



Tennessee Valley Authority, 400 West Summit Hill Drive, Knoxville, Tennessee 37902-1401

April 18, 2016

TVARS Directors,

The health of the retirement system has caused concern among our retiree and employee populations, customers, ratepayers, and investors. I appreciate both the TVARS board and the TVA Board working to find ways to create a healthier retirement system that will be able to meet the needs of its members for the long-term.

We have reviewed your March 3, 2016 proposal and have some minor proposed changes. We appreciate the amount of time and effort that each side has contributed to create a fair compromise.

As both TVA and TVARS know, these changes are not made lightly. They address the current demographic, economic, business, and funding realities, and are intended to mitigate the impact to those who have less time to incorporate them into their retirement planning. The ultimate goal is to create a sustainable system over the long-term for all participants.

CHANGES TO THE MARCH 2016 TVARS PROPOSAL

- Members that joined the system on or after January 1, 1996, will not be able to contribute additional money to the "fixed fund" accounts.
- Except for those that joined the system prior to January 1, 1996, the interest crediting rate on all cash balance and fixed fund accounts will be the Consumer Price Index (CPI) plus 2 percent. The minimum interest crediting rating will be TVARS projected rate of return (ASC 960) minus 2 percent. The maximum crediting rate will be TVARS projected rate of return (ASC 960) minus 0.50 percent. The interest credit rating will not change for members that joined the system prior to January 1, 1996.
- The total monthly cap on the additional supplemental benefit will remain unchanged at \$150/month.
- To maintain the current structure and balance of the TVARS board, all references to a "supermajority" will be a majority except in the case of the removal of a TVARS Director by the TVARS board. TVA defers to the TVARS board on this disciplinary process.
- Lump sum cash outs and cash balance transfers will be paid out of the TVARS system assets.
- Any changes to the investments or asset allocation that changes the projected rate of return (ASC 960) to system assets will be provided to TVA for review and agreement. If no action is taken by TVA within 60 days, the changes would automatically go into effect.

COMPROMISE PROPOSAL- SPECIFICS

Proposed rules amendments would be prepared to incorporate the following changes to be effective October 1, 2016. This list represents the entirety of proposed changes and supersedes previous proposals.

Cash Balance to Defined Contribution (401k)

Participants in the cash balance benefit system that joined on or after January 1, 1996, and have less than 10 years of service on the date the rules are implemented will be transitioned to a 401(k) only plan. Their balance in the cash balance account, as of the effective date, will continue to accrue interest credits. New retirement benefits going forward will be in a 401(k) only account. As a part of this transition, TVA will provide a 6 percent automatic contribution and 100 percent match on up to an additional 6 percent of employee contributions. This provides a very competitive employer contribution of up to 12 percent by TVA into the 401(k) account of these affected employees.

Cash Balance participants that joined before January 1, 1996, will remain in the current cash balance system with no changes.

Cash Balance participants that joined on or after January 1, 1996, but have more than 10 years of service will move into a modified cash balance benefit system which includes 3 percent pay credits into a cash balance account, 3 percent automatic 401(k) contribution by TVA, and a 75 percent match by TVA on voluntary employee contributions of up to 6 percent in the 401(k).

Employees that joined after July 2014 will not be affected.

Fixed Fund

The ability to contribute after-tax dollars to the fixed fund will be suspended for all cash balance benefit system employees who joined TVA on or after January 1, 1996. Contributions currently in the fixed fund and any future contributions will accrue interest at the rate of CPI plus 2 percent. The minimum interest crediting rate will be TVARS' projected rate of return minus 2 percent, and the maximum will be TVARS projected rate of return minus 0.50 percent.

Lump Sum Payout

Employees in the cash balance benefit system will be given the option to receive their entire cash balance account and value of their supplemental benefit in cash upon retirement. This cash out option would not include cost of living adjustments (COLAs). These lump sum cash outs will be paid for utilizing TVARS' assets.

Interest Crediting Rate on Cash Balance Accounts

The interest crediting rate on cash balance benefits system accounts for those participants that joined prior to January 1, 1996, will not change. The interest crediting rate on all other cash balance accounts will be reduced to the CPI plus 2 percent. The minimum crediting rate will be TVARS projected rate of return minus 2 percent, and the maximum crediting rate will be TVARS' expected asset return less 0.50 percent.

COLA

A certain vested COLA would be provided to participants. The maximum COLA on a benefit in any one year would be 6 percent. The minimum would remain at 0 percent. The calculation of the COLA amount would change to CPI minus 0.25 percent.

COLA Eligibility Age

For those employees and retirees under the age of 50 on October 1, 2016, the eligibility for a COLA increase on pension or supplemental benefits will begin at actual age 65.

COLA Salary Cap

For original plan participants, the COLA increase on pension benefits will apply only on earnings up to Executive Level IV. No TVARS COLA will be received for SERP participants with less than 10 years of service.

Supplemental Benefit

The cap on the supplemental benefit will be \$12.36 per month per year of service. The cap on the additional benefit will remain unchanged at \$150 per month. The current caps are \$15 and \$150. Those participants with more than 10 years of service will continue to accrue additional years of service toward the supplemental benefit. Those with less than 10 years of service will receive a prorated \$150 per month cap based on current years of service. The current rule of 10 years of service and actual age 55 to be eligible for the supplemental benefit will remain.

Contributions

TVA will make a minimum contribution commitment of \$300 million (or the minimum formula calculation, whichever is greater) per year over the next 20 years to the system or until it is 100 percent funded. TVA will have the ability to prepay contributions. The TVARS board will have the ability to suspend contribution requirements with a majority approval vote of the TVARS board.

Investments

Any changes to the investments or asset allocation that changes the projected rate of return to system assets will be provided to TVA for review and agreement. If no action is taken by TVA within 60 days, the changes will automatically go into effect. The review by TVA will not apply in the event of plan termination. This right of review is for the TVA Board's oversight of its contributions to the Retirement System, and by granting TVA this right we understand that TVARS is not delegating, nor is TVA assuming, any additional duties to members of the Retirement System.

401(k)

No change to the current rules, which provide that a change to the 401(k) contribution amounts will require a majority vote of the TVARS board subject to TVA's existing veto authority.

Governance

The TVARS board is making additional amendments to the rules to provide for a disciplinary process for TVARS directors. TVA defers to the TVARS board on this matter.

TVARS will also provide that the seventh member be a retiree and will explore naming an emergency (in the event of resignation or inability to serve) standing seventh member to serve in the seat until a formal selection process can be conducted and the seat voted on by the TVARS board. It is envisioned this would be a TVARS advisor, external expert, or other pension related expert that is familiar with the TVARS system. The seventh member's term will continue until a replacement is chosen by the TVARS board.

Other Items

The TVARS board agrees to adopt additional amendments to the TVARS Rules and Regulations and 401(k) plan that will offer employees remaining in the cash balance structure the option to voluntarily switch their future participation to the 401(k) only plan with 6 percent automatic contributions from TVA and 100 percent match on up to an additional 6 percent of employee contributions. This voluntary election may also include the additional option to allow employees to transfer their existing cash balance accounts to the 401(k) plan. These are subject to IRS review and approval.

TVARS Directors
Page 5
April 18, 2016

Thank you for your continued work on this matter.

Sincerely,

A handwritten signature in black ink, appearing to read "William D. Johnson". The signature is fluid and cursive, with a long horizontal stroke at the end.

William D. Johnson
President and Chief Executive Officer