

T E N N E S S E E V A L L E Y A U T H O R I T Y

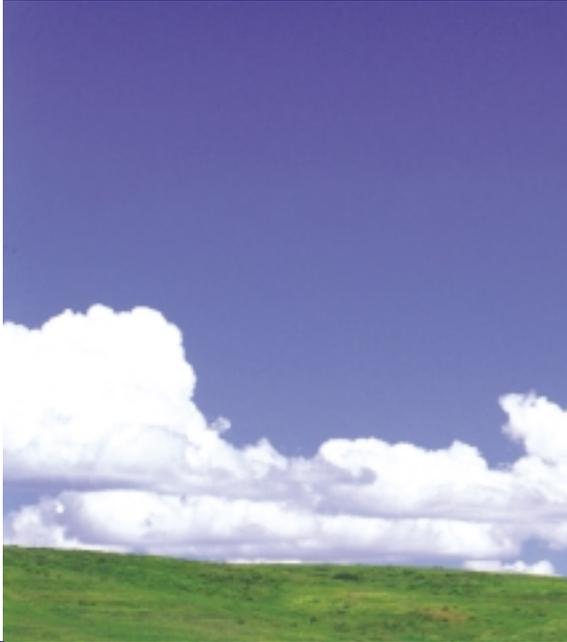


Retirement System

2001 | Annual Report



2001





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Dear Members:

The TVA Retirement System Board of Directors is pleased to submit the System's 2001 Annual Report. Fiscal year 2001 was a year of turbulent market conditions, and, in general, a slowing of the economy. This has resulted in a decrease in market value of the System's assets. At September 30, 2001, the System's assets for the Fixed Benefit Fund totaled \$5.8 billion, down from \$7.3 billion at the end of fiscal year 2000. Despite the market downturn, the System continues to be in strong financial condition.

The Board is committed to its investment strategy of emphasizing long-term, broadly diversified investments. To this end, the Board continually monitors the System's asset allocation policy and the ratio of assets to liabilities to ensure adequate funding for all future obligations. During the year, the Board adopted the following asset allocation policy for investment of the System's funds: 48 percent of the assets to U.S. equities, of which 5 percent may be private equity or other similar alternative investments; 40 percent to fixed income investments; and 12 percent to international equities. To further diversify the investment mix, the Board approved the hiring of five new investment managers, three of which manage private equity allocations, a new asset class. The System currently employs 23 investment managers. Each manager periodically meets with the Board to report on investment performance.

During the year, the Board approved a 3.24 percent cost-of-living increase in the monthly pension and the supplemental benefit for retirees, approved a 6.24 percent annual interest rate for Cash Balance Benefit Structure participants, and changed the 401(k) Plan to a four-tier structure that provides participants with over 200 investment options. The staff continued to offer educational benefit seminars to employees through a partnership with Fidelity Investments and TVA University.

The Board and staff remain committed to their goal of providing to TVA employees, retirees, and beneficiaries the very best retirement services. Your continued support and input is encouraged.

Sincerely,

A handwritten signature in cursive script that reads "Lewis E. Wallace".

Lewis E. Wallace
Chairman

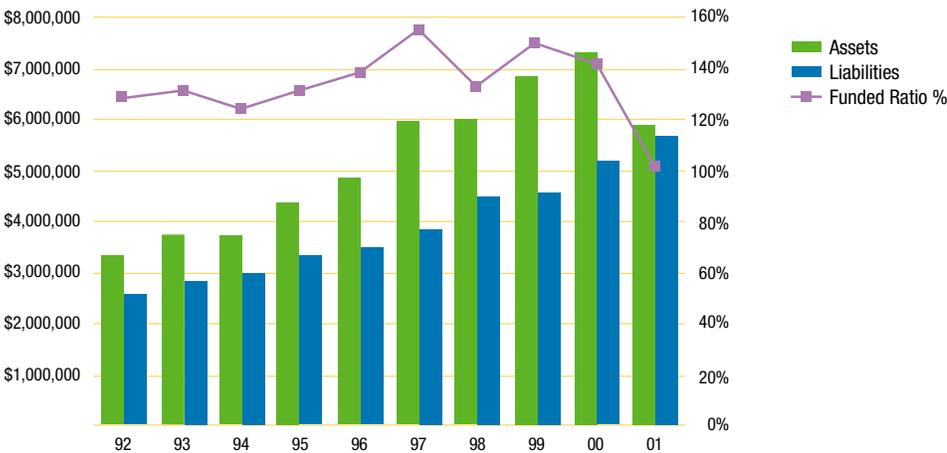
(Dollars in thousands)

	2001	2000	Change	% Change
Net Assets Available for Benefits				
Fixed Benefit Fund	\$5,872,752	\$7,310,976	\$(1,438,224)	(20)
Variable Annuity Fund	299,457	460,836	(161,379)	(35)
TVA Savings and Deferral Retirement Plan [401(k) Plan]	827,746	1,057,328	(229,582)	(22)
Total	\$6,999,955	\$8,829,140	\$(1,829,185)	(21)
Contributions				
Employer	\$ 11,649	\$ 12,579	\$ (930)	(7)
Employee (all funds)	\$ 83,750	\$ 84,071	\$ (321)	-
Benefits Paid (all funds)	\$ 385,753	\$ 367,320	\$ 18,433	5
Accumulated Benefit Obligation (Fixed Benefit Fund)	\$5,632,600	\$5,342,100	\$ 290,500	5
Number of Active Members	13,245	12,910	335	3
Number of Retirees	21,255	21,055	200	1

Fixed Benefit Fund

MARKET VALUE OF ASSETS AND LIABILITIES, AND FUNDED RATIO—SEPTEMBER 30

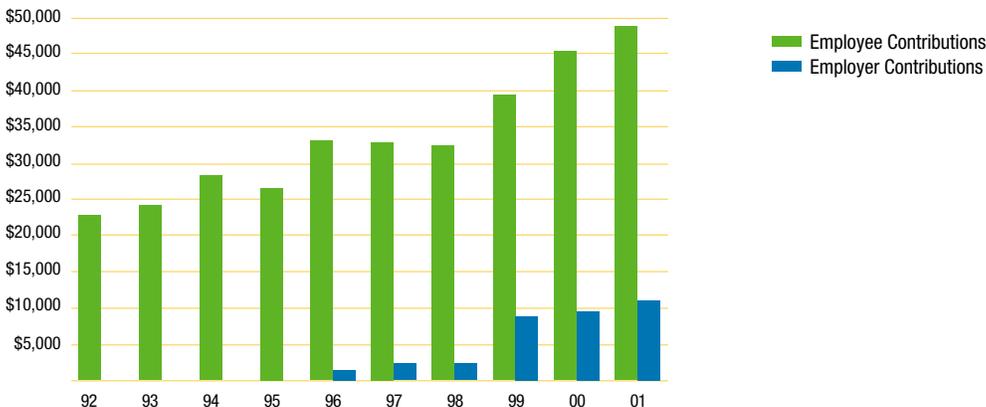
(thousands)



In fiscal year 2001, domestic and international equities declined over 28 percent. This decline was partially offset by a 13 percent increase in the bond market. Because of the Fixed Benefit Fund's strong financial condition and its diversified asset mix of stocks and bonds, the Fixed Benefit Fund ended the fiscal year 104 percent funded.

401(k) Plan Contributions

(thousands)



Total assets in the 401(k) Plan, predominantly invested in equity funds, decreased 22 percent for the fiscal year. Employee contributions continued to increase at \$48 million in fiscal year 2001, while TVA matching contributions increased over 21 percent from last year to \$11.6 million.

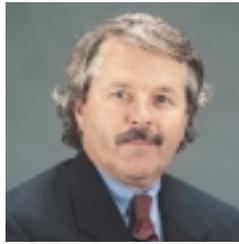
Board of Directors

**Elected
by Members**



Floyd J. Johnson
Elected November 1, 1995

**Appointed
by TVA**



John E. Long, Jr.
Appointed April 27, 1992

**Selected by
Other Directors**



Gretchen D. Thal
Elected February 3, 1997



William M. Oden
Appointed January 27, 1995



Lewis E. Wallace
Selected November 1, 1994



Robert H. Cash
Elected November 1, 1997



Mark O. Medford
Appointed November 6, 1995

Standing Committees**Audit**

William M. Oden, Chair
Mark O. Medford
Gretchen D. Thal

Election

Robert H. Cash, Chair
William M. Oden
Gretchen D. Thal

Investment

John E. Long, Jr., Chair
Robert H. Cash
Floyd J. Johnson
Mark O. Medford
William M. Oden
Gretchen D. Thal
Lewis E. Wallace

Retirement

Floyd J. Johnson, Chair
Robert H. Cash
John E. Long, Jr.
Mark O. Medford

Board Officers

Lewis E. Wallace
Chairman

Floyd J. Johnson
Vice Chairman

Randy A. Snyder
Executive Secretary

Robert J. Vaughn
Assistant Secretary and
Assistant Treasurer

Sherry C. Kelly
Treasurer

Richard A. Boyd
Assistant Treasurer

Robert G. McCall
Assistant Treasurer

Pamela K. Ramsey
Assistant Treasurer

Professional Advisors**Actuary**

William M. Mercer, Incorporated
Atlanta

Auditors

PricewaterhouseCoopers LLP
Knoxville

E.H. Johnson & Company, P.C.
Knoxville

Investment Consultant

Wilshire Associates Incorporated
Pittsburgh

Legal Counsel

Nicholas P. Goschy
Senior Attorney
TVA, Knoxville

Master Trustee

Mellon Bank NA
Pittsburgh

Medical Advisor

A. Estes Felker, M.D.
Chattanooga

Medical Board

Maurice S. Rawlings, M.D.
Chairman, Chattanooga

Deborah D. Barton, M.D.
Knoxville

Robert W. Myers, M.D.
Chattanooga

Investment Managers**Fixed Benefit Fund**

Abbott Capital Private Equity Partners IV, L.P.

BlackRock Financial Management Inc.

BlackRock International, Ltd.

Bradford & Marzec, Inc.

David J. Greene and Company, LLC

David L. Babson & Company Inc.

Geewax, Terker & Company

Goldman Sachs Asset Management

J.P. Morgan Fleming Asset Management

MacKay Shields LLC

Mellon Bond Associates, LLP

Mellon Capital Management

Nicholas-Applegate Capital Management

Pacific Investment Management Company

Smith Breeden Associates Inc.

T. Rowe Price International, Inc.

Taplin, Canida & Habacht

Wellington Management Company, LLP

Western Asset Management Company

Wilshire Associates Incorporated

W.R. Huff Asset Management Co., L.L.C.

WRH Partners Global Securities, L.P.

WRH Partners II, L.L.C.

Variable Annuity Fund

Mellon Capital Management Corporation

Mellon Employee Benefit Solutions



Currently one of the largest pension plans in the world, the TVA Retirement System provides retirement, disability, and death benefits for approximately 35,000 employees and retirees.

Established in 1939, the TVA Retirement System (System) is a defined benefit plan (Plan) covering most full-time and part-time annual employees. The System is a separate legal entity from TVA and is under the control and direction of a seven-member Board of Directors. Three of the directors are appointed by TVA, and three are elected by and from the membership. A seventh director is selected by the other six. The System Board also has responsibility for administration of a defined contribution plan, the TVA Savings and Deferral Retirement Plan [401(k) Plan].

TVA contributes to the System such amounts as are necessary on an actuarial basis to provide the System with assets sufficient to meet TVA-financed benefit obligations to be paid to members. While members are not required to make contributions to the System, certain members are eligible to make voluntary contributions to the System's Fixed and/or Variable Annuity Funds. Members can also contribute to the 401(k) Plan, and TVA makes matching contributions to that Plan.

Retirement Benefits

A member's retirement benefit consists of a pension derived from TVA's contributions and earnings on Plan assets and a Social Security benefit derived from both TVA's and the member's contributions. A member's retirement benefit may also include an annuity and/or a lump-sum benefit derived from the member's contributions to the Fixed and/or Variable Annuity Funds and the 401(k) Plan. The pension plus the annuity, if applicable, compose the TVA Retirement System retirement allowance. In addition, a supplemental benefit is provided to eligible retirees which may be used to help with the cost of medical insurance.

Original Benefit Structure

The pension from the Original Benefit Structure is based on the member's years (to the nearest month) of creditable service, highest average base pay during any three consecutive years of creditable service, and a pension factor, less a Social Security offset.

Creditable service is the length of time spent as a member of the System. It also includes any annual leave forfeited after January 1, 1980, and, at the member's election, the total balance of any unused sick leave. Leave is counted hour for hour for the first 1,000 hours and 2 hours for each hour in excess of 1,000 hours (2,080 hours equates to one year of creditable service). Forfeited annual leave and unused sick leave may be used in determining both the amount of the benefit and the eligibility for retirement. Creditable service may also include previous periods of membership in the System, certain military service, and some periods of leave without pay.

Members with at least 5 years of creditable service who are at least attained age 55 are always eligible to receive an immediate benefit. Vested members less than attained age 55 may also receive an immediate benefit unless they are terminated for cause. Members who are at least actual age 45 and whose age plus creditable service equals 80 or more receive the maximum pension factor of 1.3 percent. Vested members who are at least attained age 60 also receive the maximum pension factor even if they do not have 80 points.

Cash Balance Benefit Structure

The System implemented the Cash Balance Benefit Structure for employees who became members on or after January 1, 1996, with no prior Retirement System membership. Employees rehired by TVA after a break-in-service of 180 or more consecutive days and who have previous service as participants in the Original Benefit Structure are given an opportunity to participate in the Cash Balance Benefit Structure when they are rehired or at the time they become eligible for System membership.

The Cash Balance Benefit Structure provides a TVA-funded pension benefit where an account is established for each member. This account receives pay credits each pay period equal to 6 percent of compensation, as well as interest credits each month at the rate established by the Board each January 1. The interest rate is determined by

calculating the percentage change of the 12-month average of the Consumer Price Index (CPI) for the period ending the previous October 31 over the preceding 12-month period, plus 3 percent. The System has established a minimum annual interest rate of 6 percent for interest credits.

Cash balance service is the length of time spent as a member of the System. It does not include credit for unused sick leave, forfeited annual leave, or pre-TVA employment military service. Cash balance service may include previous periods of membership in the System and some periods of leave without pay.

Members with at least 5 years of cash balance service who are at least actual age 55 are always eligible to receive an immediate benefit. Vested members less than actual age 55 may also receive an immediate benefit unless they are terminated for cause.

Supplemental Benefit

If upon retirement a member meets the eligibility criteria, the member will receive a supplemental benefit regardless of the member's benefit structure. This benefit is provided to eligible retirees and eligible surviving spouses to help with the cost of their medical insurance, although it is not required to be used to pay for medical insurance.

Level Income Plan

Regardless of the member's benefit structure, if a member chooses the level income plan, the System will increase the TVA pension payments until age 62, when early Social Security payments can begin. Then, once the member is eligible to receive Social Security payments, the level income plan increase stops and the TVA pension payments are reduced. To be eligible for the level income plan, a member must be under age 62 and must have earned enough quarters of Social Security coverage at the time of retirement to be eligible for a Social Security benefit at age 62.

Annuity and 401(k) Plan

During Employment

The annuity provides two after-tax investment options to members, the Fixed Benefit Fund and the Variable Annuity Fund. These funds are available to members who are or have ever been participants in the Original Benefit Structure unless they have transferred their annuity fund balance(s) to the 401(k) Plan. The Fixed Benefit Fund earns a specified rate of interest set by the System's Board of Directors (currently 10 percent). The

Variable Annuity Fund is invested in the Dreyfus Basic S&P 500 Stock Index Fund. Employees participating in the Variable Annuity Fund purchase shares in the Dreyfus Basic S&P 500 Stock Index Fund, which is invested in the stocks of companies included in the S&P 500 Composite Stock Price Index.

Members are also permitted to transfer their contributions between the Fixed Benefit Fund and the Variable Annuity Fund once per calendar month and may, at any time during employment, transfer their entire balance to the 401(k) Plan. Members who transfer their balance to the 401(k) Plan are no longer eligible to contribute to the Fixed Benefit Fund or the Variable Annuity Fund. Upon retirement, members may transfer all or any portion of their after-tax balance(s) in the 401(k) Plan to the System to receive monthly payments.

In addition, members may elect to participate in the 401(k) Plan on a before- and/or after-tax basis. TVA provides 401(k) Plan employer matching contributions for members participating in the Cash Balance Benefit Structure and the Original Benefit Structure. The amount of this match for Cash Balance Benefit Structure participants is 75 cents on every dollar contributed on a before- and/or after-tax basis up to a maximum of 4.5 percent of fiscal year-to-date base compensation. The amount of this match for Original Benefit Structure participants is 25 cents on every dollar contributed on a before- and/or after-tax basis up to a maximum of 1.5 percent of fiscal year-to-date base compensation. Investment options available through the 401(k) Plan have varying degrees of risk and potential return.

In calendar year 2001, contributions to the Fixed Benefit Fund, Variable Annuity Fund, and 401(k) Plan may not exceed the lesser of \$35,000 or 25 percent of calendar year-to-date compensation. Higher paid employees are subject to further limitations on before-tax contributions to the 401(k) Plan. Additionally, before-tax contributions may not exceed the annually published IRS maximum (\$10,500 for 2001).

After Retirement

A member may receive a monthly annuity payment from the Fixed Benefit Fund, the Variable Annuity Fund, or both. Annuity payments from the Fixed Benefit Fund are based on a specified rate of interest set by the System's Board of Directors. Members who elect to receive an annuity payment from the Variable Annuity Fund will have their shares in the Dreyfus Basic S&P 500 Stock

Index Fund redeemed and the proceeds used to purchase units in the Variable Annuity Fund. The monthly annuity payments will vary based on the value of these units. The investment strategy of the Variable Annuity Fund is the same as the Dreyfus Basic S&P 500 Stock Index Fund.

Social Security

A retired member may be eligible to receive Social Security benefits at age 62, or earlier for disability. The Social Security Administration determines eligibility for Social Security benefits.

Survivor Options

At Retirement

A member decides whether to take the maximum monthly retirement allowance during the member's lifetime with nothing payable after death or to take a reduced amount and provide benefits for a survivor.

All of the many survivor options are the actuarial equivalent of the maximum retirement allowance. Married members who first become members of the System after January 1, 1990, must designate their spouse as beneficiary to receive a survivor benefit as specified by the Rules and Regulations of the Retirement System (Rules) governing the defined benefit plan, or receive their spouse's written consent to select a different survivor option at retirement.

After Retirement

Retirees who marry or remarry after commencement of their retirement allowance may elect to designate their new spouse for either a 50 percent or 100 percent survivor benefit.

Retirees have 90 days from the date of such marriage or remarriage to elect this second survivor benefit. This election and actuarial reduction to the retirement benefit would be effective the first day of the month following the first anniversary of the marriage or remarriage. Previous survivor benefit elections remain in effect.

Disability Benefits

A vested member may be retired on disability retirement if it is determined that the member cannot be continued in the present position because of a physical or mental disability that is likely to be permanent and that there is no other TVA position available for which the member is qualified and can perform with the member's medical restrictions.

Death Benefits

During Employment

The designated beneficiary or the estate of a member who dies during employment will receive the member's accumulated contributions, if applicable, and a benefit provided by TVA's contributions.

After Retirement

Upon the death of a member after retirement, the benefits payable (if any) depend upon the survivor option selected.

Cost-of-Living Increases

Eligible retirees receive cost-of-living increases on the pension portion of monthly benefits (exclusive of level income plan) in January following any year in which the 12-month average of the CPI exceeds by as much as 1 percent the CPI average for the preceding year. The amount of the adjustment is the percentage increase in the CPI, up to 5 percent in any one year. The System's Board may, with the approval of the TVA Board, apply an increase greater than 5 percent.

Eligible retirees and beneficiaries on the retirement payroll on or before January 1 receive the cost-of-living increase. If a member retires after January 1, that member's pension will be at least as much as it would have been on January 1 with the cost-of-living increase if the member was eligible to retire on January 1.

The supplemental benefit will receive an annual cost-of-living increase until it reaches the maximum as specified in the Rules, at which time the cost-of-living increases will stop.

System Termination

In the event the System is terminated, the net assets of the Plan will be allocated generally to provide benefits in the following order: (1) benefits based upon members' contributions, (2) nonforfeitable benefits based upon TVA's contributions, and (3) if feasible, cost-of-living increases thereto.

This summary is intended to help members understand the System and its benefits under the defined benefit plan and the 401(k) Plan. The rules governing these plans, not this summary, are used to determine the benefits to which a member is entitled. For additional information about your Retirement System benefits, please contact Retirement Services at the location or numbers listed on the back of this report.



Report of Independent Accountants

*Board of Directors
Tennessee Valley Authority Retirement System*

In our opinion, the accompanying statements of net assets available for benefits and the related statements of changes in net assets available for benefits present fairly, in all material respects, the net assets available for benefits of the Tennessee Valley Authority Retirement System (the System) Fixed Benefit Fund, the Variable Annuity Fund, and the TVA Savings and Deferral Retirement Plan at September 30, 2001 and 2000, and the changes in net assets available for benefits for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the System's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Knoxville, Tennessee
November 30, 2001

Statements of Net Assets Available for Benefits

September 30, 2001 and 2000

(Dollars in thousands)

	2001	2000
Assets		
Investments at fair value	\$6,184,137	\$7,597,874
Receivables		
Dividends and interest	43,370	51,107
Securities sold	140,445	177,529
Due from Variable Annuity Fund	5	368
Other	14,841	382
Total assets	<u>6,382,798</u>	<u>7,827,260</u>
Liabilities		
Accounts payable		
Securities purchased	504,620	496,955
Due to Variable Annuity Fund	7	78
Other	5,419	19,251
Total liabilities	<u>510,046</u>	<u>516,284</u>
Net Assets Available for Benefits	<u>\$5,872,752</u>	<u>\$7,310,976</u>

Statements of Changes in Net Assets Available for Benefits

Fiscal Years ended September 30, 2001 and 2000

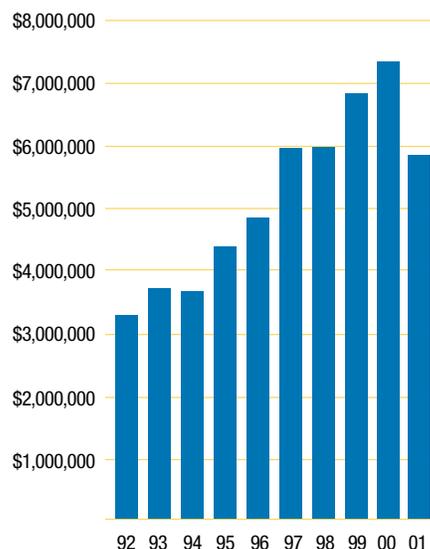
(Dollars in thousands)

	2001	2000
Investment Income		
Net appreciation (depreciation) in fair value of investments	\$(1,454,356)	\$ 466,836
Interest	276,713	274,552
Dividends	41,050	43,547
	<u>(1,136,593)</u>	<u>784,935</u>
Less investment expenses	22,714	21,090
	<u>(1,159,307)</u>	<u>763,845</u>
Contributions		
TVA	—	3,000
Members	28,581	28,275
Transfers from Variable Annuity Fund	35,089	19,753
Transfers from 401(k) Plan	3,699	2,855
	<u>67,369</u>	<u>53,883</u>
Total increase (decrease)	<u>(1,091,938)</u>	<u>817,728</u>
Benefits, Transfers, and Expenses		
Retirement benefits	297,855	272,244
Death benefits	3,636	3,545
Withdrawals	6,610	13,435
Administrative expenses	4,098	3,663
Transfers to 401(k) Plan	21,698	32,466
Transfers to Variable Annuity Fund	12,389	23,245
Total benefits, transfers, and expenses	<u>346,286</u>	<u>348,598</u>
Net increase (decrease)	<u>(1,438,224)</u>	<u>469,130</u>
Net Assets Available for Benefits		
Beginning of year	7,310,976	6,841,846
End of year	<u>\$ 5,872,752</u>	<u>\$7,310,976</u>

The accompanying notes are an integral part of the financial statements.

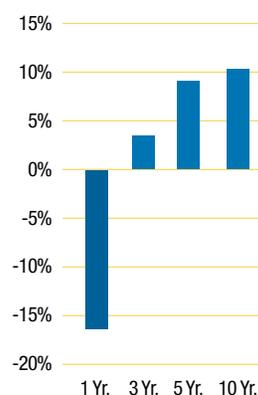
Fixed Benefit Fund

NET ASSETS AVAILABLE FOR BENEFITS
(thousands)



Fixed Benefit Fund

ANNUALIZED RATE OF RETURN



NOTES TO FINANCIAL STATEMENTS

Significant Accounting Policies**General**

The TVA Retirement System (System) is a defined benefit plan (Plan) covering most full-time and part-time annual employees. The System is administered and controlled by an independent, seven-member Board of Directors which also administers a defined contribution plan, the TVA Savings and Deferral Retirement Plan [401(k) Plan]. The System provides retirement, disability, and death benefits. There are two benefit structures within the Plan: the Original Benefit Structure and the Cash Balance Benefit Structure. New members hired on or after January 1, 1996, with no prior Retirement System membership must participate in the Cash Balance Benefit Structure. Employees who were members of the System as of December 31, 1995, were given the opportunity to either participate in the Cash Balance Benefit Structure or to remain in the Original Benefit Structure.

There are two investment funds within the Plan: the Fixed Benefit Fund and the Variable Annuity Fund. TVA contributes to the Fixed Benefit Fund such amounts as are necessary on an actuarial basis to provide assets sufficient to meet TVA-financed benefits to be paid to members. Participants in the Original Benefit Structure and participants in the Cash Balance Benefit Structure who were members of the System as of December 31, 1995, have a choice of making contributions to the Fixed Benefit Fund, the Variable Annuity Fund, or both. New members hired on or after January 1, 1996, participating in the Cash Balance Benefit Structure, are not eligible to contribute to the Fixed Benefit Fund or the Variable Annuity Fund.

TVA's contributions are deposited in the Fixed Benefit Fund. Members' contributions in the Fixed Benefit Fund were credited an annual rate of interest of 10 percent for the years ended September 30, 2001 and 2000. For participants in the Cash Balance Benefit Structure, TVA provided matching contributions of 75 cents on every dollar contributed to the 401(k) Plan on a before- and/or after-tax basis, with maximum matching contributions of 4.5 percent of fiscal year-to-date base compensation. Participants in the Original Benefit Structure received employer matching contributions of 25 cents on every dollar contributed on a before- and/or after-tax basis, with maximum matching contributions of 1.5 percent of fiscal year-to-date base compensation.

Benefits are provided in the form of a pension funded by TVA contributions and, if eligible, an annuity derived from the members' contributions. The Fixed Benefit Fund contains assets for funding of both the pension and annuity with the net assets available for benefits being allocated between members' and TVA's contributions (see note on Net Assets Available for Benefits).

A more detailed description of contributions, benefits, vesting, and funding is available from the TVA Retirement System.

Valuation of Investments

Investments held in the Fixed Benefit Fund are stated at fair value which is determined by the Trustee of the fund as follows: common stocks, notes, and commingled trust funds are stated at the last closing sale price for securities listed on national exchanges or the last bid price for securities traded over the counter. All investments such as bonds and temporary investments for which there are no quoted prices are valued based on market values of comparable securities.

During fiscal year 2001, the Board amended the asset allocation policy that 5 percent of the United States equity allocation may be invested in private equity or other similar alternative investments but not to include holding title to real property. The 5 percent is measured as a percentage of the total funds. The private equity and other similar alternative investments are reported at market value, which is based on market quotations if available. For investments where no readily ascertainable market value exists, funds are valued by independent appraisals or investment management judgment.

Derivatives

Investments are held in S&P futures and bond futures of approximately \$709 million in fiscal year 2001 and \$718 million in fiscal year 2000. These futures are held to generate earnings and are valued at quoted market values with gains and losses reflected in the Statements of Changes in Net Assets Available for Benefits.

Options are held in foreign currency futures to reduce loss due to changes in the exchange rates. The risk management asset (liability) of the foreign currency futures is approximately \$(82) million in fiscal year 2001 and \$60 million in fiscal year 2000. The futures are related to the foreign stocks and bonds portfolio of \$888 million in fiscal year 2001 and \$1,102 million in fiscal year 2000.

Options are also held in bond futures primarily to reduce loss due to changes in interest rates. The risk management asset (liability) of the bond futures is approximately \$(71) million in fiscal year 2001 and \$136 million in fiscal year 2000. The bond futures are related to the \$2.1 billion domestic fixed income security portfolio in fiscal year 2001 and \$2.7 billion in fiscal year 2000.

Investment Income

The Plan presents in the Statements of Changes in Net Assets Available for Benefits the net appreciation (depreciation) in the fair value of its investments which consists of the realized

gains or losses and the unrealized appreciation (depreciation) on those investments. Dividend income is recorded on the ex-dividend date, and interest income is recorded as earned on an accrual basis.

Member Contributions

Eligible members may voluntarily contribute to either the Fixed Benefit Fund, the Variable Annuity Fund, or both. Federal income tax is deferred on earnings until annuity payments start or withdrawals are made. Members are also permitted to transfer their contributions between the Fixed Benefit Fund and the Variable Annuity Fund once per calendar month and may, at any time during employment, transfer their entire balance to the 401(k) Plan. Members who transfer their balance to the 401(k) Plan are no longer eligible to contribute to the Fixed Benefit Fund or the Variable Annuity Fund. Upon retirement, members may transfer all or any portion of their after-tax balance in the 401(k) Plan to the System to receive monthly payments.

Termination

In the event the System terminates, the net assets will be allocated generally to provide benefits in the following order: (1) benefits based upon members' contributions (if applicable), (2) nonforfeitable benefits based upon TVA's contributions, and (3) if feasible, cost-of-living increases thereto.

Amendment to the Rules and Regulations

During fiscal year 2001, the Rules were amended to change the definition of wages and salaries in determining pension benefits at retirement. Wages and salaries now include certain lump-sum payments made in lieu of base wage or salary increases for fiscal years 1998 through 2002. Wages and salaries also now include lump-sum payments for certain TVA performance incentive plans beginning in fiscal year 2000.

Actuarial Assumptions

Accumulated benefits are those future periodic payments, including single-sum payments, that are attributable under the System's provisions to the service members have rendered and contributions members have made. Accumulated benefits include benefits expected to be paid to (1) retired or terminated members or to their beneficiaries, (2) beneficiaries of members who have died, and (3) current members or their beneficiaries.

Pension benefits under the System's Original Benefit Structure are based on members' years (to the nearest month) of creditable service, highest average base pay during any three consecutive years of creditable service, and a pension factor, less a Social Security offset. Calculations of the accumulated pension benefits

for active employees are based on their average compensation during the last three years ending on the valuation date.

Pension benefits under the System's Cash Balance Benefit Structure are based on pay credits and interest credits which accumulate over the members' cash balance service. Pay credits accumulate at a rate equal to 6 percent of members' compensation, and interest is credited each month at the rate established by the Board each January 1. The interest rate will be determined by calculating the percentage increase of the 12-month average of the Consumer Price Index (CPI) for the period ending the previous October 31 over the preceding 12-month period, plus 3 percent. The System has established a minimum annual interest rate of 6 percent for interest credits.

Benefits payable under all circumstances—retirement, death, disability, and termination of employment—are included to the extent they are deemed attributable to members' service rendered to the valuation date.

The actuarial present value of accumulated benefits is determined by the System's Actuary, William M. Mercer, Incorporated, and is that amount that results from applying actuarial assumptions to adjust the accumulated benefits to reflect the time value of money (through discounts for interest) and the probability of payment (by means of decrements such as for death, disability, withdrawals, or retirement) between the valuation date and the expected date of payment. The significant actuarial assumptions used in the valuations as of September 30, 2001 and 2000 were:

- A. Actuarial Cost Method—Projected unit credit method.
- B. Life expectancy of participants—The 1983 Group Annuity Table for 2001 and 2000.
- C. Normal retirement age—65 for 2001 and 2000.
- D. Interest rate—8 percent annually for 2001 and 2000.
- E. Retiree cost-of-living increases—4 percent annually for 2001 and 2000.

The foregoing actuarial assumptions are based on the presumption that the System will continue. Were the System to terminate, different actuarial assumptions and other factors might be applicable in determining the actuarial present value of accumulated benefits.

Management Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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(s) of the financial statements and the reported amounts of revenues and expenses during the reporting period(s). Actual results could differ from those estimates.

Accumulated Benefits

The estimated actuarial present value of accumulated benefits for the System payable from the Fixed Benefit Fund is as follows:

(Dollars in thousands)	September 30	
	2001	2000
Vested benefits		
Retired or terminated participants	\$3,388,600	\$3,249,300
Active participants	1,885,000	1,862,600
Total	5,273,600	5,111,900
Nonvested benefits	359,000	230,200
Total estimated actuarial present value of accumulated benefits payable from the Fixed Benefit Fund	\$5,632,600	\$5,342,100

The changes in the estimated actuarial present value of accumulated benefits payable from the Fixed Benefit Fund are as follows:

(Dollars in thousands)	Fiscal Years Ended September 30	
	2001	2000
Estimated actuarial present value of accumulated benefits payable from the Fixed Benefit Fund at beginning of year	\$5,342,100	\$4,565,000
Increase during the year attributable to:		
Additional benefits accumulated and actuarial gains and losses	202,300	469,600
Plan amendments	-	276,900
Interest due to decrease in the discount period	414,300	352,300
Benefits paid to participants	(326,100)	(321,700)
Estimated actuarial present value of accumulated benefits payable from the Fixed Benefit Fund at end of year	\$5,632,600	\$5,342,100

Net Assets Available for Benefits

The net assets available for benefits are as follows:

(Dollars in thousands)	September 30	
	2001	2000
Accumulation for benefits and expenses	\$5,124,314	\$6,611,393
Accumulated members' contributions with interest	748,438	699,583
Net assets available for benefits	\$5,872,752	\$7,310,976

Investments

The following summarizes the investments of the Fixed Benefit Fund:

(Dollars in thousands)	September 30	
	2001	2000
Common stocks at fair value		
Domestic		
S&P 500 index futures contracts	\$ 710,326	\$ 718,059
Commingled index funds	646,017	741,578
Consumer Non-Durables	295,584	361,139
Health Care	280,840	278,387
Technology	276,866	689,134
Financial	238,406	205,991
Capital Goods	123,626	223,283
Energy	77,168	89,738
Basic Industries	46,769	34,706
Other	34,104	28,922
Utilities	30,343	42,494
Consumer Durables	24,935	65,522
Transportation	15,246	13,220
Foreign	598,632	828,920
	3,398,862	4,321,093
Preferred stocks at fair value	20,573	30,600
Limited Partnership	9,868	-
Bonds at fair value		
Domestic		
Mortgage backed securities	635,598	944,655
Industrial	579,727	645,393
U.S. Government	373,128	518,967
Financial	291,909	363,671
Utilities	107,141	128,751
Asset backed securities	30,599	49,127
Other	25,674	18,184
Convertible	16,091	14,307
Foreign	289,247	272,622
	2,349,114	2,955,677
Temporary investments at fair value		
Cash and cash equivalents	405,720	290,504
Total	\$ 6,184,137	\$ 7,597,874

During 2001 and 2000, the System's investments (including investments bought and sold, as well as held during the year) appreciated (depreciated) in value as follows:

(Dollars in thousands)	Fiscal Years Ended September 30	
	2001	2000
Common and preferred stocks	\$ (1,422,532)	\$ 503,144
Bonds	(31,824)	(36,308)
Net appreciation (depreciation)	\$ (1,454,356)	\$ 466,836



Statements of Net Assets Available for Benefits

September 30, 2001 and 2000

(Dollars in thousands)

	2001	2000
Assets		
Investments at fair value	\$299,455	\$461,126
Receivables		
Due from Variable Annuity Fund	7	78
Total assets	299,462	461,204
Liabilities		
Accounts payable		
Due to Fixed Benefit Fund	5	368
Total liabilities	5	368
Net Assets Available for Benefits	\$299,457	\$460,836

Statements of Changes in Net Assets Available for Benefits

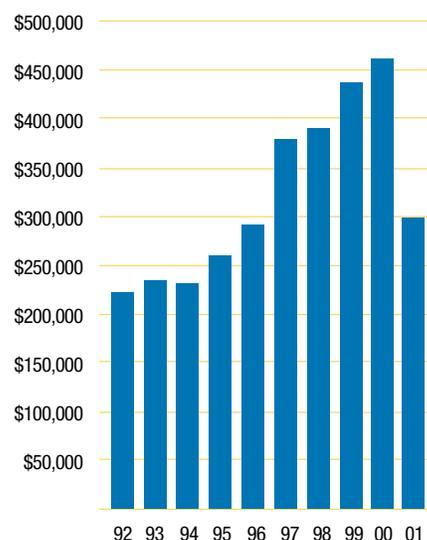
Fiscal Years Ended September 30, 2001 and 2000

(Dollars in thousands)

	2001	2000
Investment Income		
Net appreciation (depreciation)		
in fair value of investments	\$(121,574)	\$ 52,163
Dividends	5,097	5,871
	(116,477)	58,034
Contributions		
Members	7,187	7,571
Transfers from Fixed Benefit Fund	12,389	23,245
Transfers from 401(k) Plan	132	200
	19,708	31,016
Total increase (decrease)	(96,769)	89,050
Benefits and Transfers		
Retirement benefits	18,640	22,452
Death benefits	441	797
Withdrawals	3,075	4,378
Transfers to 401(k) Plan	7,365	16,906
Transfers to Fixed Benefit Fund	35,089	19,753
Total benefits and transfers	64,610	64,286
Net increase (decrease)	(161,379)	24,764
Net Assets Available for Benefits		
Beginning of year	460,836	436,072
End of year	\$ 299,457	\$460,836

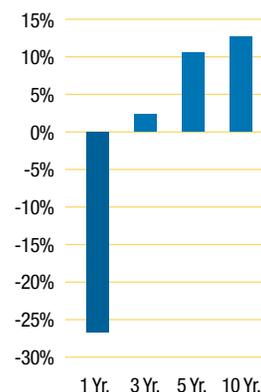
Variable Annuity Fund

NET ASSETS AVAILABLE FOR BENEFITS
(thousands)



Variable Annuity Fund

ANNUALIZED RATE OF RETURN



The accompanying notes are an integral part of the financial statements.

NOTES TO FINANCIAL STATEMENTS

Significant Accounting Policies**General**

The Variable Annuity Fund (Fund) is an investment option for eligible members as part of the defined benefit plan (Plan). On August 1, 2000, the Fund was split into two accounts. An Employee Account was established whereby contributions purchase shares in a stock mutual fund. The Retiree Account is used to pay monthly benefits to electing members.

The Employee Account is invested in the Dreyfus Basic S&P 500 Stock Index Fund. Members' contributions purchase shares at the net asset value of the fund on the date of contribution. If members, upon retirement or termination from employment, elect to withdraw the balance in their accounts, the shares in the mutual fund will be redeemed and the proceeds will be paid.

When members retire and elect to receive a monthly annuity benefit, their shares in the Dreyfus Basic S&P 500 Stock Index Fund are redeemed and the proceeds are used to purchase units in the Retiree Account. This account is invested in a commingled trust fund with the underlying investment in stocks included in the S&P 500 Stock Index. The value of the members' units fluctuates with the value of the net assets in the Retiree Account. The units were credited 6 percent interest units for the years ended September 30, 2001 and 2000.

A more detailed description of investments, benefits, and vesting is available from the TVA Retirement System.

Valuation of Investments

Investments held in the Variable Annuity Fund are stated at fair value which is determined by the Trustee of the fund as follows: common stocks, mutual funds, and commingled trust funds are stated at the last closing price for securities listed on national exchanges or the last bid price for securities traded over the counter.

Investment Income

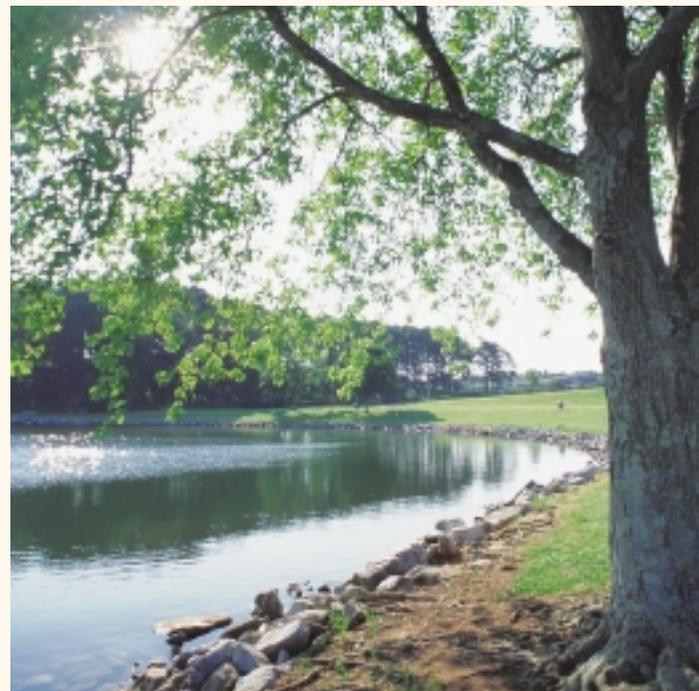
The Plan presents in the Statements of Changes in Net Assets Available for Benefits the net appreciation (depreciation) in the fair value of its investments which consists of the realized gains or losses and the unrealized appreciation (depreciation) on those investments. Dividend income is recorded on the ex-dividend date, and interest income is recorded as earned on an accrual basis.

Member Contributions

Eligible members may voluntarily contribute to either the Fixed Benefit Fund or the Variable Annuity Fund or to both. Federal income tax is deferred on earnings until annuity payments start or withdrawals are made. Members are also permitted to transfer their contributions between the Fixed Benefit Fund and the Variable Annuity Fund once per calendar month and may, at any time during employment, transfer their entire balance to the 401(k) Plan. Upon retirement, members may transfer all or any portion of their after-tax balance in the 401(k) Plan to the System to receive monthly payments. After retirement, members may elect to transfer between the Fixed Benefit Fund and the Variable Annuity Fund once per calendar year.

Termination

In the event the System terminates, the net assets will be allocated generally to provide benefits based upon members' pro rata share of the fund.





NOTES TO FINANCIAL STATEMENTS CONTINUED

Investments

For the years ended September 30, 2001 and 2000, the investments of the Variable Annuity Fund consisted entirely of S&P 500 index common stock funds.

At September 30, 2001, the investments by account were as follows:

(Dollars in thousands)

Employee Account

	2001	2000
Dreyfus Basic S&P 500 Stock Index Fund	\$171,117	\$269,780

Retiree Account

Commingled Index Funds	128,338	191,346
	<u>\$299,455</u>	<u>\$461,126</u>

Management Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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(s) of the financial statements and the reported amounts of revenues and expenses during the reporting period(s). Actual results could differ from those estimates.

Statements of Net Assets Available for Benefits

September 30, 2001 and 2000
(Dollars in thousands)

	2001	2000
Assets		
Investments at fair value	\$827,746	\$1,057,328
Net Assets Available for Benefits	\$827,746	\$1,057,328

Statements of Changes in Net Assets Available for Benefits

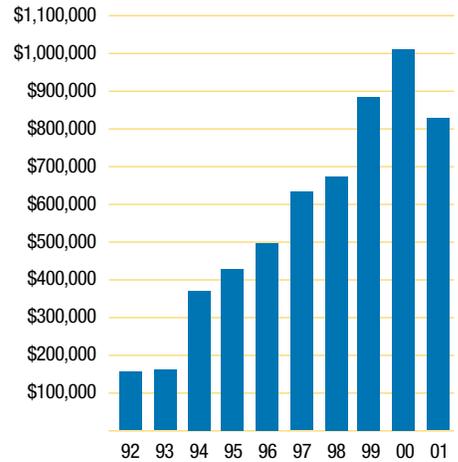
Fiscal Years Ended September 30, 2001 and 2000
(Dollars in thousands)

	2001	2000
Investment Income		
Net appreciation (depreciation)	\$ (313,659)	\$ 66,051
Interest and dividends	50,879	70,895
Contributions		
Members	47,982	45,170
TVA	11,649	9,579
Transfers from annuity funds	29,063	49,372
Total increase (decrease)	(174,086)	241,067
Benefits and Withdrawals	55,496	50,469
Net increase (decrease)	(229,582)	190,598
Net Assets Available for Benefits		
Beginning of year	1,057,328	866,730
End of year	\$ 827,746	\$1,057,328

401(k) Plan

NET ASSETS AVAILABLE FOR BENEFITS

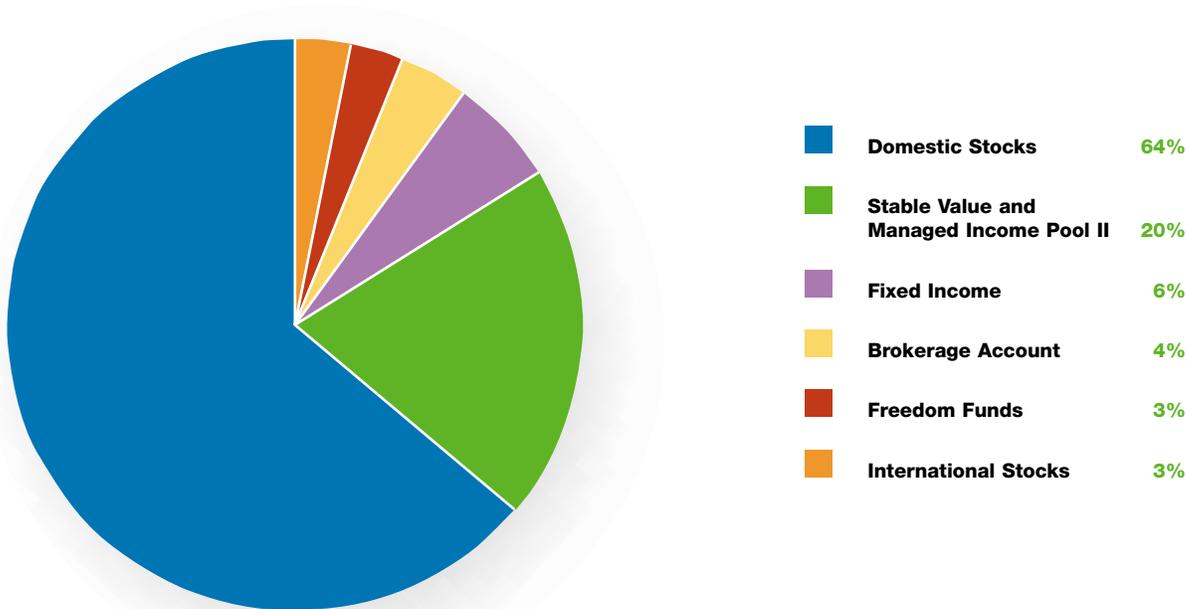
(thousands)



The accompanying notes are an integral part of the financial statements.

401(k) Plan Asset Allocation

(SEPTEMBER 30, 2001)



NOTES TO FINANCIAL STATEMENTS

Significant Accounting Policies

General

The TVA Savings and Deferral Retirement Plan [401(k) Plan] is a defined contribution plan for members of the System funded by members' after-tax contributions and before-tax salary deferrals. Additionally, eligible members receive matching contributions. Investment options for the after-tax, before-tax, and matching contributions are comprised of 25 eligible funds. A detailed description of the 401(k) Plan and the various investment options offered is available from the TVA Retirement System.

Amendments to the Provisions of the 401(k) Plan

During fiscal year 2001, the Provisions were amended to change the definition of wages and salaries in calculating 401(k) Plan matching contributions. TVA matching contributions are now made on certain lump-sum payments made in lieu of base wage or salary increases for fiscal years 1998 through 2002. Matching contributions are also now made on lump-sum payments for certain TVA performance incentive plans beginning in fiscal year 2000.

Also, in fiscal year 2001, the Board approved expanding the 401(k) Plan to include investment options in more than 200 new mutual funds (to be implemented in fiscal year 2002).

Valuation of Investments

The values of mutual fund shares are stated at fair value based on the last bid price or net asset value per share at the end of each plan year. The Managed Income Pool II and Stable Value Fund investments are stated at cost plus accrued interest. Other investments are stated at the last closing sale price for securities listed on national exchanges or the last bid price for securities traded over the counter.

Investment Income

The 401(k) Plan presents in the Statements of Changes in Net Assets Available for Benefits the net appreciation (depreciation) in the fair value of its investments which consists of the realized gains or losses and the unrealized appreciation (depreciation) on those investments. Dividend income is recorded on the ex-dividend date, and interest income is recorded as earned on an accrual basis.

Contributions

After-tax

Contributions, subject to certain limitations, may be made by payroll deductions, cash payment, or transfer from other

funds in the 401(k) Plan. A member may increase, decrease, transfer, or stop contributions at any time.

Before-tax

Salary deferrals are made through payroll deductions only. A member may increase, decrease, transfer, or stop contributions at any time.

Matching

Cash Balance Benefit Structure participants who contributed to the 401(k) Plan received employer matching contributions equal to 75 cents on every dollar contributed to the 401(k) Plan on a before- and/or after-tax basis, with maximum matching contributions of 4.5 percent of fiscal year-to-date base compensation. Participants in the Original Benefit Structure received employer matching contributions of 25 cents on every dollar contributed on a before- and/or after-tax basis, with maximum matching contributions of 1.5 percent of fiscal year-to-date base compensation.

In calendar year 2001, total contributions to the Fixed Benefit Fund, Variable Annuity Fund, and 401(k) Plan may not exceed the lesser of \$35,000 or 25 percent of calendar year-to-date compensation.

Withdrawals

After-tax

Members are permitted to withdraw from any or all of the funds in the 401(k) Plan at any time. Upon retirement, members are also permitted to transfer their funds to the System to receive monthly payments.

Before-tax

Federal income tax rules restrict withdrawals from the 401(k) Plan while the member is still employed except for the following situations:

- If the member is over age 59½, salary deferral contributions may be withdrawn at any time.
- If the member is under age 59½, salary deferral contributions may be withdrawn only upon the Retirement System Board's approval and only upon a showing of financial hardship. Generally, the only financial needs considered to meet the definition of hardship are: (1) certain deductible medical expenses; (2) purchase of a principal residence; (3) post-secondary tuition and related educational fees; or (4) payments necessary to prevent eviction from or foreclosure on the participant's principal residence.

Members may receive the full balance of their funds upon retirement, disability, death, or termination, except that a retiree may defer distribution until no later than April 1 of the calendar year after the year in which the member reaches age 70½. In addition, members may

choose, after termination, to receive periodic installment payments from their balance.

Vesting

Participants who contribute to the 401(k) Plan become vested in their matching contributions upon completion of 5 years of actual service. Actual service is defined as the length of time spent as a member of the TVA Retirement System, not including credit for unused sick leave, forfeited annual leave, or pre-TVA employment military service. Upon completion of this service requirement, a member may withdraw matching contributions only upon retirement, disability, or termination of TVA employment. Upon death, matching contributions may be withdrawn without regard to the vesting requirement.

Loans

With certain limits, the 401(k) Plan permits loans to participants. Members may borrow a percentage of their account balance (maximum \$50,000) for up to 5 years, or 10 years if the loan is to be used to purchase a primary residence. The loan interest rate is the Prime Rate plus 1 percent. Such interest is credited directly to the account of the member.

Termination

In the event the 401(k) Plan terminates, the net assets will be distributed to members in proportion to their respective accounts in the 401(k) Plan. In the event the 401(k) Plan terminates, payment of nonforfeitable benefits based on contributions to participants' accounts will be assured.

Management Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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(s) of the financial statements and the reported amounts of revenues and expenses during the reporting period(s). Actual results could differ from those estimates.

Investments in Stable Value Fund

The Stable Value Fund consisted of the following investment contracts and securities as of September 30, 2001 and 2000 as follows:

<i>(Dollars in thousands)</i>	2001	2000
Investment Contracts		
GE Life and Annuity Assurance Company	\$ 3,386	\$ 3,193
CDC Capital (BIC)	1,008	1,008
Asset Backed Securities		
Morgan Guaranty	6,423	7,683
State Street	6,330	6,629
Monumental Life	3,689	3,707
AIG Financial Products	2,062	2,848
Union Bank of Switzerland	2,021	2,352
Deutsche Bank	2,020	2,033
Westdeutsche Landsbank	2,002	1,999
Chase Manhattan	1,448	2,701
Mortgage Backed Securities		
Monumental Life	1,774	1,783
Deutsche Bank	1,632	2,679
AIG Financial Products	1,423	2,066
Union Bank of Switzerland	1,266	1,999
Chase Manhattan	737	1,394
Transamerican Life Insurance Company	717	1,005
Fidelity Short Term Investment Fund	53,172	40,812
Total	\$91,110	\$85,891



TVA Savings and Deferral Retirement Plan [401(k) Plan]

Investments

The net assets of all investment options as of September 30, 2001 and 2000 are as follows:

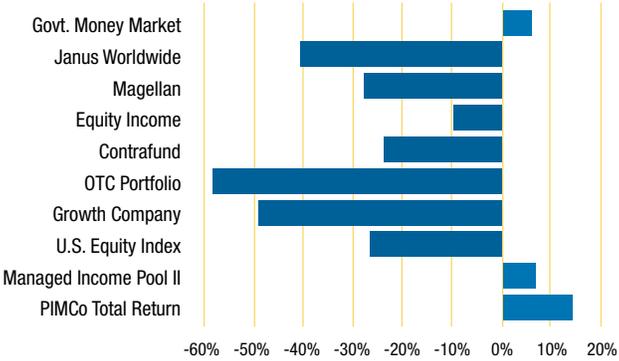
<i>(Dollars in thousands)</i>	2001	2000
Bond Funds		
<i>Bond Funds over 5%</i>		
Stable Value	\$ 91,110	\$ 85,891
Managed Income Pool II	70,296	70,197
<i>Bond Funds under 5%</i>		
Fidelity Retirement Government Money Market Portfolio	37,468	33,609
PIMCo Total Return	10,605	5,098
Fidelity U.S. Bond Index Portfolio	483	442
Fidelity U.S. Investments - Government Securities Fund, L.P.	213	231
Total Bond Funds	<u>210,175</u>	<u>195,468</u>
Equity Funds		
<i>Equity Funds over 5%</i>		
Fidelity Magellan	219,079	300,364
Fidelity Growth Company	70,250	140,521
Fidelity Equity Income Fund I	66,510	73,185
<i>Equity Funds under 5%</i>		
Brokerage Link*	31,500	58,061
Fidelity Contrafund	28,319	37,734
Fidelity Dividend Growth	25,430	24,911
Fidelity Growth & Income Fund	22,717	26,999
Fidelity Puritan Fund	21,965	20,424
Fidelity OTC Portfolio	20,713	46,374
Janus Worldwide Fund	20,677	34,975
Fidelity U.S. Equity Index Fund	15,158	18,448
Fidelity Freedom 2010 Fund	9,563	8,863
Fidelity Low Price Stock Fund	9,247	3,630
Fidelity Blue Chip Growth Fund	4,162	6,994
Fidelity Freedom 2020 Fund	3,785	4,145
Fidelity Freedom 2000 Fund	3,687	3,594
Fidelity Trend Fund	3,674	5,568
Fidelity Freedom 2030 Fund	3,191	3,426
Fidelity Balanced Fund	3,128	3,541
WP Emerging Growth Fund	2,300	4,543
MAS Value Fund	2,210	445
Fidelity Diversified International Fund	2,107	2,116
Fidelity Equity Income Fund II	2,071	2,699
Fidelity Mid-Cap Stock Fund	2,053	3,068
Fidelity Fund	1,931	3,154
Fidelity Freedom Income Fund	1,216	1,531
Fidelity Fifty Fund	568	882
Brinson U.S. Equity Fund	546	458
T. Rowe Price International Stock Fund	523	549
Fidelity Worldwide Fund	510	709
Fidelity Small Cap Stock Fund	474	603
Fidelity Overseas Fund	373	611
Fidelity Convertible Securities Fund	365	475
Fidelity Disciplined Equity Fund	343	502
Fidelity International Growth & Income Fund	263	398
Fidelity Retirement Growth Fund	209	497
Total Equity Funds	<u>600,817</u>	<u>844,997</u>
Participant Loans	<u>16,754</u>	<u>16,863</u>
Net Assets Available for Benefits	<u>\$ 827,746</u>	<u>\$1,057,328</u>

*The brokerage account option is not a mutual fund. The brokerage account option allows participants to purchase individual securities or other mutual funds not offered as one of the core 401(k) Plan investments.



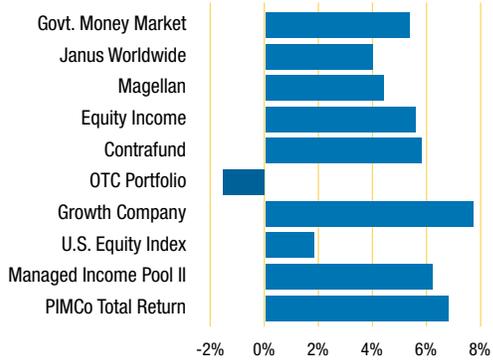
Cumulative Return

FOR YEAR ENDED SEPTEMBER 30, 2001



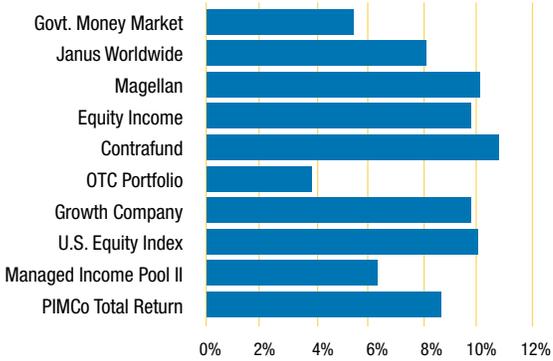
Annualized Return

FOR 3 YEARS ENDED SEPTEMBER 30, 2001



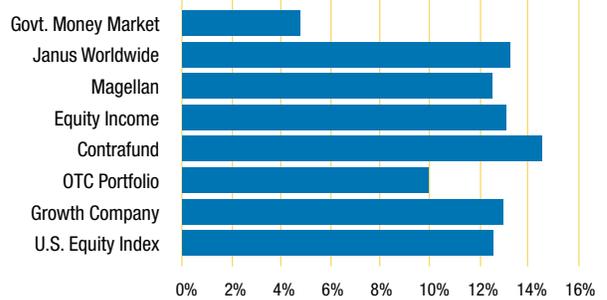
Annualized Return

FOR 5 YEARS ENDED SEPTEMBER 30, 2001



Annualized Return

FOR 10 YEARS ENDED SEPTEMBER 30, 2001





Tennessee Valley Authority
Retirement System
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Knoxville, Tennessee 37902

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