variable annuities	100	50		67	(67)
Total	6%	33%	%	10%	(8)%

* *Includes the effect of an out of period UCITS adjustment in 2006. For the nine-month period ended September 30, 2006 the effect was an increase of $208 million and $137 million in net investment income and operating income, respectively.*

Revenues for the first nine months of 2007 were higher than the same period in 2006, but operating income declined compared to the same period in 2006 due to net realized capital losses in 2007 compared to net realized capital gains in 2006 and the positive effect from out of period adjustments in 2006. Premiums and other considerations increased over the same period in 2006, reflecting a continued trend toward investment-oriented products where only a portion of policy charges are reported as premium. Sales of investment-linked life products have been particularly strong in Hong Kong, Korea, Singapore, and more recently in Taiwan. Net investment income grew due to higher policyholder trading gains, higher equity dividends in Taiwan of $41 million and growth in underlying invested assets. Net investment income and operating income for the nine months ended September 30, 2006 included out of period income related to UCITS of $208 million and $137 million, respectively. Net realized capital losses in the current period compared to net realized capital gains in the same period in 2006 reduced the growth rate in revenues and caused the decline in operating income. The net realized capital losses in the current period were driven primarily by the change in fair value of derivatives that do not qualify for hedge accounting treatment under FAS 133.

Life insurance premiums and other considerations were up slightly in the first nine months of 2007 compared to the same period in 2006, benefiting from improved sales in Thailand and the favorable effect of foreign exchange rates, partially offset by the shift in product mix from traditional life insurance products to investment-oriented products as discussed above. Net investment income grew in the current period compared to the same period in 2006, due primarily to higher policyholder trading gains, the growth in the underlying invested assets and higher equity dividends in Taiwan. Operating income decreased in the first nine months of 2007 compared to the same period in 2006, due to net realized capital losses and the positive effect on prior year operating income from the out of period adjustments discussed above. Operating income for the first nine months of 2007 included a $50 million charge related to balance sheet reconciliation remediation activity.

Personal accident revenues grew for the first nine months of 2007 compared to the same period in 2006 primarily due to higher premiums and other considerations particularly in Korea and Taiwan. Operating earnings reflect the combined effect of premium growth and stable loss ratios and a $10 million positive effect related to SOP 05-1.

Group products premiums and other considerations grew in the first nine months of 2007 compared to the same period in 2006 due to higher pension management fees and sales in the first nine months of 2007 compared to the same period in 2006. Operating income declined in the first nine months of 2007 compared to the same period in 2006, primarily due to net realized capital losses resulting from hedging activities and higher incurred policy losses and benefits of $10 million due to a 2007 out of period reserve charge.

Individual fixed annuities total revenues were unchanged in the first nine months of 2007 compared to the same period in 2006, due primarily to higher investment income, offset by lower premiums and other considerations and realized capital losses in 2007 compared to realized capital gains in 2006. Deposits for the nine months ended September 30, 2007 were flat compared to the same period in 2006 due to increased competition and a market shift to variable life products in Korea.

Domestic Life Insurance Results

Quarterly Domestic Life Insurance Results

Domestic Life Insurance results, presented by sub-product were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended September 30, 2007					
Life insurance	**$ 586**	**$ 375**	**$ (253)**	**$ 708**	**$ (56)**
Home service	**189**	**160**	**(29)**	**320**	**52**
Group life/health	**211**	**48**	**(5)**	**254**	**53**
Payout annuities[(a)]	**494**	**287**	**(10)**	**771**	**(13)**
Individual fixed annuities	**2**	**27**	**5**	**34**	**10**
Individual annuities runoff[(b)]	**13**	**88**	**(3)**	**98**	**15**
Total	**$ 1,495**	**$ 985**	**$ (295)**	**$2,185**	**$ 61**
Three Months Ended September 30, 2006					

Life insurance	$ 546	$ 347	$ (110)	$ 783	$ 97
Home service	196	167	1	364	87
Group life/health	256	55	(1)	310	19
Payout annuities	414	253	(9)	658	25
Individual fixed annuities	2	21		23	8
Individual annuities runoff[(b)]	10	115	(4)	121	25
Total	$ 1,424	$ 958	$ (123)	$ 2,259	$ 261
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	7%	8%	%	(10)%	%
Home service	(4)	(4)		(12)	(40)
Group life/health	(18)	(13)		(18)	179
Payout annuities	19	13		17	
Individual fixed annuities		29		48	25
Individual annuities runoff[(b)]	30	(23)		(19)	(40)
Total	5%	3%	%	(3)%	(77)%

(a) *Premiums and other considerations include structured settlements, single premium immediate annuities and terminal funding annuities.*

(b) *Primarily represents runoff annuity business sold through discontinued distribution relationships.*

57

Domestic Life Insurance premiums and other considerations increased in the three months ended September 30, 2007 compared to the same period in 2006, primarily due to growth in the life insurance business in force, which includes increased policyholder charges related to interest sensitive whole life product sales, and in payout annuity deposits, reflecting increased sales of single premium immediate annuities and terminal funding annuities. The increase was partially offset by the decline in group life/health premiums and other considerations, primarily due to the exiting of the financial institutions credit life business at the end of 2006, and in home service premiums and other considerations, as the reduction in premiums in force from normal lapses and maturities exceeded sales growth.
Domestic Life Insurance operating income decreased in the three months ended September 30, 2007 compared to the same period in 2006. The decrease was primarily driven by higher net realized capital losses which consisted of both losses related to the sales of securities and an increase in other-than-temporary declines related to the fixed income portfolio and derivative losses. Operating income also included a $30 million out of period adjustment to increase group annuity reserves for payout annuities in connection with AIG s continuing remediation efforts. These negative effects were partially offset by growth in the life insurance in-force block of business, increased net investment income, continued improvement in profit margins for the home service business and a $52 million increase primarily related to additional reinsurance recoveries related to Superior National. Offsetting these increases was an $18 million increase in DAC amortization related to SOP 05-1.
Year-to-date Domestic Life Insurance Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Nine Months Ended September 30, 2007					
Life insurance	**$ 1,767**	**$ 1,149**	**$ (213)**	**$ 2,703**	**$ 393**
Home service	**576**	**479**	**(42)**	**1,013**	**200**
Group life/health	**637**	**152**	**(10)**	**779**	**57**
Payout annuities[(a)]	**1,370**	**852**	**(51)**	**2,171**	**55**
Individual fixed annuities	**6**	**78**	**5**	**89**	**22**
Individual annuities runoff[(b)]	**36**	**286**	**(12)**	**310**	**47**
Total	**$ 4,392**	**$ 2,996**	**$ (323)**	**$ 7,065**	**$ 774**
Nine Months Ended September 30, 2006					
Life insurance	$ 1,619	$ 998	$ (77)	$ 2,540	$ 485
Home service	593	470	(32)	1,031	212
Group life/health	743	161	(5)	899	30
Payout annuities	1,261	734	(45)	1,950	59
Individual fixed annuities	3	55	(3)	55	14
Individual annuities runoff[(b)]	35	366	(28)	373	62
Total	$ 4,254	$ 2,784	$ (190)	$ 6,848	$ 862

Percentage Increase/(Decrease) from Prior Year:					
Life insurance	9%	15%	%	6%	(19)%
Home service	(3)	2		(2)	(6)
Group life/health	(14)	(6)		(13)	90
Payout annuities	9	16		11	(7)
Individual fixed annuities	100	42		62	57
Individual annuities runoff[(b)]	3	(22)		(17)	(24)
Total	3%	8%	%	3%	(10)%

(a) *Premiums and other considerations include structured settlements, single premium immediate annuities and terminal funding annuities.*

(b) *Primarily represents runoff annuity business sold through discontinued distribution relationships.*

Domestic Life Insurance premiums and other considerations increased in the first nine months of 2007 compared to the same period in 2006. The increase was primarily due to the growth in life insurance business in force and payout annuity deposits from increased sales of structured settlements and terminal funding annuities, offset by the effect of exiting the financial institutions credit life business at the end of 2006, tightened pricing and underwriting in the group employer lines and the decline in home service premiums and other considerations. Domestic Life Insurance operating income decreased in the first nine months of 2007 compared to the same period in 2006, primarily due to higher net realized capital losses, offset by an increase in life insurance net investment income from higher partnership income and a positive change from foreign denominated emerging market bonds, higher call and tender income for life insurance and payout annuities operations, a $52 million decrease in policy benefits associated with the Superior National workers compensation reinsurance program described above and a $15 million reduction of certain litigation accruals due to favorable developments on the related matters. Life insurance operating income was also adversely affected by higher mortality in 2007, although mortality was still within normal ranges. The underlying profit margins on payout annuities continue to trail the increase in payout annuity reserves due to interest spread compression from prior period calls. The higher net realized capital losses consisted primarily of an increase in other-than-temporary declines related to the fixed income portfolio and derivative losses. Operating income for the nine-month period ended September 30, 2007 was also adversely affected by a $30 million out of period adjustment to increase payout annuity reserves related to AIG s continuing remediation efforts and a $57 million increase in DAC amortization related to SOP 05-1, $37 million of which was attributable to group life/health operations. Operating income for the nine-month period ended September 30, 2006 included a $25 million charge for litigation accruals in group life/health operations. Individual annuities runoff net investment income and operating income decreased for the nine-month period ended September 30, 2007 compared to the same period in 2006 consistent with the declining insurance reserves partially offset by lower realized capital losses.

The following table reflects periodic Domestic Life Insurance sales by product:

(in millions)	Three Months Ended September 30, 2007	2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2007	2006	Percentage Increase/ (Decrease)
Periodic premium sales by product*:						
Universal life	**$52**	$46	13%	**$150**	$289	(48)%
Variable universal life	**19**	15	27	**44**	42	5
Term life	**53**	59	(10)	**165**	182	(9)
Whole life/other	**2**	3	(33)	**7**	9	(22)
Total	**$126**	$123	2%	**$366**	$522	(30)%

** Periodic premium represents premium from new business expected to be collected over a one-year period.*

Periodic life insurance sales increased slightly for the three months ended September 30, 2007 compared to the same period in 2006 primarily as a result of the increase in indexed universal life sales and the sale of a large private placement variable universal life case. Periodic life insurance sales declined for the nine months ended September 30, 2007 compared to the same period in 2006 primarily as a result of the re-pricing of certain universal life and term products and the tightening of underwriting standards during the second half of 2006.

Domestic Retirement Services Results

Quarterly Domestic Retirement Services Results

Domestic Retirement Services results, on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					

Group retirement products	**$ 114**	**$510**	**$ (116)**	**$508**	**$ 120**
Individual fixed annuities	**24**	**828**	**(177)**	**675**	**42**
Individual variable annuities	**159**	**38**	**(22)**	**175**	**41**
Individual annuities runoff*	**3**	**95**	**(19)**	**79**	**(1)**
Total	**$ 300**	**$ 1,471**	**$ (334)**	**$ 1,437**	**$ 202**
Three Months Ended September 30, 2006					
Group retirement products	$94	$563	$(3)	$654	$267
Individual fixed annuities	30	872	(12)	890	275
Individual variable annuities	132	51	8	191	56
Individual annuities runoff*	6	111	(17)	100	5
Total	$262	$ 1,597	$(24)	$ 1,835	$ 603
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	21%	(9)%	%	(22)%	(55)%
Individual fixed annuities	(20)	(5)		(24)	(85)
Individual variable annuities	20	(25)		(8)	(27)
Individual annuities runoff*	(50)	(14)		(21)	
Total	15%	(8)%	%	(22)%	(67)%

**Primarily represents runoff annuity business sold through discontinued distribution relationships.*

Total revenues and operating income for each sub-product group included in Domestic Retirement Services declined for the three months ended September 30, 2007 compared to the same period in 2006, primarily due to increased realized capital losses and lower net investment income. Net realized capital losses for group retirement products and individual fixed annuities increased due to an increase in other-than-temporary impairments and sales to reposition assets in

Table of Contents

certain investment portfolios. For individual variable annuities, net realized capital losses were higher in 2007 compared to 2006, primarily due to changes in the value of certain product guarantees and related hedges associated with living benefit features. Net investment income decreased in group retirement and individual fixed annuities primarily due to lower income from partnerships. For individual variable annuities, net investment income was lower in 2007 compared to 2006 resulting from lower balances in the guaranteed fixed income option due to policyholder elections and lower partnership income. These declines were partially offset by an overall increase in variable annuity fees resulting from an increase in assets under management. Individual variable annuity fees also increased due to an increased number of contracts with living benefit features. Individual annuities runoff operating income declined for the three months ended September 30, 2007 compared to the same period in 2006 due to lower net investment income resulting from decreases in the underlying reserves and lower yield enhancement income.

Year-to-date Domestic Retirement Services Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Nine Months Ended September 30, 2007					
Group retirement products	**$ 331**	**$ 1,721**	**$ (229)**	**$ 1,823**	**$661**
Individual fixed annuities	**75**	**2,723**	**(346)**	**2,452**	**606**
Individual variable annuities	**460**	**123**	**(29)**	**554**	**146**
Individual annuities runoff*	**16**	**294**	**(20)**	**290**	**39**
Total	**$ 882**	**$ 4,861**	**$ (624)**	**$ 5,119**	**$1,452**
Nine Months Ended September 30, 2006					
Group retirement products	$ 284	$ 1,674	$ (116)	$ 1,842	$724
Individual fixed annuities	93	2,650	(264)	2,479	694
Individual variable annuities	390	153	3	546	143
Individual annuities runoff*	15	323	(37)	301	27
Total	$ 782	$ 4,800	$ (414)	$ 5,168	$1,588
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	17%	3%	%	(1)%	(9)%
Individual fixed annuities	(19)	3		(1)	(13)
Individual variable annuities	18	(20)		1	2
Individual annuities runoff*	7	(9)		(4)	44
Total	13%	1%	%	(1)%	(9)%

* *Primarily represents runoff annuity business sold through discontinued distribution relationships.*

Revenues and operating income for Domestic Retirement Services for the first nine months of 2007 declined compared to the same period in 2006 primarily due to increased realized capital losses, partially offset by higher net investment income in group retirement products and individual fixed annuities, and an overall increase in variable annuity fees resulting from the increase in assets under management and more individual variable annuity contracts with living benefit features. Net realized capital losses for Domestic Retirement Services increased due to higher other-than-temporary impairments and sales to reposition assets in certain investment portfolios for both group retirement products and individual fixed annuities, as well as from changes in the value of certain individual variable annuity product guarantees and related hedges associated with living benefit features. The increases in net investment income in group retirement products and individual fixed annuities resulted from higher partnership and yield enhancement income, while net investment income for individual variable annuities was lower in 2007 primarily due to policyholders election to shift from the fixed income option to the variable income option. Operating income for group retirement products and individual fixed annuities decreased for the nine months in 2007 driven by the lower revenues and higher expenses, including higher amortization of DAC for both product groups and higher sales inducement costs for individual fixed annuities. DAC amortization increases for group retirement products were related to the increase in surrenders and policy changes adding guaranteed minimum withdrawal benefit riders to existing contracts. DAC amortization and sales inducement cost increases for individual fixed annuities were related to increased surrenders and an approximately $32 million adjustment reflecting certain changes in actuarial estimates from the conversion to a new DAC system, as well as unlocking future assumptions and experience updates.

Individual annuities runoff operating income increased in the first nine months of 2007 over the same period of 2006 largely due to lower realized capital losses.

Domestic Retirement Services Supplemental Data

The following table presents deposits*:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2007**	2006	**2007**	2006
Group retirement products:				
Annuities	**$ 1,533**	$ 1,335	**$ 4,414**	$ 4,083
Mutual funds	**501**	284	**1,296**	1,085
Individual fixed annuities	**993**	1,035	**3,857**	3,770
Individual variable annuities	**1,181**	1,059	**3,393**	3,234
Individual fixed annuities runoff	**13**	13	**40**	42
Total	**$ 4,221**	$ 3,726	**$ 13,000**	$ 12,214

* *Excludes internal replacements.*

Domestic Retirement Services deposits increased for the three months ended September 30, 2007 compared to the same period in 2006. Group retirement deposits increased 26 percent in the three months ended September 30, 2007 compared to the same period in 2006 as a result of an increase in both group annuity deposits and group mutual funds. Over time, AIG expects that group mutual fund sales will result in a gradual reduction in overall profit margins in this business due to the growth in the lower-margin mutual fund products relative to the annuity products. Individual fixed annuity deposits decreased slightly for the three months ended September 30, 2007 compared to the same period in 2006 as a result of increased competition from bank deposit products and money market funds offering competitive short-term rates in the current yield curve environment. Individual variable annuity deposits increased 12 percent for the three months ended September 30, 2007 compared to the same period in 2006.

Individual fixed annuity surrenders increased 19 percent in the three months ended September 30, 2007 over the same period in 2006 due to policies coming out of their surrender charge periods and increased competition from banks. AIG expects this trend to continue into 2008 as a significant amount of business comes out of its surrender charge period. Individual fixed annuity net flows for the three months ended September 30, 2007 declined compared to the same period in 2006, reflecting the higher surrenders discussed above.

Domestic Retirement Services deposits increased for the first nine months of 2007 compared to the same period in 2006. The increase primarily reflects higher deposits from group retirement products, individual fixed annuities and individual variable annuities. Group retirement deposits increased 10 percent in the first nine months of 2007 compared to the same period in 2006 as a result of an increase in both group variable annuity and group mutual funds deposits, partially offset by slightly lower deposits in group fixed annuities. Although individual fixed annuity sales continued to face increased competition from bank deposit products and money market funds offering very competitive short-term rates in the current yield curve environment, individual fixed annuity deposits increased 2 percent for the nine months ended September 30, 2007 compared to the same period in 2006. Individual variable annuity deposits increased 5 percent in the first nine months of 2007 compared to the same period in 2006 despite the discontinuation of a major bank proprietary product.

Group retirement surrenders increased as a result of normal maturing of the business and due to a few large group surrenders in the first three months of 2007 compared to the same period last year. Individual fixed annuity surrenders increased in the first nine months of 2007 compared to the same period in 2006 due to policies coming out of their surrender charge period and increased competition from banks. Individual fixed annuities net flows for the first nine months of 2007 declined compared to the same period in 2006, reflecting the higher surrenders discussed above, partially offset by slightly higher deposits.

The following table presents Domestic Retirement Services reserves by surrender charge category as of September 30, 2007:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$ 46,193	$ 9,763	$ 13,142
0% - 2%	6,519	2,835	5,597
Greater than 2% - 4%	3,771	7,904	5,598
Greater than 4%	3,191	27,205	9,348
Non-Surrenderable	875	3,429	92
Total	$ 60,549	$ 51,136	$ 33,777

* *Excludes mutual funds of $8.2 billion.*

Surrender rates increased for group retirement products and individual fixed annuities for the first nine months of 2007 compared to the same period in 2006. Surrender rates for group retirement products increased as a result of normal maturing of the business and due to a few large group surrenders in the first nine months of 2007 compared to the same period in 2006. New products and strategies have been introduced to retain assets. The increase in the surrender rate for fixed annuities continues to be driven by a relatively flat yield curve and the general aging of the in-force block; however, less than 20 percent of the individual fixed annuity reserves as of September 30, 2007 were available for surrender without charge. Individual variable annuities surrender rates were slightly lower in the first nine months of 2007 compared to the same period in 2006.

An increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

The following table presents the net flows(a) by line of business:

(in millions)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Group retirement products*(b)*	**$ 319**	$ 158	**$ 453**	$ 793
Individual fixed annuities	**(1,535)**	(1,179)	**(3,047)**	(2,198)
Individual variable annuities	**26**	11	**(59)**	(34)
Individual fixed annuities runoff	**(213)**	(286)	**(705)**	(772)
Total	**$ (1,403)**	$ (1,296)	**$ (3,358)**	$ (2,211)

(a) Net flows are defined as deposits received less benefits, surrenders, withdrawals and death benefits.
(b) Includes mutual funds.

Higher surrenders in the group retirement and individual fixed annuity blocks, offset somewhat by increased deposits on both blocks, resulted in negative net flows for the first nine months of 2007. The continuation of the current interest rate and competitive environment would prolong this trend.

American International Group, Inc. and Subsidiaries

Life Insurance & Retirement Services Net Investment Income and Net Realized Capital Gains (Losses)

The following table summarizes the components of Net investment income:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2007**	2006	**2007**	2006
Foreign Life Insurance & Retirement Services:				
Fixed maturities, including short-term investments	**$ 2,031**	$ 1,720	**$ 5,846**	$ 4,968
Equity securities	**239**	142	**386**	255
Interest on mortgage, policy and collateral loans	**119**	114	**346**	333
Partnership income		36	**86**	76
Unit investment trusts[(a)]	**(14)**	28	**107**	223
Other[(b)]	**(42)**	26	**89**	91
Total investment income before policyholder income and trading gains (losses)	**2,333**	2,066	**6,860**	5,946
Policyholder investment income and trading gains (losses)[(c)]	**141**	485	**2,017**	969
Total investment income	**2,474**	2,551	**8,877**	6,915
Investment expenses	**107**	61	**266**	200
Net investment income	**$ 2,367**	$ 2,490	**$ 8,611**	$ 6,715
Domestic Life Insurance:				
Fixed maturities, including short-term investments	**$ 865**	$ 864	**$ 2,646**	$ 2,563
Equity securities	**3**	1	**1**	3
Interest on mortgage, policy and collateral loans	**110**	88	**312**	257
Partnership income excluding Synfuels	**26**	24	**113**	36
Partnership income (loss) Synfuels	**(26)**	(20)	**(101)**	(79)
Unit investment trusts	**(2)**	2	**2**	2
Other[(b)]	**11**	13	**51**	43
Total investment income before policyholder income and trading gains (losses)	**987**	972	**3,024**	2,825
Policyholder investment income and trading gains (losses)[(c)]	**9**	-	**9**	-
Total investment income	**996**	972	**3,033**	2,825
Investment expenses	**11**	14	**37**	41
Net investment income	**$ 985**	$ 958	**$ 2,996**	$ 2,784

Domestic Retirement Services:				
Fixed maturities, including short-term investments	**$ 1,325**	$ 1,404	**$ 4,089**	$ 4,232
Equity securities	**4**	5	**28**	10
Interest on mortgage, policy and collateral loans	**141**	113	**397**	328
Partnership income excluding Synfuels	**6**	79	**389**	280
Other(b)	**9**	10	**1**	(10)
Total investment income	**1,485**	1,611	**4,904**	4,840
Investment expenses	**14**	14	**43**	40
Net investment income	**$ 1,471**	$ 1,597	**$ 4,861**	$ 4,800
Total:				
Fixed maturities, including short-term investments	**$ 4,221**	$ 3,988	**$ 12,581**	$ 11,763
Equity securities	**246**	148	**415**	268
Interest on mortgage, policy and collateral loans	**370**	315	**1,055**	918
Partnership income excluding Synfuels	**32**	139	**588**	392
Partnership income (loss) Synfuels	**(26)**	(20)	**(101)**	(79)
Unit investment trusts(a)	**(16)**	30	**109**	225
Other(b)	**(22)**	49	**141**	124
Total investment income before policyholder income and trading gains (losses)	**4,805**	4,649	**14,788**	13,611
Policyholder investment income and trading gains (losses)(c)	**150**	485	**2,026**	969
Total investment income	**4,955**	5,134	**16,814**	14,580
Investment expenses	**132**	89	**346**	281
Net investment income(d)	**$ 4,823**	$ 5,045	**$ 16,468**	$ 14,299

(a) *Includes the effect of an out of period UCITS adjustment in 2006. For the three and nine-month periods ended September 30, 2006 the effect was an increase of $24 million and $240 million, respectively, in net investment income and $24 million and $169 million, respectively, in operating income.*

(b) *Other includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services equal share of the results of AIG Credit Card Company (Taiwan).*

(c) *Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are offset by an equal change included in incurred policy losses and benefits.*

(d) *Includes call and tender income.*

Net investment income decreased for the three-month period ended September 30, 2007 compared to the same period in 2006. Securities market volatility significantly affected the net investment income results for this quarter as partnership and hedge fund income, UCITS and mutual fund income and policyholder trading gains fell below last year s results. Net

63

investment income increased for the nine-month period ended September 30, 2007 compared to the same period in 2006. Fixed maturities income rose as the underlying invested asset base grew. Yield enhancement activity increased over the same period in 2006. Earnings on certain interests in UCITS for the first nine months of 2007 were lower than the same period in 2006 as results in 2006 included a $240 million out of period adjustment. Policyholder trading gains (losses) increased for the nine months ended September 30, 2007 compared to the same period in 2006 and generally follow the trend of equity markets in the respective periods. Net investment income for certain operations include investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. For 2007, these investments generated income of $1 million and $44 million for the three and nine-month periods ended September 30, 2007, respectively, compared to income of $6 million and losses of $22 million for the same periods in 2006. In addition, period to period comparisons of investment income for some investment activities, particularly partnership income, are affected by yield enhancement activity. See also Insurance and Asset Management Invested Assets herein.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits separately from segment operating results in its consolidated provision for income taxes. The amounts of those income tax credits were $115 million and $79 million for the first nine months of 2007 and 2006, respectively. For a further discussion of the effect of fluctuating domestic crude oil prices on synfuel tax credits, see Note 6(c) of Notes to Consolidated Financial Statements.

The following table summarizes Net realized capital gains (losses) by major category:

(in millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Foreign Life Insurance & Retirement Services:				
Sales of fixed maturities	**$ (122)**	$ (28)	**$ (167)**	$ (174)
Sales of equity securities	**205**	14	**417**	415
Other:				
Foreign exchange transactions	**247**	133	**337**	43
Derivatives instruments	**(130)**	(219)	**(195)**	127
Other-than-temporary decline	**(90)**	(33)	**(552)**	(78)
Other[(a)]	**28**	104	**81**	154
Total Foreign Life Insurance & Retirement Services	**$ 138**	$ (29)	**$ (79)**	$ 487
Domestic Life Insurance:				
Sales of fixed maturities	**$ (18)**	$ 1	**$ (57)**	$ (60)
Sales of equity securities	**1**	8	**6**	14
Other:				
Foreign exchange transactions	**5**	(6)	**7**	(6)
Derivatives instruments	**(121)**	(98)	**(91)**	17
Other-than-temporary decline	**(96)**	(24)	**(164)**	(139)
Other[(b)]	**(66)**	(4)	**(24)**	(16)
Total Domestic Life Insurance	**$ (295)**	$ (123)	**$ (323)**	$ (190)

Domestic Retirement Services:				
Sales of fixed maturities	**$ (20)**	$ 19	**$ (80)**	$ (69)
Sales of equity securities	**4**	(8)	**20**	23
Other:				
Foreign exchange transactions	**6**	(13)	**13**	(13)
Derivatives instruments	**(34)**	13	**(81)**	(23)
Other-than-temporary decline	**(148)**	(40)	**(334)**	(301)
Other[b]	**(142)**	5	**(162)**	(31)
Total Domestic Retirement Services	**$ (334)**	$ (24)	**$ (624)**	$ (414)
Total:				
Sales of fixed maturities	**$ (160)**	$ (8)	**$ (304)**	$ (303)
Sales of equity securities	**210**	14	**443**	452
Other:				
Foreign exchange transactions	**258**	114	**357**	24
Derivative instruments	**(285)**	(304)	**(367)**	121
Other-than-temporary decline	**(334)**	(97)	**(1,050)**	(518)
Other	**(180)**	105	**(105)**	107
Total:	**$ (491)**	$ (176)	**$ (1,026)**	$ (117)

(a) Includes losses of $16 million and $15 million for the three-month periods ended September 30, 2007 and 2006, respectively, and losses of $21 million and gains of $33 million for the nine months ended September 30, 2007 and 2006, respectively, allocated to participating policyholders.

(b) Includes losses of $71 million and $130 million for Domestic Life Insurance and Domestic Retirement Services, respectively, for the three and nine-month periods ended September 30, 2007, related to sales to reposition assets in certain investment portfolios.

Net realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses and other-than-temporary declines in the value of investments. In the first nine months of 2007, Life Insurance & Retirement Services operations incurred losses of $1 billion from the decrease in the value of securities deemed to be other than temporarily impaired. These losses were related to both the decline in value of U.S. dollar bonds held in Thailand and Singapore, which reflects the depreciation of the U.S. dollar against local currencies, and a change in management s intent to hold the securities to recovery, in part, due to the recent volatility in the securities markets. Net realized capital losses in the Foreign Life operations in the first nine months of 2007 include losses of $195 million related to derivatives that did not qualify for hedge accounting treatment compared to a gain of $127 million in the same period in 2006. Derivatives in the Foreign Life operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the respective currency of the country, principally in Taiwan, Thailand, and Singapore. The corresponding foreign exchange gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income until the bond is sold or deemed to be other than temporarily impaired.

Deferred Policy Acquisition Costs, Sales Inducement Assets and Future Policy Benefit Reserves

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products), are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Total acquisition costs deferred increased $138 million in the first nine months of 2007 compared to the first nine months in 2006, primarily due to higher production in the Foreign Life operations partially offset by lower Domestic Life sales. Total amortization expense increased $307 million compared to the first nine months in 2006. Annualized amortization expense levels for 2007 and 2006 are approximately 13 percent of the opening DAC balance.

American International Group, Inc. and Subsidiaries

The following table summarizes the major components of the changes in DAC/ Value of Business Acquired (VOBA) and Sales Inducement Assets (SIA):

	Nine Months Ended September 30,					
(in millions)	**2007**			2006		
	DAC/VOBA	**SIA**	**Total**	DAC/VOBA	SIA	Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$ 21,153**	**$ 404**	**$ 21,557**	$ 17,638	$ 192	$ 17,830
Acquisition costs deferred	**4,047**	**99**	**4,146**	3,735	79	3,814
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**44**		**44**	3		3
Related to unlocking future assumptions	**53**	**4**	**57**	63		63
All other amortization	**(2,141)**	**(12)**	**(2,153)**	(1,894)	(16)	(1,910)
Change in unrealized gains (losses) on securities	**558**	**13**	**571**	232	(2)	230
Increase (decrease) due to foreign exchange	**125**	**4**	**129**	554	9	563
Other *	**68**		**68**		96	96
Balance at end of period	**$ 23,907**	**$ 512**	**$ 24,419**	$ 20,331	$ 358	$ 20,689
Domestic Life Insurance						
Balance at beginning of year	**$ 6,006**	**$ 46**	**$ 6,052**	$ 5,184	$ 31	$ 5,215
Acquisition costs deferred	**656**	**12**	**668**	856	14	870
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**8**		**8**	20		20
All other amortization	**(526)**	**(4)**	**(530)**	(529)	(1)	(530)
Change in unrealized gains (losses) on securities	**197**		**197**	369		369
Increase (decrease) due to foreign exchange	**80**		**80**	20		20
Other *	**(64)**		**(64)**			
Balance at end of period	**$ 6,357**	**$ 54**	**$ 6,411**	$ 5,920	$ 44	$ 5,964
Domestic Retirement Services						
Balance at beginning of year	**$ 5,651**	**$ 887**	**$ 6,538**	$ 5,284	$ 871	$ 6,155

Acquisition costs deferred	**553**	**150**	**703**	522	173	695
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**96**	**22**	**118**	58	19	77
Related to unlocking future assumptions	**4**	**(17)**	**(13)**	(1)		(1)
All other amortization	**(677)**	**(120)**	**(797)**	(572)	(109)	(681)
Change in unrealized gains (losses) on securities	**314**	**62**	**376**	353	(91)	262
Balance at end of period	**$ 5,941**	**$ 984**	**$ 6,925**	$ 5,644	$ 863	$ 6,507
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$ 32,810**	**$ 1,337**	**$ 34,147**	$ 28,106	$ 1,094	$ 29,200
Acquisition costs deferred	**5,256**	**261**	**5,517**	5,113	266	5,379
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**148**	**22**	**170**	81	19	100
Related to unlocking future assumptions	**57**	**(13)**	**44**	62		62
All other amortization	**(3,344)**	**(136)**	**(3,480)**	(2,995)	(126)	(3,121)
Change in unrealized gains (losses) on securities	**1,069**	**75**	**1,144**	954	(93)	861
Increase (decrease) due to foreign exchange	**205**	**4**	**209**	574	9	583
Other *	**4**		**4**		96	96
Balance at end of period	**$ 36,205**	**$ 1,550**	**$ 37,755**	$ 31,895	$ 1,265	$ 33,160

* *Current year primarily represents the cumulative effect of the adoption of SOP 05-1. Prior year represents a balance sheet reclassification.*

DAC for insurance-oriented, investment-oriented and retirement services products is reviewed for recoverability, which involves estimating the future profitability of current business. This review involves significant management judgment. If actual future profitability is substantially lower than estimated, AIG s results of operations could be significantly affected in future periods.

Future Policy Benefit Reserves

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for Life Insurance & Retirement Services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a lock-in principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in force outside of North America, 46 percent of total policyholder benefit liabilities at September 30, 2007 resulted from traditional business where the lock-in principle applies. In most foreign locations, guarantees have been made to pay benefits to policyholders for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect the observed changes. Because of the long-term nature of many of AIG s liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy.

Taiwan

Beginning in 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to approximately 2.6 percent at September 30, 2007. Yields on most other invested assets have correspondingly dropped over the same period. Current sales are focused on products such as:

- variable separate account products which do not contain interest rate guarantees,
- participating products which contain very low implied interest rate guarantees, and
- A&H policies and riders.

In developing the reserve adequacy analysis for Nan Shan, several key best estimate assumptions have been made:

- Observed historical mortality improvement trends have been projected to 2014;
- Morbidity, expense and termination rates have been updated to reflect recent experience;
- Taiwan government bond rates are expected to remain at current levels for 10 years and gradually increase to best estimate assumptions of a market consensus view of long-term interest rate expectations. Foreign assets are assumed to comprise 35 percent of invested assets, resulting in a composite long-term investment assumption of approximately 4.8 percent; and
- The currently permitted practice of offsetting positive mortality experience with negative interest margins, thus eliminating the need for mortality dividends, will continue.

Future results of the reserve adequacy tests involve significant management judgment as to mortality, morbidity, expense and termination rates and investment yields. Changes in these assumptions accelerate DAC amortization and necessitate reserve strengthening.

Financial Services Operations

AIG s Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results were as follows:

	Three Months Ended September 30,	Percentage Increase/	Nine Months Ended September 30,	Percentage Increase/

(in millions)	**2007**	2006	(Decrease)	**2007**	2006	(Decrease)
Revenues:						
Aircraft Leasing[(a)]	**$ 1,237**	$ 950	30 %	**$ 3,468**	$ 3,013	15 %
Capital Markets[(b)(c)]	**540**	1,118	(52)	**701**	30	
Consumer Finance[(d)(e)]	**992**	901	10	**2,824**	2,768	2
Other, including intercompany adjustments	**16**	42	(62)	**116**	112	4
Total	**$ 2,785**	$ 3,011	(8) %	**$ 7,109**	$ 5,923	20 %
Operating income (loss):						
Aircraft Leasing[(a)]	**$ 254**	$ 47	440 %	**$ 625**	$ 421	48 %
Capital Markets[(b)(c)]	**370**	965	(62)	**183**	(457)	
Consumer Finance[(d)(e)]	**69**	151	(54)	**180**	529	(66)
Other, including intercompany adjustments	**(24)**	16	( )	**20**	48	(58)
Total	**$ 669**	$ 1,179	(43) %	**$ 1,008**	$ 541	86 %

(a) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(19) million and

$(111) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(32) million and $(56) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Revenues, shown net of interest expense of $1.4 billion and $802 million for the three-month periods ended September 30, 2007 and 2006, respectively, and $3.3 billion and $2.1 billion for the nine-month periods ended September 30, 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $428 million and $783 million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(185) million and $(1.1) billion, respectively. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million, respectively, related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain transactions.

(c) For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP s super senior credit default swap portfolio.

(d) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(6) million and $(73) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(21) million and $(65) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(e) The nine-month period ended September 30, 2007 includes a pre-tax charge of $178 million in connection with domestic consumer finance s mortgage banking activities.

Financial Services operating income decreased in the three-month period and increased in the nine-month period ended September 30, 2007 compared to the same periods in 2006 primarily due to differences in the accounting treatment for hedging activities. In the first quarter of 2007, AIGFP began applying hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings. During 2006, hedge accounting under FAS 133 was not being applied to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the related hedged assets and liabilities.

The third quarter and the first nine months of 2007 included out of period charges of $49 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 included an out of period gain of $115 million and a charge of $223 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133.

Beginning in the first quarter of 2007, net realized capital gains and losses, including derivative gains and losses and foreign exchange transaction gains and losses for Financial Services entities other than AIGFP, which were previously reported as part of AIG s Other category, are now included in Financial Services revenues and operating income. For the three and nine-month periods ended September 30, 2007, the amount included in both Financial Services revenues and operating income was a loss of $66 million and a loss of $70 million, respectively. All prior periods have been revised to conform to the current presentation.

Aircraft Leasing

Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial aircraft for ILFC s own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC economically hedges the majority of its floating rate and foreign currency denominated debt using interest rate and foreign currency derivatives. Starting in the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives. All of ILFC s derivatives are effective economic hedges; however, since hedge accounting under FAS 133 was not applied prior to April 2, 2007, the benefits of using derivatives to hedge these exposures are not reflected in ILFC s 2006 corporate borrowing rate. The composite borrowing rates at September 30, 2007 and 2006 were 5.28 percent and 5.14 percent, respectively.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft idle or off lease when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had one aircraft off lease at September 30, 2007, and all but two new aircraft scheduled for delivery through 2008 have been leased.

Quarterly Aircraft Leasing Results

ILFC s operating income increased in the three months ended September 30, 2007 compared to the same period of 2006 by $207 million, or 440 percent. Rental revenues increased by $160 million or 15 percent, driven by a larger aircraft fleet, higher lease rates and higher utilization. As of September 30, 2007, ILFC s fleet subject to operating leases consisted of 894 aircraft compared to 818 aircraft as of September 30, 2006. Flight equipment marketing revenues increased by $12 million in the third quarter of 2007 compared to the same period in 2006 due to higher realization on aircraft sales. During the third quarter of 2007, ILFC realized income of $24 million from the sale of its rights against a bankrupt airline. The increase in revenues was partially offset by increases in depreciation and interest expense. Depreciation expense increased by $42 million, or 10 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $20 million, or 5 percent, driven by additional borrowings to fund aircraft purchases and the rising cost of funds. As noted above, ILFC s interest expense did not reflect the benefit of hedging these exposures in 2006. For the three-month periods ended September 30, 2007 and 2006, the losses from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $19 million and $111 million, respectively, in both revenues and operating income.

Year-to-date Aircraft Leasing Results

ILFC s operating income increased in the first nine months of 2007 compared to the same period in 2006 by $204 million, or 48 percent. Rental revenues increased by $432 million or 15 percent, driven by a larger aircraft fleet and higher lease rates. During the first nine months of 2007, ILFC realized income of $24 million from the sale of its rights against a bankrupt airline. The increase in revenues was partially offset by reduced flight equipment marketing revenues and increases in depreciation and interest expense. Flight marketing revenues decreased by $23 million compared to the same period in 2006 due to fewer aircraft sales. Depreciation expense increased by $133 million, or 11 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $162 million, or 15 percent, driven by additional borrowings to fund aircraft purchases and the rising cost of funds. ILFC s interest expense did not reflect the benefit of hedging these exposures in the first quarter of 2007 and in 2006. For the first nine months of 2007 and 2006, the losses from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $32 million and $56 million, respectively, in both revenues and operating income. During the first nine months of 2006, ILFC recorded adjustments related to a tax settlement in Australia, increased credit reserves and lease accruals totaling $37 million.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving the issuance of standard and structured notes and other securities, and entering into guaranteed investment agreements (GIAs).

Beginning in 2007, AIGFP applied hedge accounting under FAS 133 to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks offsetting the gains and losses on the derivatives designated as hedges. Prior to 2007, AIGFP did not apply hedge accounting under FAS 133 to any of its derivatives or related assets and liabilities.

Since 1998, AIGFP has written super senior (AAA+) protection through credit default swaps, a portion of which is exposed to CDOs of residential mortgage-backed securities and other asset-backed securities. AIGFP has structured this portfolio to provide protection such that AIGFP is at risk on only the super senior portion related to a diversified portfolio of credits referenced to loans or debt securities. The super senior risk portion is the last tranche to suffer losses after significant subordination. Credit losses would have to erode all tranches junior to the super senior tranche before AIGFP would have any payment obligation. The subordination level required for each transaction is determined based on internal modeling and analysis of the pool of underlying credits. The subordination levels are not dependent on ratings determined by the rating agencies.

At September 30, 2007, the notional amount of this credit derivative portfolio was $513 billion, covering the following asset classes:

(in billions)	Net Notional Exposure
Corporate	$294
European residential mortgages	141
Multi-sector CDO*	78
Total	$513

* *Approximately $63 billion of the multi-sector CDO pools includes some exposure to U.S. subprime mortgages.*

As of October 31, 2007, all of AIGFP s super senior exposures continued to have tranches below AIGFP s attachment point that have been explicitly rated AAA or, in AIGFP s judgment, would have been rated AAA had they been rated. AIGFP s portfolio of credit default swaps is carefully structured, undergoes regular monitoring, modeling and analysis and contains significant protection through collateral subordination. In addition, in December 2005, AIGFP stopped committing to writing super senior protection for CDOs that included any U.S. subprime collateral, although collateral managers are permitted to substitute collateral in some of the underlying CDOs, in each case subject to certain restrictions.

AIGFP accounts for the super senior credit default swaps in accordance with FAS 133 Accounting For Derivative Instruments and Hedging Activities and Emerging Issues Task Force 02-3, Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities (EITF 02-3). In accordance with EITF 02-3, AIGFP does not recognize income in earnings at the inception of each transaction because the inputs to value these instruments are not derivable from observable market data. AIGFP values its super senior credit default swaps using internal methodologies that utilize available market observable information and incorporate management estimates and judgments when information is not available. It also employs the Binomial Expansion Technique (BET) model where appropriate to help estimate the fair value of these derivatives. The BET model utilizes credit spreads for the collateral pool obtained from an independent source. The model also utilizes diversity scores, weighted average lives, recovery rates and discount rates. The BET model does not adequately quantify the benefit of certain structural mitigants, such as triggers that accelerate the amortization of the more senior tranches, that AIGFP believes are important to the appropriate valuation of its transactions. AIG believes that the value of these mitigants could range from zero to $50 million, but is not able to reliably estimate their value at this time. Therefore, AIG s estimate of the fair value of AIGFP s super senior credit default swaps as of September 30, 2007 does not attribute value to these features.

The valuation of the super senior credit derivatives has become increasingly challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets has increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

As of October 31, 2007, AIG is aware that estimates made by certain AIGFP counterparties with respect to the fair value of certain AIGFP super senior credit default swaps and the collateral required in connection with such instruments differ significantly from AIGFP s estimates.

For a further description of AIGFP s risk management practices in its credit default swaps business, see Management s Discussion and Analysis of Financial Condition and Results of Operations Risk Management Segment Risk Management Financial Services in the 2006 Annual Report on Form 10-K.

Quarterly Capital Markets Results

Capital Markets operating income decreased in the three months ended September 30, 2007 by $595 million compared to the same period in 2006, primarily due to changes in accounting related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, as described below. During the third quarter of 2007, AIGFP continued to experience good transaction flow in its rates and currency products which contributed to its revenues. AIGFP recognized total net gains of $153 million for the three months ended September 30, 2007 related to credit default swaps and embedded credit derivatives in credit-linked notes. This gain was offset by an unrealized market valuation loss of $352 million related to AIGFP s super senior credit default swap portfolio, principally written on multi-sector CDOs, and an out of period charge of $51 million for a change in the projected timing of income tax cash flows from a series of lease transactions.

The $352 million unrealized market valuation loss represented a decline in the fair value of super senior credit derivatives for the three-month period ended September 30, 2007, resulting from the significant disruption in the structured finance markets. AIG continues to believe that it is highly unlikely that AIGFP will be required to make payments with respect to these derivatives.

Included in the net gains of $153 million recognized by AIGFP was a net unrealized market valuation gain of $131 million on certain credit default swaps and embedded credit derivatives in credit-linked notes for the three and nine-month periods ended September 30, 2007. In these transactions, AIGFP purchased protection at the AAA to BBB-rated risk layers on portfolios of reference obligations that include multi-sector CDO obligations. This gain was driven by the significant widening in credit spreads during the period. Also included were net gains of $22 million for the three and nine-month periods ended September 30, 2007 on credit derivatives on home equity, CMBS and corporate credits.

In addition, in the three months ended September 30, 2007 AIGFP recognized a net gain of $428 million related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, compared to a net gain of $783 million for the same period in 2006. The net gain in the three months ended September 30, 2007 reflects the effect of decreases in U.S. interest rates and the weakening of the U.S. dollar on derivatives hedging AIGFP s assets and liabilities. The net gain in the third quarter of 2006 included an out of period charge of $115 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133.

Financial market conditions in the three months ended September 30, 2007 were characterized by decreases in global interest rates, increases in credit spreads, higher equity valuations and a weaker U.S. dollar.

The most significant component of Capital Markets operating expenses is compensation, which was $136 million and $115 million in the three-month periods ended September 30, 2007 and 2006, respectively. The amount of compensation is not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133. AIG does not currently intend to have the unrealized market valuation gains and losses described above affect the amount of compensation. Accordingly, compensation expense for the three and nine-month periods does not reflect these amounts.

AIG elected to early adopt FAS 155, Accounting for Certain Hybrid Financial Instruments (FAS 155) in 2006 and AIGFP elected to apply the fair value option to certain structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. AIGFP recognized a gain of $21 million in the third quarter of 2007 and a gain of $85 million in the third quarter of 2006 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP s operating income.

Year-to-date Capital Markets Results

Capital Markets operating income increased in the first nine months of 2007 by $640 million compared to the same period in 2006, primarily due to changes in accounting related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, as described below. AIGFP experienced higher transaction flow in the first nine months of 2007 in its rates and currency products. Operating income for the first nine months of 2007 also includes a net unrealized market valuation gain of $131 million related to certain credit default swaps purchased against the AAA to BBB-rated risk layers on portfolios of reference obligations and net gains of $35 million on home equity, CMBS and corporate credit derivatives. These gains were offset by the net unrealized market valuation loss of $352 million and the out of period charge of $51 million, discussed above.

In the first nine months of 2007, AIGFP also recognized a net loss of $185 million related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, compared to a net loss of $1.1 billion for the same period in 2006. The first nine months of 2007 included out of period charges of $346 million, as noted above, including a charge of $380 million to reverse net gains recognized in previous periods on transfers of available for sale securities among legal entities consolidated within AIGFP, and a $166 million reduction in fair value at March 31, 2007 of certain derivatives that are an integral part of, and economically hedge, the structured transactions potentially affected by the proposed regulations issued by the U.S. Treasury Department discussed above in Overview of Operations and Business Outlook. The net loss on AIGFP s derivatives recognized in the first nine months of 2006 included an out of period charge of $223 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133. The net loss also reflects the effect of increases in U.S. interest rates and a weakening of the U.S. Dollar on derivatives hedging AIGFP s assets and liabilities.

Financial market conditions in the first nine months of 2007 were characterized by increases in global interest rates, increases in credit spreads, higher equity valuations and a slightly weaker U.S. dollar.

Compensation expense was $412 million and $380 million in the first nine months of 2007 and 2006, respectively.

AIGFP recognized a gain of $51 million in the first nine months of 2007 and a loss of $4 million in the first nine months of 2006 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP s operating income.

Consumer Finance

AIG s consumer finance operations in North America are principally conducted through AGF. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. The real estate loans are comprised principally of first-lien mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. The real estate loans may be closed-end accounts or open-end home equity lines of credit and are principally fixed rate products. AGF does not offer mortgage products with borrower payment options that allow for negative amortization of the principal balance. The secured non-real estate loans are secured by consumer goods, automobiles or other personal property. Both secured and unsecured non-real estate loans and retail sales finance receivables generally have a maximum term of 60 months.

The majority of AGF s finance receivables are sourced through its branches. However, a significant volume of real estate loans is also sourced through its centralized real estate operations, which include its mortgage banking activities. These loans are collateralized by first and second liens on one to four-family properties and are originated largely through broker relationships and to a lesser extent are originated through correspondent relationships and directly to consumers. The majority of these loans are sold to investors on a servicing-released basis. These real estate loans usually have maximum original terms of 360 months, are generally considered non conforming and include fixed, adjustable and hybrid-adjustable loans. From July 2003 through May 2006, AGF s centralized real estate operations originated loans through a servicing arrangement with AIG Federal Savings Bank (AIG Bank), a federally chartered thrift. The origination relationship was terminated in the first quarter of 2006. Since then, all new loans have been originated directly by AGF subsidiaries under their own state licenses.

On June 7, 2007, AIG s domestic consumer finance operations, consisting of AIG Bank, AGF s mortgage banking subsidiary Wilmington Finance, Inc. (WFI) and AGF, entered into a Supervisory Agreement with the Office of Thrift Supervision (OTS). The Supervisory Agreement pertains to certain mortgage loans originated in the name of AIG Bank from July 2003 through early May 2006 pursuant to a servicing agreement between WFI and AIG Bank, which was terminated in February 2006. Pursuant to the terms of the Supervisory Agreement, AIG Bank, WFI and AGF have undertaken a financial remediation program whereby certain borrowers may be provided loans on more affordable terms and/or reimbursed for certain fees. Pursuant to the requirements of the Supervisory Agreement, AGF has engaged the services of an external consultant to monitor, evaluate and periodically report to the OTS with respect to the matters covered by the Supervisory Agreement. Separately, the domestic consumer finance operations also committed to donate $15 million to certain not-for-profit organizations to support their efforts to promote financial literacy and credit counseling.

Management s best estimate of the cost of implementing the financial remediation plan contemplated by the Supervisory Agreement, including the $15 million donation, was $178 million at September 30, 2007. A charge in the amount of $128 million was recorded in the first quarter of 2007 while the remaining $50 million was recorded in the second quarter of 2007 at the time the terms of the Supervisory Agreement were finalized. As the estimate is based on judgments and assumptions made by management, the actual cost of implementing the financial remediation plan may differ from this estimate.

AIG s foreign consumer finance operations are principally conducted through AIG Consumer Finance Group, Inc. (AIGCFG). AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan and Thailand and most recently began operations in India through the acquisition of a majority interest in a sales finance lending operation during the first quarter of 2007 and the acquisition of a mortgage lending operation in the second quarter of 2007. In addition, AIGCFG expanded its distribution channels in Thailand by acquiring in the first quarter of 2007 an 80 percent interest in a company with a network of over 130 branches for secured consumer lending. AIGCFG is continuously exploring expansion opportunities in its existing operations as well as new geographic locations throughout the world. Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Quarterly Consumer Finance Results

Consumer Finance operating income decreased by $82 million, or 54 percent, in the three months ended September 30, 2007 compared to the same period in 2006.

The operating income from the domestic consumer finance operations, which include the operations of AGF and AIG Bank, decreased by $68 million, or 49 percent, for the three months ended September 30, 2007 compared to the same period in 2006. For the three months ended September 30, 2007, domestic results were adversely affected by the weakening housing market and tighter underwriting guidelines, which resulted in lower originations of real estate loans.

AGF s net finance receivables totaled $25.4 billion at September 30, 2007, an increase of approximately $1 billion compared to the prior year period, including $19.5 billion of real estate secured loans, most of which were underwritten with full income verification. The increase in the net finance receivables resulted in a similar increase in revenues generated from these assets.

AGF s revenues increased $34 million or 5 percent during the three-month period ended September 30, 2007 compared to the same period in 2006. Revenues from AGF s mortgage banking activities decreased $68 million or 87 percent during the three-month period ended September 30, 2007 compared to the same period in 2006. The decrease in revenues was primarily caused by a significantly reduced origination volume, and to a lesser extent, tighter underwriting guidelines, reduced third party margins and higher warranty reserves, which cover obligations to repurchase loans sold to third-party investors should there be a first payment default or breach of representations and warranties.

AGF s interest expense increased by $9 million or 3 percent as its long-term borrowing rate increased in the three months ended September 30, 2007 compared to the same period in 2006. During the three months ended September 30, 2007, AGF recorded a net loss of $5 million on its derivatives that did not qualify for hedge accounting under FAS 133, including the related foreign exchange losses, compared to a net loss of $67 million for the same period in 2006. Commencing in the second quarter of 2007, AGF began applying hedge accounting.

Revenues from the foreign consumer finance operations increased by approximately 32 percent to $232 million in the three months ended September 30, 2007 compared to the same period in 2006. Loan growth, particularly in Poland, Thailand and Latin America, was the primary driver of the higher revenues. The increase in revenues was more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns.

Year-to-date Consumer Finance Results

Consumer Finance operating income decreased by $349 million, or 66 percent, in the first nine months of 2007 compared to the same period in 2006.

The operating income for the first nine months of 2007 from the domestic consumer finance operations decreased by $379 million or 72 percent from the same period of 2006. Pursuant to the terms of the Supervisory Agreement, as discussed above, charges of $178 million were recorded during the first nine months of 2007.

Additionally, for the first nine months of 2007, domestic results were adversely affected by the weakening housing market and tighter underwriting guidelines, which resulted in lower originations for real estate loans.

Although mortgage loan originations declined in the first nine months of 2007, the softening of home price appreciation (reducing the equity customers may be able to extract from their homes by refinancing) contributed to an increase in non-real estate loans of 12 percent at September 30, 2007 compared to September 30, 2006. Retail sales finance receivables also increased 19 percent compared to September 30, 2006 due to increased marketing efforts and customer demand. AGF s centralized real estate business segment finance receivables decreased by 2 percent while branch business segment finance receivables increased by 9 percent. AGF s results for the first nine months of 2007 also included a recovery of $65 million from a favorable out of court settlement.

AGF s revenues decreased $69 million or 3 percent for the nine-month period ended September 30, 2007 compared to the same period in 2006. Revenues from AGF s mortgage banking activities decreased $306 million or 152 percent during the nine-month period ended September 30, 2007 compared to the same period in 2006, which also reflects charges relating to the Supervisory Agreement. The decrease in revenues was primarily caused by significantly reduced origination volume, and to a lesser extent, tighter underwriting guidelines, a shift in distribution channels, and higher warranty reserve, which covers AGF s obligations to repurchase loans sold to third-party investors should there be a first payment default or breach of representations and warranties.

AGF s interest expense increased by $73 million or 8 percent as both its short-term and long-term borrowing rates increased in the first nine months of 2007 compared to the same period in 2006. Its short-term borrowing rates averaged 5.40 percent in the first nine months of 2007 compared to 5.06 percent in the same period of 2006, while long-term borrowing rates averaged 5.19 percent in the first nine months of 2007 compared to 4.97 percent in the first nine months of 2006.

For the first nine months of 2007, domestic consumer finance revenues and operating income also declined from the prior year, partially due to the change in fair value of the derivatives hedging borrowings which did not qualify for hedge accounting treatment under FAS 133 during either period. During the first nine months of 2007, AGF recorded a net loss of $24 million on such derivatives, including the related foreign exchange losses, compared to a net loss of $63 million for the same period in 2006.

Revenues from the foreign consumer finance operations increased by 25 percent in the first nine months of 2007 compared to the same period of 2006. Loan growth, particularly in Poland, Thailand and Latin America, was the primary driver of the increased revenues. The increase in revenues were more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns. Operating income in the first nine months of 2006 reflects AIGCFG s $44 million share of the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market.

Credit Quality of Finance Receivables

The overall credit quality of AGF s finance receivables portfolio deteriorated modestly due to negative economic fundamentals, a higher proportion of non-real estate loans and retail sales finance loans and the aging of the real estate loan portfolio.

As of September 30, 2007, the 60-day delinquency rate for the entire portfolio increased by 55 basis points to 2.47 percent compared to the same period in 2006, while the 60-day delinquency rate for the real estate loans increased by 63 basis points to 2.22 percent. For the three months ended September 30, 2007, AGF s net charge-off rate increased to 1.15 percent compared to 0.92 percent for the same period in 2006 and for the nine months ended September 30, 2007 increased to 1.05 percent compared to 0.89 percent for the same period in 2006, which reflected $6 million of non-recurring recoveries recorded in the first quarter of 2006.

AGF s allowance for finance receivables losses as a percentage of outstanding receivables was 2.11 percent at September 30, 2007 compared to 1.99 percent at September 30, 2006.

Asset Management Operations

AIG s Asset Management operations comprise a wide variety of investment-related services and investment products. Such services and products are offered to individuals and institutions both domestically and overseas, and are primarily comprised of Spread-Based Investment Businesses, Institutional Asset Management and Brokerage Services and Mutual Funds.

The revenues and operating income for this segment are affected by the general conditions in the equity and credit markets. In addition, net realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions.

Spread-Based Investment Business

In prior years, the sale of GICs to investors, both domestically and overseas, was AIG s primary institutional Spread-Based Investment Business. During 2005, AIG launched its MIP and its asset management subsidiaries, primarily SunAmerica Life, ceased writing new GIC business. The GIC business will continue to run off for the foreseeable future while the MIP business is expected to grow.

Institutional Asset Management

AIG s Institutional Asset Management business provides an array of investment products and services globally to institutional investors, AIG subsidiaries and affiliates and high net worth investors. These products and services include traditional equity and fixed income investment management and a full range of alternative asset classes. Delivery of AIG s Institutional Asset Management products and services is accomplished via a global network of operating subsidiaries comprising AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIG Investments). The primary operating entities within this group are AIG Global Investment Corp., AIG Global Real Estate Investment Corp. and AIG Private Bank. AIG Private Bank offers banking, trading and investment management services to private client and high net worth individuals and institutions globally.

Within the alternative investment asset class, AIG Investments offers hedge and private equity fund-of-funds, direct investments and distressed debt investments. Within the structured fixed income and equity product asset class, AIG Investments offers various forms of structured and credit linked notes, various forms of collateralized debt obligations and other investment strategies aimed at achieving superior returns or capital preservation.

From time to time, AIG Investments acquires alternative investments, primarily consisting of direct private equity investments, on a temporary basis, warehousing such investments until the investment or economic benefit thereof is transferred to a fund or other AIG managed investment product. As a consequence of this warehousing activity, AIG incurs the cost of carrying these investments and consolidates the balance sheet and operating results until the new managed investment product is launched.

Brokerage Services and Mutual Funds

AIG s Brokerage Services and Mutual Funds business provides mutual fund and broker-dealer related services to retail investors, group trusts and corporate accounts through an independent network of financial advisors. The AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other

Included in the Other category for Asset Management is income or loss from certain SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results were as follows:

(in millions)	Three Months Ended September 30, 2007	2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2007	2006	Percentage Increase/ (Decrease)
Revenues:						
Spread-Based Investment Business	**$ 555**	$ 552	1%	**$ 2,304**	$ 1,924	20%
Institutional Asset Management:						
Institutional Asset Management	**362**	255	42	**1,635**	883	85
Consolidated Managed Partnerships & Funds	**300**	58	417	**765**	422	81
Consolidated Warehouse Investments	**458**	-	-	**465**	-	-
Total Institutional Asset Management	**1,120**	313	258	**2,865**	1,305	120
Brokerage Services and Mutual Funds	**83**	71	17	**243**	217	12
Other	**66**	57	16	**309**	201	54
Total	**$ 1,824**	$ 993	84%	**$ 5,721**	$ 3,647	57%
Operating income:						
Spread-Based Investment Business	**$ 24**	$ 44	(45)%	**$ 759**	$ 467	63%
Institutional Asset Management:						
Institutional Asset Management	**49**	46	7	**737**	311	137
Consolidated Managed Partnerships & Funds	**293**	44	566	**748**	410	82
Consolidated Warehouse Investments*	**(39)**	-	-	**(79)**	-	-
Total Institutional Asset Management	**303**	90	237	**1,406**	721	95
Brokerage Services and Mutual Funds	**27**	23	17	**74**	67	10
Other	**65**	54	20	**302**	190	59
Total	**$ 419**	$ 211	99%	**$ 2,541**	$ 1,445	76%

* *Includes operating costs as well as the cost of funding these investments.*

Asset Management revenues and operating income increased in the three and nine-month periods ended September 30, 2007 compared to the same periods in 2006 due to the effect of consolidated managed partnerships and funds, consolidated warehouse investments and, for the first nine months of 2007, a gain of $398 million from the sale of a portion of AIG s investment in Blackstone Group, LP in connection with its initial public offering. Income arising from consolidated managed partnerships and funds is included in operating income, but offset in minority interest expense, which is not a component of operating income. Offsetting the increase in revenues is an operating loss due to the effect of consolidating the operating results of warehoused investments for the three and nine-month periods ended September 30, 2007. AIG expects to divest the consolidated warehouse investments through various managed investment products in future periods.

Beginning in the first quarter of 2007, net realized capital gains and losses, including derivative gains and losses and foreign exchange transaction gains and losses, which were previously reported as part of AIG s Other category, are now included in Asset Management revenues and operating income. For the three and nine-month periods of 2007, the amount included in both Asset Management revenues and operating income was a loss of $232 million and a gain of $100 million, respectively. The three and nine-month periods of 2006 reflected losses of $106 million and $109 million, respectively. All prior periods have been revised to conform to the current presentation.

In order to better align financial reporting with the manner in which AIG s chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, revenues and operating income related to foreign investment contracts, which were historically reported as a component of the Spread-Based Investment business, are now being reported in the Life Insurance & Retirement Services segment. All prior periods have been revised to conform to the current presentation.

Quarterly Spread-Based Investment Business Results

Operating income related to the Spread-Based Investment business decreased in the three months ended September 30, 2007 compared to the same period in 2006 due to losses associated with the MIP. MIP operating income decreased during the three months ended September 30, 2007 compared to the same period of 2006 primarily due to foreign exchange losses on foreign-denominated debt that, while economically hedged, did not qualify for hedge accounting treatment under FAS 133, as well as other than temporary write-downs on certain investments and mark to market losses on derivatives that did not qualify for hedge accounting treatment under FAS 133. These losses are partially offset by an increase in partnership income associated with the GIC program and higher income from private equity partnerships. Partnership income is primarily derived from alternative investments and is affected by performance in the equity and credit markets. Thus, revenues, operating income and cash flows attributable to GICs will vary from reporting period to reporting period.

As anticipated, GIC balances continue to run off. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG believes these hedges are economically effective, but they did not qualify for hedge accounting treatment under FAS 133. Income or loss from these hedges are classified as net realized capital gains or losses in the Asset Management segment results.

The following table illustrates the anticipated runoff of the domestic GIC portfolio at September 30, 2007:

(in billions)	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
Domestic GICs	$ 4.8	$ 11.9	$ 2.7	$ 6.7	$ 26.1

During 2005, the MIP replaced the GIC program as AIG s principal institutional spread-based investment activity. AIG does not expect that income growth in the MIP will offset the runoff in the GIC portfolio for the foreseeable future because the asset mix under the MIP does not include the alternative investments utilized in the GIC program. Commencing in the first quarter of 2007, AIG applied hedge accounting for certain derivative transactions related to the MIP.

Year-to-date Spread-Based Investment Business Results

Operating income related to the Spread-Based Investment business increased in the first nine months of 2007 compared to the same period in 2006 due to a significant increase in partnership income associated with the Domestic GIC program. Partnership income in the first nine months of 2007 included a distribution from a single partnership of $164 million, which became available after a five-year restriction on capital withdrawals.

MIP operating income decreased in the first nine months of 2007 compared to the same period in 2006, reflecting foreign exchange losses on foreign-denominated debt that, while economically hedged, did not qualify for hedge accounting treatment under FAS 133, as well as other-than-temporary write-downs on certain investments and mark to market losses on derivatives not receiving hedge accounting treatment. Through September 30, 2007, AIG has issued the equivalent of $6.8 billion of securities to fund the MIP in the Euromarkets and the U.S. public and private markets.

Quarterly Institutional Asset Management Results

Operating income for Institutional Asset Management increased in the three months ended September 30, 2007 compared to the same period in 2006, due to higher asset management fees resulting from growth in assets under management; an increase in carried interest, which was driven by higher valuations of portfolio investments and is generally associated with improved equity markets performance; and increased income from consolidated managed partnerships and funds, which are offset in minority interest expense that is not a component of operating income. These increases were partially offset by the effect of consolidating the operating results of various warehoused investments, an increase in distribution expenses related to the launch of several new investment products and the timing of real estate sales compared to the year ago quarter.

Year-to-date Institutional Asset Management Results

Operating income for Institutional Asset Management increased in the first nine months of 2007 compared to the same period in 2006 reflecting the $398 million gain from the sale of a portion of AIG s investment in Blackstone Group, LP in connection with its initial public offering and increased carried interest driven by higher valuations of portfolio investments which are generally associated with improved performance in the equity markets. Operating income also reflects higher income from certain consolidated managed partnerships and funds; however, this income is offset in minority interest expense. Partly offsetting this income was a decrease in net realized capital gains related to real estate investments as well as increased expenses resulting from investment in sales and infrastructure enhancements and the effect of consolidating the operating results of various warehoused investments.

AIG s unaffiliated client assets under management, including retail mutual funds and institutional accounts, increased 24 percent to $93.1 billion from December 31, 2006 to September 30, 2007, contributing to growth in base management fees. Additionally, AIG Investments successfully launched several new private equity and real estate funds in the first nine months of 2007, which provide both a base management fee and the opportunity for future performance fees.

While unaffiliated client assets under management and the resulting management fees continue to increase, the growth in operating income has trailed the growth in revenues due to additional warehousing activities as well as the costs associated with sales and infrastructure enhancements. The sales and infrastructure enhancements are associated with AIG s planned expansion of marketing and distribution capabilities, combined with technology and operational infrastructure-related improvements.

Table of Contents

Other Operations

The operating loss of AIG s Other category was as follows:

(in millions)	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Other operating income (loss):				
Equity earnings in unconsolidated entities	**$ 37**	$ 48	**$ 128**	$ 178
Interest expense	**(315)**	(227)	**(869)**	(633)
Unallocated corporate expenses*	**(157)**	(89)	**(519)**	(337)
Compensation expense SICO Plans	**(9)**	(14)	**(29)**	(104)
Compensation expense Starr tender offer				(54)
Net realized capital gains (losses)	**(199)**	85	**(226)**	31
Other miscellaneous, net	**16**	11	**(42)**	(34)
Total Other	**$ (627)**	$ (186)	**$ (1,557)**	$ (953)

* *Includes expenses of corporate staff not attributable to specific business segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses.*

The operating loss of AIG s Other category increased in the third quarter and first nine months of 2007 compared to the comparable periods in 2006, reflecting higher interest expenses resulting from increased borrowings, higher unallocated corporate expenses and foreign exchange losses on foreign-denominated debt of which a portion is economically hedged, but did not qualify for hedge accounting treatment under FAS 133.

Operating loss for the first nine months of 2006 included an out of period charge of $61 million related to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million.

Beginning in the first quarter of 2007, derivative gains and losses and foreign exchange transaction gains and losses for Asset Management and Financial Services entities (other than AIGFP) are now included in Asset Management and Financial Services revenues and operating income. These amounts were previously reported as part of AIG s Other category. All prior periods have been revised to conform to the current presentation.

Capital Resources and Liquidity

Borrowings

At September 30, 2007, AIG s total borrowings amounted to $176.2 billion as follows:

(in millions)	**September 30, 2007**	December 31, 2006
AIG s net borrowings	**$ 20,299**	$ 17,126
Junior subordinated debt	**4,681**	
Liabilities connected to trust preferred stock	**1,440**	1,440
MIP matched notes and bonds payable	**12,754**	5,468
Series AIGFP matched notes and bonds payable	**530**	72
AIGFP		

GIAs		**19,495**		20,664
Matched notes and bonds payable		**41,552**		35,776
Hybrid financial instrument liabilities*		**7,692**		8,856
Borrowings not guaranteed by AIG		**67,742**		59,277
Total	**$**	**176,185**	$	148,679

** Represents structured notes issued by AIGFP that are accounted for using the fair value option.*

Borrowings issued or guaranteed by AIG and subsidiary borrowings not guaranteed by AIG were as follows:

(in millions)		**September 30, 2007**		December 31, 2006
AIG borrowings:				
Notes and bonds payable	**$**	**10,784**	$	8,915
Junior subordinated debt		**4,681**		
Loans and mortgages payable		**210**		841
MIP matched notes and bonds payable		**12,754**		5,468
Series AIGFP matched notes and bonds payable		**530**		72
Total AIG Borrowings		**28,959**		15,296
Borrowings guaranteed by AIG:				
AIGFP				
GIAs		**19,495**		20,664
Notes and bonds payable		**44,215**		37,528
Hybrid financial instrument liabilities[(a)]		**7,692**		8,856
Total		**71,402**		67,048
AIG Funding, Inc. commercial paper		**5,845**		4,821
AIGLH Notes and bonds payable		**797**		797
Liabilities connected to trust preferred stock		**1,440**		1,440
Total borrowings issued or guaranteed by AIG		**108,443**		89,402
Borrowings not guaranteed by AIG:				
ILFC				
Commercial paper		**3,818**		2,747
Junior subordinated debt		**999**		999
Notes and bonds payable[(b)]		**26,904**		25,592
Total		**31,721**		29,338
AGF				
Commercial paper		**5,229**		4,328
Junior subordinated debt		**349**		

Notes and bonds payable	**18,998**	19,595
Total	**24,576**	23,923
AIGCFG		
Commercial paper	**177**	227
Loans and mortgages payable	**1,534**	1,453
Total	**1,711**	1,680

(in millions)		**September 30, 2007**		December 31, 2006
AIG Finance Taiwan Limited commercial paper		**15**		26
Other Subsidiaries		**753**		672
Borrowings of consolidated investments:				
A.I. Credit		**881**		880
AIG Investments		**3,364**		193
AIG Global Real Estate Investment		**4,523**		2,307
AIG SunAmerica		**193**		203
ALICO		**5**		55
Total		**8,966**		3,638
Total borrowings not guaranteed by AIG		**67,742**		59,277
Total Debt	**$**	**176,185**	$	148,679

(a) Represents structured notes issued by AIGFP that are accounted for using the fair value option.
(b) Includes borrowings under Export Credit Facility of $2.7 billion at September 30, 2007 and $2.7 billion at December 31, 2006.

The debt activity, excluding commercial paper and extendible commercial notes of $15.08 billion and borrowings of consolidated investments of $8.97 billion, for the nine months ended September 30, 2007 was as follows:

(in millions)

	Balance at December 31, 2006	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes	**Balance at September 30, 2007**
AIG						
Notes and bonds payable	$ 8,915	$ 1,759	$ (65)	$ 110	$ 65	**$ 10,784**
Junior subordinated debt		4,490		191		**4,681**
Loans and mortgages payable	841	82	(724)	11		**210**
MIP matched notes and bonds payable	5,468	6,835		94	357	**12,754**
Series AIGFP matched notes and bonds payable	72	457			1	**530**

AIGFP						
GIAs	20,664	6,430	(7,545)		(54)	**19,495**
Notes and bonds payable and hybrid financial instrument liabilities	46,384	36,045	(31,118)	508	88	**51,907**
AIGLH notes and bonds payable	797					**797**
Liabilities connected to trust preferred stock	1,440					**1,440**
ILFC notes and bonds payable	25,592	3,748	(2,811)	371	4	**26,904**
ILFC junior subordinated debt	999					**999**
AGF notes and bonds payable	19,595	3,199	(3,829)	226	(193)	**18,998**
AGF junior subordinated debt		346			3	**349**
AIGCFG loans and mortgages payable	1,453	2,541	(2,510)	50		**1,534**
Other subsidiaries	672	21	(30)	(3)	93	**753**
Total	$ 132,892	$ 65,953	$ (48,632)	$ 1,558	$ 364	**$ 152,135**

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for the MIP. As of September 30, 2007, AIG had up to $21.9 billion of debt securities, preferred stock and other securities, and up to $16.5 billion of common stock, registered and available for issuance under its universal shelf registration statement.

AIG maintains a medium term note program under its shelf registration statement. As of September 30, 2007, approximately $4.2 billion principal amount of notes were outstanding under the medium term note program, of which $749 million was used for AIG s general corporate purposes, $529 million was used by AIGFP and $3.0 billion was used to fund the MIP. The maturity dates of these notes range from 2008 to 2052. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

AIG also maintains a Euro medium term note program under which, as of September 30, 2007, an aggregate nominal amount of up to $20.0 billion of notes may be outstanding at any one time. As of September 30, 2007, the equivalent of $10.9 billion of notes were outstanding under the program, of which $8.4 billion were used to fund the MIP and the remainder was used for AIG s general corporate purposes. The aggregate amount outstanding includes $839 million loss resulting from foreign exchange translation into U.S. dollars, of which $288 million loss relates to notes issued by AIG for general corporate purposes and $551 million loss relates to notes issued to fund the MIP.

During the first nine months of 2007, AIG issued in Rule 144A offerings an aggregate of $2.0 billion principal amount of senior notes, of which $650 million was used to fund the MIP and $1.4 billion was used for AIG s general corporate purposes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes, of which the equivalent of $434 million was outstanding as of September 30, 2007, the proceeds of which were used for AIG s general corporate purposes. AIG also maintains an Australian dollar debt program under which senior notes with an aggregate principal amount of up to 5 billion Australian dollars may be outstanding at any one time. Although as of September 30, 2007 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG s general corporate purposes.

During the first nine months of 2007, AIG issued an aggregate of $4.49 billion of junior subordinated debentures in four series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to repurchase shares of AIG s common stock. In connection with each series of junior subordinated debentures, AIG entered into a Replacement Capital Covenant (RCC) for the benefit of the holders of AIG s 6.25 percent senior notes due 2036. The RCCs provide that AIG will not repay, redeem, or purchase the applicable series of junior subordinated debentures on or before a specified date, unless it has received qualifying proceeds from the sale of replacement capital securities.

AIG began applying hedge accounting for certain AIG parent transactions in the first quarter of 2007.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP s notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG s early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP s notes and bonds and GIA borrowings. See Operating Review Financial Services Operations, Liquidity and Derivatives herein.

AIGFP has a Euro medium term note program under which, as of September 30, 2007, an aggregate nominal amount of up to $20.0 billion of notes may be outstanding at any one time. As of September 30, 2007, $7.18 billion of notes were outstanding under the program, including $899 million loss resulting from foreign exchange translation into U.S. dollars. The notes issued under this program are guaranteed by AIG and are included in AIGFP s Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding) issues commercial paper that is guaranteed by AIG in order to help fulfill the short-term cash requirements of AIG and its subsidiaries. The issuance of AIG Funding s commercial paper, including the guarantee by AIG, is subject to the approval of AIG s Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of September 30, 2007, had an aggregate of $9.2 billion available to be drawn and which are summarized below under Revolving Credit Facilities.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC s Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which, as of September 30, 2007, totaled $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC s maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At September 30, 2007, $4.65 billion of debt securities had been issued under this registration statement and $5.89 billion had been issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $4.28 billion in notes were outstanding at September 30, 2007. Notes issued under the Euro medium term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The cumulative foreign exchange adjustment loss for the foreign currency denominated debt was $1.1 billion at September 30, 2007 and $733 million at December 31, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro-denominated operating lease payments.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At September 30, 2007, ILFC had $748 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2008. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a nine-month forward-looking calendar, and the interest rate is determined through a bid process. At September 30, 2007, ILFC had $1.9 billion outstanding under this facility. Borrowings with respect to these facilities are included in ILFC s notes and bonds payable in the preceding table of borrowings. The debt is collateralized by a pledge of shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

From time to time, ILFC enters into funded financing agreements. As of September 30, 2007, ILFC had a total of $1.1 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

The proceeds of ILFC s debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Operating Review Financial Services Operations and Liquidity herein.

AGF

AGF fulfills most of its short-term cash borrowing requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF s Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of September 30, 2007, totaled $4.75 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF s commercial paper programs.

As of September 30, 2007, notes and bonds aggregating $19.01 billion were outstanding with maturity dates ranging from 2007 to 2031 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes and bonds. As a well-known seasoned issuer, AGF filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At September 30, 2007, AGF had remaining corporate authorization to issue up to $10.8 billion of debt securities under its shelf registration statements.

AGF s funding sources include a medium term note program, private placement debt, retail note issuances, bank financing and securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables are used to fund cash needs including the payment of principal and interest on AGF s debt. AIG does not guarantee any of the debt obligations of AGF. See also Operating Review Financial Services Operations and Liquidity herein.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including retail and wholesale deposits, short-term and long-term bank loans, securitizations and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, and AIG Retail Bank PLC, a full service consumer bank in Thailand, have issued commercial paper for the funding of their respective operations. AIG does not guarantee any borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

AIG, ILFC and AGF maintain committed, unsecured revolving credit facilities listed on the table below in order to support their respective commercial paper programs and for general corporate purposes. AIG, ILFC and AGF expect to replace or extend these credit facilities on or prior to their expiration. Some of the facilities, as noted below, contain a term-out option allowing for the conversion by the borrower of any outstanding loans at expiration into one-year term loans.

As of September 30, 2007 (in millions)

Facility	Size	Borrower(s)	Available Amount	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$ 2,125	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	**$ 2,125**	July 2008	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	**1,625**	July 2011	No
364-Day Bilateral Facility [(b)]	3,200	AIG/AIG Funding	**72**	November 2007	Yes
364-Day Intercompany Facility[(c)]	5,335	AIG	**5,335**	September 2008	Yes
Total AIG	$ 12,285		**$ 9,157**		
ILFC:					
5-Year Syndicated Facility	$ 2,500	ILFC	**$ 2,500**	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2009	No
Total ILFC	$ 6,500		**$ 6,500**		
AGF:					
364-Day Syndicated Facility	$ 2,625	American General Finance Corporation American General Finance, Inc.[(d)]	**$ 2,625**	July 2008	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	**2,125**	July 2010	No
Total AGF	$ 4,750		**$ 4,750**		

(a) Guaranteed by AIG.

(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.

(c) Subsidiaries of AIG are the lenders on this facility.

(d) American General Finance, Inc. is an eligible borrower for up to $400 million only.

81

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short-term and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of October 31, 2007. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating s relative rank within the agency s rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody s	S&P	Fitch	Moody (g)	S&P(b)	Fitch(c)
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa2 (2nd of 9)	AA (2nd of 8)	AA (2nd of 9)
AIG Financial Products Corp.(d)	P-1	A-1+		Aa2	AA	
AIG Funding, Inc. (d)	P-1	A-1+	F1+			
ILFC	P-1	A-1+	F1 (1st of 5)	A1 (3rd of 9)	AA-(e) (2nd of 8)	A+ (3rd of 9)
American General Finance Corporation	P-1	A-1 (1st of 6)	F1	A1	A+ (3rd of 8)	A+
American General Finance, Inc.	P-1	A-1	F1			A+

(a) *Moody s Investors Service (Moody s). Moody s appends numerical modifiers 1, 2 and 3 to the generic rating categories to show relative position within rating categories.*

(b) *Standard & Poor s, a division of the McGraw-Hill Companies (S&P). S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.*

(c) *Fitch Ratings (Fitch). Fitch ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.*

(d) *AIG guarantees all obligations of AIG Financial Products Corp. and AIG Funding, Inc.*

(e) *Negative rating outlook. A negative outlook by S&P indicates that a rating may be lowered, but is not necessarily a precursor of a ratings change. The outlook on all other credit ratings in the table is stable.*

These credit ratings are current opinions of the rating agencies. As such, they may be changed, suspended or withdrawn at any time by the rating agencies as a result of changes in, or unavailability of, information or based on other circumstances. Ratings may also be withdrawn at AIG management s request. This discussion of ratings is not a complete list of ratings of AIG and its subsidiaries.

Rating triggers have been defined by one independent rating agency to include clauses or agreements the outcome of which depends upon the level of ratings maintained by one or more rating agencies. Ratings triggers generally relate to events which (i) could result in the termination or limitation of credit availability, or require accelerated repayment, (ii) could result in the termination of business contracts or (iii) could require a company to post collateral for the benefit of counterparties.

AIG believes that any of its own or its subsidiaries contractual oblpx;padding-right:2px;">

1

Cash dividends on common stock
—

—

—

(339
)

—

(339
)
Other
—

—

1

—

(2
)

(1
)
Balance at March 31, 2018
9

$
398

$
8,805

$
4,228

$
(11
)

$
13,420

Balance at December 31, 2018
9

$
398

$
10,322

$
3,612

$
(9
)

$
14,323

Net income
—

—

—

311

—

311

Capital contributions from parent company
—

—

29

—

—

29

Other comprehensive income (loss)
—

—

—

—

1

1

Cash dividends on common stock
—

—

—

(394
)

—

(394
)
Other
—

—

(1
)

—

—

(1
)
Balance at March 31, 2019
9

$
398

$
10,350

$
3,529

$
(8
)

$
14,269

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

FIRST QUARTER 2019 vs. FIRST QUARTER 2018

OVERVIEW

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

Many factors affect the opportunities, challenges, and risks of Georgia Power's business of providing electric service. These factors include the ability to maintain a constructive regulatory environment, to maintain and grow energy sales and customers, and to effectively manage and secure timely recovery of costs. These costs include those related to projected long-term demand growth, stringent environmental standards, including CCR rules, reliability, fuel, capital expenditures, including new generating facilities and expanding and improving transmission and distribution facilities, and restoration following major storms. Georgia Power has various regulatory mechanisms that operate to address cost recovery. Effectively operating pursuant to these regulatory mechanisms and appropriately balancing required costs and capital expenditures with customer prices will continue to challenge Georgia Power for the foreseeable future. Georgia Power is required to file a base rate case by July 1, 2019.

Georgia Power continues to focus on several key performance indicators, including, but not limited to, customer satisfaction, plant availability, system reliability, the execution of major construction projects, and net income.

Plant Vogtle Units 3 and 4 Status

In 2009, the Georgia PSC certified construction of Plant Vogtle Units 3 and 4 (with electric generating capacity of approximately 1,100 MWs each). Georgia Power holds a 45.7% ownership interest in Plant Vogtle Units 3 and 4. In March 2017, the EPC Contractor filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code. In December 2017, the Georgia PSC approved Georgia Power's recommendation to continue construction. The current expected in-service dates remain November 2021 for Unit 3 and November 2022 for Unit 4.

In the second quarter 2018, Georgia Power revised its base capital cost forecast and estimated contingency to complete construction and start-up of Plant Vogtle Units 3 and 4 to $8.0 billion and $0.4 billion, respectively, for a total project capital cost forecast of $8.4 billion (net of $1.7 billion received under the Guarantee Settlement Agreement and approximately $188 million in related Customer Refunds), with respect to Georgia Power's ownership interest.

As a result of the increase in the total project capital cost forecast and Georgia Power's decision not to seek rate recovery of the increase in the base capital costs, the holders of at least 90% of the ownership interests in Plant Vogtle Units 3 and 4 were required to vote to continue construction. In September 2018, the Vogtle Owners unanimously voted to continue construction of Plant Vogtle Units 3 and 4. In connection with the vote to continue construction, Georgia Power entered into (i) a binding term sheet (Vogtle Owner Term Sheet) with the other Vogtle Owners and certain of MEAG's wholly-owned subsidiaries, including MEAG Power SPVJ, LLC (MEAG SPVJ), to take certain actions which partially mitigate potential financial exposure for the other Vogtle Owners and (ii) a term sheet (MEAG Term Sheet) with MEAG and MEAG SPVJ to provide funding with respect to MEAG SPVJ's ownership interest in Plant Vogtle Units 3 and 4 under certain circumstances. On January 14, 2019, Georgia Power, MEAG, and MEAG SPVJ entered into an agreement to implement the provisions of the MEAG Term Sheet. On February 18, 2019, Georgia Power, the other Vogtle Owners, and certain of MEAG's wholly-owned subsidiaries entered into certain amendments to their joint ownership agreements to implement the provisions of the Vogtle Owner Term Sheet.

In April 2019, Southern Nuclear completed a cost and schedule validation process to verify and update quantities of commodities remaining to install, labor hours to install remaining quantities and related productivity, testing and system turnover requirements, and forecasted staffing needs and related costs. This process confirmed the total estimated project capital cost forecast for Plant Vogtle Units 3 and 4. The expected in-service dates of November 2021 for Unit 3 and November 2022 for Unit 4, as previously approved by the Georgia PSC, remain unchanged.

In March 2019, Georgia Power entered into the Amended and Restated Loan Guarantee Agreement with the DOE, under which the proceeds of borrowings may be used to reimburse Georgia Power for Eligible Project Costs incurred in connection with its construction of Plant Vogtle Units 3 and 4, up to approximately $5.130 billion. At March 31, 2019, Georgia Power had a total of $3.46 billion of borrowings outstanding under the related multi-advance credit facilities.

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

See FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Nuclear Construction" and Note (F) to the Condensed Financial Statements under "DOE Loan Guarantee Borrowings" herein for additional information.

RESULTS OF OPERATIONS

Net Income

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(41)	(11.6)

In the first quarter 2019, net income was $311 million compared to $352 million for the corresponding period in 2018. The decrease was primarily due to a decrease in retail revenues largely due to milder weather compared to the corresponding period in 2018 and higher non-fuel operations and maintenance expenses.

Retail Revenues

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(130)	(7.2)

In the first quarter 2019, retail revenues were $1.67 billion compared to $1.80 billion for the corresponding period in 2018.

Details of the changes in retail revenues were as follows:

	First Quarter 2019	
	(in millions)	(% change)
Retail – prior year	$1,798	
Estimated change resulting from –		
Rates and pricing	9	0.5
Sales growth	5	0.3
Weather	(57)	(3.2)
Fuel cost recovery	(87)	(4.8)
Retail – current year	$1,668	(7.2)%

Revenues associated with changes in rates and pricing increased in the first quarter 2019 when compared to the corresponding period in 2018 primarily due to the rate pricing effect of decreased customer usage and increases in revenues recognized under the NCCR tariff, partially offset by lower contributions from commercial and industrial customers with variable demand-driven pricing. See FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Nuclear Construction – Regulatory Matters" herein for additional information related to the NCCR tariff.

Revenues attributable to changes in sales increased in the first quarter 2019 when compared to the corresponding period in 2018. Weather-adjusted residential KWH sales increased 2.1% in the first quarter 2019 largely due to customer growth. Weather-adjusted commercial KWH sales decreased 1.1% in the first quarter 2019 largely due to a decline in average customer usage resulting from an increase in energy saving initiatives, partially offset by customer growth. Weather-adjusted industrial KWH sales were relatively flat in the first quarter 2019. The primary drivers were decreases in the textile and stone, clay, and glass sectors, largely offset by increases in the paper, primary and fabricated metal, and chemical sectors.

Fuel revenues and costs are allocated between retail and wholesale jurisdictions. Retail fuel cost recovery revenues decreased in the first quarter 2019 when compared to the corresponding period in 2018 primarily due to decreased energy sales driven by milder weather, resulting in lower customer demand, and lower generation costs. Electric rates include provisions to periodically adjust billings for fluctuations in fuel costs, including the energy component of purchased power costs. Under these fuel cost recovery provisions, fuel revenues generally equal fuel expenses and do not affect net income. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Fuel Cost Recovery" of Georgia Power in Item 7 of the Form 10-K for additional information.

Wholesale Revenues – Non-Affiliates

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(15)	(34.1)

Wholesale revenues from sales to non-affiliates consist of PPAs and short-term opportunity sales. Wholesale revenues from PPAs have both capacity and energy components. Wholesale capacity revenues from PPAs are recognized either on a levelized basis over the appropriate contract period or the amounts billable under the contract terms and provide for recovery of fixed costs and a return on investment. Wholesale revenues from sales to non-affiliates will vary depending on fuel prices, the market prices of wholesale energy compared to the cost of Georgia Power's and the Southern Company system's generation, demand for energy within the Southern Company system's electric service territory, and the availability of the Southern Company system's generation. Increases and decreases in energy revenues that are driven by fuel prices are accompanied by an increase or decrease in fuel costs and do not have a significant impact on net income. Short-term opportunity sales are made at market-based rates that generally provide a margin above Georgia Power's variable cost of energy.

In the first quarter 2019, wholesale revenues from sales to non-affiliates were $29 million compared to $44 million for the corresponding period in 2018. The decrease was due to a decrease in energy revenues primarily due to lower customer demand and scheduled generation outages.

Other Revenues

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$24	22.0

In the first quarter 2019, other revenues were $133 million compared to $109 million for the corresponding period in 2018. The increase was primarily due to revenue increases of $11 million from unregulated sales primarily associated with new energy conservation projects, $6 million from OATT sales, and $4 million from solar application fees.

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

Fuel and Purchased Power Expenses

	First Quarter 2019 vs. First Quarter 2018	
	(change in millions)	(% change)
Fuel	$ (113)	(27.4)
Purchased power – non-affiliates	(3)	(2.5)
Purchased power – affiliates	5	2.9
Total fuel and purchased power expenses	$ (111)	

In the first quarter 2019, total fuel and purchased power expenses were $593 million compared to $704 million in the corresponding period in 2018. The decrease was primarily due to a $130 million decrease related to the average cost of fuel and purchased power primarily related to lower energy prices and more rainfall for hydro generation, partially offset by a net increase of $19 million related to the volume of KWHs generated and purchased.

Fuel and purchased power energy transactions do not have a significant impact on earnings since these fuel expenses are generally offset by fuel revenues through Georgia Power's fuel cost recovery mechanism. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Fuel Cost Recovery" of Georgia Power in Item 7 of the Form 10-K for additional information.

Details of Georgia Power's generation and purchased power were as follows:

	First Quarter 2019	First Quarter 2018
Total generation (in billions of KWHs)	13	16
Total purchased power (in billions of KWHs)	8	6
Sources of generation (percent) —		
Gas	50	44
Coal	18	29
Nuclear	26	24
Hydro	6	3
Cost of fuel, generated (in cents per net KWH) —		
Gas	2.59	2.72
Coal	3.23	3.36
Nuclear	0.81	0.82
Average cost of fuel, generated (in cents per net KWH)	2.21	2.43
Average cost of purchased power (in cents per net KWH)(*)	3.94	5.38

(*) Average cost of purchased power includes fuel purchased by Georgia Power for tolling agreements where power is generated by the provider.

Fuel

In the first quarter 2019, fuel expense was $299 million compared to $412 million in the corresponding period in 2018. The decrease was primarily due to a 22.1% decrease in the volume of KWHs generated largely due to scheduled generation outages and milder weather, a 9.1% decrease in the average cost of fuel primarily related to lower natural gas and coal prices, and more rainfall for hydro generation.

Purchased Power – Non-Affiliates

In the first quarter 2019, purchased power expense from non-affiliates was $118 million compared to $121 million in the corresponding period in 2018. The decrease was primarily due to a 32.5% decrease in the average cost per KWH purchased primarily due to lower natural gas and coal prices, largely offset by a 35.2% increase in the volume of KWHs purchased primarily due to scheduled generation outages at Georgia Power-owned generating units. The volume increase also reflects purchases from Gulf Power which were classified as affiliate prior to January 1, 2019. See Note (K) to the Condensed Financial Statements under "Southern Company" herein for information regarding the sale of Gulf Power.

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

Purchased Power – Affiliates

In the first quarter 2019, purchased power expense from affiliates was $176 million compared to $171 million in the corresponding period in 2018. The increase was primarily due to a 36.0% increase in the volume of KWHs purchased primarily due to scheduled generation outages at Georgia Power-owned generating units, partially offset by a 22.8% decrease in the average cost per KWH purchased primarily resulting from lower natural gas and coal prices. The increase in the volume of KWHs purchased was partially offset by the effect of classifying purchases from Gulf Power as non-affiliate beginning January 1, 2019. See Note (K) to the Condensed Financial Statements under "Southern Company" herein for information regarding the sale of Gulf Power.

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

Other Operations and Maintenance Expenses

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$38	9.3

In the first quarter 2019, other operations and maintenance expenses were $446 million compared to $408 million in the corresponding period in 2018. The increase was primarily due to increases of $16 million in certain compensation and benefit expenses, $14 million in scheduled generation outage expenses, $9 million of expenses from unregulated sales primarily associated with new energy conservation projects, and $6 million primarily due to the timing of vegetation management and other distribution-related maintenance expenses, partially offset by a decrease of $6 million in customer accounts and sales expenses.

Depreciation and Amortization

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$12	5.3

In the first quarter 2019, depreciation and amortization was $240 million compared to $228 million in the corresponding period in 2018. The increase was primarily due to additional plant in service.

Interest Expense, Net of Amounts Capitalized

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(10)	(9.4)

In the first quarter 2019, interest expense, net of amounts capitalized was $96 million compared to $106 million in the corresponding period in 2018. The decrease was primarily due to a $13 million decrease in interest expense associated with a decrease in outstanding borrowings, partially offset by an increase of $4 million related to PPAs

70

with Southern Power accounted for as finance leases following the adoption of FASB ASC Topic 842, Leases (ASC 842). In prior periods, these expenses were included in purchased power, affiliates. See FINANCIAL CONDITION AND LIQUIDITY – "Sources of Capital" and "Financing Activities" herein for additional information on borrowings and Note (L) to the Condensed Financial Statements herein for additional information regarding Georgia Power's adoption of ASC 842.

Income Taxes

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(12)	(12.9)

In first quarter 2019, income taxes were $81 million compared to $93 million in the corresponding period in 2018. The decrease was primarily due to lower pre-tax earnings and an increase in state ITCs, partially offset by an adjustment in 2018 related to the Tax Reform Legislation.

FUTURE EARNINGS POTENTIAL

The results of operations discussed above are not necessarily indicative of Georgia Power's future earnings potential. The level of Georgia Power's future earnings depends on numerous factors that affect the opportunities, challenges, and risks of Georgia Power's business of providing electric service. These factors include Georgia Power's ability to maintain a constructive regulatory environment that continues to allow for the timely recovery of prudently-incurred costs during a time of increasing costs, continued customer growth, and the weak pace of growth in electricity use per customer, especially in residential and commercial markets. Plant Vogtle Units 3 and 4 construction and rate recovery are also major factors. Earnings will also depend upon maintaining and growing sales, considering, among other things, the adoption and/or penetration rates of increasingly energy-efficient technologies, increasing volumes of electronic commerce transactions, and more multi-family home construction, all of which could contribute to a net reduction in customer usage. Earnings are subject to a variety of other factors. These factors include weather, competition, new energy contracts with other utilities, energy conservation practiced by customers, the use of alternative energy sources by customers, the price of electricity, the price elasticity of demand, and the rate of economic growth or decline in Georgia Power's service territory. Demand for electricity is primarily driven by the pace of economic growth that may be affected by changes in regional and global economic conditions, which may impact future earnings.

For additional information relating to these issues, see RISK FACTORS in Item 1A and MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL of Georgia Power in Item 7 of the Form 10-K.

Environmental Matters

Georgia Power's operations are regulated by state and federal environmental agencies through a variety of laws and regulations governing air, water, land, and protection of other natural resources. Georgia Power maintains comprehensive environmental compliance and GHG strategies to assess upcoming requirements and compliance costs associated with these environmental laws and regulations. The costs, including capital expenditures, operations and maintenance costs, and costs reflected in ARO liabilities, required to comply with environmental laws and regulations and to achieve stated goals may impact future electric generating unit retirement and replacement decisions, results of operations, cash flows, and/or financial condition. Related costs may result from the installation of additional environmental controls, closure and monitoring of CCR facilities, unit retirements, or changing fuel sources for certain existing units, as well as related upgrades to Georgia Power's transmission and distribution systems. A major portion of these costs is expected to be recovered through retail rates. The ultimate impact of environmental laws and regulations and GHG goals will depend on various factors, such as state adoption and implementation of requirements, the availability and cost of any deployed technology, fuel prices, and the outcome of pending and/or future legal challenges.

New or revised environmental laws and regulations could affect many areas of Georgia Power's operations. The impact of any such changes cannot be determined at this time. Environmental compliance costs could affect earnings if such costs cannot continue to be recovered in rates on a timely basis. Georgia Power's Environmental Compliance Cost Recovery (ECCR) tariff allows for the recovery of capital and operations and maintenance costs related to environmental controls mandated by state and federal regulations. Further, increased costs that are recovered through regulated rates could contribute to reduced demand for electricity, which could negatively affect results of operations, cash flows, and/or financial condition. Additionally, many commercial and industrial customers may also be affected by existing and future environmental requirements, which for some may have the potential to ultimately affect their demand for electricity. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Environmental Matters" of Georgia Power in Item 7 and Note 3 to the financial statements under "Environmental Remediation" in Item 8 of the Form 10-K for additional information.

FERC Matters

See Note 2 to the financial statements under "FERC Matters – Open Access Transmission Tariff" in Item 8 of the Form 10-K for additional information.

On March 25, 2019, the Alabama Municipal Electric Authority and Cooperative Energy and SCS and the traditional electric operating companies (including Georgia Power) filed a formal settlement agreement with the FERC agreeing to a rate reduction based on a 10.6% ROE, with a retroactive effective date of May 10, 2018, and a five-year moratorium on these parties seeking changes to the OATT formula rate. The ultimate outcome of this matter cannot be determined at this time; however, if approved by the FERC as filed, the OATT settlement would not have a material impact on the financial statements of Georgia Power.

Retail Regulatory Matters

Georgia Power's revenues from regulated retail operations are collected through various rate mechanisms subject to the oversight of the Georgia PSC. Georgia Power currently recovers its costs from the regulated retail business through the 2013 ARP, which includes traditional base tariff rates, Demand-Side Management tariffs, ECCR tariffs, and Municipal Franchise Fee tariffs. Georgia Power is scheduled to file a base rate case by July 1, 2019, which may continue or modify these tariffs. In addition, financing costs related to certified construction costs of Plant Vogtle Units 3 and 4 are being collected through the NCCR tariff and fuel costs are collected through a separate fuel cost recovery tariff. See Note 2 to the financial statements under "Georgia Power" in Item 8 of the Form 10-K for additional information regarding regulatory matters.

Nuclear Construction

See Note 2 to the financial statements under "Georgia Power – Nuclear Construction" in Item 8 of the Form 10-K for additional information regarding the construction of Plant Vogtle Units 3 and 4, the joint ownership agreements and related funding agreement, VCM reports, and the NCCR tariff.

In 2009, the Georgia PSC certified construction of Plant Vogtle Units 3 and 4. Georgia Power holds a 45.7% ownership interest in Plant Vogtle Units 3 and 4. In 2012, the NRC issued the related combined construction and operating licenses, which allowed full construction of the two AP1000 nuclear units (with electric generating capacity of approximately 1,100 MWs each) and related facilities to begin. Until March 2017, construction on Plant Vogtle Units 3 and 4 continued under the Vogtle 3 and 4 Agreement, which was a substantially fixed price agreement. In March 2017, the EPC Contractor filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code. In connection with the EPC Contractor's bankruptcy filing, Georgia Power, acting for itself and as agent for the other Vogtle Owners, entered into several transitional arrangements to allow construction to continue. In July 2017, Georgia Power, acting for itself and as agent for the other Vogtle Owners, entered into the Vogtle Services Agreement, whereby Westinghouse provides facility design and engineering services, procurement and technical support, and staff augmentation on a time and materials cost basis. The Vogtle Services Agreement provides that it will continue until the start-up and testing of Plant Vogtle Units 3 and 4 are complete and electricity

is generated and sold from both units. The Vogtle Services Agreement is terminable by the Vogtle Owners upon 30 days' written notice.

In October 2017, Georgia Power, acting for itself and as agent for the other Vogtle Owners, executed the Bechtel Agreement, a cost reimbursable plus fee arrangement, whereby Bechtel is reimbursed for actual costs plus a base fee and an at-risk fee, which is subject to adjustment based on Bechtel's performance against cost and schedule targets. Each Vogtle Owner is severally (not jointly) liable for its proportionate share, based on its ownership interest, of all amounts owed to Bechtel under the Bechtel Agreement. The Vogtle Owners may terminate the Bechtel Agreement at any time for their convenience, provided that the Vogtle Owners will be required to pay amounts related to work performed prior to the termination (including the applicable portion of the base fee), certain termination-related costs, and, at certain stages of the work, the applicable portion of the at-risk fee. Bechtel may terminate the Bechtel Agreement under certain circumstances, including certain Vogtle Owner suspensions of work, certain breaches of the Bechtel Agreement by the Vogtle Owners, Vogtle Owner insolvency, and certain other events.

Cost and Schedule

Georgia Power's approximate proportionate share of the remaining estimated capital cost to complete Plant Vogtle Units 3 and 4 by the expected in-service dates of November 2021 and November 2022, respectively, is as follows:

	(in billions)
Base project capital cost forecast[(a)(b)]	$ 8.0
Construction contingency estimate	0.4
Total project capital cost forecast[(a)(b)]	8.4
Net investment as of March 31, 2019[(b)]	(4.9)
Remaining estimate to complete[(a)]	$ 3.5

(a) Excludes financing costs expected to be capitalized through AFUDC of approximately $325 million.

(b) Net of $1.7 billion received from Toshiba under the Guarantee Settlement Agreement and approximately $188 million in related Customer Refunds.

Georgia Power estimates that its financing costs for construction of Plant Vogtle Units 3 and 4 will total approximately $3.1 billion, of which $1.9 billion had been incurred through March 31, 2019.

In April 2019, Southern Nuclear completed a cost and schedule validation process to verify and update quantities of commodities remaining to install, labor hours to install remaining quantities and related productivity, testing and system turnover requirements, and forecasted staffing needs and related costs. This process confirmed the total estimated project capital cost forecast for Plant Vogtle Units 3 and 4. The expected in-service dates of November 2021 for Unit 3 and November 2022 for Unit 4, as previously approved by the Georgia PSC, remain unchanged.

As construction continues, challenges with management of contractors, subcontractors, and vendors; supervision of craft labor and related craft labor productivity, ability to attract and retain craft labor, and/or related cost escalation; procurement, fabrication, delivery, assembly, and/or installation and the initial testing and start-up, including any required engineering changes, of plant systems, structures, or components (some of which are based on new technology that only recently began initial operation in the global nuclear industry at this scale), any of which may require additional labor and/or materials; or other issues could arise and change the projected schedule and estimated cost. Monthly construction production targets established as part of a strategy to maintain and build margin to the approved in-service dates will continue to increase significantly throughout 2019. To meet these increasing monthly targets, existing craft construction productivity must improve and additional craft laborers must be retained and deployed.

There have been technical and procedural challenges to the construction and licensing of Plant Vogtle Units 3 and 4 at the federal and state level and additional challenges may arise. Processes are in place that are designed to assure compliance with the requirements specified in the Westinghouse Design Control Document and the combined

construction and operating licenses, including inspections by Southern Nuclear and the NRC that occur throughout construction. As a result of such compliance processes, certain license amendment requests have been filed and approved or are pending before the NRC. Various design and other licensing-based compliance matters, including the timely resolution of ITAAC and the related approvals by the NRC, may arise, which may result in additional license amendments or require other resolution. If any license amendment requests or other licensing-based compliance issues are not resolved in a timely manner, there may be delays in the project schedule that could result in increased costs. The ultimate outcome of these matters cannot be determined at this time. However, any extension of the regulatory-approved project schedule is currently estimated to result in additional base capital costs of approximately $50 million per month, based on Georgia Power's ownership interests, and AFUDC of approximately $12 million per month. While Georgia Power is not precluded from seeking recovery of any future capital cost forecast increase, management will ultimately determine whether or not to seek recovery. Any further changes to the capital cost forecast that are not expected to be recoverable through regulated rates will be required to be charged to income and such charges could be material.

Joint Owner Contracts

In November 2017, the Vogtle Owners entered into an amendment to their joint ownership agreements for Plant Vogtle Units 3 and 4 to provide for, among other conditions, additional Vogtle Owner approval requirements. Effective in August 2018, the Vogtle Owners further amended the joint ownership agreements to clarify and provide procedures for certain provisions of the joint ownership agreements related to adverse events that require the vote of the holders of at least 90% of the ownership interests in Plant Vogtle Units 3 and 4 to continue construction (as amended, and together with the November 2017 amendment, the Vogtle Joint Ownership Agreements). The Vogtle Joint Ownership Agreements also confirm that the Vogtle Owners' sole recourse against Georgia Power or Southern Nuclear for any action or inaction in connection with their performance as agent for the Vogtle Owners is limited to removal of Georgia Power and/or Southern Nuclear as agent, except in cases of willful misconduct.

As a result of the increase in the total project capital cost forecast and Georgia Power's decision not to seek rate recovery of the increase in the base capital costs in conjunction with the nineteenth VCM report, the holders of at least 90% of the ownership interests in Plant Vogtle Units 3 and 4 were required to vote to continue construction. In September 2018, the Vogtle Owners unanimously voted to continue construction of Plant Vogtle Units 3 and 4.

Amendments to the Vogtle Joint Ownership Agreements

In connection with the vote to continue construction, Georgia Power entered into (i) the Vogtle Owner Term Sheet with the other Vogtle Owners and MEAG's wholly-owned subsidiaries MEAG SPVJ, MEAG Power SPVM, LLC (MEAG SPVM), and MEAG Power SPVP, LLC (MEAG SPVP) to take certain actions which partially mitigate potential financial exposure for the other Vogtle Owners, including additional amendments to the Vogtle Joint Ownership Agreements and the purchase of PTCs from the other Vogtle Owners at pre-established prices, and (ii) the MEAG Term Sheet with MEAG and MEAG SPVJ to provide funding with respect to MEAG SPVJ's ownership interest in Plant Vogtle Units 3 and 4 under certain circumstances. On January 14, 2019, Georgia Power, MEAG, and MEAG SPVJ entered into an agreement to implement the provisions of the MEAG Term Sheet. On February 18, 2019, Georgia Power, the other Vogtle Owners, and MEAG's wholly-owned subsidiaries MEAG SPVJ, MEAG SPVM, and MEAG SPVP entered into certain amendments to the Vogtle Joint Ownership Agreements to implement the provisions of the Vogtle Owner Term Sheet.

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

Regulatory Matters

In 2009, the Georgia PSC voted to certify construction of Plant Vogtle Units 3 and 4 with a certified capital cost of $4.418 billion. In addition, in 2009 the Georgia PSC approved inclusion of the Plant Vogtle Units 3 and 4 related CWIP accounts in rate base, and the State of Georgia enacted the Georgia Nuclear Energy Financing Act, which allows Georgia Power to recover financing costs for Plant Vogtle Units 3 and 4. Financing costs are recovered on all

applicable certified costs through annual adjustments to the NCCR tariff up to the certified capital cost of $4.418 billion. At March 31, 2019, Georgia Power had recovered approximately $1.9 billion of financing costs. Financing costs related to capital costs above $4.418 billion will be recovered through AFUDC; however, Georgia Power will not record AFUDC related to any capital costs in excess of the total deemed reasonable by the Georgia PSC (currently $7.3 billion) and not requested for rate recovery. In December 2018, the Georgia PSC approved Georgia Power's request to increase the NCCR tariff by $88 million annually, effective January 1, 2019.

Georgia Power is required to file semi-annual VCM reports with the Georgia PSC by February 28 and August 31 of each year. In 2013, in connection with the eighth VCM report, the Georgia PSC approved a stipulation between Georgia Power and the staff of the Georgia PSC to waive the requirement to amend the Plant Vogtle Units 3 and 4 certificate in accordance with the 2009 certification order until the completion of Plant Vogtle Unit 3, or earlier if deemed appropriate by the Georgia PSC and Georgia Power.

In 2016, the Georgia PSC voted to approve a settlement agreement (Vogtle Cost Settlement Agreement) resolving certain prudency matters in connection with the fifteenth VCM report. In December 2017, the Georgia PSC voted to approve (and issued its related order on January 11, 2018) Georgia Power's seventeenth VCM report and modified the Vogtle Cost Settlement Agreement. The Vogtle Cost Settlement Agreement, as modified by the January 11, 2018 order, resolved the following regulatory matters related to Plant Vogtle Units 3 and 4: (i) none of the $3.3 billion of costs incurred through December 31, 2015 and reflected in the fourteenth VCM report should be disallowed from rate base on the basis of imprudence; (ii) the Contractor Settlement Agreement was reasonable and prudent and none of the amounts paid pursuant to the Contractor Settlement Agreement should be disallowed from rate base on the basis of imprudence; (iii) (a) capital costs incurred up to $5.68 billion would be presumed to be reasonable and prudent with the burden of proof on any party challenging such costs, (b) Georgia Power would have the burden to show that any capital costs above $5.68 billion were prudent, and (c) a revised capital cost forecast of $7.3 billion (after reflecting the impact of payments received under the Guarantee Settlement Agreement and related Customer Refunds) was found reasonable; (iv) construction of Plant Vogtle Units 3 and 4 should be completed, with Southern Nuclear serving as project manager and Bechtel as primary contractor; (v) approved and deemed reasonable Georgia Power's revised schedule placing Plant Vogtle Units 3 and 4 in service in November 2021 and November 2022, respectively; (vi) confirmed that the revised cost forecast does not represent a cost cap and that prudence decisions on cost recovery will be made at a later date, consistent with applicable Georgia law; (vii) reduced the ROE used to calculate the NCCR tariff (a) from 10.95% (the ROE rate setting point authorized by the Georgia PSC in the 2013 ARP) to 10.00% effective January 1, 2016, (b) from 10.00% to 8.30%, effective January 1, 2020, and (c) from 8.30% to 5.30%, effective January 1, 2021 (provided that the ROE in no case will be less than Georgia Power's average cost of long-term debt); (viii) reduced the ROE used for AFUDC equity for Plant Vogtle Units 3 and 4 from 10.00% to Georgia Power's average cost of long-term debt, effective January 1, 2018; and (ix) agreed that upon Unit 3 reaching commercial operation, retail base rates would be adjusted to include carrying costs on those capital costs deemed prudent in the Vogtle Cost Settlement Agreement. The January 11, 2018 order also stated that if Plant Vogtle Units 3 and 4 are not commercially operational by June 1, 2021 and June 1, 2022, respectively, the ROE used to calculate the NCCR tariff will be further reduced by 10 basis points each month (but not lower than Georgia Power's average cost of long-term debt) until the respective Unit is commercially operational. The ROE reductions negatively impacted earnings by approximately $100 million in 2018 and are estimated to have negative earnings impacts of approximately $75 million in 2019 and an aggregate of approximately $635 million from 2020 to 2022.

In its January 11, 2018 order, the Georgia PSC also stated if other conditions change and assumptions upon which Georgia Power's seventeenth VCM report are based do not materialize, the Georgia PSC reserved the right to reconsider the decision to continue construction.

In February 2018, Georgia Interfaith Power & Light, Inc. (GIPL) and Partnership for Southern Equity, Inc. (PSE) filed a petition appealing the Georgia PSC's January 11, 2018 order with the Fulton County Superior Court. In March 2018, Georgia Watch filed a similar appeal to the Fulton County Superior Court for judicial review of the Georgia PSC's decision and denial of Georgia Watch's motion for reconsideration. In December 2018, the Fulton County Superior Court granted Georgia Power's motion to dismiss the two appeals. On January 9, 2019, GIPL, PSE, and Georgia Watch filed an appeal of this decision with the Georgia Court of Appeals. Georgia Power believes the

appeal has no merit; however, an adverse outcome in the appeal combined with subsequent adverse action by the Georgia PSC could have a material impact on Georgia Power's results of operations, financial condition, and liquidity.
In August 2018, Georgia Power filed its nineteenth VCM report with the Georgia PSC, which requested approval of $578 million of construction capital costs incurred from January 1, 2018 through June 30, 2018. On February 19, 2019, the Georgia PSC approved the nineteenth VCM, but deferred approval of $51.6 million of expenditures related to Georgia Power's portion of an administrative claim filed in the Westinghouse bankruptcy proceedings. Through the nineteenth VCM, the Georgia PSC has approved total construction capital costs incurred through June 30, 2018 of $5.4 billion (before $1.7 billion of payments received under the Guarantee Settlement Agreement and approximately $188 million in related Customer Refunds). In addition, the staff of the Georgia PSC requested, and Georgia Power agreed, to report the results of the cost and schedule validation process to the Georgia PSC (which is expected to occur by May 1, 2019) and to file its twentieth VCM report concurrently with the twenty-first VCM report by August 31, 2019.

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

See RISK FACTORS of Georgia Power in the Form 10-K for a discussion of certain risks associated with the licensing, construction, and operation of nuclear generating units, including potential impacts that could result from a major incident at a nuclear facility anywhere in the world.

DOE Financing

At March 31, 2019, Georgia Power had borrowed $3.46 billion related to Plant Vogtle Units 3 and 4 costs as provided through the Amended and Restated Loan Guarantee Agreement and related multi-advance credit facilities among Georgia Power, the DOE, and the FFB, which provide for borrowings of up to approximately $5.130 billion, subject to the satisfaction of certain conditions. See Note 8 to the financial statements under "Long-term Debt – DOE Loan Guarantee Borrowings" in Item 8 of the Form 10-K and Note (F) to the Condensed Financial Statements under "DOE Loan Guarantee Borrowings" herein for additional information, including applicable covenants, events of default, mandatory prepayment events, and conditions to borrowing.

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

Other Matters

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

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

ACCOUNTING POLICIES

Application of Critical Accounting Policies and Estimates

Georgia Power prepares its financial statements in accordance with GAAP. Significant accounting policies are described in Notes 1, 5, and 6 to the financial statements in Item 8 of the Form 10-K. In the application of these policies, certain estimates are made that may have a material impact on Georgia Power's results of operations and related disclosures. Different assumptions and measurements could produce estimates that are significantly different from those recorded in the financial statements. See MANAGEMENT'S DISCUSSION AND ANALYSIS – ACCOUNTING POLICIES – "Application of Critical Accounting Policies and Estimates" of Georgia Power in Item 7 of the Form 10-K for a complete discussion of Georgia Power's critical accounting policies and estimates.

Recently Issued Accounting Standards

See Note (A) to the Condensed Financial Statements herein for information regarding Georgia Power's recently adopted accounting standards.

FINANCIAL CONDITION AND LIQUIDITY

Overview

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Overview" of Georgia Power in Item 7 of the Form 10-K for additional information. Georgia Power's financial condition remained stable at March 31, 2019. Georgia Power intends to continue to monitor its access to short-term and long-term capital markets as well as bank credit agreements to meet future capital and liquidity needs. See "Capital Requirements and Contractual Obligations," "Sources of Capital," and "Financing Activities" herein for additional information.

Net cash provided from operating activities totaled $212 million for the first three months of 2019 compared to $373 million for the corresponding period in 2018. The decrease was primarily due to the timing of fossil fuel stock purchases and higher payments for property taxes and municipal franchise fees. Net cash used for investing activities totaled $980 million for the first three months of 2019 primarily related to installation of equipment to comply with environmental standards and construction of generation, transmission, and distribution facilities, including approximately $360 million related to the construction of Plant Vogtle Units 3 and 4. Net cash provided from financing activities totaled $665 million for the first three months of 2019 primarily due to borrowings from the FFB for construction of Plant Vogtle Units 3 and 4 and the reoffering of pollution control revenue bonds, partially offset by payment of common stock dividends and the redemption of pollution control revenue bonds. Cash flows from financing activities vary from period to period based on capital needs and the maturity or redemption of securities.

Significant balance sheet changes for the first three months of 2019 include recording $1.5 billion in operating lease right-of-use assets, net of amortization and $1.5 billion in operating lease obligations related to the adoption of ASC 842, an increase of $1.1 billion in long-term debt (including securities due within one year) primarily due to borrowings from the FFB for construction of Plant Vogtle Units 3 and 4 and the reoffering of pollution control revenue bonds previously purchased and held by Georgia Power, and an increase of $0.7 billion in property, plant, and equipment to comply with environmental standards and the construction of generation, transmission, and distribution facilities. See Note (L) to the Condensed Financial Statements herein for additional information on the adoption of ASC 842. Also see Notes (B) and (F) to the Condensed Financial Statements under "Georgia Power – Nuclear Construction" and "DOE Loan Guarantee Borrowings," respectively, herein for additional information regarding Plant Vogtle Units 3 and 4 and the related Amended and Restated Loan Guarantee Agreement.

Capital Requirements and Contractual Obligations

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" of Georgia Power in Item 7 of the Form 10-K for a description

of Georgia Power's capital requirements and contractual obligations. Approximately $973 million will be required through March 31, 2020 to fund maturities of long-term debt. See "Sources of Capital" herein for additional information. Also see FUTURE EARNINGS POTENTIAL – "Retail Regulatory Matters – Nuclear Construction" for additional information regarding Plant Vogtle Units 3 and 4.

The construction program is subject to periodic review and revision, and actual construction costs may vary from these estimates because of numerous factors. These factors include: changes in business conditions; changes in load projections; changes in environmental laws and regulations; the outcome of any legal challenges to environmental rules; changes in generating plants, including unit retirements and replacements and adding or changing fuel sources at existing generating units, to meet regulatory requirements; changes in FERC rules and regulations; Georgia PSC approvals; changes in the expected environmental compliance program; changes in legislation; the cost and efficiency of construction labor, equipment, and materials; project scope and design changes; storm impacts; and the cost of capital. In addition, there can be no assurance that costs related to capital expenditures will be fully recovered. The construction program also includes Plant Vogtle Units 3 and 4, which includes components based on new technology that only recently began initial operation in the global nuclear industry at this scale and which may be subject to additional revised cost estimates during construction. The ability to control costs and avoid cost and schedule overruns during the development, construction, and operation of new facilities is subject to a number of factors, including, but not limited to, changes in labor costs, availability, and productivity; challenges with management of contractors, subcontractors, or vendors; adverse weather conditions; shortages, increased costs, or inconsistent quality of equipment, materials, and labor; contractor or supplier delay; non-performance under construction, operating, or other agreements; operational readiness, including specialized operator training and required site safety programs; engineering or design problems; design and other licensing-based compliance matters, including the timely resolution of ITAAC and the related approvals by the NRC; challenges with start-up activities, including major equipment failure and system integration; and/or operational performance. See Note 2 to the financial statements under "Georgia Power – Nuclear Construction" in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements under "Georgia Power – Nuclear Construction" herein for information regarding additional factors that may impact construction expenditures.

Sources of Capital

Georgia Power 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, external security issuances, borrowings from financial institutions, equity contributions from Southern Company, and borrowings from the FFB. However, the amount, type, and timing of any future financings, if needed, will depend upon regulatory approvals, prevailing market conditions, and other factors. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Sources of Capital" of Georgia Power in Item 7 of the Form 10-K for additional information.

In 2014, Georgia Power entered into a loan guarantee agreement with the DOE and, in March 2019, entered into the Amended and Restated Loan Guarantee Agreement, under which the proceeds of borrowings may be used to reimburse Georgia Power for Eligible Project Costs incurred in connection with its construction of Plant Vogtle Units 3 and 4.

Under the Amended and Restated Loan Guarantee Agreement, the DOE has agreed to guarantee the obligations of Georgia Power under note purchase agreements among the DOE, Georgia Power, and the FFB and related promissory notes which provide for two multi-advance term loan facilities (FFB Credit Facilities). Under the FFB Credit Facilities, Georgia Power may make term loan borrowings through the FFB in an amount up to approximately $5.130 billion, provided that total aggregate borrowings under the FFB Credit Facilities may not exceed 70% of (i) Eligible Project Costs minus (ii) approximately $1.492 billion (reflecting the amounts received by Georgia Power under the Guarantee Settlement Agreement less the Customer Refunds). At March 31, 2019, Georgia Power had borrowed $3.46

billion under the FFB Credit Facilities.

See Note (F) to the Condensed Financial Statements under "DOE Loan Guarantee Borrowings" herein for additional information regarding the Amended and Restated Loan Guarantee Agreement, including applicable covenants, events of default, mandatory prepayment events, and additional conditions to borrowing. Also see Note (B) to the Condensed Financial Statements under "Georgia Power – Nuclear Construction" herein for additional information regarding Plant Vogtle Units 3 and 4.

Georgia Power's current liabilities frequently exceed current assets because of scheduled maturities of long-term debt and the periodic use of short-term debt as a funding source, as well as significant seasonal fluctuations in cash needs. At March 31, 2019, Georgia Power's current liabilities exceeded current assets by $1.4 billion primarily due to long-term debt that is due within one year of $973 million and notes payable of $275 million.

At March 31, 2019, Georgia Power had approximately $9 million of cash and cash equivalents. Georgia Power's committed credit arrangement with banks was $1.75 billion at March 31, 2019, of which $1.74 billion was unused. This credit arrangement expires in 2022.

This bank credit arrangement contains a covenant that limits debt levels and contains a cross-acceleration provision to other indebtedness (including guarantee obligations) of Georgia Power. Such cross-acceleration provision to other indebtedness would trigger an event of default if Georgia Power defaulted on indebtedness, the payment of which was then accelerated. At March 31, 2019, Georgia Power was in compliance with this covenant. This bank credit arrangement does not contain a material adverse change clause at the time of borrowing.

Subject to applicable market conditions, Georgia Power expects to renew or replace this credit arrangement as needed prior to expiration. In connection therewith, Georgia Power may extend the maturity date and/or increase or decrease the lending commitments thereunder.

See Note 8 to the financial statements under "Bank Credit Arrangements" in Item 8 of the Form 10-K and Note (F) to the Condensed Financial Statements under "Bank Credit Arrangements" herein for additional information.

A portion of the $1.74 billion unused credit with banks is allocated to provide liquidity support to Georgia Power's pollution control revenue bonds and commercial paper program. The amount of variable rate pollution control revenue bonds outstanding requiring liquidity support as of March 31, 2019 was approximately $550 million. In addition, at March 31, 2019, Georgia Power had $345 million of pollution control revenue bonds outstanding that were required to be remarketed within the next 12 months. Subsequent to March 31, 2019, Georgia Power purchased and held approximately $115 million of outstanding pollution control revenue bonds required to be remarketed.

Georgia Power may also meet short-term cash needs through a Southern Company subsidiary organized to issue and sell commercial paper at the request and for the benefit of Georgia Power and the other traditional electric operating companies. Proceeds from such issuances for the benefit of Georgia Power are loaned directly to Georgia Power. The obligations of each traditional electric operating company under these arrangements are several and there is no cross-affiliate credit support. Short-term borrowings are included in notes payable in the balance sheets.

Details of short-term borrowings were as follows:

	Short-term Debt at March 31, 2019		Short-term Debt During the Period(*)		
	Amount Outstanding	Weighted Average Interest Rate	Average Amount Outstanding	Weighted Average Interest Rate	Maximum Amount Outstanding
	(in millions)		(in millions)		(in millions)
Commercial paper	$275	2.8 %	$437	2.9 %	$ 935

(*) Average and maximum amounts are based upon daily balances during the three-month period ended March 31, 2019.

Georgia Power believes the need for working capital can be adequately met by utilizing the commercial paper program, lines of credit, short-term bank notes, and operating cash flows.

Credit Rating Risk

At March 31, 2019, Georgia Power did 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 purchases, fuel transportation and storage, energy price risk management, transmission, interest rate management, and construction of new generation at Plant Vogtle Units 3 and 4.

The maximum potential collateral requirements under these contracts at March 31, 2019 were as follows:

Credit Ratings	Maximum Potential Collateral Requirements
	(in millions)
At BBB- and/or Baa3	$ 92
Below BBB- and/or Baa3	$ 1,102

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

As a result of the Tax Reform Legislation, certain financial metrics, such as the funds from operations to debt percentage, used by the credit rating agencies to assess Southern Company and its subsidiaries, including Georgia Power, may be negatively impacted. A settlement agreement between Georgia Power and the staff of the Georgia PSC regarding the retail rate impact of the Tax Reform Legislation, as approved by the Georgia PSC on April 3, 2018, is expected to help mitigate these potential adverse impacts to certain credit metrics by allowing a higher retail equity ratio until the conclusion of Georgia Power's next base rate case, which is scheduled to be filed by July 1, 2019. See Note 2 to the financial statements under "Georgia Power – Rate Plans" in Item 8 of the Form 10-K for additional information.

Financing Activities

In January 2019, Georgia Power redeemed approximately $13 million, $20 million, and $75 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), First Series 1992, Eighth Series 1994, and Second Series 1995, respectively.

In March 2019, Georgia Power made additional borrowings under the FFB Credit Facilities in an aggregate principal amount of $835 million at an interest rate of 3.213% through the final maturity date of February 20, 2044. The proceeds were used to reimburse Georgia Power for Eligible Project Costs relating to the construction of Plant Vogtle Units 3 and 4.

Also in March 2019, Georgia Power reoffered to the public the following pollution control revenue bonds that previously had been purchased and held by Georgia Power:

- $173 million aggregate principal amount of Development Authority of Bartow County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Bowen Project), First Series 2009;
- approximately $105 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), First Series 2013; and
- $65 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Second Series 2008.

Table of Contents

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

Subsequent to March 31, 2019, Georgia Power purchased and held the following pollution control revenue bonds, which may be reoffered to the public at a later date:

- $55 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Fourth Series 1994;
- $30 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Fourth Series 1995;
- $20 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Ninth Series 1994; and
- $10 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Second Series 1994.

In addition to any financings that may be necessary to meet capital requirements and contractual obligations, Georgia Power 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.

Table of Contents

MISSISSIPPI POWER COMPANY

82

Table of Contents

MISSISSIPPI POWER COMPANY
CONDENSED STATEMENTS OF OPERATIONS (UNAUDITED)

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Operating Revenues:		
Retail revenues	$203	$194
Wholesale revenues, non-affiliates	57	68
Wholesale revenues, affiliates	22	34
Other revenues	5	6
Total operating revenues	287	302
Operating Expenses:		
Fuel	93	98
Purchased power	3	9
Other operations and maintenance	59	75
Depreciation and amortization	48	41
Taxes other than income taxes	26	28
Estimated loss on Kemper IGCC	2	44
Total operating expenses	231	295
Operating Income (Loss)	56	7
Other Income and (Expense):		
Interest expense, net of amounts capitalized	(17)	(19)
Other income (expense), net	5	1
Total other income and (expense)	(12)	(18)
Earnings (Loss) Before Income Taxes	44	(11)
Income taxes (benefit)	7	(4)
Net Income (Loss)	$37	$(7)

CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Net Income (Loss)	$37	$(7)
Other comprehensive income (loss):		
Qualifying hedges:		
Changes in fair value, net of tax of $- and $(1), respectively	—	(1)
Total other comprehensive income (loss)	—	(1)
Comprehensive Income (Loss)	$37	$(8)

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

83

Table of Contents

MISSISSIPPI POWER COMPANY
CONDENSED STATEMENTS OF CASH FLOWS (UNAUDITED)

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Operating Activities:		
Net income (loss)	$37	$(7)
Adjustments to reconcile net income (loss) to net cash used for operating activities —		
Depreciation and amortization, total	50	44
Deferred income taxes	(8)	155
Estimated loss on Kemper IGCC	6	37
Other, net	(10)	3
Changes in certain current assets and liabilities —		
-Receivables	11	(129)
-Other current assets	7	(12)
-Accounts payable	(38)	(21)
-Accrued taxes	(62)	(110)
-Accrued compensation	(22)	(22)
-Other current liabilities	6	—
Net cash used for operating activities	(23)	(62)
Investing Activities:		
Property additions	(45)	(33)
Construction payables	(8)	(2)
Other investing activities	(10)	(17)
Net cash used for investing activities	(63)	(52)
Financing Activities:		
Decrease in notes payable, net	—	(4)
Proceeds —		
Senior notes	—	600
Short-term borrowings	—	300
Pollution control revenue bonds	43	—
Redemptions — Other long-term debt	—	(900)
Return of capital	(38)	—
Other financing activities	—	(5)
Net cash provided from (used for) financing activities	5	(9)
Net Change in Cash, Cash Equivalents, and Restricted Cash	(81)	(123)
Cash, Cash Equivalents, and Restricted Cash at Beginning of Period	293	248
Cash, Cash Equivalents, and Restricted Cash at End of Period	$212	$125
Supplemental Cash Flow Information:		
Cash paid during the period for —		
Interest (net of $- and $- capitalized for 2019 and 2018, respectively)	$13	$21
Income taxes, net	—	19
Noncash transactions — Accrued property additions at end of period	27	30

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

Table of Contents

MISSISSIPPI POWER COMPANY
CONDENSED BALANCE SHEETS (UNAUDITED)

Assets	At March 31, 2019	At December 31, 2018
	(in millions)	
Current Assets:		
Cash and cash equivalents	$212	$ 293
Receivables —		
Customer accounts receivable	29	34
Unbilled revenues	37	41
Affiliated	16	21
Other accounts and notes receivable	36	31
Fossil fuel stock	23	20
Materials and supplies	52	53
Other regulatory assets	102	116
Other current assets	6	19
Total current assets	513	628
Property, Plant, and Equipment:		
In service	4,821	4,900
Less: Accumulated provision for depreciation	1,467	1,429
Plant in service, net of depreciation	3,354	3,471
Construction work in progress	110	103
Total property, plant, and equipment	3,464	3,574
Other Property and Investments	123	24
Deferred Charges and Other Assets:		
Deferred charges related to income taxes	33	33
Other regulatory assets, deferred	487	474
Accumulated deferred income taxes	148	150
Other deferred charges and assets	17	3
Total deferred charges and other assets	685	660
Total Assets	$4,785	$ 4,886

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

Table of Contents

MISSISSIPPI POWER COMPANY
CONDENSED BALANCE SHEETS (UNAUDITED)

Liabilities and Stockholder's Equity	At March 31, 2019	At December 31, 2018
	(in millions)	
Current Liabilities:		
Securities due within one year	$339	$ 40
Accounts payable —		
Affiliated	52	60
Other	50	90
Accrued taxes	33	95
Accrued interest	20	15
Accrued compensation	16	38
Accrued plant closure costs	26	29
Asset retirement obligations	28	34
Over recovered regulatory clause liabilities	14	14
Other current liabilities	55	40
Total current liabilities	633	455
Long-term Debt	1,280	1,539
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	373	378
Deferred credits related to income taxes	367	382
Employee benefit obligations	111	115
Asset retirement obligations, deferred	127	126
Other cost of removal obligations	186	185
Other regulatory liabilities, deferred	80	81
Other deferred credits and liabilities	18	16
Total deferred credits and other liabilities	1,262	1,283
Total Liabilities	3,175	3,277
Common Stockholder's Equity (See accompanying statements)	1,610	1,609
Total Liabilities and Stockholder's Equity	$4,785	$ 4,886

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

Table of Contents

MISSISSIPPI POWER COMPANY
CONDENSED STATEMENTS OF COMMON STOCKHOLDER'S EQUITY (UNAUDITED)

	Number of Common Shares Issued	Common Stock	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	(in millions)					
Balance at December 31, 2017	1	$ 38	$4,529	$(3,205)	$ (4)	$1,358
Net loss after dividends on preferred stock	—	—	—	(7)	—	(7)
Capital contributions from parent company	—	—	2	—	—	2
Other comprehensive income (loss)	—	—	—	—	(1)	(1)
Other	—	—	—	(1)	—	(1)
Balance at March 31, 2018	1	$ 38	$4,531	$(3,213)	$ (5)	$1,351
Balance at December 31, 2018	1	$ 38	$4,546	$(2,971)	$ (4)	$1,609
Net income	—	—	—	37	—	37
Return of capital to parent company	—	—	(38)	—	—	(38)
Capital contributions from parent company	—	—	2	—	—	2
Balance at March 31, 2019	1	$ 38	$4,510	$(2,934)	$ (4)	$1,610

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

87

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

FIRST QUARTER 2019 vs. FIRST QUARTER 2018

OVERVIEW

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

Many factors affect the opportunities, challenges, and risks of Mississippi Power's business of providing electric service. These factors include Mississippi Power's ability to maintain and grow energy sales and number of customers and to operate in a constructive regulatory environment that provides timely recovery of prudently-incurred costs. These costs include those related to projected long-term demand growth, stringent environmental standards, including CCR rules, reliability, fuel, capital and operations and maintenance expenditures, including expanding and improving transmission and distribution facilities, and restoration following major storms. Appropriately balancing required costs and capital expenditures with customer prices will continue to challenge Mississippi Power for the foreseeable future. Mississippi Power is scheduled to file a base rate case in the fourth quarter 2019 (Mississippi Power 2019 Base Rate Case).

On March 28, 2019, Mississippi Power filed a request with the FERC for a decrease in wholesale base revenues under the MRA tariff as agreed upon in a settlement agreement reached with its wholesale customers resolving all matters related to the Kemper County energy facility similar to the retail rate settlement agreement approved by the Mississippi PSC in February 2018 and reflecting the impacts of the Tax Reform Legislation. The MRA settlement agreement provides that base rates will decrease $3.7 million annually, effective January 1, 2019. Mississippi Power expects the matter to be resolved in the second quarter 2019. The ultimate outcome of this matter cannot be determined at this time. See Note 2 to the financial statements under "FERC Matters" in Item 8 of the Form 10-K for additional information.

Mississippi Power continues to focus on several key performance indicators. In recognition that Mississippi Power's long-term financial success is dependent upon how well it satisfies its customers' needs, Mississippi Power's retail base rate mechanism, PEP, includes performance indicators that directly tie customer service indicators to Mississippi Power's allowed ROE. Mississippi Power also focuses on broader measures of customer satisfaction, plant availability, system reliability, and net income.

RESULTS OF OPERATIONS

Net Income (Loss)

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$44	N/M

N/M - Not meaningful

Mississippi Power's net income for the first quarter 2019 was $37 million compared to a loss of $7 million for the corresponding period in 2018. The increase in net income is primarily attributable to lower charges associated with the Kemper IGCC and a decrease in operations and maintenance expenses.

Table of Contents
MISSISSIPPI POWER COMPANY
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Retail Revenues

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$9	4.6

In the first quarter 2019, retail revenues were $203 million compared to $194 million for the corresponding period in 2018.

Details of the changes in retail revenues were as follows:

	First Quarter 2019	
	(in millions)	(% change)
Retail – prior year	$194	
Estimated change resulting from –		
Rates and pricing	15	7.7 %
Sales growth	1	0.5
Weather	(9)	(4.6)
Fuel and other cost recovery	2	1.0
Retail – current year	$203	4.6 %

Revenues associated with changes in rates and pricing increased in the first quarter 2019 when compared to the corresponding period in 2018 primarily due to increases in PEP and ECO Plan rates that became effective for the first billing cycle of September 2018, partially offset by a rate decrease related to the Kemper County energy facility that became effective for the first billing cycle of April 2018 and a new tolling arrangement accounted for as a sales-type lease. See Note 2 to the financial statements under "Mississippi Power – Performance Evaluation Plan," " – Environmental Compliance Overview Plan," and " – Kemper County Energy Facility – Rate Recovery" in Item 8 of the Form 10-K and Note (L) to the Condensed Financial Statements herein for additional information.

Revenues attributable to changes in sales increased in the first quarter 2019 compared to the corresponding period in 2018. Weather-adjusted residential KWH sales increased 1.5% in the first quarter 2019 due to increased customer usage. Weather-adjusted commercial KWH sales decreased 3.4% due to decreased customer usage. Industrial KWH sales decreased 3.9% primarily due to decreased customer usage by several large industrial customers.

Revenues associated with weather decreased in the first quarter 2019 compared to the corresponding period in 2018 primarily due to milder weather.

Fuel and other cost recovery revenues increased in the first quarter 2019 when compared to the corresponding period in 2018 primarily as a result of higher recoverable fuel costs. Recoverable fuel costs include fuel and purchased power expenses reduced by the fuel portion of wholesale revenues from energy sold to customers outside Mississippi Power's service territory. Electric rates include provisions to adjust billings for fluctuations in fuel costs, including the energy component of purchased power costs. Under these provisions, fuel revenues generally equal fuel expenses, including the energy component of purchased power costs, and do not affect net income.

Wholesale Revenues – Non-Affiliates

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(11)	(16.2)

Wholesale revenues from sales to non-affiliates will vary depending on fuel prices, the market prices of wholesale energy compared to the cost of Mississippi Power's and the Southern Company system's generation, demand for energy within the Southern Company system's electric service territory, and the availability of the Southern

Company system's generation. Increases and decreases in energy revenues that are driven by fuel prices are accompanied by an increase or decrease in fuel costs and do not have a significant impact on net income. In addition, Mississippi Power provides service under long-term contracts with rural electric cooperative associations and municipalities located in southeastern Mississippi under cost-based electric tariffs which are subject to regulation by the FERC. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "FERC Matters" of Mississippi Power in Item 7 of the Form 10-K and FUTURE EARNINGS POTENTIAL – "FERC Matters" herein for additional information.

In the first quarter 2019, wholesale revenues from sales to non-affiliates were $57 million compared to $68 million for the corresponding period in 2018. This decrease primarily resulted from a $6 million decrease due to lower market-based contract capacity and energy sales and fewer opportunity sales and a $5 million decrease in cost-based electric tariff revenues due to decreased customer usage and milder weather.

Wholesale Revenues – Affiliates

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(12)	(35.3)

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

In the first quarter 2019, wholesale revenues from sales to affiliates were $22 million compared to $34 million for the corresponding period in 2018. This decrease was primarily due to a $19 million decrease associated with lower natural gas prices, partially offset by a $7 million increase associated with higher KWH sales due to the dispatch of Mississippi Power's lower cost generation resources to serve the Southern Company system's territorial load.

Fuel and Purchased Power Expenses

	First Quarter 2019 vs. First Quarter 2018	
	(change in millions)	(% change)
Fuel	$(5)	(5.1)
Purchased power	(6)	(66.7)
Total fuel and purchased power expenses	$(11)	

In the first quarter 2019, total fuel and purchased power expenses were $96 million compared to $107 million for the corresponding period in 2018. The decrease was due to lower average costs of natural gas and purchased power.

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

Table of Contents
MISSISSIPPI POWER COMPANY
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Details of Mississippi Power's generation and purchased power were as follows:

	First Quarter 2019	First Quarter 2018
Total generation (in millions of KWHs)	3,950	4,003
Total purchased power (in millions of KWHs)	207	194
Sources of generation (percent) –		
Coal	4	4
Gas	96	96
Cost of fuel, generated (in cents per net KWH) –		
Coal	4.42	3.62
Gas	2.46	2.60
Average cost of fuel, generated (in cents per net KWH)	2.53	2.65
Average cost of purchased power (in cents per net KWH)	1.62	4.74

Fuel

In the first quarter 2019, fuel expense was $93 million compared to $98 million for the corresponding period in 2018. The decrease was primarily due to a 5.6% decrease in the average cost of natural gas.

Purchased Power

In the first quarter 2019, purchased power expense was $3 million compared to $9 million for the corresponding period in 2018. The decrease was primarily due to a 66% decrease in the average cost per KWH purchased as a result of colder weather in the first quarter 2018 as compared to the corresponding period in 2019.

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

Other Operations and Maintenance Expenses

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(16)	(21.3)

In the first quarter 2019, other operations and maintenance expenses were $59 million compared to $75 million for the corresponding period in 2018. The decrease was primarily due to decreases of $9 million in generation planned outage expenses and $4 million in employee compensation and benefit expenses related to an employee attrition plan recorded in 2018.

Depreciation and Amortization

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$7	17.1

In the first quarter 2019, depreciation and amortization was $48 million compared to $41 million for the corresponding period in 2018. The increase was primarily related to $6 million of amortization associated with ECO

Plan regulatory assets. See Note 2 to the financial statements under "Mississippi Power – Environmental Compliance Overview Plan" in Item 8 of the Form 10-K for additional information.

Estimated Loss on Kemper IGCC

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(42)	(95.5)

In the first quarter 2019, estimated losses on the Kemper IGCC were $2 million compared to $44 million for the corresponding period in 2018, resulting from lower charges related to abandonment and closure activities for the mine and gasifier-related assets recorded in 2019 as compared to the corresponding period in 2018.
See Note 2 to the financial statements under "Mississippi Power – Kemper County Energy Facility" in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements under "Mississippi Power – Kemper County Energy Facility" herein for additional information.

Other Income (Expense), Net

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$4	N/M

N/M - Not meaningful

In the first quarter 2019, other income (expense), net was $5 million compared to $1 million for the corresponding period in 2018. The increase was primarily due to higher interest income associated with a new tolling arrangement accounted for as a lease. See Note (L) to the Condensed Financial Statements herein for additional information.

Income Taxes (Benefit)

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$11	275.0

In the first quarter 2019, income taxes were $7 million compared to an income tax benefit of $4 million for the corresponding period in 2018. This change was primarily due to higher pre-tax earnings primarily due to lower estimated losses on the Kemper IGCC, partially offset by an increase in the flowback of excess deferred income taxes as a result of a settlement agreement reached with wholesale customers under the MRA tariff. See Note (B) to the Condensed Financial Statements under "Mississippi Power" herein for additional information.

FUTURE EARNINGS POTENTIAL

The results of operations discussed above are not necessarily indicative of Mississippi Power's future earnings potential. The level of Mississippi Power's future earnings depends on numerous factors that affect the opportunities, challenges, and risks of Mississippi Power's business of providing electric service. These factors include Mississippi Power's ability to recover its prudently-incurred costs in a timely manner during a time of increasing costs and its ability to prevail against legal challenges associated with the Kemper County energy facility. Future earnings will be driven primarily by continued customer growth and the weak pace of growth in electricity use per customer, especially in residential and commercial markets. Earnings will also depend upon maintaining and growing sales, considering, among other things, the adoption and/or penetration rates of increasingly energy-efficient technologies and increasing volumes of electronic commerce transactions, both of which could contribute to a net reduction in customer usage. Earnings are subject to a variety of other factors. These factors include weather, competition, developing new and maintaining existing energy contracts and associated load requirements

with other utilities and other wholesale customers, energy conservation practiced by customers, the use of alternative energy sources by customers, the price of electricity, the price elasticity of demand, and the rate of economic growth or decline in Mississippi Power's service territory. Demand for electricity is primarily driven by the pace of economic growth that may be affected by changes in regional and global economic conditions, which may impact future earnings.

For additional information relating to these issues, see RISK FACTORS in Item 1A and MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL of Mississippi Power in Item 7 of the Form 10-K.

Environmental Matters

Mississippi Power's operations are regulated by state and federal environmental agencies through a variety of laws and regulations governing air, water, land, and protection of other natural resources. Mississippi Power maintains comprehensive environmental compliance and GHG strategies to assess upcoming requirements and compliance costs associated with these environmental laws and regulations. The costs, including capital expenditures, operations and maintenance costs, and costs reflected in ARO liabilities, required to comply with environmental laws and regulations and to achieve stated goals may impact future electric generating unit retirement and replacement decisions, results of operations, cash flows, and/or financial condition. Related costs may result from the installation of additional environmental controls, closure and monitoring of CCR facilities, unit retirements, or changing fuel sources for certain existing units, as well as related upgrades to Mississippi Power's transmission and distribution systems. A major portion of these costs is expected to be recovered through retail and wholesale rates. The ultimate impact of environmental laws and regulations and GHG goals will depend on various factors, such as state adoption and implementation of requirements, the availability and cost of any deployed technology, fuel prices, and the outcome of pending and/or future legal challenges.

New or revised environmental laws and regulations could affect many areas of Mississippi Power's operations. The impact of any such changes cannot be determined at this time. Environmental compliance costs could affect earnings if such costs cannot continue to be recovered in rates on a timely basis or through long-term wholesale agreements. Further, increased costs that are recovered through regulated rates could contribute to reduced demand for electricity, which could negatively affect results of operations, cash flows, and/or financial condition. Additionally, many commercial and industrial customers may also be affected by existing and future environmental requirements, which for some may have the potential to ultimately affect their demand for electricity. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Environmental Matters" of Mississippi Power in Item 7 and Note 3 to the financial statements under "Environmental Matters" in Item 8 of the Form 10-K for additional information.

FERC Matters

See Note 2 to the financial statements under "FERC Matters" in Item 8 of the Form 10-K for additional information.

Municipal and Rural Association Tariff

On March 28, 2019, Mississippi Power filed a request with the FERC for a decrease in wholesale base revenues under the MRA tariff as agreed upon in a settlement agreement reached with its wholesale customers resolving all matters related to the Kemper County energy facility similar to the retail rate settlement agreement approved by the Mississippi PSC in February 2018 and reflecting the impacts of the Tax Reform Legislation. The MRA settlement agreement provides that base rates will decrease $3.7 million annually, effective January 1, 2019. Mississippi Power expects the matter to be resolved in the second quarter 2019. The ultimate outcome of this matter cannot be determined at this time.

Open Access Transmission Tariff

On March 25, 2019, the Alabama Municipal Electric Authority and Cooperative Energy and SCS and the traditional electric operating companies (including Mississippi Power) filed a formal settlement agreement with the FERC

93

agreeing to a rate reduction based on a 10.6% ROE, with a retroactive effective date of May 10, 2018, and a five-year moratorium on these parties seeking changes to the OATT formula rate. The ultimate outcome of this matter cannot be determined at this time; however, if approved by the FERC as filed, the OATT settlement would not have a material impact on the financial statements of Mississippi Power.

Retail Regulatory Matters

Mississippi Power's rates and charges for service to retail customers are subject to the regulatory oversight of the Mississippi PSC. Mississippi Power's rates are a combination of base rates under PEP and several separate cost recovery clauses for specific categories of costs. These separate cost recovery clauses address such items as fuel and purchased power, energy efficiency programs, ad valorem taxes, property damage, and the costs of compliance with environmental laws and regulations. Costs not addressed through one of the specific cost recovery clauses are expected to be recovered through Mississippi Power's base rates. Mississippi Power is scheduled to file a base rate case in the fourth quarter 2019.

See Note 2 to the financial statements under "Mississippi Power" in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements under "Mississippi Power" herein for additional information.

Kemper County Energy Facility

See Note 2 to the financial statements under "Mississippi Power – Kemper County Energy Facility" in Item 8 of the Form 10-K for additional information.

As the mining permit holder, Liberty Fuels Company, LLC has a legal obligation to perform mine reclamation, and Mississippi Power has a contractual obligation to fund all reclamation activities. As a result of the abandonment of the Kemper IGCC, final mine reclamation began in 2018 and is expected to be substantially completed in 2020, with monitoring expected to continue through 2027. See Note 6 to the financial statements in Item 8 of the Form 10-K for additional information.

During the first quarter 2019, Mississippi Power recorded pre-tax charges to income of $2 million ($1 million after tax), primarily resulting from the abandonment and related closure activities and ongoing period costs, net of sales proceeds, for the mine and gasifier-related assets at the Kemper County energy facility. Additional closure costs for the mine and gasifier-related assets, currently estimated at up to $10 million pre-tax (excluding salvage, net of dismantlement costs), may be incurred through the first half of 2020. In addition, period costs, including, but not limited to, costs for compliance and safety, ARO accretion, and property taxes for the mine and gasifier-related assets, are estimated at $11 million for the remainder of 2019 and $2 million to $6 million annually in 2020 through 2023.

In addition, Mississippi Power constructed the CO_2 pipeline for the planned transport of captured CO_2 for use in enhanced oil recovery and is currently evaluating its options regarding the final disposition of the CO_2 pipeline, including removal of the pipeline. This evaluation is expected to be complete later in 2019. If Mississippi Power ultimately decides to remove the CO_2 pipeline, the cost of removal would have a material impact on Mississippi Power's financial statements.

In December 2018, Mississippi Power filed with the DOE its request for property closeout certification under the contract related to the $387 million of grants received. Mississippi Power and the DOE are currently in discussions regarding the requested closeout and property disposition, which may require payment to the DOE for a portion of certain property that is to be retained by Mississippi Power. In connection with the DOE closeout discussions, on April 29, 2019, the Civil Division of the Department of Justice informed Southern Company and Mississippi Power of an investigation related to the Kemper County energy facility. The ultimate outcome of these matters cannot be determined at this time; however, they could have a material impact on Mississippi Power's financial statements.

Other Matters

Mississippi Power is involved in various other matters that could affect future earnings, including matters being litigated and regulatory matters. In addition, Mississippi Power is subject to certain claims and legal actions arising

in the ordinary course of business. Mississippi Power's business activities are subject to extensive governmental regulation related to public health and the environment, such as laws and regulations governing air, water, land, and protection of other natural resources. Litigation over environmental issues and claims of various types, including property damage, personal injury, common law nuisance, and citizen enforcement of environmental laws and regulations, has occurred throughout the U.S. This litigation has included claims for damages alleged to have been caused by CO_2 and other emissions, CCR, and alleged exposure to hazardous materials, and/or requests for injunctive relief in connection with such matters.

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

In conjunction with Southern Company's sale of Gulf Power, Mississippi Power and Gulf Power have committed to seek a restructuring of their 50% undivided ownership interests in Plant Daniel such that each of them would, after the restructuring, own 100% of a generating unit. On January 15, 2019, Gulf Power provided notice to Mississippi Power that Gulf Power will retire its share of the generating capacity of Plant Daniel on January 15, 2024. Mississippi Power has the option to purchase Gulf Power's ownership interest for $1 on January 15, 2024, provided that Mississippi Power exercises the option no later than 120 days prior to that date. Mississippi Power is assessing the potential operational and economic effects of Gulf Power's notice. The ultimate outcome of these matters remains subject to completion of Mississippi Power's evaluations and applicable regulatory approvals, including by the FERC and the Mississippi PSC, and cannot be determined at this time. See Note (K) to the Condensed Financial Statements under "Southern Company" herein for information regarding the sale of Gulf Power.

Litigation

See Note 2 to the financial statements under "Mississippi Power – Kemper County Energy Facility" in Item 8 of the Form 10-K for additional information.

In May 2018, Southern Company and Mississippi Power received a notice of dispute and arbitration demand filed by Martin Product Sales, LLC (Martin) based on two agreements, both related to Kemper IGCC byproducts for which Mississippi Power provided termination notices in 2017. Martin alleges breach of contract, breach of good faith and fair dealing, fraud and misrepresentation, and civil conspiracy and makes a claim for damages in the amount of approximately $143 million, as well as additional unspecified damages, attorney's fees, costs, and interest. In the first quarter 2019, Mississippi Power and Southern Company filed motions to dismiss.

In November 2018, Ray C. Turnage and 10 other individual plaintiffs filed a putative class action complaint against Mississippi Power and the three current members of the Mississippi PSC in the U.S. District Court for the Southern District of Mississippi. Mississippi Power received Mississippi PSC approval in 2013 to charge a mirror CWIP rate premised upon including in its rate base pre-construction and construction costs for the Kemper IGCC prior to placing the Kemper IGCC into service. The Mississippi Supreme Court reversed that approval and ordered Mississippi Power to refund the amounts paid by customers under the previously-approved mirror CWIP rate. The plaintiffs allege that the initial approval process, and the amount approved, were improper. They also allege that Mississippi Power underpaid customers in the refund process by applying an incorrect interest rate. The plaintiffs seek to recover, on behalf of themselves and their putative class, actual damages, punitive damages, pre-judgment interest, post-judgment interest, attorney's fees, and costs. In response to Mississippi Power and the Mississippi PSC each filing a motion to dismiss, the plaintiffs filed an amended complaint on March 14, 2019. The amended complaint included four additional plaintiffs and additional claims for gross negligence, reckless conduct, and intentional wrongdoing. Mississippi Power and the Mississippi PSC have each filed a motion to dismiss the amended complaint.

Mississippi Power believes these legal challenges have no merit; however, an adverse outcome in either of these proceedings could have a material impact on Mississippi Power's results of operations, financial condition, and liquidity. The ultimate outcome of these matters cannot be determined at this time.

ACCOUNTING POLICIES

Application of Critical Accounting Policies and Estimates

Mississippi Power prepares its financial statements in accordance with GAAP. Significant accounting policies are described in Notes 1, 5, and 6 to the financial statements in Item 8 of the Form 10-K. In the application of these policies, certain estimates are made that may have a material impact on Mississippi Power's results of operations and related disclosures. Different assumptions and measurements could produce estimates that are significantly different from those recorded in the financial statements. See MANAGEMENT'S DISCUSSION AND ANALYSIS – ACCOUNTING POLICIES – "Application of Critical Accounting Policies and Estimates" of Mississippi Power in Item 7 of the Form 10-K for a complete discussion of Mississippi Power's critical accounting policies and estimates.

Recently Issued Accounting Standards

See Note (A) to the Condensed Financial Statements herein for information regarding Mississippi Power's recently adopted accounting standards.

FINANCIAL CONDITION AND LIQUIDITY

Overview

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Overview" of Mississippi Power in Item 7 of the Form 10-K for additional information.

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

Net cash used for operating activities totaled $23 million for the first three months of 2019, a decrease of $39 million as compared to the corresponding period in 2018. The decrease in net cash used for operating activities is primarily related to lower income tax and ad valorem tax payments in 2019. Net cash used for investing activities totaled $63 million for the first three months of 2019 primarily due to gross property additions related to distribution and transmission facilities. Net cash provided from financing activities totaled $5 million for the first three months of 2019 primarily due to $43 million of pollution control revenue bonds reoffered to the public, partially offset by a return of capital to Southern Company. Cash flows from financing activities vary from period to period based on capital needs and the maturity or redemption of securities.

Significant balance sheet changes for the first three months of 2019 include a decrease of $259 million in long-term debt, primarily due to the reclassification of $300 million in unsecured senior notes to securities due within one year, partially offset by $43 million in securities reoffered to the public; a decrease of $62 million in accrued taxes primarily due to the payment of ad valorem taxes; and a decrease of $81 million in cash and cash equivalents. Other significant changes include a decrease of $79 million in plant in service and an increase of $99 million in other property and investments primarily due to a new tolling arrangement, effective January 1, 2019, accounted for as a sales-type lease. See Note (L) to the Condensed Financial Statements herein for additional information.

Capital Requirements and Contractual Obligations

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" of Mississippi Power in Item 7 of the Form 10-K for a description of Mississippi Power's capital requirements and contractual obligations. Approximately $300 million will be required through March 31, 2020 to fund maturities of long-term debt. See "Sources of Capital" herein for additional information.

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

Sources of Capital

Mississippi Power plans to obtain the funds to meet its future capital needs from operating cash flows, external securities issuances, borrowings from financial institutions, including commercial paper to the extent Mississippi Power is eligible to participate, and equity contributions from Southern Company. However, the amount, type, and timing of any future financing, if needed, will depend upon prevailing market conditions, regulatory approval, and other factors. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" in Item 7 of the Form 10-K for additional information.

As of March 31, 2019, Mississippi Power's current liabilities exceeded current assets by approximately $120 million primarily as a result of $339 million of long-term debt that is due within one year.

At March 31, 2019, Mississippi Power had approximately $212 million of cash and cash equivalents. Mississippi Power's committed credit arrangements with banks totaled $100 million at March 31, 2019, all of which was unused. These credit arrangements expire in 2019.

See Note 8 to the financial statements under "Bank Credit Arrangements" in Item 8 of the Form 10-K and Note (F) to the Condensed Financial Statements under "Bank Credit Arrangements" herein for additional information.

All of these bank credit arrangements contain covenants that limit debt levels and typically contain cross-acceleration provisions to other indebtedness (including guarantee obligations) of Mississippi Power. Such cross-acceleration provisions to other indebtedness would trigger an event of default if Mississippi Power defaulted on indebtedness, the payment of which was then accelerated. At March 31, 2019, Mississippi Power was in compliance with all such covenants. None of the bank credit arrangements contain material adverse change clauses at the time of borrowing.

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

A portion of the $100 million unused credit arrangements with banks is allocated to provide liquidity support to Mississippi Power's variable rate revenue bonds. The amount of variable rate revenue bonds outstanding requiring liquidity support as of March 31, 2019 was approximately $40 million.

Short-term debt, including the average amount and maximum amount outstanding, was immaterial at March 31, 2019 and during the three-month period ended March 31, 2019.

Mississippi Power believes the need for working capital can be adequately met by utilizing lines of credit, short-term bank notes, commercial paper to the extent Mississippi Power is eligible to participate, operating cash flows, and other cash.

Credit Rating Risk

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Credit Rating Risk" of Mississippi Power in Item 7 of the Form 10-K for additional information.

At March 31, 2019, Mississippi Power did 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 have required or could require collateral, but not accelerated payment, in the event of a credit rating change to BBB and/or Baa2 or below. These contracts are for physical electricity purchases and sales, fuel transportation and storage, energy price risk management, and transmission. At March 31, 2019, the maximum potential collateral requirements at a rating below BBB- and/or Baa3 equaled approximately $281 million.

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

As a result of the Tax Reform Legislation, certain financial metrics, such as the funds from operations to debt percentage, used by the credit rating agencies to assess Southern Company and its subsidiaries, including Mississippi Power, may be negatively impacted. The settlement agreement approved by the Mississippi PSC in August 2018 with respect to the 2018 PEP filings and all unresolved PEP filings for prior years is expected to help mitigate these potential adverse impacts by allowing Mississippi Power to retain the excess deferred taxes resulting from the Tax Reform Legislation until the conclusion of the Mississippi Power 2019 Base Rate Case. See Note 2 to the financial statements under "Mississippi Power" in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements under "Mississippi Power" herein for additional information.

Financing Activities

In March 2019, Mississippi Power reoffered to the public $43 million of Mississippi Business Finance Corporation Pollution Control Revenue Refunding Bonds, Series 2002, that previously had been purchased and held by Mississippi Power.

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

Table of Contents

SOUTHERN POWER COMPANY
AND SUBSIDIARY COMPANIES

Table of Contents

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

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Operating Revenues:		
Wholesale revenues, non-affiliates	$352	$424
Wholesale revenues, affiliates	87	83
Other revenues	4	2
Total operating revenues	443	509
Operating Expenses:		
Fuel	145	169
Purchased power	24	61
Other operations and maintenance	84	93
Depreciation and amortization	119	114
Taxes other than income taxes	11	12
Total operating expenses	383	449
Operating Income	60	60
Other Income and (Expense):		
Interest expense, net of amounts capitalized	(44)	(47)
Other income (expense), net	2	3
Total other income and (expense)	(42)	(44)
Earnings Before Income Taxes	18	16
Income taxes (benefit)	(9)	(99)
Net Income	27	115
Net loss attributable to noncontrolling interests	(29)	(6)
Net Income Attributable to Southern Power	$56	$121

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Net Income	$27	$115
Other comprehensive income (loss):		
Qualifying hedges:		
Changes in fair value, net of tax of $(10) and $16, respectively	(29)	48
Reclassification adjustment for amounts included in net income, net of tax of $8 and $(8), respectively	25	(24)
Total other comprehensive income (loss)	(4)	24
Comprehensive Income	23	139
Comprehensive loss attributable to noncontrolling interests	(29)	(6)

Comprehensive Income Attributable to Southern Power	$52	$145

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

Table of Contents

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

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Operating Activities:		
Net income	$27	$115
Adjustments to reconcile net income to net cash provided from operating activities —		
Depreciation and amortization, total	125	122
Deferred income taxes	17	(50)
Amortization of investment tax credits	(14)	(14)
Other, net	(7)	2
Changes in certain current assets and liabilities —		
-Receivables	10	48
-Prepaid income taxes	(9)	(32)
-Other current assets	3	5
-Accounts payable	(32)	(43)
-Accrued compensation	(15)	(13)
-Other current liabilities	5	9
Net cash provided from operating activities	110	149
Investing Activities:		
Business acquisitions	(2)	(46)
Property additions	(66)	(121)
Change in construction payables	(7)	25
Payments pursuant to LTSAs	(15)	(18)
Other investing activities	11	7
Net cash used for investing activities	(79)	(153)
Financing Activities:		
Increase in notes payable, net	5	29
Distributions to noncontrolling interests	(36)	(13)
Capital contributions from noncontrolling interests	3	8
Payment of common stock dividends	(51)	(78)
Net cash used for financing activities	(79)	(54)
Net Change in Cash, Cash Equivalents, and Restricted Cash	(48)	(58)
Cash, Cash Equivalents, and Restricted Cash at Beginning of Period	181	140
Cash, Cash Equivalents, and Restricted Cash at End of Period	$133	$82
Supplemental Cash Flow Information:		
Cash paid (received) during the period for —		
Interest (net of $4 and $5 capitalized for 2019 and 2018, respectively)	$28	$29
Income taxes, net	1	(39)
Noncash transactions — Accrued property additions at end of period	19	57

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

101

Table of Contents

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

Assets	At March 31, 2019	At December 31, 2018
	(in millions)	
Current Assets:		
Cash and cash equivalents	$133	$ 181
Receivables —		
Customer accounts receivable	120	111
Affiliated	33	55
Other	116	116
Materials and supplies	218	220
Prepaid income taxes	1,190	25
Other current assets	37	37
Total current assets	1,847	745
Property, Plant, and Equipment:		
In service	13,284	13,271
Less: Accumulated provision for depreciation	2,288	2,171
Plant in service, net of depreciation	10,996	11,100
Construction work in progress	409	430
Total property, plant, and equipment	11,405	11,530
Other Property and Investments:		
Intangible assets, net of amortization of $67 and $61 at March 31, 2019 and December 31, 2018, respectively	340	345
Other investments	2	—
Total other property and investments	342	345
Deferred Charges and Other Assets:		
Operating lease right-of-use assets, net of amortization	372	—
Prepaid LTSAs	102	98
Accumulated deferred income taxes	17	1,186
Income taxes receivable, non-current	33	30
Assets held for sale	644	576
Other deferred charges and assets	342	373
Total deferred charges and other assets	1,510	2,263
Total Assets	$15,104	$ 14,883

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

Table of Contents

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

Liabilities and Stockholders' Equity	At March 31, 2019	At December 31, 2018
	(in millions)	
Current Liabilities:		
Securities due within one year	$599	$ 599
Notes payable	105	100
Accounts payable —		
Affiliated	69	92
Other	66	77
Accrued income taxes	11	6
Accrued interest	44	36
Liabilities held for sale	9	15
Other current liabilities	111	106
Total current liabilities	1,014	1,031
Long-term Debt	4,396	4,418
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	107	105
Accumulated deferred ITCs	1,817	1,832
Operating lease obligations	371	—
Other deferred credits and liabilities	181	213
Total deferred credits and other liabilities	2,476	2,150
Total Liabilities	7,886	7,599
Total Stockholders' Equity (See accompanying statements)	7,218	7,284
Total Liabilities and Stockholders' Equity	$15,104	$ 14,883

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

Table of Contents

SOUTHERN POWER COMPANY AND SUBSIDIARY COMPANIES
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (UNAUDITED)

	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Common Stockholders' Equity	Noncontrolling Interests	Total
	(in millions)					
Balance at December 31, 2017	$3,662	$1,478	$ (2)	$ 5,138	$ 1,360	$6,498
Net income attributable to Southern Power	—	121	—	121	—	121
Capital contributions from parent company	1	—	—	1	—	1
Other comprehensive income (loss)	—	—	24	24	—	24
Cash dividends on common stock	—	(78)	—	(78)	—	(78)
Capital contributions from noncontrolling interests	—	—	—	—	9	9
Distributions to noncontrolling interests	—	—	—	—	(13)	(13)
Net income (loss) attributable to noncontrolling interests	—	—	—	—	(6)	(6)
Other	—	(2)	5	3	(1)	2
Balance at March 31, 2018	$3,663	$1,519	$ 27	$ 5,209	$ 1,349	$6,558
Balance at December 31, 2018	$1,600	$1,352	$ 16	$ 2,968	$ 4,316	$7,284
Net income attributable to Southern Power	—	56	—	56	—	56
Capital contributions from parent company	1	—	—	1	—	1
Other comprehensive income (loss)	—	—	(4)	(4)	—	(4)
Cash dividends on common stock	—	(51)	—	(51)	—	(51)
Capital contributions from noncontrolling interests	—	—	—	—	3	3
Distributions to noncontrolling interests	—	—	—	—	(41)	(41)
Net income (loss) attributable to noncontrolling interests	—	—	—	—	(29)	(29)
Other	(1)	(1)	—	(2)	1	(1)
Balance at March 31, 2019	$1,600	$1,356	$ 12	$ 2,968	$ 4,250	$7,218

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

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

FIRST QUARTER 2019 vs. FIRST QUARTER 2018

OVERVIEW

Southern Power develops, constructs, acquires, owns, and manages power generation assets, including renewable energy projects, and sells electricity at market-based rates in the wholesale market. Southern Power continually seeks opportunities to execute its strategy to create value through various transactions including acquisitions, dispositions, and sales of partnership interests, development and construction of new generating facilities, and entry into PPAs primarily with investor-owned utilities, independent power producers, municipalities, electric cooperatives, and other load-serving entities, as well as commercial and industrial customers. In general, Southern Power commits to the construction or acquisition of new generating capacity only after entering into or assuming long-term PPAs for the new facilities.

During the three months ended March 31, 2019, Southern Power continued construction of the 100-MW Wildhorse Mountain wind facility, the 200-MW Reading wind facility, and the expansion of the 385-MW Mankato natural gas facility. See FUTURE EARNINGS POTENTIAL – "Construction Projects" herein for additional information.

In November 2018, Southern Power entered into an agreement to sell all of its equity interests in Plant Mankato (including the 385-MW expansion currently under construction) for an aggregate purchase price of approximately $650 million. The completion of the disposition is subject to the expansion unit reaching commercial operation as well as various other customary conditions to closing, including FERC and state commission approvals. On April 17, 2019, Southern Power entered into an agreement to sell all of its equity interests in the Nacogdoches biomass-fueled facility to Austin Energy for an aggregate purchase price of $460 million, subject to customary closing conditions and working capital adjustments. Each of these sales is expected to close in mid-2019; however, the ultimate outcome of these matters cannot be determined at this time.

At March 31, 2019, Southern Power's average investment coverage ratio for its generating assets (including Plants Mankato and Nacogdoches), based on the ratio of investment under contract to total investment using the respective generation facilities' net book value (or expected in-service value for facilities under construction) as the investment amount, was 93% through 2023 and 91% through 2028, with an average remaining contract duration of approximately 15 years.

Southern Power continues to focus on several key performance indicators, including, but not limited to, peak season equivalent forced outage rate, contract availability, and net income.

RESULTS OF OPERATIONS

Net Income Attributable to Southern Power

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(65)	(53.7)

Net income attributable to Southern Power for the first quarter 2019 was $56 million compared to $121 million for the corresponding period in 2018. The decrease was primarily due to $50 million in state income tax benefits recorded in 2018 arising from the reorganization of Southern Power's legal entities that own and operate certain solar facilities and a reduction in 2019 of $39 million in PTCs, partially offset by $28 million in HLBV income allocations to Southern Power related to tax equity partnerships entered into in 2018. See Notes 7 and 10 to the financial statements in Item 8 of the Form 10-K for additional information on the legal entity reorganization and the tax equity partnerships, respectively.

105

Table of Contents
SOUTHERN POWER COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Operating Revenues

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(66)	(13.0)

Total operating revenues include PPA capacity revenues, which are derived primarily from long-term contracts involving natural gas and biomass generating facilities, and PPA energy revenues from Southern Power's generation facilities. To the extent Southern Power has capacity not contracted under a PPA, it may sell power into an accessible wholesale market, or, to the extent those generation assets are part of the FERC-approved IIC, it may sell power into the power pool.

Natural Gas and Biomass Capacity and Energy Revenue

Capacity revenues generally represent the greatest contribution to operating income and are designed to provide recovery of fixed costs plus a return on investment.

Energy is generally sold at variable cost or is indexed to published natural gas indices. Energy revenues will vary depending on the energy demand of Southern Power's customers and their generation capacity, as well as the market prices of wholesale energy compared to the cost of Southern Power's energy. Energy revenues also include fees for support services, fuel storage, and unit start charges. Increases and decreases in energy revenues under PPAs that are driven by fuel or purchased power prices are accompanied by an increase or decrease in fuel and purchased power costs and do not have a significant impact on net income.

Solar and Wind Energy Revenue

Southern Power's energy sales from solar and wind generating facilities are predominantly through long-term PPAs that do not have a capacity charge. Customers either purchase the energy output of a dedicated renewable facility through an energy charge or pay a fixed price related to the energy generated from the respective facility and sold to the grid. As a result, Southern Power's ability to recover fixed and variable operations and maintenance expenses is dependent upon the level of energy generated from these facilities, which can be impacted by weather conditions, equipment performance, transmission constraints, and other factors.

See FUTURE EARNINGS POTENTIAL – "Power Sales Agreements" herein for additional information regarding Southern Power's PPAs.

Details of Southern Power's operating revenues were as follows:

	First Quarter 2019	First Quarter 2018
	(in millions)	
PPA capacity revenues	$ 127	$ 138
PPA energy revenues	227	254
Total PPA revenues	354	392
Non-PPA revenues	85	115
Other revenues	4	2
Total operating revenues	$ 443	$ 509

Table of Contents
SOUTHERN POWER COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In the first quarter 2019, total operating revenues were $443 million, reflecting a $66 million, or 13%, decrease from the corresponding period in 2018. The decrease in operating revenues was primarily due to the following:

- PPA capacity revenues decreased $11 million, or 8%, primarily due to a decrease of $17 million attributable to the sale of Plant Oleander and Plant Stanton Unit A (together, the Florida Plants) in December 2018, partially offset by a $5 million increase in new PPA capacity revenues from existing natural gas facilities.
- PPA energy revenues decreased $27 million, or 11%, primarily due to a $22 million decrease in sales related to natural gas facilities, driven by a $51 million decrease in the average cost of fuel and purchased power, partially offset by a $29 million increase in the volume of KWHs sold due to increased customer load.
- Non-PPA revenues decreased $30 million, or 26%, due to a $21 million decrease in the volume of KWHs sold through short-term sales, primarily due to a reduction in uncovered natural gas capacity, and an $8 million decrease in the market price of energy.

Fuel and Purchased Power Expenses

Details of Southern Power's generation and purchased power were as follows:

	First Quarter 2019	First Quarter 2018
	(in billions of KWHs)	
Generation	10.1	9.8
Purchased power	0.7	0.9
Total generation and purchased power	10.8	10.7
Total generation and purchased power, excluding solar, wind, and tolling agreements	6.6	6.7

Southern Power's PPAs for natural gas and biomass generation generally provide that the purchasers are responsible for either procuring the fuel (tolling agreements) or reimbursing Southern Power for substantially all of the cost of fuel relating to the energy delivered under such PPAs. Consequently, changes in such fuel costs are generally accompanied by a corresponding change in related fuel revenues and do not have a significant impact on net income. Southern Power is responsible for the cost of fuel for generating units that are not covered under PPAs. Power from these generating units is sold into the wholesale market or into the power pool for capacity owned directly by Southern Power.

Purchased power expenses will vary depending on demand, availability, and the cost of generating resources throughout the Southern Company system and other contract resources. Load requirements are submitted to the power pool on an hourly basis and are fulfilled with the lowest cost alternative, whether that is generation owned by Southern Power, an affiliate company, or external parties. Such purchased power costs are generally recovered through PPA revenues.

Details of Southern Power's fuel and purchased power expenses were as follows:

	First Quarter 2019 vs. First Quarter 2018	
	(change in millions)	(% change)
Fuel	$ (24)	(14.2)
Purchased power	(37)	(60.7)
Total fuel and purchased power expenses	$ (61)	

In the first quarter 2019, total fuel and purchased power expenses decreased $61 million, or 27%, compared to the corresponding period in 2018. Fuel expense decreased $24 million primarily due to a decrease associated with the average cost of fuel per KWH generated. Purchased power expense decreased $37 million primarily due to a $24 million decrease associated with the average cost of purchased power and a $13 million decrease associated with the volume of KWHs purchased.

Other Operations and Maintenance Expenses

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(9)	(9.7)

In the first quarter 2019, other operations and maintenance expenses were $84 million compared to $93 million for the corresponding period in 2018. The decrease was primarily due to lower scheduled outage and maintenance expenses and the recovery of legal costs related to the Roserock settlement agreement. See Note (C) to the Condensed Financial Statements under "General Litigation Matters – Southern Power" herein for additional information.

Income Taxes (Benefit)

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$90	90.9

In the first quarter 2019, income tax benefit was $9 million compared to $99 million for the corresponding period in 2018. This change was primarily due to $50 million in tax benefits recorded in 2018 related to changes in state apportionment rates following the reorganization of Southern Power's legal entities that own and operate certain solar facilities and a $39 million reduction of tax benefits from wind PTCs primarily as a result of the sale of a noncontrolling tax equity interest in SP Wind. See Note (G) to the Condensed Financial Statements herein for additional information.

Net Loss Attributable to Noncontrolling Interests

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$23	N/M

In the first quarter 2019, net loss attributable to noncontrolling interests was $29 million compared to $6 million for the corresponding period in 2018. The increase was primarily related to tax equity partnerships entered into in 2018. See Note 7 to the financial statements in Item 8 of the Form 10-K under "Southern Power" for additional information.

FUTURE EARNINGS POTENTIAL

The results of operations discussed above are not necessarily indicative of Southern Power's future earnings potential. Future earnings potential will be impacted by the sales of noncontrolling renewable facility interests and the sale of the Florida Plants in 2018 and the pending dispositions of Plants Mankato and Nacogdoches in 2019. The level of Southern Power's future earnings depends on numerous factors that affect the opportunities, challenges, and risks of Southern Power's competitive wholesale business. These factors include: Southern Power's ability to achieve sales growth while containing costs; regulatory matters; creditworthiness of customers; total generating capacity available in Southern Power's market areas; the successful remarketing of capacity as current contracts expire; and Southern Power's ability to execute its growth strategy through the development or acquisition of renewable facilities and other energy projects.

In November 2018, Southern Power entered into an agreement with Northern States Power to sell all of its equity interests in Plant Mankato (including the 385-MW expansion currently under construction) for an aggregate purchase price of approximately $650 million. The completion of the disposition is subject to the expansion unit reaching commercial operation as well as various other customary conditions to closing, including working capital and timing adjustments. This transaction is subject to FERC and state commission approvals. On April 17, 2019, Southern Power entered into an agreement to sell all of its equity interests in the Nacogdoches biomass-fueled facility to Austin Energy for an aggregate purchase price of $460 million, subject to customary closing conditions and working capital adjustments. Each of these sales is expected to close in mid-2019; however, the ultimate outcome of these matters cannot be determined at this time.

Demand for electricity is primarily driven by the pace of economic growth that may be affected by changes in regional and global economic conditions, as well as renewable portfolio standards, which may impact future earnings. Other factors that could influence future earnings include weather, transmission constraints, cost of generation from units within the power pool, and operational limitations. For additional information relating to these factors, see RISK FACTORS in Item 1A and MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL of Southern Power in Item 7 of the Form 10-K.

Power Sales Agreements

See BUSINESS – "The Southern Company System – Southern Power" in Item 1 of the Form 10-K for additional information regarding Southern Power's PPAs. Generally, under the solar and wind generation PPAs, the purchasing party retains the right to keep or resell the renewable energy credits.

Environmental Matters

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Environmental Matters" of Southern Power in Item 7 of the Form 10-K for information on the development by federal and state environmental regulatory agencies of additional control strategies for emissions of air pollution from industrial sources, including electric generating facilities. Compliance with possible additional federal or state legislation or regulations related to global climate change, air quality, water quality, or other environmental and health concerns could also significantly affect Southern Power. While Southern Power's PPAs generally contain provisions that permit charging the counterparty with some of the new costs incurred as a result of changes in environmental laws and regulations, the full impact of any such legislative or regulatory changes cannot be determined at this time.

Construction Projects

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Acquisitions" and "Construction Projects" of Southern Power in Item 7 of the Form 10-K and FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" herein for additional information.

Construction Projects in Progress

During the three months ended March 31, 2019, Southern Power continued construction of the projects set forth in the table below. Total aggregate construction costs, excluding the acquisition costs, are expected to be between $575 million and $640 million for the Plant Mankato expansion and the Wildhorse Mountain and Reading facilities. At March 31, 2019, total costs of construction incurred for these projects were $347 million and are included in CWIP, except for the Plant Mankato expansion, which is included in assets held for sale in the financial statements. The ultimate outcome of these matters cannot be determined at this time.

Project Facility	Resource	Approximate Nameplate Capacity (MW)	Location	Expected COD	PPA Counterparties	PPA Contract Period
Mankato expansion[(a)]	Natural Gas	385	Mankato, MN	May 2019	Northern States Power Company	20 years
Wildhorse Mountain[(b)]	Wind	100	Pushmataha County, OK	Fourth quarter 2019	Arkansas Electric Cooperative	20 years
Reading[(c)]	Wind	200	Osage and Lyon Counties, KS	Second quarter 2020	Royal Caribbean Cruises LTD	12 years

(a) In November 2018, Southern Power entered into an agreement to sell all of its equity interests in Plant Mankato, including this expansion currently under construction. This transaction is subject to FERC and state commission approvals and is expected to close mid-2019. The ultimate outcome of this matter cannot be determined at this time.

(b) In May 2018, Southern Power purchased 100% of the Wildhorse Mountain facility. Southern Power may enter into a tax equity partnership, in which case it would then own 100% of the class B membership interests. The ultimate outcome of this matter cannot be determined at this time.

(c) In August 2018, Southern Power purchased 100% of the membership interests of the Reading facility from the joint development arrangement with Renewable Energy Systems Americas, Inc. described below. Southern Power may enter into a tax equity partnership, in which case it would then own 100% of the class B membership interests. The ultimate outcome of this matter cannot be determined at this time.

Development Projects

Southern Power continues to evaluate and refine the deployment of the wind turbine equipment purchased in 2016 and 2017 to potential joint development and construction projects as well as the amount of MW capacity to be constructed. During the three months ended March 31, 2019, approximately $53 million of equipment was marketed for sale and, subsequent to March 31, 2019, was sold. At March 31, 2019, the equipment was classified as held for sale on Southern Power's balance sheet.

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

Other Matters

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Other Matters" and "Power Sales Agreements – General" of Southern Power in Item 7 for additional information.

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

The ultimate outcome of such pending or potential litigation, regulatory matters, or other business matters cannot be predicted at this time; however, for current proceedings not specifically reported in Notes (B) and (C) to the Condensed Financial Statements herein, management does not anticipate that the ultimate liabilities, if any, arising from such current proceedings would have a material effect on Southern Power's financial statements.

Southern Power indirectly owns a 51% membership interest in RE Roserock LLC (Roserock), the owner of the Roserock facility in Pecos County, Texas. Prior to the facility being placed in service in 2016, certain solar panels were damaged during installation by the construction contractor, McCarthy Building Companies, Inc. (McCarthy), and certain solar panels were damaged by a hail event that also occurred during construction. In connection therewith, Southern Power withheld payment of approximately $26 million to the construction contractor, which placed a lien on the Roserock facility for the same amount. In 2017, Roserock filed a lawsuit in the state district court in Pecos County, Texas against XL Insurance America, Inc. and North American Elite Insurance Company seeking recovery from an insurance policy for damages resulting from the hail event and McCarthy's installation practices. In June 2018, the court granted Roserock's motion for partial summary judgment, finding that the insurers were in breach of contract and in violation of the Texas Insurance Code for failing to pay any monies owed for the hail claim. Separate lawsuits were filed between Roserock and McCarthy, as well as other parties, and that litigation was consolidated in the U.S. District Court for the Western District of Texas. On April 18, 2019, Roserock and the parties to the state and federal lawsuits executed a settlement agreement and mutual release that resolves both lawsuits. Under the agreement, the lawsuits will be dismissed and McCarthy will release its lien following payments of all amounts (which are expected to occur in May 2019). Roserock will pay $26 million to McCarthy that was withheld and included in the original construction costs and will receive funds that will cover all related legal costs and the replacement costs of certain solar panels. In addition, during the first quarter 2019, Roserock received a partial payment of approximately $5 million in insurance proceeds toward the hail event. Any additional funds received in excess of the initial replacement costs are expected to be recognized as a gain when received by Roserock in the second quarter 2019, but are not expected to have a material impact on Southern Power's net income.

ACCOUNTING POLICIES

Application of Critical Accounting Policies and Estimates

Southern Power prepares its consolidated financial statements in accordance with GAAP. Significant accounting policies are described in Notes 1, 4, and 10 to the financial statements in Item 8 of the Form 10-K. In the application of these policies, certain estimates are made that may have a material impact on Southern Power's results of operations and related disclosures. Different assumptions and measurements could produce estimates that are significantly different from those recorded in the financial statements. See MANAGEMENT'S DISCUSSION AND ANALYSIS – ACCOUNTING POLICIES – "Application of Critical Accounting Policies and Estimates" of Southern Power in Item 7 of the Form 10-K for a complete discussion of Southern Power's critical accounting policies and estimates.

Recently Issued Accounting Standards

See Note (A) to the Condensed Financial Statements herein for information regarding Southern Power's recently adopted accounting standards.

FINANCIAL CONDITION AND LIQUIDITY

Overview

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Overview" of Southern Power in Item 7 of the Form 10-K for additional information. Southern Power's financial condition remained stable at March 31, 2019. Southern Power intends to continue to monitor its access to short-term and long-term capital markets as well as bank credit agreements as needed to meet future capital and liquidity needs. See "Sources of Capital" herein for additional information on lines of credit.

Southern Power also utilizes tax equity partnerships, where the tax partner takes significantly all of the federal tax benefits, as a financing source. These tax equity partnerships are consolidated in Southern Power's financial statements and are accounted for using a HLBV methodology to allocate partnership gains and losses. During the first three months of 2019, Southern Power did not receive any material tax equity funding amounts. See Note 1 to the financial statements under "Hypothetical Liquidation at Book Value" in Item 8 of the Form 10-K for additional information on the HLBV methodology.

Net cash provided from operating activities totaled $110 million for the first three months of 2019 compared to $149 million for the first three months of 2018. The decrease in net cash provided from operating activities was primarily due to a reduction in income tax refunds. Net cash used for investing activities totaled $79 million for the first three months of 2019 primarily due to ongoing construction activities. Net cash used for financing activities

totaled $79 million for the first three months of 2019 primarily due to payment of a common stock dividend and distributions to noncontrolling interests. Cash flows from financing activities may vary from period to period based on capital needs and the maturity or redemption of securities.

Significant balance sheet changes for the first three months of 2019 include a $1.2 billion increase in prepaid income taxes, with an offsetting $1.2 billion reduction in accumulated deferred income tax assets, due to the expected utilization of tax credits for the 2019 tax year, a $372 million increase in operating lease right-of-use assets along with a corresponding increase in operating lease obligations of $371 million, due to the adoption of ASU No. 2016-02, a $68 million increase in assets held for sale due to wind turbine equipment and the continued construction of the Plant Mankato expansion, and a $66 million decrease in noncontrolling interests primarily due to HLBV income allocations to Southern Power and distributions to partners. See Note (K) under "Southern Power" and Note (L) to the Condensed Financial Statements herein for additional information on the Plant Mankato disposition and ASU No. 2016-02, respectively.

See FUTURE EARNINGS POTENTIAL – "Construction Projects" herein for additional information.

Capital Requirements and Contractual Obligations

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" of Southern Power in Item 7 of the Form 10-K for a description of Southern Power's capital requirements and contractual obligations. Approximately $600 million will be required through March 31, 2020 to fund maturities of long-term debt. See "Sources of Capital" herein for additional information.

Southern Power's construction program includes estimates for potential plant acquisitions and placeholder growth, new construction and development, capital improvements, and work to be performed under LTSAs and is subject to periodic review and revision. Actual construction costs, including acquisitions, may vary from these estimates because of numerous factors such as: changes in business conditions; changes in the expected environmental compliance program; changes in environmental laws and regulations; the outcome of any legal challenges to environmental rules; changes in FERC rules and regulations; changes in load projections; changes in legislation; the cost and efficiency of construction labor, equipment, and materials; project scope and design changes; and the cost of capital. See FUTURE EARNINGS POTENTIAL – "Construction Projects" herein for additional information.

Sources of Capital

Southern Power plans to obtain the funds required for acquisitions, construction, development, debt maturities, and other purposes from operating cash flows, external securities issuances, borrowings from financial institutions, tax equity partnership contributions, divestitures, and equity contributions from Southern Company. However, the amount, type, and timing of any future financings, if needed, will depend upon prevailing market conditions, regulatory approval, and other factors. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Sources of Capital" of Southern Power in Item 7 of the Form 10-K for additional information.

Southern Power's current liabilities sometimes exceed current assets due to the use of short-term debt as a funding source and construction payables, as well as fluctuations in cash needs due to seasonality. Southern Power believes the need for working capital can be adequately met by utilizing the commercial paper program, the Facility (as defined below), borrowings from financial institutions, equity contributions from Southern Company, external securities issuances, and operating cash flows.

As of March 31, 2019, Southern Power had cash and cash equivalents of approximately $133 million.

Southern Power's commercial paper program is used to finance acquisition and construction costs related to electric generating facilities and for general corporate purposes, including maturing debt. Commercial paper is included in notes payable on the condensed consolidated balance sheets.

Table of Contents
SOUTHERN POWER COMPANY AND SUBSIDIARY COMPANIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Details of short-term borrowings were as follows:

	Short-term Borrowings at March 31, 2019		Short-term Borrowings During the Period (*)		
	Amount Outstanding	Weighted Average Interest Rate	Average Amount Outstanding	Weighted Average Interest Rate	Maximum Amount Outstanding
	(in millions)		(in millions)		(in millions)
Commercial paper	$ 5	2.8 %	$ 3	2.7 %	$ 45
Short-term loans	100	3.1 %	100	3.1 %	100
Total	$ 105	3.1 %	$ 103	3.1 %	

(*) Average and maximum amounts are based upon daily balances during the three-month period ended March 31, 2019.

At March 31, 2019, Southern Power had a committed credit facility (Facility) of $750 million, of which $9 million has been used for letters of credit and $741 million remains unused. The Facility expires in 2022. Proceeds from the Facility may be used for working capital and general corporate purposes as well as liquidity support for Southern Power's commercial paper program. Subject to applicable market conditions, Southern Power expects to renew or replace the Facility, as needed, prior to expiration. In connection therewith, Southern Power may extend the maturity date and/or increase or decrease the lending commitment thereunder. See Note 8 to the financial statements under "Bank Credit Arrangements" in Item 8 of the Form 10-K and Note (F) to the Condensed Financial Statements under "Bank Credit Arrangements" herein for additional information.

The Facility, as well as Southern Power's term loan agreements, contains a covenant that limits the ratio of debt to capitalization (as defined in the Facility) to a maximum of 65% and contains a cross-default provision that is restricted only to indebtedness of Southern Power. For purposes of this definition, debt excludes any project debt incurred by certain subsidiaries of Southern Power to the extent such debt is non-recourse to Southern Power, and capitalization excludes the capital stock or other equity attributable to such subsidiary. Southern Power is currently in compliance with all covenants in the Facility.

Southern Power also has a $120 million continuing letter of credit facility expiring in 2021 for standby letters of credit. At March 31, 2019, $96 million has been used for letters of credit, primarily as credit support for PPA requirements, and $24 million remains unused.

In addition, at March 31, 2019, Southern Power had $103 million of cash collateral posted related to PPA requirements.

Southern Power's subsidiaries do not borrow under the commercial paper program and are not parties to, and do not borrow under, the Facility or the continuing letter of credit facility.

Credit Rating Risk

Southern Power does not have any credit arrangements that would require material changes in payment schedules or terminations as a result of a credit rating downgrade.

There are certain contracts that could require collateral, but not accelerated payment, in the event of a credit rating change to BBB and/or Baa2, or below. These contracts are for physical electricity purchases and sales, fuel transportation and storage, energy price risk management, and transmission.

The maximum potential collateral requirements under these contracts at March 31, 2019 were as follows:

Credit Ratings	Maximum Potential Collateral Requirements	
	(in millions)	
At BBB and/or Baa2	$	29
At BBB- and/or Baa3	$	339
At BB+ and/or Ba1(*)	$	1,041

(*) Any additional credit rating downgrades at or below BB- and/or Ba3 could increase collateral requirements up to an additional $38 million.

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

In addition, Southern Power has a PPA that could require collateral, but not accelerated payment, in the event of a downgrade of Southern Power's credit. The PPA requires credit assurances without stating a specific credit rating. The amount of collateral required would depend upon actual losses resulting from a credit downgrade.

Financing Activities

Southern Power did not issue or redeem any securities during the three months ended March 31, 2019.

In addition to any financings that may be necessary to meet capital requirements and contractual obligations, Southern Power 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.

Table of Contents

SOUTHERN COMPANY GAS
AND SUBSIDIARY COMPANIES

Table of Contents

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

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Operating Revenues:		
Natural gas revenues (includes revenue taxes of $55 and $51, respectively)	$1,476	$1,631
Alternative revenue programs	(2)	(24)
Other revenues	—	32
Total operating revenues	1,474	1,639
Operating Expenses:		
Cost of natural gas	686	720
Cost of other sales	—	7
Other operations and maintenance	235	276
Depreciation and amortization	118	129
Taxes other than income taxes	82	77
Goodwill impairment	—	42
Total operating expenses	1,121	1,251
Operating Income	353	388
Other Income and (Expense):		
Earnings from equity method investments	48	42
Interest expense, net of amounts capitalized	(59)	(59)
Other income (expense), net	5	12
Total other income and (expense)	(6)	(5)
Earnings Before Income Taxes	347	383
Income taxes	77	104
Net Income	$270	$279

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Net Income	$270	$279
Other comprehensive income (loss):		
Qualifying hedges:		
Changes in fair value, net of tax of $- and $-, respectively	—	1
Reclassification adjustment for amounts included in net income, net of tax of $- and $1, respectively	—	2
Pension and other postretirement benefit plans:		
Reclassification adjustment for amounts included in net income, net of tax of $- and $-, respectively	(1)	(1)
Total other comprehensive income (loss)	(1)	2
Comprehensive Income	$269	$281

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

Table of Contents

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

	For the Three Months Ended March 31,	
	2019	2018
	(in millions)	
Operating Activities:		
Net income	$270	$279
Adjustments to reconcile net income to net cash provided from operating activities —		
Depreciation and amortization, total	118	129
Deferred income taxes	42	47
Mark-to-market adjustments	45	(59)
Goodwill impairment	—	42
Other, net	(20)	(2)
Changes in certain current assets and liabilities —		
-Receivables	238	175
-Natural gas for sale, net of temporary LIFO liquidation	363	413
-Other current assets	59	35
-Accounts payable	(353)	(119)
-Accrued taxes	21	28
-Accrued compensation	(50)	(38)
-Other current liabilities	(50)	48
Net cash provided from operating activities	683	978
Investing Activities:		
Property additions	(256)	(268)
Cost of removal, net of salvage	(12)	(14)
Change in construction payables, net	1	(46)
Investment in unconsolidated subsidiaries	(10)	(29)
Other investing activities	(13)	(4)
Net cash used for investing activities	(290)	(361)
Financing Activities:		
Decrease in notes payable, net	(289)	(483)
Payment of common stock dividends	(118)	(118)
Other financing activities	5	6
Net cash used for financing activities	(402)	(595)
Net Change in Cash, Cash Equivalents, and Restricted Cash	(9)	22
Cash, Cash Equivalents, and Restricted Cash at Beginning of Period	70	78
Cash, Cash Equivalents, and Restricted Cash at End of Period	$61	$100
Supplemental Cash Flow Information:		
Cash paid (received) during the period for —		
Interest (net of $2 and $1 capitalized for 2019 and 2018, respectively)	$55	$52
Income taxes, net	(1)	—
Noncash transactions — Accrued property additions at end of period	98	89

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

Table of Contents

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

Assets	At March 31, 2019	At December 31, 2018
	(in millions)	
Current Assets:		
Cash and cash equivalents	$57	$ 64
Receivables —		
Energy marketing receivables	529	801
Customer accounts receivable	472	370
Unbilled revenues	179	213
Affiliated	9	11
Other accounts and notes receivable	108	142
Accumulated provision for uncollectible accounts	(27)	(30)
Natural gas for sale	189	524
Prepaid expenses	99	118
Assets from risk management activities, net of collateral	108	219
Other regulatory assets	46	73
Other current assets	42	50
Total current assets	1,811	2,555
Property, Plant, and Equipment:		
In service	15,417	15,177
Less: Accumulated depreciation	4,466	4,400
Plant in service, net of depreciation	10,951	10,777
Construction work in progress	577	580
Total property, plant, and equipment	11,528	11,357
Other Property and Investments:		
Goodwill	5,015	5,015
Equity investments in unconsolidated subsidiaries	1,557	1,538
Other intangible assets, net of amortization of $153 and $145 at March 31, 2019 and December 31, 2018, respectively	93	101
Miscellaneous property and investments	20	20
Total other property and investments	6,685	6,674
Deferred Charges and Other Assets:		
Operating lease right-of-use assets, net of amortization	86	—
Other regulatory assets, deferred	657	669
Other deferred charges and assets	185	193
Total deferred charges and other assets	928	862
Total Assets	$20,952	$ 21,448

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

118

Table of Contents

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

Liabilities and Stockholder's Equity	At March 31, 2019	At December 31, 2018
	(in millions)	
Current Liabilities:		
Securities due within one year	$354	$ 357
Notes payable	361	650
Energy marketing trade payables	532	856
Accounts payable —		
Affiliated	31	45
Other	391	402
Customer deposits	91	133
Accrued taxes —		
Accrued income taxes	89	66
Other accrued taxes	72	75
Accrued interest	64	55
Accrued compensation	49	100
Liabilities from risk management activities, net of collateral	26	76
Other regulatory liabilities	86	79
Other current liabilities	160	130
Total current liabilities	2,306	3,024
Long-term Debt	5,574	5,583
Deferred Credits and Other Liabilities:		
Accumulated deferred income taxes	1,064	1,016
Deferred credits related to income taxes	926	940
Employee benefit obligations	351	357
Operating lease obligations	71	—
Other cost of removal obligations	1,598	1,585
Accrued environmental remediation	261	268
Other deferred credits and liabilities	63	105
Total deferred credits and other liabilities	4,334	4,271
Total Liabilities	12,214	12,878
Common Stockholder's Equity (See accompanying statements)	8,738	8,570
Total Liabilities and Stockholder's Equity	$20,952	$ 21,448

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

Table of Contents

SOUTHERN COMPANY GAS AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY (UNAUDITED)

	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	(in millions)			
Balance at December 31, 2017	$9,214	$ (212)	$ 20	$9,022
Net income	—	279	—	279
Capital contributions from parent company	14	—	—	14
Other comprehensive income (loss)	—	—	2	2
Cash dividends on common stock	—	(118)	—	(118)
Other	—	(4)	4	—
Balance at March 31, 2018	$9,228	$ (55)	$ 26	$9,199
Balance at December 31, 2018	$8,856	$ (312)	$ 26	$8,570
Net income	—	270	—	270
Capital contributions from parent company	17	—	—	17
Other comprehensive income (loss)	—	—	(1)	(1)
Cash dividends on common stock	—	(118)	—	(118)
Balance at March 31, 2019	$8,873	$ (160)	$ 25	$8,738

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

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

FIRST QUARTER 2019 vs. FIRST QUARTER 2018

OVERVIEW

Southern Company Gas is an energy services holding company whose primary business is the distribution of natural gas through utilities in four states – Nicor Gas in Illinois, Atlanta Gas Light in Georgia, Virginia Natural Gas in Virginia, and Chattanooga Gas in Tennessee. Southern Company Gas is also involved in several other complementary businesses.

Southern Company Gas manages its business through four reportable segments – gas distribution operations, gas pipeline investments, wholesale gas services, and gas marketing services – and one non-reportable segment, all other. See Note (M) to the Condensed Financial Statements herein and "BUSINESS – The Southern Company System – Southern Company Gas" in Item 1 of the Form 10-K for additional information.

Many factors affect the opportunities, challenges, and risks of Southern Company Gas' business. These factors include the ability to maintain safety, to maintain constructive regulatory environments, to maintain and grow natural gas sales and number of customers, and to effectively manage and secure timely recovery of costs. These costs include those related to projected long-term demand growth, environmental standards, safety, reliability, resilience, natural gas, and capital expenditures, including updating and expanding the natural gas distribution systems. The natural gas distribution utilities have various regulatory mechanisms that address cost recovery. Effectively operating pursuant to these regulatory mechanisms and appropriately balancing required costs and capital expenditures with customer prices will continue to challenge Southern Company Gas for the foreseeable future.

Nicor Gas filed a rate case in November 2018 and Atlanta Gas Light is required to file a rate case no later than June 3, 2019. These rate cases are both expected to conclude in 2019. The ultimate outcome of these matters cannot be determined at this time. See FUTURE EARNINGS POTENTIAL – "Regulatory Matters" herein and Note 2 to the financial statements under "Southern Company Gas – Rate Proceedings" in Item 8 of the Form 10-K for additional information.

During 2018, Southern Company Gas completed the following sales, resulting in approximately $2.7 billion in aggregate proceeds.

- On June 4, 2018, Southern Company Gas completed the stock sale of Pivotal Home Solutions to American Water Enterprises LLC.
- On July 1, 2018, a Southern Company Gas subsidiary, Pivotal Utility Holdings, completed the sales of the assets of two of its natural gas distribution utilities, Elizabethtown Gas and Elkton Gas, to South Jersey Industries, Inc.
- On July 29, 2018, Southern Company Gas and its wholly-owned direct subsidiary, NUI Corporation, completed the stock sale of Pivotal Utility Holdings, which primarily consisted of Florida City Gas, to NextEra Energy.

See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information on these dispositions.

Operating Metrics

Southern Company Gas continues to focus on several operating metrics, including Heating Degree Days, customer count, and volumes of natural gas sold.

Southern Company Gas measures weather and the effect on its business using Heating Degree Days. Generally, increased Heating Degree Days result in higher demand for natural gas on Southern Company Gas' distribution system. With the exception of Nicor Gas, Southern Company Gas has various regulatory mechanisms, such as weather normalization and straight-fixed-variable rate design, which limit its exposure to weather changes within typical ranges in each of its utilities' respective service territory. However, the operating revenues from utility customers in Illinois and gas marketing services customers primarily in Georgia and Illinois can be impacted by warmer- or colder-than-normal weather. Southern Company Gas utilizes weather hedges to limit the negative income impacts in the event of warmer-than-normal weather, while retaining a significant portion of the positive benefits of colder-than-normal weather for these businesses.

The number of customers served by gas distribution operations and gas marketing services can be impacted by natural gas prices, economic conditions, and competition from alternative fuels.

Southern Company Gas' natural gas volume metrics for gas distribution operations and gas marketing services illustrate the effects of weather and customer demand for natural gas. Wholesale gas services' physical sales volumes represent the daily average natural gas volumes sold to its customers.

See RESULTS OF OPERATIONS herein for additional information on these operating metrics.

Seasonality of Results

During the Heating Season, natural gas usage and operating revenues are generally higher as more customers are connected to the gas distribution systems and natural gas usage is higher in periods of colder weather. Occasionally in the summer, wholesale gas services' operating revenues are impacted due to peak usage by power generators in response to summer energy demands. Southern Company Gas' base operating expenses, excluding cost of natural gas, bad debt expense, and certain incentive compensation costs, are incurred relatively evenly throughout the year.

Seasonality also affects the comparison of certain balance sheet items across quarters, including receivables, unbilled revenues, natural gas for sale, and notes payable. However, these items are comparable when reviewing Southern Company Gas' annual results. Operating results for the interim periods presented are not necessarily indicative of annual results and can vary significantly from quarter to quarter.

RESULTS OF OPERATIONS

Net Income

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(9)	(3.2)

In the first quarter 2019, net income was $270 million compared to $279 million for the corresponding period in 2018. Excluding an $8 million net loss in the first quarter 2018 from the Southern Company Gas Dispositions, which includes the related goodwill impairment charge of $42 million recorded in contemplation of the sale of Pivotal Home Solutions, net income decreased $17 million. This decrease was driven by a $57 million decrease at wholesale gas services primarily due to significant natural gas price volatility during the first quarter 2018. Excluding the impacts of the Southern Company Gas Dispositions and wholesale gas services, net income increased $40 million. This increase was primarily due to a $52 million increase in revenues, net of gas costs and other cost recovery, primarily from infrastructure replacement programs and base rate changes as well as colder weather in Illinois in the first quarter 2019 compared to the corresponding period in 2018. Partially offsetting these increases were a $7 million contractor litigation settlement recorded in the first quarter 2018 and increased depreciation and amortization.

Table of Contents
SOUTHERN COMPANY GAS AND SUBSIDIARY COMPANIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Natural Gas Revenues, including Alternative Revenue Programs

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(133)	(8.3)

In the first quarter 2019, natural gas revenues, including alternative revenue programs, were $1.5 billion compared to $1.6 billion for the corresponding period in 2018.

Details of the changes in natural gas revenues, including alternative revenue programs, were as follows:

	First Quarter 2019	
	(in millions)	(% change)
Natural gas revenues – prior year	$1,607	
Estimated change resulting from –		
Infrastructure replacement programs and base rate changes	32	2.0
Gas costs and other cost recovery	62	3.9
Weather	7	0.4
Wholesale gas services	(80)	(5.0)
Southern Company Gas Dispositions	(167)	(10.4)
Other	13	0.8
Natural gas revenues – current year	$1,474	(8.3)%

Revenues from infrastructure replacement programs and base rate changes increased in the first quarter 2019 compared to the corresponding period in 2018 primarily due to a $22 million increase at Nicor Gas and a $9 million increase at Atlanta Gas Light. These amounts include gas distribution operations' continued investments recovered through infrastructure replacement programs and base rate increases as well as the effect of revenues deferred in 2018 as a result of the Tax Reform Legislation. See Note 2 to the financial statements under "Southern Company Gas – Rate Proceedings" in Item 8 of the Form 10-K for additional information.

Revenues associated with gas costs and other cost recovery increased in the first quarter 2019 compared to the corresponding period in 2018 primarily due to higher natural gas prices and increased volumes of natural gas sold for the remaining four natural gas distribution utilities in the first quarter 2019. Natural gas distribution rates include provisions to adjust billings for fluctuations in natural gas costs. Therefore, gas costs recovered through natural gas revenues generally equal the amount expensed in cost of natural gas and do not affect net income from gas distribution operations. See "Cost of Natural Gas" herein for additional information. Revenue impacts from weather and customer growth are described further below.

Revenues increased due to colder weather in Illinois in the first quarter 2019 compared to the corresponding period in 2018. See the weather discussion herein for additional information.

Revenues from wholesale gas services decreased in the first quarter 2019 compared to the corresponding period in 2018 primarily due to decreased commercial activity, partially offset by derivative gains. See "Segment Information – Wholesale Gas Services" herein for additional information.

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

During Heating Season, natural gas usage and operating revenues are generally higher. Weather typically does not have a significant net income impact other than during the Heating Season. The following table presents the Heating Degree Days information for Illinois and Georgia, the primary locations where Southern Company Gas' operations are impacted by weather.

	First Quarter			2019 vs. 2018	2019 vs. normal
	Normal(*)	2019	2018	colder (warmer)	colder (warmer)
Illinois	3,045	3,297	3,042	8.4 %	8.3 %
Georgia	1,441	1,213	1,364	(11.1)%	(15.8)%

(*) Normal represents the 10-year average from January 1, 2009 through March 31, 2018 for Illinois at Chicago Midway International Airport and for Georgia at Atlanta Hartsfield-Jackson International Airport, based on information obtained from the National Oceanic and Atmospheric Administration, National Climatic Data Center.

Southern Company Gas hedged its exposure to warmer-than-normal weather in Illinois for gas distribution operations and in Illinois and Georgia for gas marketing services. The remaining impacts of weather on earnings are reflected in the chart below.

	Gas Distribution Operations		Gas Marketing Services	
	First Quarter		First Quarter	
	2019	2018	2019	2018
	(in millions)		(in millions)	
Pre-tax	$ 2	$ (2)	$ —	$ (3)
After tax	2	(2)	—	(2)

The following table provides the number of customers served by Southern Company Gas at March 31, 2019 and 2018:

	March 31,		
	2019	2018	2019 vs. 2018
	(in thousands, except market share %)		(% change)
Gas distribution operations[a]	4,276	4,654	(8.1)%
Gas marketing services			
Energy customers[b]	701	779	(10.0)%
Market share of energy customers in Georgia	28.8 %	29.2 %	

(a) Includes total customers of approximately 407,000 at March 31, 2018 related to Elizabethtown Gas, Elkton Gas, and Florida City Gas, which were sold in July 2018. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

(b) Gas marketing services' customers are primarily located in Georgia and Illinois. Also included are customers in Ohio contracted through an annual auction process to serve for 12 months beginning April 1 of each year. At March 31, 2019 and 2018, there were approximately 70,000 and 140,000 contracted customers, respectively.

Southern Company Gas anticipates overall customer growth trends at the remaining four natural gas distribution utilities in gas distribution operations to continue as it expects continued improvement in the new housing market and low natural gas prices. Southern Company Gas uses a variety of targeted marketing programs to attract new customers and to retain existing customers.

Other Revenues

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(32)	(100.0)

Other revenues related to Pivotal Home Solutions, which was sold in June 2018. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas – Sale of Pivotal Home Solutions" for additional information.

Cost of Natural Gas

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(34)	(4.7)

Excluding Atlanta Gas Light, which does not sell natural gas to end-use customers, natural gas distribution rates include provisions to adjust billings for fluctuations in natural gas costs. Therefore, gas costs recovered through natural gas revenues generally equal the amount expensed in cost of natural gas and do not affect net income from gas distribution operations. Cost of natural gas at gas distribution operations represented 87% of total cost of natural gas in the first quarter 2019. See MANAGEMENT'S DISCUSSION AND ANALYSIS – RESULTS OF OPERATIONS – "Cost of Natural Gas" of Southern Company Gas in Item 7 of the Form 10-K and "Natural Gas Revenues, including Alternative Revenue Programs" herein for additional information.

In the first quarter 2019, cost of natural gas was $686 million compared to $720 million for the corresponding period in 2018. Excluding a $79 million decrease related to the Southern Company Gas Dispositions that resulted in a decrease in the volume of natural gas sold as a result of fewer gas distribution operations customers, cost of natural gas increased $45 million. This increase reflects a 4.9% increase in natural gas prices and an increase in the volume of natural gas sold in the first quarter 2019 primarily as a result of colder weather in Illinois compared to the corresponding period in 2018.

Table of Contents
SOUTHERN COMPANY GAS AND SUBSIDIARY COMPANIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following table details the volumes of natural gas sold during all periods presented.

	First Quarter 2019	2018	2019 vs. 2018
Gas distribution operations (mmBtu in millions)			
Firm	296	314	(5.7)%
Interruptible	25	25	— %
Total(*)	321	339	(5.3)%
Wholesale gas services (mmBtu in millions/day)			
Daily physical sales	7.0	6.8	2.9 %
Gas marketing services (mmBtu in millions)			
Firm:			
Georgia	15	16	(6.3)%
Illinois	6	6	— %
Other	8	10	(20.0)%
Interruptible large commercial and industrial	4	4	— %
Total	33	36	(8.3)%

(*) Includes total volumes of natural gas sold of 26 mmBtu for the three months ended March 31, 2018 related to Elizabethtown Gas, Elkton Gas, and Florida City Gas, which were sold in July 2018. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas – Sale of Elizabethtown Gas and Elkton Gas" and " – Sale of Florida City Gas" for additional information.

Cost of Other Sales

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(7)	(100.0)

Cost of other sales related to Pivotal Home Solutions, which was sold in June 2018. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas – Sale of Pivotal Home Solutions" for additional information.

Other Operations and Maintenance Expenses

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(41)	(14.9)

In the first quarter 2019, other operations and maintenance expenses were $235 million compared to $276 million for the corresponding period in 2018. Excluding a $29 million decrease related to the Southern Company Gas Dispositions, other operations and maintenance expenses decreased $12 million. This decrease was primarily due to a one-time adjustment in the first quarter 2018 for the adoption of a new paid time off policy. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Other Matters" of Southern Company Gas in Item 7 of the Form 10-K for additional information.

Depreciation and Amortization

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(11)	(8.5)

In the first quarter 2019, depreciation and amortization was $118 million compared to $129 million for the corresponding period in 2018. Excluding a $16 million decrease related to the Southern Company Gas Dispositions, depreciation and amortization increased $5 million. This increase was primarily due to continued infrastructure investments at gas distribution operations.

Taxes Other Than Income Taxes

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$5	6.5

In the first quarter 2019, taxes other than income taxes were $82 million compared to $77 million for the corresponding period in 2018. Excluding a $3 million decrease related to the Southern Company Gas Dispositions, taxes other than income taxes increased $8 million. This increase primarily reflects increases in Nicor Gas' invested capital tax and revenue tax expenses as a result of higher natural gas revenues at Nicor Gas, both of which are passed through directly to customers.

Goodwill Impairment

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(42)	N/M

N/M - Not meaningful

In the first quarter 2018, a goodwill impairment charge of $42 million was recorded in contemplation of the sale of Pivotal Home Solutions. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas – Sale of Pivotal Home Solutions" for additional information.

Earnings from Equity Method Investments

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$6	14.3

In the first quarter 2019, earnings from equity method investments were $48 million compared to $42 million for the corresponding period in 2018. This increase was primarily due to higher earnings from SNG as a result of rate increases implemented by SNG that became effective September 2018. See Note (E) to the Condensed Financial Statements under "Southern Company Gas" herein for additional information.

Other Income (Expense), Net

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(7)	(58.3)

In the first quarter 2019, other income (expense), net was $5 million compared to $12 million for the corresponding period in 2018. This decrease was primarily due to a contractor litigation settlement in the first quarter 2018. See

Note 2 to the financial statements under "Southern Company Gas – Infrastructure Replacement Programs and Capital Projects – Atlanta Gas Light – PRP" in Item 8 of the Form 10-K for additional information.

Income Taxes

First Quarter 2019 vs. First Quarter 2018	
(change in millions)	(% change)
$(27)	(26.0)%

In the first quarter 2019, income taxes were $77 million compared to $104 million for the corresponding period in 2018. Excluding a $13 million decrease related to the Southern Company Gas Dispositions, income taxes decreased $14 million. This decrease was primarily due to lower pre-tax earnings compared to the prior year and an increase in the flowback of excess deferred income taxes in 2019 primarily at Atlanta Gas Light as previously authorized by the Georgia PSC. See Note (G) to the Condensed Financial Statements herein under "Southern Company Gas" for additional information.

Performance and Non-GAAP Measures

Adjusted operating margin is a non-GAAP measure that is calculated as operating revenues less cost of natural gas, cost of other sales, and revenue tax expense. Adjusted operating margin excludes other operations and maintenance expenses, depreciation and amortization, taxes other than income taxes, and goodwill impairment, which are included in the calculation of operating income as calculated in accordance with GAAP and reflected in the statements of income. The presentation of adjusted operating margin is believed to provide useful information regarding the contribution resulting from base rate changes, infrastructure replacement programs and capital projects, and customer growth at gas distribution operations since the cost of natural gas and revenue tax expense can vary significantly and are generally billed directly to customers. Southern Company Gas further believes that utilizing adjusted operating margin at gas pipeline investments, wholesale gas services, and gas marketing services allows it to focus on a direct measure of performance before overhead costs. The applicable reconciliation of operating income to adjusted operating margin is provided herein.

Adjusted operating margin should not be considered an alternative to, or a more meaningful indicator of, Southern Company Gas' operating performance than operating income as determined in accordance with GAAP. In addition, Southern Company Gas' adjusted operating margin may not be comparable to similarly titled measures of other companies.

	First Quarter 2019	First Quarter 2018
	(in millions)	
Operating Income	$353	$ 388
Other operating expenses[(a)]	435	524
Revenue taxes[(b)]	(54)	(50)
Adjusted Operating Margin	$734	$ 862

(a) Includes other operations and maintenance expenses, depreciation and amortization, taxes other than income taxes, and goodwill impairment.

(b) Nicor Gas' revenue tax expenses, which are passed through directly to customers.

128

Segment Information

Adjusted operating margin, operating expenses, and net income for each segment are provided in the table below. See Note (M) to the Condensed Financial Statements under "Southern Company Gas" herein for additional information.

	First Quarter 2019			First Quarter 2018		
	Adjusted Operating Margin[(a)]	Operating Expenses[(a)]	Net Income (Loss)	Adjusted Operating Margin[(a)]	Operating Expenses[(a)(b)]	Net Income (Loss)[(b)]
	(in millions)			(in millions)		
Gas distribution operations	$524	$ 314	$ 133	$557	$ 323	$ 149
Gas pipeline investments	8	3	32	8	3	27
Wholesale gas services	84	19	47	163	22	104
Gas marketing services	115	31	61	128	95	13
All other	6	17	(3)	9	34	(14)
Intercompany eliminations	(3)	(3)	—	(3)	(3)	—
Consolidated	$734	$ 381	$ 270	$862	$ 474	$ 279

(a) Adjusted operating margin and operating expenses are adjusted for Nicor Gas' revenue tax expenses, which are passed through directly to customers.

(b) Operating expenses and net income for gas distribution operations and gas marketing services include the impacts of the Southern Company Gas Dispositions. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

Gas Distribution Operations

Gas distribution operations is the largest component of Southern Company Gas' business and is subject to regulation and oversight by agencies in each of the states it serves. These agencies approve natural gas rates designed to provide Southern Company Gas with the opportunity to generate revenues to recover the cost of natural gas delivered to its customers and its fixed and variable costs, including depreciation, interest, operations and maintenance, taxes, and overhead costs, and to earn a reasonable return on its investments.

With the exception of Atlanta Gas Light, Southern Company Gas' second largest utility that operates in a deregulated natural gas market and has a straight-fixed-variable rate design that minimizes the variability of its revenues based on consumption, the earnings of the natural gas distribution utilities can be affected by customer consumption patterns that are a function of weather conditions, price levels for natural gas, and general economic conditions that may impact customers' ability to pay for natural gas consumed. Southern Company Gas has various weather mechanisms, such as weather normalization mechanisms and weather derivative instruments, that limit its exposure to weather changes within typical ranges in its natural gas distribution utilities' service territories.

In July 2018, a Southern Company Gas subsidiary, Pivotal Utility Holdings, completed the sales of the assets of two of its natural gas distribution utilities, Elizabethtown Gas and Elkton Gas, to South Jersey Industries, Inc. In July 2018, Southern Company Gas and its wholly-owned direct subsidiary, NUI Corporation, completed the sale of Pivotal Utility Holdings, which primarily consisted of Florida City Gas, to NextEra Energy. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

First Quarter 2019 vs. First Quarter 2018

In the first quarter 2019, net income decreased $16 million, or 10.7%, compared to the corresponding period in 2018. This decrease primarily relates to a $33 million decrease in adjusted operating margin and a $7 million decrease in other income (expense), net, partially offset by a decrease of $16 million in income tax expense and a $9 million decrease in operating expenses.

Excluding an $89 million decrease attributable to the utilities sold during 2018, adjusted operating margin increased $56 million, which primarily reflects additional revenue from continued investments recovered through infrastructure replacement programs and base rate increases, the effect of revenues deferred in 2018 as a result of the Tax Reform Legislation, and colder weather in Illinois during the first quarter 2019 compared to the corresponding period in 2018. Excluding a $40 million decrease attributable to the utilities sold during 2018, operating expenses increased $31 million, which includes increased compensation and benefit costs, higher expenses passed through directly to customers, increased expenses for storage facilities, and additional depreciation primarily due to additional assets placed in service. The decrease in other income (expense), net is due to a contractor litigation settlement in the first quarter 2018. Excluding $6 million of interest expense attributable to the utilities sold during 2018, interest expense increased $7 million primarily from the issuance of first mortgage bonds at Nicor Gas. Excluding a $12 million decrease attributable to the utilities sold in 2018, income tax expense decreased $4 million, primarily due to an increase in the flowback of excess deferred income taxes in 2019, partially offset by higher pre-tax earnings.

Gas Pipeline Investments

Gas pipeline investments consists primarily of joint ventures in natural gas pipeline investments including SNG, Atlantic Coast Pipeline, PennEast Pipeline, and a 50% joint ownership interest in the Dalton Pipeline. See Note (E) to the Condensed Financial Statements herein and Note 7 to the financial statements in Item 8 of the Form 10-K for additional information.

First Quarter 2019 vs. First Quarter 2018

In the first quarter 2019, net income increased $5 million, or 18.5%, compared to the corresponding period in 2018. This increase primarily relates to a $6 million increase in earnings from equity method investments largely due to higher earnings from SNG, partially offset by a $2 million increase in income tax expense due to higher pre-tax earnings.

Wholesale Gas Services

Wholesale gas services is involved in asset management and optimization, storage, transportation, producer and peaking services, natural gas supply, natural gas services, and wholesale gas marketing. Southern Company Gas has positioned the business to generate positive economic earnings on an annual basis even under low volatility market conditions that can result from a number of factors. When market price volatility increases, wholesale gas services is well positioned to capture significant value and generate stronger results. Operating expenses primarily reflect employee compensation and benefits.

First Quarter 2019 vs. First Quarter 2018

In the first quarter 2019, net income decreased $57 million, or 54.8%, compared to the corresponding period in 2018. This decrease primarily relates to a $79 million decrease in adjusted operating margin, partially offset by a decrease of $19 million in income tax expense and a $3 million decrease in operating expenses. Details of the decrease in adjusted operating margin are provided in the table below. The decrease in operating expenses primarily reflects lower compensation and benefit expense. The decrease in income tax expense was driven by lower pre-tax earnings.

Table of Contents

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

	First Quarter 2019	First Quarter 2018
	(in millions)	
Commercial activity recognized	$38	$ 172
Gain on storage derivatives	3	2
Gain (loss) on transportation and forward commodity derivatives	29	(16)
LOCOM adjustments, net of current period recoveries	(2)	(3)
Purchase accounting adjustments to fair value inventory and contracts	16	8
Adjusted operating margin	$84	$ 163

Change in Commercial Activity

The commercial activity at wholesale gas services includes recognition of storage and transportation values that were generated in prior periods, which reflect the impact of prior period hedge gains and losses as associated physical transactions occur. The positive commercial activity recognized in the first quarter 2019 was primarily due to natural gas price volatility that resulted from intermittent cold weather throughout the period. The decrease in commercial activity in the first quarter 2019 compared to the corresponding period in 2018 was primarily due to significant natural gas price volatility that resulted from prolonged cold weather during the first quarter 2018 coupled with low natural gas supply.

Change in Storage and Transportation Derivatives

Volatility in the natural gas market arises from a number of factors, such as weather fluctuations or changes in supply or demand for natural gas in different regions of the U.S. The volatility of natural gas commodity prices has a significant impact on Southern Company Gas' customer rates, long-term competitive position against other energy sources, and the ability of wholesale gas services to capture value from locational and seasonal spreads. Forward storage or time spreads applicable to the locations of wholesale gas services' specific storage positions in 2019 resulted in storage derivative gains. Transportation and forward commodity derivative gains in 2019 are primarily the result of narrowing transportation spreads due to supply constraints and increases in natural gas supply, which impacted forward prices at natural gas receipt and delivery points, primarily in the Northeast and Midwest regions.

Withdrawal Schedule and Physical Transportation Transactions

The expected natural gas withdrawals from storage and expected offset to prior hedge losses/gains associated with the transportation portfolio of wholesale gas services are presented in the following table, along with the net operating revenues expected at the time of withdrawal from storage and the physical flow of natural gas between contracted transportation receipt and delivery points. Wholesale gas services' expected net operating revenues exclude storage and transportation demand charges, as well as other variable fuel, withdrawal, receipt, and delivery charges, and exclude estimated profit sharing under asset management agreements. Further, the amounts that are realizable in future periods are based on the inventory withdrawal schedule, planned physical flow of natural gas between the transportation receipt and delivery points, and forward natural gas prices at March 31, 2019. A portion of wholesale gas services' storage inventory and transportation capacity is economically hedged with futures contracts, which results in the realization of substantially fixed net operating revenues.

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

	Storage withdrawal schedule		
	Total storage[(a)]	Expected net operating gains[(b)]	Physical transportation transactions – expected net operating losses[(c)]
	(in mmBtu in millions)	(in millions)	(in millions)
2019	7	$ 1	$ (6)
2020 and thereafter	1	1	(23)
Total at March 31, 2019	8	$ 2	$ (29)

(a) At March 31, 2019, the WACOG of wholesale gas services' expected natural gas withdrawals from storage was $2.24 per mmBtu.

(b) Represents expected operating gains from planned storage withdrawals associated with existing inventory positions and could change as wholesale gas services adjusts its daily injection and withdrawal plans in response to changes in future market conditions and forward NYMEX price fluctuations.

(c) Represents the transportation derivative gains and losses that will be settled during the period and the physical transportation transactions that offset the derivative gains and losses previously recognized.

The unrealized storage and transportation derivative gains do not change the underlying economic value of wholesale gas services' storage and transportation positions and will be reversed when the related transactions occur and are recognized. For more information on wholesale gas services' energy marketing and risk management activities, see MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Market Price Risk" of Southern Company Gas in Item 7 of the Form 10-K.

Gas Marketing Services

Gas marketing services provides energy-related products and services to natural gas markets and participants in customer choice programs that were approved in various states to increase competition. These programs allow customers to choose their natural gas supplier while the local distribution utility continues to provide distribution and transportation services. Gas marketing services is weather sensitive and uses a variety of hedging strategies, such as weather derivative instruments and other risk management tools, to partially mitigate potential weather impacts.

On June 4, 2018, Southern Company Gas completed the sale of Pivotal Home Solutions to American Water Enterprises LLC. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

First Quarter 2019 vs. First Quarter 2018

In the first quarter 2019, net income increased $48 million compared to the corresponding period in 2018. This increase primarily relates to a $64 million decrease in operating expenses, partially offset by a $13 million decrease in adjusted operating margin and a $3 million increase in income tax expense.

Excluding a $25 million decrease attributable to the 2018 disposition of Pivotal Home Solutions, adjusted operating margin increased $12 million, which primarily reflects favorable margins and recovery of prior period hedge losses.

Excluding a $61 million decrease attributable to the 2018 disposition of Pivotal Home Solutions that includes the related goodwill impairment charge, operating expense decreased $3 million.

All Other

All other includes Southern Company Gas' storage and fuels operations and its investment in Triton, AGL Services Company, and Southern Company Gas Capital, as well as various corporate operating expenses that are not allocated to the reportable segments and interest income (expense) associated with affiliate financing arrangements.

First Quarter 2019 vs. First Quarter 2018

In the first quarter 2019, net loss decreased $11 million compared to the corresponding period in 2018. This decrease primarily reflects an $17 million decrease in operating expenses, partially offset by a $3 million decrease in adjusted operating margin. The decrease in operating expenses primarily reflects a one-time adjustment in compensation expense in the first quarter 2018 for the adoption of a new paid time off policy and a decrease in depreciation and amortization. The decrease in adjusted operating margin primarily relates to a decrease in storage revenues.

Segment Reconciliations

Reconciliations of operating income to adjusted operating margin for the first quarter 2019 and 2018 are reflected in the following tables. See Note (M) to the Condensed Financial Statements herein for additional information.

	First Quarter 2019						
	Gas Distribution Operations	Gas Pipeline Investments	Wholesale Gas Services	Gas Marketing Services	All Other	Intercompany Elimination	Consolidated
	(in millions)						
Operating Income (Loss)	$210	$ 5	$ 65	$ 84	$(11)	$ —	$ 353
Other operating expenses[(a)]	368	3	19	31	17	(3)	435
Revenue tax expense[(b)]	(54)	—	—	—	—	—	(54)
Adjusted Operating Margin	$524	$ 8	$ 84	$ 115	$6	$ (3)	$ 734

	First Quarter 2018						
	Gas Distribution Operations	Gas Pipeline Investments	Wholesale Gas Services	Gas Marketing Services	All Other	Intercompany Elimination	Consolidated
	(in millions)						
Operating Income (Loss)	$234	$ 5	$ 141	$ 33	$(25)	$ —	$ 388
Other operating expenses[(a)]	373	3	22	95	34	(3)	524
Revenue tax expense[(b)]	(50)	—	—	—	—	—	(50)
Adjusted Operating Margin	$557	$ 8	$ 163	$ 128	$9	$ (3)	$ 862

(a) Includes other operations and maintenance expenses, depreciation and amortization, taxes other than income taxes, and goodwill impairment.

(b) Nicor Gas' revenue tax expenses, which are passed through directly to customers.

FUTURE EARNINGS POTENTIAL

The results of operations discussed above are not necessarily indicative of Southern Company Gas' future earnings potential. The Southern Company Gas Dispositions are expected to materially decrease future earnings and cash flows to Southern Company Gas. In the first quarter 2018, net income attributable to these dispositions, excluding the related goodwill impairment, was $34 million. The level of Southern Company Gas' future earnings depends on numerous factors that affect the opportunities, challenges, and risks of Southern Company Gas' primary business of natural gas distribution and its complementary businesses in the gas pipeline investments, wholesale gas services, and gas marketing services sectors. These factors include Southern Company Gas' ability to maintain constructive regulatory environments that allow for the timely recovery of prudently-incurred costs, the completion and subsequent operation of ongoing infrastructure and other construction projects, creditworthiness of customers, its ability to optimize its transportation and storage positions, and its ability to re-contract storage rates at favorable prices.

Future earnings will be driven by customer growth and are subject to a variety of other factors. These factors include weather, competition, new energy contracts with other utilities and other wholesale customers, energy conservation practiced by customers, the use of alternative energy sources by customers, the price of natural gas, the price elasticity of demand, and the rate of economic growth or decline in Southern Company Gas' service territories.

Demand for natural gas is primarily driven by the pace of economic growth that may be affected by changes in regional and global economic conditions, which may impact future earnings.

Volatility of natural gas prices has a significant impact on Southern Company Gas' customer rates, its long-term competitive position against other energy sources, and the ability of its gas marketing services and wholesale gas services segments to capture value from locational and seasonal spreads. Additionally, changes in commodity prices subject a significant portion of Southern Company Gas' operations to earnings variability. Over the longer term, volatility is expected to be low to moderate and locational and/or transportation spreads are expected to decrease as new pipelines are built to reduce the existing supply constraints in the shale areas of the Northeast U.S. To the extent these pipelines are delayed or not built, volatility could increase. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "FERC Matters" of Southern Company Gas in Item 7 of the Form 10-K for additional information on permitting challenges experienced by the Atlantic Coast Pipeline. Additional economic factors may contribute to this environment, including a significant drop in oil and natural gas prices, which could lead to consolidation of natural gas producers or reduced levels of natural gas production. Further, if economic conditions continue to improve, including the new housing market, the demand for natural gas may increase, which may cause natural gas prices to rise and drive higher volatility in the natural gas markets on a longer-term basis.

As part of its business strategy, Southern Company Gas regularly considers and evaluates joint development arrangements as well as acquisitions and dispositions of businesses and assets.

Due to the seasonal nature of the natural gas business and other factors including, but not limited to, weather, regulation, competition, customer demand, and general economic conditions, the first quarter 2019 results are not necessarily indicative of the results to be expected for any other period.

Environmental Matters

New or revised environmental laws and regulations could affect many areas of Southern Company Gas' operations. The impact of any such changes cannot be determined at this time. Environmental compliance costs could affect earnings if such costs cannot continue to be fully recovered in rates on a timely basis. Further, increased costs that are recovered through regulated rates could contribute to reduced demand for natural gas, which could negatively affect results of operations, cash flows, and/or financial condition. Additionally, many commercial and industrial customers may also be affected by existing and future environmental requirements, which for some may have the potential to ultimately affect their demand for natural gas. See Note (C) to the Condensed Financial Statements under "Environmental Remediation" herein and MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Environmental Matters" of Southern Company Gas in Item 7 and Note 3 to the financial statements under "Environmental Remediation" in Item 8 of the Form 10-K for additional information.

Regulatory Matters

See Note 2 to the financial statements under "Southern Company Gas" in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements under "Southern Company Gas" herein for additional information regarding Southern Company Gas' regulatory matters.

Rate Proceedings

Nicor Gas

In November 2018, Nicor Gas filed a general base rate case with the Illinois Commission requesting a $230 million increase in annual base rate revenues. The requested increase is based on a projected test year for the 12-month period ending September 30, 2020, a ROE of 10.6%, and an increase in the equity ratio from 52% to 54% to address the negative cash flow and credit metric impacts of the Tax Reform Legislation.

On April 16, 2019, Nicor Gas entered into a stipulation agreement to resolve all related issues with the Staff of the Illinois Commission, including a ROE of 9.86% and an equity ratio of 54%. Also on April 16, 2019, Nicor Gas filed its rebuttal testimony with the Illinois Commission incorporating the stipulation agreement and addressing the

remaining items outstanding with the other two intervenors. As a result of the stipulation agreement and rebuttal testimony, the revised requested annual revenue increase is $180 million.

The Illinois Commission is expected to rule on the requested increase within the statutory time limit of 11 months from the filing of the rate case, after which rate adjustments will be effective. The ultimate outcome of this matter cannot be determined at this time.

Atlanta Gas Light

Atlanta Gas Light is required to file a traditional base rate case no later than June 3, 2019 for rates effective January 1, 2020.

Virginia Natural Gas

In December 2018, the Virginia Commission approved Virginia Natural Gas' annual information form filing, which reduced annual base rates by $14 million effective January 1, 2019 due to lower tax expense as a result of the Tax Reform Legislation. This approval also required Virginia Natural Gas to issue customer refunds, via bill credits, for $14 million related to 2018 tax benefits deferred as a regulatory liability, current, on the balance sheet at December 31, 2018. These customer refunds were completed in the first quarter 2019.

Regulatory Infrastructure Programs

In addition to capital expenditures recovered through base rates by each of the natural gas distribution utilities, Nicor Gas and Virginia Natural Gas have separate rate riders that provide for timely recovery of capital expenditures for specific infrastructure replacement programs. Infrastructure expenditures incurred under these programs in the first three months of 2019 were as follows:

Utility	Program	First Quarter 2019 (in millions)
Nicor Gas	Investing in Illinois	$ 29
Virginia Natural Gas	Steps to Advance Virginia's Energy (SAVE)	9
Total		$ 38

On April 8, 2019, Virginia Natural Gas filed an application with the Virginia Commission to amend and extend its SAVE program. The proposal would allow Virginia Natural Gas to continue replacing aging pipeline infrastructure and increase its authorized investment under the currently-approved plan. Virginia Natural Gas seeks to amend its currently-approved plan by increasing the authorized investment in 2019 from $35 million to $40 million and to extend the plan for an additional five years until 2024, with proposed annual investments of $50 million in 2020, $60 million in 2021, and $70 million in each year from 2022 through 2024, for a maximum total investment over the six-year term (2019 through 2024) of $370 million. The proposed investment schedule would also allow for variances of up to $6 million in 2019, $8 million in 2020, $9 million in 2021, and $10 million in each year from 2022 through 2024, with a total potential net variance of up to $10 million allowed for the program. The Virginia Commission is expected to rule on the request in the third quarter 2019. The ultimate outcome of this matter cannot be determined at this time.

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Regulatory Matters – Infrastructure Replacement Programs and Capital Projects" of Southern Company Gas in Item 7 and Note 2 to the financial statements under "Southern Company Gas – Infrastructure Replacement Programs and Capital Projects" in Item 8 of the Form 10-K for additional information.

Table of Contents
SOUTHERN COMPANY GAS AND SUBSIDIARY COMPANIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Affiliate Asset Management Agreements

On March 15, 2019, the Virginia Commission approved an extension of Virginia Natural Gas' asset management agreement with Sequent to March 31, 2021. Southern Company Gas does not expect the new agreement to have a material impact on its financial statements.

FERC Matters

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "FERC Matters" of Southern Company Gas in Item 7 of the Form 10-K and Notes 7 and 9 to the financial statements under "Southern Company Gas – Equity Method Investments" and "Guarantees," respectively, in Item 8 of the Form 10-K for additional information regarding Southern Company Gas' gas pipeline construction projects.

Other Matters

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FUTURE EARNINGS POTENTIAL – "Other Matters" and "FERC Matters" of Southern Company Gas in Item 7 for additional information.

Southern Company Gas is involved in various other matters that could affect future earnings, including matters being litigated, as well as other regulatory matters and matters that could result in asset impairments. In addition, Southern Company Gas is subject to certain claims and legal actions arising in the ordinary course of business. The ultimate outcome of such pending or potential litigation, regulatory matters, or potential asset impairments cannot be predicted at this time; however, for current proceedings not specifically reported in Notes (B) and (C) to the Condensed Financial Statements herein, management does not anticipate that the ultimate liabilities, if any, arising from such current proceedings would have a material effect on Southern Company Gas' financial statements. See Notes (B) and (C) to the Condensed Financial Statements herein for a discussion of various other contingencies, regulatory matters, and other matters being litigated which may affect future earnings potential.

ACCOUNTING POLICIES

Application of Critical Accounting Policies and Estimates

Southern Company Gas prepares its financial statements in accordance with GAAP. Significant accounting policies are described in Notes 1, 5, and 6 to the financial statements in Item 8 of the Form 10-K. In the application of these policies, certain estimates are made that may have a material impact on Southern Company Gas' results of operations and related disclosures. Different assumptions and measurements could produce estimates that are significantly different from those recorded in the financial statements. See MANAGEMENT'S DISCUSSION AND ANALYSIS – ACCOUNTING POLICIES – "Application of Critical Accounting Policies and Estimates" of Southern Company Gas in Item 7 of the Form 10-K for a complete discussion of Southern Company Gas' critical accounting policies and estimates.

Recently Issued Accounting Standards

See Note (A) to the Condensed Financial Statements herein for information regarding Southern Company Gas' recently adopted accounting standards.

FINANCIAL CONDITION AND LIQUIDITY

Overview

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Overview" of Southern Company Gas in Item 7 of the Form 10-K for additional information. Southern Company Gas' financial condition remained stable at March 31, 2019. Southern Company Gas intends to continue to monitor its access to short-term and long-term capital markets as well as bank credit agreements to meet future capital and liquidity needs. See "Capital Requirements and Contractual Obligations," "Sources of Capital," and "Financing Activities" herein for additional information.

Table of Contents

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

By regulation, Nicor Gas is restricted, to the extent of its retained earnings balance, in the amount it can dividend or loan to affiliates and is not permitted to make money pool loans to affiliates. At March 31, 2019, the amount of subsidiary retained earnings restricted to dividend totaled $875 million. This restriction did not impact Southern Company Gas' ability to meet its cash obligations.

Net cash provided from operating activities totaled $683 million for the first three months of 2019, a decrease of $295 million from the corresponding period in 2018. The decrease was primarily due to the impacts of the Southern Company Gas Dispositions and the timing of vendor payments. Net cash used for investing activities totaled $290 million for the first three months of 2019 primarily due to gross property additions related to utility capital expenditures and infrastructure investments recovered through replacement programs at gas distribution operations and capital contributed to equity method pipeline investments. Net cash used for financing activities totaled $402 million for the first three months of 2019 primarily due to repayments of commercial paper borrowings and a common stock dividend payment to Southern Company. Cash flows from financing activities vary from period to period based on capital needs and the maturity or redemption of securities.

Significant balance sheet changes for the first three months of 2019 include a decrease of $363 million in natural gas for sale, net of temporary LIFO liquidation, due to the use of stored natural gas and a $289 million decrease in notes payable primarily related to net repayments of commercial paper borrowings. Other significant balance sheet changes include decreases of $272 million and $324 million in energy marketing receivables and payables, respectively, due to lower natural gas prices and volumes of natural gas sold, and an increase of $171 million in total property, plant, and equipment primarily due to utility capital expenditures and infrastructure investments recovered through replacement programs. Balance sheet changes for the first three months of 2019 also include recording $86 million in operating lease right-of use assets and $84 million in operating lease obligations related to the adoption of ASU No. 2016-02, Leases (Topic 842) (ASC 842). See Note (L) to the Condensed Financial Statements herein for additional information on the adoption of ASC 842.

Capital Requirements and Contractual Obligations

See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Capital Requirements and Contractual Obligations" of Southern Company Gas in Item 7 of the Form 10-K for a description of Southern Company Gas' capital requirements and contractual obligations. Approximately $350 million will be required through March 31, 2020 to fund maturities of long-term debt. See "Sources of Capital" herein for additional information.

The regulatory infrastructure programs and other construction programs are subject to periodic review and revision, and actual costs may vary from these estimates because of numerous factors. These factors include: changes in business conditions; changes in FERC rules and regulations; state regulatory approvals; changes in legislation; the cost and efficiency of labor, equipment, and materials; project scope and design changes; and the cost of capital. In addition, there can be no assurance that costs related to capital expenditures will be fully recovered. See Note 2 to the financial statements under "Southern Company Gas" in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements herein for information regarding additional factors that may impact infrastructure investment expenditures.

Sources of Capital

Southern Company Gas plans to obtain the funds to meet its future capital needs from sources similar to those used in the past, which were primarily from operating cash flows, external securities issuances, borrowings from financial institutions, and equity contributions from Southern Company. However, the amount, type, and timing of any future financings, if needed, depend upon prevailing market conditions, regulatory approval, and other factors. The issuance of securities by Nicor Gas is generally subject to the approval of the Illinois Commission. See MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Sources of Capital" of Southern Company Gas in Item 7 of the Form 10-K for additional information.

Southern Company Gas' current liabilities exceeded current assets by $495 million primarily as a result of $361 million in notes payable and $354 million in securities due within one year. Southern Company Gas' current

137

liabilities frequently exceed current assets because of commercial paper borrowings used to fund daily operations, scheduled maturities of long-term debt, and significant seasonal fluctuations in cash needs.

At March 31, 2019, Southern Company Gas had $57 million of cash and cash equivalents. Committed credit arrangements with banks at March 31, 2019 were as follows:

Company	Expires 2022	Unused
	(in millions)	
Southern Company Gas Capital[(a)]	$1,400	$1,395
Nicor Gas	500	500
Total[(b)]	$1,900	$1,895

(a) Southern Company Gas guarantees the obligations of Southern Company Gas Capital.

(b) Pursuant to the credit arrangement, the allocations between Southern Company Gas Capital and Nicor Gas may be adjusted.

See Note 8 to the consolidated financial statements under "Bank Credit Arrangements" in Item 8 of the Form 10-K and Note (F) to the Condensed Financial Statements under "Bank Credit Arrangements" herein for additional information.

The multi-year credit arrangement of Southern Company Gas Capital and Nicor Gas (Facility) contains a covenant that limits the debt levels and contains a cross-acceleration provision to other indebtedness (including guarantee obligations) of the applicable company. Such cross-acceleration provision to other indebtedness would trigger an event of default of the applicable company if Southern Company Gas or Nicor Gas defaulted on indebtedness, the payment of which was then accelerated. At March 31, 2019, both companies were in compliance with such covenant. The Facility does not contain a material adverse change clause at the time of borrowings.

Subject to applicable market conditions, the applicable company expects to renew or replace the Facility as needed, prior to expiration. In connection therewith, the applicable company may extend the maturity dates and/or increase or decrease the lending commitments thereunder. A portion of unused credit with banks provides liquidity support to Southern Company Gas.

Southern Company Gas has substantial cash flow from operating activities and access to capital markets, including the commercial paper programs, and financial institutions to meet liquidity needs. Southern Company Gas makes short-term borrowings primarily through commercial paper programs that have the liquidity support of the committed bank credit arrangements described above. Short-term borrowings are included in notes payable in the balance sheets. Details of short-term borrowings were as follows:

	Short-Term Debt at March 31, 2019		Short-Term Debt During the Period[(*)]		
	Amount Outstanding	Weighted Average Interest Rate	Average Amount Outstanding	Weighted Average Interest Rate	Maximum Amount Outstanding
Commercial paper:	(in millions)		(in millions)		(in millions)
Southern Company Gas Capital	$326	2.8 %	$ 364	2.9 %	$ 472
Nicor Gas	35	2.6 %	106	2.9 %	247
Total	$361	2.8 %	$ 470	2.9 %	

(*) Average and maximum amounts are based upon daily balances during the three-month period ended March 31, 2019.

Southern Company Gas believes that the need for working capital can be adequately met by utilizing commercial paper programs, lines of credit, and operating cash flows.

Table of Contents
SOUTHERN COMPANY GAS AND SUBSIDIARY COMPANIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Credit Rating Risk

Southern Company Gas 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 below BBB- and/or Baa3. These contracts are for physical gas purchases and sales and energy price risk management. The maximum potential collateral requirement under these contracts at March 31, 2019 was approximately $12 million.

Generally, collateral may be provided by a Southern Company guaranty, letter of credit, or cash. Additionally, a credit rating downgrade could impact the ability of Southern Company Gas to access capital markets and would be likely to impact the cost at which it does so.

As a result of the Tax Reform Legislation, certain financial metrics, such as the funds from operations to debt percentage, used by the credit rating agencies to assess Southern Company and its subsidiaries, including Southern Company Gas, may be negatively impacted. Southern Company Gas and its regulated subsidiaries have taken actions to mitigate the resulting impacts, which, among other alternatives, include adjusting capital structure. Absent actions by Southern Company and its subsidiaries that fully mitigate the impacts, Southern Company Gas', Southern Company Gas Capital's, and Nicor Gas' credit ratings could be negatively affected. The Georgia PSC's May 15, 2018 approval of a stipulation for Atlanta Gas Light's annual rate adjustment maintained the previously authorized earnings band and increased the equity ratio to address the negative cash flow and credit metric impacts of the Tax Reform Legislation. See Note 2 to the financial statements under "Southern Company Gas" in Item 8 of the Form 10-K and Note (B) to the Condensed Financial Statements under "Southern Company Gas" herein for information on additional rate proceedings for Nicor Gas and Atlanta Gas Light expected to conclude in 2019.

Financing Activities

The long-term debt on Southern Company Gas' balance sheets includes both principal and non-principal components. As of March 31, 2019, the non-principal components totaled $444 million, which consisted of the unamortized portions of the fair value adjustment recorded in purchase accounting, debt premiums, debt discounts, and debt issuance costs.

Southern Company Gas did not issue or redeem any securities during the three months ended March 31, 2019.

In addition to any financings that may be necessary to meet capital requirements and contractual obligations, Southern Company Gas 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.

Market Price Risk

Other than the items discussed below, there were no material changes to Southern Company Gas' disclosures about market price risk during the first quarter 2019. For an in-depth discussion of Southern Company Gas' market price risks, see MANAGEMENT'S DISCUSSION AND ANALYSIS – FINANCIAL CONDITION AND LIQUIDITY – "Market Price Risk" of Southern Company Gas in Item 7 of the Form 10-K. Also see Notes (I) and (J) to the Condensed Financial Statements herein for information relating to derivative instruments.

Southern Company Gas is exposed to market risks, primarily commodity price risk, interest rate risk, and weather risk. Due to various cost recovery mechanisms, the natural gas distribution utilities of Southern Company Gas that sell natural gas directly to end-use customers have limited exposure to market volatility of natural gas prices. Certain natural gas distribution utilities of Southern Company Gas may manage fuel-hedging programs implemented per the guidelines of their respective state regulatory agencies to hedge the impact of market fluctuations in natural gas prices for customers. For the weather risk associated with Nicor Gas, Southern Company Gas has a corporate weather hedging program that utilizes weather derivatives to reduce the risk of lower operating margins potentially resulting from significantly warmer-than-normal weather. In addition, certain non-regulated operations routinely utilize various types of derivative instruments to economically hedge certain commodity price

and weather risks inherent in the natural gas industry. These instruments include a variety of exchange-traded and over-the-counter energy contracts, such as forward contracts, futures contracts, options contracts, and swap agreements. Some of these economic hedge activities may not qualify, or are not designated, for hedge accounting treatment. For the periods presented below, the changes in net fair value of Southern Company Gas' derivative contracts were as follows:

	First Quarter 2019	First Quarter 2018
	(in millions)	
Contracts outstanding at beginning of period, assets (liabilities), net	$(167)	$(106)
Contracts realized or otherwise settled	(5)	49
Current period changes[(a)]	44	(13)
Contracts outstanding at the end of period, assets (liabilities), net	$(128)	$(70)
Netting of cash collateral	190	223
Cash collateral and net fair value of contracts outstanding at end of period[(b)]	$62	$153

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

(b) Net fair value of derivative contracts outstanding excludes premium and the intrinsic value associated with weather derivatives of $11 million and $4 million at March 31, 2019 and 2018, respectively.

The maturities of Southern Company Gas' energy-related derivative contracts at March 31, 2019 were as follows:

		Fair Value Measurements March 31, 2019 Maturity		
	Total Fair Value	Year 1	Years 2 & 3	Years 4 and thereafter
	(in millions)			
Level 1[(a)]	$(144)	$(36)	$(76)	$(32)
Level 2[(b)]	35	26	10	(1)
Level 3[(c)]	(19)	2	(2)	(19)
Fair value of contracts outstanding at end of period[(d)]	$(128)	$(8)	$(68)	$(52)

(a) Valued using NYMEX futures prices.

(b) Valued using basis transactions that represent the cost to transport natural gas from a NYMEX delivery point to the contract delivery point. These transactions are based on quotes obtained either through electronic trading platforms or directly from brokers.

(c) Valued using a combination of observable and unobservable inputs.

(d) Excludes cash collateral of $190 million as well as premium and associated intrinsic value associated with weather derivatives of $11 million at March 31, 2019.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS
FOR
THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
ALABAMA POWER COMPANY
GEORGIA POWER COMPANY
MISSISSIPPI POWER COMPANY
SOUTHERN POWER COMPANY AND SUBSIDIARY COMPANIES
SOUTHERN COMPANY GAS AND SUBSIDIARY COMPANIES
(UNAUDITED)

INDEX TO THE NOTES TO THE CONDENSED FINANCIAL STATEMENTS

INDEX TO APPLICABLE NOTES TO FINANCIAL STATEMENTS BY REGISTRANT

The following unaudited notes to the condensed financial statements are a combined presentation. The list below indicates the registrants to which each footnote applies.

Registrant	Applicable Notes
Southern Company	A, B, C, D, E, F, G, H, I, J, K, L, M
Alabama Power	A, B, C, D, F, G, H, I, J, L
Georgia Power	A, B, C, D, F, G, H, I, J, L
Mississippi Power	A, B, C, D, F, G, H, I, J, L
Southern Power	A, C, D, E, F, G, H, I, J, K, L
Southern Company Gas	A, B, C, D, E, F, G, H, I, J, K, L, M

Table of Contents

THE SOUTHERN COMPANY AND SUBSIDIARY COMPANIES
ALABAMA POWER COMPANY
GEORGIA POWER COMPANY
MISSISSIPPI POWER COMPANY
SOUTHERN POWER COMPANY AND SUBSIDIARY COMPANIES
SOUTHERN COMPANY GAS AND SUBSIDIARY COMPANIES

NOTES TO THE CONDENSED FINANCIAL STATEMENTS:
(UNAUDITED)

(A) INTRODUCTION

The condensed quarterly financial statements of each registrant included herein have been prepared by such registrant, without audit, pursuant to the rules and regulations of the SEC. The Condensed Balance Sheets as of December 31, 2018 have been derived from the audited financial statements of each registrant. In the opinion of each registrant's management, the information regarding such registrant furnished herein reflects all adjustments, which, except as otherwise disclosed, are of a normal recurring nature, necessary to present fairly the results of operations for the periods ended March 31, 2019 and 2018. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations, although each registrant believes that the disclosures regarding such registrant are adequate to make the information presented not misleading. Disclosures which would substantially duplicate the disclosures in the Form 10-K and details which have not changed significantly in amount or composition since the filing of the Form 10-K are generally omitted from this Quarterly Report on Form 10-Q unless specifically required by GAAP. Therefore, these Condensed Financial Statements should be read in conjunction with the financial statements and the notes thereto included in the Form 10-K. Due to the seasonal variations in the demand for energy, operating results for the periods presented are not necessarily indicative of the operating results to be expected for the full year.

Certain prior year data presented in the financial statements have been reclassified to conform to the current year presentation. These reclassifications had no impact on the results of operations, financial position, or cash flows of any registrant.

Recently Adopted Accounting Standards

In 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (ASU 2016-02). ASU 2016-02 requires lessees to recognize on the balance sheet a lease liability and a right-of-use asset for all leases. ASU 2016-02 also changes the recognition, measurement, and presentation of expense associated with leases and provides clarification regarding the identification of certain components of contracts that would represent a lease. The accounting required by lessors is relatively unchanged and there is no change to the accounting for existing leveraged leases. The registrants adopted the new standard effective January 1, 2019. See Note (L) for additional information and related disclosures.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Goodwill and Other Intangible Assets
Goodwill at March 31, 2019 and December 31, 2018 was as follows:

	At March 31, 2019	At December 31, 2018
	(in millions)	
Southern Company	$5,284	$ 5,315
Southern Company Gas:		
Gas distribution operations	$4,034	$ 4,034
Gas marketing services	981	981
Southern Company Gas total	$5,015	$ 5,015

Goodwill is not amortized but is subject to an annual impairment test during the fourth quarter of each year or more frequently if impairment indicators arise.

143

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Other intangible assets were as follows:

	At March 31, 2019			At December 31, 2018		
	Gross Carrying Amount	Accumulated Amortization	Other Intangible Assets, Net	Gross Carrying Amount	Accumulated Amortization	Other Intangible Assets, Net
	(in millions)			(in millions)		
Southern Company						
Other intangible assets subject to amortization:						
Customer relationships	$211	$ (100)	$ 111	$223	$ (94)	$ 129
Trade names	70	(22)	48	70	(21)	49
Storage and transportation contracts	64	(56)	8	64	(54)	10
PPA fair value adjustments	405	(67)	338	405	(61)	344
Other	11	(6)	5	11	(5)	6
Total other intangible assets subject to amortization	$761	$ (251)	$ 510	$773	$ (235)	$ 538
Other intangible assets not subject to amortization:						
Federal Communications Commission licenses	75	—	75	75	—	75
Total other intangible assets	$836	$ (251)	$ 585	$848	$ (235)	$ 613
Southern Power						
Other intangible assets subject to amortization:						
PPA fair value adjustments	$405	$ (67)	$ 338	$405	$ (61)	$ 344
Southern Company Gas						
Other intangible assets subject to amortization:						
Gas marketing services						
Customer relationships	$156	$ (89)	$ 67	$156	$ (84)	$ 72
Trade names	26	(8)	18	26	(7)	19
Wholesale gas services						
Storage and transportation contracts	64	(56)	8	64	(54)	10
Total other intangible assets subject to amortization	$246	$ (153)	$ 93	$246	$ (145)	$ 101

144

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Amortization associated with other intangible assets was as follows:

	Three Months Ended March 31, 2019 (in millions)
Southern Company	$ 17
Southern Power[(a)]	$ 6
Southern Company Gas	
Gas marketing services[(b)]	$ 6
Wholesale gas services[(a)]	2
Southern Company Gas total	$ 8

(a) Recorded as a reduction to operating revenues.
(b) Included in depreciation and amortization.

Restricted Cash

At December 31, 2018, Georgia Power had restricted cash related to the redemption of pollution control revenue bonds, which were redeemed in January 2019. See Note (F) under "Financing Activities" for additional information. At both March 31, 2019 and December 31, 2018, Southern Company Gas had restricted cash held as collateral for worker's compensation, life insurance, and long-term disability insurance.

The following tables provide a reconciliation of cash, cash equivalents, and restricted cash reported within the condensed balance sheets that total to the amounts shown in the condensed statements of cash flows for the registrants that had restricted cash at March 31, 2019 and/or December 31, 2018:

	Southern Company	Southern Company Gas
	(in millions)	
At March 31, 2019		
Cash and cash equivalents	$1,361	$ 57
Restricted cash:		
Other accounts and notes receivable	4	4
Total cash, cash equivalents, and restricted cash	$1,364[(*)]	$ 61

(*) Total does not add due to rounding.

	Southern Company	Georgia Power	Southern Company Gas
	(in millions)		
At December 31, 2018			
Cash and cash equivalents	$1,396	$ 4	$ 64
Cash and cash equivalents held for sale	9	—	—
Restricted cash:			
Restricted cash	—	108	—
Other accounts and notes receivable	114	—	6
Total cash, cash equivalents, and restricted cash	$1,519	$ 112	$ 70

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Natural Gas for Sale

Southern Company Gas, with the exception of Nicor Gas, carries natural gas inventory on a WACOG basis. For any declines in market prices below the WACOG considered to be other than temporary, an adjustment is recorded to reduce the value of natural gas inventories to market value. Southern Company Gas had no material adjustment in any period presented.

Nicor Gas' natural gas inventory is carried at cost on a LIFO basis. Inventory decrements occurring during the year that are restored prior to year end are charged to cost of natural gas at the estimated annual replacement cost. Inventory decrements that are not restored prior to year end are charged to cost of natural gas at the actual LIFO cost of the inventory layers liquidated. Nicor Gas' inventory decrement at March 31, 2019 is expected to be restored prior to year end.

(B) REGULATORY MATTERS

See Note 2 to the financial statements in Item 8 of the Form 10-K for additional information relating to regulatory matters.

The recovery balances for certain of Alabama Power's, Georgia Power's, and Mississippi Power's regulatory clauses at March 31, 2019 and December 31, 2018 were as follows:

Regulatory Clause	Balance Sheet Line Item	March 31, 2019	December 31, 2018
		(in millions)	
Alabama Power			
Rate CNP Compliance	Deferred under recovered regulatory clause revenues	$ —	$ 42
	Customer accounts receivable	25	—
Rate CNP PPA	Deferred under recovered regulatory clause revenues	21	25
Retail Energy Cost Recovery(*)	Deferred under recovered regulatory clause revenues	—	109
	Other regulatory liabilities, deferred	2	—
Natural Disaster Reserve	Other regulatory liabilities, deferred	22	20
Georgia Power			
Fuel Cost Recovery	Receivables – under recovered fuel clause revenues	$ 73	$ 115
Mississippi Power			
Fuel Cost Recovery	Over recovered retail fuel costs	$ 10	$ 8

(*) In accordance with an accounting order issued on February 5, 2019 by the Alabama PSC, Alabama Power utilized $75 million of the 2018 Rate RSE refund liability to reduce the Rate ECR under recovered balance. See Note 2 to the financial statements under "Alabama Power – Rate ECR" in Item 8 of the Form 10-K for additional information.

Alabama Power

Environmental Accounting Order

In connection with management's decision to retire Plant Gorgas, in February 2019, Alabama Power reclassified approximately $1.3 billion for Plant Gorgas Unit 10 from plant in service, net of depreciation to other utility plant, net and continued to depreciate the asset according to the original depreciation rates. On April 15, 2019, Alabama Power retired Plant Gorgas Units 8, 9, and 10 and reclassified approximately $740 million of the remaining net investment costs of the units to a regulatory asset to be recovered over the units' remaining useful lives as established prior to the decision to retire. Additionally, approximately $700 million of net capitalized asset

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

retirement costs will be reclassified to a regulatory asset and recovered in accordance with accounting guidance provided by the Alabama PSC. See Note 2 to the financial statements under "Alabama Power – Environmental Accounting Order" and Note 6 in Item 8 of the Form 10-K for additional information.

Georgia Power

Nuclear Construction

See Note 2 to the financial statements under "Georgia Power – Nuclear Construction" in Item 8 of the Form 10-K for additional information regarding Georgia Power's construction of Plant Vogtle Units 3 and 4, the joint ownership agreements and related funding agreement, VCM reports, and the NCCR tariff.

In 2009, the Georgia PSC certified construction of Plant Vogtle Units 3 and 4. Georgia Power holds a 45.7% ownership interest in Plant Vogtle Units 3 and 4. In 2012, the NRC issued the related combined construction and operating licenses, which allowed full construction of the two AP1000 nuclear units (with electric generating capacity of approximately 1,100 MWs each) and related facilities to begin. Until March 2017, construction on Plant Vogtle Units 3 and 4 continued under the Vogtle 3 and 4 Agreement, which was a substantially fixed price agreement. In March 2017, the EPC Contractor filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code. In connection with the EPC Contractor's bankruptcy filing, Georgia Power, acting for itself and as agent for the other Vogtle Owners, entered into several transitional arrangements to allow construction to continue. In July 2017, Georgia Power, acting for itself and as agent for the other Vogtle Owners, entered into the Vogtle Services Agreement, whereby Westinghouse provides facility design and engineering services, procurement and technical support, and staff augmentation on a time and materials cost basis. The Vogtle Services Agreement provides that it will continue until the start-up and testing of Plant Vogtle Units 3 and 4 are complete and electricity is generated and sold from both units. The Vogtle Services Agreement is terminable by the Vogtle Owners upon 30 days' written notice.

In October 2017, Georgia Power, acting for itself and as agent for the other Vogtle Owners, executed the Bechtel Agreement, a cost reimbursable plus fee arrangement, whereby Bechtel is reimbursed for actual costs plus a base fee and an at-risk fee, which is subject to adjustment based on Bechtel's performance against cost and schedule targets. Each Vogtle Owner is severally (not jointly) liable for its proportionate share, based on its ownership interest, of all amounts owed to Bechtel under the Bechtel Agreement. The Vogtle Owners may terminate the Bechtel Agreement at any time for their convenience, provided that the Vogtle Owners will be required to pay amounts related to work performed prior to the termination (including the applicable portion of the base fee), certain termination-related costs, and, at certain stages of the work, the applicable portion of the at-risk fee. Bechtel may terminate the Bechtel Agreement under certain circumstances, including certain Vogtle Owner suspensions of work, certain breaches of the Bechtel Agreement by the Vogtle Owners, Vogtle Owner insolvency, and certain other events.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Cost and Schedule

Georgia Power's approximate proportionate share of the remaining estimated capital cost to complete Plant Vogtle Units 3 and 4 by the expected in-service dates of November 2021 and November 2022, respectively, is as follows:

	(in billions)
Base project capital cost forecast[(a)(b)]	$ 8.0
Construction contingency estimate	0.4
Total project capital cost forecast[(a)(b)]	8.4
Net investment as of March 31, 2019[(b)]	(4.9)
Remaining estimate to complete[(a)]	$ 3.5

(a) Excludes financing costs expected to be capitalized through AFUDC of approximately $325 million.

(b) Net of $1.7 billion received from Toshiba under the Guarantee Settlement Agreement and approximately $188 million in related Customer Refunds.

Georgia Power estimates that its financing costs for construction of Plant Vogtle Units 3 and 4 will total approximately $3.1 billion, of which $1.9 billion had been incurred through March 31, 2019.

In April 2019, Southern Nuclear completed a cost and schedule validation process to verify and update quantities of commodities remaining to install, labor hours to install remaining quantities and related productivity, testing and system turnover requirements, and forecasted staffing needs and related costs. This process confirmed the total estimated project capital cost forecast for Plant Vogtle Units 3 and 4. The expected in-service dates of November 2021 for Unit 3 and November 2022 for Unit 4, as previously approved by the Georgia PSC, remain unchanged.

As construction continues, challenges with management of contractors, subcontractors, and vendors; supervision of craft labor and related craft labor productivity, ability to attract and retain craft labor, and/or related cost escalation; procurement, fabrication, delivery, assembly, and/or installation and the initial testing and start-up, including any required engineering changes, of plant systems, structures, or components (some of which are based on new technology that only recently began initial operation in the global nuclear industry at this scale), any of which may require additional labor and/or materials; or other issues could arise and change the projected schedule and estimated cost. Monthly construction production targets established as part of a strategy to maintain and build margin to the approved in-service dates will continue to increase significantly throughout 2019. To meet these increasing monthly targets, existing craft construction productivity must improve and additional craft laborers must be retained and deployed.

There have been technical and procedural challenges to the construction and licensing of Plant Vogtle Units 3 and 4 at the federal and state level and additional challenges may arise. Processes are in place that are designed to assure compliance with the requirements specified in the Westinghouse Design Control Document and the combined construction and operating licenses, including inspections by Southern Nuclear and the NRC that occur throughout construction. As a result of such compliance processes, certain license amendment requests have been filed and approved or are pending before the NRC. Various design and other licensing-based compliance matters, including the timely resolution of ITAAC and the related approvals by the NRC, may arise, which may result in additional license amendments or require other resolution. If any license amendment requests or other licensing-based compliance issues are not resolved in a timely manner, there may be delays in the project schedule that could result in increased costs.

The ultimate outcome of these matters cannot be determined at this time. However, any extension of the regulatory-approved project schedule is currently estimated to result in additional base capital costs of approximately $50 million per month, based on Georgia Power's ownership interests, and AFUDC of approximately $12 million per month. While Georgia Power is not precluded from seeking recovery of any future capital cost forecast increase, management will ultimately determine whether or not to seek recovery. Any further changes to the capital cost forecast that are not expected to be recoverable through regulated rates will be required to be charged to income and such charges could be material.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Joint Owner Contracts

In November 2017, the Vogtle Owners entered into an amendment to their joint ownership agreements for Plant Vogtle Units 3 and 4 to provide for, among other conditions, additional Vogtle Owner approval requirements. Effective in August 2018, the Vogtle Owners further amended the joint ownership agreements to clarify and provide procedures for certain provisions of the joint ownership agreements related to adverse events that require the vote of the holders of at least 90% of the ownership interests in Plant Vogtle Units 3 and 4 to continue construction (as amended, and together with the November 2017 amendment, the Vogtle Joint Ownership Agreements). The Vogtle Joint Ownership Agreements also confirm that the Vogtle Owners' sole recourse against Georgia Power or Southern Nuclear for any action or inaction in connection with their performance as agent for the Vogtle Owners is limited to removal of Georgia Power and/or Southern Nuclear as agent, except in cases of willful misconduct.

As a result of the increase in the total project capital cost forecast and Georgia Power's decision not to seek rate recovery of the increase in the base capital costs in conjunction with the nineteenth VCM report, the holders of at least 90% of the ownership interests in Plant Vogtle Units 3 and 4 were required to vote to continue construction. In September 2018, the Vogtle Owners unanimously voted to continue construction of Plant Vogtle Units 3 and 4.

Amendments to the Vogtle Joint Ownership Agreements

In connection with the vote to continue construction, Georgia Power entered into (i) a binding term sheet (Vogtle Owner Term Sheet) with the other Vogtle Owners and MEAG's wholly-owned subsidiaries MEAG Power SPVJ, LLC (MEAG SPVJ), MEAG Power SPVM, LLC (MEAG SPVM), and MEAG Power SPVP, LLC (MEAG SPVP) to take certain actions which partially mitigate potential financial exposure for the other Vogtle Owners, including additional amendments to the Vogtle Joint Ownership Agreements and the purchase of PTCs from the other Vogtle Owners at pre-established prices, and (ii) a term sheet (MEAG Term Sheet) with MEAG and MEAG SPVJ to provide funding with respect to MEAG SPVJ's ownership interest in Plant Vogtle Units 3 and 4 under certain circumstances. On January 14, 2019, Georgia Power, MEAG, and MEAG SPVJ entered into an agreement to implement the provisions of the MEAG Term Sheet. On February 18, 2019, Georgia Power, the other Vogtle Owners, and MEAG's wholly-owned subsidiaries MEAG SPVJ, MEAG SPVM, and MEAG SPVP entered into certain amendments to the Vogtle Joint Ownership Agreements to implement the provisions of the Vogtle Owner Term Sheet.

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

Regulatory Matters

In 2009, the Georgia PSC voted to certify construction of Plant Vogtle Units 3 and 4 with a certified capital cost of $4.418 billion. In addition, in 2009 the Georgia PSC approved inclusion of the Plant Vogtle Units 3 and 4 related CWIP accounts in rate base, and the State of Georgia enacted the Georgia Nuclear Energy Financing Act, which allows Georgia Power to recover financing costs for Plant Vogtle Units 3 and 4. Financing costs are recovered on all applicable certified costs through annual adjustments to the NCCR tariff up to the certified capital cost of $4.418 billion. At March 31, 2019, Georgia Power had recovered approximately $1.9 billion of financing costs. Financing costs related to capital costs above $4.418 billion will be recovered through AFUDC; however, Georgia Power will not record AFUDC related to any capital costs in excess of the total deemed reasonable by the Georgia PSC (currently $7.3 billion) and not requested for rate recovery. In December 2018, the Georgia PSC approved Georgia Power's request to increase the NCCR tariff by $88 million annually, effective January 1, 2019.

Georgia Power is required to file semi-annual VCM reports with the Georgia PSC by February 28 and August 31 of each year. In 2013, in connection with the eighth VCM report, the Georgia PSC approved a stipulation between Georgia Power and the staff of the Georgia PSC to waive the requirement to amend the Plant Vogtle Units 3 and 4 certificate in accordance with the 2009 certification order until the completion of Plant Vogtle Unit 3, or earlier if deemed appropriate by the Georgia PSC and Georgia Power.

In 2016, the Georgia PSC voted to approve a settlement agreement (Vogtle Cost Settlement Agreement) resolving certain prudency matters in connection with the fifteenth VCM report. In December 2017, the Georgia PSC voted to

149

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

approve (and issued its related order on January 11, 2018) Georgia Power's seventeenth VCM report and modified the Vogtle Cost Settlement Agreement. The Vogtle Cost Settlement Agreement, as modified by the January 11, 2018 order, resolved the following regulatory matters related to Plant Vogtle Units 3 and 4: (i) none of the $3.3 billion of costs incurred through December 31, 2015 and reflected in the fourteenth VCM report should be disallowed from rate base on the basis of imprudence; (ii) the Contractor Settlement Agreement was reasonable and prudent and none of the amounts paid pursuant to the Contractor Settlement Agreement should be disallowed from rate base on the basis of imprudence; (iii) (a) capital costs incurred up to $5.68 billion would be presumed to be reasonable and prudent with the burden of proof on any party challenging such costs, (b) Georgia Power would have the burden to show that any capital costs above $5.68 billion were prudent, and (c) a revised capital cost forecast of $7.3 billion (after reflecting the impact of payments received under the Guarantee Settlement Agreement and related Customer Refunds) was found reasonable; (iv) construction of Plant Vogtle Units 3 and 4 should be completed, with Southern Nuclear serving as project manager and Bechtel as primary contractor; (v) approved and deemed reasonable Georgia Power's revised schedule placing Plant Vogtle Units 3 and 4 in service in November 2021 and November 2022, respectively; (vi) confirmed that the revised cost forecast does not represent a cost cap and that prudence decisions on cost recovery will be made at a later date, consistent with applicable Georgia law; (vii) reduced the ROE used to calculate the NCCR tariff (a) from 10.95% (the ROE rate setting point authorized by the Georgia PSC in the 2013 ARP) to 10.00% effective January 1, 2016, (b) from 10.00% to 8.30%, effective January 1, 2020, and (c) from 8.30% to 5.30%, effective January 1, 2021 (provided that the ROE in no case will be less than Georgia Power's average cost of long-term debt); (viii) reduced the ROE used for AFUDC equity for Plant Vogtle Units 3 and 4 from 10.00% to Georgia Power's average cost of long-term debt, effective January 1, 2018; and (ix) agreed that upon Unit 3 reaching commercial operation, retail base rates would be adjusted to include carrying costs on those capital costs deemed prudent in the Vogtle Cost Settlement Agreement. The January 11, 2018 order also stated that if Plant Vogtle Units 3 and 4 are not commercially operational by June 1, 2021 and June 1, 2022, respectively, the ROE used to calculate the NCCR tariff will be further reduced by 10 basis points each month (but not lower than Georgia Power's average cost of long-term debt) until the respective Unit is commercially operational. The ROE reductions negatively impacted earnings by approximately $100 million in 2018 and are estimated to have negative earnings impacts of approximately $75 million in 2019 and an aggregate of approximately $635 million from 2020 to 2022.

In its January 11, 2018 order, the Georgia PSC also stated if other conditions change and assumptions upon which Georgia Power's seventeenth VCM report are based do not materialize, the Georgia PSC reserved the right to reconsider the decision to continue construction.

In February 2018, Georgia Interfaith Power & Light, Inc. (GIPL) and Partnership for Southern Equity, Inc. (PSE) filed a petition appealing the Georgia PSC's January 11, 2018 order with the Fulton County Superior Court. In March 2018, Georgia Watch filed a similar appeal to the Fulton County Superior Court for judicial review of the Georgia PSC's decision and denial of Georgia Watch's motion for reconsideration. In December 2018, the Fulton County Superior Court granted Georgia Power's motion to dismiss the two appeals. On January 9, 2019, GIPL, PSE, and Georgia Watch filed an appeal of this decision with the Georgia Court of Appeals. Georgia Power believes the appeal has no merit; however, an adverse outcome in the appeal combined with subsequent adverse action by the Georgia PSC could have a material impact on Southern Company's and Georgia Power's results of operations, financial condition, and liquidity.

In August 2018, Georgia Power filed its nineteenth VCM report with the Georgia PSC, which requested approval of $578 million of construction capital costs incurred from January 1, 2018 through June 30, 2018. On February 19, 2019, the Georgia PSC approved the nineteenth VCM, but deferred approval of $51.6 million of expenditures related to Georgia Power's portion of an administrative claim filed in the Westinghouse bankruptcy proceedings. Through the nineteenth VCM, the Georgia PSC has approved total construction capital costs incurred through June 30, 2018 of $5.4 billion (before $1.7 billion of payments received under the Guarantee Settlement Agreement and approximately $188 million in related Customer Refunds). In addition, the staff of the Georgia PSC requested, and Georgia Power agreed, to report the results of the cost and schedule validation process to the Georgia PSC (which is expected to occur by May 1, 2019) and to file its twentieth VCM report concurrently with the twenty-first VCM report by August 31, 2019.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

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

DOE Financing

At March 31, 2019, Georgia Power had borrowed $3.46 billion related to Plant Vogtle Units 3 and 4 costs as provided through the Amended and Restated Loan Guarantee Agreement and related multi-advance credit facilities among Georgia Power, the DOE, and the FFB, which provide for borrowings of up to approximately $5.130 billion, subject to the satisfaction of certain conditions. See Note 8 to the financial statements under "Long-term Debt – DOE Loan Guarantee Borrowings" in Item 8 of the Form 10-K and Note (F) under "DOE Loan Guarantee Borrowings" for additional information, including applicable covenants, events of default, mandatory prepayment events, and conditions to borrowing.

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

Mississippi Power

Municipal and Rural Association Tariff

On March 28, 2019, Mississippi Power filed a request with the FERC for a decrease in wholesale base revenues under the MRA tariff as agreed upon in a settlement agreement reached with its wholesale customers resolving all matters related to the Kemper County energy facility similar to the retail rate settlement agreement approved by the Mississippi PSC in February 2018 and reflecting the impacts of the Tax Reform Legislation. The MRA settlement agreement provides that base rates will decrease $3.7 million annually, effective January 1, 2019. Mississippi Power expects the matter to be resolved in the second quarter 2019. The ultimate outcome of this matter cannot be determined at this time.

Kemper County Energy Facility

As the mining permit holder, Liberty Fuels Company, LLC has a legal obligation to perform mine reclamation, and Mississippi Power has a contractual obligation to fund all reclamation activities. As a result of the abandonment of the Kemper IGCC, final mine reclamation began in 2018 and is expected to be substantially completed in 2020, with monitoring expected to continue through 2027. See Note 6 to the financial statements in Item 8 of the Form 10-K for additional information.

During the first quarter 2019, Mississippi Power recorded pre-tax charges to income of $2 million ($1 million after tax), primarily resulting from the abandonment and related closure activities and ongoing period costs, net of sales proceeds, for the mine and gasifier-related assets at the Kemper County energy facility. Additional closure costs for the mine and gasifier-related assets, currently estimated at up to $10 million pre-tax (excluding salvage, net of dismantlement costs), may be incurred through the first half of 2020. In addition, period costs, including, but not limited to, costs for compliance and safety, ARO accretion, and property taxes for the mine and gasifier-related assets, are estimated at $11 million for the remainder of 2019 and $2 million to $6 million annually in 2020 through 2023.

In addition, Mississippi Power constructed the CO_2 pipeline for the planned transport of captured CO_2 for use in enhanced oil recovery and is currently evaluating its options regarding the final disposition of the CO_2 pipeline, including removal of the pipeline. This evaluation is expected to be complete later in 2019. If Mississippi Power ultimately decides to remove the CO_2 pipeline, the cost of removal would have a material impact on Mississippi Power's financial statements and could have a material impact on Southern Company's financial statements.

In December 2018, Mississippi Power filed with the DOE its request for property closeout certification under the contract related to the $387 million of grants received. Mississippi Power and the DOE are currently in discussions regarding the requested closeout and property disposition, which may require payment to the DOE for a portion of certain property that is to be retained by Mississippi Power. In connection with the DOE closeout discussions, on April 29, 2019, the Civil Division of the Department of Justice informed Southern Company and Mississippi Power of an investigation related to the Kemper County energy facility. The ultimate outcome of these matters cannot be

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

determined at this time; however, they could have a material impact on Mississippi Power's and Southern Company's financial statements.

Southern Company Gas

Rate Proceedings

Nicor Gas

In November 2018, Nicor Gas filed a general base rate case with the Illinois Commission requesting a $230 million increase in annual base rate revenues. The requested increase is based on a projected test year for the 12-month period ending September 30, 2020, a ROE of 10.6%, and an increase in the equity ratio from 52% to 54% to address the negative cash flow and credit metric impacts of the Tax Reform Legislation.

On April 16, 2019, Nicor Gas entered into a stipulation agreement to resolve all related issues with the Staff of the Illinois Commission, including a ROE of 9.86% and an equity ratio of 54%. Also on April 16, 2019, Nicor Gas filed its rebuttal testimony with the Illinois Commission incorporating the stipulation agreement and addressing the remaining items outstanding with the other two intervenors. As a result of the stipulation agreement and rebuttal testimony, the revised requested annual revenue increase is $180 million.

The Illinois Commission is expected to rule on the requested increase within the statutory time limit of 11 months from the filing of the rate case, after which rate adjustments will be effective. The ultimate outcome of this matter cannot be determined at this time.

Virginia Natural Gas

In December 2018, the Virginia Commission approved Virginia Natural Gas' annual information form filing, which reduced annual base rates by $14 million effective January 1, 2019 due to lower tax expense as a result of the Tax Reform Legislation. This approval also required Virginia Natural Gas to issue customer refunds, via bill credits, for $14 million related to 2018 tax benefits deferred as a regulatory liability, current, on the balance sheet at December 31, 2018. These customer refunds were completed in the first quarter 2019.

Regulatory Infrastructure Programs

Southern Company Gas is engaged in various infrastructure programs that update or expand its gas distribution systems to improve reliability and help ensure the safety of its utility infrastructure, and recovers in rates its investment and a return associated with these infrastructure programs. In addition to capital expenditures recovered through base rates by each of the natural gas distribution utilities, Nicor Gas and Virginia Natural Gas have separate rate riders that provide for timely recovery of capital expenditures for specific infrastructure replacement programs.

Virginia Natural Gas

On April 8, 2019, Virginia Natural Gas filed an application with the Virginia Commission to amend and extend its Steps to Advance Virginia's Energy program. The proposal would allow Virginia Natural Gas to continue replacing aging pipeline infrastructure and increase its authorized investment under the currently-approved plan. Virginia Natural Gas seeks to amend its currently-approved plan by increasing the authorized investment in 2019 from $35 million to $40 million and to extend the plan for an additional five years until 2024, with proposed annual investments of $50 million in 2020, $60 million in 2021, and $70 million in each year from 2022 through 2024, for a maximum total investment over the six-year term (2019 through 2024) of $370 million. The proposed investment schedule would also allow for variances of up to $6 million in 2019, $8 million in 2020, $9 million in 2021, and $10 million in each year from 2022 through 2024, with a total potential net variance of up to $10 million allowed for the program. The Virginia Commission is expected to rule on the request in the third quarter 2019. The ultimate outcome of this matter cannot be determined at this time.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Affiliate Asset Management Agreements
On March 15, 2019, the Virginia Commission approved an extension of Virginia Natural Gas' asset management agreement with Sequent to March 31, 2021.
FERC Matters
See Note 2 to the financial statements under "FERC Matters – Open Access Transmission Tariff" in Item 8 of the Form 10-K for additional information.
On March 25, 2019, the Alabama Municipal Electric Authority and Cooperative Energy and SCS and the traditional electric operating companies filed a formal settlement agreement with the FERC agreeing to a rate reduction based on a 10.6% ROE, with a retroactive effective date of May 10, 2018, and a five-year moratorium on these parties seeking changes to the OATT formula rate. The ultimate outcome of this matter cannot be determined at this time; however, if approved by the FERC as filed, the OATT settlement would not have a material impact on the financial statements of any of the traditional electric operating companies or Southern Company.
(C) CONTINGENCIES
See Note 3 to the financial statements in Item 8 of the Form 10-K for information relating to various lawsuits and other contingencies.
General Litigation Matters
Each registrant is subject to certain claims and legal actions arising in the ordinary course of business. In addition, the business activities of Southern Company's subsidiaries are subject to extensive governmental regulation related to public health and the environment, such as laws and regulations governing air, water, land, and protection of natural resources. Litigation over environmental issues and claims of various types, including property damage, personal injury, common law nuisance, and citizen enforcement of environmental laws and regulations, has occurred throughout the U.S. This litigation has included claims for damages alleged to have been caused by CO_2 and other emissions, CCR, and alleged exposure to hazardous materials, and/or requests for injunctive relief in connection with such matters.
The ultimate outcome of such pending or potential litigation against each registrant and any subsidiaries cannot be predicted at this time; however, for current proceedings not specifically reported herein, management does not anticipate that the ultimate liabilities, if any, arising from such current proceedings would have a material effect on such registrant's financial statements.
Southern Company
In January 2017, a putative securities class action complaint was filed against Southern Company, certain of its officers, and certain former Mississippi Power officers in the U.S. District Court for the Northern District of Georgia by Monroe County Employees' Retirement System on behalf of all persons who purchased shares of Southern Company's common stock between April 25, 2012 and October 29, 2013. The complaint alleges that Southern Company, certain of its officers, and certain former Mississippi Power officers made materially false and misleading statements regarding the Kemper County energy facility in violation of certain provisions under the Securities Exchange Act of 1934, as amended. The complaint seeks, among other things, compensatory damages and litigation costs and attorneys' fees. In 2017, the plaintiffs filed an amended complaint that provided additional detail about their claims, increased the purported class period by one day, and added certain other former Mississippi Power officers as defendants. Also in 2017, the defendants filed a motion to dismiss the plaintiffs' amended complaint with prejudice, to which the plaintiffs filed an opposition. In March 2018, the court issued an order granting, in part, the defendants' motion to dismiss. The court dismissed certain claims against certain officers of Southern Company and Mississippi Power and dismissed the allegations related to a number of the statements that plaintiffs challenged as being false or misleading. In April 2018, the defendants filed a motion for reconsideration of the court's order, seeking dismissal of the remaining claims in the lawsuit. In August 2018, the court denied the motion for reconsideration and denied a motion to certify the issue for interlocutory appeal.

153

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

In February 2017, Jean Vineyard and Judy Mesirov each filed a shareholder derivative lawsuit in the U.S. District Court for the Northern District of Georgia. Each of these lawsuits names as defendants Southern Company, certain of its directors, certain of its officers, and certain former Mississippi Power officers. In 2017, these two shareholder derivative lawsuits were consolidated in the U.S. District Court for the Northern District of Georgia. The complaints allege that the defendants caused Southern Company to make false or misleading statements regarding the Kemper County energy facility cost and schedule. Further, the complaints allege that the defendants were unjustly enriched and caused the waste of corporate assets and also allege that the individual defendants violated their fiduciary duties. Each plaintiff seeks to recover, on behalf of Southern Company, unspecified actual damages and, on each plaintiff's own behalf, attorneys' fees and costs in bringing the lawsuit. Each plaintiff also seeks certain changes to Southern Company's corporate governance and internal processes. In April 2018, the court entered an order staying this lawsuit until 30 days after the resolution of any dispositive motions or any settlement, whichever is earlier, in the putative securities class action.

In May 2017, Helen E. Piper Survivor's Trust filed a shareholder derivative lawsuit in the Superior Court of Gwinnett County, Georgia that names as defendants Southern Company, certain of its directors, certain of its officers, and certain former Mississippi Power officers. The complaint alleges that the individual defendants, among other things, breached their fiduciary duties in connection with schedule delays and cost overruns associated with the construction of the Kemper County energy facility. The complaint further alleges that the individual defendants authorized or failed to correct false and misleading statements regarding the Kemper County energy facility schedule and cost and failed to implement necessary internal controls to prevent harm to Southern Company. The plaintiff seeks to recover, on behalf of Southern Company, unspecified actual damages and disgorgement of profits and, on its behalf, attorneys' fees and costs in bringing the lawsuit. The plaintiff also seeks certain unspecified changes to Southern Company's corporate governance and internal processes. In May 2018, the court entered an order staying this lawsuit until 30 days after the resolution of any dispositive motions or any settlement, whichever is earlier, in the putative securities class action.

Southern Company believes these legal challenges have no merit; however, an adverse outcome in any of these proceedings could have an impact on Southern Company's results of operations, financial condition, and liquidity. The ultimate outcome of these matters cannot be determined at this time.

Georgia Power

In 2011, plaintiffs filed a putative class action against Georgia Power in the Superior Court of Fulton County, Georgia alleging that Georgia Power's collection in rates of amounts for municipal franchise fees (which fees are paid to municipalities) exceeded the amounts allowed in orders of the Georgia PSC and alleging certain state tort law claims. In 2016, the Georgia Court of Appeals reversed the trial court's previous dismissal of the case and remanded the case to the trial court. Georgia Power filed a petition for writ of certiorari with the Georgia Supreme Court, which was granted in 2017. In June 2018, the Georgia Supreme Court affirmed the judgment of the Georgia Court of Appeals and remanded the case to the trial court for further proceedings. Following a motion by Georgia Power, on February 13, 2019, the Superior Court of Fulton County ordered the parties to submit petitions to the Georgia PSC for a declaratory ruling to address certain terms the court previously held were ambiguous as used in the Georgia PSC's orders. The order entered by the Superior Court of Fulton County also conditionally certified the proposed class. In March 2019, Georgia Power and the plaintiffs filed petitions with the Georgia PSC seeking confirmation of the proper application of the municipal franchise fee schedule pursuant to the Georgia PSC's orders. Georgia Power and the plaintiffs also have filed notices of appeal with the Georgia Court of Appeals regarding the Superior Court of Fulton County's February 2019 order. Georgia Power believes the plaintiffs' claims have no merit. The amount of any possible losses cannot be calculated at this time because, among other factors, it is unknown whether conditional class certification will be upheld and the ultimate composition of any class and whether any losses would be subject to recovery from any municipalities. The ultimate outcome of this matter cannot be determined at this time.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Mississippi Power

In May 2018, Southern Company and Mississippi Power received a notice of dispute and arbitration demand filed by Martin Product Sales, LLC (Martin) based on two agreements, both related to Kemper IGCC byproducts for which Mississippi Power provided termination notices in 2017. Martin alleges breach of contract, breach of good faith and fair dealing, fraud and misrepresentation, and civil conspiracy and makes a claim for damages in the amount of approximately $143 million, as well as additional unspecified damages, attorney's fees, costs, and interest. In the first quarter 2019, Mississippi Power and Southern Company filed motions to dismiss. Southern Company and Mississippi Power believe this legal challenge has no merit; however, an adverse outcome in this proceeding could have a material impact on Southern Company's and Mississippi Power's results of operations, financial condition, and liquidity. The ultimate outcome of this matter cannot be determined at this time.

In November 2018, Ray C. Turnage and 10 other individual plaintiffs filed a putative class action complaint against Mississippi Power and the three current members of the Mississippi PSC in the U.S. District Court for the Southern District of Mississippi. Mississippi Power received Mississippi PSC approval in 2013 to charge a mirror CWIP rate premised upon including in its rate base pre-construction and construction costs for the Kemper IGCC prior to placing the Kemper IGCC into service. The Mississippi Supreme Court reversed that approval and ordered Mississippi Power to refund the amounts paid by customers under the previously-approved mirror CWIP rate. The plaintiffs allege that the initial approval process, and the amount approved, were improper. They also allege that Mississippi Power underpaid customers in the refund process by applying an incorrect interest rate. The plaintiffs seek to recover, on behalf of themselves and their putative class, actual damages, punitive damages, pre-judgment interest, post-judgment interest, attorney's fees, and costs. In response to Mississippi Power and the Mississippi PSC each filing a motion to dismiss, the plaintiffs filed an amended complaint on March 14, 2019. The amended complaint included four additional plaintiffs and additional claims for gross negligence, reckless conduct, and intentional wrongdoing. Mississippi Power and the Mississippi PSC have each filed a motion to dismiss the amended complaint. Mississippi Power believes this legal challenge has no merit; however, an adverse outcome in this proceeding could have a material impact on Mississippi Power's results of operations, financial condition, and liquidity. The ultimate outcome of this matter cannot be determined at this time.

Southern Power

Southern Power indirectly owns a 51% membership interest in RE Roserock LLC (Roserock), the owner of the Roserock facility in Pecos County, Texas. Prior to the facility being placed in service in 2016, certain solar panels were damaged during installation by the construction contractor, McCarthy Building Companies, Inc. (McCarthy), and certain solar panels were damaged by a hail event that also occurred during construction. In connection therewith, Southern Power withheld payment of approximately $26 million to the construction contractor, which placed a lien on the Roserock facility for the same amount. In 2017, Roserock filed a lawsuit in the state district court in Pecos County, Texas against XL Insurance America, Inc. and North American Elite Insurance Company seeking recovery from an insurance policy for damages resulting from the hail event and McCarthy's installation practices. In June 2018, the court granted Roserock's motion for partial summary judgment, finding that the insurers were in breach of contract and in violation of the Texas Insurance Code for failing to pay any monies owed for the hail claim. Separate lawsuits were filed between Roserock and McCarthy, as well as other parties, and that litigation was consolidated in the U.S. District Court for the Western District of Texas. On April 18, 2019, Roserock and the parties to the state and federal lawsuits executed a settlement agreement and mutual release that resolves both lawsuits. Under the agreement, the lawsuits will be dismissed and McCarthy will release its lien following payments of all amounts (which are expected to occur in May 2019). Roserock will pay $26 million to McCarthy that was withheld and included in the original construction costs and will receive funds that will cover all related legal costs and the replacement costs of certain solar panels. In addition, during the first quarter 2019, Roserock received a partial payment of approximately $5 million in insurance proceeds toward the hail event. Any additional funds received in excess of the initial replacement costs are expected to be recognized as a gain when received by Roserock in the second quarter 2019, but are not expected to have a material impact on Southern Power's net income.

155

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Environmental Remediation

The Southern Company system must comply with environmental laws and regulations governing the handling and disposal of waste and releases of hazardous substances. Under these various laws and regulations, the Southern Company system could incur substantial costs to clean up affected sites. The traditional electric operating companies and the natural gas distribution utilities in Illinois and Georgia have each received authority from their respective state PSCs or other applicable state regulatory agencies to recover approved environmental compliance costs through regulatory mechanisms. These regulatory mechanisms are adjusted annually or as necessary within limits approved by the state PSCs or other applicable state regulatory agencies.

Georgia Power's environmental remediation liability was $18 million and $23 million as of March 31, 2019 and December 31, 2018, respectively. Georgia Power has been designated or identified as a potentially responsible party at sites governed by the Georgia Hazardous Site Response Act and/or by the federal Comprehensive Environmental Response, Compensation, and Liability Act, and assessment and potential cleanup of such sites is expected.

Southern Company Gas' environmental remediation liability was $289 million and $294 million as of March 31, 2019 and December 31, 2018, respectively, based on the estimated cost of environmental investigation and remediation associated with known current and former manufactured gas plant operating sites. These environmental remediation expenditures are recoverable from customers through rate mechanisms approved by the applicable state regulatory agencies of the natural gas distribution utilities, with the exception of one site representing $2 million of the total accrued remediation costs.

The ultimate outcome of these matters cannot be determined at this time; however, as a result of the regulatory treatment for environmental remediation expenses described above, the final disposition of these matters is not expected to have a material impact on the financial statements of Southern Company, Georgia Power, or Southern Company Gas.

Other Matters

Mississippi Power

In conjunction with Southern Company's sale of Gulf Power, Mississippi Power and Gulf Power have committed to seek a restructuring of their 50% undivided ownership interests in Plant Daniel such that each of them would, after the restructuring, own 100% of a generating unit. On January 15, 2019, Gulf Power provided notice to Mississippi Power that Gulf Power will retire its share of the generating capacity of Plant Daniel on January 15, 2024. Mississippi Power has the option to purchase Gulf Power's ownership interest for $1 on January 15, 2024, provided that Mississippi Power exercises the option no later than 120 days prior to that date. Mississippi Power is assessing the potential operational and economic effects of Gulf Power's notice. The ultimate outcome of these matters remains subject to completion of Mississippi Power's evaluations and applicable regulatory approvals, including by the FERC and the Mississippi PSC, and cannot be determined at this time. See Note (K) under "Southern Company" for information regarding the sale of Gulf Power.

(D) REVENUE FROM CONTRACTS WITH CUSTOMERS

The registrants generate revenues from a variety of sources, some of which are excluded from the scope of ASC 606, Revenue from Contracts with Customers (ASC 606), such as leases, derivatives, and certain cost recovery mechanisms. See Note 1 to the financial statements under "Recently Adopted Accounting Standards – Revenue" in Item 8 of the Form 10-K for additional information on the adoption of ASC 606 for revenue from contracts with customers and Note 1 to the financial statements under "Revenues" and "Other Taxes" in Item 8 of the Form 10-K for additional information on the revenue policies of the registrants. For additional information on revenues accounted for under other accounting guidance, see Notes (J) and (L) for energy-related derivative contracts and lessor revenues, respectively, Note 1 to the financial statements under "Revenues – Southern Company Gas" in Item 8 of the Form 10-K for alternative revenue programs at the natural gas distribution utilities, and Note 2 to the financial statements in Item 8 of the Form 10-K for cost recovery mechanisms.

156

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

The following tables disaggregate revenue sources for the three months ended March 31, 2019 and 2018:

	For the Three Months Ended March 31, 2019	For the Three Months Ended March 31, 2018
	(in millions)	
Southern Company		
Operating revenues		
Retail electric revenues[a]		
Residential	$1,288	$1,539
Commercial	1,093	1,243
Industrial	677	756
Other	26	30
Natural gas distribution revenues	1,163	1,224
Alternative revenue programs[b]	(2)	(24)
Total retail electric and gas distribution revenues	$4,245	$4,768
Wholesale energy revenues[c][d]	367	472
Wholesale capacity revenues[d]	132	151
Other natural gas revenues[e][f]	313	407
Other revenues[g]	355	574
Total operating revenues	$5,412	$6,372

(a) Retail electric revenues include $8 million and $18 million of revenues accounted for as leases for the three months ended March 31, 2019 and 2018, respectively, and a (net reduction) or net increase of $(103) million and $117 million for the three months ended March 31, 2019 and 2018, respectively, from certain cost recovery mechanisms that are not accounted for as revenue under ASC 606.

(b) Alternative revenue program revenues are presented net of any previously recognized program amounts billed to customers during the same accounting period.

(c) Wholesale energy revenues include $53 million and $93 million for the three months ended March 31, 2019 and 2018, respectively, of revenues accounted for as derivatives, primarily related to physical energy sales in the wholesale electricity market.

(d) Wholesale energy and wholesale capacity revenues include $66 million and $25 million, respectively, for the three months ended March 31, 2019 and $69 million and $30 million, respectively, for the three months ended March 31, 2018 related to PPAs accounted for as leases.

(e) Other natural gas revenues related to Southern Company Gas' energy and risk management activities are presented net of the related costs of those activities and include gross third-party revenues of $1.9 billion for each of the three months ended March 31, 2019 and 2018, of which $1.2 billion and $1.1 billion, respectively, relates to contracts that are accounted for as derivatives. See Note (M) under "Southern Company Gas" for additional information on the components of wholesale gas services operating revenues.

(f) Other natural gas revenues for the three months ended March 31, 2019 include $9 million of revenues accounted for as leases.

(g) Other revenues include $96 million and $90 million for the three months ended March 31, 2019 and 2018, respectively, of revenues not accounted for under ASC 606, including $31 million and $33 million in 2019 and 2018, respectively, accounted for as leases.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

	Alabama Power	Georgia Power	Mississippi Power
	(in millions)		
For the Three Months Ended March 31, 2019			
Operating revenues			
Retail revenues[(a)(b)]			
Residential	$540	$688	$ 60
Commercial	354	674	65
Industrial	313	289	74
Other	6	17	4
Total retail electric revenues	$1,213	$1,668	$ 203
Wholesale energy revenues[(c)]	94	18	78
Wholesale capacity revenues	27	14	1
Other revenues[(b)(d)]	74	133	5
Total operating revenues	$1,408	$1,833	$ 287
For the Three Months Ended March 31, 2018			
Operating revenues			
Retail revenues[(a)(b)]			
Residential	$570	$744	$ 60
Commercial	371	717	62
Industrial	338	316	70
Other	6	21	2
Total retail electric revenues	$1,285	$1,798	$ 194
Wholesale energy revenues[(c)]	101	40	98
Wholesale capacity revenues	24	14	4
Other revenues[(b)(d)]	63	109	6
Total operating revenues	$1,473	$1,961	$ 302

(a) Retail revenues at Alabama Power, Georgia Power, and Mississippi Power include a net increase or (net reduction) of $(57) million, $(47) million, and $1 million, respectively, for the three months ended March 31, 2019 and $47 million, $10 million, and $76 million, respectively, for the three months ended March 31, 2018 related to certain cost recovery mechanisms that are not accounted for as revenue under ASC 606.

(b) Retail revenues and other revenues at Georgia Power include $8 million and $11 million, respectively, for the three months ended March 31, 2019 and $18 million and $33 million, respectively, for the three months ended March 31, 2018 of revenues accounted for as leases.

(c) Wholesale energy revenues at Alabama Power, Georgia Power, and Mississippi Power include $3 million, $4 million, and $1 million, respectively, for the three months ended March 31, 2019 and $5 million, $7 million, and $1 million, respectively, for the three months ended March 31, 2018 accounted for as derivatives primarily related to physical energy sales in the wholesale electricity market.

(d) Other revenues at Alabama Power and Georgia Power include $28 million and $31 million, respectively, for the three months ended March 31, 2019 and $25 million and $26 million, respectively, for the three months ended March 31, 2018 of revenues not accounted for under ASC 606.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

	For the Three Months Ended March 31, 2019	For the Three Months Ended March 31, 2018
	(in millions)	
Southern Power		
PPA capacity revenues[(a)]	$127	$ 138
PPA energy revenues[(a)]	227	254
Non-PPA revenues[(b)]	85	115
Other revenues	4	2
Total operating revenues	$443	$ 509

(a) PPA capacity revenues and PPA energy revenues include $41 million and $72 million, respectively, for the three months ended March 31, 2019 and $47 million and $76 million, respectively, for the three months ended March 31, 2018 related to PPAs accounted for as leases.

(b) Non-PPA revenues include $45 million and $79 million for the three months ended March 31, 2019 and 2018, respectively, of revenues from short-term sales related to physical energy sales from uncovered capacity in the wholesale electricity market.

	For the Three Months Ended March 31, 2019	For the Three Months Ended March 31, 2018
	(in millions)	
Southern Company Gas		
Operating revenues		
Natural gas distribution revenues		
Residential	$601	$660
Commercial	170	192
Transportation	256	277
Industrial	17	17
Other	119	78
Alternative revenue programs[(a)]	(2)	(24)
Total natural gas distribution revenues	$1,161	$1,200
Gas pipeline investments[(b)]	8	8
Wholesale gas services[(c)]	66	146
Gas marketing services[(d)]	229	271
Other revenues	10	14
Total operating revenues	$1,474	$1,639

(a) Alternative revenue program revenues are presented net of any previously recognized program amounts billed to customers during the same accounting period.

(b) Revenues from gas pipeline investments include $8 million for the three months ended March 31, 2019 accounted for as leases.

(c) Wholesale gas services revenues are presented net of the related costs associated with its energy trading and risk management activities. Operating revenues, as presented, include gross third-party revenues of $1.9 billion for each of the three months ended March 31, 2019 and 2018, of which $1.2 billion and $1.1 billion, respectively, relates to contracts accounted for as derivatives. See Note (M) under "Southern Company Gas" for additional information on the components of wholesale gas services operating revenues.

(d) Gas marketing services includes $6 million and $4 million for the three months ended March 31, 2019 and 2018, respectively, of revenues not accounted for under ASC 606.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Contract Balances

The following table reflects the closing balances of receivables, contract assets, and contract liabilities related to revenues from contracts with customers as of March 31, 2019 and December 31, 2018:

	Receivables		Contract Assets		Contract Liabilities	
	March 31, 2019	December 31, 2018	March 31, 2019	December 31, 2018	March 31, 2019	December 31, 2018
	(in millions)					
Southern Company(*)	$2,522	$ 2,630	$ 84	$ 102	$ 62	$ 32
Alabama Power	514	520	1	—	10	12
Georgia Power	668	721	41	58	25	7
Mississippi Power	85	100	—	—	—	—
Southern Power	99	118	—	—	4	11
Southern Company Gas	948	952	—	—	1	2

(*) Includes amounts related to held for sale investments.

As of March 31, 2019 and December 31, 2018, Georgia Power had contract assets primarily related to unregulated service agreements where payment is contingent on project completion and fixed retail customer bill programs where the payment is contingent upon Georgia Power's continued performance and the customer's continued participation in the program over the one-year contract term. Alabama Power had contract liabilities for outstanding performance obligations primarily related to extended service agreements. Contract liabilities for Georgia Power and Southern Power relate to cash collections recognized in advance of revenue for certain unregulated service agreements and certain levelized PPAs, respectively. Southern Company's unregulated distributed generation business had $34 million and $39 million of contract assets and $25 million and $11 million of contract liabilities at March 31, 2019 and December 31, 2018, respectively, remaining for outstanding performance obligations.

The following table reflects revenue from contracts with customers recognized in the three-month period ended March 31, 2019 included in the contract liability at December 31, 2018:

	Three Months Ended March 31, 2019
	(in millions)
Southern Company	$ 17
Southern Power	10

Revenues recognized in the three-month period ended March 31, 2019, which were included in contract liabilities at December 31, 2018, were immaterial for Alabama Power, Georgia Power, and Southern Company Gas.

160

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Remaining Performance Obligations

The traditional electric operating companies and Southern Power have long-term contracts with customers in which revenues are recognized when the performance obligations are satisfied during the contract term. These contracts primarily relate to PPAs whereby the traditional electric operating companies and Southern Power provide electricity and generation capacity to a customer. The revenue recognized for the delivery of electricity is variable; however, certain PPAs include a fixed payment for fixed generation capacity over the term of the contract. Southern Company's unregulated distributed generation business also has partially satisfied performance obligations related to certain fixed price contracts. Registrants with revenues from contracts with customers related to these performance obligations remaining at March 31, 2019 expect the revenues to be recognized as follows:

	2019 (remaining)	2020	2021	2022	2023	Thereafter
	(in millions)					
Southern Company(*)	$451	$349	$315	$310	$301	$ 2,219
Alabama Power	16	22	27	23	22	140
Georgia Power	30	38	40	30	31	82
Mississippi Power	2	3	1	—	—	—
Southern Power	248	295	270	276	269	2,143

(*) Includes amounts related to held for sale investments.

(E) CONSOLIDATED ENTITIES AND EQUITY METHOD INVESTMENTS

Southern Power

Variable Interest Entities

See Note 7 to the financial statements in Item 8 of the Form 10-K for additional information on Southern Power's VIEs.

Southern Power has certain wholly-owned subsidiaries that are determined to be VIEs. Southern Power is considered the primary beneficiary of these VIEs because it controls the most significant activities of the VIEs, including operating and maintaining the respective assets, and has the obligation to absorb expected losses of these VIEs to the extent of its equity interests. Southern Power previously consolidated SP Solar and SP Wind. Southern Power continues to consolidate them following the 2018 sales of noncontrolling interests in each entity, as the primary beneficiary of each VIE, since it controls the most significant activities of each entity, including operating and maintaining their assets. Transfers and sales of the assets in the VIEs are subject to limited partner consent and the liabilities are non-recourse to the general credit of Southern Power. Liabilities consist of customary working capital items and do not include any long-term debt.

SP Solar

At March 31, 2019, SP Solar had total assets of $6.5 billion, total liabilities of $373 million, and noncontrolling interests of $1.2 billion. Cash distributions from SP Solar are allocated 67% to Southern Power and 33% to Global Atlantic in accordance with their partnership interest percentage. Under the terms of the limited partnership agreement, distributions without limited partner consent are limited to available cash and SP Solar is obligated to distribute all such available cash to its partners each quarter. Available cash includes all cash generated in the quarter subject to the maintenance of appropriate operating reserves.

SP Wind

At March 31, 2019, SP Wind had total assets of $2.6 billion, total liabilities of $141 million, and noncontrolling interests of $46 million. Under the terms of the limited liability agreement, distributions without Class A member consent are limited to available cash and SP Wind is obligated to distribute all such available cash to its members

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

each quarter. Available cash includes all cash generated in the quarter subject to the maintenance of appropriate operating reserves. Cash distributions from SP Wind are generally allocated 60% to Southern Power and 40% to the three financial investors in accordance with the limited liability agreement.

Southern Company Gas

See Note 7 to the financial statements in Item 8 of the Form 10-K for additional information on Southern Company Gas' equity method investments.

Equity Method Investments

The carrying amounts of Southern Company Gas' equity method investments as of March 31, 2019 and December 31, 2018 and related income from those investments for the three-month periods ended March 31, 2019 and 2018 were as follows:

Investment Balance	March 31, 2019	December 31, 2018
	(in millions)	
SNG	$1,262	$ 1,261
Atlantic Coast Pipeline	96	83
PennEast Pipeline	75	71
Other	124	123
Total	$1,557	$ 1,538

Earnings from Equity Method Investments	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
	(in millions)	
SNG	$ 42	$ 39
Atlantic Coast Pipeline	3	1
PennEast Pipeline	2	1
Other	1	1
Total	$ 48	$ 42

SNG

Selected financial information of SNG for the three months ended March 31, 2019 and 2018 is as follows:

Income Statement Information	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
	(in millions)	
Revenues	$166	$ 160
Operating income	106	99
Net income	84	78

(F) FINANCING

Bank Credit Arrangements

Bank credit arrangements provide liquidity support to the registrants' commercial paper borrowings and the traditional electric operating companies' revenue bonds. The amount of variable rate revenue bonds of the traditional electric operating companies outstanding requiring liquidity support as of March 31, 2019 was approximately $1.4 billion (comprised of approximately $854 million at Alabama Power, $550 million at Georgia

162

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Power, and $40 million at Mississippi Power). In addition, at March 31, 2019, the traditional electric operating companies had approximately $432 million (comprised of approximately $87 million at Alabama Power and $345 million at Georgia Power) of revenue bonds outstanding that were required to be remarketed within the next 12 months. Subsequent to March 31, 2019, Georgia Power purchased and held approximately $115 million of outstanding pollution control revenue bonds required to be remarketed. See Note 8 to the financial statements under "Bank Credit Arrangements" in Item 8 of the Form 10-K and "Financing Activities" herein for additional information.
The following table outlines the committed credit arrangements by company as of March 31, 2019:

Company	Expires 2019	2020	2022	Total	Unused[(d)]
	(in millions)				
Southern Company[(a)]	$—	$—	$2,000	$2,000	$ 1,999
Alabama Power	33	500	800	1,333	1,333
Georgia Power	—	—	1,750	1,750	1,736
Mississippi Power	100	—	—	100	100
Southern Power[(b)]	—	—	750	750	741
Southern Company Gas[(c)]	—	—	1,900	1,900	1,895
Other	30	—	—	30	30
Southern Company Consolidated	$163	$500	$7,200	$7,863	$ 7,834

(a) Represents the Southern Company parent entity.
(b) Does not include Southern Power Company's $120 million continuing letter of credit facility for standby letters of credit expiring in 2021, of which $24 million was unused at March 31, 2019. Southern Power's subsidiaries are not parties to its bank credit arrangement.
(c) Southern Company Gas, as the parent entity, guarantees the obligations of Southern Company Gas Capital, which is the borrower of $1.4 billion of this arrangement. Southern Company Gas' committed credit arrangement also includes $500 million for which Nicor Gas is the borrower and which is restricted for working capital needs of Nicor Gas. Pursuant to this multi-year credit arrangement, the allocations between Southern Company Gas Capital and Nicor Gas may be adjusted.
(d) Amounts used are for letters of credit.

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

DOE Loan Guarantee Borrowings

See Note 8 to the financial statements under "Long-term Debt – DOE Loan Guarantee Borrowings" in Item 8 of the Form 10-K for additional information regarding Georgia Power's 2014 loan guarantee agreement.
Pursuant to the loan guarantee program established under Title XVII of the Energy Policy Act of 2005 (Title XVII Loan Guarantee Program), Georgia Power and the DOE entered into a loan guarantee agreement in 2014 and the Amended and Restated Loan Guarantee Agreement in March 2019. Under the Amended and Restated Loan Guarantee Agreement, the DOE has agreed to guarantee the obligations of Georgia Power under note purchase agreements among the DOE, Georgia Power, and the FFB and related promissory notes which provide for two multi-advance term loan facilities (FFB Credit Facilities). Under the FFB Credit Facilities, Georgia Power may make term loan borrowings through the FFB in an amount up to approximately $5.130 billion, provided that total aggregate borrowings under the FFB Credit Facilities may not exceed 70% of (i) Eligible Project Costs minus (ii) approximately $1.492 billion (reflecting the amounts received by Georgia Power under the Guarantee Settlement Agreement less the Customer Refunds).
In March 2019, Georgia Power made borrowings under the FFB Credit Facilities in an aggregate principal amount of $835 million at an interest rate of 3.213% through the final maturity date of February 20, 2044. At March 31, 2019,

Georgia Power had a total of $3.46 billion of borrowings outstanding under the FFB Credit Facilities.

163

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

All borrowings under the FFB Credit Facilities are full recourse to Georgia Power, and Georgia Power is obligated to reimburse the DOE for any payments the DOE is required to make to the FFB under its guarantee. Georgia Power's reimbursement obligations to the DOE are full recourse and secured by a first priority lien on (i) Georgia Power's 45.7% undivided ownership interest in Plant Vogtle Units 3 and 4 (primarily the units under construction, the related real property, and any nuclear fuel loaded in the reactor core) and (ii) Georgia Power's rights and obligations under the principal contracts relating to Plant Vogtle Units 3 and 4. There are no restrictions on Georgia Power's ability to grant liens on other property.

In addition to the conditions described above, future advances are subject to satisfaction of customary conditions, as well as certification of compliance with the requirements of the Title XVII Loan Guarantee Program, including accuracy of project-related representations and warranties, delivery of updated project-related information, and evidence of compliance with the prevailing wage requirements of the Davis-Bacon Act of 1931, as amended, and certification from the DOE's consulting engineer that proceeds of the advances are used to reimburse Eligible Project Costs.

Upon satisfaction of all conditions described above, advances may be requested on a quarterly basis through 2023. The final maturity date for each advance under the FFB Credit Facilities is February 20, 2044. Interest is payable quarterly and principal payments will begin on February 20, 2020. Borrowings under the FFB Credit Facilities will bear interest at the applicable U.S. Treasury rate plus a spread equal to 0.375%.

Under the Amended and Restated Loan Guarantee Agreement, Georgia Power is subject to customary borrower affirmative and negative covenants and events of default. In addition, Georgia Power is subject to project-related reporting requirements and other project-specific covenants and events of default.

In the event certain mandatory prepayment events occur, the FFB's commitment to make further advances under the FFB Credit Facilities will terminate and Georgia Power will be required to prepay the outstanding principal amount of all borrowings under the FFB Credit Facilities over a period of five years (with level principal amortization). Among other things, these mandatory prepayment events include (i) the termination of the Vogtle Services Agreement or rejection of the Vogtle Services Agreement in any Westinghouse bankruptcy if Georgia Power does not maintain access to intellectual property rights under the related intellectual property licenses; (ii) termination of the Bechtel Agreement, unless the Vogtle Owners enter into a replacement agreement; (iii) cancellation of Plant Vogtle Units 3 and 4 by the Georgia PSC or by Georgia Power; (iv) failure of the holders of 90% of the ownership interests in Plant Vogtle Units 3 and 4 to vote to continue construction following certain schedule extensions; (v) cost disallowances by the Georgia PSC that could have a material adverse effect on completion of Plant Vogtle Units 3 and 4 or Georgia Power's ability to repay the outstanding borrowings under the FFB Credit Facilities; or (vi) loss of or failure to receive necessary regulatory approvals. Under certain circumstances, insurance proceeds and any proceeds from an event of taking must be applied to immediately prepay outstanding borrowings under the FFB Credit Facilities. In addition, if Georgia Power discontinues construction of Plant Vogtle Units 3 and 4, Georgia Power would be obligated to immediately repay a portion of the outstanding borrowings under the FFB Credit Facilities to the extent such outstanding borrowings exceed 70% of Eligible Project Costs, net of the proceeds received by Georgia Power under the Guarantee Settlement Agreement less the Customer Refunds. Georgia Power also may voluntarily prepay outstanding borrowings under the FFB Credit Facilities. Under the FFB Credit Facilities, any prepayment (whether mandatory or optional) will be made with a make-whole premium or discount, as applicable.

In connection with any cancellation of Plant Vogtle Units 3 and 4, the DOE may elect to continue construction of Plant Vogtle Units 3 and 4. In such an event, the DOE will have the right to assume Georgia Power's rights and obligations under the principal agreements relating to Plant Vogtle Units 3 and 4 and to acquire all or a portion of Georgia Power's ownership interest in Plant Vogtle Units 3 and 4.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Financing Activities

The following table outlines the long-term debt financing activities for Southern Company and its subsidiaries for the first three months of 2019:

Company	Senior Note Maturities, Redemptions, and Repurchases	Revenue Bond Issuances and Reofferings of Purchased Bonds	Revenue Bond Maturities, Redemptions, and Repurchases	Other Long-Term Debt Issuances	Other Long-Term Debt Redemptions and Maturities[(a)]
	(in millions)				
Southern Company[(b)]	$2,100	$ —	$ —	$ —	$ —
Alabama Power	200	—	—	—	—
Georgia Power	—	343	108	835	2
Mississippi Power	—	43	—	—	—
Other	—	—	—	—	19
Southern Company Consolidated	$2,300	$ 386	$ 108	$ 835	$ 21

(a) Includes reductions in finance lease obligations resulting from cash payments under finance leases.
(b) Represents the Southern Company parent entity.

Except as otherwise described herein, Southern Company and its subsidiaries used the proceeds of debt issuances for their redemptions and maturities shown in the table above, to repay short-term indebtedness, and for general corporate purposes, including working capital. The subsidiaries also used the proceeds for their construction programs.

Southern Company

In January 2019, Southern Company repaid a $250 million short-term uncommitted bank credit arrangement and a $1.5 billion short-term floating rate bank loan.

Also in January 2019, through cash tender offers, Southern Company repurchased and retired approximately $522 million of the $1.0 billion aggregate principal amount outstanding of its 1.85% Senior Notes due July 1, 2019 (1.85% Notes), approximately $180 million of the $350 million aggregate principal amount outstanding of its Series 2014B 2.15% Senior Notes due September 1, 2019 (Series 2014B Notes), and approximately $504 million of the $750 million aggregate principal amount outstanding of its Series 2018A Floating Rate Notes due February 14, 2020 (Series 2018A Notes), for an aggregate purchase price, excluding accrued and unpaid interest, of approximately $1.2 billion. In addition, following the completion of the cash tender offers, in February 2019, Southern Company completed the redemption of all of the Series 2018A Notes, 1.85% Notes, and Series 2014B Notes remaining outstanding.

Georgia Power

In January 2019, Georgia Power redeemed approximately $13 million, $20 million, and $75 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), First Series 1992, Eighth Series 1994, and Second Series 1995, respectively.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

In March 2019, Georgia Power reoffered to the public the following pollution control revenue bonds that previously had been purchased and held by Georgia Power:

- $173 million aggregate principal amount of Development Authority of Bartow County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Bowen Project), First Series 2009;
- approximately $105 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), First Series 2013; and
- $65 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Second Series 2008.

Subsequent to March 31, 2019, Georgia Power purchased and held the following pollution control revenue bonds, which may be reoffered to the public at a later date:

- $55 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Fourth Series 1994;
- $30 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Fourth Series 1995;
- $20 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Ninth Series 1994; and
- $10 million aggregate principal amount of Development Authority of Burke County (Georgia) Pollution Control Revenue Bonds (Georgia Power Company Plant Vogtle Project), Second Series 1994.

Mississippi Power

In March 2019, Mississippi Power reoffered to the public $43 million of Mississippi Business Finance Corporation Pollution Control Revenue Refunding Bonds, Series 2002, that previously had been purchased and held by Mississippi Power.

Earnings per Share

For Southern Company, the only difference in computing basic and diluted earnings per share is attributable to awards outstanding under stock-based compensation plans. See Note 12 to the financial statements in Item 8 of the Form 10-K for information on stock-based compensation plans. The effect of stock-based compensation plans was determined using the treasury stock method. Shares used to compute diluted earnings per share were as follows:

	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
	(in millions)	
As reported shares	1,038	1,011
Effect of stock-based compensation	7	5
Diluted shares	1,045	1,016

There were no stock-based compensation awards that were not included in the diluted earnings per share calculation because they were anti-dilutive for the three months ended March 31, 2019 and an immaterial amount of such awards was not included for the three months ended March 31, 2018.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

(G) INCOME TAXES

See Note 10 to the financial statements in Item 8 of the Form 10-K for additional tax information.

Effective Tax Rate

Details of significant changes in the effective tax rate for the applicable registrants are provided herein.

Southern Company

Southern Company's effective tax rate is typically lower than the statutory rate due to employee stock plans' dividend deduction, non-taxable AFUDC equity and flowback of excess deferred income taxes at the regulated utilities, and federal income tax benefits from ITCs and PTCs, primarily at Southern Power.

Southern Company's effective tax rate was 39.8% for the three months ended March 31, 2019 compared to 10.8% for the corresponding period in 2018. The effective tax rate increase was primarily due to the tax impact from the sale of Gulf Power. See Note (K) for additional information.

Alabama Power

Alabama Power's effective tax rate was 21.9% for the three months ended March 31, 2019 compared to 26.3% for the corresponding period in 2018. The effective tax rate decrease was primarily due to the application in 2018 of the accounting order approved by the Alabama PSC in May 2018 related to the Tax Reform Legislation. See Note 2 to the financial statements under "Alabama Power – Tax Reform Accounting Order" in Item 8 of the Form 10-K for additional information.

Mississippi Power

Mississippi Power's effective tax rate was 15.5% for the three months ended March 31, 2019 compared to a benefit rate of (34.7)% for the corresponding period in 2018. The effective tax rate increase was primarily due to lower estimated losses on the Kemper IGCC in 2019, partially offset by an increase in the flowback of excess deferred income taxes as a result of a settlement agreement reached with wholesale customers under the MRA tariff. See Note (B) under "Mississippi Power" for additional information.

Southern Power

Southern Power's effective tax benefit rate was (49.8)% for the three months ended March 31, 2019 compared to (647.0)% for the corresponding period in 2018. The effective tax benefit rate decrease was primarily due to changes in state apportionment rates following the reorganization of Southern Power's legal entities that own and operate certain solar facilities and a reduction of tax benefits from wind PTCs primarily as a result of the sale of a noncontrolling tax equity interest in SP Wind.

Southern Company Gas

Southern Company Gas' effective tax rate was 22.3% for the three months ended March 31, 2019 compared to 27.2% for the corresponding period in 2018. This decrease was primarily related to tax impacts of the goodwill impairment charge recorded in the first quarter 2018 and an increase in the flowback of excess deferred income taxes in 2019 primarily at Atlanta Gas Light as previously authorized by the Georgia PSC. See Note 2 to the financial statements under "Southern Company Gas – Rate Proceedings" in Item 8 of the Form 10-K for additional information.

(H) RETIREMENT BENEFITS

The Southern Company system has a qualified defined benefit, trusteed, pension plan covering substantially all employees, with the exception of employees at PowerSecure. The qualified pension plan is funded in accordance with requirements of the Employee Retirement Income Security Act of 1974, as amended (ERISA). No mandatory contributions to the qualified pension plan are anticipated for the year ending December 31, 2019. The Southern

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Company system also provides certain non-qualified defined benefits for a select group of management and highly compensated employees, which are funded on a cash basis. In addition, the Southern Company system provides certain medical care and life insurance benefits for retired employees through other postretirement benefit plans. The traditional electric operating companies fund other postretirement trusts to the extent required by their respective regulatory commissions. Southern Company Gas has a separate unfunded supplemental retirement health care plan that provides medical care and life insurance benefits to employees of discontinued businesses.
See Note 11 to the financial statements in Item 8 of the Form 10-K for additional information.
Components of the net periodic benefit costs for the three months ended March 31, 2019 and 2018 are presented in the following tables.

Three Months Ended March 31, 2019	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)					
Pension Plans						
Service cost	$73	$ 17	$ 19	$ 3	$ 2	$ 6
Interest cost	123	28	39	6	1	9
Expected return on plan assets	(221)	(51)	(73)	(10)	(2)	(15)
Amortization:						
Prior service costs	—	—	—	—	—	(1)
Regulatory asset	—	—	—	—	—	3
Net (gain)/loss	30	9	11	1	—	1
Net periodic pension cost (income)	$5	$ 3	$ (4)	$ —	$ 1	$ 3
Postretirement Benefits						
Service cost	$5	$ 1	$ 1	$ —	$ —	$ 1
Interest cost	17	4	7	1	—	2
Expected return on plan assets	(16)	(6)	(6)	—	—	(2)
Amortization:						
Prior service costs	1	1	—	—	—	—
Regulatory asset	—	—	—	—	—	2
Net (gain)/loss	(1)	—	—	—	—	(1)
Net periodic postretirement benefit cost	$6	$ —	$ 2	$ 1	$ —	$ 2

168

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Three Months Ended March 31, 2018	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)					
Pension Plans						
Service cost	$90	$ 19	$ 22	$ 4	$ 2	$ 8
Interest cost	116	25	35	5	1	10
Expected return on plan assets	(236)	(51)	(74)	(10)	(3)	(18)
Amortization:						
Prior service costs	1	—	—	—	—	(1)
Regulatory asset	—	—	—	—	—	3
Net (gain)/loss	53	14	17	3	1	3
Net periodic pension cost (income)	$24	$ 7	$ —	$ 2	$ 1	$ 5
Postretirement Benefits						
Service cost	$6	$ 1	$ 2	$ —	$ —	$ 1
Interest cost	19	4	7	1	—	2
Expected return on plan assets	(17)	(6)	(6)	—	—	(2)
Amortization:						
Prior service costs	2	1	—	—	—	—
Regulatory asset	—	—	—	—	—	1
Net (gain)/loss	3	—	2	—	—	—
Net periodic postretirement benefit cost	$13	$ —	$ 5	$ 1	$ —	$ 2

169

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

(I) FAIR VALUE MEASUREMENTS
As of March 31, 2019, assets and liabilities measured at fair value on a recurring basis during the period, together with their associated level of the fair value hierarchy, were as follows:

As of March 31, 2019:	Fair Value Measurements Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Net Asset Value as a Practical Expedient (NAV)	Total
	(in millions)				
Southern Company					
Assets:					
Energy-related derivatives[a][b]	$322	$ 128	$ 4	$ —	$454
Foreign currency derivatives	—	38	—	—	38
Investments in trusts:[c][d]					
Domestic equity	682	120	—	—	802
Foreign equity	60	195	—	—	255
U.S. Treasury and government agency securities	—	283	—	—	283
Municipal bonds	—	73	—	—	73
Pooled funds – fixed income	—	14	—	—	14
Corporate bonds	24	298	—	—	322
Mortgage and asset backed securities	—	72	—	—	72
Private equity	—	—	—	48	48
Cash and cash equivalents	1	—	—	—	1
Other	28	4	—	—	32
Cash equivalents	907	3	—	—	910
Other investments	9	14	—	—	23
Total	$2,033	$ 1,242	$ 4	$ 48	$3,327
Liabilities:					
Energy-related derivatives[a][b]	$466	$ 106	$ 23	$ —	$595
Interest rate derivatives	—	35	—	—	35
Foreign currency derivatives	—	24	—	—	24
Contingent consideration	—	—	21	—	21
Total	$466	$ 165	$ 44	$ —	$675

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

As of March 31, 2019:	Fair Value Measurements Using: Quoted Prices in Active Markets for Identical Assets (Level 1) (in millions)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Net Asset Value as a Practical Expedient (NAV)	Total
Alabama Power					
Assets:					
Energy-related derivatives	$—	$ 6	$ —	$ —	$6
Nuclear decommissioning trusts:(c)					
Domestic equity	446	108	—	—	554
Foreign equity	60	57	—	—	117
U.S. Treasury and government agency securities	—	18	—	—	18
Municipal bonds	—	1	—	—	1
Corporate bonds	24	139	—	—	163
Mortgage and asset backed securities	—	24	—	—	24
Private equity	—	—	—	48	48
Other	5	—	—	—	5
Cash equivalents	569	3	—	—	572
Other investments	—	14	—	—	14
Total	$1,104	$ 370	$ —	$ 48	$1,522
Liabilities:					
Energy-related derivatives	$—	$ 7	$ —	$ —	$7
Georgia Power					
Assets:					
Energy-related derivatives	$—	$ 9	$ —	$ —	$9
Nuclear decommissioning trusts:(c)(d)					
Domestic equity	236	1	—	—	237
Foreign equity	—	134	—	—	134
U.S. Treasury and government agency securities	—	265	—	—	265
Municipal bonds	—	72	—	—	72
Corporate bonds	—	160	—	—	160
Mortgage and asset backed securities	—	47	—	—	47
Other	23	4	—	—	27
Total	$259	$ 692	$ —	$ —	$951
Liabilities:					
Energy-related derivatives	$—	$ 16	$ —	$ —	$16
Interest rate derivatives	—	2	—	—	2
Total	$—	$ 18	$ —	$ —	$18

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

As of March 31, 2019:	Fair Value Measurements Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Net Asset Value as a Practical Expedient (NAV)	Total
	(in millions)				
Mississippi Power					
Assets:					
Energy-related derivatives	$—	$ 3	$ —	$ —	$3
Cash equivalents	202	—	—	—	202
Total	$202	$ 3	$ —	$ —	$205
Liabilities:					
Energy-related derivatives	$—	$ 6	$ —	$ —	$6
Southern Power					
Assets:					
Energy-related derivatives	$—	$ 1	$ —	$ —	$1
Foreign currency derivatives	—	38	—	—	38
Cash equivalents	10	—	—	—	10
Total	$10	$ 39	$ —	$ —	$49
Liabilities:					
Energy-related derivatives	$—	$ 3	$ —	$ —	$3
Foreign currency derivatives	—	24	—	—	24
Contingent consideration	—	—	21	—	21
Total	$—	$ 27	$ 21	$ —	$48
Southern Company Gas					
Assets:					
Energy-related derivatives(a)(b)	$322	$ 108	$ 4	$ —	$434
Non-qualified deferred compensation trusts:					
Domestic equity	—	11	—	—	11
Foreign equity	—	4	—	—	4
Pooled funds – fixed income	—	14	—	—	14
Cash equivalents	1	—	—	—	1
Cash equivalents	13	—	—	—	13
Total	$336	$ 137	$ 4	$ —	$477
Liabilities:					
Energy-related derivatives(a)(b)	$466	$ 73	$ 23	$ —	$562

(a) Energy-related derivatives exclude $11 million associated with premiums and certain weather derivatives accounted for based on intrinsic value rather than fair value.

(b) Energy-related derivatives exclude cash collateral of $190 million.

(c) Excludes receivables related to investment income, pending investment sales, payables related to pending investment purchases, and currencies. See Note 6 to the financial statements in Item 8 of the Form 10-K for additional information.

(d) Includes investment securities pledged to creditors and collateral received and excludes payables related to the securities lending program. As of March 31, 2019, approximately $72 million of the fair market value of Georgia Power's nuclear decommissioning trust funds' securities were on loan to creditors under the funds' managers' securities lending program. See Note 6 to the financial statements in Item 8 of the Form 10-K for additional information.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Southern Company, Alabama Power, and Georgia Power continue to elect the option to fair value investment securities held in the nuclear decommissioning trust funds. The fair value of the funds, including reinvested interest and dividends and excluding the funds' expenses, increased for the three months ended March 31, 2019 and decreased for the three months ended March 31, 2018 by the amounts shown in the table below. The changes were recorded as a change to the regulatory assets and liabilities related to AROs for Georgia Power and Alabama Power, respectively.

	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
	(in millions)	
Southern Company	$152	$ (11)
Alabama Power	87	(5)
Georgia Power	65	(6)

Valuation Methodologies

The energy-related derivatives primarily consist of exchange-traded and over-the-counter financial products for natural gas and physical power products, including, from time to time, basis swaps. These are standard products used within the energy industry and are valued using the market approach. The inputs used are mainly from observable market sources, such as forward natural gas prices, power prices, implied volatility, and overnight index swap interest rates. Interest rate derivatives are also standard over-the-counter products that are valued using observable market data and assumptions commonly used by market participants. The fair value of interest rate derivatives reflects the net present value of expected payments and receipts under the swap agreement based on the market's expectation of future interest rates. Additional inputs to the net present value calculation may include the contract terms, counterparty credit risk, and occasionally, implied volatility of interest rate options. The fair value of cross-currency swaps reflects the net present value of expected payments and receipts under the swap agreement based on the market's expectation of future foreign currency exchange rates. Additional inputs to the net present value calculation may include the contract terms, counterparty credit risk, and discount rates. The interest rate derivatives and cross-currency swaps are categorized as Level 2 under Fair Value Measurements as these inputs are based on observable data and valuations of similar instruments. See Note (J) for additional information on how these derivatives are used.

For fair value measurements of the investments within the nuclear decommissioning trusts and the non-qualified deferred compensation trusts, external pricing vendors are designated for each asset class with each security specifically assigned a primary pricing source. For investments held within commingled funds, fair value is determined at the end of each business day through the net asset value, which is established by obtaining the underlying securities' individual prices from the primary pricing source. A market price secured from the primary source vendor is then evaluated by management in its valuation of the assets within the trusts. As a general approach, fixed income market pricing vendors gather market data (including indices and market research reports) and integrate relative credit information, observed market movements, and sector news into proprietary pricing models, pricing systems, and mathematical tools. Dealer quotes and other market information, including live trading levels and pricing analysts' judgments, are also obtained when available.

The NRC requires licensees of commissioned nuclear power reactors to establish a plan for providing reasonable assurance of funds for future decommissioning. See Note 6 to the financial statements under "Nuclear Decommissioning" in Item 8 of the Form 10-K for additional information.

Southern Power has contingent payment obligations related to certain acquisitions whereby Southern Power is primarily obligated to make generation-based payments to the seller, which commenced at the commercial operation of the respective facility and continue through 2026. The obligation is categorized as Level 3 under Fair Value

Measurements as the fair value is determined using significant unobservable inputs for the forecasted facility generation in MW-hours, as well as other inputs such as a fixed dollar amount per MW-hour, and a discount rate.

173

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

The fair value of contingent consideration reflects the net present value of expected payments and any periodic change arising from forecasted generation is expected to be immaterial.

As of March 31, 2019, the fair value measurements of private equity investments held in Alabama Power's nuclear decommissioning trusts that are calculated at net asset value per share (or its equivalent) as a practical expedient totaled $48 million and unfunded commitments related to the private equity investments totaled $49 million. Private equity funds include funds-of-funds that invest in high-quality private equity funds across several market sectors, funds that invest in real estate assets, and a fund that acquires companies to create resale value. Private equity funds do not have redemption rights. Distributions from these funds will be received as the underlying investments in the funds are liquidated.

As of March 31, 2019, other financial instruments for which the carrying amount did not equal fair value were as follows:

	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas(*)
	(in millions)					
Long-term debt, including securities due within one year:						
Carrying amount	$42,535	$ 7,921	$10,910	$ 1,619	$ 4,995	$ 5,928
Fair value	43,910	8,424	11,249	1,619	5,131	6,176

(*) The long-term debt of Southern Company Gas is recorded at amortized cost, including the fair value adjustments at the effective date of the Merger. Southern Company Gas amortizes the fair value adjustments over the lives of the respective bonds.

The fair values are determined using Level 2 measurements and are based on quoted market prices for the same or similar issues or on the current rates available to Southern Company, Alabama Power, Georgia Power, Mississippi Power, Southern Power, and Southern Company Gas.

Commodity Contracts with Level 3 Valuation Inputs

As of March 31, 2019, the fair value of Southern Company Gas' Level 3 physical natural gas forward contracts was $19 million. Since commodity contracts classified as Level 3 typically include a combination of observable and unobservable components, the changes in fair value may include amounts due in part to observable market factors, or changes to assumptions on the unobservable components. The following table includes transfers to Level 3, which represent the fair value of Southern Company Gas' commodity derivative contracts that include a significant unobservable component for the first time during the period.

	Three Months Ended March 31, 2019
	(in millions)
Beginning balance	$ —
Transfers to Level 3	(30)
Changes in fair value	11
Ending balance	$ (19)

Changes in fair value of Level 3 instruments represent changes in gains and losses for the periods that are reported on Southern Company Gas' statements of income in natural gas revenues.

The valuation of certain commodity contracts requires the use of certain unobservable inputs. All forward pricing used in the valuation of such contracts is directly based on third-party market data, such as broker quotes and exchange settlements, when that data is available. If third-party market data is not available, then industry standard methodologies are used to develop inputs that maximize the use of relevant observable inputs and minimize the use of unobservable inputs. Observable inputs, including some forward prices used for determining fair value, reflect the best available market information. Unobservable inputs are updated using industry standard techniques such as extrapolation, combining observable forward inputs supplemented by historical market and other relevant data. Level 3 physical natural gas forward contracts include unobservable forward price inputs (ranging from $0.07 to $1.15 per mmBtu). Forward price increases (decreases) as of March 31, 2019 would have resulted in higher (lower) values on a net basis.

(J) DERIVATIVES

Southern Company, the traditional electric operating companies, Southern Power, and Southern Company Gas are exposed to market risks, including commodity price risk, interest rate risk, weather risk, and occasionally foreign currency exchange rate risk. To manage the volatility attributable to these exposures, each company nets its exposures, where possible, to take advantage of natural offsets and enters into various derivative transactions for the remaining exposures pursuant to each company's policies in areas such as counterparty exposure and risk management practices. Southern Company Gas' wholesale gas operations use various contracts in its commercial activities that generally meet the definition of derivatives. For the traditional electric operating companies, Southern Power, and Southern Company Gas' other businesses, each company's policy is that derivatives are to be used primarily for hedging purposes and mandates strict adherence to all applicable risk management policies. Derivative positions are monitored using techniques including, but not limited to, market valuation, value at risk, stress testing, and sensitivity analysis. Derivative instruments are recognized at fair value in the balance sheets as either assets or liabilities and are presented on a net basis. See Note (I) for additional fair value information. In the statements of cash flows, any cash impacts of settled energy-related and interest rate derivatives are recorded as operating activities. Any cash impacts of settled foreign currency derivatives are classified as operating or financing activities to correspond with classification of the hedged interest or principal, respectively. See Note 1 to the financial statements under "Financial Instruments" in Item 8 of the Form 10-K for additional information.

Energy-Related Derivatives

The traditional electric operating companies, Southern Power, and Southern Company Gas enter into energy-related derivatives to hedge exposures to electricity, natural gas, and other fuel price changes. However, due to cost-based rate regulations and other various cost recovery mechanisms, the traditional electric operating companies and the natural gas distribution utilities have limited exposure to market volatility in energy-related commodity prices. Each of the traditional electric operating companies and certain of the natural gas distribution utilities of Southern Company Gas manage fuel-hedging programs, implemented per the guidelines of their respective state PSCs or other applicable state regulatory agencies, through the use of financial derivative contracts, which are expected to continue to mitigate price volatility. The traditional electric operating companies (with respect to wholesale generating capacity) and Southern Power have limited exposure to market volatility in energy-related commodity prices because their long-term sales contracts shift substantially all fuel cost responsibility to the purchaser. However, the traditional electric operating companies and Southern Power may be exposed to market volatility in energy-related commodity prices to the extent any uncontracted capacity is used to sell electricity. Southern Company Gas retains exposure to price changes that can, in a volatile energy market, be material and can adversely affect its results of operations. Southern Company Gas also enters into weather derivative contracts as economic hedges of operating margins in the event of warmer-than-normal weather. Exchange-traded options are carried at fair value, with changes reflected in operating revenues. Non-exchange-traded options are accounted for using the intrinsic value method. Changes in the intrinsic value for non-exchange-traded contracts are reflected in operating revenues.

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

- Regulatory Hedges — Energy-related derivative contracts designated as regulatory hedges relate primarily to the traditional electric operating companies' and the natural gas distribution utilities' fuel-hedging programs, where gains and losses are initially recorded as regulatory liabilities and assets, respectively, and then are included in fuel expense as the underlying fuel is used in operations and ultimately recovered through the respective fuel cost recovery clauses.
- Cash Flow Hedges — Gains and losses on energy-related derivatives designated as cash flow hedges (which are mainly used to hedge anticipated purchases and sales) are initially deferred in accumulated OCI before being recognized in the statements of income in the same period and in the same income statement line item as the earnings effect of the hedged transactions.
- Not Designated — Gains and losses on energy-related derivative contracts that are not designated or fail to qualify as hedges are recognized in the statements of income as incurred.

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

At March 31, 2019, the net volume of energy-related derivative contracts for natural gas positions, together with the longest hedge date over which the respective entity is hedging its exposure to the variability in future cash flows for forecasted transactions and the longest non-hedge date for derivatives not designated as hedges, were as follows:

	Net Purchased mmBtu (in millions)	Longest Hedge Date	Longest Non-Hedge Date
Southern Company(*)	538	2022	2029
Alabama Power	72	2022	—
Georgia Power	153	2022	—
Mississippi Power	61	2022	—
Southern Power	9	2020	—
Southern Company Gas(*)	243	2021	2029

(*) Southern Company Gas' derivative instruments include both long and short natural gas positions. A long position is a contract to purchase natural gas and a short position is a contract to sell natural gas. Southern Company Gas' volume represents the net of long natural gas positions of 3.8 billion mmBtu and short natural gas positions of 3.6 billion mmBtu as of March 31, 2019, which is also included in Southern Company's total volume.

In addition to the volumes discussed above, the traditional electric operating companies and Southern Power enter into physical natural gas supply contracts that provide the option to sell back excess natural gas due to operational constraints. The maximum expected volume of natural gas subject to such a feature is 40 million mmBtu for Southern Company, which includes 6 million mmBtu for Alabama Power, 12 million mmBtu for Georgia Power, 5 million mmBtu for Mississippi Power, and 13 million mmBtu for Southern Power.

For cash flow hedges of energy-related derivatives, the estimated pre-tax gains (losses) expected to be reclassified from accumulated OCI to earnings for the next 12-month period ending March 31, 2020 are immaterial for all registrants.

Interest Rate Derivatives

Southern Company and certain subsidiaries may enter into interest rate derivatives to hedge exposure to changes in interest rates. The derivatives employed as hedging instruments are structured to minimize ineffectiveness. Derivatives related to existing variable rate securities or forecasted transactions are accounted for as cash flow

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

hedges where the derivatives' fair value gains or losses are recorded in OCI and are reclassified into earnings at the same time and presented on the same income statement line item as the earnings effect of the hedged transactions. Derivatives related to existing fixed rate securities are accounted for as fair value hedges, where the derivatives' fair value gains or losses and hedged items' fair value gains or losses are both recorded directly to earnings on the same income statement line item. Fair value gains or losses on derivatives that are not designated or fail to qualify as hedges are recognized in the statements of income as incurred.

At March 31, 2019, the following interest rate derivatives were outstanding:

	Notional Amount (in millions)	Interest Rate Received	Weighted Average Interest Rate Paid	Hedge Maturity Date	Fair Value Gain (Loss) at March 31, 2019 (in millions)
Fair Value Hedges of Existing Debt					
Southern Company(*)	$ 300	2.75%	3-month LIBOR+0.92%	June 2020	$ (3)
Southern Company(*)	1,500	2.35%	1-month LIBOR+0.87%	July 2021	(30)
Georgia Power	200	4.25%	3-month LIBOR+2.46%	December 2019	(2)
Southern Company Consolidated	$ 2,000				$ (35)

(*) Represents the Southern Company parent entity.

The estimated pre-tax gains (losses) related to interest rate derivatives expected to be reclassified from accumulated OCI to interest expense for the next 12-month period ending March 31, 2020 are $(19) million for Southern Company and immaterial for all other registrants. Deferred gains and losses related to interest rate derivatives are expected to be amortized into earnings through 2046 for the Southern Company parent entity, 2035 for Alabama Power, 2037 for Georgia Power, 2028 for Mississippi Power, and 2046 for Southern Company Gas.

Foreign Currency Derivatives

Southern Company and certain subsidiaries, including Southern Power, may enter into foreign currency derivatives to hedge exposure to changes in foreign currency exchange rates, such as that arising from the issuance of debt denominated in a currency other than U.S. dollars. Derivatives related to forecasted transactions are accounted for as cash flow hedges where the derivatives' fair value gains or losses are recorded in OCI and are reclassified into earnings at the same time and on the same income statement line as the earnings effect of the hedged transactions, including foreign currency gains or losses arising from changes in the U.S. currency exchange rates. The derivatives employed as hedging instruments are structured to minimize ineffectiveness.

At March 31, 2019, the following foreign currency derivatives were outstanding:

	Pay Notional (in millions)	Pay Rate	Receive Notional (in millions)	Receive Rate	Hedge Maturity Date	Fair Value Gain (Loss) at March 31, 2019 (in millions)
Cash Flow Hedges of Existing Debt						
Southern Power	$ 677	2.95%	€600	1.00%	June 2022	$ 2

Southern Power	564	3.78%	500	1.85%	June 2026	11
Total	$ 1,241		€1,100			$ 13

177

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

The estimated pre-tax gains (losses) related to Southern Power's foreign currency derivatives expected to be reclassified from accumulated OCI to earnings for the next 12-month period ending March 31, 2020 are $(24) million.

Derivative Financial Statement Presentation and Amounts

Southern Company, the traditional electric operating companies, Southern Power, and Southern Company Gas enter into derivative contracts that may contain certain provisions that permit intra-contract netting of derivative receivables and payables for routine billing and offsets related to events of default and settlements. Southern Company and certain subsidiaries also utilize master netting agreements to mitigate exposure to counterparty credit risk. These agreements may contain provisions that permit netting across product lines and against cash collateral. The fair value amounts of derivative assets and liabilities on the balance sheet are presented net to the extent that there are netting arrangements or similar agreements with the counterparties.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

The fair value of energy-related derivatives, interest rate derivatives, and foreign currency derivatives was reflected in the balance sheets as follows:

Derivative Category and Balance Sheet Location	As of March 31, 2019 Assets	Liabilities	As of December 31, 2018 Assets	Liabilities
	(in millions)		(in millions)	
Southern Company				
Derivatives designated as hedging instruments for regulatory purposes				
Energy-related derivatives:				
Other current assets/Other current liabilities	$12	$ 10	$8	$ 23
Other deferred charges and assets/Other deferred credits and liabilities	11	21	9	26
Assets held for sale, current/Liabilities held for sale, current	—	—	—	6
Total derivatives designated as hedging instruments for regulatory purposes	$23	$ 31	$17	$ 55
Derivatives designated as hedging instruments in cash flow and fair value hedges				
Energy-related derivatives:				
Other current assets/Other current liabilities	$1	$ 3	$3	$ 7
Other deferred charges and assets/Other deferred credits and liabilities	—	1	1	2
Interest rate derivatives:				
Other current assets/Other current liabilities	—	20	—	19
Other deferred charges and assets/Other deferred credits and liabilities	—	15	—	30
Foreign currency derivatives:				
Other current assets/Other current liabilities	—	24	—	23
Other deferred charges and assets/Other deferred credits and liabilities	38	—	75	—
Total derivatives designated as hedging instruments in cash flow and fair value hedges	$39	$ 63	$79	$ 81
Derivatives not designated as hedging instruments				
Energy-related derivatives:				
Other current assets/Other current liabilities	$259	$ 291	$561	$ 575
Other deferred charges and assets/Other deferred credits and liabilities	171	269	180	325
Total derivatives not designated as hedging instruments	$430	$ 560	$741	$ 900
Gross amounts recognized	$492	$ 654	$837	$ 1,036
Gross amounts offset[(a)]	$(333)	$ (523)	$(524)	$ (801)
Net amounts recognized in the Balance Sheets[(b)]	$159	$ 131	$313	$ 235

179

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

	As of March 31, 2019		As of December 31, 2018	
Derivative Category and Balance Sheet Location	Assets	Liabilities	Assets	Liabilities
	(in millions)		(in millions)	
Alabama Power				
Derivatives designated as hedging instruments for regulatory purposes				
Energy-related derivatives:				
Other current assets/Other current liabilities	$3	$ 2	$3	$ 4
Other deferred charges and assets/Other deferred credits and liabilities	3	5	3	6
Total derivatives designated as hedging instruments for regulatory purposes	$6	$ 7	$6	$ 10
Gross amounts recognized	$6	$ 7	$6	$ 10
Gross amounts offset	$(5)	$ (5)	$(4)	$ (4)
Net amounts recognized in the Balance Sheets	$1	$ 2	$2	$ 6
Georgia Power				
Derivatives designated as hedging instruments for regulatory purposes				
Energy-related derivatives:				
Other current assets/Other current liabilities	$4	$ 5	$2	$ 8
Other deferred charges and assets/Other deferred credits and liabilities	5	11	4	13
Total derivatives designated as hedging instruments for regulatory purposes	$9	$ 16	$6	$ 21
Derivatives designated as hedging instruments in cash flow and fair value hedges				
Interest rate derivatives:				
Other current assets/Other current liabilities	$—	$ 2	$—	$ 2
Total derivatives designated as hedging instruments in cash flow and fair value hedges	$—	$ 2	$—	$ 2
Gross amounts recognized	$9	$ 18	$6	$ 23
Gross amounts offset	$(8)	$ (8)	$(6)	$ (6)
Net amounts recognized in the Balance Sheets	$1	$ 10	$—	$ 17

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

	As of March 31, 2019		As of December 31, 2018	
Derivative Category and Balance Sheet Location	Assets	Liabilities	Assets	Liabilities
	(in millions)		(in millions)	
Mississippi Power				
Derivatives designated as hedging instruments for regulatory purposes				
Energy-related derivatives:				
Other current assets/Other current liabilities	$2	$ 2	$1	$ 3
Other deferred charges and assets/Other deferred credits and liabilities	1	4	2	6
Total derivatives designated as hedging instruments for regulatory purposes	$3	$ 6	$3	$ 9
Gross amounts recognized	$3	$ 6	$3	$ 9
Gross amounts offset	$(3)	$ (3)	$(2)	$ (2)
Net amounts recognized in the Balance Sheets	$—	$ 3	$1	$ 7
Southern Power				
Derivatives designated as hedging instruments in cash flow and fair value hedges				
Energy-related derivatives:				
Other current assets/Other current liabilities	$1	$ 2	$3	$ 6
Other deferred charges and assets/Other deferred credits and liabilities	—	1	1	2
Foreign currency derivatives:				
Other current assets/Other current liabilities	—	24	—	23
Other deferred charges and assets/Other deferred credits and liabilities	38	—	75	—
Total derivatives designated as hedging instruments in cash flow and fair value hedges	$39	$ 27	$79	$ 31
Gross amounts recognized	$39	$ 27	$79	$ 31
Gross amounts offset	$(1)	$ (1)	$(3)	$ (3)
Net amounts recognized in the Balance Sheets	$38	$ 26	$76	$ 28
Southern Company Gas				
Derivatives designated as hedging instruments for regulatory purposes				
Energy-related derivatives:				
Assets from risk management activities/Liabilities from risk management activities-current	$3	$ 1	$2	$ 8
Other deferred charges and assets/Other deferred credits and liabilities	1	—	—	1
Total derivatives designated as hedging instruments for regulatory purposes	$4	$ 1	$2	$ 9
Derivatives designated as hedging instruments in cash flow and fair value hedges				
Energy-related derivatives:				
Assets from risk management activities/Liabilities from risk management activities-current	$—	$ 1	$—	$ 1
Total derivatives designated as hedging instruments in cash flow and fair value hedges	$—	$ 1	$—	$ 1

181

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Derivative Category and Balance Sheet Location	As of March 31, 2019 Assets	Liabilities	As of December 31, 2018 Assets	Liabilities
	(in millions)		(in millions)	
Derivatives not designated as hedging instruments				
Energy-related derivatives:				
Assets from risk management activities/Liabilities from risk management activities-current	$259	$ 291	$559	$ 574
Other deferred charges and assets/Other deferred credits and liabilities	171	269	180	325
Total derivatives not designated as hedging instruments	$430	$ 560	$739	$ 899
Gross amounts of recognized	$434	$ 562	$741	$ 909
Gross amounts offset[(a)]	$(316)	$ (506)	$(508)	$ (785)
Net amounts recognized in the Balance Sheets[(b)]	$118	$ 56	$233	$ 124

(a) Gross amounts offset include cash collateral held on deposit in broker margin accounts of $190 million and $277 million as of March 31, 2019 and December 31, 2018, respectively.

(b) Net amounts of derivative instruments outstanding exclude premium and intrinsic value associated with weather derivatives of $11 million and $8 million as of March 31, 2019 and December 31, 2018, respectively.

At March 31, 2019 and December 31, 2018, the pre-tax effects of unrealized derivative gains (losses) arising from energy-related derivative instruments designated as regulatory hedging instruments and deferred were as follows:

Regulatory Hedge Unrealized Gain (Loss) Recognized in the Balance Sheet at March 31, 2019

Derivative Category and Balance Sheet Location	Southern Company	Alabama Power[(*)]	Georgia Power	Mississippi Power	Southern Company Gas[(*)]
	(in millions)				
Energy-related derivatives:					
Other regulatory assets, current	$(5)	$ (1)	$ (2)	$ (1)	$ (1)
Other regulatory assets, deferred	(11)	(2)	(6)	(3)	—
Other regulatory liabilities, current	7	1	1	1	4
Total energy-related derivative gains (losses)	$(9)	$ (2)	$ (7)	$ (3)	$ 3

(*) Fair value gains and losses recorded in regulatory assets and liabilities include cash collateral held on deposit in broker margin accounts of $2 million at March 31, 2019.

Regulatory Hedge Unrealized Gain (Loss) Recognized in the Balance Sheet at December 31, 2018

Derivative Category and Balance Sheet Location	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Company Gas
	(in millions)				
Energy-related derivatives:					
Other regulatory assets, current	$(19)	$ (3)	$ (6)	$ (2)	$ (8)
Other regulatory assets, deferred	(16)	(3)	(9)	(4)	—
Assets held for sale, current	(6)	—	—	—	—
Other regulatory liabilities, current	1	—	—	—	1
Total energy-related derivative gains (losses)	$(40)	$ (6)	$ (15)	$ (6)	$ (7)

182

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

For the three months ended March 31, 2019 and 2018, the pre-tax effects of cash flow hedge accounting on accumulated OCI were as follows:

Gain (Loss) Recognized in OCI on Derivative	For the Three Months Ended March 31, 2019	2018
	(in millions)	
Southern Company		
Energy-related derivatives	$—	$12
Interest rate derivatives	—	(2)
Foreign currency derivatives	(39)	53
Total	$(39)	$63
Southern Power		
Energy-related derivatives	$—	$11
Foreign currency derivatives	(39)	53
Total	$(39)	$64

For the three months ended March 31, 2019 and 2018, the pre-tax effects of energy-related derivatives and interest rate derivatives designated as cash flow hedging instruments on accumulated OCI were immaterial for the other registrants.

For the three months ended March 31, 2019 and 2018, the pre-tax effects of cash flow and fair value hedge accounting on income were as follows:

Location and Amount of Gain (Loss) Recognized in Income on Cash Flow and Fair Value Hedging Relationships	For the Three Months Ended March 31, 2019	2018
	(in millions)	
Southern Company		
Total depreciation and amortization	$751	$769
Gain (loss) on energy-related cash flow hedges[a]	(3)	1
Total interest expense, net of amounts capitalized	(430)	(458)
Gain (loss) on interest rate cash flow hedges[a]	(5)	(5)
Gain (loss) on foreign currency cash flow hedges[a]	(6)	(5)
Gain (loss) on interest rate fair value hedges[b]	14	(24)
Total other income (expense), net	78	60
Gain (loss) on foreign currency cash flow hedges[a][c]	(24)	36
Southern Power		
Total depreciation and amortization	$119	$114
Gain (loss) on energy-related cash flow hedges[a]	(3)	1
Total interest expense, net of amounts capitalized	(44)	(47)
Gain (loss) on foreign currency cash flow hedges[a]	(6)	(5)
Total other income (expense), net	2	3

Gain (loss) on foreign currency cash flow hedges[a][c]	(24)	36

(a) Reclassified from accumulated OCI into earnings.

(b) For fair value hedges, changes in the fair value of the derivative contracts are generally equal to changes in the fair value of the underlying debt and have no material impact on income.

(c) The reclassification from accumulated OCI into other income (expense), net completely offsets currency gains and losses arising from changes in the U.S. currency exchange rates used to record the euro-denominated notes.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

For the three months ended March 31, 2019 and 2018, the pre-tax effects of cash flow and fair value hedge accounting on income for energy-related derivatives and interest rate derivatives were immaterial for the traditional electric operating companies and Southern Company Gas.
As of March 31, 2019 and December 31, 2018, the following amounts were recorded on the balance sheets related to cumulative basis adjustments for fair value hedges:

Balance Sheet Location of Hedged Items	Carrying Amount of the Hedged Item		Cumulative Amount of Fair Value Hedging Adjustment included in Carrying Amount of the Hedged Item	
	As of March 31, 2019	As of December 31, 2018	As of March 31, 2019	As of December 31, 2018
	(in millions)		(in millions)	
Southern Company				
Securities due within one year	$(499)	$ (498)	$ 1	$ 2
Long-term debt	(2,065)	(2,052)	28	41
Georgia Power				
Securities due within one year	$(499)	$ (498)	$ 1	$ 2
Long-term debt	—	—	—	—

For the three months ended March 31, 2019 and 2018, the pre-tax effects of energy-related derivatives not designated as hedging instruments on the statements of income of Southern Company and Southern Company Gas were as follows:

Derivatives in Non-Designated Hedging Relationships	Statements of Income Location	Gain (Loss) Three Months Ended March 31, 2019	2018
		(in millions)	
Energy-related derivatives:	Natural gas revenues(*)	$33	$(15)
	Cost of natural gas	8	2
Total derivatives in non-designated hedging relationships		$41	$(13)

(*) Excludes immaterial gains (losses) recorded in natural gas revenues associated with weather derivatives for the three months ended March 31, 2019 and 2018.

For the three months ended March 31, 2019 and 2018, the pre-tax effects of energy-related derivatives and interest rate derivatives not designated as hedging instruments were immaterial for the traditional electric operating companies and Southern Power.
Contingent Features

Southern Company, the traditional electric operating companies, Southern Power, and Southern Company Gas do not have any credit arrangements that would require material changes in payment schedules or terminations as a result of a credit rating downgrade. There are certain derivatives that could require collateral, but not accelerated payment, in the event of various credit rating changes of certain Southern Company subsidiaries. At March 31, 2019, the registrants had no collateral posted with derivative counterparties to satisfy these arrangements.

For the registrants with interest rate derivatives at March 31, 2019, the fair value of interest rate derivative liabilities with contingent features and the maximum potential collateral requirements arising from the credit-risk-related contingent features, at a rating below BBB- and/or Baa3, was immaterial. At March 31, 2019, the fair value of energy-related derivative liabilities with contingent features and the maximum potential collateral requirements arising from the credit-risk-related contingent features, at a rating below BBB- and/or Baa3, were immaterial for all

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

registrants. The maximum potential collateral requirements arising from the credit-risk-related contingent features for the traditional electric operating companies and Southern Power include certain agreements that could require collateral in the event that one or more Southern Company power pool participants has a credit rating change to below investment grade. Following the sale of Gulf Power to NextEra Energy, Gulf Power is continuing to participate in the Southern Company power pool for a defined transition period that, subject to certain potential adjustments, is scheduled to end on January 1, 2024.

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

Alabama Power and Southern Power maintain accounts with certain regional transmission organizations to facilitate financial derivative transactions. Based on the value of the positions in these accounts and the associated margin requirements, Alabama Power and Southern Power may be required to post collateral. At March 31, 2019, cash collateral posted in these accounts was immaterial. Southern Company Gas maintains accounts with brokers or the clearing houses of certain exchanges to facilitate financial derivative transactions. Based on the value of the positions in these accounts and the associated margin requirements, Southern Company Gas may be required to deposit cash into these accounts. At March 31, 2019, cash collateral held on deposit in broker margin accounts was $190 million.

The registrants are exposed to losses related to financial instruments in the event of counterparties' nonperformance. The registrants only enter into agreements and material transactions with counterparties that have investment grade credit ratings by Moody's and S&P or with counterparties who have posted collateral to cover potential credit exposure. The registrants have also established risk management policies and controls to determine and monitor the creditworthiness of counterparties in order to mitigate their exposure to counterparty credit risk. Prior to entering into a physical transaction, Southern Company Gas assigns physical wholesale counterparties an internal credit rating and credit limit based on the counterparties' Moody's, S&P, and Fitch Ratings Inc. ratings, commercially available credit reports, and audited financial statements. Southern Company Gas may require counterparties to pledge additional collateral when deemed necessary.

In addition, Southern Company Gas conducts credit evaluations and obtains appropriate internal approvals for the counterparty's line of credit before any transaction with the counterparty is executed. In most cases, the counterparty must have an investment grade rating, which includes a minimum long-term debt rating of Baa3 from Moody's and BBB- from S&P. Generally, Southern Company Gas requires credit enhancements by way of a guaranty, cash deposit, or letter of credit for transaction counterparties that do not have investment grade ratings.

Southern Company Gas also utilizes master netting agreements whenever possible to mitigate exposure to counterparty credit risk. When Southern Company Gas is engaged in more than one outstanding derivative transaction with the same counterparty and it also has a legally enforceable netting agreement with that counterparty, the "net" mark-to-market exposure represents the netting of the positive and negative exposures with that counterparty and a reasonable measure of Southern Company Gas' credit risk. Southern Company Gas also uses other netting agreements with certain counterparties with whom it conducts significant transactions. Master netting agreements enable Southern Company Gas to net certain assets and liabilities by counterparty. Southern Company Gas also nets across product lines and against cash collateral provided the master netting and cash collateral agreements include such provisions. Southern Company Gas may require counterparties to pledge additional collateral when deemed necessary.

The registrants do not anticipate a material adverse effect on their respective financial statements as a result of counterparty nonperformance.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

(K) ACQUISITIONS AND DISPOSITIONS
See Note 15 to the financial statements in Item 8 of the Form 10-K for additional information.
Southern Company
On January 1, 2019, Southern Company completed the sale of all of the capital stock of Gulf Power to 700 Universe, LLC, a wholly-owned subsidiary of NextEra Energy, for an aggregate cash purchase price of approximately $5.8 billion (less $1.3 billion of indebtedness assumed), subject to customary working capital adjustments. The preliminary gain associated with the sale of Gulf Power totaled $2.5 billion pre-tax ($1.3 billion after tax). The assets and liabilities of Gulf Power were classified as assets held for sale and liabilities held for sale on Southern Company's balance sheet as of December 31, 2018.
Management has started the process to sell one of PowerSecure's business units; therefore, the related assets and liabilities have been reclassified as held for sale on Southern Company's balance sheet as of March 31, 2019. The ultimate outcome of this matter cannot be determined at this time; however, any related gain or loss on the potential sale is not expected to have a material effect on Southern Company's financial statements.
See "Assets Held for Sale" herein for additional information.
Southern Power
Construction Projects in Progress
During the three months ended March 31, 2019, Southern Power continued construction of the projects set forth in the table below. Total aggregate construction costs, excluding the acquisition costs, are expected to be between $575 million and $640 million for the Plant Mankato expansion and the Wildhorse Mountain and Reading facilities. At March 31, 2019, total costs of construction incurred for these projects were $347 million and are included in CWIP, except for the Plant Mankato expansion, which is included in assets held for sale in the financial statements. The ultimate outcome of these matters cannot be determined at this time.

Project Facility	Resource	Approximate Nameplate Capacity (MW)	Location	Expected COD	PPA Contract Period
Mankato expansion[(a)]	Natural Gas	385	Mankato, MN	May 2019	20 years
Wildhorse Mountain[(b)]	Wind	100	Pushmataha County, OK	Fourth quarter 2019	20 years
Reading[(c)]	Wind	200	Osage and Lyon Counties, KS	Second quarter 2020	12 years

(a) In November 2018, Southern Power entered into an agreement to sell all of its equity interests in Plant Mankato, including this expansion currently under construction. This transaction is subject to FERC and state commission approvals and is expected to close mid-2019. The ultimate outcome of this matter cannot be determined at this time. See "Sales of Natural Gas and Biomass Plants" below.
(b) In May 2018, Southern Power purchased 100% of the Wildhorse Mountain facility. Southern Power may enter into a tax equity partnership, in which case it would then own 100% of the class B membership interests. The ultimate outcome of this matter cannot be determined at this time.
(c) In August 2018, Southern Power purchased 100% of the membership interests of the Reading facility from the joint development arrangement with Renewable Energy Systems Americas, Inc. described below. Southern Power may enter into a tax equity partnership, in which case it would then own 100% of the class B membership interests. The ultimate outcome of this matter cannot be determined at this time.

Development Projects
Southern Power continues to evaluate and refine the deployment of the wind turbine equipment purchased in 2016 and 2017 to potential joint development and construction projects as well as the amount of MW capacity to be constructed. During the three months ended March 31, 2019, approximately $53 million of equipment was marketed for sale and, subsequent to March 31, 2019, was sold. At March 31, 2019, the equipment was classified as held for

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

sale on Southern Company's and Southern Power's balance sheets. See "Assets Held for Sale" herein for additional information.

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

Sales of Natural Gas and Biomass Plants

In November 2018, Southern Power entered into an agreement with Northern States Power to sell all of its equity interests in Plant Mankato (including the 385-MW expansion currently under construction) for an aggregate purchase price of approximately $650 million. The completion of the disposition is subject to the expansion unit reaching commercial operation as well as various other customary conditions to closing, including working capital and timing adjustments. This transaction is subject to FERC and state commission approvals. The assets and liabilities of Plant Mankato are classified as assets held for sale and liabilities held for sale on Southern Company's and Southern Power's balance sheets as of March 31, 2019 and December 31, 2018. See "Assets Held for Sale" herein for additional information.

On April 17, 2019, Southern Power entered into an agreement to sell all of its equity interests in the Nacogdoches biomass-fueled facility to Austin Energy for an aggregate purchase price of $460 million, subject to customary closing conditions and working capital adjustments.

Each of these sales is expected to close in mid-2019; however, the ultimate outcome of these matters cannot be determined at this time.

Assets Subject to Lien

Under the terms of the PPA and the expansion PPA for Plant Mankato, approximately $538 million of assets, primarily related to property, plant, and equipment, are subject to lien at March 31, 2019.

Assets Held for Sale

As discussed above, Southern Company and Southern Power each have assets and liabilities held for sale on their balance sheets at March 31, 2019 and December 31, 2018. Assets and liabilities held for sale have been classified separately on each company's balance sheet at the lower of carrying value or fair value less costs to sell at the time the criteria for held-for-sale classification were met. For assets and liabilities held for sale recorded at fair value on a nonrecurring basis, the fair value of assets held for sale is based primarily on unobservable inputs (Level 3), which includes the agreed upon sales prices in executed sales agreements.

Upon classification as held for sale in November 2018 for Plant Mankato, Southern Power ceased recognizing depreciation and amortization on the long-lived assets to be sold.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

The following table provides Southern Company's and Southern Power's major classes of assets and liabilities classified as held for sale at March 31, 2019 and December 31, 2018:

	Southern Company	Southern Power
	(in millions)	
At March 31, 2019		
Assets Held for Sale:		
Current assets	$55	$ 11
Total property, plant, and equipment	637	604
Goodwill and other intangible assets	82	40
Other non-current assets	44	—
Total Assets Held for Sale	$818	$ 655
Liabilities Held for Sale:		
Current liabilities	$38	$ 9
Other non-current liabilities	39	—
Total Liabilities Held for Sale	$77	$ 9
At December 31, 2018		
Assets Held for Sale:		
Current assets	$393	$ 8
Total property, plant, and equipment	4,583	536
Goodwill and other intangible assets	40	40
Other non-current assets	727	—
Total Assets Held for Sale	$5,743	$ 584
Liabilities Held for Sale:		
Current liabilities	$425	$ 15
Long-term debt	1,286	—
Accumulated deferred income taxes	618	—
Other non-current liabilities	932	—
Total Liabilities Held for Sale	$3,261	$ 15

Southern Company and Southern Power each concluded that the sale of their assets, both individually and combined, did not represent a strategic shift in operations that has, or is expected to have, a major effect on its operations and financial results; therefore, none of the assets related to the sales have been classified as discontinued operations for any of the periods presented.

188

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Gulf Power and Southern Power's equity interests in Plant Oleander and Plant Stanton Unit A (together, the Florida Plants) represented individually significant components of Southern Company and Southern Power, respectively; therefore, pre-tax profit for these components for the three months ended March 31, 2018 is presented below:

	For the Three Months Ended March 31, 2018
	(in millions)
Earnings before income taxes:	
Gulf Power	$ 55
Southern Power's Florida Plants	$ 8

(L) LEASES

On January 1, 2019, the registrants adopted the provisions of FASB ASC Topic 842 (as amended), Leases (ASC 842), which require lessees to recognize leases with a term of greater than 12 months on the balance sheet as lease obligations, representing the discounted future fixed payments due, along with right-of-use (ROU) assets that will be amortized over the term of each lease.

The registrants elected the transition methodology provided by ASC 842, whereby the applicable requirements are applied on a prospective basis as of the adoption date of January 1, 2019, without restating prior periods. The registrants also elected the package of practical expedients provided by ASC 842 that allows prior determinations of whether existing contracts are, or contain, leases and the classification of existing leases to continue without reassessment. Additionally, the registrants applied the use-of-hindsight practical expedient in determining lease terms as of the date of adoption and elected the practical expedient that allows existing land easements not previously accounted for as leases not to be reassessed.

Lessee

As lessee, the registrants lease certain electric generating units (including renewable energy facilities), real estate/land, communication towers, railcars, and other equipment and vehicles. The major categories of lease obligations are as follows:

	As of March 31, 2019					
	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)					
Electric generating units	$1,094	$ 159	$1,606	$ —	$ —	$ —
Real estate/land	803	3	63	2	393	83
Communication towers	131	1	3	—	—	—
Railcars	55	25	26	3	—	—
Other	153	10	16	3	—	1
Total	$2,236	$ 198	$1,714	$ 8	$ 393	$ 84

Real estate/land leases primarily consist of commercial real estate leases at Southern Company, Georgia Power, and Southern Company Gas and various land leases primarily associated with renewable energy facilities at Southern Power. The commercial real estate leases have remaining terms of up to 25 years while the land leases have remaining terms of up to 48 years, including renewal periods.

Communication towers are leased for the installation of equipment to provide cellular phone service to customers and to support the automated meter infrastructure programs at the traditional electric operating companies. Communication tower leases have terms of up to 10 years with options to renew for periods up to 20 years.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

While renewal options exist in many of the leases, other than for land leases associated with renewable energy facilities, the expected term used in calculating the lease obligation generally reflects only the noncancelable period of the lease as it is not considered reasonably certain that the lease will be extended. The expected term of land leases associated with renewable energy facilities includes renewal periods reasonably certain of exercise resulting in an expected lease term at least equal to the expected life of the renewable energy facilities.

Contracts that Contain a Lease

While not specifically structured as a lease, some of the PPAs at Alabama Power and Georgia Power are deemed to represent a lease of the underlying electric generating units when the terms of the PPA convey the right to control the use of the underlying assets. Amounts recorded for leases of electric generating units are generally based on the amount of scheduled capacity payments due over the remaining term of the affiliate PPA, which varies between four and 18 years. Georgia Power has several PPAs with Southern Power that Georgia Power accounts for as leases with a lease obligation of approximately $670 million at March 31, 2019. The amount paid for energy under these affiliate PPAs reflects a price that would be paid in an arm's-length transaction as those amounts have been reviewed and approved by the Georgia PSC.

Short-term Leases

Leases with an initial term of 12 months or less are not recorded on the balance sheet; the registrants generally recognize lease expense for these leases on a straight-line basis over the lease term.

Residual Value Guarantees

Residual value guarantees exist primarily in railcar leases at Alabama Power and Georgia Power and the amounts probable of being paid under those guarantees are included in the lease payments. All such amounts are immaterial as of March 31, 2019.

Lease and Nonlease Components

For all asset categories, with the exception of electric generating units, gas pipelines, and real estate leases, the registrants combine lease payments and any nonlease components, such as asset maintenance, for purposes of calculating the lease obligation and the right-of-use asset.

Balance sheet amounts recorded for operating and finance leases are as follows:

	As of March 31, 2019					
	Southern Company	Alabama Power (*)	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)					
Operating Leases						
Operating lease ROU assets, net	$1,926	$ 160	$ 1,519	$ 8	$ 372	$ 86
Operating lease obligations - current	$239	$ 47	$ 139	$ 3	$ 22	$ 13
Operating lease obligations - non current	1,752	147	1,404	5	371	71
Total operating lease obligations	$1,991	$ 194	$ 1,543	$ 8	$ 393	$ 84
Finance Leases						
Finance lease ROU assets, net	$242	$ 4	$ 145	$ —	$ —	$ —
Finance lease obligations - current	$38	$ 1	$ 10	$ —	$ —	$ —
Finance lease obligations - noncurrent	207	3	161	—	—	—
Total finance lease obligations	$245	$ 4	$ 171	$ —	$ —	$ —

(*) Includes operating lease ROU assets, net and operating lease obligations classified as held for sale.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Lease costs for the three months ended March 31, 2019, which includes both amounts recognized as operations and maintenance expense and amounts capitalized as part of the cost of another asset, are as follows:

	For the Three Months Ended March 31, 2019					
	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)					
Lease cost						
Operating lease cost	$69	$ 7	$ 49	$ 1	$ 7	$ 4
Finance lease cost:						
Amortization of ROU assets	7	—	4	—	—	—
Interest on lease obligations	3	—	4	—	—	—
Total finance lease cost	10	—	8	—	—	—
Short-term lease costs	14	5	3	—	—	—
Variable lease cost	19	—	16	—	1	—
Sublease income	—	—	—	—	—	—
Total lease cost	$112	$ 12	$ 76	$ 1	$ 8	$ 4

Georgia Power has variable lease payments that are based on the amount of energy produced by certain renewable generating facilities subject to PPAs.

Other information with respect to cash and noncash activities related to leases, as well as weighted-average lease terms and discount rates, is as follows:

	For the Three Months Ended March 31, 2019					
	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)					
Other information						
Cash paid for amounts included in the measurements of lease obligations:						
Operating cash flows from operating leases	$74	$ 13	$ 32	$ 1	$ 7	$ 4
Operating cash flows from finance leases	6	—	13	—	—	—
Financing cash flows from finance leases	8	—	2	—	—	—
ROU assets obtained in exchange for new operating lease obligations	15	2	4	—	—	—
ROU assets obtained in exchange for new finance lease obligations	29	—	28	—	—	—

191

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

	As of March 31, 2019					
	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
Weighted-average remaining lease term in years:						
Operating leases	13.5	3.8	10.1	6.8	33.7	9.0
Finance leases	18.5	14.8	11.3	—	—	—
Weighted-average discount rate:						
Operating leases	4.49%	3.33%	4.42%	4.03%	5.68%	3.70%
Finance leases	5.00%	3.75%	10.68%	—%	—%	—%

Maturities of lease liabilities are as follows:

	As of March 31, 2019					
	Southern Company	Alabama Power	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)					
Maturity Analysis						
Operating leases:						
2019 (remaining)	$253	$ 46	$182	$ 2	$ 17	$ 12
2020	291	53	202	2	22	16
2021	274	52	197	1	23	16
2022	263	52	195	1	23	12
2023	198	3	196	1	24	10
Thereafter	1,637	1	984	2	848	36
Total	2,916	207	1,956	9	957	102
Less: Present value discount	925	13	413	1	564	18
Operating lease obligations	$1,991	$ 194	$1,543	$ 8	$ 393	$ 84
Finance leases:						
2019 (remaining)	$24	$ 1	$22	$ —	$ —	$ —
2020	32	1	28	—	—	—
2021	26	1	25	—	—	—
2022	22	1	25	—	—	—
2023	18	1	25	—	—	—
Thereafter	273	—	165	—	—	—
Total	395	5	290	—	—	—
Less: Present value discount	150	1	119	—	—	—
Finance lease obligations	$245	$ 4	$171	$ —	$ —	$ —

Payments made under PPAs at Georgia Power for energy generated from certain renewable energy facilities accounted for as operating and finance leases are considered variable lease costs and are therefore not reflected in the above maturity analysis. As of March 31, 2019, Southern Company and Southern Power have additional operating leases, primarily for land, that have not yet commenced. These operating leases are expected to commence during the remainder of 2019 through 2021, with lease terms of up to 30 years, and have estimated total obligations of $77 million.

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

For additional information on each registrant's operating lease obligations at December 31, 2018, see Note 9 to the financial statements in Item 8 of the Form 10-K.

Lessor

With the exception of Southern Company Gas, the registrants are each considered lessors in various arrangements that have been determined to contain a lease due to the customer's ability to control the use of the underlying asset owned by the applicable registrant. For the traditional electric operating companies, these arrangements consist of outdoor lighting contracts accounted for as operating leases with initial terms of up to five years, after which the contracts renew on a month-to-month basis at the customer's option. For Mississippi Power, these arrangements also include tolling arrangements related to electric generating units accounted for as sales-type leases with terms of up to 20 years. For Southern Power, these arrangements consist of PPAs related to electric generating units, including renewable energy facilities, accounted for as operating leases with terms of up to 28 years. For Southern Company, these arrangements also include PPAs related to fuel cells accounted for as operating leases with terms of up to 15 years. Southern Company Gas is the lessor in operating leases related to gas pipelines with remaining terms of up to 24 years.

Lease income for the three months ended March 31, 2019 is as follows:

	For the Three Months Ended March 31, 2019				
	Southern Company	Georgia Power	Mississippi Power	Southern Power	Southern Company Gas
	(in millions)				
Lease income - interest income on sales-type leases	$2	$ —	$ 2	$ —	$ —
Lease income - operating leases	71	19	—	41	9
Variable lease income	66	—	—	72	—
Total lease income	$139	$ 19	$ 2	$ 113	$ 9

No profit or loss was recognized by Mississippi Power upon commencement of a sales-type lease during the first quarter 2019.

Lease income for Southern Power is included in wholesale revenues. Lease payments received under tolling arrangements and PPAs consist of either scheduled payments or variable payments based on the amount of energy produced by the underlying electric generating units. Scheduled payments to be received under outdoor lighting contracts, tolling arrangements, and PPAs accounted for as leases are presented in the following maturity analyses.

193

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

The undiscounted cash flows to be received under tolling arrangements accounted for as sales-type leases are as follows:

	As of March 31, 2019	
	Southern Company	Mississippi Power
	(in millions)	
2019 (remaining)	$11	$ 11
2020	14	14
2021	14	14
2022	13	13
2023	12	12
Thereafter	135	135
Total undiscounted cash flows	$199	$ 199
Lease receivable	108	108
Difference between undiscounted cash flows and discounted cash flows	$91	$ 91

The undiscounted cash flows to be received under operating leases and contracts accounted for as operating leases (adjusted for intercompany eliminations) are as follows:

	As of March 31, 2019			
	Southern Company	Georgia Power	Southern Power	Southern Company Gas
	(in millions)			
2019 (remaining)	$163	$ 20	$ 123	$ 26
2020	188	26	128	34
2021	183	18	131	34
2022	174	8	134	34
2023	171	2	137	34
Thereafter	1,809	—	1,017	498
Total	$2,688	$ 74	$ 1,670	$ 660

Southern Power receives payments for renewable energy under PPAs accounted for as operating leases that are considered contingent rents and are therefore not reflected in the table above. Southern Power allocates revenue to the nonlease components of PPAs based on the stand-alone selling price of capacity and energy. The undiscounted cash flows to be received under outdoor lighting contracts accounted for as operating leases at Alabama Power and Mississippi Power are immaterial.

(M) SEGMENT AND RELATED INFORMATION

Southern Company

The primary businesses of the Southern Company system are electricity sales by the traditional electric operating companies and Southern Power and the distribution of natural gas by Southern Company Gas. The traditional electric operating companies – Alabama Power, Georgia Power, and Mississippi Power – are vertically integrated utilities providing electric service in three Southeastern states. Southern Power develops, constructs, acquires, owns, and manages power generation assets, including renewable energy projects, and sells electricity at market-based rates in the wholesale market. Southern Company Gas distributes natural gas through its natural gas distribution utilities and is involved in several other complementary businesses including gas pipeline investments, wholesale gas services, and gas marketing services.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Southern Company's reportable business segments are the sale of electricity by the traditional electric operating companies, the sale of electricity in the competitive wholesale market by Southern Power, and the sale of natural gas and other complementary products and services by Southern Company Gas. Revenues from sales by Southern Power to the traditional electric operating companies were $87 million for the three months ended March 31, 2019 and $83 million for the three months ended March 31, 2018. Revenues from sales of natural gas from Southern Company Gas to the traditional electric operating companies were immaterial for each of the three months ended March 31, 2019 and 2018. Revenues from sales of natural gas from Southern Company Gas to Southern Power were $17 million for the three months ended March 31, 2019 and $36 million for the three months ended March 31, 2018. The "All Other" column includes the Southern Company parent entity, which does not allocate operating expenses to business segments. Also, this category includes segments below the quantitative threshold for separate disclosure. These segments include providing energy technologies and services to electric utilities and large industrial, commercial, institutional, and municipal customers, as well as investments in telecommunications and leveraged lease projects. All other inter-segment revenues are not material.
Financial data for business segments and products and services for the three months ended March 31, 2019 and 2018 was as follows:

	Electric Utilities							
	Traditional Electric Operating Companies	Southern Power	Eliminations	Total	Southern Company Gas	All Other	Eliminations	Consolidated
	(in millions)							
Three Months Ended March 31, 2019:								
Operating revenues	$3,445	$ 443	$ (93)	$3,795	$ 1,474	$182	$ (39)	$ 5,412
Segment net income (loss)(a)(b)(c)	565	56	—	621	270	1,195	(2)	2,084
At March 31, 2019:								
Goodwill	$—	$ 2	$ —	$2	$ 5,015	$268	$ (1)	$ 5,284
Total assets	76,798	15,104	(779)	91,123	20,952	3,391	(1,370)	114,096
Three Months Ended March 31, 2018:								
Operating revenues	$3,979	$ 509	$ (106)	$4,382	$ 1,639	$401	$ (50)	$ 6,372
Segment net income (loss)(a)(b)(d)	612	121	—	733	279	(74)	—	938
At December 31, 2018:								
Goodwill	$—	$ 2	$ —	$2	$ 5,015	$298	$ —	$ 5,315
Total assets	79,382	14,883	(306)	93,959	21,448	3,285	(1,778)	116,914

(a) Attributable to Southern Company.

(b) Segment net income (loss) for the traditional electric operating companies includes pre-tax charges for estimated losses on plants under construction of $2 million ($1 million after tax) and $44 million ($33 million after tax) for the three months ended March 31, 2019 and 2018, respectively. See Note 2 to the financial statements in Item 8 of the Form 10-K and Note (B) under "Mississippi Power – Kemper County Energy Facility" for additional information.

(c) Segment net income (loss) for the "All Other" column includes the preliminary pre-tax gain associated with the sale of Gulf Power of $2.5 billion ($1.3 billion after tax) for the three months ended March 31, 2019. See Note (K) under "Southern Company" for additional information.

(d) Segment net income (loss) for Southern Company Gas includes a goodwill impairment charge of $42 million for the three months ended March 31, 2018 related to the sale of Pivotal Home Solutions. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

195

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Products and Services

	Electric Utilities' Revenues			
	Retail	Wholesale	Other	Total
	(in millions)			
Three Months Ended March 31, 2019	$3,084	$ 499	$212	$3,795
Three Months Ended March 31, 2018	3,568	623	191	4,382

	Southern Company Gas' Revenues			
	Gas Distribution Operations(a)	Gas Marketing Services(b)	Other	Total
	(in millions)			
Three Months Ended March 31, 2019	$1,161	$ 229	$ 84	$1,474
Three Months Ended March 31, 2018	1,200	271	168	1,639

(a) Operating revenues for the three gas distribution operations dispositions were $167 million for the three months ended March 31, 2018.

(b) Operating revenues for Pivotal Home Solutions were $32 million for the three months ended March 31, 2018.

Southern Company Gas

Southern Company Gas manages its business through four reportable segments – gas distribution operations, gas pipeline investments, wholesale gas services, and gas marketing services. The non-reportable segments are combined and presented as all other.

Gas distribution operations is the largest component of Southern Company Gas' business and includes natural gas local distribution utilities that construct, manage, and maintain intrastate natural gas pipelines and gas distribution facilities in four states.

Gas pipeline investments consists of joint ventures in natural gas pipeline investments including a 50% interest in SNG, two significant pipeline construction projects, and a 50% joint ownership interest in the Dalton Pipeline. These natural gas pipelines enable the provision of diverse sources of natural gas supplies to the customers of Southern Company Gas.

Wholesale gas services provides natural gas asset management and/or related logistics services for each of Southern Company Gas' utilities except Nicor Gas as well as for non-affiliated companies. Additionally, wholesale gas services engages in natural gas storage and gas pipeline arbitrage and related activities.

Gas marketing services provides natural gas marketing to end-use customers primarily in Georgia and Illinois through SouthStar Energy Services, LLC.

The all other column includes segments below the quantitative threshold for separate disclosure, including the storage and fuels operations, and the other subsidiaries that fall below the quantitative threshold for separate disclosure.

196

Table of Contents

NOTES TO THE CONDENSED FINANCIAL STATEMENTS: (Continued)
(UNAUDITED)

Business segment financial data for the three months ended March 31, 2019 and 2018 was as follows:

	Gas Distribution Operations[a] (in millions)	Gas Pipeline Investments	Wholesale Gas Services[b]	Gas Marketing Services[c][d]	Total	All Other	Eliminations	Consolidated
Three Months Ended March 31, 2019:								
Operating revenues	$1,172	$ 8	$ 86	$ 229	$1,495	$ 11	$ (32)	$ 1,474
Segment net income (loss)	133	32	47	61	273	(3)	—	270
Total assets at March 31, 2019:	17,379	1,781	821	1,611	21,592	10,900	(11,540)	20,952
Three Months Ended March 31, 2018:								
Operating revenues	$1,212	$ 8	$ 166	$ 271	$1,657	$ 15	$ (33)	$ 1,639
Segment net income (loss)	149	27	104	13	293	(14)	—	279
Total assets at December 31, 2018:	17,266	1,763	1,302	1,587	21,918	11,112	(11,582)	$ 21,448

(a) Operating revenues for the three gas distribution operations dispositions were $167 million for the three months ended March 31, 2018. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

(b) The revenues for wholesale gas services are netted with costs associated with its energy and risk management activities. A reconciliation of operating revenues and intercompany revenues is shown in the following table.

	Third Party Gross Revenues (in millions)	Intercompany Revenues	Total Gross Revenues	Less Gross Gas Costs	Operating Revenues
Three Months Ended March 31, 2019	$1,926	$ 88	$ 2,014	$1,928	$ 86
Three Months Ended March 31, 2018	1,938	167	2,105	1,939	166

(c) Operating revenues for the gas marketing services disposition were $32 million for the three months ended March 31, 2018. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

(d) Segment net income (loss) for gas marketing services includes a goodwill impairment charge of $42 million for the three months ended March 31, 2018 related to the sale of Pivotal Home Solutions. See Note 15 to the financial statements in Item 8 of the Form 10-K under "Southern Company Gas" for additional information.

197

Table of Contents

PART II — OTHER INFORMATION
Item 1. Legal Proceedings.
See the Notes to the Condensed Financial Statements herein for information regarding certain legal and administrative proceedings in which the registrants are involved.
Item 1A. Risk Factors.
See RISK FACTORS in Item 1A of the Form 10-K for a discussion of the risk factors of the registrants. There have been no material changes to these risk factors from those previously disclosed in the Form 10-K.
Item 6. Exhibits.
The exhibits below with an asterisk (*) preceding the exhibit number are filed herewith. The remaining exhibits have previously been filed with the SEC and are incorporated herein by reference. The exhibits marked with a pound sign (#) are management contracts or compensatory plans or arrangements.

(4) Instruments Describing Rights of Security Holders, Including Indentures

Georgia Power

(c)1 - Amended and Restated Loan Guarantee Agreement, dated as of March 22, 2019, between Georgia Power and the DOE. (Designated in Form 8-K dated March 22, 2019, File No. 1-6468, as Exhibit 4.1.)

(c)2 - Note Purchase Agreement, dated as of March 22, 2019, between Georgia Power, the DOE, and the FFB. (Designated in Form 8-K dated March 22, 2019, File No. 1-6468, as Exhibit 4.2.)

(c)3 - Promissory Note of Georgia Power, dated as of March 22, 2019. (Designated in Form 8-K dated March 22, 2019, File No. 1-6468, as Exhibit 4.3.)

(c)4 - Amended and Restated Deed to Secure Debt, Security Agreement and Fixture Filing, dated as of March 22, 2019, by Georgia Power to PNC Bank, National Association, doing business as Midland Loan Services, Inc., a division of PNC Bank, National Association. (Designated in Form 8-K dated March 22, 2019, File No. 1-6468, as Exhibit 4.4.)

(c)5 - Amended and Restated Owners Consent to Assignment and Direct Agreement and Amendment to Plant Alvin W. Vogtle Additional Units Ownership Participation Agreement, dated as of March 22, 2019, among Georgia Power, the other Vogtle Owners, the DOE, and PNC Bank, National Association, doing business as Midland Loan Services, Inc., a division of PNC Bank, National Association. (Designated in Form 8-K dated March 22, 2019, File No. 1-6468, as Exhibit 4.5.)

(10) Material Contracts

Southern Company

#*(a)1 - Performance Stock Units Agreement, dated May 23, 2018, between Southern Company and Stephen E. Kuczynski.

#*(a)2 - Retention and Restricted Stock Unit Agreement, dated May 23, 2018, between Southern Company and Stephen E. Kuczynski.

#*(a)3 - Form of Terms for 2018 Named Executive Officer Equity Awards granted under the Southern Company 2011 Omnibus Incentive Compensation Plan.

Alabama Power

\# (b)1 - Form of Terms for 2018 Named Executive Officer Equity Awards granted under the Southern Company 2011 Omnibus Incentive Compensation Plan. See Exhibit 10(a)3 herein.

(24) Power of Attorney and Resolutions

Southern Company

(a) - Power of Attorney and resolution. (Designated in the Form 10-K for the year ended December 31, 2018, File No. 1-3526 as Exhibit 24(a)1.)

Alabama Power

(b) - Power of Attorney and resolution. (Designated in the Form 10-K for the year ended December 31, 2018, File No. 1-3164 as Exhibit 24(b).)

Georgia Power

(c) - Power of Attorney and resolution. (Designated in the Form 10-K for the year ended December 31, 2018, File No. 1-6468 as Exhibit 24(c).)

Mississippi Power

(d) - Power of Attorney and resolution. (Designated in the Form 10-K for the year ended December 31, 2018, File No. 001-11229 as Exhibit 24(d).)

Southern Power

(e) - Power of Attorney and resolution. (Designated in the Form 10-K for the year ended December 31, 2018, File No. 001-37803 as Exhibit 24(e)1.)

Southern Company Gas

(f)1 - Power of Attorney and resolution. (Designated in the Form 10-K for the year ended December 31, 2018, File No. 1-14174 as Exhibit 24(f)1.)

(f)2 - Power of Attorney of Daniel S. Tucker. (Designated in the Form 10-K for the year ended December 31, 2018, File No. 1-14174 as Exhibit 24(f)2.)

(31) Section 302 Certifications

Southern Company

* (a)1 - Certificate of Southern Company's Chief Executive Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

* (a)2 - Certificate of Southern Company's Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

Alabama Power

* (b)1 - Certificate of Alabama Power's Chief Executive Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

* (b)2 - Certificate of Alabama Power's Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

199

Table of Contents

Georgia Power

*(c)1 - Certificate of Georgia Power's Chief Executive Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

*(c)2 - Certificate of Georgia Power's Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

Mississippi Power

*(d)1 - Certificate of Mississippi Power's Chief Executive Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

*(d)2 - Certificate of Mississippi Power's Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

Southern Power

*(e)1 - Certificate of Southern Power Company's Chief Executive Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

*(e)2 - Certificate of Southern Power Company's Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

Southern Company Gas

*(f)1 - Certificate of Southern Company Gas' Chief Executive Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

*(f)2 - Certificate of Southern Company Gas' Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

(32) Section 906 Certifications

Southern Company

*(a) - Certificate of Southern Company's Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

Alabama Power

*(b) - Certificate of Alabama Power's Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

Georgia Power

*(c) - Certificate of Georgia Power's Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

Mississippi Power

*(d)	-	Certificate of Mississippi Power's Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

Southern Power

*(e)	-	Certificate of Southern Power Company's Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

Southern Company Gas

*(f)	-	Certificate of Southern Company Gas' Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

Table of Contents

(101) Interactive Data Files

*	INS	- XBRL Instance Document
*	SCH	- XBRL Taxonomy Extension Schema Document
*	CAL	- XBRL Taxonomy Calculation Linkbase Document
*	DEF	- XBRL Definition Linkbase Document
*	LAB	- XBRL Taxonomy Label Linkbase Document
*	PRE	- XBRL Taxonomy Presentation Linkbase Document

201

Table of Contents

THE SOUTHERN COMPANY
SIGNATURES
Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. The signature of the undersigned company shall be deemed to relate only to matters having reference to such company and any subsidiaries thereof included in such company's report.

THE SOUTHERN COMPANY

By Thomas A. Fanning
Chairman, President, and Chief Executive Officer
(Principal Executive Officer)

By Andrew W. Evans
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

By /s/ Melissa K. Caen
(Melissa K. Caen, Attorney-in-fact)
Date: April 30, 2019

Table of Contents

ALABAMA POWER COMPANY
SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. The signature of the undersigned company shall be deemed to relate only to matters having reference to such company and any subsidiaries thereof included in such company's report.

ALABAMA POWER COMPANY

By Mark A. Crosswhite
Chairman, President, and Chief Executive Officer
(Principal Executive Officer)

By Philip C. Raymond
Executive Vice President, Chief Financial Officer, and Treasurer
(Principal Financial Officer)

By /s/ Melissa K. Caen
(Melissa K. Caen, Attorney-in-fact)
Date: April 30, 2019

203

Table of Contents

GEORGIA POWER COMPANY
SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. The signature of the undersigned company shall be deemed to relate only to matters having reference to such company and any subsidiaries thereof included in such company's report.

GEORGIA POWER COMPANY

By W. Paul Bowers
Chairman, President, and Chief Executive Officer
(Principal Executive Officer)

By David P. Poroch
Executive Vice President, Chief Financial Officer, Treasurer,
and Comptroller
(Principal Financial Officer)

By /s/ Melissa K. Caen
(Melissa K. Caen, Attorney-in-fact)

Date: April 30, 2019

MISSISSIPPI POWER COMPANY
SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. The signature of the undersigned company shall be deemed to relate only to matters having reference to such company and any subsidiaries thereof included in such company's report.

MISSISSIPPI POWER COMPANY

By Anthony L. Wilson
Chairman, President, and Chief
Executive Officer
(Principal Executive Officer)

By Moses H. Feagin
Vice President, Chief Financial Officer,
and Treasurer
(Principal Financial Officer)

By /s/ Melissa K. Caen
(Melissa K. Caen, Attorney-in-fact)

Date: April 30, 2019

Table of Contents

SOUTHERN POWER COMPANY
SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. The signature of the undersigned company shall be deemed to relate only to matters having reference to such company and any subsidiaries thereof included in such company's report.

SOUTHERN POWER COMPANY

By Mark S. Lantrip
Chairman, President, and Chief Executive Officer
(Principal Executive Officer)

By William C. Grantham
Senior
Vice President, Chief Financial Officer, and Treasurer
(Principal Financial Officer)

By /s/ Melissa K. Caen
(Melissa K. Caen, Attorney-in-fact)
Date: April 30, 2019

206

Table of Contents

SOUTHERN COMPANY GAS
SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. The signature of the undersigned company shall be deemed to relate only to matters having reference to such company and any subsidiaries thereof included in such company's report.

SOUTHERN COMPANY GAS

By Kimberly S. Greene
Chairman, President, and Chief Executive Officer
(Principal Executive Officer)

By Daniel S. Tucker
Executive
Vice President, Chief Financial Officer, and Treasurer
(Principal Financial Officer)

By /s/ Melissa K. Caen
(Melissa K. Caen, Attorney-in-fact)

Date: April 30, 2019