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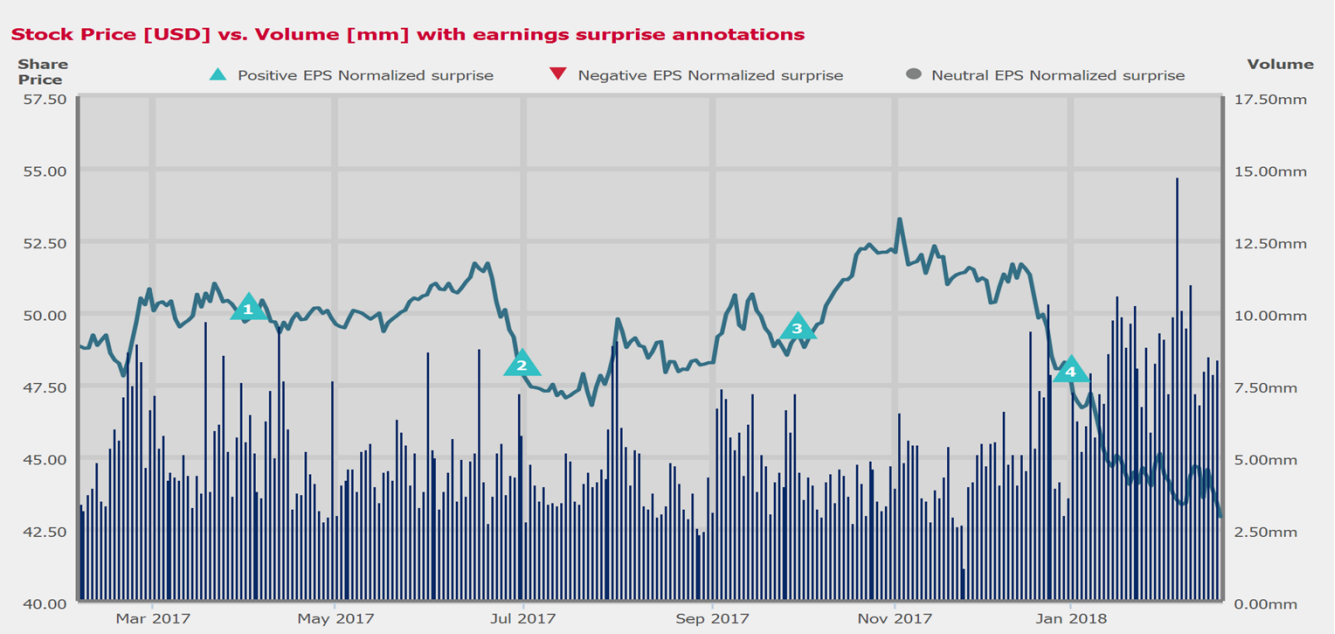
FQ4 2017 Earnings Call Transcripts

Wednesday, February 21, 2018 6:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2017-			-FQ1 2018-	-FY 2017-			-FY 2018-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	0.46	0.51	▲10.87	0.69	2.96	3.02	▲2.03	2.99
Revenue (mm)	5167.73	5629.00	▲8.93	5567.60	22472.06	23031.00	▲2.49	22907.19

Currency: USD
Consensus as of Feb-20-2018 10:55 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2017	0.58	0.66	1 13.79 %
FQ2 2017	0.71	0.73	2 2.82 %
FQ3 2017	1.07	1.11	3 3.74 %
FQ4 2017	0.46	0.51	4 10.87 %

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Presentation

Operator

Ladies and gentlemen, good afternoon. My name is Frank, and I will be your conference operator today. At this time, I would like to welcome everyone to the Southern Company Fourth Quarter 2017 Earnings Call. [Operator Instructions] As a reminder, this conference is being recorded on Wednesday, February 21, 2018.

Southern Company's fourth quarter earnings call will feature slides that are available on our Investor Relations website. You can access the slides at www.investor.southerncompany.com/webcast (sic) [investor.southerncompany.com/information-for-investors/investor-information/webcasts-and-presentations].

I would now like to turn the call over to Mr. Aaron Abramovitz, Director of Investor Relations. Please go ahead, sir.

Aaron Abramovitz

Thank you, Frank. Welcome to Southern Company's Fourth Quarter 2017 Earnings Call. Joining me this afternoon are Tom Fanning, Chairman, President and Chief Executive Officer of Southern Company; and Art Beattie, Chief Financial Officer.

Let me remind you that we will make forward-looking statements today in addition to providing historical information. Various important factors could cause actual results to differ materially from those indicated in the forward-looking statements, including those discussed in our Form 10-K and subsequent filings.

In addition, we will present non-GAAP financial information on this call. Reconciliation to the applicable GAAP measure are included in the financial information we released this morning as well as the slides for this conference call. The slides we will discuss today -- during today's call may be reviewed on our Investor Relations website at investor.southerncompany.com.

At this time, I'll turn the call over to Tom Fanning.

Thomas A. Fanning
Chairman, President & CEO

Good afternoon, and thank you for joining us. As always, we appreciate your interest in Southern Company. As we report our 2017 results and look ahead to 2018 and beyond, our focus remains on investing in premier, state-regulated utilities and providing outstanding risk-adjusted returns for investors. Whether it's great customer satisfaction, high reliability, strong economies, constructive regulatory frameworks or credit quality, our portfolio of electric and gas utilities is a tremendous driver of value. Additionally, Southern Power's large, national portfolio of long-term, contracted renewable and natural gas assets, and PowerSecure's small-but-growing portfolio of distributed energy resources continue to be great complements to our customer-focused business model.

In 2017, we continued to provide the best customer service in the business. In fact, Southern Company and its 4 state-regulated electric utilities continued to achieve the top 5 rankings on the Customer Value Benchmark survey, while Nicor Gas and Virginia Natural Gas were named among the most trusted brands in their industry. Customers are at the center of everything we do, and our utility franchises operate in some of the most constructive jurisdictions in the country, as evidenced by rate outcomes at several of our electric and gas utilities.

2017 represented one of our strongest operational performance years in recent history. Our transmission team had its best year ever, and our generation fleet performed exceptionally well. We also continued our track record of outstanding storm response during an active 2017 hurricane season.

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Let's turn now to Plant Vogtle 3 and 4. Over the course of 2017, Georgia Power and the plant's other co-owners successfully navigated the bankruptcy filing by the project's primary contractor, Westinghouse. Southern Nuclear, the licensee and eventual operator of the plant, successfully assumed control of the site. And the Vogtle owners brought nuclear-experienced, Bechtel, on-site as the prime contractor. The project owners also negotiated a new services contract with Westinghouse, which includes the necessary intellectual property rights to complete and run the project.

Georgia Power filed its recommendation to complete the plant in August of 2017. Since then, there have been significant risk-mitigating milestones. First, in September, Georgia Power received a $1.7 billion Conditional Commitment for incremental DOE loan guarantees, which now total $5.13 billion and are expected to save Georgia Power customers over $500 million in interest costs.

Between October and December, the Vogtle owners received 100% of the $3.7 billion Toshiba guarantee obligation, of which Georgia Power share is $1.7 billion. In late December, the Georgia Public Service Commission unanimously approved and deemed reasonable the revised project cost and schedule estimates, which included an additional $1.6 billion in costs as well as November 2021 and November 2022 in-service dates for Units 3 and 4, respectively.

As part of the approval, the commission further adjusted ROEs during construction and allowed for decoupling of the rate base treatment of Unit 3 and Unit 4. Recall in 2016, the Commission deemed or presumed prudent $5.68 billion in project costs.

And more recently, following extensive bipartisan efforts in the House and in the Senate, the United States Congress eliminated the deadline for receiving advanced nuclear production tax credits, providing approximately $1 billion in future benefits for Georgia Power customers.

We are grateful to the current administration and Congress for recognizing the importance of new nuclear generation and demonstrating renewed federal support for Vogtle 3 and 4. And at the state level, the Georgia Public Service Commission continued its vision and support by moving this project forward.

Now for an update on construction at Vogtle 3 and 4. Since Southern Nuclear has taken control of the site, we have sustained improvements in productivity and critical path execution. As you can see in the materials provided this morning, the team at the site is working towards a construction schedule that is approximately 8 months in advance of the November 2021 and November 2022 in-service dates that were approved by the Georgia Public Service Commission.

Productivity is on track with milestones continuing to be met, including the placement of the 225,000-pound Unit 3 pressurizer in January and the placement of 1,300 cubic yards of concrete inside the Unit 4 containment vessel in December. Of course, there is a long way to go, but these early results are encouraging.

And finally, federal tax reform has been a hot topic for many, and it is no different for Southern Company. The net effect of the new law is that it is tremendously beneficial to customers and our economy. The lower corporate tax rate and the preservation of interest deductibility for utilities are expected to lower customer bills over the long term and help drive continued economic growth throughout our service territories. However, in conjunction with those benefits, the new law also reduces cash flow to our companies. We are keenly focused on preserving our credit profile. Strong credit ratings accrue to the benefit of all of our stakeholders, and preserving those ratings is the focus of ongoing dialogue with our state regulators. As Art will cover later, we will work to support our ratings in a customer- and investor-friendly manner.

I'll turn the call over now to Art for a financial review.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Thank you, Tom. Good afternoon, everyone. As you can see from the materials released this morning, the adjusted results for the fourth quarter of 2017 exceeded our estimates. And for the full year of 2017, we earned at the top end of our guidance range on an adjusted basis. For the fourth quarter of 2017, we had

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reported earnings of $496 million or $0.49 per share, compared with $197 million or $0.20 per share in the fourth quarter of 2016. For the full year of 2017, reported earnings were $842 million or $0.84 per share, compared with $2.45 billion or $2.57 per share in 2016.

On an adjusted basis, for the fourth quarter, Southern Company earned $509 million or $0.51 per share, compared with earnings of $295 million or $0.30 per share during the fourth quarter of 2016. For the full year of 2017, on an adjusted basis, which excludes the charges associated with the Kemper Project along with the related AFUDC equity resulting from extending the schedule prior to the suspension of construction, charges associated with Plant Scherer Unit 3 as a part of Gulf Power's rate case settlement, Wholesale Gas Services, acquisition and integration costs and the net impacts of federal tax reform legislation. Southern Company earned $3.02 billion or $3.02 per share, compared with earnings of $2.76 billion or $2.90 a share in 2016. A reconciliation of our as-reported and as-adjusted results is included in the materials we released this morning. The major earnings drivers for the full year of 2017 when compared to our $2.90 per share adjusted results for 2016 were the inclusion of a full year of Southern Company Gas, including our 50% interest in the Southern Natural Gas pipeline; retail revenue effects at our state-regulated electric utilities; and an aggressive management of O&M at our state-regulated utilities; offset by mild weather, increased interest expense and increased shares.

Before we cover the details of our 2018 guidance and long-term outlook, I'd like to cover the impact of tax reform on our financial outlook. As Tom mentioned earlier, tax reform clearly provides an enormous benefit to customers and the economy. This opportunity, however, comes with a cost in the form of lower operating cash flows at our state-regulated utilities and, absent mitigation, lower FFO to debt ratios.

As we engage with each of our state regulatory jurisdictions regarding the impacts of tax reform, our objective is to provide meaningful rate benefits to customers while preserving our credit quality, which clearly benefit customers over the long run. Working constructively with our regulators, we are seeking to implement a variety of balanced solutions, which achieve both of those key objectives.

For example, in some cases, we'll seek to preserve cash flow by amortizing existing regulatory assets as an offset to tax-related regulatory liabilities. Also, where possible, we'll look to reduce debt at the utility level, which comes in the form of a higher mix of equity in our regulated capital structures. And finally, to ensure adequate credit metrics, we expect some level of deleveraging at the parent company as well. Successful execution of this strategy will result in a financial outlook with less leverage and stronger credit quality, which support the value proposition from our state-regulated utilities.

Now turning to our 2018 EPS guidance. As you can see in the materials provided this morning, our 2018 EPS guidance range is $2.80 per share to $2.95 per share with the midpoint of $2.87. A key driver for the starting point of this range is the receipt by Georgia Power of 100% of its $1.7 billion portion of the Toshiba parent guarantee. Our success in this effort represents an important benefit to shareholders through a significant risk reduction for the Vogtle 3 and 4 project and results in lower cost for Georgia Power customers during construction. A high-level reconciliation of our 2018 EPS guidance range is available in the materials for this call. As for the earnings estimate for the first quarter of 2018, we estimate that we'll earn $0.84 per share.

Looking towards our long-term outlook, starting with the 2018 midpoint of $2.87 per share. Our long-term earnings per share growth outlook is 4% to 6%. It's important to note that the year-over-year earnings contribution from Vogtle 3 -- Units 3 and 4 over the next several years is not linear due to the various construction period ROEs recently approved in VCM 17.

The earnings from Vogtle 3 and 4 represent less than 6% of our expected earnings over the next 5 years. Removing the Vogtle 3 and 4 contribution from the mix results in an underlying Southern Company earnings profile, supported by strong growth across our state-regulated electric and gas utilities that is still expected to grow at 4% to 6%.

Compared to our 2016 Analyst Day, our long-term outlook is being driven by stronger state-regulated earnings profile that is backed by higher invested capital growth in our state-regulated electric utilities and a continued strong performance from our gas LDCs. Invested capital in our state-regulated utilities is projected to grow at an annual rate of approximately 6%. This is driven by a $22 billion, 5-year

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investment plan for our electric utilities, which excludes Vogtle Units 3 and 4 and supports a 4% electric-invested capital growth. Additionally, the state-regulated LDCs within Southern Company Gas are projected to invest $6 billion over the next 5 years with an invested capital growth rate of approximately 9%.

As we discussed on our last earnings call, our future equity needs have continued to evolve over the past year. Over the next 5 years, we forecast an average annual equity need of approximately $1.4 billion. Approximately 80% of this equity is expected to be invested directly into our state-regulated electric and gas utilities to support increased credit-supported equity ratios and to fund increased capital investments, such as Vogtle Units 3 and 4, and our business modernization initiatives. These are terrific opportunities to improve our overall value proposition by enhancing our risk-return profile of our regulated franchises.

We have robust equity plans, which can provide upwards of $1.5 billion per year of new equity, and we have demonstrated an ability to source equity in an investor-friendly manner. For example, we announced in 2017 the sale of Elizabethtown Gas, our planned sale of 33% of Southern Power's solar portfolio and the use of third-party tax equity on new Southern Power projects. As we look to fund our current equity need forecast, we plan to be equally thoughtful and investor focused.

Our 4% to 6% growth rate assumes continued constructive regulatory treatment across our utilities, including tax reform mitigation plans and consolidated FFO to debt of 16% to 16.5%, excluding the impact of Vogtle 3 and 4 during construction. Financial integrity and strong credit ratings provide significant benefits to customers and have always been a priority for us. That emphasis remains unchanged. The top end of our earnings per share growth rate assumes incremental investment opportunities in our state-regulated utilities, combined with aggressive management of O&M inflation, optimized equity funding and better-than-expected growth from our unregulated businesses, including Southern Power.

Now let me touch briefly on our dividend. Southern Company has an outstanding 70-year track record of dividends and dividend growth. Over this period, we've paid 280 consecutive quarterly dividends that have been the same or higher than the previous quarter. We are proud of this track record and continue to make thoughtful, sustainable dividend growth recommendations to our board. We fully believe the financial outlook we have presented, with its improved state-regulated profile, continues to support our objectives of growing the dividend at $0.08 per year.

I will now turn the call back over to Tom for his closing remarks.

Thomas A. Fanning
Chairman, President & CEO

Thanks, Art. As we look forward, we believe Southern Company is solidly positioned to deliver on its value proposition as our customer and community-focused business model continues to serve us well across our portfolio of companies.

We have a transparent, well-balanced path forward to 4% to 6% EPS growth, which should also support our dividend objectives. As we optimize the risk-return equation of our business, our strategies to preserve credit quality post tax reform are intended to provide a solid foundation for value creation for both customers and investors alike.
Thanks, once again, for joining us this afternoon. We'll now move to question-and-answer portion of the call.

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Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Shahriar Pourreza with Guggenheim Partners.

Shahriar Pourreza
Guggenheim Securities, LLC, Research Division

So just 2 quick ones. First, on the $1.4 billion in equity per year that was disclosed today. How much should we think about being allocated to sort of increasing the equity layers at the various utilities? Or another way to ask is, do you sort of have an allocation in mind between the various states for modeling purposes?

Thomas A. Fanning
Chairman, President & CEO

Yes, about half.

Shahriar Pourreza
Guggenheim Securities, LLC, Research Division

Okay, about half, okay.

Thomas A. Fanning
Chairman, President & CEO

Yes.

Shahriar Pourreza
Guggenheim Securities, LLC, Research Division

Okay, that's helpful. And then just on, lastly, on the tax reform assumptions that's in your base assumption, what you're assuming as far as the plan to credit back to rate payers? And is there any potential to spread out further in time, redeploying to sort of near-term capital opportunities in order to get you that incremental investment opportunities to get you to the top end, sort of? How are you thinking about this?

Thomas A. Fanning
Chairman, President & CEO

Yes. You know what's interesting about the incremental capital opportunities, as we looked at the profile of our CapEx over time, I think you've probably heard this before, but we tend to be conservative in our projections. And one of the things that we have seen is that we budget really well for this year and pretty well for the next year and the year after. But starting in years 4 and 5, because they can't see some of the CapEx opportunities, we tend to budget less and less. And so it's very common for us to have kind of a downward-sloping CapEx projection. When we looked in history, in fact, we tend to fill those things in. So in effect, what we have thought about is essentially levelizing as a concept a CapEx appetite at the state companies. And that kind of incremental opportunity gets you more to the top of the range. Of course, we will manage O&M so that there are no price increases to customers as a result of that activity. And I think we have good capacity to do that.

Operator

Our next question comes from the line of Jonathan Arnold with Deutsche Bank.

Jonathan P. Arnold
Deutsche Bank AG, Research Division

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Just curious on the dividend and sticking with the $0.08 when you have such a kind of significant incremental equity need. How did you sort of weigh that up here? Would you -- is it you're targeting a percentage growth? Because I know you've been at this $0.08 level for a while now. How should we think about where you want to be on payout eventually?

Thomas A. Fanning
Chairman, President & CEO

Yes. So one of the things we're looking at, dividend policy is one of the ultimate signaling theories in finance, right? And when we look at our profile kind of over the next 5 years, it's clear that while our payout ratio may be in the 80% range for a period of time, once Vogtle clears to in-service, there is a sharp drop in our payout ratio. When we look at the viability of our ability to deliver on the growth objectives that we've outlined here, we think it's very advisable to stay the course on the dividends, regular, predictable, sustainable, and live with, for a period of time, kind of an 80% payout ratio, maybe a little north of that from year-to-year. Because we believe once we emerge from the construction of Vogtle, we'll be back down in the 70s pretty -- in a pretty healthy way. It's better to stay the course than it is to try and vary over a temporary period.

Jonathan P. Arnold
Deutsche Bank AG, Research Division

Great. And then just on Slide 25, where you look at the growth, with or without Vogtle. Just -- I just want to be clear that the red 4% to 6% is starting off that midpoint of 2018. So...

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes.

Jonathan P. Arnold
Deutsche Bank AG, Research Division

And you're -- effectively, the gray lines are showing us where you would fall within that, given the earnings at Vogtle in any particular year.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes. You got it, right, Jonathan. The starting point is 2018, and the gray lines do represent the nonlinear benefit of Vogtle over that next 4-year time frame, the 5-year -- or yes, 4 years beyond '18.

Thomas A. Fanning
Chairman, President & CEO

And I think it was important for us to point out kind of that fact, Jonathan. When you look at what Vogtle represents to our total earnings picture, it is only 6% of our projected EPS during this next 4 to 5 years. 94% of our earnings are going to still deliver 4% to 6%. So we would want to have that reflected in things like our P/E ratio and stock price performance.

Jonathan P. Arnold
Deutsche Bank AG, Research Division

Please just correct me. You're pretty much saying that the top end of the gray, dotted lines, that you would expect to still be within the 4% to 6% off of the '18 guidance in all of those years? And so I'm curious, what's the purpose of the -- without Vogtle? Because it seems a scenario where you just don't have the Vogtle earnings, but sort of everything else is fine. Just seems to be hard for me to imagine.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

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Well, I think we're just trying to point out the strength of the underlying business, ex -- excluding the earnings associated with Vogtle over the next few years.

Thomas A. Fanning
Chairman, President & CEO

Yes, 90 -- let me say it another way. 94% of our earnings are coming ex Vogtle, and those are exceedingly strong and predictable over time. So all we're laying in is the notion that only 6% is associated with Vogtle during this construction period. Of course, once it goes in-service, it goes back to the earnings rate at Georgia Power.

Jonathan P. Arnold
Deutsche Bank AG, Research Division

So can I maybe just -- I was just going to -- do you have any update on the latest with the Chinese AP1000? And when that might start up? And I'll leave it there.

Thomas A. Fanning
Chairman, President & CEO

That's right. Yes, sure. Westinghouse continues to say they're ready to load fuel. What we believe, the delay in Sanmen and Haiyang is additional regulatory review of the reactor coolant pump and the squib valves. Now we believe -- Westinghouse believes there's no issue there. This appears to be a technical regulatory oversight delay. So we believe any -- we don't know of any problem, and once the regulator in China agrees to go forward, they'll load fuel. We see no impediments.

Jonathan P. Arnold
Deutsche Bank AG, Research Division

For what you've just described, if there was an issue with that sort of feature, is that something that could be changed at the stage you're at? Or is that something that would be so endemic to the design, that it would be hard to change?

Thomas A. Fanning
Chairman, President & CEO

Well, recall some years ago, there were some issues about the reactor coolant pump and there were changes made to the RCP. So that was done way back when. I think everything conforms with our understanding of the engineering and ultimate operational performance. We think there's no issue. It's hard to speculate, if there were a change required, what that would mean to comps and schedule. I just wouldn't want to go there. But the clear understanding we have from Westinghouse, you know that we've had people on-site for years now, is that there is no problem. This is a regulatory matter that the Chinese are dealing with.

Jonathan P. Arnold
Deutsche Bank AG, Research Division

So you still have people at that site kind of reporting back to you.

Thomas A. Fanning
Chairman, President & CEO

Yes, we do.

Operator

Our next question comes from the line of Greg Gordon with Evercore ISI.

Gregory Harmon Gordon
Evercore ISI Institutional Equities, Research Division

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So when I'm looking at the guidance on FFO to debt, presumably the difference between 15% to 15.5%, including Vogtle and the 16% to 16.5% excluding Vogtle is just -- really relates to the earnings stream that you talked about online -- on Slide 24 where the CWIP above the $4.4 billion won't flip into cash flow until the plant's complete?

Thomas A. Fanning
Chairman, President & CEO

That's it. And we've run this by the -- yes, and Greg, we've run this by the rating agencies, and they think that this approach is sensible.

Gregory Harmon Gordon
Evercore ISI Institutional Equities, Research Division

Okay. So assuming the plant comes in when it's supposed to come in, goes into rates, that closes the gap between those 2 numbers.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes, it does.

Gregory Harmon Gordon
Evercore ISI Institutional Equities, Research Division

Great. In terms of the regulatory approaches you're making with the different states, and I guess I'm going -- I'm looking for a slide here, it's Slide 13. You're taking the equity that you're raising, and you're putting it into the following uses: higher regulated equity ratios, reduced parent debt, Vogtle CapEx essentially. Can you take us on a -- without burning up a ton of time, just take us through where you've already got sort of a plan in place? Like in Florida, for instance, I think you've already got a deal on how you're going to use tax. But what's the -- what should we look for in terms of milestones and timing for understanding the outcomes on tax in Georgia, Mississippi and Alabama?

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes, Greg. This is Art. You're right. Gulf Power has a -- has filed a plan or stipulated agreement with a couple of important intervenors. I think the Office of the Public Counsel and the industrial group there has signed on to do the deal where there is an immediate, I believe, refund to customers of a lot of the unprotected deferred taxes. And it also provides for an increase in the equity ratios from 52.5% to 53.5%. And there are also some additional rate reductions that go into place for both their environmental rates and their base rates as well. So it's a comprehensive settlement, but it is a great example of what we're looking for in each of our jurisdictions. That will be different for every jurisdiction we talk about. Georgia, you mentioned, asked for some kind of input or filing last week, and that has been postponed for another couple of weeks. So there's not -- there's still discussions going on there, but nothing to point to. Mississippi has filed an amended PEP filing there as well, and they have basically requested an increase of the equity ratio and provided for some mitigation of the rate increase that was initially filed there. That was about a 4% increase. That has now dropped to 2.5%. So there -- that's another good example of what we are asking the regulator to do. It varies by jurisdictions. In the gas business, we have a number of ongoing rate requests that will include impacts of tax reform. I believe in Illinois, they're going to adjust tax reform based on the January order that they got out of the rate request they filed last year. So it just varies by jurisdictions. Some we may see this year, some we may see next year, so just stay tuned.

Gregory Harmon Gordon
Evercore ISI Institutional Equities, Research Division

And -- I'm sorry, I -- did you mention Alabama? What -- how you might go about that -- this conversation in Alabama?

Arthur P. Beattie

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Former Executive VP & Chief Risk Officer

There's nothing that's -- there have been discussions ongoing, but nothing concrete to share at this point.

Operator

Our next question comes from the line of Paul Fremont with Mizuho.

Paul Basch Michael Fremont
Mizuho Securities USA LLC, Research Division

Sort of a housekeeping question. I guess when we do the numbers, it sort of looks like Southern Power came in a lot stronger than what you had initially have been guiding to. I think you were looking sort of in the 30 -- in the $0.40 range for them and for SONAT. And it looks like it came in sort of north of $1. And it looks like the regulated pieces came in a little bit weaker. Are we reading that right? Or are we missing some adjustments?

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Are you talking for the quarter, Paul? Or are you talking for the year?

Paul Basch Michael Fremont
Mizuho Securities USA LLC, Research Division

For the year.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes. Well, there are a lot of moving parts with Southern Power. They had a lot of new contracts, 7 new solars, 4 new wind contracts, where you've got most of a full year's worth of benefit there year-over-year. You have a lot of increase in depreciation there, but -- I guess one aspect that was not expected last year -- and I'm assuming we're talking on a ex-item basis here, that was some state solar investment tax credits that we discovered we qualified for, that accounted for a roughly $0.04 pickup at Southern Power. So that, in my mind, is the only thing that was really boosting their numbers up this year. The year-over-year, I think the numbers were fairly close in terms of net income.

Paul Basch Michael Fremont
Mizuho Securities USA LLC, Research Division

Okay. So maybe we just need to take it offline to see if we're missing some other adjustments.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Now Paul, on Page 11 of the release, those are not ex items. Those are as-reported items so...

Paul Basch Michael Fremont
Mizuho Securities USA LLC, Research Division

We tried to just apply the adjustments that were broken out at the bottom of the page. But...

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

We can get back to you, and get it right.

Paul Basch Michael Fremont
Mizuho Securities USA LLC, Research Division

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And then, I guess, with respect to infusing equity into the regulated operations, would that happen after you get some form of decision out of the regulators? Or should we start infusing equity even in advance of getting a regulatory response?

Thomas A. Fanning
Chairman, President & CEO

No. We will only invest equity when we have the authority to do so and earn on it appropriately.

Paul Basch Michael Fremont
Mizuho Securities USA LLC, Research Division

Okay. And then is there sort of north limit on what you would ask for in terms of an equity ratio?

Thomas A. Fanning
Chairman, President & CEO

You mean a ceiling?

Paul Basch Michael Fremont
Mizuho Securities USA LLC, Research Division

Yes.

Thomas A. Fanning
Chairman, President & CEO

Well, what we're solving for is to get back to that sort of a debt percent. That's kind of the way we're doing it. And the beauty of this tax reform is, if you solve to an equity ratio, that's the only thing you're doing. I said this on TV this morning, just broad numbers. I think we can preserve our financial integrity and still deliver in the range of 5% to 7% rate reductions. But that just -- that's all you do. There could be a host of other things that could impact the regulatory treatment. But this is a win-win. There's plenty of room for us to preserve our financial integrity and deliver rate reductions.

Operator

Our next question comes from the line of Julien Dumoulin-Smith with Bank of America Merrill Lynch.

Julien Patrick Dumoulin-Smith
BofA Merrill Lynch, Research Division

So on Southern Power, let me just pick up where you left off. Curious on what kind of growth you're seeing out of that business. I know you've talked about tax equity, et cetera. But through the forecast period, how much is that contributing given the updated forecast? And then maybe just a second, on the back of that would be, what's the future of the company, given what seems to be a little bit more of a modest growth profile -- or that's sustained rather?

Thomas A. Fanning
Chairman, President & CEO

So I'm going to let Art fill in the blanks here. I'll give you the top line. And that is certainly, we have seen a bit of a slowdown in the market. For 2018, we expect to earn somewhere in the $325 million range. But you're right. When you look at our overall plan, we are generally deemphasizing the contribution of Southern Power to our growth rate. You must remember though, one of the things that we put in place in the past is a joint development agreement largely for wind with RES. So we're still pursuing all of that discretionary growth, and we'll see how that turns out. With respect to the equity required for those growth opportunities, I think the kind of incremental equity will be minimal, and they'll likely be funded with things like third-party tax equity and internally sourced funds. When you think about that, you should think about that contribution in Southern Power as one of the variables that could drive us upwards in the 4% to 6% range. Art, would you have anything to add there?

Arthur P. Beattie

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Former Executive VP & Chief Risk Officer

Julien, you were asking about where we're going to go. And if you look at our '18 expectations out of Southern Power, there's -- not a lot of that growth is expected to be -- or not a lot of that income, is expected to be driven by new projects. Most of our joint development agreements, the opportunities there, would probably begin delivering income in 2019. As we look year-over-year though, we'll certainly keep about the same level of production tax credits. We just put into -- I guess we just signed an agreement on a new small solar deal.

Thomas A. Fanning
Chairman, President & CEO

Solar deal, 20 megawatts.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes. And then we've got our ongoing energy margins and our amortizations of ITC, which are, I think, year-over-year, will be pretty close to the same. But we've also -- are probably going to book in the first quarter some restructuring gains that will primarily be benefiting our -- or optimizing our state apportionment rates across all the states that we have. And that will be a pickup of, oh, $0.04 or $0.05 of earnings at Southern Power. So when you look at year-over-year, we're going to be pretty close to the same level of net income as we were in 2017.

Julien Patrick Dumoulin-Smith
BofA Merrill Lynch, Research Division

What's the state of the overall business, if it isn't contributing meaningful amounts of growth? I mean, obviously, that's a variable to be solved for. But how do you think about it in that context?

Thomas A. Fanning
Chairman, President & CEO

Well, we think that the state-regulated businesses, especially the way we recast it, represents the lion's share of our growth opportunity. And in fact, when you think about kind of the equity needs, however we solve them, whether it's shares over programs or through investor friendlier kind of means, it represents I think 80% of the shares are going to be tied up in the state-regulated businesses. That provides the lion's share of growth going forward.

Julien Patrick Dumoulin-Smith
BofA Merrill Lynch, Research Division

Right. In fact, actually, if you were to break it down, how much of the 4%, even at the bottom end, is driven by the state programs versus, call it, energy infrastructure versus gas?

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes. That one's hard to break down. We've got so many moving parts in here so that...

Thomas A. Fanning
Chairman, President & CEO

What's -- we need to get back to you on that. But I'll tell you this -- we have thought about this one. The net income profile of Southern Power isn't going to grow a whole lot over the future. But the earnings per share profile, we'll still deliver. In other words, because we're using tax-advantaged equity, while R will grow modestly, E won't grow hardly at all. And so we'll still deliver pretty good EPS. But the thrust is right, and we'll get you the right percents and everything else between the 2. The real lion's share of our EPS growth right now is in the state-regulated businesses.

Operator

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Our next question comes from the line of Paul Ridzon with KeyBanc.

Paul Thomas Ridzon
KeyBanc Capital Markets Inc., Research Division

Quick question. You've had some monetizations to raise equity. What will be a reasonable share count to use for '18?

Thomas A. Fanning
Chairman, President & CEO

Hold on a second.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Let's see, Paul. Our guidance range really assumes a range of possible outcomes. We said we have $1.4 billion need. We certainly got a lot of tools at our disposal. The timing of that will be spread over the year. But as we've also said, we've got opportunities to do it in a shareholder-friendly way, which might mitigate that as well. So it's a hard question to answer. And the range that we've given you is really the outcome of a number of different assumptions around all of the moving parts, so...

Thomas A. Fanning
Chairman, President & CEO

So I guess, one way to say it, Art, is kind of, at its most conservative, we can fully support this 4% to 6% growth rate and our credit metrics by using our internal plans and any at-the-market kind of effort. To the extent we do "investor-friendly means," means other than those shares, we could certainly improve within the range. I mean, so Art's right. It's hard to say. It depends on the success and the opportunity we see elsewhere in the market on some of these other ideas.

Paul Thomas Ridzon
KeyBanc Capital Markets Inc., Research Division

Okay. Then on your slide deck, Slide 16, you've got parent contributing negative $0.47. What was that in '17?

Thomas A. Fanning
Chairman, President & CEO

We'll have somebody looking for it and -- somebody will look for it. I just don't have it at my fingertips.

Paul Thomas Ridzon
KeyBanc Capital Markets Inc., Research Division

And then just back to a previous question. You said look for net income at Southern Power to be essentially flat in '18 versus '17.

Thomas A. Fanning
Chairman, President & CEO

Yes. That's -- 3.25% would be my best guess. Of course, it varies all over the place. Be my guess.

Paul Thomas Ridzon
KeyBanc Capital Markets Inc., Research Division

Is Southern Power not going to see a pickup from tax reform?

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

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Yes, they will be a beneficiary of that and to the tune of $15 million to $20 million. But recall also that we're in the process of monetizing the 33% of the solar portfolio, which would coincidently kind of offset the benefit of the tax gain.

Thomas A. Fanning
Chairman, President & CEO

Through the loss of that income.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

In 2018. So that's right.

Thomas A. Fanning
Chairman, President & CEO

The benefit of tax reform equals the loss of income from the sale of solar. So the net effect is, you keep income constant and you raise cash and offset shares.

Paul Thomas Ridzon
KeyBanc Capital Markets Inc., Research Division

Got it. Got it. I'm good, and if you find that number, you can just inject later on.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Hold on. $0.31. Okay.

Paul Thomas Ridzon
KeyBanc Capital Markets Inc., Research Division

$0.31. What's the driver there? I know that, obviously, the tax shield is a piece of that.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

[indiscernible] the debt has increased. It's a full year effect of a lot of the parent debt, right?

Operator

Our next question comes from the line of Paul Patterson with Glenrock Associates.

Paul Patterson
Glenrock Associates LLC

On Slide 6, I'm sorry if I missed this, but the gasifier write-off of $0.10 for 2018, what's causing that? I mean, could you just elaborate a little bit more on that? Is that sort of onetime in nature?

Thomas A. Fanning
Chairman, President & CEO

That was the amount of shares associated with replacing the hole, the credit quality hole from the write-off of the gasifier last year in '17. That's the ongoing carry and also the income loss associated with that.

Paul Patterson
Glenrock Associates LLC

I got you. So it's the income loss associated with no longer having the gasifier, regulatory speaking, and the impact of issuing equity.

Thomas A. Fanning
Chairman, President & CEO

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Not having an earning asset there. And I'm proud to say, these guys do more of the share than I do. But even the share that I was at. I can remember, drawing people a line that showed the 5% growth, which is the $0.15, and then the write-off and then the $1.7 billion from Toshiba. This is stuff that we've had out there for some time. And this tax reform, this negative $0.06, we're going to work really hard to mitigate that. So I think we're going to be exactly kind of where we thought we might be based on the talk we gave kind of at the balance of '19 -- I mean, 2017.

Paul Patterson
Glenrock Associates LLC

Okay. Then when we look at the Slide 9, you mentioned that there's this business modernization that you're going to be doing some spending on, but O&M is supposed to be reducing or offsetting the revenue impact associated with that number. What I was wondering is, given the other sort of substantial CapEx that you guys are projecting at the regulated utilities, what we should think about the ongoing rate impact of that sort of -- how do we think about the amount of capital that you're spending -- that you're putting into these businesses and your ability to do the business modernization stuff that's outlined on Slide 9 with the other non-business mod, non-Vogtle CapEx, if you follow me?

Thomas A. Fanning
Chairman, President & CEO

Yes, you bet. If you want to look at a company that's done just a terrific job at this, I would go right to Georgia Power. They did a variety of things where they invested in technology and really took money out of the business, not only O&M, but some other investments, like a lot of the local towns. But in that process, we've actually increased the reach to those customers, I want to say by a factor of 4. So you know, it's interesting. Our customer base is getting used to more and more the use of technology in terms of managing our relationship with them. We still have important personal touch in the communities that we're privileged to serve, but I think Georgia Power has been a great example of taking O&M down and improving their CapEx potential. One other really -- and let me say this just another way, if I reverse that. The technology investment that is the modernization effort, in many ways, permit the ability to take O&M out. And if you think about Georgia Power during this time, they were named the most trusted electric utility in America. So we were all worried about, what does this all mean to our relationship with customers, and it remains really strong. One other concept. You guys know that I helped lead for all the electric industry in America, whether it's IOUs, co-ops and munis, but the whole notion of providing appropriate levels of national security for this most critical part of our infrastructure is something that I'm very focused on. And I think this new word that starts to creep into, whether it's an infrastructure bill in Congress or in our dialogues around modernization, goes not to reliability or potentially even service, but to the notion of resilience. That's going to become increasingly important as we think about protecting this most valuable asset.

Paul Patterson
Glenrock Associates LLC

Okay, but I guess what I'm wondering is, what -- how should we think about the rates that -- the rate increases that are associated with your CapEx and EPS growth? Do you follow what I'm saying? In just generally speaking, I'm not asking for granularity here. But just generally speaking, how much do you think you could offset right...

Thomas A. Fanning
Chairman, President & CEO

Something below inflation.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes. That's what I would. And even our profile on nonfuel O&M will be to eliminate the inflation in the numbers. And again, to drive it below 0 if we can to help fund these opportunities for mod capital.

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Thomas A. Fanning
Chairman, President & CEO

And frankly, I think we have the capacity to do that. But if you wanted a number to use, it would be below an inflation rate.

Paul Patterson
Glenrock Associates LLC

Okay. And then just finally on the sales growth. I noticed in the sort of Appendix to the slides that you said flat to extremely modest, I think. Maybe I'm missing the term, but it sounded -- I'm just wondering, just reiterate the sales growth that you guys are looking at in your service territory.

Thomas A. Fanning
Chairman, President & CEO

A bit flat.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Yes, if you get specific by class, it's probably a bit of growth in the industrial class and a bit -- slightly negative on the residential and commercial.

Thomas A. Fanning
Chairman, President & CEO

The southeast still is good though. If you think about it, we've had better than U.S. experience on population growth for both our gas and electric properties. And job growth is much better than the national average in terms of our electric properties. So I mean, what we're seeing in terms of flat is really a function, I think, of technology on behalf of customers. One other effect that we think may occur during this year is, as other companies -- this is actually good for the economy. But as other companies now can expense their CapEx, we may see a lot more facility improvements, store restructurings, manufacturing. And that may have the effect of increasing the rate of investment of energy efficiency. That's why we believe this year is flat.

Operator

Our next question comes from the line of Michael Lapides with Goldman Sachs.

Michael Jay Lapides
Goldman Sachs Group Inc., Research Division

I have 2 focus areas. First, when I look at Slide 26, which has your CapEx by subsidiary on the regulated and at Southern Power, and if I compare it to the same slide in last year's guidance, so the fourth quarter 2016, 5-year outlook, 2 things stand out: One is that the 5-year capital plan for Alabama Power is up materially, $1.5 billion. And the other is that the 5-year gas LDC spend is actually down from 6.7 -- $6.1 billion, so $500 million or $600 million. Can you just talk about what the -- what's happening on the capital side? And what that money is being spent on in those 2 jurisdictions -- or those 2 businesses?

Thomas A. Fanning
Chairman, President & CEO

Yes, the gas one's easy. It's the sale of Elizabethtown that's assumed. So you lost Elizabethtown's CapEx, that's what that is.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

And then Alabama's increase is reflective of modernization capital that was not in last year's numbers.

Michael Jay Lapides

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Goldman Sachs Group Inc., Research Division

Got it, okay. So lots of the incremental T&D in Alabama, and when you file for rate recovery under the annual rate recovery methodologies, you'll benefit and customers will benefit by having the rate reduction that's caused by tax reform. And that gets partially offset by the incremental capital.

Thomas A. Fanning
Chairman, President & CEO

That's right.

Michael Jay Lapides
Goldman Sachs Group Inc., Research Division

Okay. The other thing is -- my other question is, it sounded like you're going to do the $1.4 billion or so of equity every year over the 5 years. But I'm just curious, when I look at the Slide 26, CapEx comes down meaningfully after year really 2, meaning after 2019, meaning it's down almost $2 billion in '20 over '18 and almost $3 billion by '22. Are you really -- shouldn't you be in a position, if that's really what your capital budget is in the out years, that you're basically generating a lot of cash?

Thomas A. Fanning
Chairman, President & CEO

Yes. Well, there's a couple effects in there. Recall, we talked about a variety of means to raise the equity. And what you're referring to is essentially a plan that still achieves 4% to 6% growth, but which uses kind of sales of shares through our plants, okay? To the extent we could do, say, more investor-friendly means of raising cash and equity, that certainly would be lumpier and maybe potentially more front-end loaded and may reduce, frankly, the number of shares required. We'll just see.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

And I think, Michael, as you look at Southern Power on that line, it basically reflects only the committed capital and maintenance capital to support existing assets or new projects that we've committed to. It would be incremental needs for beyond that, and we've kind of set that out in a separate Southern Power slide. I believe it's in the Appendix.

Thomas A. Fanning
Chairman, President & CEO

And the other thing that's going to impact timing for sure will be how the regulatory processes evolve at each of the companies. As I said earlier on this call, we're not going to invest equity until we have a regulatory construct that supports earning on it. So that, also, will have an influence as to how we spend out the capital.

Operator

Our next question comes from the line of Praful Mehta with Citigroup.

Praful Mehta
Citigroup Inc, Research Division

So my question actually was on the regulatory construct you just talked about. Can you be a little bit more specific in terms of some of the variables that are at play? For example, there's a $7.3 billion deferred tax liability. I wanted to understand how is that -- is that protected or unprotected? Or how much is protected and unprotected? What kind of time frame are you working towards in terms of refund? Or are you offsetting against regulatory asset? Some color or context around that cash flow profile would be helpful.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

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Yes, Praful. This is Art. Listen, I don't want to go state-by-state because we're going to be getting ahead of the regulatory process a bit. It will vary by state. Some states have amounts of, say, storm damage cost that is a reg asset on their books. That might be something they avail themselves of to provide a temporary pickup in cash or recovery of that.

Thomas A. Fanning
Chairman, President & CEO

And then deal with equity ratio later.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

And then deal with equity ratios later. So there are all kinds of pieces. And if you take out all of the assets, right, that's the total of the protected and unprotected deferred tax assets, would be, what, $7 billion, $8 billion? And about...

Thomas A. Fanning
Chairman, President & CEO

$7 billion.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

$5.7 billion of that is protected, and the remainder would be unprotected. And that's at a Southern level. So it's going to vary by operating company, and I believe in the K, you can find a breakdown by each of the companies.

Thomas A. Fanning
Chairman, President & CEO

And the other thing that would probably be helpful in thinking about this, what we're solving for is this kind of preserving financial integrity. So that means getting back to appropriate FFO to debt levels. Without mitigations, tax reform would translate to approximately 2% to 3% impact at the states and maybe 3% to 4% at the Southern Company level. That's kind of what we're solving for here. That may be helpful.

Praful Mehta
Citigroup Inc, Research Division

I got you. No, that is super helpful. Appreciate that. And then secondly, just in terms of the Southern Power investment, you talked about $1.5 billion. And you've not kind of shown in your plan, but you've footnoted that there are scenarios under which you can have an incremental $1.5 billion in the out years in terms of Southern Power investment. Like, what would be the variables that would trigger that potential incremental investment?

Thomas A. Fanning
Chairman, President & CEO

Greater-than-expected penetration on the RES investment, for example.

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

The joint development agreement.

Thomas A. Fanning
Chairman, President & CEO

That's right. The wind deal that we've signed up that joint development for. And there could be a variety of other things that come through the transom. I mean, the whole point though is that is purely

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discretionary. And our plan is that largely, we believe that would be funded through internal means or alternative sources of equity, like tax equity, project finance or whatever. The clear message here is this 4% to 6% growth is being driven by investments and performance at our state-regulated entities.

Operator

Our next question comes from the line of Stephen Byrd with Morgan Stanley.

Stephen Calder Byrd
Morgan Stanley, Research Division

I think my questions have been addressed. As I understand it, just on the impact to FFO and tax reform, just given that essentially, you're in discussions with a variety of subsidiaries, that your overall take is it's not the right time to try to give more detailed guidance in terms of the exact impact to FFO from tax reform, just given how many variables are at play. Am I understanding that right?

Thomas A. Fanning
Chairman, President & CEO

Yes, basically. When it's done, it will be done, and we'll tell you everything about it. I think we have outlined though the potential effect of tax reform. We've outlined kind of how we believe we're going about it. So it's some combination of unwinding our regulatory asset or liability or how we expect to restore our credit metric through equity ratios, for example. So that's kind of the how. The what will show themselves when we reach agreement. But we -- historically, we don't like to get in front of the states as they go through these sensitive discussions.

Operator

We have a follow-up question from the line of Shahriar Pourreza with Guggenheim Partners.

Eugene Hennelly
Guggenheim Securities, LLC, Research Division

This is Eugene actually on for Shahriar. Well, I think you kind of touched on it already with saying you don't want to get in front of the state approval process. But I guess, to the extent -- and to follow up to Shahriar's question about the equity going into the regulated utilities, to the extent you're asking for approval for higher equity ratios, could we also -- could we assume that once that's approved, that you'd be earning on that -- the higher equity ratio, like a hypothetical capital structure, as opposed to waiting for actual equity to be infused into the utilities?

Arthur P. Beattie
Former Executive VP & Chief Risk Officer

Well, I think that's a great question, and it's all going to revolve around the timing, the timing of the approvals and when the equity is funded, or how quickly it's funded. And that may occur over time as well so...

Thomas A. Fanning
Chairman, President & CEO

But I think it would be our intention. You're asking a hypothetical. It would be our intention, and it would be simultaneous. In other words, if we got the authority to increase equity ratio, we would make sure that they have the capital that represented that equity in place. And I think that goes back to somebody's earlier question that said, you're looking at a $1.4 billion per year, and we said that might be lumpy based on regulatory outcomes. That would be a reason why.

Operator

At this time, there are no further questions. Sir, are there any closing remarks?

Thomas A. Fanning
Chairman, President & CEO

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Well, it's been an exciting time in the industry. I know -- I think everybody's been wrestling with what does tax reform mean, and it's quite a process. The net of it is, we think there's plenty of economics there to have a win-win agreement with all of our jurisdictions. That is, that we can preserve our financial integrity and reduce rates to customers. And we think that's good, not only for our customers, for the company, but also for the growing economy. I think it's been a real shot in the arm to us all. The other thing I hope you take from this call is that, as we've evaluated these opportunities, there's been a real redistribution of growth away from Southern Power. We're still committed to Southern Power. We still think there's opportunity, and that provides upside to our forecast. But the real redistribution of growth in our focus really goes now to the regulated utilities that we have in some of the best jurisdictions in America. We think this is a plan that will be very promising. And we will execute as well as we can, and we'll update you as things develop. Thank you very much for being with us on this call. We appreciate your interest in Southern Company. See you soon.

Operator
Thank you, sir. Ladies and gentlemen, this does conclude the Southern Company Fourth Quarter 2017 Earnings Call. You may now disconnect. Have a great day, everyone.

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