

Meeting No. 441

MINUTES OF MEETING
OF THE BOARD OF DIRECTORS
RETIREMENT SYSTEM OF THE TENNESSEE VALLEY AUTHORITY

December 11, 2012

(Edited to remove personal information related to individual members and retirees and proprietary information)

The regular quarterly meeting of the Board of Directors (Board) of the TVA Retirement System (System) was held on Tuesday, December 11, 2012, at 11:48 a.m., CST, in Room 118, 1st Floor, Tennessee Valley Authority, One Century Plaza, 26 Century Boulevard, Nashville, Tennessee.

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The following directors were present: Leslie P. Bays, Chair; Allen E. Stokes, Vice-Chair; Janet C. Herrin; John M. Hoskins; Leonard J. Muzyn; Anthony L. Troyani; and Tammy W. Wilson. Also present were Patrick D. Brackett, Executive Secretary; Pamela K. Ramsey, Assistant Secretary; W. Colby Carter, Legal Counsel; and Eric J. Davis, Program Manager, Investment Management & Risk.

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441-1 Each director was notified in an e-mail dated November 16, 2012, of the regular quarterly meeting to be held on December 11, 2012. A copy of the notice from the Executive Secretary is filed as Exhibit 441-1.

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441-2 (A-5992). The Chairman's report included the following:

- The Chairman noted the meeting the Board had with Tom Kilgore, TVA's Chief Executive Officer, prior to Board meeting to discuss matters regarding the System.
- The Chairman expressed the need to develop a policy for succession planning and to engage in a Board-self evaluation and Executive Secretary evaluation as upcoming work items for the Board.

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441-3 (A-5993). The Executive Secretary's report included the following:

- The Executive Secretary provided the Board with information regarding the System's favorable investment performance over one-, three-, and ten-year periods relative to the plan universe database rankings maintained by Wilshire Associates Incorporated (Wilshire).
- The Executive Secretary informed the Board that an experience study for the System will need to be performed by Mercer this year as required by the System Rules.
- The Executive Secretary updated the Board on recent and upcoming visits by staff with other large retirement plans in Tennessee to help provide information on latest trends and benchmarking.

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441-4 (A-5994). On December 10, 2012, Bradley Arant Boult Cummings, outside counsel representing the System in the current lawsuit against TVA and System, discussed with the System Board issues regarding the lawsuit.

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441-5 (A-5995). The Board approved the minutes of Meeting No. 440 held September 20, 2012.

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441-6 (A-5996). The Board accepted the Treasurer's Report for the quarter ending September 30, 2012. A copy of the Treasurer's Report is filed as Exhibit 441-6. This report is available for review at the Retirement Services office.

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441-7 (A-5997). The Board accepted the Investment Performance Report prepared by Wilshire for the quarter ending September 30, 2012. A copy of the Investment Performance Report is filed as Exhibit 441-7. This report is available for review at the Retirement Services office.

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441-8 (A-5998). The Board accepted the report of retirements approved for the quarter ending September 30, 2012. A copy of the report and a copy of summary demographic information regarding retirements in the quarter are filed as Exhibit 441-8. These reports contain information on individual cases and are not available for review.

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441-9 (A-5999). The Board accepted the Investment Review for the Savings and Deferral Retirement Plan (401(k) Plan) prepared by Fidelity Investment Institutional Services Company (Fidelity) for the quarter ending September 30, 2012. A copy of the 401(k) Plan Investment Review is filed as Exhibit 441-9. This report is available for review at the Retirement Services office.

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441-10 (A-6000). The Investment Committee report consisted of the items reported below at A-6001, A-6002, A-6003, and A-6004, and of the following items:

- The Board was provided and took note of the quarterly report on manager compliance with investment guidelines. A copy of the report, dated September 30, 2012, is filed as Exhibit 441-10(a).
- The Board was provided and took note of information regarding investment manager asset transfers during the third quarter of 2012. A copy of this information is filed as Exhibit 441-10(b).
- The Board was provided and took note of information on due diligence meetings and conference calls between System staff and investment managers during the fourth quarter of 2012. A copy of the information is filed as Exhibit 441-10(c).
- The Board was provided and took note of the quarterly analysis of 401(k) Plan investment options with respect to the Plan's watch list criteria. A copy of this information is filed as Exhibit 441-10(d).
- The Board was provided and took note of a staff report on quarterly economic indicators. A copy of the report is filed as Exhibit 441-10(e).
- The Board was provided and took note of a report giving the status and performance of the System's asset allocation to its "Tail Risk" strategy managed by Pacific Investment Management Company (PIMCO). A copy of this report is filed as Exhibit 441-10(f).
- The Board was provided an update on the funded status of the System as of November 16, 2012. A copy of the report is filed as Exhibit 441-10(g).
- The Board was provided an update from the System staff on the Dodd-Frank rules regarding derivatives and how those will impact the System with respect to its investments.
- The Board was provided an equity, FX, and fixed income transaction cost analysis of the System's investments during the third quarter of 2012 by Zeno Consulting Group (Zeno). After review and discussion of the analysis, the Board requested further

information on the cost to continue receiving transaction cost analyses from Zeno on an annual basis. A copy of the transaction cost analysis is filed as Exhibit 441-10(h).

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441-11 (A-6001). As requested at the previous Board meeting (see Minute Entry 440-14), and upon the recommendation of the Investment Committee, the Board voted to approve a revised Investment Policy Statement incorporating changes to the asset allocation policy mix that will be in place until the first funded status trigger point is reached in the glide path of the new dynamic asset allocation policy. A copy of the revised Investment Policy Statement is filed as Exhibit 441-11.

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441-12 (A-6002). Upon the recommendation of the Investment Committee, the Board voted to approve, and authorized the Executive Secretary to execute, a contract with Wilshire for investment consulting services for the period January 1, 2013, through December 31, 2013. A copy of the contract is filed as Exhibit 441-12.

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441-13 (A-6003). After discussion, and upon the recommendation of the Investment Committee, the Board voted to approve, and authorized the Executive Secretary to execute, an amendment to the Limited Partnership Agreement related to the System's investment in the Huff Alternative Fund to allow follow-up investments in energy-related opportunities out of the Limited Partnership's existing cash on hand. A copy of information on the amendment is filed as Exhibit 441-13.

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441-14 (A-6004). After discussion, and upon the recommendation of the Investment Committee, the Board voted to approve, and authorized the Executive Secretary to execute, certain amendments to the Limited Partnership Agreement related to the System's investment in the Kennedy Wilson Real Estate Fund IV, which include an extension of the final closing date for the Fund to March 31, 2013. A copy of information on the amendments is filed as Exhibit 441-14.

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441-15 (A-6005). The Retirement Committee report consisted of items reported below at A-6006, A-6007, A-6008, A-6009, A-6010, A-6011, and A-6012 and of the following items:

- The Board was provided and took note of the quarterly report on System communications, including TVARA website update, TVARA news article, TVARA meetings, TVARA chapter president bulletins, TVARS website updates, TVA Today

articles, and additional communication initiatives. A copy of the Quarterly Communication Update is filed as Exhibit 441-15(a).

- The Board was presented with the System's FY 2013 budget as well as proposed objectives and work plan items for FY 2013. A copy of the FY 2013 budget and objectives is filed as Exhibit 441-15(b).
- After discussion over additional lawsuit settlement-related work that was performed by Mercer Human Resource Consulting (Mercer), the System's actuary, upon the recommendation of the Retirement Committee, the Board voted to increase the maximum allowable shared cost for Mercer's actuarial services related to lawsuit settlement negotiations from \$50,000 to \$100,000 and directed the Executive Secretary to work out the appropriate split in the responsibility for the additional fees between the System and TVA.
- The Board discussed proposals regarding a 50% level-income option, amendments to credit lump-sums given in lieu of salary increases for FY 2013, and open meetings. No actions were taken.

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441-16 (A-6006). Upon the recommendation of the Retirement Committee, the Board accepted the actuarial valuation of the Variable Annuity Fund, as of March 31, 2012, by Mercer, and its recommendation that, because the Variable Annuity Fund had a small surplus as of March 31, 2012, the outstanding variable units should be decreased by 5,356. The decrease in the number of units will result in no significant change in the December 2012 unit value. A copy of a letter from Réal Lamarche, Partner, Mercer, to the Board, and a copy of the TVA Retirement System Variable Annuity Valuation Report as of March 31, 2012, are filed as Exhibit 441-16.

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441-17 (A-6007). The Board approved the calculation of a 2.3% cost-of-living allowance (COLA) increase in the monthly pension and supplemental benefits payable to eligible retirees and beneficiaries in accordance with the System Rules. The COLAs are effective with the January 2013 payments as provided for in sections 6I, 7L and 18C3 of the System Rules. A copy of the COLA calculation is filed as Exhibit 441-17.

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441-18 (A-6008). The Board approved the calculation of a 6% annual interest rate credit to participants' accounts in the Cash Balance Benefit Structure for calendar year 2013 in accordance with the System Rules. Under section 7C3 of the System Rules, this interest rate credit is calculated as the greater of (i) the percentage change in the Consumer Price Index plus 3% (not to exceed 10 percent unless approved by the System Board and TVA) or (ii) 6%. The

relevant CPI increase of 2.3% plus 3% equaled 5.3%. A copy of the Cash Balance annual interest rate calculation is filed as Exhibit 441-18.

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441-19 (A-6009). This item contains information on an individual case and is not available for review.

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441-20 (A-6010). The Chairman presented recommendations for the Board's standing and special committee members. After discussion of the recommendations, the Board approved the following standing and special committee assignments, as recommended by the Chairman:

Audit Committee

Leonard J. Muzyn, Chair
Allen E. Stokes
Tammy W. Wilson

Retirement Committee

Janet C. Herrin, Chair
Allen E. Stokes
Anthony L. Troyani

Investment Committee

John M. Hoskins, Chair
Leonard J. Muzyn, Vice Chair
Leslie P. Bays
Janet C. Herrin
Allen E. Stokes
Anthony L. Troyani
Tammy W. Wilson
Michael Brakebill (non-voting)

Election Committee

Anthony L. Troyani, Chair
Leslie P. Bays
John M. Hoskins

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441-21 (A-6011). The Board discussed and approved a tentative schedule and locations for the Board meetings to be held in calendar year 2013. This tentative schedule is filed as Exhibit 441-21.

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441-22 (A-6012). After discussion of a fee transparency and proactive pricing presentation with Fidelity regarding the 401(k) Plan and Fixed and Variable Funds, and upon the recommendation of the Retirement Committee, the Board voted to approve new recordkeeping administrative fee structure for the 401(k) Plan and Fixed and Variable Funds, which will result in lower fees to the plans and 401(k) Plan participants. As a part of this approval, the Board

authorized the Executive Secretary to take any actions necessary to implement the new fee structure. A copy of Fidelity's presentation is filed as Exhibit 441-22.

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441-23 (A-6013). The Election Committee had no items to report.

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441-24 (A-6014). The Audit Committee report consisted of the item reported below at A-6015 and of the following items:

- The Board was provided and took note of the System Board's travel expenses for the previous quarter.
- The Board was provided and took note of a summary of charges on the System's credit card for the previous quarter.
- The Board was provided and took note of the audit timeline for the System and the 401(k) Plan by Crowe Horwath, the System's external auditor, and E.H. Johnson & Company, the System's internal auditor. On December 6, a phone conference with Crowe Horwath was held to discuss progress and status of the audit. A copy of the audit timeline is filed as Exhibit 441-24.

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441-25 (A-6015). After discussion, and upon the recommendation of the Audit Committee, the Board accepted the Service Organization Control (SOC1) Report for the System for the period August 1, 2011, to July 31, 2012, prepared by E.H. Johnson & Company, P.C., the System's internal auditor. A copy of the SOC1 Report is filed as Exhibit 441-25.

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441-26. A motion was made by Mr. Muzyn for the System Board to adopt the following resolution:

Resolved: All future TVARS Board meetings will be open to observation by the members of the system. Having employees and retirees attend the meetings will help build trust between the TVARS Board and its members. It will demonstrate that the TVARS Board truly wants to provide open and transparent communication with all the members. Provisions shall be made for the Board to go into executive session to discuss confidential matters.

The motion was lost for lack of a second.

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441-27. A motion was made by Mr. Muzyn to add the following subsection L, "Procedure for Handling TVA Requests for Benefit Reductions," under "General Conditions" in Section 11 of the System Rules:

- L. In the event TVA asks TVARS for benefit concessions, the TVARS Board will do the following:
 - 1. Request an official written statement from TVA detailing the benefit concessions being requested, the rationale behind these requests, and the alternatives if the benefit concessions are not accepted. The statement should detail the effect of the benefit concessions and the alternatives on at least four subsets of TVARS beneficiaries: 1) Current Original Benefit (OB) retirees; 2) Current Cash Balance (CB) retirees; 3) Current OB employees; and 4) Current CB employees.
 - 2. Upon receipt of the written request, the TVARS Board will:
 - (a) determine if there are likely to be disparate effects on additional subsets of TVARS beneficiaries. If any such subsets are identified, the TVARS Board will request that TVA revise its written statement to include these additional subsets.
 - (b) Ask TVA to assess the legality of the request, and its probability of being upheld, as it pertains to each affected TVARS beneficiary subset.
 - 3. Once the official written TVA statement is determined by the TVARS Board to contain sufficient detail as to affected subsets of TVARS beneficiaries, and to contain what it considers to be only legal benefit concessions, the TVARS Board will then publicly share the written TVA statement with TVARS stakeholders. If one of the alternatives listed by TVA is system termination, or a reduction of future annual TVA contributions below that necessary to cover annual normal cost, the TVARS Board will secure the opinions of three reputable law firms specializing in pension law as to the legality of all of the proposed benefit concessions, and these opinions will be publicly shared with TVARS stakeholders along with the written TVA statement.
 - 4. The TVARS Board will then put the benefit concessions to a vote of the TVARS membership, with the official TVA written statement included with the ballot, along with the three expert legal opinions if applicable, so that the membership will have sufficient information to cast an informed vote.

5. Voting results will be tallied by each previously identified subset of TVARS beneficiaries.
6. Such a vote will be advisory in nature, but the TVARS Board will not act on the benefit concession request until the voting is complete and the results by previously identified subsets of TVARS beneficiary are publicly shared with all TVARS stakeholders.

The motion was lost for lack of a second.

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441-28. A motion was made by Mr. Muzyn for the System Board to send the following letter to the TVA Board:

TVA Board Members:

Given our knowledge gained over the years in governing the TVA Retirement System, we believe it is our duty to inform you of some important concepts behind pension funding. The assumed return referenced in the answer provided by TVA to the attached OpenLine question is a long-term rate of return. In order to achieve this long-term rate of return, actual returns are anticipated to be above it in some years and below it in others. If contributions are not made in years when the actual returns are above the assumed rate, it is to be expected that these will have to be made up in years when the actual returns are below the assumed rate. The \$1 billion contribution in 2009 should be considered as compensation for prior years when no contributions were made. If the goal is a healthy pension fund able to fulfill its obligations to retirees, the 2009 contribution should not be viewed as prefunding of future contributions. The fiscal year 2012 return exceeding the assumed long-term rate should not be viewed as a reason to provide no contribution in fiscal year 2013, unless TVA is at the same time committing to higher contributions in future years. This is stated very clearly in the attached excerpt from the Feb 12, 2010 IG Review of TVA's Pension Risk (Audit 2009-12326). The complete IG review is also attached.

We would be happy to discuss this with you further at your convenience.

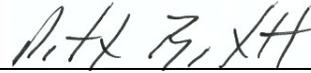
Sincerely,

TVARS Board

The motion was lost for lack of a second.

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The meeting was adjourned at 12:24 p.m., CST.



Executive Secretary



Chairman