

New 401(k) Plan Lineup

Summary

The TVARS Board is responsible for administering the 401(k) Plan, an important part of retirement benefits for all TVA employees in every TVARS benefit structure.

We're focused on providing an industry-best 401(k) Plan that helps all employees meet their retirement income goals.

The TVARS Board performed a comprehensive evaluation of 401(k) investments and fees. We worked with a leading defined contribution plan consultant (Aon Hewitt), and while the current plan is good, we identified areas where the plan could be better based on:

- Best practices
- Consideration of participants' retirement income needs
- Providing investments and services at the lowest cost possible for participants

Results of comprehensive evaluation

The TVARS Board made the decision to provide a simpler, more targeted investment lineup that is appropriate for all plan participants

Some key considerations on the current lineup:

- The current lineup has 75 funds.
- Too many funds confuse participants and are more difficult for the TVARS Board to monitor.
- There are multiple funds within most of the asset classes (i.e., 25 U.S. equity funds, 15 fixed income funds, 18 international equity funds, including several country or region sector funds).
- There are overlaps in investment strategies among funds, which led to a lack of diversification.
- There are many funds with small percentages of plan assets, which make it difficult to obtain best pricing.

The new lineup includes four tiers to give participants choice, based on investment style and needs

- **Tier 1 – Target Date funds (TDFs)**
- **Tier 2 – Passively managed funds (4 index funds)**
- **Tier 3 – Actively managed funds (9 funds)**
- **Tier 4 – Self-directed brokerage account**

Target Date Funds

- TDFs will be managed by BlackRock, a leading international provider of retirement and investment services for retirement plans and institutional investors with nearly \$3 trillion under management.

- BlackRock developed the first TDFs and is a leading innovator in research and ideas in this area.
- TDF funds are appropriate for the majority of participants, given the level of contributions to participant accounts.
- The funds are designed for participants to put all or most of their money in, they are professionally managed and adjust asset allocation over time.
- Funds are selected based on anticipated retirement date (normally assume age 65).
- TDF funds have an expense ratio of only 9 basis points (0.09%).

Passively managed funds in major asset classes

- U.S. bond fund; U.S. large cap stocks; U.S. small/mid cap stocks; International stocks

Actively managed funds in diverse group of asset classes

- Money market; stable value fund; global bond fund; real asset fund (TIPS, REITs, and commodities); U.S. large cap value stocks; U.S. large cap growth stocks; U.S. small/mid cap value stocks; U.S. small/mid cap growth stocks; international stocks (including emerging markets)
- Selection criteria for funds
 - Buy rated funds based on investment research from Aon Hewitt
 - Strong track record over market cycles relative to benchmark index
 - Investment approach that fits within selected asset class and does not cross over into other asset classes or market cap space
 - Through selection process, TVARS Board kept Fidelity Stable Value Fund and Fidelity Growth Company Fund which had a significant amount of participant assets

Once the funds for each tier were selected, the TVARS Board worked with Aon Hewitt to identify the lowest cost vehicle available for each investment:

- TDFs will use a unitized account vehicle
- Most other funds will use a collective investment trust vehicle
- All remaining funds will use mutual fund vehicle
- Performance and pricing:
 - All new funds will have daily performance and pricing information available on Fidelity NetBenefits.
 - TDFs are new funds and do not have historical performance info.
 - TVARS Board will evaluate the performance of the TDFs based on whether the funds are meeting retirement income goals and performing as expected, relative to other types of TDFs.
 - Other funds with collective investment trust vehicles also lack long periods of historical performance data, but there are identical funds (with higher fee share classes) for each one that can show participants how these strategies have performed over time relative to the appropriate benchmark.

Important dates

- New funds were added to the investment lineup on Thursday, Feb. 4, 2016.

- Old funds will be removed from the investment lineup on Friday, April 8.
- In between these dates, participants have the opportunity to make new elections and move any money to the new funds.
- Decision guides have been mailed to all participants to provide information on the new funds and to help them in their decision making.
- TVARS and Fidelity will host sessions to go over the new investment lineup. Participants may go to the TVARS website (and select TVARS SharePoint/401k Employee Meetings) to sign up to attend. Sessions will be held at plant and office sites.
- For participants who are comfortable with their money in the TDFs or who do not choose new elections to the new funds by Friday April 8, their current and future investments will be automatically defaulted into the age-appropriate TDF (based on assumed retirement age of 65).
- As mentioned before, these TDFs are good diverse investments at a low cost and are appropriate for the majority of participants.

The TVARS Board worked with Aon Hewitt to perform a blind Request for Proposal for the plan's record-keeping services

- New, lower recordkeeping fees were negotiated, and Fidelity Investments was retained as the provider of record-keeping services
- As a best practice, the TVARS Board also elected to move to a transparent pricing model to pay for the plan's record-keeping fees
 - Previously, in many funds in the lineup, participants paid for record-keeping services as a percentage of assets, which was reflected in the net asset value of the fund.
 - Under the new, more transparent pricing model, each participant will be charged a flat record-keeping fee of \$47 per year (deducted from participant accounts in the amount of \$11.75 per quarter).

Overall summary:

- The TVARS Board has been working with Aon Hewitt for over a year on these improvements to the Plan, which deliver:
 - Streamlined fund lineup in clearly targeted asset classes
 - New TDFs designed specifically for TVA employees at a lower cost
 - Actively managed funds with lowest cost available to plans of our size
 - Lower and transparent recordkeeping fees for participants
 - Brokerage accounts still available to all participants

These changes are currently being implemented by TVARS and Fidelity and are separate from TVA's pension proposal to the TVARS Board

In addition, the TVARS Board remains committed to providing the necessary tools and education for participants to manage their accounts in the 401(k) Plan

- Fidelity continues to provide dedicated plan consultants who are available to meet with participants one-on-one to review their accounts and help make decisions.

- Participants may elect to use a managed account service where professional financial advisers manage your account for an additional fee based on account size which is lower than what participants can find with other financial advisory firms.
- Fidelity NetBenefits contains a number of research portals and self-directed analysis tools for participants.
- TDFs are designed for participants to put all of their money in and have a professionally-managed investment strategy that will likely meet their retirement goals with the Plan.