

South Mississippi Electric Power Association
Key Indicators - Five Year Analysis

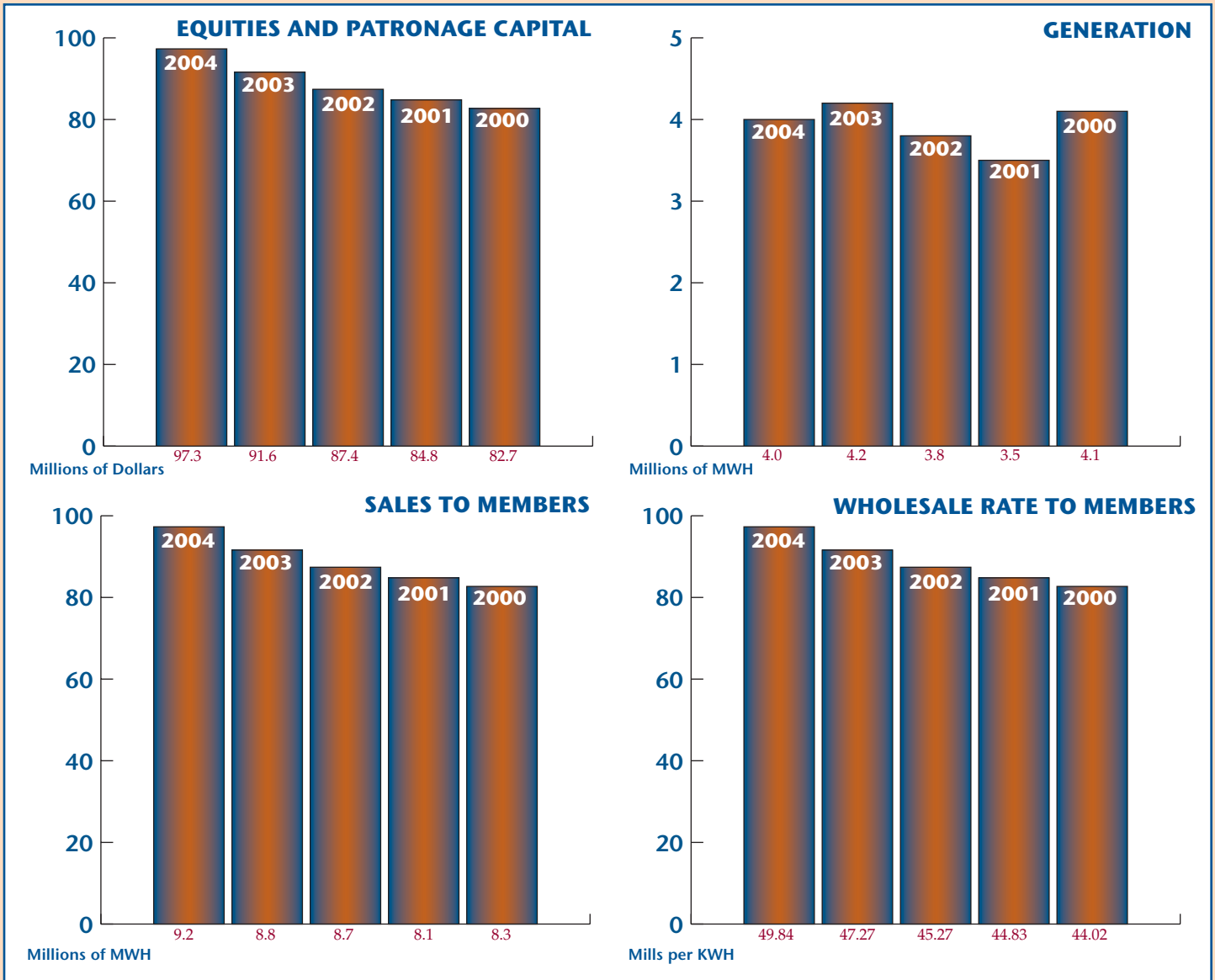


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South Mississippi Electric Power Association *2004 Financial Review*

The year 2004 was another year of solid financial results for SMEPA even as the electric utility industry faced volatile fuel prices. Revenues from Member cooperatives were \$464 million, up 13%. Energy sales to Members were up 4.4% to 9.2 million megawatt hours, a new all-time record. Generation by SMEPA-owned plants was down 3% to 4.0 million megawatt hours. Demand billings for the year were up 2.7% with a monthly average of 1,718 megawatts. The net margin for the year was up noticeably to \$5.7 million. Total equity increased to \$97 million and improved slightly to 11.1% of net assets.

The wholesale rate to Members for the year averaged 49.8 mills per kilowatt hour, up 2.5 mills or 5.4% compared to year 2003. The rising cost of coal and natural gas during 2004 affected SMEPA and other utilities and led to a September 1 increase in the benchmark fuel cost adjustment rate. SMEPA's average cost for coal increased 24% for all of 2004. SMEPA's actual average cost for natural gas for 2004 was down about 10% compared to 2003 because of advance price-quantity actions before the year started, but market prices during the year were higher and extremely volatile. The high cost of coal and natural gas caused SMEPA to rely on contract power when it was available at a more favorable price. For the year, SMEPA purchased 5.3 million megawatt hours, up 11%.

SMEPA invested \$51 million in new generation, transmission and other utility plant assets during 2004, bringing gross investment to \$1.15 billion. At mid-year, SMEPA successfully placed into service an 83.5 megawatt natural gas fueled combustion tur-

bine generator valued at more than \$35 million including related transmission improvements. The new asset brought SMEPA's owned capacity to 1,067 megawatts. \$46 million has been invested in two additional combustion turbines rated at 83.5 megawatts each which are at different stages of construction and installation at year-end.

On April 1, 2004, SMEPA received its first Federal Financing Bank (FFB) loan advance under the Rural Utilities Service (RUS) \$275 million loan guarantee which provides permanent 30 year financing for the combustion turbine project. The \$100 million advance was priced for 30 years at 5.03% with the proceeds used to repay interim financing provided by National Rural Utilities Cooperative Finance Corporation (CFC). Market interest rates were historically low during 2004 and SMEPA firmed the interest rate on \$213 million of FFB debt at an average cost of 5.04% for 30 years. The average cost of all debt (\$719 million) at year-end 2004 increased to 5.4% as short-term interim debt was replaced with long-term permanent debt.

Looking forward, the rising and volatile cost of coal and natural gas continues to challenge SMEPA and all utilities using those fuels to generate electricity. Many economists consider the price of natural gas to be the most volatile of all commodities. SMEPA has a blend of resources including coal, nuclear, hydro and purchased power contracts and remains committed to providing its core customer-owners, the eleven Member cooperatives, with reliable wholesale power at the best possible rate. SMEPA's Members serve the electricity needs of consumers through more than 377,000 meters in parts of rural Mississippi.

South Mississippi Electric Power Association *Comparative Balance Sheets*

In thousands as of December 31,	2004	2003	2002	2001	2000
Assets					
Electric Utility Plant					
In Service - at Cost	\$ 1,066,979	\$ 996,241	\$ 859,736	\$ 845,253	\$ 828,332
Construction Work in Process	87,846	111,894	188,948	84,354	42,277
	1,154,825	1,108,135	1,048,684	929,607	870,609
Less Accumulated Depreciation	473,886	446,938	420,938	397,434	373,874
Net Utility Plant	680,939	661,197	627,746	532,173	496,735
Investments	37,621	58,508	50,982	35,444	22,720
Current Assets					
Cash - General Funds and Cash Equivalent Investments	21,978	12,468	15,434	24,639	22,119
Accounts Receivable - Members	42,882	37,343	31,731	28,952	33,745
Coal and Other Fuel Inventories	6,282	8,046	10,572	7,804	5,206
Other Current Assets	17,979	20,181	19,581	16,327	16,771
Total Current Assets	89,121	78,038	77,318	77,722	77,841
Deferred Charges	72,353	76,112	83,897	86,212	90,084
Total Assets	\$ 880,034	\$ 873,855	\$ 839,943	\$ 731,551	\$ 687,380
Equities and Liabilities					
Patronage and Other Capital	\$ 97,251	\$ 91,581	\$ 87,404	\$ 84,848	\$ 82,722
Long-Term Debt (excluding current maturities)	676,576	680,760	659,249	559,105	516,265
Accrued Decommissioning Obligation	15,055	12,718	10,021	10,501	10,407
Deferred Credits and Other Long-Term Liabilities	5,030	12,442	8,377	10,850	4,075
Current Liabilities					
Accounts Payable	33,046	28,066	30,718	30,807	29,243
Notes Payable	7,000	10,600	8,000	2,000	-
Other Current Liabilities	46,076	37,688	36,174	33,440	44,668
Total Current Liabilities	86,122	76,354	74,892	66,247	73,911
Total Equities and Liabilities	\$ 880,034	\$ 873,855	\$ 839,943	\$ 731,551	\$ 687,380
Equity as % of Assets	11.1%	10.5%	10.4%	11.6%	12.0%
Debt					
Long-Term Debt and Notes Payable	\$ 683,576	\$ 691,360	\$ 667,249	\$ 561,105	\$ 516,265
Current Maturities on Long-Term Debt	35,050	33,921	32,736	30,591	34,277
Total Debt	\$ 718,626	\$ 725,281	\$ 699,985	\$ 591,696	\$ 550,542
Average Interest Rate	5.43%	4.84%	5.40%	5.88%	6.30%

South Mississippi Electric Power Association

Comparative Operating Statements

In thousands as of December 31,	2004	2003	2002	2001	2000
Revenues					
Electric Energy Revenue from Members	\$ 464,313	\$ 410,734	\$ 393,123	\$ 354,120	\$ 363,535
Interest Income and AFUDC	1,920	2,609	2,329	3,152	2,064
Other Revenue - net	782	934	446	603	3,068
Expenses					
Purchased Power	245,213	210,981	215,819	185,497	183,174
Fuel	90,689	82,927	67,086	63,881	78,217
Production	17,393	16,856	15,687	13,639	13,987
Transmission	15,830	13,661	12,245	11,710	12,171
Maintenance	14,613	14,894	14,888	13,216	11,430
Depreciation and Amortization	33,877	30,376	27,707	26,960	26,461
Interest	37,630	34,727	34,993	36,489	37,344
Administrative and General	6,076	5,640	4,883	4,328	4,030
Other Deductions	24	38	34	29	14
Net Margin	\$ 5,670	\$ 4,177	\$ 2,556	\$ 2,126	\$ 1,839
Financial Ratios					
TIER	1.15	1.11	1.07	1.06	1.05
DSC	1.06	1.03	1.04	1.03	1.06
Rates/Costs - Mills per KWH					
Wholesale Rate to Members	49.84	47.27	45.27	44.83	44.02
Average Cost of Purchased Power	46.10	44.02	43.07	39.86	41.66
Average Cost of Fuel (per net generation)	22.48	19.94	17.62	18.00	19.31
Energy Sources - MWH					
Generated	4,033,649	4,159,337	3,806,529	3,548,906	4,051,486
Purchased	5,318,771	4,792,965	5,010,337	4,653,782	4,396,938
Total Energy Available	9,352,420	8,952,302	8,816,866	8,202,688	8,448,424
Energy Sales - MWH					
Members					
Coahoma EPA	167,687	166,325	152,281	136,694	137,280
Coast EPA	1,610,506	1,553,667	1,538,159	1,429,392	1,497,819
Delta EPA	531,285	530,031	545,505	517,677	529,637
Dixie EPA	784,321	772,959	758,571	712,545	721,905
Magnolia EPA	641,977	602,981	583,274	549,602	559,367
Pearl River Valley EPA	963,012	922,775	900,961	826,141	831,542
Singing River EPA	1,367,944	1,326,422	1,323,324	1,232,291	1,280,415
Southern Pine EPA	1,934,503	1,852,988	1,826,044	1,670,862	1,678,363
Southwest Mississippi EPA	458,372	457,106	451,258	414,021	437,638
Twin County EPA	351,912	259,532	262,307	260,148	302,357
Yazoo Valley EPA	358,664	335,913	310,270	301,046	282,862
Total Sales to Members	9,170,183	8,780,699	8,651,954	8,050,419	8,259,185
Non-Members	16,019	12,775	16,361	26,269	81,704
Total Sales	9,186,202	8,793,474	8,668,315	8,076,688	8,340,889
Member Demand - KW (non-current peak)	2,071,412	2,176,084	2,010,942	1,976,642	2,030,075

South Mississippi Electric Power Association Independent Auditors' Report

To the Board of Directors of
South Mississippi Electric Power Association
Hattiesburg, Mississippi

We have audited the accompanying balance sheets of South Mississippi Electric Power Association ("SMEPA") as of December 31, 2004 and 2003, and the related statements of revenues, expenses and patronage capital, and cash flows for the years then ended. These financial statements are the responsibility of SMEPA's management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of SMEPA as of December 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Ridgeland, Mississippi
February 3, 2005

South Mississippi Electric Power Association
Balance Sheets

In thousands as of December 31,	2004	2003
Assets		
Electric utility plant:		
In service - at cost	\$ 1,066,979	\$ 996,241
Construction work in progress	87,846	111,894
	1,154,825	1,108,135
Less accumulated depreciation	473,886	446,938
Net utility plant	680,939	661,197
Investments:		
Investments in associated organizations	12,256	35,771
Debt service reserve and other investments	4,666	4,648
Decommissioning trust investments	15,055	12,718
Debt service prepayments	5,644	5,371
Total investments	37,621	58,508
Current assets:		
Cash - general funds and cash equivalent investments	21,978	12,468
Accounts receivable:		
Members	42,882	37,343
Others	337	1,214
Inventories (at average cost):		
Coal and other fuels	6,282	8,046
Materials and supplies	16,643	17,631
Other	999	1,336
Total current assets	89,121	78,038
Deferred charges	72,353	76,112
Total Assets	\$ 880,034	\$ 873,855
Equities and Liabilities		
Equities:		
Patronage capital	\$ 96,716	\$ 91,046
Memberships and donated capital	535	535
Total equities	97,251	91,581
Long-term debt (excluding current maturities)	676,576	680,760
Accrued decommissioning obligation	15,055	12,718
Deferred credits and other long-term liabilities	5,030	12,442
Current liabilities:		
Accounts payable	33,046	28,066
Notes payable	7,000	10,600
Accrued interest	9,239	1,660
Other accrued expenses	1,787	2,107
Current maturities of long-term debt	35,050	33,921
Total current liabilities	86,122	76,354
Commitments and contingencies (Notes 3 and 14)	-	-
Total Equities and Liabilities	\$ 880,034	\$ 873,855

See notes to financial statements

South Mississippi Electric Power Association
Statements of Revenues, Expenses and Patronage Capital

In thousands for the years ended December 31,	2004	2003
Operating Revenues		
Electric energy revenue from members	\$ 464,313	\$ 410,734
Other electric energy revenue	587	455
Other - net	(188)	399
Total operating revenues	464,712	411,588
Operating Expenses		
Fuel	90,689	82,927
Production	17,393	16,856
Purchased power	245,213	210,981
Transmission	15,830	13,661
Administrative and general	6,076	5,640
Maintenance expenses:		
Production	10,258	11,121
Transmission	3,235	2,768
General	1,120	1,005
Depreciation and amortization	33,877	30,376
Total operating expenses	423,691	375,335
Operating margin before interest and other deductions	41,021	36,253
Interest and Other Deductions		
Interest	37,630	34,727
Other deductions	24	38
Total interest and other deductions	37,654	34,765
Operating margin	3,367	1,488
Nonoperating Margin		
Interest income	1,663	2,348
Allowance for funds used during construction	257	261
Other	383	80
Total Nonoperating Margin	2,303	2,689
Net Margin	5,670	4,177
Patronage Capital at Beginning of Year	91,046	86,869
Patronage Capital at End of Year	\$ 96,716	\$ 91,046

See notes to financial statements

South Mississippi Electric Power Association
Statements of Cash Flows

In thousands for the years ended December 31,	2004	2003
Operating Activities		
Net margin	\$ 5,670	\$ 4,177
Adjustments necessary to reconcile net margin to net cash provided by operating activities:		
Depreciation, amortization, and depletion	37,333	34,069
Allowance for funds used during construction	(257)	(261)
Change in operating assets and liabilities:		
Accounts receivable	(4,664)	(4,032)
Inventories	2,752	815
Other assets	337	(466)
Accounts payable and other liabilities	4,512	(2,842)
Accrued interest payable	7,579	216
Nuclear outage maintenance costs	(2,141)	-
Fuel cost adjustments	(7,263)	4,366
Accrued decommissioning obligation	2,739	1,993
Net cash provided by operating activities	46,597	38,035
Investing Activities		
Construction and acquisitions of electric utility plant	(50,921)	(57,323)
Redemption of CFC equity certificates	23,512	-
Purchase of available for sale securities	(2,739)	(2,836)
Sale of available for sale securities	-	843
Investment in associated organizations	-	(6,823)
Purchase of held to maturity securities and debt service prepayments	(291)	(22)
Net cash used in investing activities	(30,439)	(66,161)
Financing Activities		
Principal payments on long-term debt	(259,244)	(30,941)
Debt prepayment penalties	-	(2,161)
Proceeds from long-term borrowings	256,196	55,662
Proceeds from short-term borrowings	(3,600)	2,600
Net cash provided by (used in) financing activities	(6,648)	25,160
Net increase (decrease) in cash and cash equivalents	9,510	(2,966)
Cash and cash equivalents at beginning of year	12,468	15,434
Cash and cash equivalents at end of year	\$ 21,978	\$ 12,468
Additional Cash Flow Disclosures:		
Non-cash investing and financing activity - redemption of cushion of credit investments applied as a reduction of related debt	\$ -	\$ 2,018
Interest paid	\$ 29,966	\$ 36,923

See notes to financial statements

Notes to Financial Statements

NOTE 1 – NATURE OF OPERATIONS

South Mississippi Electric Power Association (“SMEPA”) is a member-owned, not-for-profit electric generation and transmission cooperative that supplies wholesale electricity and other services to its eleven member distribution cooperatives, which, in turn, provide retail electric service to consumers in certain areas of Mississippi through approximately 377,000 meters. Under long-term wholesale power contracts with each of its members, SMEPA is obligated to provide all of the power required by the member systems to the extent that SMEPA has power available. Financing assistance is provided by the United States Department of Agriculture, Rural Utilities Service (“RUS”). In addition to being subject to regulation by its own governing board of directors, SMEPA is subject to certain rules and regulations promulgated for rural electric borrowers by RUS. SMEPA maintains its accounting records in accordance with the Federal Energy Regulatory Commission’s (“FERC”) Chart of Accounts as modified and adopted by RUS. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. As a regulated utility, the methods of allocating costs and revenue to time periods may differ from those principles generally applied to nonregulated companies.

SMEPA owns a 10% undivided interest in a nuclear generating plant known as Grand Gulf Unit 1 (“Grand Gulf”). System Energy Resources, Inc. (“System Energy”), a subsidiary of Entergy Corporation (“Entergy”), owns the remaining 90% either outright or through leasehold interests. Entergy Operations, also a subsidiary of Entergy, operates the plant along with other nuclear plants owned by Entergy, subject to owner oversight. Grand Gulf commenced commercial operation on July 1, 1985.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES

Electric Utility Plant and Depreciation

Electric utility plant is stated at cost, which includes contract work, materials and direct labor, allowance for funds used during construction, and allocable overhead costs. The cost of electric generating stations and related facilities also includes costs of training and production incurred, less revenue earned, prior to the date of commercial operation.

Depreciation is provided by the straight-line method for utility plant at the following annual composite rates:

Nuclear generation plant	2.85%
Non-nuclear generation plant	3.00% to 3.10%
Transmission plant	2.75%
General plant and transportation equipment	2.00% to 25.00%

At the time units of electric utility plant are retired, their original cost and cost of removal, less salvage value, are charged to accumulated depreciation. Replacements of electric utility plant involving less than a designated unit of property are charged to maintenance

expense. At each balance sheet date, SMEPA evaluates the recoverability of long-lived assets based upon expectations of nondiscounted cash flows and operating income.

Cost of Decommissioning Nuclear Plant

SMEPA’s portion of the estimated decommissioning cost of Grand Gulf is charged to operating expenses as it is funded over the estimated service life of the plant. The current operating license received from the Nuclear Regulatory Commission terminates in 2024.

Allowance for Funds Used During Construction

SMEPA capitalizes interest on certain significant construction and development projects while in progress. The interest cost capitalized related to debt specifically borrowed for construction and development projects during construction is reflected as a reduction in interest expense. The imputed interest cost related to construction and development projects funded without specific borrowings during construction is reflected as allowance for funds used during construction.

Investment Securities

Decommissioning trust investments are categorized as available for sale and are carried at fair value. In accordance with the regulatory treatment for decommissioning trust funds, realized and unrealized gains on investment securities are also included as a regulatory liability as part of the accrued decommissioning obligation.

Debt service reserve and other investments are categorized as held to maturity and are carried on the balance sheet at amortized cost. SMEPA has the intent and ability to hold these securities until their estimated maturities but may sell them under certain circumstances.

The primary components that determine a security’s fair value are its coupon rate, maturity and credit characteristics. When the fair value of a security falls below amortized cost an evaluation must be made to determine if the unrealized loss is a temporary or other than temporary impairment. Securities that are not deemed to be temporarily impaired are written down to net realizable value by a charge to expense. Premiums and discounts are amortized and accreted to operations using the level yield method, adjusted for prepayments as applicable. Gains and losses on sales of investment securities are computed using the specific identification method.

Cash and Cash Equivalents

For purposes of reporting cash flows, all temporary investments with original maturities of three months or less are deemed to be cash equivalents.

Deferred Charges

SMEPA was a 10% owner in a second unit at the Grand Gulf site when construction was terminated in 1989. With the approval of the RUS, SMEPA is amortizing its remaining investment over a 27-year period ending in 2016.

As a condition of repricing certain outstanding debt in recent years so as to significantly reduce annual interest expense, SMEPA paid

Notes to Financial Statements

penalties of varying amounts that are accounted for as deferred charges to be amortized over the remaining life of the debt.

Bond issue costs are being amortized by the straight-line method, which does not differ materially from the interest method, over the term of the related debt. The amortization during the period of construction is capitalized.

Nuclear outage maintenance costs represent SMEPA's ten percent share of Grand Gulf's incremental maintenance costs associated with refueling outages. These costs are recorded as deferred charges when incurred and are amortized by the straight-line method over the eighteen months between outages.

From time to time, the Board of Directors will set a benchmark fuel cost adjustment rate to be collected from Members so as to match revenues with actual and forecasted fuel and purchased power costs consistent with the cooperative not-for-profit operation of SMEPA. Material variances between these revenues and costs may cause the recognition of deferred credits or deferred charges from one year to the next.

SMEPA's accounting policies include compliance with Statement of Financial Accounting Standards ("SFAS") 71, "Accounting for the Effects of Certain Types of Regulation." In accordance with SFAS 71, SMEPA has regulatory assets of approximately \$72.3 million, including \$47.5 million relating to the unamortized cost of abandoned plant (Note 7). In the event that SMEPA is no longer able to comply with SFAS 71 as the result of a change in regulation or effects of competition, SMEPA would be required to recognize the effects of its regulatory assets and liabilities currently in its statements of revenue, expenses, and patronage capital.

Patronage Capital

The bylaws of SMEPA provide that any excess of revenue over expenses and accumulated prior-year deficits shall be treated as advances of capital by the member patrons and credited to them on the basis of their patronage.

Income Taxes

SMEPA is exempt from United States income taxes pursuant to Section 501(c)(12) of the Internal Revenue Code, which requires that at least 85% of SMEPA's gross income be derived from its members.

NOTE 3 – COMMITMENTS AND CONTINGENCIES REGARDING GRAND GULF

SMEPA and System Energy are co-licensees and parties to a joint ownership contract that sets forth the rights and obligations of the Grand Gulf owners, with SMEPA generally obligated to pay 10% of all operating and capital costs and entitled to receive 10% of the electricity generated by the plant. SMEPA paid \$22,076,000 and \$19,830,000 under the contract in 2004 and 2003, respectively. Ownership of nuclear capacity entails risks and uncertainties somewhat more complex than those for non-nuclear capacity, and these are discussed below.

Nuclear Insurance and Assessments

As the 90% majority co-owner of Grand Gulf, System Energy is responsible for arranging appropriate insurance and industry assessment programs for itself and SMEPA. SMEPA is obligated to pay 10% of all appropriate costs and assessments, if any. Under the program, SMEPA could be assessed up to approximately \$10.1 million for each nuclear incident involving licensed reactors, payable at a rate of \$1 million per reactor per year.

The property insurance presently arranged by System Energy exceeds the Nuclear Regulatory Commission's (NRC) minimum requirement for nuclear power plant licensees of \$1.06 billion per site. NRC regulations provide that the proceeds of this insurance must be used, first, to place and maintain the reactor in a safe and stable condition and, second, to complete decontamination operations. Only after proceeds are dedicated for such use and regulatory approval is secured would any remaining proceeds be made available for the benefit of plant owners or their creditors. The property insurance provides for recovery of property damage losses in the event of domestic-sponsored or foreign-sponsored acts of terrorism. Under a member assessment program, SMEPA could be assessed approximately \$1.3 million for property damage, decontamination, or premature decommissioning expense involving other members' nuclear generation plants.

Nuclear Fuel

System Energy contracts with System Fuels Inc., another Entergy subsidiary company, for nuclear fuel for Grand Gulf, including maintaining inventories. System Energy has a nuclear fuel lease arrangement for up to \$110 million with respect to Grand Gulf. SMEPA pays for nuclear fuel as it is consumed; and such payments include appropriate charges for processing, fabrication, storage, inventory, shipment, and handling.

Spent Nuclear Fuel

System Energy and SMEPA provide for estimated future disposal costs for spent nuclear fuel in accordance with the Nuclear Waste Policy Act of 1982. System Energy entered into contracts with the United States Department of Energy ("DOE"), whereby the DOE will furnish disposal service at a cost of one mill per net KWh generated and sold. The fees payable to the DOE may be adjusted in the future to assure full recovery. Delays have occurred in the DOE's program for the acceptance and disposal of spent nuclear fuel at a permanent repository. Yucca Mountain, Nevada has been legislated to be the permanent spent fuel repository in the United States. The DOE will proceed with licensing and, if the license is granted by the NRC, eventual construction of the repository will begin and receipt of spent fuel may begin sometime after 2010. Considerable uncertainty remains regarding the time frame under which the DOE will begin to accept spent fuel for storage or disposal and as a result, future expenditures will be required to increase spent fuel storage capacity at the Grand Gulf plant site. Pending DOE acceptance and disposal of spent nuclear fuel, the owners of nuclear plants are responsible for their own spent fuel storage. Current on-site spent fuel storage capacity at Grand Gulf is estimated to be sufficient until approximately 2007, at which time dry cask storage facilities will be placed into service.

Notes to Financial Statements

As a result of DOE's failure to begin disposal of spent nuclear fuel in 1998 pursuant to the Nuclear Waste Policy Act of 1982, System Energy and SMEPA have incurred and will continue to incur damages. Litigation was initiated in November 2003 to recover the damages caused by DOE's delay in performance. Management cannot predict the timing or amount of any potential recovery.

Decommissioning Costs

The total cost to decommission Grand Gulf has been estimated to be approximately \$601 million (based on a 1999 cost study). SMEPA is responsible for 10% of the estimated cost and has submitted a formal plan to the NRC that demonstrated assurance that sufficient financial resources would be available at the time it becomes necessary to decommission. In addition, SMEPA received approval from the Internal Revenue Service to establish a "tax-free" grantor trust as a vehicle to fund the estimated decommissioning costs. SMEPA is currently funding \$1,050,000 on an annual basis through 2024. The estimated funding requirement is recalculated and adjusted periodically based on market changes.

The Energy Policy Act of 1992 has a provision that assesses nuclear utilities with fees for the decontamination and decommissioning of the DOE's past uranium enrichment operations. The decontamination and decommissioning assessments will last for fifteen years and will be used to set up a fund into which contributions from utilities and the federal government will be placed. SMEPA's initial aggregate liability was estimated at \$2,500,000 and is being paid in annual increments through 2007.

NOTE 4 - ELECTRIC UTILITY PLANT

Electric utility plant consisted of the following:

In thousands as of December 31,	Cost		Accumulated Depreciation	
	2004	2003	2004	2003
Grand Gulf Nuclear	\$ 422,420	\$ 414,203	\$ 205,569	\$ 193,758
Morrow Steam	192,670	191,730	143,400	138,047
Moselle Steam	25,092	23,996	22,627	22,617
Moselle Gas Turbine	21,750	21,723	4,901	4,250
Silver Creek/Sylvarena Gas Turbines	163,585	114,739	6,125	1,795
Bennedale/Paulding Gas Turbines	4,725	4,420	3,631	3,644
Total Generating Plant	830,242	770,811	386,253	364,111
Transmission Plant	186,876	179,429	58,533	55,340
General Plant and Equipment	24,723	20,854	12,818	11,906
Electric Plant Leased to Others	25,138	25,147	16,411	15,856
Electric Plant in Service	1,066,979	996,241	474,015	447,213
Construction Work in Process	87,846	111,894	(129)	(275)
Total Utility Plant	\$1,154,825	\$1,108,135	\$ 473,886	\$ 446,938

NOTE 5 - INVESTMENTS IN ASSOCIATED ORGANIZATIONS

Investments in associated organizations are stated at cost and consisted of the following:

In thousands as of December 31,	2004	2003
National Rural Utilities Cooperative Finance Corporation ("CFC") Certificates:		
Membership subscription	\$ 6,223	\$ 6,223
Loan and guarantee	5,363	29,059
Other	670	489
	\$ 12,256	\$ 35,771

CFC membership subscription certificates bear interest at a 5.0% rate and mature in 2070 through 2080. The loan and guarantee certificates bear interest at rates of 3.0%, 5.2% and 5.8% and mature in 2005 through 2007.

NOTE 6 - INVESTMENT SECURITIES

The amortized cost and related approximate fair values of investment securities were as follows:

In thousands as of December 31, 2004	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Decommissioning Trust:				
Equity mutual funds	\$ 13,488	\$ -	\$ 1,385	\$ 12,103
Fixed income mutual funds	2,896	56	-	2,952
	\$ 16,384	\$ 56	\$ 1,385	\$ 15,055

Securities to be held to maturity:

Obligations of states and political subdivisions	\$ 4,666	\$ 434	\$ -	\$ 5,100
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In thousands as of December 31, 2003

Decommissioning Trust:				
Equity mutual funds	\$ 11,137	\$ -	\$ 1,008	\$ 10,129
Fixed income mutual funds	2,508	81	-	2,589
	\$ 13,645	\$ 81	\$ 1,008	\$ 12,718

Securities to be held to maturity:

Obligations of states and political subdivisions	\$ 4,648	\$ 503	\$ -	\$ 5,151
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All investment securities to be held to maturity have contractual maturities providing for the securities to mature after five years but less than ten years from December 31, 2004. Actual maturities may differ from nominal maturities because of the borrowers' right to call or prepay obligations.

All temporarily impaired securities are equity mutual funds and are summarized below:

In thousands as of December 31, 2004	Estimated Fair Value	Unrealized Losses
Held less than 12 months	\$ 2,351	\$ 5
Held 12 months or more	9,752	1,380
	\$ 12,103	\$ 1,385

Sales of decommissioning trust assets by the trustee aggregated \$843,000 in 2003, resulting in a realized gain of \$6,000 in 2003. During 2004, there were no sales of investment securities.

Notes to Financial Statements

NOTE 7 - DEFERRED CHARGES (INCLUDING REGULATORY ASSETS)

The following is a summary of amounts recorded as deferred charges:

In thousands as of December 31,	2004	2003
Unamortized costs of abandoned plant	\$ 47,508	\$ 50,846
Unamortized penalties on repriced debt	20,793	22,884
Unamortized debt discount and issuance cost	500	577
Nuclear outage maintenance cost	1,129	157
Deferred DOE assessments (see Note 3)	560	712
Other	1,863	936
	<u>\$ 72,353</u>	<u>\$ 76,112</u>

Plans for constructing a second unit at the Grand Gulf site were terminated in 1989. SMEPA was to have been a 10% owner in the second unit and had invested approximately \$104 million, net of recoveries and transfers. With the written approval of the RUS, SMEPA is amortizing its remaining investment in the abandoned plant over a 27-year period ending in 2016, with such amortization being \$3,338,000 and \$3,253,000 in 2004 and 2003, respectively.

SMEPA repriced or refinanced significant amounts of its outstanding debt in recent years. As a condition of the transactions, SMEPA paid various prepayment penalties, which are treated as deferred charges to be amortized over the remaining life of the debt. Amortization of all such penalties was \$2,091,000 in 2004 and 2003.

In 2003, SMEPA repriced debt of \$44,300,000 and paid a penalty of \$2,161,000. The interest rate on the debt for the remaining life is 3.76%, repriced from 7.68%.

NOTE 8 - PATRONAGE CAPITAL

Patronage capital consisted of the following:

In thousands as of December 31,	2004	2003
Cumulative margins	\$ 102,570	\$ 96,900
Less: Retirements to date	5,854	5,854
	<u>\$ 96,716</u>	<u>\$ 91,046</u>

Under the provisions of debt covenants, until the patronage capital equals or exceeds forty percent of the total assets of SMEPA, the return to patrons of contributed capital is generally limited to twenty-five percent of the patronage capital or margins received by SMEPA in the prior calendar year. The patronage capital of SMEPA represents 11.0% and 10.4% of the total assets at December 31, 2004 and 2003, respectively.

NOTE 9 - LONG-TERM DEBT

Long-term debt consisted of the following:

In thousands as of December 31,	2004	2003
Mortgage notes payable in quarterly installments to Federal Financing Bank ("FFB") at interest rates varying from 3.657% to 10.705%, through 2030 to 2033	\$ 601,205	\$ 408,268
CFC advances at interest rates ranging from 4.20% to 6.45% to finance construction of new turbines	37,226	225,861
Mortgage notes payable in quarterly installments to CFC (4.20% at December 31, 2004, 2.55% in 2003), maturing in 2022	4,063	4,207
RUS mortgage notes payable in monthly or quarterly installments:		
2% notes maturing in 2009	1,624	2,946
5% - 5.75% notes maturing in 2015 through 2020	23,900	25,591
Mortgage notes payable in quarterly installments to CoBank (4.96% at December 31, 2004 and 2003), maturing in 2019	1,751	1,849
Lamar County, Mississippi, Pollution Control Bonds:		
1978 A Series, 6.125%, due semi-annually through 2008	645	805
1993 S Series, 4.65% to 4.95%, due annually through 2007	7,367	9,609
Claiborne County, Mississippi, Pollution Control Bonds:		
1985 G Series, variable interest rates (1.97% to 2.00% at December 31, 2004), due annually through 2015	33,845	35,545
	711,626	714,681
Less current maturities	35,050	33,921
Long-term debt (excluding current maturities)	<u>\$ 676,576</u>	<u>\$ 680,760</u>

In 2001, RUS approved a \$58,653,000 guaranteed loan from the FFB to SMEPA to finance the addition of transmission facilities. At December 31, 2004, the remaining unadvanced commitment was \$13,037,000.

In 2004, RUS approved a \$275,000,000 guaranteed loan from the FFB to SMEPA that provided permanent financing for its combustion turbine project (See Note 14). At December 31, 2004, the remaining unadvanced commitment was \$71,889,000. CFC had provided construction financing for the project in the form of a four-year loan. A condition of the CFC interim loan required SMEPA to purchase equity certificates in CFC and therefore CFC also provided a \$39 million loan to SMEPA for that purpose. The equity certificates earn interest income and are being redeemed as the \$275 million loan is repaid. At December 31, 2004 SMEPA owed \$32.6 million on the CFC loan related to the combustion turbine project and \$4.7 million on the equity certificate loan. Substantially all assets of SMEPA are pledged as collateral on long-term debt.

SMEPA is required by debt compliance covenants to maintain certain financial ratios of interest coverage and annual debt service coverage. SMEPA was in compliance with such requirements at December 31, 2004 and 2003.

Approximate annual maturities (scheduled periodic principal payments) of long-term debt for the next five years are as follows (in thousands):

2005	\$ 35,050
2006	40,503
2007	42,612
2008	42,045
2009	44,590
	<u>\$ 204,800</u>

Notes to Financial Statements

NOTE 10 - DEFERRED CREDITS AND OTHER LONG-TERM LIABILITIES

The following is a summary of deferred credits and other long-term liabilities:

In thousands as of December 31,	2004	2003
Deferred revenue (fuel cost adjustment)	\$ 1,389	\$ 8,653
Postretirement benefit obligation (other than pensions)	3,337	3,312
Deferred DOE assessments (see Note 3)	182	355
Miscellaneous	122	122
	<u>\$ 5,030</u>	<u>\$ 12,442</u>

The benchmark fuel cost adjustment rate approved by the Board and collected from Members may result in under-recovery or over-recovery of actual costs and cause a deferred charge or deferred credit. The deferred revenue (fuel cost adjustment) amounts of \$1,389,000 (2004) and \$8,653,000 (2003) were collected from Members in the year deferred and will be or have been recognized as revenue in the succeeding year.

NOTE 11 - SHORT-TERM BORROWINGS

SMEPA has a \$25,000,000 short-term line of credit available with CFC that is subject to renewal in September 2005 and a \$10,000,000 short-term line of credit with a bank that expires May 1, 2005. SMEPA had \$7,000,000 and \$2,600,000 of borrowings against the CFC line of credit at December 31, 2004 and 2003, respectively, at an interest rate of 4.05% and 2.8%, respectively and \$8,000,000 of borrowings against the bank line of credit at December 31, 2003, at an interest rate of 3.5%.

NOTE 12 - FAIR VALUES OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by SMEPA in estimating its fair value disclosures for financial instruments:

Cash and cash equivalents

The carrying amount reported in the balance sheets for cash and cash equivalents approximates fair value.

Investment securities

The fair values for debt and equity securities are based on quoted market prices when available and the present value of future cash flows discounted at a commensurate market rate. Medium-term CFC obligations have been estimated based upon published terms of recent issues of comparable instruments since quoted market prices are not available. See Note 6 for additional information.

Investments in associated organizations

The fair value of investments in associated organizations is not estimable since these instruments must be held by SMEPA and can only be returned to CFC. CFC requires SMEPA to hold these investments as a condition of CFC financing.

Notes payable and long-term debt

The carrying amount reported in the balance sheets for notes payable approximates fair value. The fair values of SMEPA's

long-term debt are estimated using discounted cash flow analysis based on SMEPA's current incremental borrowing rates for similar types of borrowing arrangements and rates which would be charged by the applicable issuer where appropriate.

The carrying amounts and approximate fair values of long-term debt, including current maturities, are as follows (in thousands):

	2004		2003	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
FFB	\$ 601,205	\$ 648,750	\$ 408,268	\$ 465,612
RUS	25,524	26,146	28,537	29,198
Pollution Control Bonds	41,857	42,219	45,959	46,690
CFC and CoBank advances and notes	43,040	43,040	231,917	231,917
	<u>\$ 711,626</u>	<u>\$ 760,155</u>	<u>\$ 714,681</u>	<u>\$ 773,417</u>

There was no material difference between the contract or notional amount and the estimated fair value of loan commitments. The aggregate estimated fair value amounts presented do not represent the underlying value of SMEPA and may not be indicative of amounts that might ultimately be realized upon disposition or settlement of these assets and liabilities.

NOTE 13 - EMPLOYEE BENEFITS

SMEPA sponsors a defined benefit plan that provides certain health insurance benefits to retired employees and their eligible dependents and also provides life insurance benefits to a closed group of seven employees who retired prior to January 1, 1990. The estimated costs of these benefits are accrued over the years that the employees render service. Payments relating to postretirement benefits other than pensions were approximately \$104,000 in 2004 and 2003, respectively.

The approximate periodic expense for postretirement benefits, other than pensions, included the following components:

In thousands as of December 31,	2004	2003
Service cost of benefits earned	\$ 62	\$ 57
Interest cost on accumulated benefit obligation	142	136
Amortization of actuarial gain	(75)	(75)
	<u>\$ 129</u>	<u>\$ 118</u>

The Accumulated Postretirement Benefit Obligation ("APBO") is accrued as an unfunded long-term liability and is composed of the following:

In thousands as of December 31,	2004	2003
Retirees and dependents	\$ 902	\$ 944
Fully eligible active plan participants	56	50
Active participants not yet eligible	1,285	1,149
Unrecognized gain	1,094	1,169
	<u>\$ 3,337</u>	<u>\$ 3,312</u>

The weighted average discount rate used in determining the APBO was 7.0 percent. The assumed health care cost trend rate of increase used in measuring the APBO is 7.5% in 2005, declining to 5.5 percent by the year 2009.

Notes to Financial Statements

The health care cost trend rate of increase assumption has a significant effect on the APBO and periodic expense. A one percentage point increase in the trend rate for health care costs would have increased the APBO by approximately 6.9% and service and interest costs by approximately 6.9%.

Substantially all of SMEPA's employees participate in the National Rural Electric Cooperative Association ("NRECA") retirement programs, which include both a defined benefit pension plan and a defined contribution pension plan. Both plans are qualified under Section 401 and are tax-exempt under Section 501(a) of the Internal Revenue Code. The defined benefit pension plan is a multi-employer plan available to all member cooperatives of NRECA, but the accumulated benefits and plan assets are not determined or allocated separately by individual employer. SMEPA incurred \$1,537,000 in pension expense for the defined benefit pension plan in 2004 and \$1,387,000 in 2003. SMEPA makes monthly payments to NRECA for the benefit of those employees who voluntarily participate in the defined contribution pension plan. SMEPA expenses the payments as they are accrued, and such expense amounted to \$495,000 and \$455,000 for 2004 and 2003, respectively.

SMEPA provides medical benefits to current employees through a managed care program. SMEPA makes payments during the year to a trust account controlled by an independent administrator for the claims and expenses considered appropriate. SMEPA recorded expenses amounting to \$1,403,000 and \$1,247,000, respectively, for the fiscal years ended December 31, 2004 and 2003.

NOTE 14 - COMMITMENTS AND CONTINGENCIES

In the normal course of doing business, SMEPA has entered into significant contractual commitments for coal, coal transportation, gas, and purchased power. The commitments require minimum annual purchases that extend through the year 2020. Such commitments are significantly less than anticipated purchases, and all such contractual costs are expected to be recovered through normal operating revenue.

SMEPA uses natural gas as the fuel for several of its generating units and also purchases power from others that use natural gas as fuel. A portion of natural gas purchases are subject to short-term changes in the market price for gas, and such market prices are quite volatile. In the normal course of operations, SMEPA enters into forward purchase commitments for certain quantities of gas at agreed-to prices. All such commitments are expected to be recovered through normal operating revenue.

SMEPA has a 20-year contract for rights to the output of a 280-megawatt gas-fired, combined-cycle combustion turbine-generator located near Batesville, Mississippi. SMEPA began monthly capacity payments in 2001, aggregating approximately \$20 million on an annual basis. SMEPA has the right to substantially direct how the generating unit is operated and also is obligated to pay for gas fuel consumed and certain operating and maintenance costs that will vary as the output for SMEPA's usage increases or decreases.

SMEPA has contracts for the purchase and installation of seven gas-fired combustion turbine-generators on three sites owned by SMEPA ("the combustion turbine project"). The total cost of the project is budgeted to be \$275 million including the purchase cost of the seven turbines, engineering and installation, transmission system improvements, internal costs and so forth. Five of the turbines were placed in service in 2003 and 2004, and one turbine each is scheduled to be placed in service in 2005 and 2006. The project includes four turbines rated at 84 megawatts each and three turbines rated at 47 megawatts each for a total of 477 megawatts. These natural gas fired simple cycle generators will be used to augment SMEPA's peaking resources and replace power previously purchased from other suppliers. SMEPA is using both internal funds and loan funds to pay for the project and total investment in the project was \$236.1 million and \$206.3 million at December 31, 2004 and 2003, respectively.

After conducting hearings on the matter, the Mississippi Public Service Commission ("MPSC") indicated in May 2000 that starting retail competition in the electric utility industry at that time was "premature" and not in the public interest. The MPSC indicated that it would monitor national developments and review the issue at a future date if appropriate. Management is unable to determine what effect, if any, changes related to retail competition in Mississippi would have on SMEPA's financial statements.

The FERC has issued rulings supporting major changes in the ownership and operation of transmission assets throughout the United States. While not regulated by FERC, SMEPA is monitoring what effect, if any, the presence of regional transmission organizations and the implementation of other FERC proposed rules will have on SMEPA's financial statements. SMEPA has over \$186 million invested in transmission assets as of December 31, 2004.

SMEPA is a defendant in certain litigation incurred in the normal course of business. Management, based on advice of legal counsel, is of the opinion that the ultimate resolution of such litigation will not have a material adverse effect on SMEPA's financial statements.