SOUTHERN CO
Form DEF 14A
April 14, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(A) of the

Securities Exchange Act Of 1934

Filed by the Registrant x Filed by a Party other than the Registrant o

Check the appropriate box:

o Preliminary Proxy Statement
o Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e) (2))
x Definitive Proxy Statement
o Definitive Additional Materials
o Soliciting Materials Pursuant to Rule 14a-12

THE SOUTHERN COMPANY

(Name of Registrant as Specified In Its Charter)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

o Fee computed on table below per Exchange Act Rules 14a-6(i) (1) and 0-11.

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(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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o Fee paid previously with preliminary materials.

o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

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(4) Date Filed:

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Notice of
Annual Meeting

2008
& Proxy Statement

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Letter to Stockholders

David M. Ratcliffe
Chairman, President and
Chief Executive Officer

Dear Fellow Stockholder:

You are invited to attend the 2008 Annual Meeting of Stockholders at 10:00 a.m., ET, on Wednesday, May 28, 2008 at The Lodge Conference Center at Callaway, Gardens, Pine Mountain, Georgia.

At the meeting, I will report on our business and our plans for the future. Also, we will elect our Board of Directors and vote on the other matters set forth in the accompanying Notice.

Your vote is important. Please review the proxy material and vote your proxy as soon as possible.

We look forward to seeing you on May 28th.

David M. Ratcliffe

Notice of Annual Meeting of Stockholders May 28, 2008

TIME AND DATE

10:00 a.m., ET, on Wednesday, May 28, 2008

PLACE

The Lodge Conference Center at Callaway Gardens
Highway 18
Pine Mountain, Georgia 31822

DIRECTIONS

From Atlanta, Georgia take I-85 south to I-185 (Exit 21). From I-185 south, take Exit 34, Georgia Highway 18. Take Georgia Highway 18 east to Callaway.

From Birmingham, Alabama take U.S. Highway 280 east to Opelika. Take I-85 north to Georgia Highway 18 (Exit 2). Take Georgia Highway 18 east to Callaway.

ITEMS OF BUSINESS

(1) Elect 12 members of the Board of Directors;
(2) Ratify appointment of independent registered public accounting firm;
(3) Consider and vote on an amendment to the By-laws of the Company;
(4) Consider and vote on an amendment to the Company s Certificate of Incorporation;
(5) Consider and vote on a stockholder proposal if presented at the meeting as described in Item No. 5 of the Proxy Statement; and
(6) Transact other business properly coming before the meeting or any adjournments thereof.

RECORD DATE

Stockholders of record at the close of business on March 31, 2008 are entitled to attend and vote at the meeting.

ANNUAL REPORT TO STOCKHOLDERS

The Southern Company Annual Report to Stockholders for 2007 (Annual Report) is enclosed but is not a part of this mailing or has been provided separately.

VOTING

Even if you plan to attend the meeting in person, please provide your voting instructions in one of the following ways as soon as possible:

(1) Internet use the Internet address on the proxy form
(2) Telephone use the toll-free number on the proxy form
(3) Mail mark, sign and date the proxy form and return it in the enclosed postage-paid envelope

By Order of the Board of Directors, G. Edison Holland, Jr., Corporate Secretary, April 14, 2008

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Proxy Statement

General Information

Q: How do I give voting instructions?

A: You may attend the meeting and give instructions in person or give instructions by the Internet, by telephone or by mail. Information for giving instructions is on the proxy form. The Proxies, named on the enclosed proxy form, will vote all properly executed proxies that are delivered pursuant to this solicitation and not subsequently revoked in accordance with the instructions given by you.

Q: Can I change my vote?

A: Yes, you may revoke your proxy by submitting a subsequent proxy or by written request received by the Company s corporate secretary before the meeting.

Q: Who can vote?

A: All stockholders of record on the record date of March 31, 2008. On that date, there were 767,624,255 shares of Southern Company common stock (Common Stock) outstanding and entitled to vote.

Q: How much does each share count?

A: Each share counts as one vote, except votes for Directors may be cumulative. Abstentions that are marked on the proxy form are included for the purpose of determining a quorum, but shares that a broker fails to vote are not counted toward a quorum. Neither is counted for or against the matters being considered.

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

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

Q: Can the Company s Proxy Statement and Annual Report be accessed from the Internet?

A: Yes. You can access the Company s website at www.southerncompany.com to view these documents.

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

A: Yes. Most stockholders can elect to receive an e-mail that will provide electronic links to the Annual Report and Proxy Statement. Opting to receive your proxy materials on-line will save us the cost of producing and mailing documents and also will give you an electronic link to the proxy voting site.

You may sign up for electronic delivery when you vote your proxy via the Internet or:

n Go to our investor web site at http://investor.southerncompany.com/;

n Click on the word Enroll for Electronic Delivery of Proxy Materials; and

n Follow the directions provided to complete your enrollment.

Once you enroll for electronic delivery, you will receive proxy materials electronically as long as your account remains active or until you cancel your enrollment. If you consent to electronic access, you will be responsible for your usual Internet-related charges (*e.g.*, on-line fees and telephone charges) in connection with electronic viewing and printing of proxy materials and annual reports. The Company will continue to distribute printed materials to stockholders who do not consent to access these materials electronically.

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Q: What is householding ?

A: Certain beneficial owners of the Company s common stock, sharing a single address, may receive only one copy of the Proxy Statement and Annual Report unless the broker, bank or nominee has received contrary instructions from any beneficial owner at that address. This practice known as householding is designed to reduce printing and mailing costs. If a beneficial owner does not wish to participate in householding, he or she may contact Stockholder Services at (800) 554-7626 or at 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308 and ask to receive a Proxy Statement or Annual Report. As noted earlier, beneficial owners may view the Proxy Statement and Annual Report on the Internet. **Q: When are stockholder proposals due for the 2009 Annual Meeting of Stockholders? A:** The deadline for the receipt of stockholder proposals to be considered for inclusion in the Company s proxy materials for the 2009 Annual Meeting of Stockholders is December 15, 2008. Proposals must be submitted in writing to Patricia L. Roberts, Assistant Corporate Secretary, Southern Company, 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308. Additionally, the proxy solicited by the Board of Directors for next year s meeting will confer discretionary authority to vote on any stockholder proposal presented at that meeting that is not included in the Company s proxy materials unless the Company is provided written notice of such proposal no later than February 28, 2009. **Q: Who pays the expense of soliciting proxies? A:** The Company pays the cost of soliciting proxies. The officers or other employees of the Company or its subsidiaries may solicit proxies to have a larger representation at the meeting. The Company has retained Laurel Hill Advisory Group to assist with the solicitation of proxies for a fee not to exceed $10,000, plus reimbursement of out-of-pocket expenses.

The Company s 2007 Annual Report to the Securities and Exchange Commission (the SEC) on Form 10-K will be provided without charge upon written request to Patricia L. Roberts, Assistant Corporate Secretary, Southern Company, 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308.

Important notice regarding the availability of proxy materials for the Annual Meeting of Stockholders to be held on May 28, 2008:

This Proxy Statement and the Annual Report are also available at http://investor.southerncompany.com/proxy.cfm and http://investor.southerncompany.com/annuals.cfm, respectively.

Corporate Governance

COMPANY ORGANIZATION

Southern Company is a holding company managed by a core group of officers and governed by a Board of Directors that is currently comprised of 12 members.

The nominees for election as Directors consist of eleven non-employees and one executive officer of the Company.

The Board of Directors has adopted and operates under a set of Corporate Governance Guidelines which are available on the Company s website at www.southerncompany.com under Investors/Corporate Governance.

CORPORATE GOVERNANCE WEBSITE

In addition to the Corporate Governance Guidelines, other information relating to corporate governance of the Company is available on the Company s Corporate Governance webpage at www.southerncompany.com under Investors/Corporate Governance or directly at http://investor.southerncompany.com/governance.cfm, including:

n Code of Ethics

n Political Contributions Policy and Report

n By-laws of the Company

n Executive Stock Ownership Guidelines

n Board Committee Charters

n Board of Directors Background and Experience

n Management Council Background and Experience

n SEC filings

n Composition of Board Committees

n Link for online communication with Board of Directors

The Corporate Governance documents also may be obtained by requesting a copy from Patricia L. Roberts, Assistant Corporate Secretary, Southern Company, 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308.

DIRECTOR INDEPENDENCE

No Director will be deemed to be independent unless the Board of Directors affirmatively determines that the Director has no material relationship with the Company, directly, or as an officer, shareowner or partner of an organization that has a relationship with the Company. The Board of Directors has adopted categorical guidelines which provide that a Director will not be deemed to be independent if within the preceding three years:

- The Director was employed by the Company or whose immediate family member was an executive officer of the Company.
- The Director received, or whose immediate family member received, during any 12 month period direct compensation from the Company of more than $100,000, other than director and committee fees. (Compensation received by an immediate family member for services as a non-executive employee of the Company need not be considered.)
- The Director was affiliated with or employed by, or whose immediate family member was affiliated or employed in a professional capacity by, a present or former external auditor of the Company.
- The Director was employed, or whose immediate family member was employed, as an executive officer of a company where any member of the Company s present executives serve on that company s compensation committee.

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- n A company for which the Director currently serves as an executive officer or an employee or whose immediate family member currently serves as an executive officer that makes payments to or receives payments from the Company for property or services in an amount which in any single fiscal year exceeds the greater of $1,000,000 or two percent of that company s consolidated gross revenues.

Additionally, a Director will be deemed not to be independent if the Director or the Director s spouse serves as an executive officer of a charitable organization to which the Company made discretionary contributions exceeding the greater of $1,000,000 or two percent of the organization s total annual charitable receipts.

In determining independence, the Board reviews and considers all commercial, consulting, legal, accounting, charitable or other business relationships that a Director or the Director s immediate family members have with the Company. This review specifically included all ordinary course transactions with entities with which the Directors are associated. In particular, the Board reviewed transactions between subsidiaries of the Company and The Home Depot, Inc. and Vulcan Materials Company. Messrs. Francis S. Blake and Donald M. James are the chief executive officers of The Home Depot, Inc. and Vulcan Materials Company, respectively. Throughout 2007, the subsidiaries purchased goods and services in the amount of $524,669 from The Home Depot, Inc. and $452,920 from Vulcan Materials Company. These amounts represented numerous individual purchases from The Home Depot, Inc. and several individual transactions with Vulcan Materials Company. The Board determined that its subsidiaries followed the Company procurement policies and procedures, that the amounts were well under the thresholds under the Director independence requirements and that neither Mr. Blake nor Mr. James had a direct or indirect material interest in the transactions.

While no Director or immediate family member serves in an executive capacity for a charitable organization, the Board reviewed all contributions made by the Company and its subsidiaries to charitable organizations with which the Directors are associated. The Board determined that the contributions were consistent with similar contributions and none were approved outside the Company s normal procedures.

As a result of its annual review of Director independence, the Board affirmatively determined that none of the following persons who are currently serving as a Director or are nominees for election as Directors has a material relationship with the Company and, as a result, such persons are determined to be independent: Juanita Powell Baranco, Dorrit J. Bern, Francis S. Blake, Jon A. Boscia, Thomas F. Chapman, H. William Habermeyer, Jr., Warren A. Hood, Jr., Donald M. James, J. Neal Purcell, William G. Smith, Jr. and Gerald J. St. Pé. David M. Ratcliffe, a current Director, is Chairman of the Board, President and Chief Executive Officer of the Company. Also, Zack T. Pate who served as a Director during 2007 until his retirement date of May 23, 2007, was determined not to have a material relationship with the Company and to be independent.

COMMUNICATING WITH THE BOARD

Communications may be sent to the Company s Board or to specified Directors by regular mail or electronic mail. Regular mail should be sent to the attention of Patricia L. Roberts, Assistant Corporate Secretary, Southern Company, 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308. The electronic mail address is CORPGOV@southerncompany.com. The electronic mail address also can be accessed from the Corporate Governance webpage located under Investors on the Southern Company website at www.southerncompany.com, under the link entitled Governance Inquiries. With the exception of commercial solicitations, all stockholder communications directed to the Board or to specified Directors will be relayed to them.

DIRECTOR COMPENSATION

Only non-employee Directors are compensated for Board service.

During 2007 the pay components were:

Annual retainers:

- $70,000 of which $30,000 was deferred in Common Stock until Board membership ends
- $10,000 if serving as chair of a standing Board committee with the exception that the chair of the Audit Committee received $25,000

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Equity grants:

- 1,000 additional shares of Common Stock in quarterly grants of 250 shares, deferred until Board membership ends

Meeting fees:

- $2,500 for participation in a meeting of the Board
- $2,000 for participation in a meeting of a committee of the Board other than a meeting of the Audit Committee
- $4,000 for attendance in person at a meeting of the Audit Committee
- $2,000 for participation by telephone in a meeting of the Audit Committee
- $2,000 for each day of a visit to a plant or office of the Company and for any other business meeting at which the Director participated as a representative of the Company

Effective January 1, 2008, the director compensation program was amended with pay components being as follows:

Annual retainers:

- $85,000 cash retainer
- $12,500 if serving as a chair of a committee of the Board
- $12,500 if serving as the Presiding Director of the Board

Equity grant:

- $90,000 in deferred Common Stock units until Board membership ends

Meeting fees:

- Meeting fees are not paid for participation in the initial eight meetings of the Board in a calendar year. If more than eight meetings of the Board are held in a calendar year, $2,500 will be paid for participation in each meeting of the Board beginning with the ninth meeting.
- Meeting fees are no longer paid for participation in a meeting of a committee of the Board.

DIRECTOR DEFERRED COMPENSATION PLAN

The $90,000 equity grant is required to be deferred in shares of Common Stock under the Deferred Compensation Plan for Directors of The Southern Company (the Director Deferred Compensation Plan) and invested in Common Stock units which earn dividends as if invested in Common Stock. Earnings are reinvested in additional stock units. Upon leaving the Board, distributions are made in Common Stock.

In addition, Directors may elect to defer up to 100% of their remaining compensation in the Director Deferred Compensation Plan until membership on the Board ends. Such deferred compensation may be invested as follows, at the Director s election:

- in Common Stock units which earn dividends as if invested in Common Stock and are distributed in shares of Common Stock upon leaving the Board

- at prime interest which is paid in cash upon leaving the Board

All investments and earnings in the Director Deferred Compensation Plan are fully vested and at the election of the Director, may be distributed in a lump-sum payment or in up to 10 annual distributions after leaving the Board. The Company has established a grantor trust that primarily holds Common Stock that funds the Common Stock units that are distributed in Common Stock. Directors have voting rights in the shares held in the trust attributable to these units.

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DIRECTOR COMPENSATION TABLE

The following table reports all compensation to the Company s non-employee Directors during 2007, including amounts deferred in the Director Deferred Compensation Plan. Non-employee Directors do not receive Option Awards or Non- Equity Incentive Plan compensation, and there is no pension plan for non-employee Directors.

Name	Fees Earned or Paid in Cash ($)(1)	Stock Awards ($)(2)(3)	Option Awards ($)	Non-Equity Incentive Plan Compensation ($)	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($)	All Other Compensation ($)(4)	Total ($)
Juanita Powell Baranco	92,500	66,643					159,143
Dorrit J. Bern	106,500	66,643					173,143
Francis S. Blake	81,000	66,643					147,643
Jon A. Boscia(5)							
Thomas F. Chapman	108,500	66,643					175,143
H. William Habermeyer, Jr.(6)	71,666	55,559					127,225
Warren A. Hood, Jr.(7)	19,800					391	20,191
Donald M. James	93,500	66,643					160,143
Zack T. Pate(8)	76,334	14,889				8,061	99,284
J. Neal Purcell	117,500	66,643					184,143
William G. Smith, Jr.	96,500	66,643					163,143
Gerald J. St. Pé	108,500	66,643				114	175,257

(1) Includes amounts voluntarily deferred in the Director Deferred Compensation Plan.

(2) Includes fair market value of equity grants on grant dates and retainer compensation required to be deferred in the Director Deferred Compensation Plan. All such stock awards are vested immediately upon grant.

(3) The aggregate number of Common Stock units held at year-end in the Director Deferred Compensation Plan for each person is provided in the Stock Ownership Table under the column Deferred Stock Units.

(4) Consists of tax gross-ups for an award given to Dr. Pate upon his retirement from the Board and reimbursement for taxes associated with spousal air travel.

(5) Mr. Boscia was elected a Director of the Company effective December 7, 2007. No compensation was paid to Mr. Boscia during 2007.

(6) Mr. Habermeyer was elected a Director of the Company effective March 1, 2007.

(7) Mr. Hood was elected a Director of the Company effective December 7, 2007. Mr. Hood s compensation includes compensation earned in 2007 as a Director of Mississippi Power Company, a wholly-owned subsidiary of the Company. Mr. Hood resigned as a Director of Mississippi Power Company effective December 6, 2007.

(8) Dr. Pate retired as a Director of the Company on May 23, 2007.

DIRECTOR STOCK OWNERSHIP GUIDELINES

Under the Company s Corporate Governance Guidelines, non-employee Directors are required to beneficially own, within five years of their initial election to the Board, Common Stock equal to at least four times the annual Director retainer fee.

MEETINGS OF NON-EMPLOYEE DIRECTORS

Non-employee Directors meet in executive session with no member of management present on each regularly-scheduled Board meeting date. There is a Presiding Director at each of these executive sessions. Dr. Zack T. Pate served as Presiding Director from May 25, 2005 until his retirement on May 23, 2007. Mr. Thomas F. Chapman became the Presiding Director on May 23, 2007 to serve a two-year term or until a successor is named by the non-employee Directors.

COMMITTEES OF THE BOARD

Committee Charters

Charters for each of the five standing committees can be found at the Company s website www.southerncompany.com under Investors/Corporate Governance.

Audit Committee:

n
Members are Mr. Smith, *(Chair)*, Ms. Bern, Mr. Blake and Mr. Hood(1)

n Met 10 times in 2007

n Oversees the Company s financial reporting, audit processes, internal controls and legal, regulatory and ethical compliance; appoints the Company s independent registered public accounting firm, approves its services and fees and establishes and reviews the scope and timing of its audits; reviews and discusses the Company s financial statements with management and the independent registered public accounting firm, including critical accounting policies and practices, material alternative financial treatments within generally accepted accounting principles, proposed adjustments, control recommendations, significant management judgments and accounting estimates, new accounting policies, changes in accounting principles, any disagreements with management and other material written communications between the internal auditors and/or the independent registered public accounting firm and management; and recommends the filing of the Company s annual financial statements with the SEC.

The Board has determined that the members of the Audit Committee are independent as defined by the New York Stock Exchange corporate governance rules within its listing standards and rules of the SEC promulgated pursuant to the Sarbanes-Oxley Act of 2002. The Board has determined that Mr. Smith qualifies as an audit committee financial expert as defined by the SEC.

(1) During 2007 and until January 21, 2008, Mr. Purcell served as Chair of the Committee and Ms. Baranco served as a member of the Committee. Dr. Pate served as a member of the Committee until his retirement from the Board on May 23, 2007. Mr. Smith was appointed Chair and Ms. Bern and Mr. Hood were appointed as members of the committee on January 21, 2008. The Board had determined that Mr. Purcell qualified as an audit committee financial expert.

Compensation and Management Succession Committee:

n
Members are Mr. Purcell, *(Chair)*, Mr. Boscia, Mr. Habermeyer and Mr. James(1)

n
Met eight times in 2007
n
Evaluates performance of executive officers and establishes their compensation, administers executive compensation plans and reviews management succession plans. Annually reviews a tally sheet of all components of the Chief Executive Officer s compensation and takes actions required of it under the Pension Plan for Employees of the Company.

The Board has determined that each member of the Compensation and Management Succession Committee is independent.

(1) During 2007 and until January 21, 2008, Mr. St. Pé served as Chair of the Committee and Mr. Chapman served as a member of the Committee. Mr. Purcell was appointed Chair and Messrs. Boscia and Habermeyer were appointed members of the Committee on January 21, 2008. Mr. Smith served as a member of the Committee in 2007 until his appointment to the Audit Committee on May 23, 2007.

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Governance

The Committee focuses on good governance practices in its operation. In late 2006 through 2007, this included:

Considering compensation for the named executive officers in the context of all of the components of total compensation.

Considering annual adjustments to pay over the course of two meetings and requiring more than one meeting to make other important decisions.

Receiving meeting materials several days in advance of meetings.

Having regular executive sessions of Committee members only.

Having direct access to outside compensation consultants.

Conducting a performance/payout analysis versus peer companies for the annual incentive program to provide a check on the Company s goal-setting process.

Role of Executive Officers

The Chief Executive Officer, with input from the Human Resources staff, recommends to the Committee base salary, target bonus levels, actual bonus payouts and long-term incentive grants for Company officers. The Committee considers, discusses, modifies as appropriate and takes action on such proposals.

Role of Compensation Consultants

In 2007, the Committee directly retained Hewitt Associates (Hewitt) as its outside compensation consultant. The Committee informed Hewitt in writing that it expected Hewitt to advise it if and when there were elements of management proposals to the Committee that Hewitt believed the Committee should not support, set expectations for Hewitt to be honest and direct with the Committee at all times and stated that Hewitt s ongoing engagement would be determined by the Committee.

During 2007, Hewitt assisted the Committee with comprehensive market data and its implications for pay at the Company and various other governance, design and compliance matters. The consultant also advised the Governance Committee on Director pay levels.

The Committee also retained Towers Perrin in 2007 as described in the Compensation Discussion and Analysis on page 24.

Compensation Committee Interlocks and Insider Participation

None of the persons who served as members of the Committee during 2007 was an officer or employee of the Company during 2007 or at any time in the past nor had reportable transactions with the Company.

Finance Committee:

n
Members are Mr. James, (*Chair*), Mr. Boscia and Mr. Purcell(1)

n
Met eight times in 2007
n
Reviews the Company s financial matters, recommends actions such as dividend philosophy to the Board and approves certain capital expenditures

The Board has determined that each member of the Finance Committee is independent.

(1) During 2007 and until January 21, 2008, Ms. Bern served as Chair of the Committee. Mr. James was appointed Chair and Messrs. Boscia and Purcell were appointed members of the Committee on January 21, 2008. Mr. Smith served as a member of the Committee until his appointment to the Audit Committee on May 23, 2007.

Governance Committee:

n
Members are Ms. Baranco, (*Chair*), Mr. Chapman and Mr. St. Pé(1)

- n Met eight times in 2007
- n Oversees the composition of the Board and its committees, determines non-employee Directors compensation, maintains the Company s Corporate Governance Guidelines and coordinates the performance evaluations of the Board and its committees.

The Board has determined that each member of the Governance Committee is independent.

(1) During 2007 and until January 21, 2008, Mr. Chapman served as Chair of the Committee and Ms. Bern served as a member of the Committee. Ms. Baranco was appointed a member and Chair of the Committee on January 21, 2008.

Nominees for Election to the Board

The Governance Committee, comprised entirely of independent Directors, is responsible for identifying, evaluating and recommending nominees for election to the Board. The Committee solicits recommendations for candidates for consideration from its current Directors and is authorized to engage third party advisers to assist in the identification and evaluation of candidates for consideration. Any stockholder may make recommendations to the Governance Committee by sending a written statement setting forth the candidate s qualifications, relevant biographical information and signed consent to serve. These materials should be submitted in writing to the Company s assistant corporate secretary and received by that office by December 12, 2008 for consideration by this Committee as a nominee for election at the Annual Meeting of Stockholders to be held in 2009. Any stockholder recommendation is reviewed in the same manner as candidates identified by the Committee or recommended to the Committee.

The Governance Committee only considers candidates with the highest degree of integrity and ethical standards. The Committee evaluates a candidate s independence from management, ability to provide sound and informed judgment, history of achievement reflecting superior standards, willingness to commit sufficient time, financial literacy and number of other board memberships. The Board as a whole should be diverse and have collective knowledge and experience in accounting, finance, leadership, business operations, risk management, corporate governance and the Company s industry. During 2007, the Committee engaged the services of a third-party search firm to aid in identifying prospective candidates and evaluating their qualifications. The Committee recommends candidates to the Board of Directors for consideration as nominees. Final selection of the nominees is within the sole discretion of the Board of Directors.

Mr. Jon A. Boscia and Mr. Warren A. Hood, Jr. were recommended by the Governance Committee for election to the Board and were elected as Directors effective December 7, 2007. Messrs. Boscia and Hood were identified jointly by the members of the Governance Committee and the third-party search firm.

Nuclear/Operations Committee:(1)

n
Members are Mr. Habermeyer, (*Chair*), Ms. Baranco and Mr. St. Pé(2)
n
Oversees significant information, activities and events relative to significant operations of the Company including nuclear and other generation facilities, transmission and distribution, fuel and information technology initiatives.
n
Attended seven meetings in 2007

(1) Effective January 21, 2008 the Committee s name was changed from the Nuclear Committee to the Nuclear/Operations Committee.

(2) Until his retirement on May 23, 2007, Dr. Pate served as Chair of the Committee at which time Mr. Habermeyer was appointed Chair. Ms. Baranco and Mr. St. Pé were appointed members of the Committee on January 21, 2008.

DIRECTOR ATTENDANCE

The Board of Directors met seven times in 2007. The average attendance for Directors at all Board and Committee meetings was 97 percent. No nominee attended less than 75 percent of applicable meetings.

Directors are expected to attend the Annual Meeting of Stockholders. Ten of the eleven members of the Board of Directors serving on May 23, 2007, the date of the 2007 Annual Meeting of Stockholders, attended the meeting.

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Stock Ownership Table

STOCK OWNERSHIP OF DIRECTORS, NOMINEES AND EXECUTIVE OFFICERS

The following table shows the number of shares of Common Stock owned by Directors, nominees and executive officers as of December 31, 2007. The shares owned by all directors, nominees and executive officers as a group constitute less than one percent of the total number of shares of the class.

		Shares Beneficially Owned Include:		
Directors, Nominees and Executive Officers	**Shares Beneficially Owned(1)**	**Deferred Stock Units(2)**	**Shares Individuals Have Rights to Acquire within 60 days(3)**	**Shares Held by Family Members(4)**
Juanita Powell Baranco	9,542	9,062		
Dorrit J. Bern	41,804	40,304		
Francis S. Blake	16,760	16,560		
Jon A. Boscia	4,000			
Thomas F. Chapman	27,013	27,013		
Thomas A. Fanning	287,834		283,095	
Michael D. Garrett	168,476		168,550	
H. William Habermeyer, Jr.	1,551	1,551		
G. Edison Holland, Jr.	262,498		256,348	
Warren A. Hood, Jr.	3,525	3,525		
Donald M. James	40,956	38,956		
Charles D. McCrary	263,133		258,108	
J. Neal Purcell	28,127	21,903		224
David M. Ratcliffe	1,539,731		1,522,922	
William G. Smith, Jr.	12,360	8,723		
Gerald J. St. Pé	94,587	41,049		8,537
Directors, Nominees and Executive Officers as a Group (21 people)	3,732,711	208,646	3,358,830	8,776

(1) Beneficial ownership means the sole or shared power to vote, or to direct the voting of, a security, or investment power with respect to a security, or any combination thereof.

(2) Indicates the number of Deferred Stock Units held under the Director Deferred Compensation Plan.

(3) Indicates shares of Company common stock that certain executive officers have the right to acquire within 60 days. Shares indicated are included in the Shares Beneficially Owned column.

(4) Each Director disclaims any interest in shares held by family members. Shares indicated are included in the Shares Beneficially Owned column.

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Matters to be Voted Upon

ITEM NO. 1 ELECTION OF DIRECTORS

Nominees for Election as Directors

The Proxies named on the proxy form will vote, unless otherwise instructed, each properly executed proxy form for the election of the following nominees as Directors. If any named nominee becomes unavailable for election, the Board may substitute another nominee. In that event, the proxy would be voted for the substitute nominee unless instructed otherwise on the proxy form. Each nominee, if elected, will serve until the 2009 Annual Meeting of Stockholders.

Juanita Powell Baranco

Age:	58
Director since:	2006
Board committees:	Governance (*chair*), Nuclear/Operations
Principal occupation:	Executive vice president and chief operating officer of Baranco Automotive Group, automobile sales
Other directorships:	Cox Radio Incorporated

Dorrit J. Bern

Age:	57
Director since:	1999
Board committees:	Audit
Principal occupation:	Chairman of the board, president and chief executive officer of Charming Shoppes, Inc., multi-channel apparel, home, food and retail
Other directorships:	Charming Shoppes, Inc., OfficeMax, Inc.

Francis S. Blake

Age:	58
Director since:	2004
Board committees:	Audit
Principal occupation:	Chairman of the board and chief executive officer of The Home Depot, home improvement
Recent business experience:	Served as U.S. Deputy Secretary of Energy from May 2001 to April 2002 and as executive vice president of The Home Depot until January 2007 when he assumed his current position
Other directorships:	The Home Depot, Inc.

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Jon A. Boscia

Age:	55
Director since:	2007
Board committees:	Compensation and Management Succession, Finance
Principal occupation:	President and chief executive officer of Boardroom Advisors, LLC, governance consulting
Recent business experience:	Served as chairman of the board and chief executive officer of Lincoln Financial Group, insurance, institutional investments, comprehensive financial planning and advisory services, until his retirement in 2007.
Other directorships:	None

Thomas F. Chapman

Age:	64
Director since:	2000, Presiding Director since May 23, 2007
Board committees:	Governance
Principal occupation:	Retired chairman of the board and chief executive officer of Equifax, Inc., information services, data analytics, transaction processing and consumer financial products
Recent business experience:	Served as chairman of the board and chief executive officer of Equifax, Inc. until his retirement in 2005
Other directorships:	None

H. William Habermeyer, Jr.

Age:	65
Director since:	2007

Board committees:	Nuclear/Operations (*chair*), Compensation and Management Succession
Principal occupation:	Retired president and chief executive officer of Progress Energy Florida, Inc., electric utility
Recent business experience:	Served as president and chief executive officer of Progress Energy Florida, Inc. until his retirement in 2006
Other directorships:	Raymond James Financial Services, Inc., USEC Inc.

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Warren A. Hood, Jr.

Age:	56
Director since:	2007
Board committees:	Audit
Principal occupation:	Chairman of the board and chief executive officer of Hood Companies, Inc., packaging and construction products
Other directorships:	BancorpSouth Bank, Hood Companies, Inc.

Donald M. James

Age:	59
Director since:	1999
Board committees:	Finance (*chair*), Compensation and Management Succession
Principal occupation:	Chairman of the board and chief executive officer of Vulcan Materials Company, construction materials
Other directorships:	Vulcan Materials Company, Wachovia Corporation

J. Neal Purcell

Age:	66
Director since:	2003

Board committees:	Compensation and Management Succession (*chair*), Finance
Principal occupation:	Retired vice-chairman, audit operations, of KPMG, public accounting
Recent business experience:	Served as KPMG s vice-chairman in charge of National Audit Practice Operations from October 1998 until his retirement in 2002
Other directorships:	Kaiser Permanente Healthcare and Hospitals, Synovus Financial Corporation

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David M. Ratcliffe

Age:	59
Director since:	2003
Principal occupation:	Chairman of the board, president and chief executive officer of the Company
Recent business experience:	Served as president and chief executive officer of Georgia Power Company from May 1999 until January 2004 and as chairman and chief executive officer of Georgia Power Company from January 2004 until April 2004. He served as executive vice president of the Company from May 1999 until April 2004, and as president of the Company from April 2004 until July 2004, when he assumed his current position
Other directorships:	CSX Corporation, Southern system companies Alabama Power Company, Georgia Power Company and Southern Power Company

William G. Smith, Jr.

Age:	54
Director since:	2006
Board committees:	Audit (*chair*)
Principal occupation:	Chairman of the board, president and chief executive officer of Capital City Bank Group, Inc.
Other directorships:	Capital City Bank Group, Inc.

Gerald J. St. Pé

Age:	68
Director since:	1995
Board committees:	Governance, Nuclear/Operations
Principal occupation:	Former president of Ingalls Shipbuilding and retired executive vice president of Litton Industries
Recent business experience:	Served as chief operating officer of Northrop-Grumman Ship Systems from August 1999 to November 2001
Other directorships:	Merchants and Marine Bank, McLand Disposal, Signal International

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Each nominee has served in his or her present position for at least the past five years, unless otherwise noted.

The affirmative vote of a plurality of shares present and entitled to vote is required for the election of Directors.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE NOMINEES LISTED IN ITEM NO. 1.

ITEM NO. 2 RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Audit Committee of the Board of Directors has appointed Deloitte & Touche LLP (Deloitte & Touche) as the Company s independent registered public accounting firm for 2008. This appointment is being submitted to stockholders for ratification. Representatives of Deloitte & Touche will be present at the Annual Meeting to respond to appropriate questions from stockholders and will have the opportunity to make a statement if they desire to do so.

The affirmative vote of a majority of shares present and entitled to vote is required for ratification of the appointment of the independent registered public accounting firm.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR ITEM NO. 2.

ITEM NO. 3 TO AMEND THE COMPANY S BY-LAWS TO (1) IMPLEMENT A MAJORITY VOTE STANDARD FOR THE ELECTION OF DIRECTORS IN UNCONTESTED ELECTIONS, RETAINING A PLURALITY VOTE STANDARD IN CONTESTED ELECTIONS, AND (2) ELIMINATE CUMULATIVE VOTING IN UNCONTESTED ELECTIONS, EACH CONDITIONED ON THE ELIMINATION OF CUMULATIVE VOTING IN THE CERTIFICATE OF INCORPORATION

The Company s Board of Directors determined that it would be in the best interest of the Company and its stockholders to allow for majority voting and to eliminate cumulative voting in uncontested elections of Directors. The Board recommends that the stockholders approve an amendment to the By-laws to change the standard for the election of directors in uncontested elections from a plurality voting standard to a majority voting standard and also to eliminate cumulative voting in uncontested elections, subject to the elimination of cumulative voting in the Certificate of Incorporation, as described more fully in Item No. 4 below.

Under the current plurality vote standard, a director nominee in a director election can be elected or re-elected with as little as a single affirmative vote, even while a substantial majority of the votes cast are withheld from that director nominee. The proposed majority vote standard would require that a nominee for director in an uncontested election receive a for vote from a majority of the votes present and voting at a stockholder meeting to be elected to the Board. Additionally, the By-laws currently provide that when electing directors, stockholders may exercise cumulative voting rights. Under cumulative voting, in voting for directors each holder of common stock is entitled to cast a number of votes equal to the number of votes he or she would be entitled to cast with respect to his or her shares of stock multiplied by the number of directors to be elected. A stockholder may give one candidate all the votes such stockholder is entitled to cast or may distribute such votes among as many candidates as such stockholder chooses. The Board feels that cumulative voting and a majority vote standard are incompatible, and is recommending the elimination of cumulative voting in uncontested elections in conjunction with the adoption of a majority vote standard.

The Board is seeking to eliminate cumulative voting and to implement a majority vote standard in uncontested elections because it believes that such changes are in the best interest of stockholders at this time. The Board recommends retaining cumulative voting in the By-laws for any contested election of directors, to which a plurality standard would apply. Please see Item No. 4 below for additional information regarding the proposed elimination of cumulative voting as contained in the Certificate of Incorporation.

Background of This Item

The proposed majority vote standard would require that a nominee for director in an uncontested election receive a majority of the votes cast at a stockholder meeting in order to be elected to the Board. The Board believes that the proposed majority vote standard for uncontested elections is a more equitable standard. At present, a plurality vote standard guarantees the election of a director in an uncontested election; however, a majority vote standard would mean that nominees in uncontested elections are only elected if a majority of the votes cast are voted in their favor. The Board believes that this majority vote

standard in uncontested director elections will strengthen the director nomination process and enhance director accountability.

Additionally, the Board will add appropriate provisions to its Corporate Governance Guidelines to require any nominee for election as a director of the Company to submit an irrevocable letter of resignation as a condition to being named as such nominee, which would be tendered in the event that nominee fails to receive the affirmative vote of a majority of the votes cast in an uncontested election at a meeting of stockholders. Such resignation would be considered by the Board, and the Board would be required to either accept or reject such resignation within 90 days from the certification of the election results.

The By-laws also currently provide for cumulative voting in the election of directors. The proposed amendment would eliminate cumulative voting in uncontested elections of directors, but retain cumulative voting in contested elections of directors.

The Board does not believe that it should amend the By-laws to establish a majority vote standard and to eliminate cumulative voting while the Company s Certificate of Incorporation still provides for cumulative voting. The elimination of cumulative voting is desirable in connection with the adoption of the majority vote standard with respect to uncontested elections. Because both the Certificate of Incorporation and the By-laws currently provide for cumulative voting, the Board recommends that the provisions in the Certificate of Incorporation relating to cumulative voting be eliminated. The Board believes that less confusion will result if both the majority vote standard and cumulative voting provisions are contained only in the By-laws rather than in both the By-laws and the Certificate of Incorporation. This proposed amendment does not provide any less protection to stockholders because under the Company s By-laws, stockholders are required to ratify any amendment to the By-laws, and any further change in either the majority vote standard or cumulative voting would be subject to the stockholder ratification requirement.

Amendments

The proposed By-law amendment would include the following:

The By-laws will be amended to remove provisions about cumulative voting for directors in uncontested elections and

The plurality voting provisions in the By-laws will be replaced with provisions requiring that, in order to be elected in an uncontested election, a nominee for director must receive the affirmative vote of a majority of the votes cast at a meeting of stockholders, provided that, in contested elections, the affirmative vote of a plurality of the votes cast will be required to elect a director.

A complete text of the amendment is set forth in Appendix A.

The affirmative vote of a majority of shares present and entitled to vote is required for amendment of the By-laws as presented in this Item No. 3.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR ITEM NO. 3

ADOPTION OF THIS ITEM NO. 3 IS CONDITIONED ON THE APPROVAL BY STOCKHOLDERS OF ITEM NO. 4 BELOW. NEITHER ITEM NO. 3 NOR ITEM NO. 4 WILL BE IMPLEMENTED UNLESS BOTH ITEMS ARE APPROVED.

ITEM NO. 4 TO AMEND THE CERTIFICATE OF INCORPORATION TO ELIMINATE CUMULATIVE VOTING IN ELECTIONS OF DIRECTORS, CONDITIONED UPON ADOPTION OF THE MAJORITY VOTE STANDARD AND THE ELIMINATION OF CUMULATIVE VOTING IN CONTESTED ELECTIONS IN THE BY-LAWS

The Board has determined that it would be in the best interest of the Company and its stockholders to require that a nominee or director in an uncontested election receive a majority of the votes cast at a stockholders meeting to be elected to the Board (see Item No. 3 above). The Board is seeking to eliminate cumulative voting in uncontested elections because it believes that a change to a majority vote standard in uncontested elections is in the best interest of stockholders at this time, and it views cumulative voting as inconsistent with a majority vote standard for the election of directors.

The elimination of cumulative voting in uncontested elections requires an amendment to the By-laws as discussed in Item No. 3 above, and also requires an amendment to the Certificate of Incorporation, which would remove subdivision (2) of Article Ninth (the cumulative voting provision). The Board feels it is appropriate to remove cumulative voting entirely from the Certificate of Incorporation and to amend the cumulative voting provisions discussed above in the By-laws so that all of

the provisions pertaining to voting in director elections are contained in the By-laws. As discussed above, cumulative voting will be permitted in a contested election, to which the plurality voting standard applies.

This amendment to the Certificate of Incorporation has been approved and declared advisable by the Board but requires adoption by the Company s stockholders. This elimination would facilitate adoption of the majority vote standard for the election of directors in the manner described above in Item No. 3.

This Item would not change the present number of directors, and the Board would retain the authority to change that number and to fill any vacancies or newly created directorships.

Background of This Item

The Board is seeking to eliminate cumulative voting because it believes that a change to a majority vote standard in uncontested elections would be in the best interest of stockholders at this time and it views cumulative voting as incompatible with a majority vote standard for election.

Amendment

The proposed amendment would eliminate subdivision (2) of Article Ninth of the Certificate of Incorporation in its entirety.

Approval of this Item requires the affirmative vote of at least two-thirds of the outstanding shares of the Company s common stock.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR ITEM NO. 4.

ADOPTION OF THIS ITEM NO. 4 IS CONDITIONED ON THE APPROVAL BY STOCKHOLDERS OF ITEM NO. 3 ABOVE. NEITHER ITEM NO. 3 NOR ITEM NO. 4 WILL BE IMPLEMENTED UNLESS BOTH ITEMS ARE APPROVED.

ITEM NO. 5 STOCKHOLDER PROPOSAL ON ENVIRONMENTAL REPORT

The Company has been advised that The Sisters of Charity of Saint Elizabeth, P. O. Box 476, Convent Station, New Jersey 07961, holder of 100 shares of Company common stock; American Baptist Home Mission Society of The American Baptist Churches, USA, P. O. Box 851, Valley Forge, Pennsylvania 19482, holder of 1,942 shares of Company common stock; Congregation of Benedictine Sisters, 285 Oblate Drive, San Antonio, TX holder of 14,000 shares of Company common stock, and Sisters of St. Dominic of Caldwell New Jersey, 40 South Fullerton Avenue, Montclair, New Jersey 07042, holder of 100 shares of Company common stock, propose to submit the following resolution at the 2008 Annual Meeting of Stockholders.

Whereas:

The International Energy Agency warned in its 2007 World Energy Outlook that urgent action is needed if greenhouse gas (GHG) concentrations are to be stabilized at a level that would prevent dangerous interference with the climate system.

In October 2006, a report authorized by former chief economist of The World Bank, Sir Nicolas Stern, estimated that climate change will cost between 5% and 20% of GDP if emissions are not reduced, and that GHGs can be reduced at a cost of approximately 1% of global economic growth.

U.S. power plants are responsible for nearly 40% of the country s carbon dioxide emissions, and 10% of global carbon dioxide emissions.

Coal-burning power plants are responsible for 80% of the carbon dioxide (CO_2) emissions from all U.S. power plants and Southern Company is the second-largest emitter of CO_2, the GHG linked to climate change, among U.S. power generators.

Since 1990, CO_2 emissions from U.S. power plants have increased by 27%. Moreover, the global rate of GHG emissions from burning fossil fuels increased four-fold between 2000 and 2005 (U.S. Energy Information Administration).

Levels of CO_2, which persist in the atmosphere for over 100 years, are now higher than anytime in the past 400,000 years and they will continue to rise as long as emissions from human activities continue.

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While CO_2 is not now regulated at the federal level, the U.S. Senate Environment and Public Works Committee voted to report the Lieberman-Warner Security Act (S. 2191) to the full Senate in December 2007. The bill would reduce emissions by almost 20% below current levels by 2020 and 60% by 2050.

Shareholders desire to understand how well our company would be prepared to operate under mandatory 20% and 60% CO_2 emissions reduction mandates, were such carbon constraints enacted by the U.S. Congress.

AEP, the nation s largest electric generator, Entergy and Exelon have set total GHG emissions reduction targets. Duke, Exelon, FPL, NRG, and others, through their participation in the U.S. Climate Action Partnership, have also publicly stated that the U.S. should reduce its GHG footprint by 60% to 80% from current levels by 2050. They have endorsed adoption of mandatory federal policy to limit CO_2 emissions as a way to provide economic and regulatory certainty needed for major investments in our energy future.

Southern Company however, opposes mandatory regulation of CO_2 and other GHG emissions in favor of voluntary action. While our company has added cleaner coal burning capacity, is investing in renewable energy, and has reduced the intensity of its CO_2 emissions, it has yet to adopt a voluntary reduction goal for its total CO_2 emissions. (Southern Company Response to CDP5)

RESOLVED: Shareholders request that the Board of Directors report to shareholders actions the company would need to take to reduce total CO_2 emissions, including quantitative goals for existing and proposed plants based on current and emerging technologies, by September 30, 2008. Such report shall omit proprietary information and be prepared at reasonable cost.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ITEM NO. 5 FOR THE FOLLOWING REASONS:

The Company issued in 2005 the *Environmental Assessment: Report to Shareholders,* outlining options and actions the Company is taking with regard to CO_2 and other emissions, including an extensive review of CO_2 price scenarios; issued in 2006 its *Corporate Responsibility Report,* which included data on emissions and actions being undertaken to address those emissions; and in April 2008, updated our report, *Climate Change A Summary of Southern Company Actions,* on specific current and long-term activities to address CO_2 emissions, as well as issued a report, *Energy Efficiency Regulatory Structures*, on the need for and the impacts of energy efficiency efforts as a resource to meet growth and regulatory structures. All these reports are available either through the Company s external website at www.southerncompany.com or by contacting Patricia L. Roberts, Assistant Corporate Secretary, Southern Company, 30 Ivan Allen Jr. Boulevard NW, Atlanta, Georgia 30308 and requesting a copy.

The vote needed to pass the proposed stockholders resolution is a majority of the shares represented at the meeting and entitled to vote.

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

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Audit Committee Report

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

The independent registered public accounting firm is responsible for expressing opinions on the conformity of the consolidated financial statements with accounting principles generally accepted in the United States and on the conformity of management s assessment of the effectiveness of the Company s internal control over financial reporting and the effectiveness of the Company s internal control over financial reporting with the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Committee reviewed with the independent registered public accounting firm, the firm s judgments as to the quality, not just the acceptability, of the Company s accounting principles and such other matters as are required to be discussed with the Committee under generally accepted auditing standards, rules and regulations of the Public Company Accounting Oversight Board (the PCAOB) and the SEC and the New York Stock Exchange corporate governance rules. In addition, the Committee has discussed with the independent registered public accounting firm its independence from management and the Company as required under rules of the PCAOB. The Committee also has considered whether the independent registered public accounting firm s provision of non-audit services to the Company is compatible with maintaining the firm s independence.

The Committee discussed the overall scopes and plans with the Company s internal auditors and independent registered public accounting firm for their respective audits. The Committee meets with the internal auditors and independent registered public accounting firm with and without management present, to discuss the results of their audits, evaluations by management and the independent registered public accounting firm of the Company s internal control over financial reporting, and the overall quality of the Company s financial reporting. The Committee also meets privately with the Company s compliance officer. The Committee held 10 meetings during 2007.

In reliance on the reviews and discussions referred to above, the Committee recommended to the Board of Directors (and the Board approved) that the audited consolidated financial statements be included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007 and filed with the SEC. The Committee also reappointed Deloitte & Touche as the Company s independent registered public accounting firm for 2008. Stockholders will be asked to ratify that selection at the Annual Meeting of Stockholders.

Members of the Committee:

William G. Smith, Jr., Chair
Dorrit J. Bern
Francis S. Blake
Warren A. Hood, Jr.

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PRINCIPAL ACCOUNTING FIRM FEES

The following represents the fees billed to the Company for the last two fiscal years by Deloitte & Touche the Company s principal independent registered public accounting firm:

	2007	2006
	(In thousands)	
Audit Fees(a)	$ 12,525	$ 12,994
Audit-Related Fees(b)	913	673
Tax Fees(c)	0	90
All Other Fees	0	0
Total	$ 13,438	$ 13,757

(a) Includes services performed in connection with financing transactions

(b) Includes benefit plan and other non-statutory audit services and accounting consultations in both 2007 and 2006

(c) Includes review services in connection with the consolidated federal tax return and tax compliance licensing and training costs

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

Executive Compensation

COMPENSATION DISCUSSION AND ANALYSIS

In this Compensation Discussion and Analysis (the CD&A) and elsewhere in this Proxy Statement, references to the Compensation Committee are to the Compensation and Management Succession Committee of the Company s Board of Directors.

GUIDING PRINCIPLES AND POLICIES

The Company s executive compensation program is based on a philosophy that total executive compensation must be competitive with the companies in our industry, must be tied to and motivate our executives to meet our short- and long-term performance goals and must foster and encourage alignment of executive interests with the interests of our stockholders and our customers. The program generally is designed to motivate all employees, including executives, to achieve operational excellence and financial goals while maintaining a safe work environment.

Our executive compensation program places significant focus on rewarding performance. The program is performance-based in several respects:

- Our actual earnings per share (EPS) and business unit performance, which includes return on equity (ROE) or net income, compared to target performance levels established early in the year, determine the ultimate annual incentive program payouts.
- Common Stock price changes result in higher or lower ultimate values of stock options.
- Our dividend payout and total shareholder return compared to those of our industry peers lead to higher or lower payouts under the Performance Dividend Program (performance dividends).

In support of our performance-based pay philosophy, we have no general employment contracts with our named executive officers or guaranteed severance, except upon a change in control, and no pay is conditioned solely upon continued employment of any of the named executive officers, other than base salary.

Our pay-for-performance principles apply not only to the named executive officers, but to thousands of employees. Our short-term incentive program covers nearly all of our nearly 27,000 employees and our change-in-control protection program covers all employees not part of a collective bargaining unit. Our stock options and performance dividends cover approximately 6,300 employees. These programs engage our people in our business, which ultimately is good not only for them, but for our customers and our stockholders.

OVERVIEW OF EXECUTIVE COMPENSATION COMPONENTS

Our executive compensation program is composed of several components, each of which plays a different role. The table below discusses the intended role of each material pay component, what it rewards and why we use it. Following the table is additional information that describes how we made 2007 pay decisions.

Pay Element	Intended Role and What the Element Rewards	Why We Use the Element

Base Salary	Base salary is pay for competence in the executive role, with a focus on scope of responsibilities.	Market practice. Provides a threshold level of cash compensation for job performance.
Annual Incentive	The Company s annual incentive program rewards achievement of operational, EPS and business unit financial goals.	Market practice. Focuses attention on achievement of short-term goals that ultimately works to fulfill our mission to customers and leads to increased stockholder value in the long term.

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Pay Element	Intended Role and What the Element Rewards	Why We Use the Element
Long-Term Incentive: Stock Options	Stock options reward price increases in the Common Stock over the market price on date of grant, over a 10-year term.	Market practice. Performance-based compensation. Aligns executives interests with those of stockholders.
Long-Term Incentive: Performance Dividends	Performance dividends provide cash compensation dependent on the number of stock options held at year end, the Company s dividends paid during the year and four-year total shareholder return versus industry peers.	Market practice. Performance-based compensation. Enhances the value of stock options and focuses executives on maintaining a significant dividend yield for stockholders. Aligns executives interests with stockholders interests since payouts are dependent on the returns realized by our stockholders versus those of our industry peers.
Retirement Benefits	The Southern Company Deferred Compensation Plan provides the opportunity to defer to future years up to 50% of base salary and all or part of annual incentives or performance dividends in either a prime interest rate or Common Stock account. Executives participate in employee benefit plans available to all employees of the Company, including a 401(k) savings plan and the funded Southern Company Pension Plan (Pension Plan). The Supplemental Benefit Plan counts pay, including deferred salary, ineligible to be counted under the Pension Plan and the 401(k) plan due to Internal Revenue Service rules. The Supplemental Executive Retirement Plan counts annual incentive pay above 15% of base salary for pension purposes. Additional years of service agreements provide enhanced retirement benefits as if a participant had worked additional years at the Company.	Market practice. Permitting compensation deferral is a cost-effective method of providing additional cash flow to the Company while enhancing the retirement savings of executives. The purpose of these supplemental plans is to eliminate the effect of tax limitations on the payment of retirement benefits. Additional years of service enhancements are provided on an as-needed basis to attract and retain executives who were employed by the Company earlier in their careers. Represents an important component of competitive market-based compensation in our peer group and generally.

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Pay Element	Intended Role and What the Element Rewards	Why We Use the Element
Perquisites and Other Personal Benefits	Personal financial planning maximizes the perceived value of our executive compensation program to executives and allows executives to focus on Company operations. Home security systems lower our risk of harm to executives. Club memberships are provided primarily for business use.	Perquisites benefit both the Company and executives, at low cost to the Company.
Post-Termination Pay	Change-in-control agreements provide severance pay, accelerated vesting and payment of short- and long-term incentive awards upon a change in control of the Company coupled with involuntary termination not for Cause or a voluntary termination for Good Reason.	Market practice. Providing protections to executives upon a change in control minimizes disruption during a pending or anticipated change in control. Payment and vesting occur only upon the occurrence of both an actual change in control and loss of the executive s position.

MARKET DATA

For the named executive officers, the Compensation Committee reviews compensation data from large, publicly-owned electric and gas utilities. The data was developed and analyzed by Hewitt Associates, one of the compensation consultants retained by the Compensation Committee. The companies included each year in the primary peer group are those whose data is available through the consultant s database. Those companies are drawn from this list of regulated utilities of $2 billion in revenues and up. Proxy data for this entire list of companies below also is used. No other companies data are used in our market-pay benchmarking.

Allegheny Energy, Inc.
Alliant Energy Corporation
Ameren Corporation
American Electric Power Company, Inc.
CenterPoint Energy, Inc.
CMS Energy Corporation
Consolidated Edison, Inc.
Constellation Energy Group, Inc.
Dominion Resources Inc.
DTE Energy Company
Duke Energy Corporation
Edison International
Energy East Corporation
Entergy Corporation
Exelon Corporation
FirstEnergy Corp.
FPL Group, Inc.
Great Plains Energy Incorporated
Hawaiian Electric Industries, Inc.
KeySpan Corporation
NiSource Inc.
Northeast Utilities
NSTAR
OGE Energy Corp.
Pepco Holdings, Inc.
PG&E Corporation
Pinnacle West Capital Corporation
PNM Resources, Inc.
PPL Corporation
Progress Energy, Inc.
Public Service Enterprise Group Incorporated
Puget Energy, Inc.
SCANA Corporation
Sempra Energy
Sierra Pacific Resources
TECO Energy, Inc.
TXU Corp.
Vectren Corporation
Wisconsin Energy Corporation
WPS Resources Corporation
Xcel Energy Inc.

The Company is one of the largest U.S. utility companies in revenues and market capitalization, and its largest business units are some of the largest in the industry as well. For that reason, the consultant size-adjusts the market data in order to fit it to the scope of our business.

In using this market data, market is defined as the size-adjusted 50th percentile of the data, with a focus on pay opportunities at target performance (rather than actual plan payouts). The Company specifically looks at the market data for chief executive officer positions and other positions in terms of scope of responsibilities, that most closely resemble the positions held by our named executive officers. Based on that data, the Company recommends to the Compensation Committee a total target compensation opportunity for each named executive officer. Total target compensation opportunity is the sum of base salary, annual incentive payout (at the target performance level), stock option awards at a target value and performance dividend payout at a target value. Actual compensation paid may be more or less than the total target compensation

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opportunity based on actual performance above or below target performance levels. As a result, our compensation program is designed to result in payouts that are market-appropriate given our performance for the year or period.

The Company did not target a specified weight for base salary or annual or long-term incentives as a percent of total target compensation opportunities, nor did amounts realized or realizable from prior compensation serve to increase or decrease 2007 compensation amounts. Total target compensation opportunities for senior management as a group are managed to be at the median of the market for companies our size and in our industry. The total target compensation opportunities established in 2007 for each named executive officer are shown below.

Name	Salary	Annual Incentive	Long-Term Incentive	Total Target Compensation Opportunity
D. M. Ratcliffe	$ 1,075,700	$ 1,075,700	$ 4,579,700	$ 6,731,100
T. A. Fanning	$ 616,000	$ 463,000	$ 845,000	$ 1,924,000
M. D. Garrett	$ 621,000	$ 465,750	$ 854,000	$ 1,940,750
C. D. McCrary	$ 634,000	$ 475,500	$ 871,000	$ 1,980,500
G. E. Holland, Jr.	$ 542,000	$ 325,200	$ 643,000	$ 1,510,200

As is our long-standing practice, the salary levels shown above were not effective until March 2007. Therefore, the amounts reported in the Summary Compensation Table are lower because that table reports actual amounts paid in 2007. Also, the amounts reviewed by the Committee and reported here are rounded and may differ slightly from amounts reported in the other tables and charts herein. For purposes of comparing the value of our compensation program to the market data, stock options are valued at 15%, and performance dividend targets at 10%, of the average daily Common Stock price for the year preceding the grant, both of which represent risk-adjusted present values on the date of grant and are consistent with the methodologies used to develop the market data. For the 2007 grant of stock options and the performance dividend targets established for the 2007 2010 performance period, this value was $8.515 per stock option granted. In the long-term incentive column, 60% of the value shown is attributable to stock options and 40% attributable to performance dividends. The stock option value used for market data comparisons exceeds the value reported in the Grants of Plan-Based Awards Table because the value above is calculated assuming that the options are held for their full 10-year term. The calculation of the Black-Scholes value reported in the Grants of Plan-Based Awards Table uses historical holding period averages of approximately five years.

As discussed above, the Compensation Committee targets total target compensation opportunities for senior executives as a group at market. Therefore, some executives may be paid somewhat above and others somewhat below market. This practice allows for minor differentiation based on time in the position, scope of responsibilities and individual performance. The differences in the total pay opportunities for each named executive officer are based almost exclusively on the differences indicated by the market data for persons holding similar positions. However, in setting the total target compensation opportunities for Messrs. Garrett and McCrary in 2007, the Compensation Committee recognized that Mr. McCrary has been in his position considerably longer than Mr. Garrett and that while the market data may distinguish between their two positions based on the size of the business units they lead, the Company s CEO and the Compensation Committee consider their positions equivalent in terms of scope of responsibility. They lead the Company s two largest business units. The average total target compensation opportunities for the named executive officers for 2007 were four percent above the market data described above. However, because of the use of market data from a large number of peer companies for positions that are not identical in terms of scope of responsibility from company to company, we do not consider this difference material and we continue to believe that our compensation program is market-appropriate.

In 2007, the Compensation Committee engaged an additional executive compensation consulting firm, Towers Perrin, to conduct a broad assessment of the Company s executive compensation program. Benchmarking data as well as actual levels of payouts made at our peer companies was reviewed. The consulting firm was directed to review the level of total target pay opportunities, the weight of each primary pay component and the annual and long-term incentive goal metrics. Based on the findings from this review, the Company and the Compensation Committee continue to believe that our executive compensation program provides the appropriate level and mix of compensation for the senior management of the Company, including the named executive officers.

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In 2004, the Compensation Committee received from its executive compensation consulting firm a detailed comparison of our executive benefits program to the benefits of a group of other large utilities and general industry companies. The results indicated that the Company s executive benefits program was slightly below market. The Compensation Committee plans to have this study updated in 2008.

DESCRIPTION OF KEY COMPENSATION COMPONENTS

2007 Base Salary

Base salaries for each of the named executive officers for 2007 were recommended for the Compensation Committee s approval by Mr. Ratcliffe, except for his own salary. Those recommendations took the market data into account, as well as, the need to retain an experienced team, time in position and individual performance which included the degree of competence and initiative exhibited and the individual s relative contribution to the results of operations in prior years. The Compensation Committee approved the recommended salaries in 2007.

Mr. Ratcliffe s 2007 base salary was set by the Compensation Committee and was influenced by the above-described market data and Mr. Ratcliffe s performance and time in the position.

2007 Incentive Compensation

Achieving Operational and Financial Goals Our Guiding Principle for Incentive Compensation

Our number one priority is to provide our customers outstanding reliability and superior service at low prices while achieving a level of financial performance that benefits our stockholders in the short and long-term.

In 2007, we strove for and rewarded:

Continued industry-leading reliability and customer satisfaction, while maintaining our low retail prices relative to the national average; and

Meeting increased energy demand with the best economic and environmental choices.

In 2007, we also focused on and rewarded:

EPS Growth A continuation of growing EPS an average of five percent per year from a base, excluding earnings from synthetic fuel investments, established in 2002. The target goal shown below is five percent greater than the goal established for 2006.

ROE in the top quartile of comparable electric utilities.

Dividend Growth.

Long-term total shareholder return.

Financial Integrity An attractive risk-adjusted return, sound financial policy and a stable A credit rating.

The incentive compensation program is designed to encourage achievement of these goals.

Mr. Ratcliffe, with the assistance of our Human Resources staff, recommends to the Compensation Committee program design and award amounts for senior executives, including the named executive officers.

2007 Annual Incentive Program

Program Design

The Performance Pay Program is the Company s annual incentive program. Most employees of the Company are participants, including the named executive officers, a total of nearly 27,000 participants.

The performance measured by the program uses goals set at the beginning of each year by the Compensation Committee.

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An illustration of the annual incentive goal structure for 2007 is provided below.

Operational goals for 2007 were safety, customer service, plant availability, transmission and distribution system reliability and inclusion. Each of these operational goals is explained in more detail under Goal Details below. The result of all operational goals is averaged and multiplied by the bonus impact of the EPS and business unit financial goals. The amount for each goal can range from 0.90 to 1.10, or 0.00 if a threshold performance level is not achieved as more fully described below. The level of achievement for each operational goal is determined and the results are averaged. Each of our business units has operational goals. For Messrs. Garrett and McCrary, the payout is adjusted up or down based on the operational goal results for Georgia Power Company and Alabama Power Company, respectively. For Messrs. Ratcliffe, Fanning and Holland, it is calculated using the corporate-wide weighted average of the operational goal results.

EPS is weighted at 50% of the financial goals. EPS is defined as earnings from continuing operations divided by average shares outstanding during the year, excluding earnings from synthetic fuel investments. The EPS performance measure is applicable to all participants in the Performance Pay Program, including the named executive officers.

Business unit financial performance is weighted at 50% of the financial goals. For our traditional utility operating companies (Alabama Power Company, Georgia Power Company, Gulf Power Company and Mississippi Power Company), the business unit financial performance goal is ROE, which is defined as the operating company s net income divided by average equity for the year. For our other business units, we establish financial performance measures that are tailored to each business unit.

For Messrs. Garrett and McCrary, the annual incentive payout is calculated using the ROE for Georgia Power Company and Alabama Power Company, respectively. For Messrs. Ratcliffe, Fanning and Holland it is calculated using a corporate-wide weighted average of all the business unit financial performance goals, including primarily the traditional operating companies ROE.

The Compensation Committee may make adjustments, both positive and negative, to goal achievement for purposes of determining payouts. Such adjustments include the impact of items considered one-time or outside of normal operations or not anticipated in the business plan when the earnings goal was established and of sufficient magnitude to warrant recognition. For the payouts based on 2007 performance, no adjustments were made that materially impacted the payouts to the named executive officers.

Under the terms of the program, no payout can be made if the Company s current earnings are not sufficient to fund the Common Stock dividend at the same level or higher than the prior year.

Goal Details

Operational Goals:

Customer Service The Company uses customer satisfaction surveys to evaluate the Company s performance. The survey results provide an overall ranking for each traditional operating company, as well as a ranking for each customer segment: residential, commercial and industrial.

Reliability Transmission and distribution system reliability performance is measured by the frequency and duration of outages. Performance targets for reliability are set internally based on historical performance, expected weather conditions and expected capital expenditures.

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Availability Peak season equivalent forced outage rate is an indicator of fossil/hydro plant availability and efficient generation fleet operations during the months when generation needs are greatest. The rate is calculated by dividing the number of hours of forced outages by total generation hours.

Safety The Company s Target Zero program is focused on continuous improvement in having a safe work environment. The performance is measured by the Occupational Safety and Health Administration recordable incident rate.

Inclusion/Diversity The inclusion program seeks to improve our inclusive workplace. This goal includes measures for work environment (employee satisfaction survey), representation of minorities and females in leadership roles and supplier diversity.

Southern Company capital expenditures gate or threshold goal We strive to manage total capital expenditures for the participating business units at or below $3.8 billion for 2007, excluding nuclear fuel. If the capital expenditure target is exceeded, total operational goal performance is capped at 0.90 for all business units, regardless of the actual operational goal results. Adjustments to the goal may occur due to significant events not anticipated in the business plan established early in 2007, such as acquisitions or disposition of assets, new capital projects and other events.

The range of performance levels established for the operational goals are detailed below.

Level of Performance	Customer Service	Reliability	Availability	Safety	Inclusion
Maximum (1.10)	Top quartile for each customer segment	Improve historical performance	2.00%	1.00	Significant improvement
Target (1.00)	Top quartile overall	Maintain historical performance	2.75%	1.50	Improve
Threshold (0.90)	3rd quartile	Below historical performance	3.75%	2.00	Below expectations
0 Trigger	4th quartile	Significant issues	6.00%	>2.00	Significant issues

EPS and Business Unit Financial Performance:

The range of EPS and ROE goals for 2007 is shown below. ROE goals vary from the allowed retail ROE range due to state regulatory accounting requirements, wholesale activities, other non-jurisdictional revenues and expenses and other activities not subject to state regulation.

Level of	EPS Excluding Synthetic Fuel	Payout	Payout Factor at Highest Level of	Payout Below Threshold for Operational Goal

Performance	Investment Earnings	ROE	Factor	Operational Goal Achievement	Achievement
Maximum	$2.265	14.25%	2.00	2.20	0.00
Target	$2.155	13.50%	1.00	1.10	0.00
Threshold	$2.08	10.50%	0.25	0.275	0.00
Below threshold	<$2.08	<10.50%	0.00	0.00	0.00

2007 Achievement

Each named executive officer had a target annual incentive opportunity set by the Compensation Committee at the beginning of 2007. Targets are set as a percentage of base salary. Mr. Ratcliffe s target was set at 100%. For Messrs. Fanning, Garrett and McCrary, it was set at 75% and for Mr. Holland it was set at 60%. Actual payouts were developed by adding the payouts derived from EPS and business unit financial performance goal achievement for 2007 and multiplying that sum by the result

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of the operational goal achievement. The gate goal target was not exceeded and therefore did not affect payouts. Actual 2007 goal achievement is shown in the following table.

Name	Operational Goal Multiplier (A)	EPS, Excluding Synthetic Fuel Investment Earnings	EPS Goal Performance Factor (50% Weight)	Business Unit Financial Performance	Business Unit Financial Performance Factor (50% Weight)	Total Weighted Financial Performance Factor (B)	Total Payout Factor (A x B)
D. M. Ratcliffe	1.08	$ 2.21	1.69	Corporate average	1.25	1.47	1.59
T. A. Fanning	1.08	$ 2.21	1.69	Corporate average	1.25	1.47	1.59
M. D. Garrett	1.08	$ 2.21	1.69	13.50% ROE	1.00	1.34	1.45
C. D. McCrary	1.09	$ 2.21	1.69	13.73% ROE	1.31	1.50	1.63
G. E. Holland, Jr.	1.08	$ 2.21	1.69	Corporate average	1.25	1.47	1.59

Note that the Total Payout Factor may vary from the Total Weighted Financial Performance Factor multiplied by the Operational Goal Multiplier due to rounding. To calculate an annual incentive payout amount, the target opportunity (annual incentive target times base salary) is multiplied by the Total Payout Factor.

Annual incentive payouts were determined using EPS performance results that differ somewhat from the results reported in Company s financial statements in the Annual Report (the Financial Statements). This difference is described below.

EPS excluding earnings from synthetic fuel investments In 2007, the Company s synthetic fuel investments generated tax credits as a result of synthetic fuel production. Due to higher oil prices over the past two years, such tax credits were partially phased out and one synfuel investment was terminated in 2006. These tax credits were no longer available after December 31, 2007. Company management uses EPS, excluding earnings from synthetic fuel investments, to evaluate the performance of the Company s ongoing business activities. We believe the presentation of earnings and EPS, excluding the results of the synthetic fuel investments, also is useful for investors because it provides additional information for purposes of comparing our performance for such periods. For 2007, reported EPS was $2.29 per share including earnings from synthetic fuel investments, and $2.21 per share excluding them. As established by the Compensation Committee in early 2007, the annual incentive goal for 2007 measured the EPS performance, excluding earnings from synthetic fuel investments.

Actual performance exceeded the target performance levels established by the Compensation Committee in early 2007; therefore, the payout levels also exceeded the target pay opportunities that were established. More information on how the target pay opportunities are established is provided under the section entitled Market Data in this CD&A.

The table below shows the pay opportunity set in early 2007 for the annual incentive payout at target-level performance and the actual payout based on the actual performance shown above. The actual target reported in the Grants of Plan-Based Awards Table may differ due to rounding.

Name	Target Annual Incentive Opportunity	Actual Annual Incentive Payout
D. M. Ratcliffe	$ 1,075,700	$ 1,710,336
T. A. Fanning	$ 463,000	$ 733,923
M. D. Garrett	$ 465,750	$ 675,223
C. D. McCrary	$ 475,500	$ 774,728
G. E. Holland, Jr.	$ 325,200	$ 516,633

Stock Options

Stock options are granted annually and were granted in 2007 to the named executive officers and about 6,300 other employees. Options have a 10-year term, vest over a three-year period, fully vest upon retirement or termination of

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employment following a change in control and expire at the earlier of five years from the date of retirement or the end of the 10-year term.

Stock option award sizes for 2007 were calculated using guidelines set as a percent of base salary, as shown below. These guidelines, for all but Mr. Ratcliffe, are kept stable from year to year unless the market data indicates a clear need to change them. Mr. Ratcliffe s guideline is reset by the Compensation Committee each year in their deliberations regarding his total pay package and is adjusted as necessary to remain competitive with the market data for total target pay opportunities. In 2007, the dollar amount was approximately 3.5% greater than the amount in 2006.

The number of options granted is the guideline amount divided by the average daily Common Stock price for the 12 months preceding the grant. This is done to mitigate volatility in the number of options granted from year to year and to provide a standard grant methodology.

The calculation of the 2007 stock option grants for the named executive officers is shown below.

Name	Guideline%	Salary	Guideline Amount	Average Daily Stock Price	Number of Stock Options Granted (Guideline Amount/Average Daily Stock Price)
D. M. Ratcliffe	1,703% of Salary	$ 1,075,700	$ 18,318,667	$ 34.06	537,835
T. A. Fanning	550% of Salary	$ 616,000	$ 3,388,000	$ 34.06	99,382
M. D. Garrett	550% of Salary	$ 621,000	$ 3,415,500	$ 34.06	100,261
C. D. McCrary	550% of Salary	$ 634,000	$ 3,487,000	$ 34.06	102,333
G. E. Holland, Jr.	475% of Salary	$ 542,000	$ 2,574,500	$ 34.06	75,523

For Mr. Ratcliffe, the long-term incentive compensation pay opportunity is redetermined annually as discussed and shown under the section entitled Market Data in this CD&A. To determine Mr. Ratcliffe s stock option grant, the value attributed to stock options ($2,747,800 in 2007) was divided by the stock option value. The stock option value was 15% of the average daily stock price for the year preceding the grant (approximately $5.11 in 2007).

This calculation resulted in a grant of 537,835 stock options in 2007. More information about the stock option program is contained in the Grants of Plan-Based Awards Table and the information accompanying it.

Performance Dividends

All option holders, including the named executive officers, can receive performance-based dividend equivalents on stock options held at the end of the year. Dividend equivalents can range from 0% to 100% of the Common Stock dividend paid during the year per option held at the end of the year. Actual payout will depend on our total shareholder return over a four-year performance measurement period compared to a group of other electric and gas utility companies. The peer group is determined at the beginning of each four-year performance measurement period. The peer group varies from the Market Data peer group due to the timing and criteria of the peer selection process.

The peer group for performance dividends is set by the Compensation Committee at the beginning of the four-year measurement period. However, despite these timing differences, there is substantial overlap in the companies included.

Total shareholder return is calculated by measuring the ending value of a hypothetical $100 invested in each company s common stock at the beginning of each of 16 quarters.

No performance dividends are paid if the Company s earnings are not sufficient to fund a Common Stock dividend at least equal to that paid in the prior year.

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2007 Payout

The peer group used to determine the 2007 payout for the 2004-2007 performance measurement period was made up of utilities with revenues of $2 billion or more with regulated revenues of 70% or more. Those companies are listed below.

Allegheny Energy, Inc.
Alliant Energy Corporation
Ameren Corporation
American Electric Power Company, Inc.
Avista Corporation
Consolidated Edison, Inc.
DTE Energy Company
Energy East Corporation
Entergy Corporation
Exelon Corporation
FirstEnergy Corporation
FPL Group, Inc.
NiSource Inc.
Northeast Utilities
NorthWestern Corporation
NSTAR
OGE Energy Corp.
Pepco Holdings, Inc.
Pinnacle West Capital Corporation
Progress Energy, Inc.
Public Service Enterprise Group Incorporated
Puget Energy, Inc.
SCANA Corporation
Sempra Energy
Sierra Pacific Resources
Westar Energy, Inc.
Wisconsin Energy Corporation
Xcel Energy Inc.

The scale below determined the percent of the full year s dividend paid on each option held at December 31, 2007 based on performance during the 2004-2007 performance measurement period. Payout for performance between points was interpolated on a straight-line basis.

Performance vs. Peer Group	Payout (% of Full Year s Dividend Paid)
90th percentile or higher	100%
50th percentile (Target)	50%
10th percentile or lower	0%

The above payout scale, when established in 2004, paid 25% of the dividend at the 30th percentile and zero below that. The scale was extended to the 10th percentile on a straight-line basis by the Compensation Committee in October 2005 in order to avoid the earnings volatility and employee relations issues that the payout cliff created.

Total shareholder return was calculated by measuring the ending value of a hypothetical $100 invested in each company s stock at the beginning of each of 16 quarters.

For tax purposes, the Compensation Committee approved a scale of two times the scale shown above (as originally established) and used negative discretion to arrive at a payout commensurate with the scale shown.

The Company s total shareholder return performance during the four-year period ending with 2007 was the 39th percentile, resulting in a payout of 36% of the full year s dividend, or $0.58. This figure was multiplied by each named executive officer s outstanding stock options at December 31, 2007 to calculate the payout under the program. The amount paid is included in the Non-Equity Incentive Plan Compensation column in the Summary Compensation Table.

2010 Opportunity

The peer group for the 2007-2010 performance measurement period (which will be used to determine the 2010 payout amount) is made up of utility companies with revenues of $1.2 billion or more with regulated revenues of approximately 60% or more. Those companies are listed below.

The guideline used to establish the peer group for the 2004-2007 performance measurement period was somewhat different from that used in 2007 to establish the peer group for the 2007-2010 performance measurement period. The guideline for inclusion in the peer group is reevaluated annually as needed to assist in identifying 25 to 30 companies similar to the

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Company. While the guideline does vary somewhat, 25 of the 29 companies in the peer group for the 2004-2007 performance measurement period also were in the peer group established for the 2007-2010 period.

Allegheny Energy, Inc.	Edison International	Progress Energy, Inc.
Alliant Energy Corporation	Energy East Corporation	Puget Energy, Inc.
Ameren Corporation	Entergy Corporation	SCANA Corporation
American Electric Power Company, Inc.	Exelon Corporation	Sempra Energy
Aquila, Inc.	FPL Group, Inc.	Sierra Pacific Resources
Avista Corporation	Hawaiian Electric Industries, Inc.	TECO Energy, Inc.
CenterPoint Energy, Inc.	NiSource Inc.	UIL Holdings Corporation
CMS Energy Corporation	Northeast Utilities	Unisource Energy Corporation
Consolidated Edison, Inc.	NSTAR	Vectren Corporation
DPL Inc.	Pepco Holdings, Inc.	Westar Energy, Inc.
DTE Energy Company	PG&E Corporation	Wisconsin Energy Corporation
Duke Energy Corporation	Pinnacle West Capital Corporation	Xcel Energy Inc.

The scale below will determine the percent of the full year s dividend paid on each option held at December 31, 2010, based on the 2007-2010 performance measurement period. Payout for performance between points will be interpolated on a straight-line basis.

Performance vs. Peer Group	Payout (% of Full Year s Dividend Paid)
90th percentile or higher	100%
50th percentile (Target)	50%
10th percentile or lower	0%

See the Grants of Plan-Based Awards Table and the accompanying information for more information about threshold, target and maximum payout opportunities for the 2007-2010 Performance Dividend Program.

Timing of Incentive Compensation

As discussed above, EPS and business unit financial performance goals for the 2007 annual incentive program were established at the February 2007 Compensation Committee meeting. Annual stock option grants also were made at that meeting. The establishment of incentive compensation goals and the granting of stock options were not timed with the release of non-public material information. This procedure was consistent with prior practices. Stock option grants are made to new hires or newly-eligible participants on preset, regular quarterly dates that were approved by the Compensation Committee. The exercise price of options granted to employees in 2007 was the closing price of the Common Stock on the date of grant.

Post-Employment Compensation

As mentioned above, we provide certain post-employment compensation to employees, including the named executive officers.

Retirement Benefits

Generally, all full-time employees of the Company, including the named executive officers, participate in our funded Pension Plan after completing one year of service. Normal retirement benefits become payable when participants both attain age 65 and complete five years of participation. We also provide unfunded benefits that count salary and short-term incentive pay that is ineligible to be counted under the Pension Plan. (These plans are the Supplemental Benefit Plan and the Supplemental Executive Retirement Plan that are mentioned in the chart on page 22 of this CD&A.) See the Pension Benefits Table and the information accompanying it for more information about pension-related benefits.

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

Mr. Holland also has an agreement that increases his retirement benefits to a level as if he has additional years of service. Mr. Holland was hired by the Company after providing many years of service to the Company while associated with a law firm that represents the Company. The Company entered into this agreement with Mr. Holland as a hiring incentive. More information about this agreement is included in the Pension Benefits Table and the section entitled Potential Payments upon Termination or Change in Control.

Change-in-Control Protections

The Compensation Committee approved the change-in-control protection program in 1998. The program provides some level of severance benefits to all employees not part of a collective bargaining unit, if the conditions of the program are met, as described below. The Compensation Committee established this program and the levels of severance amount in order to provide certain compensatory protections to executives upon a change in control and thereby allow them to negotiate aggressively with a prospective purchaser. Providing such protections to our employees in general minimizes disruption during a pending or anticipated change in control. For all participants, payment and vesting occur only upon the occurrence of both an actual change in control and loss of the individual s position.

Change-in-control protections, including severance pay and, in some situations, vesting or payment of long-term incentive awards, are provided upon a change in control of the Company coupled with an involuntary termination not for Cause or a voluntary termination for Good Reason. This means there is a double trigger before severance benefits are paid; *i.e.,* there must be both a change in control and a termination of employment.

If the conditions described above are met, the named executive officers are entitled to severance payments equal to three times their base salary plus the annual incentive amount assuming target-level performance. Less than 20 officers of the Company are entitled to this level of severance payment. Most officers of the Company are entitled to severance payments equal to two times their base salary plus the annual incentive amount assuming target-level performance. These amounts are consistent with that provided by other companies of our size and in our industry and were established based on market data provided to the Compensation Committee from its compensation consultant.

More information about post-employment compensation, including severance arrangements under our change-in-control program, is included in the section entitled Potential Payments upon Termination or Change in Control.

Executive Stock Ownership Requirements

Effective January 1, 2006, the Compensation Committee adopted Common Stock ownership requirements for officers of the Company and its subsidiaries that are in a position of Vice President or above. All of the named executive officers are covered by the requirements. The guidelines were implemented to further align the interest of officers and stockholders by promoting a long-term focus and long-term share ownership.

The types of ownership arrangements counted toward the requirements are shares owned outright, those held in Company-sponsored plans and Company Common Stock accounts in the Deferred Compensation Plan and the Supplemental Benefit Plan. One-third of vested Company stock options may be counted, but if so, the ownership

target is doubled.

The requirements are expressed as a multiple of base salary as per the table below.

Name	Multiple of Salary without Counting Stock Options	Multiple of Salary Counting 1/3 of Vested Options
D. M. Ratcliffe	5 Times	10 Times
T. A Fanning	3 Times	6 Times
M. D. Garrett	3 Times	6 Times
C. D. McCrary	3 Times	6 Times
G. E. Holland, Jr.	3 Times	6 Times

Current officers have until September 30, 2011 to meet the applicable ownership requirement. Newly-elected officers will have five years to meet the applicable ownership requirement.

Impact of Accounting and Tax Treatments on Compensation

Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code), limits the tax deductibility of each named executive officer s compensation that exceeds $1 million per year unless the compensation is paid under a performance-based plan as defined in the Code and that has been approved by stockholders. The Company has obtained stockholder approval of the Omnibus Incentive Compensation Plan, under which all of our incentive compensation is paid. For tax purposes, in order to ensure that the annual incentive and performance dividend payouts are fully deductible under Section 162(m) of the Code, the Compensation Committee approved in February 2007 a formula that represented a maximum annual incentive amount payable (defined as 0.6% of the Company s net income) and the maximum 2010 performance dividend amount payable for the 2007-2010 performance measurement period (0.6% of the Company s average net income during 2007-2010). In 2007, the Compensation Committee used (for annual incentive), or will use (for performance dividends), negative discretion from those amounts to determine the actual payouts pursuant to the methodologies described above.

Because our policy is to maximize long-term stockholder value, as described fully in this CD&A, tax deductibility is not the only factor considered in setting compensation.

Policy on Recovery of Awards

The Company s 2006 Omnibus Incentive Compensation Plan provides that, if the Company is required to prepare an accounting restatement due to material noncompliance as a result of misconduct, and if an executive knowingly or grossly negligently engaged in or failed to prevent the misconduct or is subject to automatic forfeiture under the Sarbanes-Oxley Act of 2002, the executive will reimburse the Company the amount of any payment in settlement of awards earned or accrued during the 12-month period following the first public issuance or filing that was restated.

Company Policy Regarding Hedging the Economic Risk of Stock Ownership

The Company s policy is that insiders, including outside directors, will not trade in Company options on the options market and will not engage in short sales.

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COMPENSATION AND MANAGEMENT SUCCESSION COMMITTEE REPORT

The Compensation Committee met with management to review and discuss the CD&A. Based on such review and discussion, the Compensation Committee recommended to the Board of Directors that the CD&A be included in the Company s Annual Report on Form 10-K covering the 2007 fiscal year and in this proxy statement. The Board of Directors approved that recommendation.

Members of the Committee:

J. Neal Purcell, Chair
Jon A. Boscia
H. William Habermeyer, Jr.
Donald M. James

SUMMARY COMPENSATION TABLE FOR 2007

The Summary Compensation Table shows the amount and type of compensation received or earned in 2006 and 2007 for the Chief Executive Officer, the Chief Financial Officer and the next three most highly-paid executive officers of the Company who served in 2007. Collectively, these five officers are referred to as the named executive officers.

ame and Principal Position (a)	Year (b)	Salary ($) (c)	Bonus ($) (d)	Stock Awards ($) (e)	Option Awards ($) (f)	Non-Equity Incentive Plan Compensation ($) (g)	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($) (h)	All Other Compensation ($) (i)	Total ($) (j)
avid M. Ratcliffe	2007	1,068,268			2,215,880	2,901,883	4,683,305	88,585	10,957,92
hairman, President	2006	1,028,471			2,152,767	2,563,680	2,036,219	73,127	7,854,26
EO									
homas A. Fanning	2007	610,624			520,341	954,988	814,123	43,658	2,943,73
ecutive Vice	2006	583,011			551,320	939,527	357,950	43,041	2,474,84
esident & COO									
ichael D. Garrett	2007	613,731			413,075	828,844	2,259,654	47,440	4,162,74
esident, Georgia	2006	575,100	29,288		391,843	967,002	880,636	47,183	2,891,05
wer Company									
harles D. McCrary	2007	629,961			421,612	983,174	1,156,038	58,132	3,248,91
	2006	609,407			411,589	900,736	203,672	55,606	2,181,01

esident, Alabama wer Company									
Edison Holland, **.**	2007	538,329			311,155	708,668	854,238	45,736	2,458,12
ecutive Vice esident & General ounsel	2006	522,709			303,755	806,198	256,730	41,564	1,930,95

Column (e)

No equity-based compensation has been awarded to the named executive officers, other than stock options awards which are reported in Column (f).

Column (f)

This column reports the dollar amounts recognized in 2006 and 2007, respectively, for financial statement reporting purposes in accordance with Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123 (revised 2004) (FAS 123R) disregarding any estimates of forfeitures relating to service-based vesting conditions. The assumptions used in calculating these amounts are discussed in Note 1 to the Financial Statements.

For all of the named executive officers except Mr. Fanning, the amounts shown equal the grant date fair value for the 2007 options granted in 2007, as reported in the Grants of Plan-Based Awards Table, because these named executive officers were retirement eligible during all of 2007 and therefore their options will vest in full upon termination. Accordingly, under

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FAS 123R, the full grant date fair value of their option awards is expensed in the year of grant. However, for Mr. Fanning, the amount expensed (and reported in this column) is greater than the amount reported in the Grants of Plan-Based Awards Table because he did not become retirement eligible until 2007. Therefore, the grant date fair value for options granted to Mr. Fanning includes amounts attributable to earlier grants as shown in the following table.

Grant Date	Amount Expensed in 2007
2004	8,342
2005	29,728
2006	72,817
2007	409,454
Total	520,341

Column (g)

The amounts in this column are the aggregate of the payouts under the annual incentive program and the performance dividend program attributable to performance periods ending December 31, 2007 that are discussed in detail in the CD&A. The amounts paid under each program to the named executive officers are shown below:

Name	Annual Incentive ($)	Performance Dividends ($)	Total ($)
D. M. Ratcliffe	1,710,336	1,191,547	2,901,883
T. A. Fanning	733,923	221,065	954,988
M. D. Garrett	675,223	153,621	828,844
C. D. McCrary	774,728	208,446	983,174
G. E. Holland, Jr.	516,633	192,035	708,668

Column (h)

This column reports the aggregate change in the actuarial present value of each named executive officer s accumulated benefit under the Pension Plan and the supplemental pension plans (collectively, Pension Benefits) during 2006 and 2007. The amount included for 2006 is the difference between the actuarial present values of the Pension Benefits measured as of September 30, 2005 and September 30, 2006; the 2007 amount is the difference in the actuarial present values of the Pension Benefits measured as of September 30, 2006 and September 30, 2007. The Pension Benefits as of each measurement date are based on the named executive officer s age, pay and service accruals and the plan provisions applicable as of the measurement date. The actuarial present values as of each measurement date reflect the assumptions the Company selected for Statement of Financial Accounting Standards No. 87, Employers Accounting for Pensions (FAS 87) cost purposes as of that measurement date; however, the named executive officers were assumed to remain employed at the Company until their benefits commence at the Pension Plans stated normal retirement date, generally age 65. As a result, the amounts in column (h) related to Pension Benefits represent the combined impact of several factors growth in the named executive officer s Pension Benefits over the measurement year; impact on the total present values of one year shorter discounting period due to the named executive officer being one year closer to normal retirement; impact on the total present values attributable to changes in assumptions

from measurement date to measurement date; and impact on the total present values attributable to plan changes between measurement dates.

For more information about the Pension Benefits and the assumptions used to calculate the actuarial present value of accumulated benefits as of September 30, 2007, see the information following the Pension Benefits Table. The key differences between assumptions used for the actuarial present values of accumulated benefits calculations as of September 30, 2006 and September 30, 2007 follow:

Discount rate was increased to 6.3% as of September 30, 2007 from 6.0% as of September 30, 2006.

Unpaid incentives have been assumed to be 135% of target levels as of September 30, 2007; payments at 130% of target levels was assumed as of September 30, 2006.

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The pension plans provisions were substantively the same as of September 30, 2005 and September 30, 2006. However, the present values of accumulated Pension Benefits as of September 30, 2007 reflect new provisions regarding the form and timing of payments from the supplemental pension plans. These changes bring those plans into compliance with Section 409A of the Code. The key change was to the form of payment. Instead of providing monthly payments for the lifetime of each named executive officer and his/her spouse, these plans will pay the single sum value of those benefits for an average lifetime in 10 annual installments. Calculations of the present value of accumulated benefits calculations shown prior to September 30, 2007 reflect supplemental pension benefits being paid monthly for the lifetimes of named executive officers and their spouses. The 2007 change in pension value reported in column (h) for each named executive officer is greater than what it otherwise would have been due to the new form of payment. This new form of payment is described more fully in the information following the Pension Benefits Table.

The following table shows how much each of the above-described factors contributed to the change in each named executive officer s pension value during 2007. As described above, the change in the way supplemental pension benefits will be paid had the biggest impact; that change was made in 2007 to comply with Code Section 409A. It is a one-time adjustment in the value of accumulated pension benefits to reflect the installment form of payment instead of monthly payments over the lifetime of participants and their spouses. As shown below, the changes in FAS 87 assumptions reduced pension values.

Name	Shorter Discount Period ($)	Additional Pay/Service ($)	Change in FAS 87 Assumptions ($)	One-Time Code Section 409A-Related Changes ($)	Total of All Factors ($)
D. M. Ratcliffe	578,827	1,768,585	–490,491	2,789,380	4,646,301
T. A. Fanning	123,533	327,880	–159,249	517,406	809,570
M. D. Garrett	280,789	972,390	–257,341	1,254,990	2,250,828
C. D. McCrary	223,761	257,316	–207,212	876,634	1,150,499
G. E. Holland, Jr.	133,504	260,252	–136,496	579,031	836,291

This column also reports above-market earnings on deferred compensation. Above-market earnings are defined by the SEC as any amount above 120% of the applicable federal long-term rate as prescribed under Section 1274(d) of the Code.

Under the Deferred Compensation Plan, eligible employees are permitted to defer up to 50% of their salary and 100% of payments under the annual incentive or performance dividend programs. The deferred amounts are then treated as if invested in one of two investment options at the election of the participant. Amounts may be treated as if invested in the Company s Common Stock (Stock Equivalent Account) or the prime interest rate as published in the *Wall Street Journal* as the base rate on corporate loans posted as of the last business day of each month by at least 75% of the United States largest banks (Prime Equivalent Account).

The amounts invested in the Stock Equivalent Account are treated as if dividends are paid and reinvested at the same rate as that paid to the Company s stockholders. That amount is not considered above-market as defined by the SEC.

In 2006 and 2007, the prime interest rate used in the Prime Equivalent Account exceeded 120% of the applicable long-term rate in effect at the measurement point under the SEC s rules. Therefore, earnings that exceed the amount calculated at that rate are reported here. The range of interest rates under the Prime Equivalent Account was 7.25% to 8.25% in 2006 and 2007 and the applicable long-term rate was 7.14%.

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The table below itemizes the amounts reported in this column.

Name	Year	Change in Pension Value ($)	Above-Market Earnings on Deferred Compensation ($)	Total ($)
D. M. Ratcliffe	2007	4,646,301	37,004	4,683,305
	2006	2,002,835	33,384	2,036,219
T. A. Fanning	2007	809,570	4,553	814,123
	2006	353,902	4,048	357,950
M. D. Garrett	2007	2,250,828	8,826	2,259,654
	2006	872,674	7,962	880,636
C. D. McCrary	2007	1,150,499	5,539	1,156,038
	2006	198,676	4,996	203,672
G. E. Holland, Jr.	2007	836,291	17,947	854,238
	2006	240,600	16,130	256,730

Column (i)

This column reports the following items: perquisites; tax reimbursements by the Company on certain perquisites; Company contributions in 2007 to the Southern Company Employee Savings Plan (ESP), which is a tax-qualified defined contribution plan intended to meet requirements of Section 401(k) of the Code, and contributions in 2007 under the Southern Company Supplemental Benefit Plan (Non-Pension Related) (SBP). The SBP is described more fully in the information following the Nonqualified Deferred Compensation Table.

The amounts reported for 2007 are itemized below.

Name	Perquisites ($)	Tax Reimbursements ($)	ESP ($)	SBP ($)	Total ($)
D. M. Ratcliffe	19,118	14,986	10,834	43,647	88,585
T. A. Fanning	7,434	5,510	11,047	19,667	43,658
M. D. Garrett	8,842	7,298	11,475	19,825	47,440
C. D. McCrary	14,535	13,020	9,924	20,653	58,132
G. E. Holland, Jr.	9,546	9,243	10,967	15,980	45,736

Description of Perquisites

Personal Financial Planning is provided for most officers of the Company, including all of the named executive officers. The Company pays for the services of the financial planner on behalf of the officers, up to a maximum amount of $8,700 per year, after the initial year that the benefit is first provided. The Company also provides a five-year allowance of $6,000 for estate planning and tax return preparation fees. The full cost paid by the Company in 2007 is reported here.

Home Security Monitoring is provided by the Company s security personnel. The amount of the benefit reported here represents the incremental cost of the Company-provided monitoring. The incremental cost is the full cost of providing security monitoring at Company-owned facilities and covered employees residences divided by the number of security systems monitored.

Personal Use of Company-Provided Club Memberships. The Company provides club memberships to certain officers, including all of the named executive officers. The memberships are provided for business use; however, personal use is permitted. The amount included reflects the pro-rata portion of the membership fees paid by the Company that are attributable to the named executive officers personal use. Direct costs associated with any personal use, such as meals, are paid for or reimbursed by the employee and therefore are not included.

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Personal Use of Corporate-Owned Aircraft. The Company owns aircraft that are used to facilitate business travel. All flights on these aircraft must have a business purpose, except under very limited circumstances. There was no such personal use during 2007. If seating is available, the Company permits a spouse or other family member to accompany an employee on a flight. However, because in such cases the aircraft is being used for a business purpose, there is no incremental cost associated with the spousal travel and no amounts are included for such travel. Any additional expenses incurred that are related to spousal travel, are included.

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

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GRANTS OF PLAN-BASED AWARDS IN 2007

The Grants of Plan-Based Awards Table provides information on stock option grants made and goals established for future payouts under the Company s incentive compensation programs during 2007 by the Compensation Committee. In this table, the annual incentive and the performance dividend amounts are referred to as PPP and PDP , respectively.

Name (a)	Grant Date (b)		Threshold $ (c)	Target ($) (d)	Maximum ($) (e)	All Other Option Awards: Number of Securities Underlying Options (#) (f)	Exercise or Base Price of Option Awards ($/Sh) (g)	Grant Date Fair Value of Stock and Option Awards ($) (h)
D. M. Ratcliffe	2/19/2007	PPP	242,029	1,075,683	2,366,503	537,835	36.42	2,215,880
	2/19/2007	PDP	163,838	1,638,377	3,276,754			
T. A. Fanning	2/19/2007	PPP	103,857	461,587	1,015,491	99,382	36.42	409,454
	2/19/2007	PDP	30,396	303,964	607,928			
M. D. Garrett	2/19/2007	PPP	104,776	465,671	1,024,476	100,261	36.42	413,075
	2/19/2007	PDP	21,123	211,228	422,456			
C. D. McCrary	2/19/2007	PPP	106,941	475,293	1,045,645	102,333	36.42	421,612
	2/19/2007	PDP	28,661	286,613	573,225			
G. E. Holland, Jr.	2/19/2007	PPP	73,109	324,927	714,839	75,523	36.42	311,155
	2/19/2007	PDP	26,405	264,047	528,095			

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

The amounts reported as PPP reflect the amounts established by the Compensation Committee in early 2007 to be paid for certain levels of performance as of December 31, 2007 under the annual incentive program, the Company s short-term incentive program. The Compensation Committee assigns each named executive officer a target incentive

opportunity, expressed as a percentage of base salary, that is paid for target-level performance under the annual incentive program. The target incentive opportunities established for the named executive officers for 2007 performance was 100% for Mr. Ratcliffe, 75% for Messrs. Fanning, Garrett and McCrary and 60% for Mr. Holland. The payout for threshold performance was set at 0.225 times the target incentive opportunity and the maximum amount payable was set at 2.20 times the target. The amount paid to each named executive officer under the annual incentive program for actual 2007 performance is included in the Non-Equity Incentive Plan Compensation column in the Summary Compensation Table and is itemized in the notes following that table. More information about the annual incentive program, including the applicable performance criteria established by the Compensation Committee, is provided in the CD&A.

The Company also has a long-term incentive program, the performance dividend program, that pays performance-based dividend equivalents based on the Company s total shareholder return compared with the total shareholder return of its peer companies over a four-year performance measurement period. The Compensation Committee establishes the level of payout for prescribed levels of performance over the measurement period.

In February 2007, the Compensation Committee established the performance dividend program goal for the four-year performance measurement period beginning on January 1, 2007 and ending on December 31, 2010. The amount earned in 2010 based on performance over that four-year performance measurement period will be paid following the end of the period. However, no amount is earned and paid unless the Compensation Committee approves the payment at the beginning of the final year of the performance measurement period. Also, nothing is earned unless the Company s earnings are sufficient to fund a Common Stock dividend at the same level or higher than the prior year.

The performance dividend program pays to all option holders a percentage of the Common Stock dividend paid to stockholders in the last year of the performance measurement period. It can range from less than five percent for performance above the 10th percentile compared with the performance of the peer companies to 100% of the dividend if the Company s total shareholder return is at or above the 90th percentile. That amount is then paid per option held at the end of the four-year period. The amount, if any, ultimately paid to the option holders, including the named executive officers, at the end of the last year of the 2007 2010 performance measurement period will be based on (1) the Company s total shareholder return

compared to that of its peer companies as of December 31, 2010, (2) the actual dividend paid in 2010 to our stockholders, if any, and (3) the number of options held by the named executive officers on December 31, 2010.

The number of options held on December 31, 2010 will be affected by the number of additional options granted to the named executive officers prior to December 31, 2010, if any, and the number of options exercised by the named executive officers prior to December 31, 2010, if any. None of these components necessary to calculate the range of payout under the performance dividend program for the 2007 2010 performance measurement period is known at the time the goal is established.

The amounts reported as PDP in columns (c), (d) and (e) were calculated based on the number of options held by the named executive officers on December 31, 2007, as reported in columns (b) and (c) of the Outstanding Equity Awards at Fiscal Year-End Table and the Common Stock dividend of $1.595 per share paid to stockholders in 2007. These factors are itemized below.

Name	Stock Options Held as of December 31, 2007 (#)	Performance Dividend Per Option Paid at Threshold Performance ($)	Performance Dividend Per Option Paid at Target Performance ($)	Performance Dividend Per Option Paid at Maximum Performance ($)
D. M. Ratcliffe	2,054,391	0.07975	0.7975	1.595
T. A. Fanning	381,146	0.07975	0.7975	1.595
M. D. Garrett	264,863	0.07975	0.7975	1.595
C. D. McCrary	359,389	0.07975	0.7975	1.595
G. E. Holland, Jr.	331,094	0.07975	0.7975	1.595

More information about the performance dividend program is provided in the CD&A.

Columns (f) and (g)

The stock options vest at the rate of one-third per year, on the anniversary date of the grant. Also, grants fully vest upon termination as a result of death, total disability or retirement and expire five years after retirement, three years after death or total disability, or their normal expiration date if earlier. Please see Potential Payments upon Termination or Change in Control below for more information about the treatment of stock options under different termination and change-in-control events.

The Compensation Committee granted these stock options to the named executive officers at its regularly scheduled meeting on February 19, 2007. The grant date was a holiday (Presidents Day) and the New York Stock Exchange was closed. Therefore, under the terms of the Omnibus Incentive Compensation Plan, the exercise price was the closing price ($36.42 per share) on the last trading day prior to the grant date which was February 16, 2007.

Column (h)

The value of stock options granted in 2007 was derived using the Black-Scholes stock option pricing model. The assumptions used in calculating these amounts are discussed in Note 1 to the Financial Statements.

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OUTSTANDING EQUITY AWARDS AT 2007 FISCAL YEAR-END

This table provides information pertaining to all outstanding stock options held by the named executive officers as of December 31, 2007.

	Option Awards					Stock Awards			
ame (a)	Number of Securities Underlying Unexercised Options Exercisable (#) (b)	Number of Securities Underlying Unexercised Options Unexercisable (#) (c)	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#) (d)	Option Exercise Price ($) (e)	Option Expiration Date (f)	Number of Shares or Units of Stock That Have Not Vested (#) (g)	Market Value of Shares or Units of Stock That Have Not Vested ($) (h)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#) (i)	Equity Incentive Plan Awards: Market or Payout Valu of Unearned Shares, Units or Other Rights That Have Not Vested ($) (j)
. M. atcliffe	92,521	0		25.26	02/15/2012				
	82,265	0		29.50	02/13/2014				
	273,031	0		29.315	08/02/2014				
	366,667	183,333		32.70	02/18/2015				
	172,913	345,826		33.81	02/20/2016				
	0	537,835		36.42	02/19/2017				
. A. anning	42,314	0		27.975	02/14/2013				
	63,215	0		29.50	02/13/2014				
	53,895	26,948		32.70	02/18/2015				
	31,798	63,594		33.81	02/20/2016				
	0	99,382		36.42	02/19/2017				
I. D. arrett	17,806	0		29.50	02/13/2014				
	26,188	26,188		32.70	02/18/2015				
	31,474	62,946		33.81	02/20/2016				
	0	100,261		36.42	02/19/2017				
	71,424	0		29.50	02/13/2014				

. D. cCrary				
	57,636	28,818	32.70	02/18/2015
	33,060	66,118	33.81	02/20/2016
	0	102,333	36.42	02/19/2017
. E. olland, r.	48,992	0	27.975	02/14/2013
	58,072	0	29.50	02/13/2014
	50,209	25,104	32.70	02/18/2015
	24,398	48,796	33.81	02/20/2016
	0	75,523	36.42	02/19/2017

Stock options vest one-third per year on the anniversary of the grant date. Options granted from 2002 through 2004, with an expiration date from 2012 through 2014 were fully vested as of December 31, 2007. The options granted in 2005, 2006 and 2007 become fully vested as shown below.

Expiration Date	**Date Fully Vested**
February 18, 2015	February 18, 2008
February 20, 2016	February 20, 2009
February 19, 2017	February 19, 2010

Only Mr. Ratcliffe received a stock option grant in August 2004. This grant was made by the Compensation Committee and was effective after he was named Chief Executive Officer and represented a significant portion of the increase in his compensation in 2004 upon assuming that position.

Options also fully vest upon death, total disability or retirement and expire three years following death or total disability or five years following retirement, or on the original expiration date if earlier. Please see the section entitled Potential Payments

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upon Termination or Change in Control for more information about the treatment of stock options under different termination and change-in-control events.

OPTION EXERCISES AND STOCK VESTED IN FISCAL 2007

This table reports the number of shares acquired upon the exercise of stock options during 2007 and the value realized based on the difference in the exercise price over the market price on the exercise date. None of the named executive officers received Stock Awards.

	Option Awards		**Stock Awards**	
Name (a)	**Number of Shares Acquired on Exercise (#) (b)**	**Value Realized on Exercise ($) (c)**	**Number of Shares Acquired on Vesting (#) (d)**	**Value Realized on Vesting ($) (e)**
D. M. Ratcliffe	83,780	881,785	0	0
T. A. Fanning	31,926	352,785	0	0
M. D. Garrett	98,116	782,764	0	0
C. D. McCrary	151,625	1,736,758	0	0
G. E. Holland, Jr.	54,624	698,679	0	0

PENSION BENEFITS AND VALUES AT 2007 FISCAL YEAR-END

Name (a)	**Plan Name (b)**	**Number of Years Credited Service (#) (c)**	**Present Value of Accumulated Benefit ($) (d)**	**Payments During Last Fiscal Year ($) (e)**
D. M. Ratcliffe	Pension Plan	35.75	864,119	
	Supplemental Benefit Plan (Pension-Related)	35.75	10,247,552	
	Supplemental Executive Retirement Plan	35.75	3,181,744	
	Supplemental Pension Agreement	0.00	0	
T. A. Fanning	Pension Plan	25.92	377,260	
	Supplemental Benefit Plan (Pension-Related)	25.92	1,875,824	
	Supplemental Executive Retirement Plan	25.92	615,370	
	Supplemental Pension Agreement	0.00	0	
M. D. Garrett	Pension Plan	38.67	888,676	
	Supplemental Benefit Plan (Pension-Related)	38.67	4,545,023	

	Supplemental Executive Retirement Plan	38.67	1,496,956
	Supplemental Pension Agreement	0.00	0
C. D. McCrary	Pension Plan	32.92	659,324
	Supplemental Benefit Plan (Pension-Related)	32.92	3,194,145
	Supplemental Executive Retirement Plan	32.92	1,026,375
	Supplemental Pension Agreement	0.00	0
G. E. Holland, Jr.	Pension Plan	14.67	273,463
	Supplemental Benefit Plan (Pension-Related)	14.67	1,020,878
	Supplemental Executive Retirement Plan	14.67	332,839
	Supplemental Pension Agreement	12.25	1,434,192

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The named executive officers earn employer-paid pension benefits from three coordinated retirement plans. The Company also has an individual agreement with Mr. Holland that provides additional pension benefits. More information about pension benefits is described in the CD&A.

The Pension Plan

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

The 1.7% offset formula amount equals 1.7% of final average pay times years of participation less an offset related to Social Security benefits. The offset equals a service ratio times 50% of the anticipated Social Security benefits in excess of $4,200. The service ratio adjusts the offset for the portion of a full career that a participant has worked. The highest three rates of pay out of a participant s last 10 calendar years of service are averaged to derive final average pay. The pay considered for this formula is the base rate of pay reduced for any voluntary deferrals. A statutory limit restricts the amount considered each year; the limit for 2007 was $225,000.

The 1.25% formula amount equals 1.25% of final average pay times years of participation. For this formula, the final average pay computation is the same as above, but annual cash incentives paid during each year are added to the base rates of pay.

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

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

Participants vest in the Pension Plan after completing five years of service. All the named executive officers are vested in their Pension Plan benefits. Participants who terminate employment after vesting can elect to have their pension benefits commencing at age 50 if they participated in the Pension Plan for 10 years. If such an election is made, the early retirement reductions that apply are actuarially determined factors and are larger than 0.3% per month.

If a participant dies while actively employed, benefits will be paid to a surviving spouse. A survivor s benefit equals 45% of the monthly benefit that the participant had earned before his or her death. Payments to a surviving spouse of a participant who could have retired will begin immediately. Payments to a survivor of a participant who was not retirement eligible will begin when the deceased participant would have attained age 50. After commencing, survivor benefits are payable monthly for the remainder of a survivor s life. Participants who are eligible for early retirement may opt to have an 80% survivor benefit paid if they die; however, there is a charge associated with this election.

If participants become totally disabled, periods that Social Security or employer-provided disability income benefits are paid will count as service for benefit calculation purposes. The crediting of this additional service ceases at the

point a disabled participant elects to commence retirement payments. Outside of the extra service crediting, the normal plan provisions apply to disabled participants.

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

The SBP-P is an unfunded retirement plan that is not tax-qualified. This plan provides high-paid employees any benefits that the Pension Plan cannot pay due to statutory pay/benefit limits and voluntary pay deferrals. The SBP-P s vesting, early retirement and disability provisions mirror those of the Pension Plan.

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The amounts paid by the SBP-P are based on the additional monthly benefit that the Pension Plan would pay if the statutory limits and pay deferrals were ignored. When an SBP-P participant separates from service, vested monthly benefits provided by the benefit formulas are converted into a single sum value. It equals the present value of what would have been paid monthly for an actuarially determined average post-retirement lifetime. The discount rate used in the calculation is based on the 30-year Treasury yields for the September preceding the calendar year of separation, but not more than six percent. Vested participants terminating prior to becoming eligible to retire will be paid their single sum value as of September 1 following the calendar of separation. If the terminating participant is retirement eligible, the single sum value will be paid in 10 annual installments starting shortly after separation. The unpaid balance of a retiree s single sum will be credited with interest at the prime rate published in The Wall Street Journal. If the separating participant is a key man under Section 409A of the Code, the first installment will be delayed for six months after the date of separation.

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

The Southern Company Supplemental Executive Retirement Plan (SERP)
The SERP is also an unfunded retirement plan that is not tax-qualified. This plan provides to high-paid employees additional benefits that the Pension Plan and the SBP-P would pay if the 1.7% offset formula calculations reflected a portion of annual cash incentives. To derive the SERP benefits, a final average pay is determined reflecting participants base rates of pay and their incentives to the extent they exceed 15% of those base rates (ignoring statutory limits and pay deferrals). This final average pay is used in the 1.7% offset formula to derive a gross benefit. The Pension Plan and the SBP-P benefits are subtracted from the gross benefit to calculate the SERP benefit. The SERP s early retirement, survivor benefit and disability provisions mirror the SBP-P s provisions. However, except upon a change in control, SERP benefits do not vest until participants retire, so no benefits are paid if a participant terminates prior to becoming eligible to retire.

Supplemental Pension Agreements (SPA)
An SPA is an individual agreement providing for additional pension benefits. These agreements provide certain executives the benefits that Southern s other three pension plans would pay if the participant had worked additional years. These agreements are usually entered into on an as-needed basis to attract and retain executives. The number of additional years of service is most often based on periods of relevant employment with another company. For example, service may be awarded for employment with an accounting or law firm. The Company is in the process of amending each SPA so that benefits will be paid in the same form and at the same time as SBP-P benefits. All information has been shown as if this amendment process had been completed. Mr. Holland is the only named executive officer with an SPA. It provides him with an additional 12.25 years of service in recognition of some of his years of service to the Company while associated with one of the Company s principal law firms.

The following assumptions were used in the present value calculations:

Discount rate 6.3% as of September 30, 2007
Retirement date Normal retirement age (65 for all named executive officers)
Mortality after normal retirement RP2000 Combined Healthy mortality rate table
Mortality, withdrawal, disability and retirement rates prior to normal retirement None
Form of payment for Pension Benefits:
- Unmarried retirees: 100% elect a single life annuity
- Married retirees: 20% elect a single life annuity; 40% elect a joint and 50% survivor annuity; and 40% elect a joint and 100% survivor annuity
- Percent married at retirement 80% of males and 70% of females

Spouse ages Wives two years younger than their husbands
Incentives earned but unpaid as of the measurement date 130% of target percentages times base rate of pay for year incentive is earned
Installment determination 5.3% discount rate for single sum calculation and 7.3% prime interest rate on unpaid balances during installment payment period.

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For all of the named executive officers, the number of years of credited service is one year less than the number of years of employment.

NONQUALIFIED DEFERRED COMPENSATION AS OF 2007 FISCAL YEAR-END

Name (a)	Executive Contributions in Last FY ($) (b)	Registrant Contributions in Last FY ($) (c)	Aggregate Earnings in Last FY ($) (d)	Aggregate Withdrawals/ Distributions ($) (e)	Aggregate Balance at Last FYE ($) (f)
D. M. Ratcliffe	0	43,647	774,971	0	9,232,125
T. A. Fanning	140,929	19,667	82,603	0	956,753
M. D. Garrett	0	19,825	97,708	0	1,231,703
C. D. McCrary	0	20,653	88,949	0	1,082,275
G. E. Holland, Jr.	0	15,980	184,642	0	2,344,766

The Company provides the Deferred Compensation Plan (DCP) which is designed to permit participants to defer income as well as certain federal, state and local taxes until a specified date or their retirement, disability, death or other separation from service. Up to 50% of base salary and up to 100% of the annual incentive and the performance dividends may be deferred, at the election of eligible employees. All the named executive officers are eligible to participate in the DCP.

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

The amounts deferred in the Stock Equivalent Account are treated as if invested at an equivalent rate of return to that of an actual investment in Common Stock, including the crediting of dividend equivalents as such are paid by the Company from time to time. It provides participants with an equivalent opportunity for the capital appreciation (or loss) and income held by a Company stockholder. During 2007, the rate of return in the Stock Equivalent Account was 9.83%, which was the Company s total shareholder return for 2007.

Alternatively, participants may elect to have their deferred compensation deemed invested in the Prime Equivalent Account which is treated as if invested at a prime interest rate compounded monthly, as published in the *Wall Street Journal* as the base rate on corporate loans posted as of the last business day of each month by at least 75% of the United States largest banks. The range of interest rates earned on amounts deferred during 2007 in the Prime Equivalent Account was 7.25% to 8.25%.

Column (b)

This column reports the actual amounts of compensation deferred under the DCP by each named executive officer in 2007. The amount of salary deferred by the named executive officers, if any, was included in the Salary column in the Summary Compensation Table. The amount of incentive compensation deferred in 2007 was the amount paid for performance under the PPP and the PDP that were earned as of December 31, 2006 but not payable until the first

quarter of 2007. This amount is not reflected in the Summary Compensation Table because that table reports incentive compensation that was earned in 2007, but not payable until early 2008. These deferred amounts may be distributed in a lump-sum or in up to 10 annual installments at termination of employment or in a lump-sum at a specified date, at the election of the participant.

Column (c)

This column reflects contributions under the Supplemental Benefit Plan (SBP). Under the Code, the Company is prohibited from making employer matching contributions under the Employee Savings Plan on employee contributions above stated limits in that plan and, if applicable, above legal limits set forth in the Code. The SBP is a nonqualified deferred compensation plan under which the Company contributes the amount of Company contributions that it is prohibited from making in the Employee Savings Plan. The contributions are treated as if invested in Common Stock and are payable in cash

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upon termination of employment in a lump-sum or in up to 20 annual installments, at the election of the participant. The amounts reported in this column also were reported in the All Other Compensation column in the Summary Compensation Table.

Column (d)

This column reports earnings on both compensation the named executive officers elected to defer and earnings on employer contributions under the SBP. See the notes to column (h) of the Summary Compensation Table for a discussion of amounts of nonqualified deferred compensation earnings included in the Summary Compensation Table.

Column (e)

There were no aggregate withdrawals or distributions.

Column (f)

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

Name	Amounts Deferred under the DCP Prior to 2007 and Reported in Prior Years Proxy Statements ($)	Employer Contributions under the SBP Prior to 2007 and Reported in Prior Years Proxy Statements ($)	Total ($)
D. M. Ratcliffe	5,381,881	203,141	5,585,022
T. A. Fanning	631,969	62,496	694,465
M. D. Garrett	0	50,171	50,171
C. D. McCrary	489,924	130,461	620,385
G. E. Holland, Jr.	298,508	46,536	345,044

POTENTIAL PAYMENTS UPON TERMINATION OR CHANGE IN CONTROL

This section describes and estimates payments that could be made to the named executive officers under different termination and change-in-control events. The estimated payments would be made under the terms of the Company s compensation and benefits programs or the change-in-control severance agreements with each of the named executive officers. The amount of potential payments is calculated as if the triggering events occurred as of December 31, 2007 and assumes that the price of Common Stock is the closing market price as of December 31, 2007.

Description of Termination and Change-in-Control Events

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

Traditional Termination Events

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

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

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

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

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

Change-in-Control-Related Events

At the Company or subsidiary level:

Southern Change in Control I Acquisition by another entity of 20% or more of Common Stock, or following a merger with another entity the Company s stockholders own 65% or less of the entity surviving the merger.

Southern Change in Control II Acquisition by another entity of 35% or more of Common Stock, or following a merger with another entity the Company s stockholders own less than 50% of the entity surviving the merger.

Southern Termination A merger or other event and the Company is not the surviving company or Common Stock is no longer publicly traded.

Subsidiary Change in Control Acquisition by another entity, other than another subsidiary of the Company, of 50% or more of the stock of a subsidiary of the Company, a merger with another entity and the subsidiary is not the surviving company or the sale of substantially all the assets of the subsidiary.

At the employee level:

Involuntary Change-in-Control Termination or Voluntary Change-in-Control Termination for Good Reason Employment is terminated within two years of a change in control, other than for cause, or the employee voluntarily terminates for Good Reason. Good Reason for voluntary termination within two years of a change in control is generally satisfied when there is a material reduction in salary, incentive compensation opportunity or benefits, relocation of over 50 miles or a diminution in duties and responsibilities.

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The following chart describes the treatment of different pay and benefit elements in connection with the Traditional Termination Events described above. All of the named executive officers are eligible to retire under the terms of our pension plans and therefore any termination of employment also would be a retirement.

Program	Retirement/Retirement Eligible	Lay Off (Involuntary Termination Not For Cause)	Resignation	Death or Disability	Involuntary Termination (For Cause)
Pension Benefit Plans	Benefits payable as described in the notes following the Pension Benefits Table.	Benefits payable as described in the notes following the Pension Benefits Table.	Same as Lay Off.	Benefits payable as described in the notes following the Pension Benefits Table.	Same as for retirement and resignation, as the case may be.
Annual Incentive Program	Pro-rated if terminate before 12/31.	Pro-rated if terminate before 12/31.	Forfeit.	Pro-rated if terminate before 12/31.	Forfeit.
Performance Dividend Program	Paid year of retirement plus two additional years.	Forfeit.	Forfeit.	Payable until options expire or exercised.	Forfeit.
Stock Options	Vest; expire earlier of original expiration date or five years.	Vested options expire in 90 days; unvested are forfeited.	Vested options expire in 90 days; unvested are forfeited.	Vest; expire earlier of original expiration or three years.	Forfeit.
Financial Planning Perquisite	Continues for one year.	Terminates.	Terminates.	Continues for one year.	Terminates.
Supplemental Benefit Plan non-pension related	Payable per prior elections (lump sum or up to 20 annual installments).	Same as Retirement.	Same as Retirement.	Same as the Deferred Compensation Plan.	Same as Retirement.
Deferred Compensation Plan	Payable per prior elections (lump sum or up to 10 annual installments).	Same as Retirement.	Same as Retirement.	Payable to beneficiary or disabled participant per prior elections; amounts deferred prior to 2005 can be paid as a lump sum per plan administration committee s discretion.	Same as Retirement.

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The chart below describes the treatment of payments under pay and benefit programs under different change-in-control events, except the Pension Plan (Change-in-Control Chart). The Pension Plan is not affected by change-in-control events.

Program	Southern Change in Control I	Southern Change in Control II	Southern Termination or Subsidiary Change in Control	Involuntary Change-in-Control-Related Termination or Voluntary Change-in-Control-Related Termination for Good Reason
Nonqualified Pension Benefits	All SERP-related benefits vest if participants vested in Pension Plan; otherwise, no impact. Benefits vest for all participants and single sum value of benefits earned to change-in-control date paid following termination or retirement.		Same as Southern Change in Control II.	Based on type of change-in-control event.
Annual Incentive Program	No plan termination is paid at greater of target or actual performance. If plan terminated within two years of change in control, pro-rated at target performance level.	Same as Southern Change in Control I.	Pro-rated at target performance level.	If not otherwise eligible for payment, if the annual incentive program still in effect, pro-rated at target performance level.
Performance Dividend Program	No plan termination is paid at greater of target or actual performance. If plan terminated within two years of change in control, pro-rated at greater of target or actual performance level.	Same as Southern Change in Control I.	Pro-rated at greater of actual or target performance level.	If not otherwise eligible for payment, if the performance dividend program is still in effect, greater of actual or target performance level for year of severance only.
Stock Options	Not affected by change-in-control events because	Not affected by change-in-control events because	Vest and convert to surviving company s securities; Southern	Vest.

	Common Stock is still publicly traded.	Common Stock is still publicly traded.	Termination; if cannot convert, pay spread in cash; if participant is an employee of a subsidiary, stock options vest upon a Subsidiary Change in Control.	
Deferred Compensation Plan	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.
SBP	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.	Not affected by change-in-control events.

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Program	Southern Change in Control I	Southern Change in Control II	Southern Termination or Subsidiary Change in Control	Involuntary Change-in-Control-Related Termination or Voluntary Change-in-Control-Related Termination for Good Reason
Severance Benefits	Not applicable.	Not applicable.	Not applicable.	Three times base salary plus target annual incentive program amount plus tax gross up if severance amounts exceed Code Section 280G excess parachute payment by 10% or more.
Health Benefits	Not applicable.	Not applicable.	Not applicable.	Up to five years participation in group health plan plus payment of three years premium amounts.
Outplacement Services	Not applicable.	Not applicable.	Not applicable.	Six months.

Potential Payments

This section describes and estimates payments that would become payable to the named executive officers upon a termination or change in control as of December 31, 2007.

Pension Benefits
The amounts that would have become payable to the named executive officers if the Traditional Termination Events occurred as of December 31, 2007 under the Pension Plan, the SBP-P, and the SERP are itemized in the chart below. The amounts shown under the column Retirement are amounts that would have become payable to the named executive officers that were retirement eligible on December 31, 2007 and are the monthly Pension Plan benefits and the first of 10 annual installments from the SBP-P and the SERP. The amounts shown under the column Resignation or Involuntary Termination are the amounts that would have become payable to the named executive officers who were not retirement eligible on December 31, 2007 and are the monthly Pension Plan benefits that would become payable as of the earliest possible date under the Pension Plan and the single sum value of benefits earned up to the termination date under the SBP-P, paid as a single payment rather than in 10 annual installments. Benefits under the SERP would be forfeited. The amounts shown that are payable to a spouse in the event of the death of the named executive officer are the monthly amounts payable to a spouse under the Pension Plan and the first of 10 annual installments from the SBP-P and the SERP. The amounts in this chart are very different from the pension values shown in the Summary Compensation Table and the Pension Benefits Table. Those tables show the present values of all the benefit amounts anticipated to be paid over the lifetimes of the named executive officers and their spouses. Those plans are described in the notes following the Pension Benefits Table.

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Name		Retirement ($)	Resignation or Involuntary Retirement (monthly payments) ($)	Death (payments to a spouse) ($)
D. M. Ratcliffe	Pension Plan	8,200	All plans treated as	4,671
	Supplemental Benefit Plan	1,341,367	retiring	1,341,367
	Supplemental Executive Retirement Plan	416,413		416,413
T. A. Fanning	Pension Plan	3,694	All plans treated as	3,413
	Supplemental Benefit Plan	289,876	retiring	289,876
	Supplemental Executive Retirement Plan	95,062		95,062
M. D. Garrett	Pension Plan	8,545	All plans treated as	5,080
	Supplemental Benefit Plan	613,775	retiring	613,775
	Supplemental Executive Retirement Plan	202,091		202,091
C. D. McCrary	Pension Plan	6,494	All plans treated as	4,304
	Supplemental Benefit Plan	458,841	retiring	458,841
	Supplemental Executive Retirement Plan	147,384		147,384
G. E. Holland, Jr.	Pension Plan	2,719	All plans treated as	1,912
	Supplemental Benefit Plan	150,872	retiring	150,872
	Supplemental Executive Retirement Plan	49,116		49,116
	Supplemental Pension Agreement	210,691		210,691

As described in the Change-in-Control Chart, the only change in the form of payment, acceleration or enhancement of the pension benefits is that the single sum value of benefits earned up to the change-in-control date under the SBP-P and the SERP could be paid as a single payment rather than in 10 annual installments. Also, the SERP benefits vest for participants who are not retirement eligible upon a change in control. Estimates of the single sum payment that would have been made to the named executive officers, assuming termination as of December 31, 2007 following a change-in-control event, other than a Southern Change in Control I (which does not impact how pension benefits are paid), are itemized below. These amounts would be paid instead of the benefits shown in the Traditional Termination Events table above; they are not paid in addition to those amounts.

Name	Supplemental Benefit Plan (Pension-Related) ($)	Supplemental Executive Retirement Plan ($)	Supplemental Pension Agreement ($)	Total ($)
D. M. Ratcliffe	13,413,665	4,164,129	0	17,577,794
T. A. Fanning	2,898,761	950,621	0	3,849,382
M. D. Garrett	6,137,748	2,020,914	0	8,158,662

C. D. McCrary	4,588,413	1,473,839	0	6,062,252
G. E. Holland, Jr.	1,508,718	419,158	2,106,910	4,034,786

The pension benefit amounts in the tables above were calculated as of December 31, 2007 assuming payments would begin as soon as possible under the terms of the plans. Accordingly, appropriate early retirement reductions were applied. Any unpaid incentives were assumed to be paid at 1.35 times the target level. Pension Plan benefits were calculated assuming named executive officers chose a single life annuity form of payment, because that results in the greatest monthly benefit. The single sum values of the SBP-P and the SERP benefits were based on a 4.85% discount rate as prescribed by the terms of the plan for those who separated from service in 2007.

Annual Incentive Program
Because this section assumes that a termination or change-in-control event occurred on December 31, 2007, there is no amount that would be payable other than what was reported and described in the Summary Compensation Table because actual performance in 2007 exceeded target performance.

Performance Dividend Program
Because the assumed termination date is December 31, 2007, there is no additional amount that would be payable other than the amount reported in the Summary Compensation Table under the Traditional Termination Events. As described in the

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Traditional Termination Events Chart, there is some continuation of benefits under the performance dividend program for retirees.

However, under Change-in-Control-Related Events, performance dividends are payable at the greater of target performance or actual performance. For the 2004-2007 performance measurement period, actual performance was less than target performance. The table below estimates the additional amount that would have been payable under the performance dividend program if a change in control occurred as of December 31, 2007.

Name	Additional Performance Dividends ($)
D. M. Ratcliffe	446,830
T. A. Fanning	82,899
M. D. Garrett	57,608
C. D. McCrary	78,167
G. E. Holland, Jr.	72,013

Stock Options

Stock options would be treated as described in the Termination and Change-in-Control charts above. Under a Southern Termination, all stock options vest. In addition, if there is an Involuntary Change-in-Control Termination or Voluntary Change-in-Control Termination for Good Reason, stock options vest. There is no payment associated with stock options unless there is a Southern Termination and the participants stock options cannot be converted into surviving company stock options. In that event, the excess of the exercise price and the closing price of Common Stock on December 31, 2007 would have been paid in cash for all stock options held by the named executive officers. The chart below shows the number of stock options for which vesting would be accelerated under a Southern Termination and the amount that would be payable under a Southern Termination if there were no conversion to the surviving entity s stock options.

Name	Number of Options with Accelerated Vesting (#)	Total Number of Options Following Accelerated Vesting under a Southern Termination (#)	Total Payable in Cash under a Southern Termination without Conversion of Stock Options ($)
D. M. Ratcliffe	1,066,994	2,054,391	11,728,333
T. A. Fanning	189,924	381,146	2,232,569
M. D. Garrett	189,395	264,863	1,181,623
C. D. McCrary	197,269	359,389	1,912,094
G. E. Holland, Jr.	149,423	331,094	2,058,245

DCP and SBP

The aggregate balances reported in the Nonqualified Deferred Compensation Table would be payable to the named executive officers as described in the Traditional Termination and Change-in-Control-Related Events charts above. There is no enhancement or acceleration of payments under these plans associated with termination or

change-in-control events, other than the lump-sum payment opportunity described in the above charts. The lump-sums that would be payable are those that are reported in the Nonqualified Deferred Compensation Table.

Health Benefits

Because all of the named executive officers are retirement eligible and health care benefits are provided to retirees, there is no incremental payment associated with the termination or change-in-control events.

Gross

Gross

Amortized

Unrealized

Unrealized

Fair

Cost

Gains

Losses

Value

September 30, 2016 (unaudited)

Issued by U.S. government-sponsored entities and agencies:

U.S. Treasury

$

8,548

$

61

$

-

$

8,609

Mortgage-backed securities - residential

375

17

-

392

Collateralized mortgage obligations

217

8

-

225

Total

$

9,140

$

86

$

-

$

9,226

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2015				
Issued by U.S. government-sponsored entities and agencies:				
U.S. Treasury	$ 8,575	$ 4	$ 43	$ 8,536
Mortgage-backed securities - residential	463	18	-	481
Collateralized mortgage obligations	339	12	-	351
Total	$ 9,377	$ 34	$ 43	$ 9,368

There was no other-than-temporary impairment recognized in accumulated other comprehensive income (loss) for securities available for sale at September 30, 2016 or September 30, 2015.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

There were no sales of securities for the three and nine months ended September 30, 2016 or September 30, 2015; however, there was an early redemption of a municipal security during the first quarter of 2015 which is reflected in net gain (loss) on sales of securities.

The amortized cost and fair value of debt securities at September 30, 2016 and December 31, 2015 are shown in the table below by contractual maturity. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

	September 30, 2016 (unaudited)		December 31, 2015	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 3,014	$ 3,015	$ 1,002	$ 1,000
Due from one to five years	5,534	5,594	7,573	7,536
Mortgage-backed securities - residential	375	392	463	481
Collateralized mortgage obligations	217	225	339	351
Total	$ 9,140	$ 9,226	$ 9,377	$ 9,368

Fair value of securities pledged was as follows:

	September 30, 2016 (unaudited)	December 31, 2015
Pledged as collateral for:		
FHLB advances	$ 3,390	$ 3,530
Public deposits	2,053	2,055
Interest-rate swaps	214	261
Total	$ 5,657	$ 5,846

At September 30, 2016 and December 31, 2015, there were no holdings of securities of any one issuer, other than U.S. government-sponsored entities and agencies, in an amount greater than 10% of stockholders' equity.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table summarizes securities with unrealized losses at September 30, 2016 and December 31, 2015 aggregated by major security type and length of time in a continuous unrealized loss position.

September 30, 2016 (unaudited)	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Issued by U.S. government-sponsored entities and agencies:						
U.S. Treasury (1)	$ 1,512	$ -	$ -	$ -	$ 1,512	$ -
Mortgage-backed securities - residential	-	-	-	-	-	-
Collateralized mortgage obligations	-	-	-	-	-	-
Total temporarily impaired	$ 1,512	$ -	$ -	$ -	$ 1,512	$ -

(1) Securities with an unrealized loss were less than $1 resulting in rounding to zero

December 31, 2015	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Issued by U.S. government-sponsored entities and agencies:						
U.S. Treasury	$ 6,541	$ 43	$ -	$ -	$ 6,541	$ 43
Mortgage-backed securities - residential	-	-	-	-	-	-
Collateralized mortgage obligations	-	-	-	-	-	-
Total temporarily impaired	$ 6,541	$ 43	$ -	$ -	$ 6,541	$ 43

The unrealized losses in U.S. Treasuries at September 30, 2016 and December 31, 2015 are related to multiple securities. Because the decline in fair value is attributable to changes in market conditions, and not credit quality, and

because the Company does not have the intent to sell these securities and it is likely that it will not be required to sell these securities before their anticipated recovery, the Company did not consider these securities to be other-than-temporarily impaired at December 31, 2015.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

NOTE 4 – LOANS AND LEASES

The following table presents the recorded investment in loans by portfolio segment. The recorded investment in loans includes the principal balance outstanding adjusted for purchase premiums and discounts, and deferred loan fees and costs.

	September 30, 2016 (unaudited)	December 31, 2015
Commercial	$ 70,128	$ 43,744
Real estate:		
Single-family residential	87,949	81,985
Multi-family residential	32,493	28,950
Commercial	100,695	96,488
Construction	21,251	24,662
Consumer:		
Home equity lines of credit	23,074	21,837
Other	679	6,018
Subtotal	336,269	303,684
Less: ALLL	(6,893)	(6,620)
Loans and leases, net	$ 329,376	$ 297,064

Mortgage Purchase Program

CFBank has participated in a Mortgage Purchase Program with Northpointe Bank (Northpointe), a Michigan banking corporation, since December 2012. Pursuant to the terms of a participation agreement, CFBank purchases participation interests in loans made by Northpointe related to fully underwritten and pre-sold mortgage loans originated by various prescreened mortgage brokers located throughout the U.S. The underlying loans are individually (MERS) registered loans which are held until funded by the end investor. The mortgage loan investors include Fannie Mae and Freddie Mac, and other major financial institutions. This process on average takes approximately 14 days. Given the short-term holding period of the underlying loans, common credit risks (such as past due, impairment and TDR, nonperforming, and nonaccrual classification) are substantially reduced. Therefore, no allowance is allocated by CFBank to these loans. These loans are 100% risk rated for CFBank capital adequacy purposes. Under the participation agreement, CFBank agrees to purchase a 95% ownership/participation interest in each of the aforementioned loans, and Northpointe maintains a 5% ownership interest in each loan it participates. At September 30, 2016 and December 31, 2015, CFBank held $43,056 and $43,517, respectively, of such loans which

have been included in single-family residential loan totals above.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

Allowance for Loan and Lease Losses

The ALLL is a valuation allowance for probable incurred credit losses in the loan portfolio based on management's evaluation of various factors including past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions and other factors. A provision for loan and lease losses is charged to operations based on management's periodic evaluation of these and other pertinent factors described in Note 1 to the 2015 Audited Financial Statements.

The following table presents the activity in the ALLL by portfolio segment for the three and nine months ended September 30, 2016:

	Three months ended September 30, 2016 (unaudited)							
		Real Estate				Consumer		
	Commercial	Single-family	Multi-family	Commercial	Construction	Home Equity lines of credit	Other	Total
Beginning balance	$ 1,458	$ 875	$ 694	$ 2,567	$ 478	$ 534	$ 7	$ 6,613
Addition to (reduction in) provision for loan losses	252	(54)	(122)	(52)	25	(62)	33	20
Charge-offs	(5)	-	-	-	-	-	(1)	(6)
Recoveries	-	3	143	100	-	20	-	266
Ending balance	$ 1,705	$ 824	$ 715	$ 2,615	$ 503	$ 492	$ 39	$ 6,893

	Nine months ended September 30, 2016 (unaudited)							
		Real Estate				Consumer		
	Commercial	Single-family	Multi-family	Commercial	Construction	Home Equity lines	Other	Total

						of credit		
Beginning balance	$ 1,380	$ 691	$ 705	$ 2,710	$ 561	$ 474	$ 99	$ 6,620
Addition to (reduction in) provision for loan losses	448	223	(133)	(195)	(58)	4	(59)	230
Charge-offs	(123)	(94)	-	-	-	(53)	(1)	(271)
Recoveries	-	4	143	100	-	67	-	314
Ending balance	$ 1,705	$ 824	$ 715	$ 2,615	$ 503	$ 492	$ 39	$ 6,893

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table presents the activity in the ALLL by portfolio segment for the three and nine months ended September 30, 2015:

	Three months ended September 30, 2015 (unaudited)							
	Real Estate					Consumer		
	Commercial	Single-family	Multi-family	Commercial	Construction	Home Equity lines of credit	Other	Total
Beginning balance	$ 1,394	$ 658	$ 754	$ 2,372	$ 722	$ 470	$ 110	$ 6,480
Addition to (reduction in) provision for loan losses	(121)	6	(4)	276	(120)	17	(4)	50
Charge-offs	-	(9)	-	-	-	-	-	(9)
Recoveries	-	-	-	(3)	-	4	-	1
Ending balance	$ 1,273	$ 655	$ 750	$ 2,645	$ 602	$ 491	$ 106	$ 6,522

	Nine months ended September 30, 2015 (unaudited)							
	Real Estate					Consumer		
	Commercial	Single-family	Multi-family	Commercial	Construction	Home Equity lines of credit	Other	Total
Beginning balance	$ 1,346	$ 634	$ 818	$ 2,541	$ 442	$ 441	$ 94	$ 6,316
Addition to (reduction in) provision for loan losses	(90)	60	(68)	96	160	26	16	200
Charge-offs	(8)	(40)	-	(25)	-	-	(10)	(83)
Recoveries	25	1	-	33	-	24	6	89
Ending balance	$ 1,273	$ 655	$ 750	$ 2,645	$ 602	$ 491	$ 106	$ 6,522

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table presents the balance in the ALLL and the recorded investment in loans by portfolio segment and based on the impairment method as of September 30, 2016 (unaudited):

		Real Estate				Consumer Home Equity lines of credit		
	Commercial	Single-family	Multi-family	Commercial	Construction		Other	Total
ALLL:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ -	$ -	$ -	$ 25	$ -	$ -	$ -	$ 25
Collectively evaluated for impairment	1,705	824	715	2,590	503	492	39	6,868
Total ending allowance balance	$ 1,705	$ 824	$ 715	$ 2,615	$ 503	$ 492	$ 39	$ 6,893
Loans:								
Individually evaluated for impairment	$ 674	$ 284	$ 39	$ 2,971	$ -	$ -	$ -	$ 3,968
Collectively evaluated for impairment	69,454	87,665	32,454	97,724	21,251	23,074	679	332,301
Total ending loan balance	$ 70,128	$ 87,949	$ 32,493	$ 100,695	$ 21,251	$ 23,074	$ 679	$ 336,269

The following table presents the balance in the ALLL and the recorded investment in loans by portfolio segment and based on the impairment method as of December 31, 2015:

		Real Estate				Consumer		
	Commercial	Single-family	Multi-family	Commercial	Construction	Home Equity lines of credit	Other	Total
ALLL:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 5	$ 1	$ -	$ 14	$ -	$ -	$ -	$ 20
Collectively evaluated for impairment	1,375	690	705	2,696	561	474	99	6,600
Total ending allowance balance	$ 1,380	$ 691	$ 705	$ 2,710	$ 561	$ 474	$ 99	$ 6,620
Loans:								
Individually evaluated for impairment	$ 422	$ 289	$ 1,590	$ 3,449	$ -	$ -	$ -	$ 5,750
Collectively evaluated for impairment	43,322	81,696	27,360	93,039	24,662	21,837	6,018	297,934
Total ending loan balance	$ 43,744	$ 81,985	$ 28,950	$ 96,488	$ 24,662	$ 21,837	$ 6,018	$ 303,684

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(Dollars in thousands)

The following table presents loans individually evaluated for impairment by class of loans at September 30, 2016. The unpaid principal balance is the contractual principal balance outstanding. The recorded investment is the unpaid principal balance adjusted for partial charge-offs, purchase premiums and discounts, deferred loan fees and costs. The table presents accrual basis interest income recognized during the three and nine months ended September 30, 2016. Cash payments of interest on these loans during the three and nine months ended September 30, 2016 totaled $60 and $174, respectively.

	As of September 30, 2016 (unaudited)			Three months ended September 30, 2016 (unaudited)		Nine months ended September 30, 2016 (unaudited)	
	Unpaid Principal Balance	Recorded Investment	ALLL Allocated	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:							
Commercial	$ 576	$ 458	$ -	$ 457	$ 4	$ 455	$ 9
Real estate:							
Single-family residential	322	161	-	161	-	161	-
Multi-family residential	-	-	-	-	-	-	-
Commercial:							
Non-owner occupied	-	-	-	-	-	-	-
Owner occupied	877	356	-	358	13	363	35
Land	-	-	-	-	-	-	-
Total with no allowance recorded	1,775	975	-	976	17	979	44
With an allowance recorded:							
Commercial	216	216	-	222	1	241	3
Real estate:							
Single-family residential	123	123	-	124	2	126	6
Multi-family residential	39	39	-	40	1	42	2
Commercial:							
Non-owner occupied	2,192	2,192	20	2,196	33	2,206	101
Owner occupied	205	205	2	206	2	209	7
Land	263	218	3	222	4	232	11
Total with an allowance recorded	3,038	2,993	25	3,010	43	3,056	130
Total	$ 4,813	$ 3,968	$ 25	$ 3,986	$ 60	$ 4,035	$ 174

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(Dollars in thousands)

The following table presents loans individually evaluated for impairment by class of loans at December 31, 2015. The unpaid principal balance is the contractual principal balance outstanding. The recorded investment is the unpaid principal balance adjusted for partial charge-offs, purchase premiums and discounts, deferred loan fees and costs. The table presents accrual basis interest income recognized during the three and nine months ended September 30, 2015. Cash payments of interest during the three and nine months ended September 30, 2015 totaled $83 and $251, respectively.

	As of December 31, 2015			Three months ended September 30, 2015 (unaudited)		Nine months ended September 30, 2015 (unaudited)	
	Unpaid Principal Balance	Recorded Investment	ALLL Allocated	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:							
Commercial	$ 36	$ 28	$ -	$ 69	$ -	$ 75	$ 1
Real estate:							
Single-family residential	322	161	-	163	-	167	-
Multi-family residential	1,545	1,545	-	1,557	24	1,565	71
Commercial:							
Non-owner occupied	546	446	-	446	-	458	-
Owner occupied	688	167	-	173	10	176	29
Land	-	-	-	-	-	-	-
Total with no allowance recorded	3,137	2,347	-	2,408	34	2,441	101
With an allowance recorded:							
Commercial	394	394	5	427	3	452	9
Real estate:							
Single-family residential	128	128	1	130	1	131	5
Multi-family residential	45	45	-	47	1	49	2
Commercial:							
Non-owner occupied	2,224	2,224	9	2,238	34	2,247	102
Owner occupied	363	363	1	369	5	373	16
Land	294	249	4	267	4	280	13
Total with an allowance recorded	3,448	3,403	20	3,478	48	3,532	147
Total	$ 6,585	$ 5,750	$ 20	$ 5,886	$ 82	$ 5,973	$ 248

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table presents the recorded investment in nonperforming loans by class of loans:

	September 30, 2016 (unaudited)	December 31, 2015
Loans past due over 90 days still on accrual	$ -	$ -
Nonaccrual loans:		
Commercial	276	224
Real estate:		
Single-family residential	546	640
Commercial:		
Non-owner occupied	-	446
Consumer:		
Home equity lines of credit:		
Originated for portfolio	46	20
Purchased for portfolio	-	95
Total nonaccrual	868	1,425
Total nonaccrual and nonperforming loans	$ 868	$ 1,425

Nonaccrual loans include both smaller balance single-family mortgage and consumer loans that are collectively evaluated for impairment and individually classified impaired loans. There were no loans 90 days or more past due and still accruing interest at September 30, 2016 or December 31, 2015.

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(Dollars in thousands)

The following table presents the aging of the recorded investment in past due loans by class of loans as of September 30, 2016 (unaudited):

	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Nonaccrual Loans Not > 90 days Past Due
Commercial	$ -	$ -	$ 119	$ 119	$ 70,009	$ 157
Real estate:						
Single-family residential	914	764	287	1,965	85,984	259
Multi-family residential	-	-	-	-	32,493	-
Commercial:						
Non-owner occupied	-	-	-	-	58,251	-
Owner occupied	-	-	-	-	33,186	-
Land	-	-	-	-	9,258	-
Construction	-	-	-	-	21,251	-
Consumer:						
Home equity lines of credit:						
Originated for portfolio	-	-	46	46	22,253	-
Purchased for portfolio	70	-	-	70	705	-
Other	-	-	-	-	679	-
Total	$ 984	$ 764	$ 452	$ 2,200	$ 334,069	$ 416

The following table presents the aging of the recorded investment in past due loans by class of loans as of December 31, 2015:

	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Nonaccrual Loans Not > 90 days Past Due
Commercial	$ -	$ 9	$ 28	$ 37	$ 43,707	$ 196
Real estate:						
Single-family residential	598	161	148	907	81,078	492

Multi-family residential	-	-	-	-	28,950	-
Commercial:						
Non-owner occupied	-	446	-	446	57,573	446
Owner occupied	-	-	-	-	30,169	-
Land	-	-	-	-	8,300	-
Construction	-	-	-	-	24,662	-
Consumer:						
Home equity lines of credit:						
Originated for portfolio	-	-	-	-	20,789	20
Purchased for portfolio	-	-	-	-	1,048	95
Other	-	-	-	-	6,018	-
Total	$ 598	$ 616	$ 176	$ 1,390	$ 302,294	$ 1,249

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Troubled Debt Restructurings (TDRs):

From time to time, the terms of certain loans are modified as TDRs, where concessions are granted to borrowers experiencing financial difficulties. The modification of the terms of such loans may have included one or a combination of the following: a reduction of the stated interest rate of the loan; an increase in the stated rate of interest lower than the current market rate for new debt with similar risk; an extension of the maturity date; or a change in the payment terms.

As of September 30, 2016 and December 31, 2015, TDRs totaled $3,648 and $5,276, respectively. The Company allocated $25 and $20 of specific reserves to loans whose terms had been modified in TDRs as of September 30, 2016 and December 31, 2015, respectively. The Company had not committed to lend any additional amounts as of September 30, 2016 or December 31, 2015 to customers with outstanding loans classified as nonaccrual TDRs.

During the three and nine months ended September 30, 2016, there was one commercial loan in the amount of $339 that was modified as a TDR, where concessions were granted to a borrower experiencing financial difficulty. During the three months ended September 30, 2015, there were no loans modified as a TDR. During the nine months ended September 30, 2015, there was one single-family residential loan in the amount of $9 and one home equity line of credit in the amount of $9 that were modified as TDRs, where concessions were granted to borrowers experiencing financial difficulties. The home equity line of credit was paid off prior to September 30, 2015.

There was one nonperforming TDR that went into payment default during the nine months ended September 30, 2016. There were no TDRs in payment default or that became nonperforming during the period ended September 30, 2015. A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms, at which time the loan is re-evaluated to determine whether an impairment loss should be recognized, either through a write-off or specific valuation allowance, so that the loan is reported, net, at the present value of estimated future cash flows, or at the fair value of collateral, less cost to sell, if repayment is expected solely from the collateral.

The terms of certain other loans were modified during the quarter ended September 30, 2016 and 2015 that did not meet the definition of a TDR. These loans had a total recorded investment of $18,255 and $6,915 as of September 30, 2016 and 2015, respectively. The modification of these loans involved either a modification of the terms of a loan to borrowers who were not experiencing financial difficulties, a delay in payments that was considered to be insignificant or there were no concessions granted.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Company’s internal underwriting policy.

Nonaccrual loans include loans that were modified and identified as TDRs and the loans are not performing. At September 30, 2016 and December 31, 2015, nonaccrual TDRs were as follows:

	September 30, 2016 (unaudited)	December 31, 2015
Commercial	$ 157	$ 195
Real estate:		
Single-family residential	161	161
Total	$ 318	$ 356

Nonaccrual loans at September 30, 2016 and December 31, 2015 do not include $3,330 and $4,920, respectively, of TDRs where customers have established a sustained period of repayment performance, generally six months, the loans are current according to their modified terms and repayment of the remaining contractual payments is expected. These loans are included in total impaired loans.

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(Dollars in thousands)

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt, such as current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. Management analyzes loans individually by classifying the loans as to credit risk. This analysis includes commercial, commercial real estate and multi-family residential real estate loans. Internal loan reviews for these loan types are performed at least annually, and more often for loans with higher credit risk. Adjustments to loan risk ratings are made based on the reviews and at any time information is received that may affect risk ratings. The following definitions are used for risk ratings:

Special Mention. Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of CFBank's credit position at some future date.

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that there will be some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Loans not meeting the criteria to be classified into one of the above categories are considered to be not rated or pass-rated loans. Loans listed as not rated are primarily groups of homogeneous loans. Past due information is the primary credit indicator for groups of homogenous loans. Loans listed as pass-rated loans are loans that are subject to internal loan reviews and are determined not to meet the criteria required to be classified as special mention, substandard or doubtful.

The recorded investment in loans by risk category and by class of loans as of September 30, 2016 and based on the most recent analysis performed follows. There were no loans rated doubtful at September 30, 2016.

(unaudited)	Not Rated	Pass	Special Mention	Substandard	Total
Commercial	$ 5,961	$ 63,370	$ 123	$ 674	$ 70,128
Real estate:					
Single-family residential	87,384	-	-	565	87,949
Multi-family residential	-	31,810	510	173	32,493
Commercial:					
Non-owner occupied	118	55,458	1,802	873	58,251
Owner occupied	-	30,054	1,895	1,237	33,186
Land	-	6,803	-	2,455	9,258

Construction	4,470	16,781	-	-	21,251
Consumer:					
Home equity lines of credit:					
Originated for portfolio	22,167	-	-	132	22,299
Purchased for portfolio	630	-	-	145	775
Other	679	-	-	-	679
	$ 121,409	$ 204,276	$ 4,330	$ 6,254	$ 336,269

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The recorded investment in loans by risk category and by class of loans as of December 31, 2015 follows. There were no loans rated doubtful at December 31, 2015.

	Not Rated	Pass	Special Mention	Substandard	Total
Commercial	$ 83	$ 41,473	$ 1,892	$ 296	$ 43,744
Real estate:					
Single-family residential	81,318	-	-	667	81,985
Multi-family residential	2,777	25,466	528	179	28,950
Commercial:					
Non-owner occupied	125	54,674	1,852	1,368	58,019
Owner occupied	-	26,923	3,079	167	30,169
Land	-	5,720	-	2,580	8,300
Construction	11,252	13,410	-	-	24,662
Consumer:					
Home equity lines of credit:					
Originated for portfolio	20,677	-	-	112	20,789
Purchased for portfolio	802	-	-	246	1,048
Other	2,172	3,846	-	-	6,018
	$ 119,206	$ 171,512	$ 7,351	$ 5,615	$ 303,684

NOTE 5 - FAIR VALUE

Fair value is the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2 – Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The Company used the following methods and significant assumptions to estimate the fair value of each type of asset and liability:

Securities available for sale: The fair value of securities available for sale is determined using pricing models that vary based on asset class and include available trade, bid and other market information or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2).

Derivatives: The fair value of derivatives, which includes yield maintenance provisions, interest rate lock commitments and interest rate swaps, is based on valuation models using observable market data as of the measurement date (Level 2).

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Impaired loans: The fair value of impaired loans with specific allocations of the ALLL is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for collateral-dependent impaired loans are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by a third-party appraisal management company approved by the Board of Directors annually. Once received, the loan officer or a member of the credit department reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics. Appraisals are updated as needed based on facts and circumstances associated with the individual properties. Real estate appraisals typically incorporate measures such as recent sales prices for comparable properties. Appraisers may make adjustments to the sales prices of the comparable properties as deemed appropriate based on the age, condition or general characteristics of the subject property. Management applies an additional discount to real estate appraised values, typically to reflect changes in market conditions since the date of the appraisal if warranted and to cover disposition costs (including selling expenses) based on the intended disposition method of the property. Non-real estate collateral may be valued using an appraisal, net book value per the borrower’s financial statements, or aging reports, adjusted or discounted based on management’s historical knowledge, changes in market conditions from the time of the valuation, and management’s expertise and knowledge of the client and client’s business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Loans held for sale: Loans held for sale are carried at fair value, as determined by outstanding commitments from third party investors (Level 2). During the second quarter of 2015, CFBank signed an agreement with the intent to sell its credit card portfolio to a third party. As a result, as of June 30, 2015, the credit card portfolio was transferred to loans held for sale at the lower of cost or market of $175,000, which approximated fair value at the time of transfer. In February 2016, the sale of the credit card portfolio was consummated.

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Assets and liabilities measured at fair value on a recurring basis, including financial assets and liabilities for which the Company has elected the fair value option, are summarized below:

	Fair Value Measurements at September 30, 2016 using Significant Other Observable Inputs (Level 2) (unaudited)	
Financial Assets:		
Securities available for sale:		
Issued by U.S. government-sponsored entities and agencies:		
U.S. Treasury	$	8,609
Mortgage-backed securities - residential		392
Collateralized mortgage obligations		225
Total securities available for sale	$	9,226
Loans held for sale		2,466
Yield maintenance provisions (embedded derivatives)	$	214
Interest rate lock commitments	$	19
Financial Liabilities:		
Interest-rate swaps	$	214

Fair Value Measurements at

	December 31, 2015 using Significant Other Observable Inputs (Level 2)
Financial Assets:	
Securities available for sale:	
Issued by U.S. government-sponsored entities and agencies:	
U.S. Treasury	$ 8,536
Mortgage-backed securities - residential	481
Collateralized mortgage obligations	351
Total securities available for sale	$ 9,368
Loans held for sale	889
Yield maintenance provisions (embedded derivatives)	$ 213
Interest rate lock commitments	$ 8
Financial Liabilities:	
Interest-rate swaps	$ 213

The Company had no assets or liabilities measured at fair value on a recurring basis that were measured using Level 1 or Level 3 inputs at September 30, 2016 or December 31, 2015. There were no transfers of assets or labilities measured at fair value between levels during the period ended September 30, 2016 and December 31, 2015.

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(Dollars in thousands)

Assets and liabilities measured at fair value on a non-recurring basis are summarized below:

	Fair Value Measurements at September 30, 2016 Using Significant Unobservable Inputs (Level 3) (unaudited)
Impaired loans:	
Commercial	$ 134
Real Estate:	
Single-family residential	123
Multi-family residential	39
Commercial:	
Non-owner occupied	2,172
Owner occupied	203
Land	215
Total impaired loans	$ 2,886

	Fair Value Measurements at December 31, 2015 Using Significant Unobservable Inputs (Level 3)
Impaired loans:	
Commercial	$ 143
Real Estate:	
Single-family residential	128
Multi-family residential	45
Commercial:	
Non-owner occupied	2,215
Owner occupied	213
Land	245

Total impaired loans	$ 2,989

The Company had no material assets or liabilities measured at fair value on a non-recurring basis that were measured using Level 1 or Level 2 inputs at September 30, 2016 or December 31, 2015.

Impaired loans that are measured for impairment using the fair value of the collateral for collateral dependent loans, had a principal balance of $2,956 with a valuation allowance of $25, at September 30, 2016. There were no write-downs of impaired collateral dependent loans during the three and nine months ended September 30, 2016 or 2015. Impaired loans that are measured for impairment using the fair value of the collateral for collateral dependent loans, had a principal balance of $3,050, with a valuation allowance of $16 at December 31, 2015.

During the three and nine months ended September 30, 2016, the Company did not have any transfers of assets or liabilities between those measured using Level 1, 2 or 3 inputs. The Company recognizes transfers of assets and liabilities between Level 1, 2 and 3 inputs based on the information relating to those assets and liabilities at the end of the reporting period.

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(Dollars in thousands)

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at September 30, 2016 (unaudited):

	Fair Value	Valuation Technique(s)	Unobservable Inputs	(Range) Weighted Average
Impaired loans:				
Commercial	$ 134	Comparable sales approach	Adjustment for differences between the comparable market transactions	3.48%
Real estate:				
Single-family residential	123	Comparable sales approach	Adjustment for differences between the comparable market transactions	(1.81% , 3.61%) 2.91%
Multi-family residential	39	Comparable sales approach	Adjustment for differences between the comparable market transactions	9.64%
Commercial:				
Non-owner occupied	2,172	Comparable sales approach	Adjustment for differences between the comparable market transactions	(1.10%, 5.74%) 1.35%
Owner occupied	203	Comparable sales approach	Adjustment for differences between the comparable market transactions	-4.46%
Land	215	Comparable sales approach	Adjustment for differences between the comparable market transactions	(-2.73%, 1.50%) -.43%

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at December 31, 2015:

	Fair Value	Valuation Technique(s)	Unobservable Inputs	(Range) Weighted Average
Impaired loans:				
Commercial	$ 143	Comparable sales approach	Adjustment for differences between the comparable market transactions	1.10%
Real estate:				
Single -family residential	128	Comparable sales approach	Adjustment for differences between the comparable market transactions	(-1.23% , 4.63%) -.17%
Multi-family residential	45	Comparable sales approach	Adjustment for differences between the comparable market transactions	5.74%

Commercial:				
Non-owner occupied	2,215	Comparable sales approach	Adjustment for differences between the comparable market transactions	(1.10%, 5.74%) 1.35%
Owner occupied	213	Comparable sales approach	Adjustment for differences between the comparable market transactions	-29.30%
Land	245	Comparable sales approach	Adjustment for differences between the comparable market transactions	(-1.89%, 2.54%) .08%

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(Dollars in thousands)

Financial Instruments Recorded Using Fair Value Option

The Company has elected the fair value option for loans held for sale. These loans are intended for sale and the Company believes that the fair value is the best indicator of the resolution of these loans. Loans originated as construction loans, that were subsequently transferred to held for sale, are carried at the lower of cost or market and are not included. Interest income is recorded based on the contractual terms of the loan and in accordance with the Company’s policy on loans held for investment. None of these loans were 90 days or more past due or on nonaccrual as of September 30, 2016 or December 31, 2015.

As of September 30, 2016 and December 31, 2015, the aggregate fair value, contractual balance and gain or loss of loans held for sale were as follows:

	September 30, 2016 (unaudited)	December 31, 2015
Aggregate fair value	$ 2,466	$ 889
Contractual balance	2,459	884
Gain (loss)	7	5

The total amount of gains and losses from changes in fair value included in earnings for the three and nine months ended September 30, 2016 and 2015 for loans held for sale were:

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
	(unaudited)		(unaudited)	
Interest income	$ 25	$ 14	$ 40	$ 54
Interest expense	-	-	-	-
Change in fair value	(2)	(14)	2	(11)
Total change in fair value	$ 23	$ -	$ 42	$ 43

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(Dollars in thousands)

The carrying amounts and estimated fair values of financial instruments at September 30, 2016 were as follows:

	Fair Value Measurements at September 30, 2016 Using (unaudited):				
	Carrying Value	Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	$ 52,302	$ 52,302	$ -	$ -	$ 52,302
Interest-bearing deposits in other financial institutions	100	100	-	-	100
Securities available for sale	9,226	-	9,226	-	9,226
Loans held for sale	2,466	-	2,466	-	2,466
Loans, net	329,376	-	-	328,979	328,979
FHLB stock	1,942	n/a	n/a	n/a	n/a
Accrued interest receivable	925	2	17	906	925
Yield maintenance provisions (embedded derivatives)	214	-	214	-	214
Interest rate lock commitments	19	-	19	-	19
Financial liabilities					
Deposits	$ (345,854)	$ (172,648)	(173,764)	$ -	$ (346,412)
FHLB advances and other borrowings	(15,500)	-	(15,880)	-	(15,880)
Advances by borrowers for taxes and insurance	(349)	-	-	(349)	(349)
Subordinated debentures	(5,155)	-	(3,492)	-	(3,492)
Accrued interest payable	(64)	-	(64)	-	(64)
Interest-rate swaps	(214)	-	(214)	-	(214)

The carrying amounts and estimated fair values of financial instruments at December 31, 2015 were as follows:

	Fair Value Measurements at December 31, 2015 Using:				
	Carrying Value	Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	$ 25,895	$ 25,895	$ -	$ -	$ 25,895
Securities available for sale	9,368	-	9,368	-	9,368
Loans held for sale	889	-	889	-	889
Loans, net	297,064	-	-	295,498	295,498

FHLB stock	1,942	n/a	n/a	n/a	n/a
Accrued interest receivable	831	1	21	809	831
Yield maintenance provisions (embedded derivatives)	213	-	213	-	213
Interest rate lock commitments	8	-	8	-	8
Financial liabilities					
Deposits	$ (290,467)	$ (147,523)	$ (143,236)	$ -	$ (290,759)
FHLB advances and other borrowings	(14,500)	-	(14,693)	-	(14,693)
Advances by borrowers for taxes and insurance	(656)	-	-	(656)	(656)
Subordinated debentures	(5,155)	-	(2,269)	-	(2,269)
Accrued interest payable	(44)	-	(44)	-	(44)
Interest-rate swaps	(213)	-	(213)	-	(213)

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The methods and assumptions, not previously presented, used to estimate fair values are described as follows:

Cash and Cash Equivalents and Interest-Bearing Deposits in Other Financial Institutions

The carrying amounts of cash and short-term instruments approximate fair values and are classified as Level 1.

FHLB Stock

It is not practical to determine the fair value of FHLB stock due to restrictions placed on its transferability.

Loans

Fair values of loans, excluding loans held for sale, are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values resulting in a Level 3 classification. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Impaired loans are valued at the lower of cost or fair value as described previously. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

Deposits

The fair values disclosed for demand deposits (e.g., interest and noninterest bearing checking, passbook savings, and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount) resulting in a Level 1 classification. Fair values for fixed rate certificates of deposit are estimated using a discounted cash flows calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.

Other Borrowings

The fair values of the Company’s long-term FHLB advances are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

The fair values of the Company’s subordinated debentures are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

Accrued Interest Receivable/Payable

The carrying amounts of accrued interest approximate fair value resulting in a Level 1, 2 or 3 classification, consistent with the asset or liability with which they are associated.

Advances by Borrowers for Taxes and Insurance

The carrying amount of advances by borrowers for taxes and insurance approximates fair value resulting in a Level 3 classification, consistent with the liability with which they are associated.

Off-Balance-Sheet Instruments

The fair value of off-balance-sheet items is not considered material.

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NOTE 6 – SUBORDINATED DEBENTURES

In December 2003, Central Federal Capital Trust I, a trust formed by the Holding Company, closed a pooled private offering of 5,000 trust preferred securities with a liquidation amount of $1 per security. The Holding Company issued $5,155 of subordinated debentures to the trust in exchange for ownership of all of the common stock of the trust and the proceeds of the preferred securities sold by the trust. The Holding Company is not considered the primary beneficiary of this trust (variable interest entity); therefore, the trust is not consolidated in the Company's financial statements, but rather the subordinated debentures are shown as a liability. The Holding Company's investment in the common stock of the trust was $155 and is included in other assets.

The subordinated debentures have a variable rate of interest, reset quarterly, equal to the three-month London Interbank Offered Rate plus 2.85%, which was 3.69% at September 30, 2016 and 3.45% at December 31, 2015.

The Holding Company may redeem the subordinated debentures, in whole or in part, in a principal amount with integral multiples of $1, at 100% of the principal amount, plus accrued and unpaid interest. The subordinated debentures mature on December 30, 2033. The subordinated debentures are also redeemable in whole or in part from time to time, upon the occurrence of specific events defined within the trust indenture. There are no required principal payments on the subordinated debentures over the next five years. The Holding Company has the option to defer interest payments on the subordinated debentures for a period not to exceed five consecutive years.

The Holding Company's Board of Directors elected to defer interest payments on the subordinated debentures from time to time beginning in December 2010 in order to preserve cash at the Holding Company. However, in June 2014, the Holding Company paid all deferred and current interest payments in the amount of $293, with the prior approval of the FRB. The Holding Company paid the interest current on the subordinated debentures for all subsequent quarters through December 31, 2015, after receiving the prior approval or written non-objection of the FRB to make such payments as required by the terms of the Holding Company Order and the subsequent commitments made by the Company following the termination of the Holding Company Order. Effective as of January 8, 2016, the Holding Company is no longer required to obtain the prior approval or non-objection of the FRB in order to pay current quarterly interest on the subordinated debentures. The Company paid the interest current for the quarters ended March 31, 2016, June 30, 2016 and September 30, 2016. There were no accrued deferred payments at September 30, 2016 and December 31, 2015.

NOTE 7 – STOCK-BASED COMPENSATION

The Company has issued awards under three stock-based compensation plans (the "Plans"), as described below. Total compensation cost that has been charged against income for those Plans totaled $33 and $92, respectively, for the three and nine months ended September 30, 2016 and $31 and $102, respectively, for the three and nine months ended September 30, 2015. The total income tax effect was $9 and $26, respectively, for the three and nine months ended September 30, 2016, and $2 and $6, respectively, for the three and nine months ended September 30, 2015.

The Plans are all stockholder-approved and authorize stock option grants and restricted stock awards to be made to directors, officers and employees. The 1999 Stock-Based Incentive Plan, which expired July 13, 2009, provided 38,778 shares of common stock for stock option grants and 15,511 shares of common stock for restricted stock awards. The 2003 Equity Compensation Plan (the “2003 Plan”), as amended and restated, provided an aggregate of 100,000 shares for stock option grants and restricted stock awards, of which up to 30,000 shares could be awarded in the form of restricted stock awards. The 2009 Equity Compensation Plan (the “2009 Plan”), which was approved by stockholders on May 21, 2009, replaced the 2003 Plan and provided for 200,000 shares, plus any remaining shares available to grant or that are later forfeited or expire under the 2003 Plan, to be made available to be issued as stock option grants, stock appreciation rights or restricted stock awards. On May 16, 2013, the Company’s stockholders approved the First Amendment to the 2009 Plan to increase the number of shares of common stock reserved for stock option grants and restricted stock awards thereunder to 1,500,000.

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Stock Options:

The Plans permit the grant of stock options to directors, officers and employees of the Holding Company and CFBank. Option awards are granted with an exercise price equal to the market price of the Company's common stock on the date of grant, generally have vesting periods ranging from one to three years, and are exercisable for ten years from the date of grant. Unvested stock options immediately vest upon a change of control.

The fair value of each option award is estimated on the date of grant using a closed form option valuation (Black-Scholes) model that uses the assumptions noted in the table below. Expected volatilities are based on historical volatilities of the Company's common stock. The Company uses historical data to estimate option exercise and post-vesting termination behavior. Employee and management options are tracked separately. The expected term of options granted is based on historical data and represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of the grant.

There were no options granted or exercised during the three and nine months ended September 30, 2016 and September 30, 2015 (unaudited).

A summary of stock option activity in the Plans for the nine months ended September 30, 2016 follows (unaudited):

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Intrinsic Value
Outstanding at beginning of year	566,696	$ 1.48		
Granted	-	-		
Exercised	-	-		
Expired	-	-		
Cancelled or Forfeited	(23,950)	2.01		
Outstanding at end of period	542,746	$ 1.46	6.7	$ -
Expected to vest	85,669	$ 1.43	7.0	$ -
Exercisable at end of period	457,077	$ 1.46	6.6	$ -

During the nine months ended September 30, 2016, there were 23,950 stock options canceled or forfeited. During the nine months ended September 30, 2015, there were 7,867 stock options canceled or forfeited. Previously recognized expense associated with forfeited stock options was reversed.

As of September 30, 2016, there was $1 of total unrecognized compensation cost related to nonvested stock options granted under the Plans. The cost is expected to be recognized over a weighted-average period of 0.1 years. Substantially all of the 85,669 nonvested stock options at September 30, 2016 are expected to vest.

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Restricted Stock Awards:

The Plans permit the grant of restricted stock awards to directors, officers and employees. Compensation is recognized over the vesting period of the awards based on the fair value of the stock at grant date. The fair value of the stock is determined using the closing share price on the date of grant and shares generally have vesting periods of one to three years. There were no shares of restricted stock issued during the three and nine months ended September 30, 2016 and 2015 (unaudited).

A summary of changes in the Company's nonvested restricted shares for the year follows (unaudited):

Nonvested Shares	Shares	Weighted Average Grant-Date Fair Value
Nonvested at January 1, 2016	200,500	$ 1.37
Granted	-	-
Vested	-	-
Forfeited	-	-
Nonvested at September 30, 2016	200,500	$ 1.37

As of September 30, 2016 and 2015, the unrecognized compensation cost related to nonvested restricted stock awards granted under the Plans was $191 and $0, respectively. There were no shares of restricted stock forfeited during the three and nine months ended September 30, 2016 and 2015. Also, there were no shares that vested during the three and nine months ended September 30, 2016 and 2015.

There were 831,792 shares remaining available for stock option grants and restricted stock awards under the 2009 Plan at September 30, 2016.

NOTE 8 – REGULATORY CAPITAL MATTERS

CFBank is subject to regulatory capital requirements administered by federal banking agencies. Prompt corrective action regulations involve quantitative measures of assets, liabilities, and certain off balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action.

Prompt corrective action regulations provide five classifications for banking organizations: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If a banking organization is classified as adequately capitalized, regulatory approval is required to accept brokered deposits. If a banking organization is classified as undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required.

In July 2013, the Holding Company’s primary federal regulator, the FRB, published final rules (the “Basel III Capital Rules”) establishing a new comprehensive capital framework for U.S. banking organizations. The rules implement the Basel Committee's December 2010 framework known as “Basel III” for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. The Basel III Capital Rules provide higher capital requirements and more restrictive leverage and liquidity ratios than those previously in place. In addition, in order to avoid limitations on capital distributions, such as dividend payments and certain bonus payments to executive officers, the Basel III Capital Rules require insured financial institutions to hold a capital conservation buffer of common equity tier 1 capital above the minimum risk-based capital requirements. The capital conservation buffer will be phased in over time, becoming effective on January 1, 2019, and will consist of an additional amount of common equity equal to 2.5% of risk-weighted assets. The Basel III Capital Rules revise the regulatory agencies' prompt corrective action framework by incorporating the new regulatory capital minimums and updating the definition of common equity. The Basel III Capital Rules became effective for CFBank on January 1, 2015, and will be fully phased in by January 1, 2019. Quantitative measures established by the Basel III Capital Rules to ensure capital adequacy require the maintenance of minimum amounts and ratios of Common Equity Tier 1 capital, Tier 1 capital and Total capital, as defined in the regulations, to risk-weighted assets, and of Tier 1 capital to adjusted

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quarterly average assets (“Leverage Ratio”). CFBank’s implementation of the new rules on January 1, 2015 did not have a material impact on our capital needs or classifications.

When fully phased in on January 1, 2019, the Basel III Capital Rules will require CFBank to maintain: 1) a minimum ratio of Common Equity Tier 1 capital to risk-weighted assets of 4.5%, plus a 2.5% “capital conservation buffer” (resulting in a minimum ratio of Common Equity Tier 1 capital to risk-weighted assets of 7.0% upon full implementation); 2) a minimum ratio of Tier 1 capital to risk-weighted assets of 6.0%, plus the capital conservation buffer (resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation); 3) a minimum ratio of Total capital to risk-weighted assets of 8.0%, plus the capital conservation buffer (resulting in a minimum Total capital ratio of 10.5% upon full implementation); and 4) a minimum Leverage Ratio of 4.0%.

The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level and will be phased in over a four-year period increasing by increments of that amount on each subsequent January 1 until it reaches 2.5% on January 1, 2019. The capital conservation buffer is designed to absorb losses during periods of economic stress. Failure to maintain the minimum Common Equity Tier 1 capital ratio plus the capital conservation buffer will result in potential restrictions on a banking institution’s ability to pay dividends, repurchase stock and/or pay discretionary compensation to its employees.

The CFBank Order previously required CFBank to maintain an 8% Tier 1 (Core) Capital to adjusted total assets and 12% Total Capital to risk weighted assets. Although the CFBank Order was terminated by the OCC effective January 23, 2014, CFBank remained subject to the heightened capital requirements imposed by the OCC and was required to maintain an 8% Tier 1 (core) Capital ratio to adjusted total assets and 12% Total Capital to risk weighted assets, until December 23, 2015. CFBank met these heightened capital requirements imposed by the OCC for all applicable periods. See Note 2-Regulatory Order Considerations for additional information.

The following tables present actual and required capital ratios as of September 30, 2016 and December 31, 2015 for CFBank under the Basel III Capital Rules. The minimum required capital amounts presented include the minimum required capital levels as of September 30, 2016, based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered well capitalized are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

	Actual		Minimum Capital Required-Basel III Phase-In Schedule		Minimum Capital Required-Basel III Fully Phased-In		To Be Well Capitalized Under Applicable Regulatory Capital Standards	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio

September 30, 2016 (unaudited)								
Total Capital to risk weighted assets	$ 43,557	13.11%	$ 28,676	8.63%	$ 34,889	10.50%	$ 33,228	10.00%
Tier 1 (Core) Capital to risk weighted assets	39,369	11.85%	22,030	6.63%	28,244	8.50%	26,582	8.00%
Common equity tier 1 capital to risk-weighted assets	39,369	11.85%	17,046	5.13%	23,260	7.00%	21,598	6.50%
Tier 1 (Core) Capital to adjusted total assets (Leverage ratio)	39,369	10.28%	15,313	4.00%	15,313	4.00%	19,141	5.00%

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	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Applicable Regulatory Capital Standards		Required Pursuant to OCC Commitment (1)	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31,2015								
Total Capital to risk weighted assets	$ 41,528	13.67%	$ 24,310	8.00%	$ 30,388	10.00%	$ N/A	N/A
Tier 1 (Core) Capital to risk weighted assets	37,694	12.40%	18,233	6.00%	24,310	8.00%	N/A	N/A
Common equity tier 1 capital to risk-weighted assets	37,694	12.40%	13,675	4.50%	19,752	6.50%	N/A	N/A
Tier 1 (Core) Capital to adjusted total assets	37,694	11.12%	13,557	4.00%	16,946	5.00%	N/A	N/A

(1) The heightened capital requirements were applicable to CFBank until December 23, 2015, under the CFBank Order and the subsequent commitments made by CFBank to the OCC. See Note 2-Regulatory Order Considerations for additional information.

The Qualified Thrift Lender test requires CFBank to maintain at least 65% of assets in housing related finance and other specified areas. If this test is not met, limits are placed on growth, branching, new investments, FHLB advances and dividends. Management believes that this test was met by CFBank at September 30, 2016 and December 31, 2015.

CFBank converted from a mutual to a stock institution in 1998, and a "liquidation account" was established in the amount of $14,300, which was the net worth reported in the conversion prospectus. The liquidation account represents a calculated amount for the purposes described below, and it does not represent actual funds included in the consolidated financial statements of the Company. Eligible depositors who have maintained their accounts, less annual reductions to the extent they have reduced their deposits, would receive a distribution from this account if CFBank liquidated and its assets exceeded its liabilities. Dividends may not reduce CFBank's stockholder's equity

below the required liquidation account balance.

Dividend Restrictions:

The Holding Company's principal source of funds for dividend payments is dividends received from CFBank. Banking regulations limit the amount of dividends that may be paid without prior approval of regulatory agencies. Under these regulations, the amount of dividends that may be paid in any calendar year is limited to the current year's net profits, combined with the retained net profits of the preceding two years, subject to the capital requirements described above. Any future dividend payments by CFBank to the Holding Company would be based on future earnings and, if necessary, regulatory approval.

Prior to January 8, 2016, any dividends by the Holding Company on its common stock or Series B Preferred Stock, and any dividends or capital contributions by CFBank to the Holding Company, were also subject to prior regulatory approval pursuant to the Orders and the commitments made by the Holding Company and CFBank in connection with the release of the Orders. The Holding Company received prior approval from the FRB for the payment of quarterly cash dividends on its Series B Preferred Stock in each of the previous quarters commencing with the first dividend payment on July 15, 2014 through the dividend payment on January 15, 2016.

The Holding Company's ability to pay dividends on its stock is also conditioned upon the payment, on a current basis, of quarterly interest payments on the subordinated debentures underlying the Company's trust preferred securities. Additionally, so long as the Company's Series B Preferred Stock remains outstanding, the Holding Company will be prohibited from paying dividends (other than dividends payable solely in shares) on the Company's common stock for the then-current dividend period, unless full dividends on the Series B Preferred Stock have been paid or set aside for payment. Dividends on the Series B Preferred Stock are non-cumulative, which means that if for any reason we do not declare cash dividends on the Series B Preferred Stock for a quarterly dividend period

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we will have no obligation to pay any dividends for that period (i.e., the dividends will not accrue or cumulate), whether or not we declare dividends on the Series B Preferred Stock for any subsequent dividend period.

Additionally, CFBank does not intend to make distributions to the Holding Company that would result in a recapture of any portion of its thrift bad debt reserve as discussed in Note 10-Income Taxes.

NOTE 9 – DERIVATIVE INSTRUMENTS

Interest-rate swaps:

CFBank utilizes interest-rate swaps as part of its asset/liability management strategy to help manage its interest rate risk position, and does not use derivatives for trading purposes. The notional amount of the interest-rate swaps does not represent amounts exchanged by the parties. The amount exchanged is determined by reference to the notional amount and the other terms of the individual interest-rate swap agreements. CFBank was party to interest-rate swaps with a combined notional amount of $2,793 at September 30, 2016 and $2,877 at December 31, 2015.

The objective of the interest-rate swaps is to protect the related fixed-rate commercial real estate loans from changes in fair value due to changes in interest rates. CFBank has a program whereby it lends to its borrowers at a fixed rate with the loan agreement containing a two-way yield maintenance provision, which will be invoked in the event of prepayment of the loan, and is expected to exactly offset the fair value of unwinding the swap. The yield maintenance provision represents an embedded derivative which is bifurcated from the host loan contract and, as such, the swaps and embedded derivatives are not designated as hedges. Accordingly, both instruments are carried at fair value and changes in fair value are reported in current period earnings. CFBank currently does not have any derivatives designated as hedges.

Contingent Features:

The counterparty to CFBank's interest-rate swaps is exposed to credit risk whenever the interest-rate swaps are in a liability position. At September 30, 2016, CFBank had $714 in securities and cash pledged as collateral for these derivatives. Should the liability increase, beyond the collateral value, CFBank will be required to pledge additional collateral.

Additionally, CFBank's interest-rate swap instruments contain provisions that require CFBank to remain well capitalized under regulatory capital standards. The interest-rate swaps may be called by the counterparty if CFBank fails to maintain well-capitalized status under regulatory capital standards. As of September 30, 2016, CFBank was well-capitalized under regulatory capital standards.

Summary information about the derivative instruments is as follows:

	September 30, 2016	December 31, 2015

	(unaudited)	
Notional amount	$ 2,793	$ 2,877
Weighted average pay rate on interest-rate swaps	3.67%	3.67%
Weighted average receive rate on interest-rate swaps	0.58%	0.39%
Weighted average maturity (years)	3.2	4.0
Fair value of interest-rate swaps	$ (214)	$ (213)
Fair value of yield maintenance provisions	214	213

The fair value of the yield maintenance provisions and interest-rate swaps is recorded in other assets and other liabilities, respectively, in the consolidated balance sheet. Changes in the fair value of the yield maintenance provisions and interest-rate swaps are reported currently in earnings, as other noninterest income in the consolidated statements of operations. There were no net gains or losses recognized in earnings related to yield maintenance provisions and interest-rate swaps for the three and nine months ended September 30, 2016 or 2015.

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Mortgage banking derivatives:

Commitments to fund certain mortgage loans (interest rate locks) to be sold into the secondary market are considered derivatives. These mortgage banking derivatives are not designated in hedge relationships. The Company had approximately $7,385 and $1,560 of interest rate lock commitments related to residential mortgage loans at September 30, 2016 and December 31, 2015, respectively. The fair value of these mortgage banking derivatives was reflected by a derivative asset of $18 and $8 at September 30, 2016 and December 31, 2015, respectively, which was included in other assets in the consolidated balance sheet. Fair values were estimated based on anticipated gains on the sale of the underlying loans. Changes in the fair values of these mortgage banking derivatives are included in net gains on sales of loans.

NOTE 10 – INCOME TAXES

Our deferred tax assets are composed of U.S. net operating losses (“NOLs”), and other temporary book to tax differences. The Company recorded a deferred tax valuation allowance which reduced the Company’s deferred tax asset to zero beginning in 2009 and continuing up until the fourth quarter of 2015; the Company maintained this valuation allowance against the net deferred tax assets during this period based on its estimate of future reversal and utilization. As a result, there was no income tax benefit recorded during the first three quarters of 2015.

When determining the amount of deferred tax assets that are more-likely-than-not to be realized, and therefore recorded as a benefit, the Company conducts a regular assessment of all available information. This information includes, but is not limited to, taxable income in prior periods, projected future income and projected future reversals of deferred tax items. Based on these criteria, the Company determined as of December 31, 2015, in part because the Company had achieved seven consecutive quarters of pretax income, that it was no longer necessary to maintain a full valuation allowance against the entire net deferred tax asset. As a result, the valuation allowance on the deferred tax asset was reversed which resulted in a credit to income tax expense of $3,200 during the fourth quarter of 2015.

In 2012, The Company completed a recapitalization program through the sale of $22,500 in common stock which improved the capital levels of CFBank and provided working capital for the Holding Company. The result of the change in stock ownership associated with the stock offering was that the Company incurred an ownership change, within the guidelines of Section 382 of the Internal Revenue Code of 1986. At year-end 2015, the Company had net operating loss carryforwards of $25,166, which expire at various dates from 2024 to 2033, and had alternative minimum tax credit carryforwards of $105, which do not expire. As a result of the ownership change in connection with the 2012 stock offering, the Company's ability to utilize carryforwards that arose before the stock offering closed is limited to $163 per year. Due to this limitation, management determined it is more likely than not that $20,520 of net operating loss carryforwards will expire unutilized. As required by accounting standards, the Company reduced the carrying value of deferred tax assets, and the corresponding valuation allowance, by the $6,977 tax effect of this lost realizability.

Federal income tax laws provided additional deductions, totaling $2,250, for thrift bad debt reserves established before 1988. Accounting standards do not require a deferred tax liability to be recorded on this amount, which

otherwise would total $765 at year-end 2015. However, if CFBank were wholly or partially liquidated or otherwise ceases to be a bank, or if tax laws were to change, this amount would have to be recaptured and a tax liability recorded. Additionally, any distributions in excess of CFBank's current or accumulated earnings and profits would reduce amounts allocated to its bad debt reserve and create a tax liability for CFBank. The amount of additional taxable income created by such a distribution is an amount that, when reduced by the tax attributable to the income, is equal to the amount of the distribution. Thus, if CFBank makes a distribution that reduces the amount allocated to its bad debt reserve, then approximately one and one-half times the amount used would be includible in gross income for federal income tax purposes, assuming a 34% corporate income tax rate. CFBank does not intend to make distributions that would result in a recapture of any portion of its bad debt reserve.

At December 31, 2015, the Company had a deferred tax asset recorded in the amount of $3,300, after reversing the valuation allowance mentioned above. At September 30, 2016, the Company had a deferred tax asset recorded in the amount of $2,700. At September 30, 2016 and December 31, 2015, the Company had no unrecognized tax benefits recorded. The Company is subject to U.S. federal income tax and is no longer subject to federal examination for years prior to 2012.

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With the reversal of the deferred tax valuation allowance as of December 31, 2015, the Company is now recording income tax expense based on the federal statutory rate adjusted for the effect of bank owned life insurance and other miscellaneous items. The effective tax rate for the three and nine months ended September 30, 2016, was approximately 33.0% and 32.7%, respectively, which management believes is a reasonable estimate for the effective tax rate.

The following table summarizes the major components creating differences between income taxes at the federal statutory tax rate and the effective tax rate recorded in the consolidated statements of income for the three and nine months ended September 30, 2016 and 2015:

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
	(unaudited)		(unaudited)	
Statutory tax rate	34.0%	0.0%	34.0%	0.0%
Increase (decrease) resulting from:				
Tax exempt income on bank owned life insurance	(1.5)%	0.0%	(1.8)%	0.0%
Other, net	0.5%	0.0%	0.5%	0.0%
Effective tax rate	33.0%	0.0%	32.7%	0.0%

NOTE 11- ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table summarizes the changes within each classification of accumulated other comprehensive income, net of tax, for the three and nine months ended September 30, 2016 and 2015 and summarizes the significant amounts reclassified out of each component of accumulated other comprehensive income:

Changes in Accumulated Other Comprehensive Income by Component (1)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
	(unaudited)		(unaudited)	
	Unrealized Gains and Losses on Available-for-Sale Securities		Unrealized Gains and Losses on Available-for-Sale Securities	
Accumulated other comprehensive income (loss), beginning of period	$ 80	$ 74	$ (9)	$ 51
Other comprehensive gain (loss) before reclassifications	(23)	5	66	16
Less amount reclassified from accumulated other comprehensive loss (2)	-	-	-	12
Net current-period other comprehensive income (loss)	(23)	5	66	28
Accumulated other comprehensive income (loss), end of period	$ 57	$ 79	$ 57	$ 79

(1) All amounts are net of tax. Amounts in parentheses indicate a reduction of other comprehensive income.

(2) There were no amounts reclassified out of other comprehensive income for the three and nine months ended September 30, 2016. There was $12 reclassified out of other comprehensive income for the nine months ended September 30, 2015 due to an early redemption on a municipal security.

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NOTE 12- PREFERRED STOCK

Series B Preferred Stock:

Commencing in April 2014, the Company conducted a private placement of up to 480,000 shares of its 6.25% Non-Cumulative Convertible Perpetual Preferred Stock, Series B ("Series B Preferred Stock") for an offering price of $25.00 per share (the "Private Placement"). Pursuant to the Private Placement, the Company sold an aggregate of 480,000 shares of Series B Preferred Stock on May 12, 2014 and July 15, 2014, for an aggregate offering price of $12,000. The Series B Preferred Stock was sold by the Company with the assistance of McDonald Partners, LLC, as placement agent, on a best efforts basis. After payment of approximately $482 in placement fees to McDonald Partners, LLC and approximately $149 of other offering expenses, the Company's net proceeds from its sale of the 480,000 shares of Series B Preferred Stock in the Private Placement were approximately $11,369.

NOTE 13- COMMON STOCK WARRANTS

Series B Preferred Stock – Warrants:

For each share of Series B Preferred Stock issued by the Company in the Private Placement, the Company also issued, at no additional charge, a Warrant to purchase (i) 2.00 shares of common stock of the Company if the purchaser purchased less than $700 (28,000 shares) of Series B Preferred Stock in the Private Placement, or (ii) 3.25 shares of common stock if the purchaser purchased $700 (28,000 shares) or more of Series B Preferred Stock in the Private Placement. Warrants to purchase an aggregate of 1,152,125 shares of common stock were issued by the Company to the purchasers of the 480,000 shares of Series B Preferred Stock sold in the Private Placement. Subject to certain limitations, the Warrants are exercisable for a period of approximately five (5) years expiring on July 15, 2019, at a cash purchase price of $1.85 per share of common stock.

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FORWARD LOOKING STATEMENTS

Statements in this quarterly report that are not statements of historical fact are forward-looking statements which are made in good faith by us. Forward-looking statements include, but are not limited to: (1) projections of revenues, income or loss, earnings or loss per common share, capital structure and other financial items; (2) plans and objectives of the management or Boards of Directors of Central Federal Corporation (the "Holding Company") or CFBank (collectively referred to as the "Company"); (3) statements regarding future events, actions or economic performance; and (4) statements of assumptions underlying such statements. Words such as "estimate," "strategy," "may," "believe," "anticipate," "expect," "predict," "will," "intend," "plan," "targeted," and the negative of these terms, or similar expressions, are intended to identify forward-looking statements, but are not the exclusive means of identifying such statements. Various risks and uncertainties may cause actual results to differ materially from those indicated by our forward-looking statements. The following, among other factors, could cause such differences:

- changes in economic and political conditions could adversely affect our earnings through declines in deposits, loan demand, the ability of our customers to repay loans and the value of the collateral securing our loans;
- changes in interest rates that may reduce net interest margin and impact funding sources;
- the possibility that we will need to make increased provisions for loan losses;
- our ability to maintain sufficient liquidity to continue to fund our operations;
- our ability to reduce our level of nonperforming assets and the associated operating expenses;
- changes in market rates and prices, including real estate values, which may adversely impact the value of financial products including securities, loans and deposits;
- the possibility of other-than-temporary impairment of securities held in our securities portfolio;
- results of examinations of the Holding Company and CFBank by the regulators, including the possibility that the regulators may, among other things, require CFBank to increase its allowance for loan losses or write-down assets;
- our ability to continue to meet regulatory requirements and guidelines to which we are subject;
- our ability to generate profits in the future;
- our ability to raise additional capital if and when necessary in the future;
- changes in tax laws, rules and regulations;
- increases in deposit insurance rates or premiums;
- further legislative and regulatory changes which may increase compliance costs and burdens;
- unexpected losses of key management;
- various monetary and fiscal policies and regulations, including those determined by the Board of Governors of the Federal Reserve System (the "FRB"), the Federal Deposit Insurance Corporation (the "FDIC") and the Office of the Comptroller of the Currency (the "OCC");
- further increases in competition from other local and regional commercial banks, savings banks, credit unions and other non-bank financial institutions;
- our ability to grow our core businesses;
- our ability to effectively manage our growth;
- any failure, interruption or breach in security of our communications and information systems;

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- technological factors which may affect our operations, pricing, products and services;
- unanticipated litigation, claims or assessments; and
- Management's ability to manage these and other risks.

Forward-looking statements are not guarantees of performance or results. A forward-looking statement may include a statement of the assumptions or bases underlying the forward-looking statement. The Company believes it has chosen these assumptions or bases in good faith and that they are reasonable. We caution you, however, that assumptions or bases almost always vary from actual results, and the differences between assumptions or bases and actual results can be material. The forward-looking statements included in this report speak only as of the date of the report. We undertake no obligation to publicly release revisions to any forward-looking statements to reflect events or circumstances after the date of such statements, except to the extent required by law.

Our filings with the Securities and Exchange Commission (the "SEC") detail other risks, all of which are difficult to predict and many of which are beyond our control.

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Business Overview

The Holding Company is a savings and loan holding company incorporated in Delaware in 1998. Substantially all of our business is conducted through our principal subsidiary, CFBank, a federally chartered savings association formed in Ohio in 1892.

CFBank is a community-oriented financial institution offering a variety of financial services to meet the needs of the communities we serve. Our business model emphasizes personalized service, clients’ access to decision makers, solution-driven lending and quick execution, efficient use of technology and the convenience of online internet banking, mobile banking, remote deposit and corporate cash management. We attract retail and business deposits from the general public and use the deposits, together with borrowings and other funds, primarily to originate commercial and commercial real estate loans, single-family and multi-family residential mortgage loans and home equity lines of credit. The majority of our customers are small businesses, small business owners and consumers.

Our principal market area for loans and deposits includes the following Ohio counties: Summit County through our office in Fairlawn, Ohio; Franklin County through our office in Worthington, Ohio; Columbiana County through our offices in Calcutta and Wellsville, Ohio; and Cuyahoga County, through our loan production office in Woodmere, Ohio. We originate commercial and residential real estate loans and business loans primarily throughout Ohio. Most of our deposits and loans come from our market area. Because of CFBank’s concentration of business activities in Ohio, the Company’s financial condition and results of operations depend upon economic conditions in Ohio.

General

Our net income is dependent primarily on net interest income, which is the difference between the interest income earned on loans and securities and our cost of funds, consisting of interest paid on deposits and borrowed funds. Net interest income is affected by regulatory, economic and competitive factors that influence interest rates, loan demand, the level of nonperforming assets and deposit flows.

Net income is also affected by, among other things, provisions for loan losses, loan fee income, service charges, gains on loan sales, operating expenses, and taxes. Operating expenses principally consist of employee compensation and benefits, occupancy, FDIC insurance premiums and other general and administrative expenses. In general, results of operations are significantly affected by general economic and competitive conditions, changes in market interest rates and real estate values, government policies and actions of regulatory authorities. Our regulators have extensive discretion in their supervisory and enforcement activities, including the authority to impose restrictions on our operations, to classify our assets and require us to increase the level of our allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material impact on our business, financial condition, results of operations and/or cash flows.

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). The Dodd-Frank Act included numerous provisions designed to strengthen the financial industry, enhance consumer protection, expand disclosures and provide for transparency. Some of these provisions included changes to FDIC insurance coverage, which included a permanent increase in the coverage to $250,000 per depositor. Additional provisions created a Bureau of Consumer Financial Protection, which is authorized to write rules

on all consumer financial products. Still other provisions created a Financial Stability Oversight Council, which is not only empowered to determine the entities that are systemically significant and therefore require more stringent regulations, but which is also charged with reviewing, and, when appropriate, submitting comments to the SEC and Financial Accounting Standards Board (FASB) with respect to existing or proposed accounting principles, standards or procedures. The aforementioned are only a few of the numerous provisions included in the Dodd-Frank Act. The overall impact of the entire Dodd-Frank Act will not be known until full implementation is completed, but the possibility of significant additional compliance costs exists, and the Dodd-Frank Act consequently may have a material adverse impact on our operations.

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Cease and Desist Orders

On May 25, 2011, the Holding Company and CFBank each consented to the issuance of an Order to Cease and Desist (the "Holding Company Order" and the "CFBank Order", respectively, and collectively, the "Orders") by the Office of Thrift Supervision (the "OTS"), the primary regulator of the Holding Company and CFBank at the time the Orders were issued. In July 2011, in accordance with the Dodd-Frank Act, the FRB replaced the OTS as the primary regulator of the Holding Company and the OCC replaced the OTS as the primary regulator of CFBank.

Effective as of January 23, 2014, the OCC released and terminated the CFBank Order based upon the improved capital position of CFBank, among other factors. Following the release of the CFBank Order, CFBank was required to continue to maintain a minimum Tier 1 Leverage Capital Ratio of 8% and a Total Risk-based Capital to Risk-Weighted Assets ratio of 12% until December 23, 2015. In addition, in connection with the release and termination of the CFBank Order, CFBank made certain commitments to the OCC to continue to adhere to certain prudent practices, including, without limitation, maintaining a written program to continue to improve CFBank's credit underwriting and administrative process; take actions to protect its interest in criticized assets as identified by CFBank, the OCC examiners or its external loan review process and implement its written program to effectively identify, monitor, control and continue to reduce the level of credit risk to CFBank; review and monitor progress against such plan with the Board of Directors and continue CFBank's aggressive workout efforts and individualized workout plans on all criticized assets greater than $250,000. The foregoing commitments remained in place until December 23, 2015.

On May 15, 2014, the FRB announced the termination of the Holding Company Order, effective as of May 9, 2014. Following the termination of the Holding Company Order, the Holding Company was required to continue to adhere to certain requirements and restrictions based on commitments made to the FRB in connection with the termination of the Holding Company Order. These commitments required the Holding Company, among other things, to continue to implement certain actions in accordance with the capital plan previously submitted to the FRB; not declare or pay dividends on its stock, purchase or redeem its stock, or accept dividends or other capital distributions from CFBank without the prior written approval of the FRB; not incur, increase or guarantee any debt without the prior written consent of the FRB; and provide prior written notice to the FRB with respect to certain changes in directors and senior executive officers. The foregoing commitments remained in place until January 8, 2016.

The significant directives contained in the Orders and the commitments made by CFBank and the Holding Company in connection with the release and termination of the Orders provided challenges for the operation of our business and our ability to effectively compete in our markets over the past several years. In addition, the Orders and our commitments to the regulators, as described above, required that we obtain approval from our regulators for any deviations from our business plan, which limited our flexibility to make changes to the scope of our business activities. We also incurred significant additional regulatory compliance expense in connection with the Orders and our regulatory commitments. Although we are no longer subject to the Orders or the regulatory commitments made following the release of the Orders, we remain subject to extensive supervision and regulation by our regulators and it is possible that regulatory compliance expenses could continue to have a material adverse impact on us in the future.

Dividend Restrictions

Banking regulations limit the amount of dividends that may be paid without prior approval of regulatory agencies. Generally, CFBank may pay a dividend to the Holding Company without prior approval as long as the dividend does not exceed the total of the current calendar year-to-date earnings plus any earnings from the previous two years not already paid out in dividends, and as long as CFBank remains well capitalized after the dividend payment. Future dividend payments by CFBank to the Holding Company would be based on future earnings and, if necessary, regulatory approval. Management believes that the Holding Company has adequate operating capital for the foreseeable future. The Holding Company had $2.7 million in cash and cash equivalents at September 30, 2016.

Management's discussion and analysis represents a review of our consolidated financial condition and results of operations for the periods presented. This review should be read in conjunction with our consolidated financial statements and related notes.

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Financial Condition

General. Assets totaled $408.4 million at September 30, 2016 and increased $57.1 million, or 16.3%, from $351.3 million at December 31, 2015. The increase was primarily due to a $32.3 million increase in net loan balances and a $26.4 million increase in cash and cash equivalents.

Cash and cash equivalents. Cash and cash equivalents totaled $52.3 million at September 30, 2016 and increased $26.4 million, or 102.0%, from $25.9 million at December 31, 2015. The increase in cash and cash equivalents was a result of management's efforts to increase deposit activity in order to fund anticipated loan growth and to improve the loan to deposit ratio.

Securities. Securities available for sale totaled $9.2 million at September 30, 2016 and decreased $142,000, or 1.5%, from $9.4 million at December 31, 2015.

Loans and Leases. Net loans totaled $329.4 million at September 30, 2016 and increased $32.3 million, or 10.9%, from $297.1 million at December 31, 2015. The increase was primarily due to a $26.4 million increase in commercial loan balances, a $6.0 million increase in single-family residential loans balances, a $4.2 million increase in commercial real estate loan balances, and a $3.5 million increase in multi-family loan balances, partially offset by a $3.4 million decrease in construction loan balances, and a $4.1 million decrease in total consumer loan balances. The increase in commercial loan balances, single-family residential, commercial real estate and multi-family loans was due to increased sales activity. The decrease in construction loan balances was primarily attributed to the completion of real estate construction projects.

CFBank has participated in a Mortgage Purchase Program with Northpointe Bank (Northpointe), a Michigan banking corporation, since December 2012. Pursuant to the terms of a participation agreement, CFBank purchases participation interests in loans made by Northpointe related to fully underwritten and pre-sold mortgage loans originated by various prescreened mortgage brokers located throughout the U.S. The underlying loans are individually (MERS) registered loans which are held until funded by the end investor. The mortgage loan investors include Fannie Mae and Freddie Mac, and other major financial institutions such as Wells Fargo Bank. This process on average takes approximately 14 days. Given the short-term holding period of the underlying loans, common credit risks (such as past due, impairment and TDR, nonperforming, and nonaccrual classification) are substantially reduced. Therefore, no allowance is allocated by CFBank to these loans. These loans are 100% risk rated for CFBank capital adequacy purposes. Under the participation agreement, CFBank agrees to purchase a 95% ownership/participation interest in each of the aforementioned loans, and Northpointe maintains a 5% ownership interest in each loan it participates. During the three and nine months ended September 30, 2016, loan origination activity totaled $206.6 million and $601.0 million, respectively, and payoffs for the same period totaled $207.8 million and $601.4 million, respectively. At September 30, 2016 and December 31, 2015, CFBank held $43.1 million and $43.5 million, respectively, of such loans which are included in single-family residential loan totals.

Allowance for loan and lease losses (ALLL). The ALLL totaled $6.9 million at September 30, 2016 and increased $273,000, or 4.1%, from $6.6 million at December 31, 2015. The increase in the ALLL was primarily due to an increase in overall loans balances and net recoveries for the quarter, which was partially offset by continued improvement in credit quality as certain historical loss rates continued to decline and total criticized assets

decreased. The ratio of the ALLL to total loans was 2.05% at September 30, 2016 compared to 2.18% at December 31, 2015. In addition, the ratio of the ALLL to nonperforming loans was 794.1% at September 30, 2016, compared to 464.6% at December 31, 2015.

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The ALLL is a valuation allowance for probable incurred credit losses. The ALLL methodology is designed as part of a thorough process that incorporates management's current judgments about the credit quality of the loan portfolio into a determination of the ALLL in accordance with generally accepted accounting principles and supervisory guidance. Management analyzes the adequacy of the ALLL quarterly through reviews of the loan portfolio, including the nature and volume of the loan portfolio and segments of the portfolio; industry and loan concentrations; historical loss experience; delinquency statistics and the level of nonperforming loans; specific problem loans; the ability of borrowers to meet loan terms; an evaluation of collateral securing loans and the market for various types of collateral; various collection strategies; current economic conditions, trends and outlook; and other factors that warrant recognition in providing for an adequate ALLL. Based on the variables involved and the significant judgments management must make about outcomes that are uncertain, the determination of the ALLL is considered to be a critical accounting policy. See the section titled "Critical Accounting Policies" for additional discussion.

The ALLL consists of specific and general components. The specific component relates to loans that are individually classified as impaired. A loan is impaired when, based on current information and events, it is probable that CFBank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans of all classes within the commercial, commercial real estate and multi-family residential loan segments, regardless of size, and loans of all other classes over $250,000, are individually evaluated for impairment when they are 90 days past due, or earlier than 90 days past due if information regarding the payment capacity of the borrower indicates that payment in full according to the loan terms is doubtful. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate, or at the fair value of collateral, less costs to sell, if repayment is expected solely from the collateral. Large groups of smaller balance loans, such as consumer and single-family residential real estate loans, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures. Loans within any class for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (TDRs) and are classified as impaired. See Notes 1 and 4 to our consolidated financial statements included in this Quarterly Report on Form 10-Q for additional information regarding the ALLL.

Individually evaluated impaired loans totaled $4.0 million at September 30, 2016, and decreased $1.8 million, or 31.0%, from $5.8 million at December 31, 2015. The decrease was primarily due to loan repayments. The amount of the ALLL specifically allocated to individually impaired loans totaled $25,000 at September 30, 2016 and $20,000 at December 31, 2015. The increase in the ALLL specifically allocated to impaired loans was primarily due to management's updated analysis.

The specific reserve on impaired loans is based on management's estimate of the present value of estimated future cash flows using the loan's effective rate or the fair value of collateral, if repayment is expected solely from the collateral. On at least a quarterly basis, management reviews each impaired loan to determine whether it should have a specific reserve or partial charge-off. Management relies on appraisals or internal evaluations to help make this determination. Determination of whether to use an updated appraisal or internal evaluation is based on factors including, but not limited to, the age of the loan and the most recent appraisal, condition of the property and whether we expect the collateral to go through the foreclosure or liquidation process. Management considers the need for a downward adjustment to the valuation based on current market conditions and on management's analysis, judgment and experience. The amount ultimately charged-off for these loans may be different from the specific reserve, as the

ultimate liquidation of the collateral and/or projected cash flows may be different from management's estimates.

Nonperforming loans, which are nonaccrual loans and loans at least 90 days past due but still accruing interest totaled $868,000 million at September 30, 2016, and decreased $557,000, or 39.1%, from $1.4 million at December 31, 2015. The ratio of nonperforming loans to total loans was 0.26% at September 30, 2016 compared to 0.47% at December 31, 2015.

Nonaccrual loans include some loans that were modified and identified as TDRs and are not performing. TDRs included in nonaccrual loans totaled $318,000 at September 30, 2016 and $356,000 at December 31, 2015. The decrease in TDRs included in nonaccrual loans was primarily due to loan repayments.

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Nonaccrual loans at September 30, 2016 and December 31, 2015 do not include $3.3 million and $4.9 million, respectively, in TDRs where customers have established a sustained period of repayment performance, generally six months, loans are current according to their modified terms and repayment of the remaining contractual payments is expected. These loans are included in total impaired loans. See Note 1 and 4 to the consolidated financial statements included in this Quarterly Report on Form 10-Q for additional information regarding impaired loans and nonperforming loans.

The general reserve component of our ALLL covers non-impaired loans of all classes and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by loan class and is based on the actual loss history experienced by CFBank over a three-year period. The general component is calculated based on CFBank's loan balances and actual historical three-year historical loss rates. For loans with little or no actual loss experience, industry estimates are used based on loan segment. This actual loss experience is supplemented with other economic and judgmental factors based on the risks present for each loan class. These economic and judgmental factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations.

Management's loan review process is an integral part of identifying problem loans and determining the ALLL. We maintain an internal credit rating system and loan review procedures specifically developed as the primary credit quality indicator to monitor credit risk for commercial, commercial real estate and multi-family residential real estate loans. We analyze these loans individually and categorize loans into risk categories based on relevant information about the ability of borrowers to service their debt, such as current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. Credit reviews for these loan types are performed at least annually, and more often for loans with higher credit risk. Loan officers maintain close contact with borrowers between reviews. Adjustments to loan risk ratings are based on the reviews and at any time information is received that may affect risk ratings. Additionally, an independent third party review of commercial, commercial real estate and multi-family residential loans is performed at least annually. Management uses the results of these reviews to help determine the effectiveness of the existing policies and procedures and to provide an independent assessment of our internal loan risk rating system.

We have incorporated the regulatory asset classifications as a part of our credit monitoring and internal loan risk rating system. In accordance with regulations, problem loans are classified as special mention, substandard, doubtful or loss, and the classifications are subject to review by the regulators. Assets designated as special mention are considered criticized assets. Assets designated as substandard, doubtful or loss are considered classified assets. See Note 4 to our consolidated financial statements included in this Quarterly Report on Form 10-Q for additional information regarding descriptions of the regulatory asset classifications.

The level of total criticized and classified loans decreased by $2.4 million, or 18.4%, during the nine months ended September 30, 2016, mostly due to the repayment from a commercial loan relationship, which consisted of three commercial loans and one commercial real estate loan. Loans designated as special mention decreased $3.0 million, or 41.1%, and totaled $4.3 million at September 30, 2016, compared to $7.4 million at December 31, 2015. Loans

classified as substandard increased $639,000, or 11.4%, and totaled $6.3 million at September 30, 2016, compared to $5.6 million at December 31, 2015. No loans were classified as doubtful at September 30, 2016 and December 31, 2015. See Note 4 to our consolidated financial statements included in this Quarterly Report on Form 10-Q for additional information regarding risk classification of loans.

In addition to credit monitoring through our internal loan risk rating system, we also monitor past due information for all loan segments. Loans that are not rated under our internal credit rating system include groups of homogenous loans, such as single-family residential real estate loans and consumer loans. The primary credit indicator for these groups of homogenous loans is past due information.

Total past due loans increased $810,000, or 58.3%, and totaled $2.2 million at September 30, 2016, compared to $1.4 million at December 31, 2015. The increase in past due loans was primarily due to residential loans. Past due loans totaled 0.7% of the loan portfolio at September 30, 2016, compared to 0.5% at December 31, 2015. See Note 4 to our consolidated financial statements included in this Quarterly Report on Form 10-Q for additional information regarding loan delinquencies.

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All lending activity involves risk of loss. Certain types of loans, such as option adjustable-rate mortgage (ARM) products, junior lien mortgages, high loan-to-value ratio mortgages, interest only loans, subprime loans and loans with initial teaser rates, can have a greater risk of non-collection than other loans. CFBank has not engaged in subprime lending, used option ARM products or made loans with initial teaser rates.

Loans that contain interest only payments may present a higher risk than those loans with an amortizing payment that includes periodic principal reductions. Interest only loans are primarily commercial lines of credit secured by business assets and inventory, and consumer home equity lines of credit secured by the borrower's primary residence. Due to the fluctuations in business assets and inventory of our commercial borrowers, CFBank has increased risk due to a potential decline in collateral values without a corresponding decrease in the outstanding principal. Interest only commercial lines of credit totaled $19.0 million, or 27.1%, of the commercial portfolio at September 30, 2016 compared to $16.5 million, or 37.7%, at December 31, 2015. Given the recessionary effects of the economy in the past several years, the collateral that secures the home equity lines of credit may have experienced a deterioration in value since the loan was originated, increasing the risk to CFBank. Interest only home equity lines of credit totaled $20.8 million, or 90.1%, of the total home equity lines of credit at September 30, 2016 compared to $19.2 million, or 85.8%, at December 31, 2015.

We believe the ALLL is adequate to absorb probable incurred credit losses in the loan portfolio as of September 30, 2016; however, future additions to the allowance may be necessary based on factors including, but not limited to, deterioration in client business performance, recessionary economic conditions, declines in borrowers' cash flows and market conditions which result in lower real estate values. Additionally, various regulatory agencies, as an integral part of their examination process, periodically review the ALLL. Such agencies may require additional provisions for loan losses based on judgments and estimates that differ from those used by management, or on information available at the time of their review. Management continues to diligently monitor credit quality in the existing portfolio and analyze potential loan opportunities carefully in order to manage credit risk. An increase in loan losses could occur if economic conditions and factors which affect credit quality, real estate values and general business conditions worsen or do not improve.

Foreclosed assets. Foreclosed assets totaled $0 at September 30, 2016 compared to $1.6 million at December 31, 2015. Foreclosed assets at December 31, 2015 consisted of one multi-family property that was transferred into REO at fair value at the time of transfer in 2013. This property was sold during the second quarter of 2016.

Deposits. Deposits totaled $345.9 million at September 30, 2016 and increased $55.4 million, or 19.1%, from $290.5 million at December 31, 2015. The increase was primarily attributed to a $30.3 million increase in certificates of deposits, a $13.1 million increase in money market account balances, and a $9.8 million increase in checking account balances. The majority of the deposit increase was a result of management's focused sales and marketing efforts to grow deposits to fund anticipated loan growth and improve the loan to deposit ratio.

CFBank is a participant in the Certificate of Deposit Account Registry Service® (CDARS) program, a network of banks that allows us to provide our customers with FDIC insurance coverage on certificate of deposit account balances up to $50 million. CDARS balances are considered brokered deposits by regulation. Brokered deposits, including CDARS balances, totaled $30.7 million at September 30, 2016, and increased $8.7 million, or 39.2%, from $22.1 million at December 31, 2015.

FHLB advances. FHLB advances totaled $15.5 million at September 30, 2016 and increased $1.0 million, or 6.9%, compared to $14.5 million at December 31, 2015. The increase was primarily due to FHLB fixed-rate advances.

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Subordinated debentures. Subordinated debentures totaled $5.2 million at both September 30, 2016 and December 31, 2015. These debentures were issued in 2003 in exchange for the proceeds of a $5.0 million trust preferred securities offering issued by a trust formed by the Holding Company. The terms of the subordinated debentures allow for the Holding Company to defer interest payments for a period not to exceed five years. The Holding Company's Board of Directors elected to defer interest payments on the subordinated debentures from time to time beginning in December 2010 in order to preserve cash at the Holding Company. However, in June 2014, the Holding Company paid all deferred and current interest payments in the amount of $293, with the prior approval of the FRB. The Holding Company subsequently paid the interest current on the subordinated debentures on a quarterly basis through December 31, 2015, after receiving the prior approval or written non-objection of the FRB to make such payments as required by the terms of the Holding Company Order and the subsequent commitments made by the Company following the termination of the Holding Company Order. Effective as of January 8, 2016, the Holding Company is no longer required to obtain the prior approval or non-objection of the FRB in order to pay current quarterly interest on the subordinated debentures. The Company paid the interest current for the quarter ended September 30, 2016.

Stockholders' equity. Stockholders' equity totaled $39.1 million at September 30, 2016, an increase of $809,000, or 2.1%, from $38.3 million at December 31, 2015. The increase in total stockholders' equity was primarily attributed to net income, which was partially offset by the dividends paid on the Company's Series B Preferred Stock during the nine months ended September 30, 2016.

In May 2016, the Company announced that its Board of Directors adopted a stock repurchase program pursuant to which the Company may repurchase up to 3% of the Company's common stock over the subsequent six-month period. The Board of Directors subsequently approved the continuation of this repurchase program for an additional six-month period commencing November 10, 2016. Any purchases under the repurchase program will be made from time to time in the open market in accordance with applicable federal and state securities laws and regulations. The timing and amount of any stock repurchases will be determined by the Company's management based on its evaluation of market conditions, regulatory requirements and other corporate considerations. Since the commencement of the program, the Company has repurchased 21,300 common shares for an aggregate purchase price of $30,000 as of September 30, 2016. All repurchased shares are held by the Company as treasury stock.

Management continues to proactively monitor capital levels and ratios in its on-going capital planning process. CFBank has leveraged its capital to support balance sheet growth and drive increased net interest income. Management remains focused on growing capital though improving results from operations; however, should the need arise, CFBank has additional sources of capital and alternatives it could utilize.

Currently, the Holding Company has excess cash to cover its expenses for the foreseeable future, and could inject capital into CFBank if necessary. Also, CFBank has the flexibility to manage its balance sheet size as a result of the short duration of the assets as discussed with the Northpointe mortgage program, as well as to deploy those assets into higher earning assets to improve net interest income as the opportunity presents itself.

Comparison of the Results of Operations for the Three Months Ended September 30, 2016 and 2015

General. Net income for the three months ended September 30, 2016 totaled $505,000 and increased $175,000, or 53.0%, compared to net income of $330,000 for the three months ended September 30, 2015. The increase in net income was due to a $482,000 increase in net interest income, a $30,000 decrease in provision expense and a $26,000 increase in noninterest income, partially offset by a $249,000 increase in income tax expense and a $114,000 increase in noninterest expense.

The Company reversed its deferred tax valuation allowance during the fourth quarter of 2015, and thus has recorded income tax expense in 2016. On a comparable basis, income before income tax expense was $754,000 for the three months ended September 30, 2016 and increased $424,000, or 128.5%, compared to $330,000 for the three months ended September 30, 2015.

Net income attributable to common stockholders for the three months ended September 30, 2016, totaled $291,000, or $0.02 per diluted common share, and increased $175,000, or 150.9%, compared to net income attributable to common stockholders of $116,000, or $0.01 per diluted common share, for the three months ended September 30, 2015. For the three months ended September 30, 2016 and 2015, preferred dividends on the Company's Series B Preferred Stock and accretion of discount reduced net income attributable to common stockholders by $214,000 for each period.

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Net interest income. Net interest income is a significant component of net income, and consists of the difference between interest income generated on interest-earning assets and interest expense incurred on interest-bearing liabilities. Net interest income is primarily affected by the volumes, interest rates and composition of interest-earning assets and interest-bearing liabilities. The tables below titled "Average Balances, Interest Rates and Yields" and "Rate/Volume Analysis of Net Interest Income" provide important information on factors impacting net interest income and should be read in conjunction with this discussion of net interest income.

Net interest income totaled $2.9 million for the quarter ended September 30, 2016 and increased $482,000, or 19.6%, compared to $2.5 million for the quarter ended September 30, 2015. The increase in net interest income was primarily due to a $595,000, or 19.0%, increase in interest income, partially offset by a $113,000, or 16.5%, increase in interest expense. The increase in interest income was primarily attributed to a $44.5 million, or 14.4%, increase in average interest-earning assets outstanding and a 16bps increase in average yield on interest-earning assets. The increase in interest expense was primarily attributed to a $31.1 million, or 11.7%, increase in average interest-bearing liabilities outstanding and a 5bps increase in the average cost of funds on interest-bearing liabilities. As a result, net interest margin of 3.32% for the quarter ended September 30, 2016 increased 15bps compared to the net interest margin of 3.17% for the quarter ended September 30, 2015.

Interest income totaled $3.7 million and increased $595,000, or 19.0%, for the quarter ended September 30, 2016, compared to $3.1 million for the quarter ended September 30, 2015. The increase in interest income was primarily due to a $47.0 million, or 17.0%, increase in average loans and loans held for sale balances from $276.3 million at September 30, 2015, to $323.3 million at September 30, 2016, coupled with an 8bps increase in the average yield on loans and loans held for sale.

Interest expense totaled $798,000 and increased $113,000, or 16.5%, for the quarter ended September 30, 2016, compared to $685,000 for the quarter ended September 30, 2015. The increase in interest expense resulted primarily from increased deposit costs due to a $28.8 million, or 11.7%, increase in average interest-bearing deposit balances, coupled with an increase in the cost of funds. The overall cost of funds on total interest-bearing liabilities increased 5bps to 108bps at September 30, 2016 compared to 103bps at September 30, 2015 primarily due to higher promotional rates paid to increase core deposit levels.

Provision for loan losses. The provision for loan losses totaled $20,000 for the quarter ended September 30, 2016 and decreased $30,000, or 60.0%, compared to $50,000 for the quarter ended September 30, 2015. The decrease in the provision for loan losses for the quarter ended September 30, 2016 was primarily due to a continued decrease in the majority of historical loss rates, favorable trends in certain qualitative factors and net recoveries for the quarter. Net recoveries for the quarter ended September 30, 2016 totaled $260,000 compared to net charge-offs of $8,000 for the quarter ended September 30, 2015. The ratio of the ALLL to nonperforming loans improved to 794.1% as of September 30, 2016.

The following table presents information regarding net charge-offs (recoveries) for the three months ended September 30, 2016 and 2015.

(unaudited)	For the three months ended September 30, 2016	2015
	(Dollars in thousands)	
Commercial	$ 5	$ -
Single-family residential real estate	(3)	9
Multi-family residential real estate	(143)	-
Commercial real estate	(100)	3
Home equity lines of credit	(20)	(4)
Other consumer loans	1	-
Total	$ (260)	$ 8

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Noninterest income. Noninterest income for the quarter ended September 30, 2016 totaled $350,000 and increased $26,000, or 8.0%, compared to $324,000 for the quarter ended September 30, 2015. The increase was primarily due to a $114,000 increase in service charges on deposit accounts, partially offset by a $70,000 decrease in other noninterest income and a $18,000 decrease in net gains on sales of loans. The increase in service charges on deposit accounts was related to increased pricing, increased deposit growth and activity and new account relationships. The decrease in other noninterest income was related to decreased activity related to the Company's joint ventures. The decrease in net gain on sales of loans was primarily due to lower sales activity.

Noninterest expense. Noninterest expense increased $114,000, or 4.8%, and totaled $2.5 million for the quarter ended September 30, 2016, compared to $2.4 million for the quarter ended September 30, 2015. The increase in noninterest expense during the three months ended September 30, 2016 was primarily due to a $116,000 increase in salaries and employee benefits expense and a $90,000 increase in professional fees, which was partially offset by a $72,000 decrease in FDIC premiums. The increase in salaries and employee benefits was due to an increase in personnel in commercial lending and operations to support revenue growth, infrastructure and risk management practices. The increase in professional fees was primarily due to increases in information technology consulting projects and legal expenses primarily related to our loan workout area, as we were able to successfully exit certain problem credits. The decrease in FDIC premiums was due to lower assessment factors charged based on CFBank's improved performance.

Income taxes. Income tax expense was $249,000 for the three months ended September 30, 2016, an increase of $249,000 compared to $0 for the three months ended September 30, 2015. As of September 30, 2015, the Company maintained a valuation allowance against the net deferred tax asset which reduced the deferred tax asset to zero; thus, no income tax expense was recorded for the quarter ended September 30, 2015. With the reversal of the deferred tax valuation allowance as of December 31, 2015, as discussed below, the Company is now recording income tax expense based on the federal statutory rate adjusted for the effect of bank owned life insurance and other miscellaneous items. The effective tax rate for the quarter ended September 30, 2016, was approximately 33.0% which management believes is a reasonable estimate for the effective tax rate.

Our deferred tax assets are composed of U.S. net operating losses ("NOLs"), and other temporary book to tax differences. The Company recorded a deferred tax valuation allowance which reduced the Company's deferred tax asset to zero beginning in 2009 and continuing up until the fourth quarter of 2015; the Company maintained this valuation allowance against the net deferred tax assets during this period based on its estimate of future reversal and utilization. As a result, there was no income tax benefit recorded during the first three quarters of 2015.

When determining the amount of deferred tax assets that are more-likely-than-not to be realized, and therefore recorded as a benefit, the Company conducts a regular assessment of all available information. This information includes, but is not limited to, taxable income in prior periods, projected future income and projected future reversals of deferred tax items. Based on these criteria, the Company determined as of December 31, 2015, in part because the Company had achieved seven consecutive quarters of pretax income, that it was no longer necessary to maintain a full valuation allowance against the entire net deferred tax asset. As a result, the valuation allowance on the deferred tax asset was reversed as of December 31, 2015 which resulted in a credit to income tax expense of $3.2 million. With the reversal of the deferred tax valuation allowance, the Company is now recording income tax expense based on the federal statutory rate adjusted for the effect of other items such as bank owned life insurance and other miscellaneous

items.

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Comparison of the Results of Operations for the Nine months Ended September 30, 2016 and 2015

General. Net income for the nine months ended September 30, 2016 totaled $1.2 million and increased $195,000, or 18.6%, compared to net income of $1.0 million for the nine months ended September 30, 2015. The increase in net income was due to a $1.1 million increase in net interest income, partially offset by a $603,000 increase in income tax expense, a $199,000 decrease in noninterest income, a $64,000 increase in noninterest expense and a $30,000 increase in provision expense.

The Company reversed its deferred tax valuation allowance during the fourth quarter of 2015, and thus has recorded income tax expense in 2016. On a comparable basis, income before income tax expense was $1.8 million for the nine months ended September 30, 2016 and increased $798,000, or 76.1%, compared to $1.0 million for the nine months ended September 30, 2015.

Net income attributable to common stockholders for the nine months ended September 30, 2016, totaled $600,000, or $0.04 per diluted common share, and increased $195,000, or 48.1%, compared to net income attributable to common stockholders of $405,000, or $0.03 per diluted common share, for the nine months ended September 30, 2015. For the nine months ended September 30, 2016 and 2015, preferred dividends on the Company's Series B Preferred Stock and accretion of discount reduced net income attributable to common stockholders by $643,000 for each period.

Net interest income. Net interest income is a significant component of net income, and consists of the difference between interest income generated on interest-earning assets and interest expense incurred on interest-bearing liabilities. Net interest income is primarily affected by the volumes, interest rates and composition of interest-earning assets and interest-bearing liabilities. The tables below titled "Average Balances, Interest Rates and Yields" and "Rate/Volume Analysis of Net Interest Income" provide important information on factors impacting net interest income and should be read in conjunction with this discussion of net interest income.

Net interest income totaled $8.4 million for the nine months ended September 30, 2016 and increased $1.1 million, or 14.9%, compared to $7.3 million for the nine months ended September 30, 2015. The increase in net interest income was primarily due to a $1.4 million, or 15.0%, increase in interest income, partially offset by a $301,000, or 15.6%, increase in interest expense. The increase in interest income was primarily attributed to a $34.5 million, or 11.4%, increase in average interest-earning assets outstanding and a 13bps increase in average yield on interest-earning assets. The increase in interest expense was primarily attributed to a $22.9 million, or 8.9%, increase in average interest-bearing liabilities outstanding and a 7bps increase in the average cost of funds on interest-bearing liabilities. As a result, net interest margin of 3.34% for the nine months ended September 30, 2016 increased 10bps compared to the net interest margin of 3.24% for the nine months ended September 30, 2015.

Interest income totaled $10.7 million and increased $1.4 million, or 15.0%, for the nine months ended September 30, 2016, compared to $9.3 million for the nine months ended September 30, 2015. The increase in interest income was primarily due to a $38.3 million, or 14.2%, increase in average loans and loans held for sale balances from $269.8 million at September 30, 2015, to $308.1 million at September 30, 2016, and a 4bps increase in the average yield on loans and loans held for sale.

Interest expense totaled $2.2 million and increased $301,000, or 15.6%, for the nine months ended September 30, 2016, compared to $1.9 million for the nine months ended September 30, 2015. The increase in interest expense resulted primarily from increased deposit costs due to a $21.6 million, or 9.0%, increase in average interest-bearing deposit balances, coupled with an increase in the cost of funds. The overall cost of funds on total interest-bearing deposits increased 6bps to 97bps at September 30, 2016 compared to 91bps at September 30, 2015 primarily due to higher promotional rates paid to increase core deposit levels.

Provision for loan losses. The provision for loan losses totaled $230,000 for the nine months ended September 30, 2016 and increased $30,000, or 15.0%, compared to $200,000 for the nine months ended September 30, 2015. The increase in the provision for loan losses for the nine months ended September 30, 2016 was primarily due to increased loan growth, which was partially offset by a continual decrease in the majority of historical loss rates and favorable trends in certain qualitative factors and net recoveries. Net recoveries for the nine months ended September 30, 2016 totaled $43,000 compared to net recoveries of $6,000 for the nine months ended September 30, 2015. The ratio of the ALLL to nonperforming loans improved to 794.1% as of September 30, 2016.

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The following table presents information regarding net charge-offs (recoveries) for the nine months ended September 30, 2016 and 2015.

	For the nine months ended September 30,	
	2016	2015
(unaudited)	(Dollars in thousands)	
Commercial	$ 123	$ (17)
Single-family residential real estate	90	39
Multi-family residential real estate	(143)	-
Commercial real estate	(100)	(8)
Home equity lines of credit	(14)	(24)
Other consumer loans	1	4
Total	$ (43)	$ (6)

Noninterest income. Noninterest income for the nine months ended September 30, 2016 totaled $944,000 and decreased $199,000, or 17.4%, compared to $1.1 million for the nine months ended September 30, 2015. The decrease was primarily due to a $260,000 decrease in net gains on sales of loans and a $205,000 decrease in other noninterest income, partially offset by a $253,000 increase in service charges on deposit accounts. The decrease in the net gains on sales of loans was primarily due to a SBA loan sale during the second quarter of 2015 and lower residential mortgage sales activity. The decrease in other noninterest income was related to decreased activity related to the Company's joint ventures. The increase in service charges on deposit accounts was related to increased pricing, deposit growth and activity and new account relationships.

Noninterest expense. Noninterest expense increased $64,000, or 0.9%, and totaled $7.3 million for the nine months ended September 30, 2016, compared to $7.2 million for the nine months ended September 30, 2015. The increase in noninterest expense during the nine months ended September 30, 2016 was primarily due to a $268,000 increase in professional fees, partially offset by a $145,000 decrease in FDIC premiums and a $69,000 decrease in regulatory assessment expense. The increase in professional fees was due to increases in recruiting fees, legal expense related to loan workouts, and information technology consulting projects. The decrease in FDIC premiums and regulatory assessment expense was due to lower assessment factors charged based on CFBank's improved performance.

Income taxes. Income tax expense was $603,000 for the nine months ended September 30, 2016, an increase of $603,000 compared to $0 for the nine months ended September 30, 2015. As of September 30, 2015, the Company maintained a valuation allowance against the net deferred tax asset which reduced the deferred tax asset to zero; thus,

no income tax expense was recorded for the nine months ended September 30, 2015. With the reversal of the deferred tax valuation allowance as of December 31, 2015, as discussed below, the Company is now recording income tax expense based on the federal statutory rate adjusted for the effect of bank owned life insurance and other miscellaneous items. The effective tax rate for the nine months ended September 30, 2016, was approximately 32.7% which management believes is a reasonable estimate for the effective tax rate.

Our deferred tax assets are composed of U.S. net operating losses (“NOLs”), and other temporary book to tax differences. The Company recorded a deferred tax valuation allowance which reduced the Company’s deferred tax asset to zero beginning in 2009 and continuing up until the fourth quarter of 2015; the Company maintained this valuation allowance against the net deferred tax assets during this period based on its estimate of future reversal and utilization. As a result, there was no income tax benefit recorded during the first three quarters of 2015.

When determining the amount of deferred tax assets that are more-likely-than-not to be realized, and therefore recorded as a benefit, the Company conducts a regular assessment of all available information. This information includes, but is not limited to, taxable income in prior periods, projected future income and projected future reversals of deferred tax items. Based on these criteria, the Company determined as of December 31, 2015, in part because the Company had achieved seven consecutive quarters of pretax income, that it was no longer necessary to maintain a full valuation allowance against the entire net deferred tax asset. As a result, the valuation allowance on the deferred tax asset was reversed as of December 31, 2015 which resulted in a credit to income tax expense

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of $3.2 million. With the reversal of the deferred tax valuation allowance, the Company is now recording income tax expense based on the federal statutory rate adjusted for the effect of other items such as incentive stock option expense, bank owned life insurance, and other miscellaneous items.

Average Balances, Interest Rates and Yields. The following table presents, for the periods indicated, the total dollar amount of fully taxable equivalent interest income from average interest-earning assets and the resultant yields, as well as the interest expense on average interest-bearing liabilities, expressed in both dollars and rates. Average balances are computed using month-end balances.

	For Three Months Ended September 30,					
	2016			2015		
	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)					
Interest-earning assets:						
Securities (1) (2)	$ 9,282	$ 29	1.26%	$ 9,050	$ 31	1.38%
Loans and loans held for sale (3)	323,348	3,658	4.53%	276,309	3,073	4.45%
Other earning assets	19,586	28	0.57%	22,396	16	0.29%
FHLB stock	1,942	19	3.91%	1,942	19	3.91%
Total interest-earning assets	354,158	3,734	4.22%	309,697	3,139	4.06%
Noninterest-earning assets	26,161			24,370		
Total assets	$ 380,319			$ 334,067		
Interest-bearing liabilities:						
Deposits	$ 274,677	683	0.99%	$ 245,918	585	0.95%
FHLB advances and other borrowings	22,015	115	2.09%	19,656	100	2.04%
Total interest-bearing liabilities	296,692	798	1.08%	265,574	685	1.03%
Noninterest-bearing liabilities	44,678			33,475		
Total liabilities	341,370			299,049		
Equity	38,949			35,018		
Total liabilities and equity	$ 380,319			$ 334,067		
Net interest-earning assets	$ 57,466			$ 44,123		
Net interest income/interest rate spread		$ 2,936	3.14%		$ 2,454	3.03%
Net interest margin			3.32%			3.17%
Average interest-earning assets to average interest-bearing liabilities	119.37%			116.61%		

[1] Average balance is computed using the carrying value of securities. Average yield is computed using the historical amortized cost average balance for available for sale securities.
[2] Average yields and interest earned are stated on a fully taxable equivalent basis.
[3] Average balance is computed using the recorded investment in loans net of the ALLL and includes nonperforming loans.

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	For Nine Months Ended September 30,					
	2016			2015		
	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)					
Interest-earning assets:						
Securities (1) (2)	$ 9,330	$ 89	1.28%	$ 9,282	$ 100	1.45%
Loans and loans held for sale (3)	308,113	10,439	4.52%	269,840	9,063	4.48%
Other earning assets	17,763	76	0.57%	21,562	49	0.30%
FHLB stock	1,942	58	3.98%	1,942	58	3.98%
Total interest-earning assets	337,148	10,662	4.22%	302,626	9,270	4.09%
Noninterest-earning assets	25,719			23,588		
Total assets	$ 362,867			$ 326,214		
Interest-bearing liabilities:						
Deposits	$ 260,136	1,899	0.97%	$ 238,572	1,628	0.91%
FHLB advances and other borrowings	21,008	326	2.07%	19,656	296	2.01%
Total interest-bearing liabilities	281,144	2,225	1.06%	258,228	1,924	0.99%
Noninterest-bearing liabilities	43,055			33,191		
Total liabilities	324,199			291,419		
Equity	38,668			34,795		
Total liabilities and equity	$ 362,867			$ 326,214		
Net interest-earning assets	$ 56,004			$ 44,398		
Net interest income/interest rate spread		$ 8,437	3.16%		$ 7,346	3.10%
Net interest margin			3.34%			3.24%
Average interest-earning assets to average interest-bearing liabilities	119.92%			117.19%		

(1) Average balance is computed using the carrying value of securities. Average yield is computed using the historical amortized cost average balance for available for sale securities.

(2) Average yields and interest earned are stated on a fully taxable equivalent basis.

(3) Average balance is computed using the recorded investment in loans net of the ALLL and includes nonperforming loans.

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Rate/Volume Analysis of Net Interest Income. The following table presents the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities. It distinguishes between the increase and decrease related to changes in balances and/or changes in interest rates. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in volume (i.e., changes in volume multiplied by the prior rate) and (ii) changes in rate (i.e., changes in rate multiplied by prior volume). For purposes of this table, changes attributable to both rate and volume which cannot be segregated have been allocated proportionately to the change due to volume and the change due to rate.

	Three Months Ended September 30, 2016 Compared to Three Months Ended September 30, 2015			Nine Months Ended September 30, 2016 Compared to Nine Months Ended September 30, 2015		
	Increase (decrease) due to			Increase (decrease) due to		
	Rate	Volume	Net	Rate	Volume	Net
	(Dollars in thousands)			(Dollars in thousands)		
Interest-earning assets:						
Securities (1)	$ (6)	$ 4	$ (2)	$ (12)	$ 1	$ (11)
Loans and loans held for sale	54	531	585	80	1,296	1,376
Other earning assets	25	(13)	12	42	(15)	27
FHLB Stock	-	-	-	-	-	-
Total interest-earning assets	73	522	595	110	1,282	1,392
Interest-bearing liabilities:						
Deposits	27	71	98	118	153	271
FHLB advances and other borrowings	3	12	15	9	21	30
Total interest-bearing liabilities	30	83	113	127	174	301
Net change in net interest income	$ 43	$ 439	$ 482	$ (17)	$ 1,108	$ 1,091

(1) Securities amounts are presented on a fully taxable equivalent basis.

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Critical Accounting Policies

We follow financial accounting and reporting policies that are in accordance with U.S. generally accepted accounting principles and conform to general practices within the banking industry. These policies are presented in Note 1 to our 2015 Audited Financial Statements. Some of these accounting policies are considered to be critical accounting policies, which are those policies that are both most important to the portrayal of the Company's financial condition and results of operations, and require management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Application of assumptions different than those used by management could result in material changes in our financial condition or results of operations. These policies, current assumptions and estimates utilized, and the related disclosure of this process, are determined by management and routinely reviewed with the Audit Committee of the Board of Directors. We believe that the judgments, estimates and assumptions used in the preparation of the consolidated financial statements were appropriate given the factual circumstances at the time.

We have identified accounting policies that are critical accounting policies, and an understanding of these policies is necessary to understand our financial statements. The following discussion details the critical accounting policies and the nature of the estimates made by management.

Determination of the ALLL. The ALLL represents management's estimate of probable incurred credit losses in the loan portfolio at each balance sheet date. The allowance consists of general and specific components. The general component covers loans not classified as impaired and is based on historical loss experience, adjusted for current factors. Current factors considered include, but are not limited to, management's oversight of the portfolio, including lending policies and procedures; nature, level and trend of the portfolio, including past due and nonperforming loans, loan concentrations, loan terms and other characteristics; current economic conditions and outlook; collateral values; and other items. The specific component of the ALLL relates to loans that are individually classified as impaired. Loans exceeding policy thresholds are regularly reviewed to identify impairment. A loan is impaired when, based on current information and events, it is probable that CFBank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. Determining whether a loan is impaired and whether there is an impairment loss requires judgment and estimates, and the eventual outcomes may differ from estimates made by management. The determination of whether a loan is impaired includes: review of historical data; judgments regarding the ability of the borrower to meet the terms of the loan; an evaluation of the collateral securing the loan and estimation of its value, net of selling expenses, if applicable; various collection strategies; and other factors relevant to the loan or loans. Impairment is measured based on the fair value of collateral, less costs to sell, if the loan is collateral dependent, or alternatively, the present value of expected future cash flows discounted at the loan's effective rate, if the loan is not collateral dependent. When the selected measure is less than the recorded investment in the loan, an impairment loss is recorded. As a result, determining the appropriate level for the ALLL involves not only evaluating the current financial situation of individual borrowers or groups of borrowers, but also current predictions about future events that could change before an actual loss is determined. Based on the variables involved and the fact that management must make judgments about outcomes that are inherently uncertain, the determination of the ALLL is considered to be a critical accounting policy. Additional information regarding this policy is included in the previous section titled "Financial Condition - Allowance for loan losses", in Note 4 to the consolidated financial statements included in this Quarterly Report on

Form 10-Q and in Notes 1, 4 and 6 to our 2015 Audited Financial Statements.

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Valuation of the deferred tax asset. Our deferred tax assets are composed of U.S. net operating losses ("NOLs"), and other temporary book to tax differences. The Company recorded a deferred tax valuation allowance which reduced the Company's deferred tax asset to zero beginning in 2009 and continuing up until the fourth quarter of 2015; the Company maintained this valuation allowance against the net deferred tax assets during this period based on its estimate of future reversal and utilization. As a result, there was no income tax benefit recorded during the first three quarters of 2015.

When determining the amount of deferred tax assets that are more-likely-than-not to be realized, and therefore recorded as a benefit, the Company conducts a regular assessment of all available information. This information includes, but is not limited to, taxable income in prior periods, projected future income and projected future reversals of deferred tax items. Based on these criteria, the Company determined as of December 31, 2015, in part because the Company had achieved seven consecutive quarters of pretax income, that it was no longer necessary to maintain a full valuation allowance against the entire net deferred tax asset. As a result, the valuation allowance on the deferred tax asset was reversed as of December 31, 2015 which resulted in a credit to income tax expense of $3.2 million.

In 2012, the Company completed a recapitalization program through the sale of $22.5 million in common stock which improved the capital levels of CFBank and provided working capital for the Holding Company. The result of the change in stock ownership associated with the stock offering was that the Company incurred an ownership change, within the guidelines of Section 382 of the Internal Revenue Code of 1986. At year-end 2015, the Company had net operating loss carryforwards of $25.2 million, which expire at various dates from 2024 to 2033, and has alternative minimum tax credit carryforwards of $105,000, which do not expire. As a result of the ownership change in connection with the 2012 stock offering, the Company's ability to utilize carryforwards that arose before the stock offering closed is limited to $163,000 per year. Due to this limitation, management determined it is more likely than not that $20.5 million of net operating loss carryforwards will expire unutilized. As required by accounting standards, the Company reduced the carrying value of deferred tax assets, and the corresponding valuation allowance, by the $7.0 million tax effect of this lost realizability.

Federal income tax laws provided additional deductions, totaling $2.3 million, for thrift bad debt reserves established before 1988. Accounting standards do not require a deferred tax liability to be recorded on this amount, which otherwise would total $765,000 at year-end 2015. However, if CFBank were wholly or partially liquidated or otherwise ceases to be a bank, or if tax laws were to change, this amount would have to be recaptured and a tax liability recorded. Additionally, any distributions in excess of CFBank's current or accumulated earnings and profits would reduce amounts allocated to its bad debt reserve and create a tax liability for CFBank. The amount of additional taxable income created by such a distribution is an amount that, when reduced by the tax attributable to the income, is equal to the amount of the distribution. Thus, if CFBank makes a distribution that reduces the amount allocated to its bad debt reserve, then approximately one and one-half times the amount used would be includible in gross income for federal income tax purposes, assuming a 34% corporate income tax rate. CFBank does not intend to make distributions that would result in a recapture of any portion of its bad debt reserve.

At December 31, 2015, the Company had a deferred tax asset recorded in the amount of $3.3 million, after reversing the valuation allowance mentioned above. At September 30, 2016, the Company had a deferred tax asset recorded in the amount of $2.7 million. At September 30, 2016 and December 31, 2015, the Company had no unrecognized tax benefits recorded. The Company is subject to U.S. federal income tax and is no longer subject to federal examination

for years prior to 2012. Additional information is included in Notes 1 and 14 to our 2015 Audited Financial Statements.

Fair value of financial instruments. Another critical accounting policy relates to the fair values of financial instruments, which are estimated using relevant market information and other assumptions. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates. Additional information is included in Note 5 to the consolidated financial statements included in this Quarterly Report on Form 10-Q and in Notes 1 and 6 to our 2015 Audited Financial Statements.

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MANAGEMENT'S DISCUSSION AND ANALYSIS

Fair value of foreclosed assets. Another critical accounting policy relates to the fair values of foreclosed assets, which are estimated based on real estate appraisals which may use a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant, and changes in assumptions or market conditions could significantly affect the values. Additional information is included in Note 5 to the consolidated financial statements included in this Quarterly Report on Form 10-Q and in Notes 1, 5 and 6 to our 2015 Audited Financial Statements.

Liquidity and Capital Resources

In general terms, liquidity is a measurement of an enterprise's ability to meet cash needs. The primary objective in liquidity management is to maintain the ability to meet loan commitments and to repay deposits and other liabilities in accordance with their terms without an adverse impact on current or future earnings. Principal sources of funds are deposits; amortization and prepayments of loans; maturities, sales and principal receipts of securities available for sale; borrowings; and operations. While maturities and scheduled amortization of loans are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition.

CFBank is required by regulation to maintain sufficient liquidity to ensure its safe and sound operation. Thus, adequate liquidity may vary depending on CFBank's overall asset/liability structure, market conditions, the activities of competitors, the requirements of our own deposit and loan customers and regulatory considerations. Management believes that each of the Holding Company's and CFBank's current liquidity is sufficient to meet their daily operating needs and fulfill their strategic planning.

Liquidity management is both a daily and long-term responsibility of management. We adjust our investments in liquid assets, primarily cash, short-term investments and other assets that are widely traded in the secondary market, based on our ongoing assessment of expected loan demand, expected deposit flows, yields available on interest-earning deposits and securities and the objective of our asset/liability management program. In addition to liquid assets, we have other sources of liquidity available including, but not limited to, access to advances from the FHLB and borrowings from the FRB and our commercial bank line of credit.

The following table summarizes CFBank's cash available from liquid assets and borrowing capacity at September 30, 2016 and December 31, 2015.

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Cash, unpledged securities and deposits in other financial institutions	$ 52,171	$ 25,617
Additional borrowing capacity at the FHLB	29,903	15,813
Additional borrowing capacity at the FRB	33,095	30,241

Unused commercial bank line of credit	1,000	1,000
Total	$ 116,169	$ 72,671

Cash, unpledged securities and deposits in other financial institutions increased $26.6 million, or 103.7%, to $52.2 million at September 30, 2016 compared $25.6 million at December 31, 2015. The increase is primarily due to an increase in cash, which was a result of management's efforts to increase deposit activity in order to fund anticipated loan growth.

CENTRAL FEDERAL CORPORATION

PART 1. Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS

CFBank's additional borrowing capacity with the FHLB increased $14.1 million to $29.9 million at September 30, 2016, compared to $15.8 million at December 31, 2015. The increase in additional borrowing capacity is a result of additional collateral pledged due to the increase in loans.

CFBank's additional borrowing capacity at the FRB increased to $33.1 million at September 30, 2016 from $30.2 million at December 31, 2015. CFBank is eligible to participate in the FRB's primary credit program, providing CFBank access to short-term funds at any time, for any reason, based on the collateral pledged.

CFBank's borrowing capacity with both the FHLB and FRB may be negatively impacted by changes such as, but not limited to, further tightening of credit policies by the FHLB or FRB, deterioration in the credit performance of CFBank's loan portfolio or CFBank's financial performance, or a decrease in the balance of pledged collateral.

CFBank had a $1.0 million unused line of credit with one commercial bank at September 30, 2016 and December 31, 2015.

Deposits are obtained predominantly from the areas in which CFBank's offices are located. We rely primarily on a willingness to pay market-competitive interest rates to attract and retain retail deposits. Accordingly, rates offered by competing financial institutions may affect our ability to attract and retain deposits.

CFBank relies on competitive interest rates, customer service, and relationships with customers to retain deposits. To promote and stabilize liquidity in the banking and financial services sector, the FDIC, pursuant to the provisions of the Dodd-Frank Act as previously discussed, permanently increased deposit insurance coverage from $100,000 to $250,000 per depositor.

The Holding Company has more limited sources of liquidity than CFBank. In general, in addition to its existing liquid assets, sources of liquidity include funds raised in the securities markets through debt or equity offerings, dividends received from its subsidiaries or the sale of assets. Pursuant to the Holding Company Order and the commitments made in connection with the termination of the Holding Company Order, the Holding Company was not permitted to declare or pay dividends on its stock, purchase or redeem its stock, or accept dividends or other capital distributions from CFBank without the prior written approval of the FRB. In addition, the Holding Company was not permitted to incur, increase or guarantee any debt without the prior written consent of the FRB. Effective as of January 8, 2016, the Holding Company ceased to be subject to the foregoing restrictions. In addition, the Holding Company is permitted to raise funds in the securities markets through equity offerings.

The Holding Company had adequate funds at September 30, 2016 to meet its current and anticipated operating needs at this time. The Holding Company's current cash requirements include operating expenses and interest on subordinated debentures. The Company may elect to pay dividends on its common stock, if and when declared by the Board of Directors, subject, in the case of dividends on common stock, to the payment in full of the dividend on the Company's Series B Preferred Stock for the current dividend period.

Currently, annual debt service on the subordinated debentures is approximately $180,000. The subordinated debentures have a variable rate of interest, reset quarterly, equal to the three-month LIBOR plus 2.85%. The total rate in effect was 3.69% at September 30, 2016. An increase in the three-month LIBOR would increase the debt service

requirement of the subordinated debentures.

Banking regulations limit the amount of dividends that can be paid to the Holding Company by CFBank without prior regulatory approval. Generally, financial institutions may pay dividends without prior approval as long as the dividend does not exceed the total of the current calendar year-to-date earnings plus any earnings from the previous two years not already paid out in dividends, and as long as the financial institution remains well capitalized after the dividend payment. Any future dividend payments by CFBank to the Holding Company would be based on future earnings and, if necessary, regulatory approval.

The ability of the Holding Company to pay dividends on its common stock and Series B Preferred Stock is generally dependent upon the receipt of dividends and other distributions from CFBank. The Holding Company is a legal entity that is separate and distinct from CFBank, which has no obligation to make any dividends or other funds available for the payment of dividends by the Holding Company. The Holding Company also is subject to various legal and regulatory policies and requirements impacting the Holding Company's ability to pay dividends on its stock. Pursuant to the Holding Company Order and the commitments made to the FRB in connection with the termination of the Holding Company Order, the Holding Company was not permitted to declare or pay dividends on its stock without the prior approval or written non-objection of the FRB. Effective January 8, 2016, however, the Holding Company is no longer required to obtain the FRB's prior approval or written non-objection to pay dividends. In addition, the Holding Company's ability to pay dividends on its stock is conditioned upon the payment, on a current basis, of quarterly interest payments on the subordinated debentures underlying the Company's trust preferred securities. Finally, so long as the Company's Series B Preferred Stock remains outstanding, the Holding Company will be prohibited from paying dividends (other than dividends payable solely for the then-current dividend period in shares) on the Company's common stock, unless full dividends on the Series B Preferred Stock have been paid or set aside for payment.

CENTRAL FEDERAL CORPORATION

PART 1. Item 3

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Management believes there has been no material change in the Company’s market risk from the information contained in the Company’s Form 10-K filed with the Securities and Exchange Commission for the year ended December 31, 2015.

CENTRAL FEDERAL CORPORATION

PART 1. Item 4

CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures. We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Securities Exchange Act of 1934 (Exchange Act) reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on such evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of and for the quarter ended September 30, 2016.

Changes in internal control over financial reporting. We made no changes in our internal controls over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) in the third quarter of 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

CENTRAL FEDERAL CORPORATION

PART II. Item 4

OTHER INFORMATION

Item 1. Legal Proceedings

We may, from time to time, be involved in various legal proceedings in the normal course of business. Periodically, there have been various claims and lawsuits involving CFBank, such as claims to enforce liens, condemnation proceedings on properties in which CFBank holds security interests, claims involving the making and servicing of real property loans and other claims and lawsuits incident to our banking business.

We are not a party to any pending legal proceeding that management believes would have a material adverse effect on our financial condition or operations, if decided adversely to us.

Item 1A. Risk Factors

There were no material changes to the risk factors as presented in the Company's Annual Report on Form 10-K for the year ended December 31, 2015.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) None
(b) Not applicable.
(c) The following table provides information concerning purchases of the Holding Company's shares of common stock made by or on behalf of the Company or any "affiliated purchaser" as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, as amended, during the three months ended September 30, 2016, as well as the maximum number of shares of common stock that may be purchased under the stock repurchase program announced by the Company in May 2016.

Period	Total number of common shares purchased	Average price paid per common share (1)	Total number of common shares purchased as part of publicly announced plans or programs	Maximum number of common shares that may yet be purchased under the plans or programs (2)
July 1 through July 31, 2016	-	-	-	460,226
August 1 through August 31, 2016	600	1.33	600	459,626
September 1 through September 30, 2016	200	1.35	200	459,426

Total	800	$ 1.34	800

(1) Excludes broker commissions.

(2) In May 2016, the Company announced that its Board of Directors adopted a stock repurchase program pursuant to which the Company may repurchase up to 3% of the Company's common stock (480,726 shares) over the next six months. The Board of Directors subsequently approved the continuation of this repurchase program for an additional six-month period commencing November 10, 2016. Any purchases under the repurchase program will be made from time to time in the open market in accordance with applicable federal and state securities laws and regulations. The timing and amount of any stock repurchases will be determined by the Company's management based on its evaluation of market conditions, regulatory requirements and other corporate considerations.

CENTRAL FEDERAL CORPORATION

PART II. Item 4

OTHER INFORMATION

Item 3. Defaults upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits.

See Exhibit Index at page 71 of this report on Form 10-Q.

CENTRAL FEDERAL CORPORATION

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.

CENTRAL FEDERAL CORPORATION

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Dated: November 9, 2016 By: /s/ Timothy T. O'Dell
Timothy T. O'Dell
President and Chief Executive Officer

Chief Financial Officer

Dated: November 9, 2016 By: /s/ John W. Helmsdoerfer
John W. Helmsdoerfer, CPA
Treasurer and Chief Financial Officer

CENTRAL FEDERAL CORPORATION

Exhibit Number	Description of Exhibit
3.1	Certificate of Incorporation of the registrant (incorporated by reference to Exhibit 3.1 to the registrant's Registration Statement on Form SB-2 (File No. 333-64089), filed with the Commission on September 23, 1998)
3.2	Amendment to Certificate of Incorporation of the registrant (incorporated by reference to Exhibit 3.2 to the registrant's Registration Statement on Form S-2 (File No. 333-129315), filed with the Commission on October 28, 2005)
3.3	Amendment to Certificate of Incorporation of the registrant (incorporated by reference to Exhibit 3.4 to the registrant's Form 10-Q for the quarter ended June 30, 2009, filed with the Commission on August 14, 2009 (File No. 0-25045))
3.4	Amendment to Certificate of Incorporation of the registrant (incorporated by reference to Exhibit 3.5 to the registrant's Form 10-Q for the quarter ended September 30, 2011, filed with the Commission on November 10, 2011 (File No. 0-25045))
3.5	Amendment to Certificate of Incorporation of the registrant (incorporated by reference to Exhibit 3.5 to the registrant's Post-Effective Amendment to the Registration Statement on Form S-1 (File No. 333-177434), filed with the Commission on May 4, 2012)
3.6	Certificate of Designations to Certificate of Incorporation of the registrant (incorporated by reference to Exhibit 3.1 to the registrant's Current Report on Form 8-K dated May 7, 2014 and filed with the Commission on May 13, 2014. (File No. 0-25045))
3.7	Second Amended and Restated Bylaws of the registrant (incorporated by reference to Exhibit 3.3 to the registrant's Form 10-K for the fiscal year ended December 31, 2007, filed with the Commission on March 27, 2008 (File No. 0-25045))
4.1	Form of Stock Certificate of Central Federal Corporation (incorporated by reference to Exhibit 4.0 to the registrant's Registration Statement on Form SB-2 (File No. 333-64089), filed with the Commission on September 23, 1998)
4.2	Form of Certificate for the Series B Preferred Stock of Central Federal Corporation (incorporated by reference to Exhibit 4.1 to the registrant's Current Report on Form 8-K dated May 7, 2014 and filed with the Commission on May 13, 2014 (File No. 0-25045))
4.3	Form of Warrant for the purchase of common stock of Central Federal Corporation (incorporated by reference to Exhibit 4.2 to the registrant's Current Report on Form 8-K dated May 7, 2014 and filed with the Commission on May 13, 2014 (File No. 0-25045))
4.4	

Form of Registration Rights Agreement (incorporated by reference to Exhibit 4.3 to the registrant's Current Report on Form 8-K dated May 7, 2014 and filed with the Commission on May 13, 2014 (File No. 0-25045))

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11.1 Statement Re: Computation of Per Share Earnings
31.1 Rule 13a-14(a) Certifications of the Chief Executive Officer
31.2 Rule 13a-14(a) Certifications of the Chief Financial Officer
32.1 Section 1350 Certifications of the Chief Executive Officer and Chief Financial Officer
101.1 Interactive Data File (XBRL)