

Meeting No. 462

MINUTES OF MEETING  
OF THE BOARD OF DIRECTORS  
RETIREMENT SYSTEM OF THE TENNESSEE VALLEY AUTHORITY  
May 9, 2016

A special-called meeting of the Board of Directors (Board) of the TVA Retirement System (System) was held on Monday, May 9, 2016, at 2:57 p.m., EDT, via teleconference.

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The following directors were present: Allen E. Stokes, Chair; Anthony L. Troyani, Vice-Chair; Brian M. Child; John M. Hoskins; James W. Hovious; Leonard J. Muzyn; and Tammy W. Wilson. Also present were Patrick D. Brackett, Executive Secretary; W. Colby Carter, Senior Counsel, Retirement Benefits & Compliance; and Sally R. Weber, Manager, Retirement Operations.

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462-1. Directors Child, Hoskins and Wilson called this special meeting of the Board pursuant to Article II, Section 2 of the System Bylaws. Each director was notified in an email dated May 4, 2016, of the special-called meeting to be held on May 9, 2016. A copy of the notice from the Executive Secretary is filed as Exhibit 462-1.

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462-2. Prior to the meeting, the Board reviewed and discussed the April 18, 2016, letter from TVA President and CEO, Bill Johnson, to the Board requesting certain changes to the proposal approved by the Board on March 3, 2016, as a counterproposal to TVA's December 16,

2015, proposed amendments to the TVARS Rules and Regulations. The Board also reviewed and discussed information received from the Board's actuary, Mercer Human Resources Consulting (Mercer), on the Board's counterproposal as modified by TVA's requested changes. A copy of the April 18, 2016, letter from Bill Johnson and the analysis by Mercer of the Board's counterproposal as modified by TVA's requested changes is filed as Exhibit 462-2.

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462-3. Director Troyani made a motion to table discussion on and consideration of TVA's requested changes to the Board's counterproposal based on on-going outside inquiries regarding the System and proposed changes to benefits and the current lawsuit against TVA and TVARS regarding the 2009 amendments and until a determination is made on these inquiries and the lawsuit. The motion received a second from Director Muzyn. After discussion, the motion to table failed by a roll call vote of 4 to 3. Directors Child, Hoskins, Stokes, and Wilson voted against the motion to table, and Directors Hovious, Muzyn and Troyani voted for the motion to table.

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462-4. Director Child made a motion to approve amendments to the TVARS Rules and Regulations and 401(k) Plan Provisions consistent with the Board's March 3, 2016, counterproposal but as modified by the changes set forth on the first page of Mr. Johnson's April 18, 2016, letter to the Board. As a part of this motion, the Board also would do the following:

- Direct the Executive Secretary to present the March 3<sup>rd</sup> counterproposal, as modified by TVA's requested changes dated April 18<sup>th</sup>, to TVA indicating the amendments the Board is approving;
- Direct the TVARS staff to draft the amendments implementing this modified counterproposal, which will then be reviewed by (i) the TVARS Board, (ii) Mercer, who is the TVARS actuary, and (iii) Bradley Arant Boult Cummings, who is TVARS outside legal counsel; and

- Direct the Executive Secretary, once these amendments have been fully reviewed and finalized, to formally present them to TVA for its review, at which point the amendments would go into effect after 30 days if TVA does not veto them as set forth in the TVARS Rules.

The motion received a second from Director Hoskins. The terms of the Board's March 3<sup>rd</sup> counterproposal, as modified by the changes set forth on the first page of Mr. Johnson's April 18<sup>th</sup> letter, are as follows:

#### Cash Balance to Defined Contribution

**Hired on or after 1/1/96 with less than 10 years of service:** Transitioned to 401(k) only plan with 6% automatic contributions from TVA and 100% match on up to an additional 6% of employee contributions.

**Hired on or after 1/1/96 with 10 or more years of service:** 3% cash balance pay credits on future earnings, 3% automatic 401(k) contributions from TVA, and 75% 401(k) match on up to an additional 6% of employee contributions. TVARS Board will pursue allowing these employees to forego future cash balance pay credits and switch to 401(k) only plan with 6% automatic contributions and 100% match on up to an additional 6% of employee contributions.

**Hired before 1/1/96:** No change and will continue to accrue 6% cash balance pay credits. TVARS Board will pursue allowing these employees to forego future cash balance pay credits and switch to 401(k) only plan with 6% automatic contributions and 100% match on up to an additional 6% of employee contributions.

**Election Option to Switch/Transfer:** The TVARS Board will pursue adopting additional amendments to the TVARS Rules and Regulations and 401(k) plan that will offer employees in the cash balance structure the option to voluntarily switch their future participation to the 401(k) only plan with 6% automatic contributions from TVA and 100% match on up to an additional 6% 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. This election option and implementing amendments may be submitted by TVARS to the IRS for review and approval pursuant to an IRS private letter ruling and may take 1-2 years.

#### Fixed Fund

No additional fixed fund contributions for employees hired on or after 1/1/96 or any employee electing to forego future cash balance pay credits by switching to a 401(k) only plan.

### Lump Sum Payout

Lump sum payout option of cash balance account increased from \$30,000 to total account value at termination/retirement, including lump sum payout of supplemental benefit (supplemental benefit lump sum calculated at 6% discount rate).

### Reduced Interest Crediting Rate

#### **Cash Balance**

**Hired before 1/1/96:** No change on interest crediting rate for existing and future cash balance pay credits.

**Hired on or after 1/1/96:** Interest crediting rate for existing and future cash balance pay credits of CPI + 2% with minimum rate of TVARS projected return minus 2% and maximum rate of TVARS projected return minus 0.5% (currently 5% and 6.5%, respectively).

#### **Fixed Fund**

**All participants:** Interest crediting rate for existing and future cash balance pay credits of CPI + 2% with minimum rate of TVARS projected return minus 2% and maximum rate of TVARS projected return minus 0.5% (currently 5% and 6.5%, respectively).

### COLA Salary Cap

COLA only applies to pension amounts based on earnings up to Executive Level IV (former TVA salary cap). Additionally, no COLA for SERP or similar to SERP non-qualified deferred compensation participants with 10 years or less of actual TVARS service.

### Supplemental Benefit Caps & Eligibility

No change from current rules as to required age and years of service (vested with 10 years of service and age 55). No more accruals of service toward benefit for employees hired on or after 1/1/96 with less than 10 years of service or any employee electing to forego future cash balance pay credits by switching to a 401(k) only plan.

**10 or more years of service:** Cap of \$12.3657 per month per year of service/Cap of \$150.00 per month. May continue to accrue additional years of service at capped rates.

**Less than 10 years of service:** Cap of \$12.3657 per month per year of service/Cap of \$150.00 per month prorated based on current service.

### Raise COLA Eligibility Age

Raise age COLA begins from 60 to 65 for employees and retirees under age 50.

Maximum COLA

Maximum COLA increased to 6% with floor of 0%. COLA formula is modified to provide CPI less 0.25%. COLA is a vested benefit.

Contributions

Greater of minimum formula or \$300 million annually for 20 years or until fully funded.

TVA will have the ability to prepay equivalent contributions.

TVARs Board will have the ability to suspend contribution requirements.

Governance

Changes to the TVARS asset allocation policy that change the actuarial assumed rate of return on the investment of System assets will be subject to TVA review and veto.

Improve retiree representation on TVARS Board (7th director must be TVA retiree).

Amend TVARS Rules and Regulations to provide that, pursuant to TVARS Board policies, the TVARS Board may initiate disciplinary actions toward a director for violation of Board policies up to and including removal of the director from his/her position on the TVARS Board. Removal would require super-majority approval of the TVARS Board.

Provide members right to seek judicial enforcement of TVARS Rules and Regulations.

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462-5. After a lengthy discussion on the proposed amendments, Director Child made a motion to call the question and end discussion. The motion received a second from Director Hoskins. The motion to call the question and end discussion passed by a roll call vote of 4 to 3. Directors Child, Hoskins, Stokes, and Wilson voted for the motion, and Directors Hovious, Muzyn and Troyani voted against the motion.

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462-6. After the vote to call the question and end discussion, the original motion set forth in Minute Entry 462-4 passed by a roll call vote of 4 to 3. Directors Child, Hoskins, Stokes and

Wilson voted for the motion, and Directors Hovious, Muzyn and Troyani voted against the motion.

Director statements submitted regarding the vote

*Statement of Director Child:*

I will keep my comments relatively brief as my comments from March 3rd when we approved our original counterproposal very much hold true today.

As I acknowledged on March 3rd, our plan is underfunded, and actions must be taken to restore the plan to the fully-funded status that we all desire. There undoubtedly continue to be those that think the solution to our funding status is as simple as TVA increasing its level of contributions to the plan. I wish things could be that simple, and I suspect TVA does as well. Unfortunately, just as there's no single reason for how our plan became under-funded, there can be no singular solution for returning it to fully-funded status.

Instead, I believe that creating a healthier System for the benefit of all participants will require both consistent and increased contributions to the plan over the long-term along with modest changes to future benefits shared across all participant groups. I recognize and appreciate TVA's willingness to listen to our feedback and compromise by the acceptance of most of the changes that were included in our March 3rd counterproposal, and in that spirit, I can accept the handful of revisions to that counterproposal that TVA has requested.

Although slightly different from what we approved on March 3rd, I believe this modified proposal continues to represent an appropriate balance between consistent and increased contributions and modest changes to future benefits that will help in putting our plan on a path toward achieving our shared goal of a fully-funded system over the next 20 years.

Accordingly, I recommend all of you to vote to approve this modified proposal.

*Statement of Director Muzyn:*

Our actuary expressed five key concerns with the funding policy in TVA's April 18, 2016 proposal. These concerns were included in a written report to TVARS and are applicable to what the board approved in the May 9, 2016 meeting. Board members owe a fiduciary duty to the beneficiaries of the system to act in their best interest independent of TVA. Therefore, as a TVARS board member, I had no choice but to vote against this proposal. This proposal may help TVA executives meet their goals and receive larger bonuses, but it exposes beneficiaries to these five very serious concerns. I am ashamed to be associated with this board whose majority so clearly demonstrates that they place their own career advancements and financial securities above the duties required of them as members of this board. This is a summary of the five key concerns expressed by our actuary about the proposal:

- It is not clear if participants or TVA are bearing the investment risk if the return on risky assets does not meet the 7% expectation, but someone is bearing that several billion dollar risk.
- There is a substantial risk that needed increases in the minimum contribution formula will not take place rapidly enough due to the continued 30-year rolling amortization of the unfunded liability. Meaningful contributions to the plan would then be required at a time when few, if any, active participants remain in the plan. Generational tension between plan participants and the then current TVA employees could occur to the extent future resources to pay both compensation and benefits are limited.
- If TVA for whatever reason ceases to contribute and the plan has to be settled, there would not be enough assets to settle the plan's obligations unless this occurs in the far distant future after many of the current participants have died.
- By proposing a power of "review and agreement" over asset allocations, TVA limits TVARS' ability to manage risks and participant benefit security.
- It does not include any provisions to more rapidly fund the increase in the deficit related to making lump sum payments. Offering to pay lump sums results in a faster depletion of fund assets and introduces additional volatility in contribution requirements which may not be easily recovered under current rules' 30-year amortization.

*Statement of Director Stokes:*

My statement associated with voting for the counterproposal approved by the TVARS Board on March 3<sup>rd</sup> detailed why I was agreeable to negotiating benefit changes. Those reasons haven't changed. TVA proposed changes. The TVA Board and CEO have said that changes must be made and that inaction is not an option. TVA cannot initiate changes, the only unilateral action that TVA can take is plan termination and I believe that is a real possibility if the TVARS Board takes no action.

The counterproposal approved by the TVARS Board on March 3<sup>rd</sup> was similar to TVA's initial proposal, but I believe kinder to participants based on feedback we received from employees and retirees. There were some elements of the counterproposal that were aggressive relative to TVA's proposal. The counterproposal kept about 3,000 more employees accruing benefits in the defined benefit plan, with a voluntary election to switch to the 401(k) plan, and it kept the interest crediting rate at 6% compared to the 4-1/2% proposed by TVA. The counterproposal also did not address several of the governance items that TVA proposed.

The response from TVA is a compromise and touches 3 benefit components of our counterproposal. It lowers the interest crediting rate on cash balance accounts to 5% from the current and our counter of 6%. That rate would also apply to the fixed fund balances. TVA's response proposes no more contributions to the fixed fund for employees hired after 1.1.1996. Currently those contributions are limited to \$10,000 per year, and employees hired after 1.1.1996

cannot annuitize those balances. They are required to withdraw those funds at retirement. So it is essentially a savings account for these employees earning a higher interest rate than what's available outside the system.

The third benefit component that TVA has proposed a change from our counterproposal is the second supplemental benefit. TVA initially proposed freezing that benefit at \$100.63, and not allowing it to grow with colas to the current cap of \$150. TVARS countered with \$140 cap, and TVA has responded leaving the cap at its current \$150. That's positive for all employees and retirees.

Regarding funding, TVA initially proposed annual contributions of \$275 million for 20 years. TVARS countered with annual contributions of \$300 million and funding any cashouts from the system until it becomes 80% funded. TVA's response provides for funding of \$300 million annually for 20 years and cashouts to be funded from system assets. That's a good compromise and positive for all members of the system. Our actuary has said that the funding method contained in the Rules today is not a best practice. We know that and TVA knows that. I would love to approve a new funding method that is a best practice that funds deficits and amortizes investment gains and losses over shorter time periods, but the TVARS Board cannot unilaterally do that. That requires TVA's agreement and they are not prepared to do that now. Our funding Rules cannot be changed without approval by TVA, but the TVARS Board will continue to annually make a contribution recommendation to TVA based on best practices funding methods. That's the best we can do at this point.

With respect to COLAs, these changes being approved by the TVARS Board today will vest the COLAs, require TVA to start prefunding those benefits, and in the event of plan termination, those COLA benefits will have to be funded and paid just like annuities and pensions. As I stated before when I voted to approve the previous TVARS counterproposal, I have always believed that some sort of negotiated agreement on COLAs between the TVARS Board and TVA was going to be necessary. It has never been my understanding from discussions with the Board's legal counsel that the position we have been taking on COLAs in the lawsuit in any way would prevent the Board from discussing a potential compromise on COLAs in its negotiations with TVA or block the Board's ability to approve such a compromise if one was reached. In the event the courts in the current lawsuit finally determine that the COLAs as originally structured are a vested benefit that couldn't be changed, then the TVARS Board will restore COLA benefits to all affected members and retirees consistent with the courts' rulings.

With respect to governance, TVA does not like supermajority votes proposed by the TVARS Board. I didn't think they would and I understand why. TVA would like the ability to review and agree to any asset allocation changes made by the TVARS Board that impacts the expected rate of return on plan assets, up or down. TVA already has the ability to review and agree to any investment manager hired by the TVARS Board. With TVA's agreement to fund and vest these benefits, I have no problem with TVA reviewing asset allocation changes. Asset allocation is something this Board has historically approved unanimously and is not a political issue. If the system were terminated in the future, TVA would not have the right to review asset allocation changes. That makes sense.

Overall this final response from TVA is much better than their initial proposal. This has been a much better process than past attempts and has been conducted in public for all employees and retirees to see and comment on. Neither TVA nor TVARS got everything they wanted. Neither TVA nor TVARS loves the agreement, but both can live with it. That's how compromise works.

*Statement of Director Troyani:*

I will attempt to make my statement as brief as possible, however, I feel the need to address the items individually. Firstly, I think a meeting of this magnitude involving a \$700 million dollar cut to employees benefits should not have been a teleconference meeting and the rule changes should have been drafted for review prior to the vote. TVARS was created to be a separate legal entity and to perform settlor and fiduciary functions, however, it became evident during this meeting there were 4 Directors who were bound and determined to let TVA tell us what needed to happen and subsequently vote in favor of whatever TVA wanted.

As for the six bulleted items:

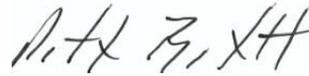
- TVARS can only get money from 3 sources: return on investments, TVA's contributions, and employee contributions. By keeping the interest on the Fixed Fund 2% less than the expected rate of return, TVARS would be foolish to cut off one of our 3 income streams.
- Modifying the interest crediting rate for existing cash balances is unethical and not a widely accepted practice in the industry, however, adjusting the rate for future balances is. This item reduces interest crediting rate on both.
- Item #3 is maintaining the existing monthly cap on the Supplemental benefit.
- I instituted the "Supermajority" language in the TVARS counterproposal and still feel it is necessary to give the beneficiaries some assurance that the 12% match would remain in place in that it would require a TVARS 5 to 2 vote to change instead of 4 to 3.
- Voting in favor of TVARS (instead of TVA) funding lump sum cash outs from a plan that is less than 60% funded is negligent and fiduciarily irresponsible. Under ERISA, this is not allowed if a plan is less than 80% funded and this action clearly shows a lack of commitment from TVA to properly fund the system.
- This item forfeits a large part of TVARS independence which we have worked so hard to enhance through our loaned employee agreement. Also, all of our other rule changes only have a 30 day veto provision, so why is this one 60 days?

There are two other items that were wrapped up in this total proposal that I feel strongly about, one is the desperate impact on participants who are not yet 50 having their COLA eligibility age pushed out to 65. There are around 370 active employees who are in the OB and are not yet 50 and have seen their eligibility age pushed out in the last 7 years from attained age 55, to actual age 60 (in 2009), and now to actual age 65. This is a grave injustice to these long service, older participants, which should not be allowed to happen. Secondly, the eligibility age for the supplemental benefit was dropped to 50 by TVA in their original proposal. I was in favor of total elimination of the age requirement; however, I think it is ludicrous for TVARS to raise the age back up to 55.

In closing, I think that the TVARS Board made a gracious compromise when we voted 2 years ago to have new hires placed in a 401(k) only plan and it is nothing but extortion for TVA to come back now and take \$700 million dollars in benefit cuts from the rank and file beneficiaries of the plan and still maintain a fully funded SERP retirement plan for its' executives.

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The meeting was adjourned at 3:12 p.m., EDT.



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Executive Secretary



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Chair