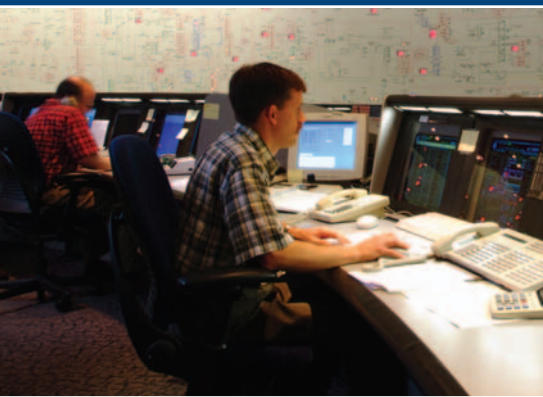


# Budget Proposal and Management Agenda



For the Fiscal Year Ending  
September 30, 2010

Submitted to Congress  
May 2009



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## Introduction

The Tennessee Valley Authority (“TVA”) serves the nation and nearly nine million people of the Tennessee Valley region by achieving measurable success in the three major areas of TVA’s mission — energy, the environment, and economic development. A corporation of the federal government, TVA operates like a business. TVA is self-funded from the sale of electricity and financings that provide capital for the power program. In fact, through 2008, TVA has returned to the U.S. Treasury approximately \$3.5 billion, including interest, on the government’s appropriation investment in TVA’s power program of \$1.4 billion. Established by Congress in 1933, TVA is charged with improving the quality of life in the seven-state Tennessee Valley region by providing navigation, flood control, agricultural and industrial development, and electric power.

**Power Generation System.** TVA provides power for Valley residents through local power distributors and sells power directly to large industries and government entities. As the nation’s largest public power system, TVA is committed to meeting the region’s growing needs for reliable, affordable, and environmentally sound energy. TVA’s power system is setting performance records as it meets power demand.

**Transmission System.** The 2,400 miles of 500kV lines in TVA’s approximately 15,860-mile transmission system are a critical link for the movement of electricity throughout the eastern United States. TVA continues to strengthen system reliability with technology that gives a clearer picture of grid conditions over a wider area at any given time.

**Natural Resource Stewardship.** Another vital part of TVA’s mission is management of the Tennessee River system, the fifth-largest river system in the United States. TVA primarily funds resource stewardship services from power receipts. User fees are also used to a much smaller extent. The 652-mile-long river, the 42,000 miles of streams and tributaries, and the 49 dams and 14 navigation locks operated by TVA are a vital part of the nation’s navigation system, providing for the shipping of over 50 million tons annually. In addition to commercial navigation, TVA’s management of the river system includes reducing flood risk, producing hydro power, and providing cooling water for TVA’s fossil and nuclear plants. Encompassing 41,000 square miles, the river and its 12 tributary watersheds touch 125 counties in portions of seven states. In addition, TVA has direct stewardship responsibility for 650,000 reservoir surface acres available for recreation, 11,000 miles of shoreline, and 293,000 acres of public land.

**Economic Development.** In 1933, TVA was tasked by Congress and President Roosevelt to help develop a vibrant regional economy for the benefit of the people of the Tennessee Valley region. To fulfill this mission, TVA serves as a catalyst for sustainable economic development by assisting states, communities, and distributor customers in recruiting and retaining targeted businesses and industries that provide high economic impact, while balancing TVA’s anticipated future system needs. By providing technical and community development related services to TVA’s various stakeholders, TVA’s economic development strives to help create and retain quality, high-paying jobs and increase the capital investment in the business community to the benefit of the community, the Valley, and TVA as a whole.

**Strategic Plan.** In Fiscal Year (“FY”) 2007, the Board developed a new Strategic Plan in conjunction with TVA staff and consultant support. The Strategic Plan leverages and realigns TVA’s strengths in five key areas: Customers, People, Financial, Assets, and Operations. First, TVA will continue to strengthen relationships with customers by providing reliable and competitively priced power, partnering with them in energy efficiency, power supply, and economic development, and building trust by communicating openly and honoring commitments. Second, it recognizes the importance of TVA’s people by building pride in TVA’s performance and reputation, treating everyone with integrity and respect, and making TVA a safe and desirable place to work. Third, the Strategic Plan emphasizes the necessity of adhering to sound guiding financial principles, spending money when and where it is a good investment to do so, while at the same time adhering to disciplined economic practices. Fourth, TVA’s strategy for assets is to balance production capabilities and load requirements by promoting conservation (i.e., demand reduction), efficient use of electricity, and by adding assets, including renewables. TVA will also continue to manage land and water resources to provide multiple benefits to the Valley. Fifth, through the Strategic Plan, TVA plans to improve its performance to be an industry leader – among the top 25 percent in key areas of operations. A vital part of the Strategic Plan is the metrics by which the Board

will evaluate progress, motivate improvement, and measure success. For each of the five key areas, the Strategic Plan identifies corporate-level metrics to monitor TVA's performance toward successfully implementing its strategy.

**Challenges.** TVA is governed by the TVA Board which is responsible for approving an annual budget. The information included in this document is based on the 2009 Annual Budget which was approved by the TVA Board in August 2008. The following challenges occurred after the 2009 Annual Budget was approved:

**Kingston Fossil Plant Ash Spill.** During the first quarter, an event at the Kingston Fossil Plant ("Kingston"), which TVA operates pursuant to the TVA Act, was reportable to federal, state, and local environmental and emergency response agencies. On December 22, 2008, a dike failed at Kingston located near Kingston, Tennessee, allowing approximately five million cubic yards of water and coal fly ash to flow out onto approximately 300 acres, including approximately 8 acres of land not managed by TVA. TVA currently believes the recovery process will take several years and has prepared an estimate of the total cost of clean up. Some of the material flowed into the nearby Watts Bar Reservoir at Emory River mile 2.5. TVA does not currently have an estimate as to how long the recovery process will take, but has begun to estimate the cost of associated cleanup and recovery activities. TVA has recognized a charge of \$675 million for the six months ended March 31, 2009, in connection with the current expected cleanup costs related to the event. Costs incurred through March 31, 2009, totaled \$77 million. This estimate does not include any amounts for regulatory actions, litigation, fines and/or penalties that may be assessed, final remediation activities or other settlements because TVA cannot estimate these at this time.

**Case Brought by North Carolina Alleging Public Nuisance.** On January 30, 2006, North Carolina filed suit against TVA in the United States District Court for the Western District of North Carolina alleging that TVA's operation of its coal-fired power plants in the states of Tennessee, Alabama, and Kentucky constitute public nuisances. North Carolina asked the court to impose caps on emissions of certain pollutants from TVA's coal-fired plants that North Carolina considers to be equivalent to caps on emissions imposed by North Carolina law on North Carolina's two largest electric utilities. On January 13, 2009, the court held that emissions from the Bull Run Fossil Plant ("Bull Run"), the Kingston Fossil Plant ("Kingston"), the John Sevier Fossil Plant ("John Sevier"), and the Widows Creek Fossil Plant ("Widows Creek") constitute a public nuisance. The first three plants are located in Tennessee, and Widows Creek is located in Alabama. The court declined to order any relief as to the remainder of TVA's coal-fired plants, holding that their emissions did not significantly impact North Carolina. TVA currently estimates that the total cost of taking all of the actions required by the court would be approximately \$1.7 billion through 2014. Of this amount, TVA was already planning to spend approximately \$0.8 billion before the court issued its order. There could be other cost impacts, including fuel, variable operation and maintenance ("O&M"), and fixed O&M, and those costs are under evaluation. TVA is currently reviewing the decision and considering its options.

**Decreased Electric Power Demand.** The effects of the economic downturn are resulting in less demand for electric power by certain customer types. Sales of electricity are about six percent below 2008 levels and could decline further if commercial and industrial employers continue to reduce production in response to the downturn. Through March 2009, directly served industrial sales are down approximately 14.9 percent, while municipal and cooperative sales have experienced a 3.1 percent decline compared to the prior year.

**Investment Performance.** The performance of debt, equity, and other markets in 2008 negatively impacted the asset values of investments held in TVA's pension system and nuclear decommissioning trust ("NDT"). During the period September 30, 2008, through March 31, 2009, the change in the Standard & Poor's ("S&P") 500 benchmark index was a decrease of 31 percent.

**Lower Commodity Prices and Effects on Fuel Cost Adjustment.** Due to falling commodity prices across domestic and international markets, TVA experienced lower-than-expected costs in short-term markets for natural gas, fuel oil, and electricity during the second quarter of 2009. The average market prices for these commodities for the six months ended March 31, 2009, were 47 percent, 52 percent, and 41 percent lower, respectively, as compared to the average market prices for the six months ended March 31, 2008. Coal markets have reacted more slowly than other fuel markets and remain well above the previous year's levels. Average market prices for coal for the six months ended March 31, 2009, were 15 percent higher as compared to the average market prices for the six months ended March 31, 2008.

Weather Conditions. Rainfall in the eastern Tennessee Valley was 86 percent of normal and runoff was 66 percent of normal for the six month period ended March 31, 2009. Hydroelectric generation increased during the six month period ended March 31, 2009, as compared to the same period in 2008. Hydroelectric generation was 5.3 billion kilowatt-hours during the six month period ended March 31, 2009, which was nearly 2 billion kilowatt-hours higher than the same period of 2008.

Pending Legislation. There is currently pending federal legislation in Washington involving clean or renewable energy, and depending on the bill that gets approved, TVA might have to ensure that anywhere from four percent to 25 percent of the energy it sells is produced by clean or renewable sources.

## **Management Initiatives**

### **Overview**

In striving for higher standards of performance, TVA is implementing several management initiatives to further improve the quality of its services and the efficiency with which those services are delivered. The following sections highlight TVA's management efforts:

- 1 – Strategic Management of Human Capital**
- 2 – Commercial Services Management**
- 3 – Improved Financial Performance**
- 4 – Expanded Electronic Government**
- 5 – Budget and Performance Integration**

## 1. Strategic Management of Human Capital

Many of the challenges the Federal Government faces in managing people have already been identified within TVA, and improvement initiatives that are well under way are achieving measurable results and identifying opportunities for further improvement.

TVA's comprehensive performance management process, which is called "Winning Performance," tracks TVA's performance on 24 critical success factors ("CSFs") and reports results monthly on the TVA-wide Balanced Scorecard. In line with TVA's performance-management initiatives, TVA's Human Resources ("HR") practices are characterized by a focus on measurement.

### Integrated Staffing Planning

Effective workforce management is a key principle of TVA's overall management strategy. As the scope and nature of TVA's business has changed during the past 20 years, so has the agency's staffing needs. For example, as TVA's focus shifted away from building power plants, staffing levels have been adjusted. During the past two decades, TVA's employment level has dropped from about 47,000 to about 12,000 — a reduction of 74 percent. Today, as a result of past downsizing actions and attrition, TVA's fundamental human resource challenge is identifying, retaining, and developing a capable workforce for the future. The TVA employee average age is 46 years, slightly older than the electric utility employee average of 45 years cited in the American Public Power Association study. In addition, average employee tenure is 15 years.

### Knowledge Retention

TVA has developed and begun to implement a process to capture the most critical undocumented knowledge of employees nearing retirement. This process enables line managers to identify critical knowledge and skills that may be lost through attrition, to evaluate the risk associated with losing the knowledge and skills, as well as develop, implement and evaluate action plans for managing the risk.

### Craft Pipeline Training

After many years of relying on a traditional single-discipline maintenance workforce, TVA transitioned to a new multi-craft / multiple-skill pipeline training program for maintenance workers at the fossil and nuclear power plants. Likewise, operations as well as maintenance skills are now included in a single pipeline program for workers at TVA's hydro generating facilities. In both cases, TVA was able to reduce the training program length from 4 years to 2.5 years, supporting improvements in labor expense as well as increased flexibility in workforce planning.

### Recruiting

Along with addressing the ongoing trend in retirements, TVA is fine-tuning its recruiting efforts. Trades-and-labor employees and experienced supervisors and managers are the majority of new hires at TVA, and this trend is expected to continue. Major TVA business efforts are anticipated that will significantly increase the need for additional talent (i.e. nuclear resurgence initiatives, transformation of certain business units and their functions, etc.).

### Succession Planning/Talent Management

In addition to its efforts to develop all its employees, TVA has implemented a focused talent management process to help identify and develop future leaders. The intent of this effort is to ensure that TVA has qualified internal candidates ready to meet its future leadership needs.

In 2006, TVA executives began utilizing a common, structured process for evaluating talent and identifying potential successors for key positions. Current talent assessment efforts utilize the "Nine-Box" model of assessing employees' current performance and future leadership potential. Particular attention is then paid to the development (training, rotational assignments, mentoring, etc.) of identified high potential employees and to improving the performance of the lowest performers.

### New Employee Engagement

TVA continues to improve and standardize the orientation experience for new employees. TVA uses Gallup research to guide its emphasis on improved employee engagement as a direct contributor to critical success factors for TVA. Benchmark data shows that a positive and content-rich orientation experience contributes to employees becoming productive faster and more effectively.

**Integrated Performance Management**

TVA's success depends on the performance and productivity of every employee. To ensure that performance expectations are met, TVA established an Integrated Performance Management ("IPM") system that aligns job performance with compensation awards, employee development activities, and TVA's strategic objectives. A standardized IPM calendar of activities is followed.

**Winning Performance**

Winning Performance is the process TVA uses to manage performance. This process reflects the Strategic Objectives and Critical Success Factors identified in the Strategic Plan, identifies TVA-wide implementation plans needed to achieve the expected results, closely monitors performance, and rewards successful achievement of results.

The Winning Performance Team Incentive Plan ("WPTIP") has introduced the concept of pay for performance to employees to give everyone a stake in the performance of the agency. TVA awards employees a lump-sum payment ranging from 0 to 16 percent depending on the composite performance results that are tracked on the TVA-wide and organization-specific scorecards. Individual WPTIP awards depend on the performance of TVA and the Business Units against goals set at the threshold, target, and stretch levels.

**Corporate Learning and Organizational Effectiveness**

TVA's Training and Development Organizational ("T&D") group provides leadership in the areas of Corporate Learning and Organizational Effectiveness, and provides a suite of services ranging from supervisory and leadership development to craft pipeline training. Other products and services include culture change and organizational effectiveness consulting. T&D serves the TVA workforce which is spread over a seven-state service area and works across a 24-hour, seven-day schedule. TVA uses a Performance Consulting model to identify and deliver appropriate solutions.

**Human Resource Information Systems**

Technology is also improving productivity in TVA's HR function and is enabling HR to revolutionize its paper-driven administrative tasks. Since 1997, HR has changed its focus from conducting administrative activities to serving as a strategic business partner with a focus on Human Capital Asset Management. A key element in this transition is *Self-Service Solutions*, which puts information and accountability in the hands of the decision-makers. *Self-Service Solutions* include interactive voice response, Web tools, and an Employee Service Center.



## 2. Commercial Services Management

TVA's supply chain philosophy includes focusing on overall contracting strategy rather than individual transactions. This emphasis on an overall contracting strategy requires obtaining the lowest total ownership cost for goods and services. This practice looks beyond purchase cost or price alone as the driving factor; in fact, many factors determine the lowest total ownership cost.

### Strategic Sourcing

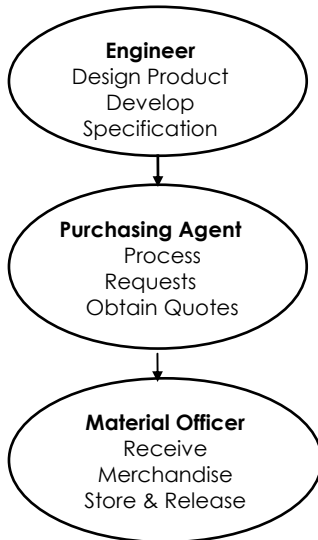
In using this focus on lowest total ownership costs, TVA follows a six-step process for "strategic sourcing." Strategic sourcing refers to a systematic methodology in which the total ownership costs of goods and services required by TVA are reduced while quality, service, and technology are improved.

### Sourcing Group Strategy

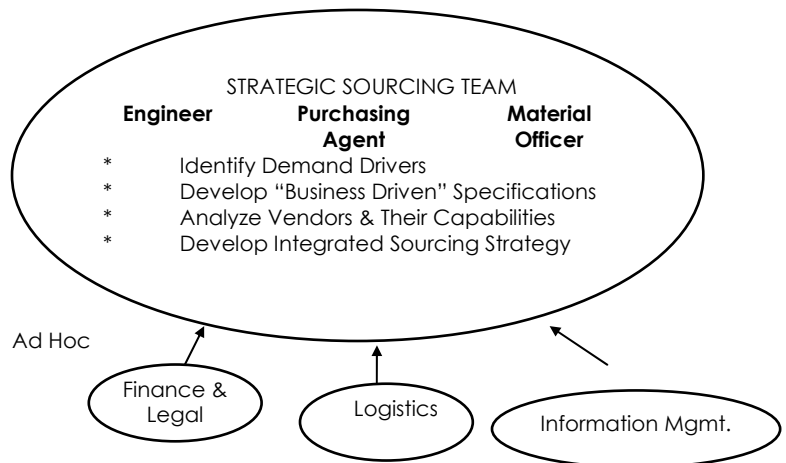
TVA has also developed a sourcing group strategy in which materials and services are grouped into 44 commodity families and a sourcing group manager is assigned to each family. The sourcing group manager is typically a contract manager or contract agent tasked with ensuring that a product or service is efficiently managed. In this role, the sourcing group manager calls upon cross-functional teams from the supply chain and customer organizations to manage the commodity. This approach is characterized by joint team responsibilities, enhanced communications, consistent supplier interface, short cycle times, common focus, and ownership.

The model below shows an example of strategic sourcing and how it differs from a traditional procurement approach:

#### TRADITIONAL HIERARCHICAL APPROACH



#### STRATEGIC SOURCING MODEL



### Standardized Business Practice

TVA has standardized its business practice governing the supply chain to help lower total costs. The improved business practice includes all activities, processes, and systems related to sourcing strategy; supplier relations; contracting for products and services; transportation and logistics; and materials management, including receipts, warehousing, distribution, inventory strategy, inventory management, disbursement, and disposal of surplus personal property.

TVA's Supply Chain policy outlines criteria on which TVA bases its supply management decisions. As mentioned, TVA considers not only price but also other factors essential to achieving the best value. These include cost, quality, competition, leverage, standardization, inventory optimization, and supplier relations.

### 3. Improved Financial Performance

#### Oversight and Governance

TVA is committed to conducting business in an open and forthright manner that earns the confidence of the Executive Branch, Congress, and TVA's investors and customers. Investors in TVA benefit from oversight, auditor independence, corporate responsibility, and TVA's commitment to timely, accurate, and comprehensive financial disclosure.

In December 2004, the President signed the Consolidated Appropriations Act, 2005, which amends the Securities Exchange Act of 1934. This act requires TVA to file annual reports with the Securities and Exchange Commission (SEC), beginning with the 2006 Annual Report filed on Form 10-K, as well as periodic, current, and supplementary information, documents, and reports. In December 2006 and June 2008, the SEC adopted rules which provide further deferrals of the reporting requirements of Sarbanes-Oxley Section 404 for non-accelerated filers such as TVA. Under these rules:

- The management reporting requirements of Section 404 became effective for non-accelerated filers for fiscal years ending on or after December 15, 2007.
- The auditor reporting requirements of Section 404 become effective for non-accelerated filers for fiscal years ending on or after December 15, 2009.

#### TVA Oversight – A Different Mission with Different Oversight

TVA is a government-owned corporation, and its mission is fundamentally different than that of publicly traded companies. TVA is governed by the TVA Board. The Consolidated Appropriations Act, 2005, amended the TVA Act by restructuring the TVA Board from three full-time members to nine part-time members, at least seven of whom must be legal residents of the TVA service area. TVA Board members are appointed by the President of the United States with the advice and consent of the U.S. Senate. The TVA Board, among other things, establishes broad goals, objectives, and policies for TVA; establishes long-range plans to carry out these goals, objectives, and policies; approves annual budgets; establishes and oversees rates; and establishes a compensation plan for employees.

Chief Executive Officer – Tom Kilgore was named President and Chief Executive Officer (“CEO”) in October 2006 after having served as President and Chief Operating Officer since joining TVA in March 2005.

An Audit Committee – The TVA Board established the Audit, Governance, and Ethics Committee. The committee is responsible for recommending an external auditor to the TVA Board, overseeing the auditor's work, and reviewing reports of the auditor and Inspector General, among other activities.

An Independent Auditor – TVA's independent auditor audits TVA's financial statements in accordance with standards of Public Company Accounting Oversight Board (United States) and with *Government Auditing Standards* issued by the Comptroller General of the United States. The auditor also provides an opinion on whether those statements are presented in conformity with U.S. Generally Accepted Accounting Principles (“GAAP”).

An Independent Inspector General – TVA has an independent Office of Inspector General (“OIG”), that conducts ongoing audits of TVA's operational and financial matters in accordance with *Government Auditing Standards*, which incorporate the American Institute of Certified Public Accountants’ (“AICPA”) generally accepted auditing standards. The OIG's staff has about 104 employees, including more than 50 auditors. TVA's Inspector General was previously appointed by the TVA Board, but pursuant to legislation enacted in November 2000, is now appointed by the President of the United States. The OIG provides semiannual reports to Congress on the results of its audit and investigative work. Additional reports will be reviewed by the Audit, Governance, and Ethics Committee.

Congressional Oversight – Congress provides formal oversight of TVA through two committees, the U.S. House of Representatives Transportation and Infrastructure Committee and the U.S. Senate Environment and Public Works Committee. The audit arm of Congress, the Government Accountability Office (“GAO”), also conducts audits of various TVA activities and programs, generally at the request of members of Congress.

Executive Branch – TVA routinely submits budget information to the Office of Management and Budget (“OMB”), and TVA's budget is included in the consolidated budget of the U.S. Government. Additionally, TVA's financial results are included in the federal government's financial statements, which are coordinated with the U.S. Treasury and are subject to audit by the GAO.

The TVA Act – TVA’s congressional charter, the TVA Act of 1933, as amended, defines the range of TVA’s business activities. TVA is also subject to the Government Performance and Results Act (“GPRA”), which requires that a strategic plan and annual performance reports be submitted to Congress.

Other Regulatory Oversight – In aspects of its operations, TVA is subject to regulations issued by other governmental agencies, including the Environmental Protection Agency, state environmental agencies, the SEC, and the Nuclear Regulatory Commission. TVA also complies with applicable regulations of other federal agencies, such as the Department of Labor’s Occupational Safety and Health Administration. Additionally, while TVA is generally not subject to regulations issued by the Federal Energy Regulatory Commission (“FERC”), FERC has some regulatory authority over TVA activities. Other organizations with major influence on TVA and others in the electric utility industry include the North American Electric Reliability Council and the industry-based Institute of Nuclear Power Operations.

#### **Auditor Independence – Providing Assurance to Stakeholders**

The TVA OIG conducts an annual audit of the work of TVA’s independent auditor to ensure compliance with generally accepted government auditing standards. To ensure that the OIG performs its audits in accordance with generally accepted government auditing standards, a peer review audit of the OIG is conducted every three years by another federal Inspector General’s office.

#### **Accounting and Financial Reporting**

TVA’s financial transactions are subject to audit by the Comptroller General under various statutes. Further, TVA’s financial statements are annually audited by independent auditors. TVA also submits financial information to OMB, the U.S. Treasury, Energy Information Agency, Nuclear Regulatory Commission, and others, in accordance with regulatory and statutory requirements. As required by the TVA Act, TVA maintains its accounting records in accordance with the FERC’s Uniform System of Accounts for Public Utilities. In addition, TVA presents its financial statements and related disclosures in conformity with GAAP promulgated by the Financial Accounting Standards Board.

#### **Financial Reporting and Disclosure**

TVA publishes an annual report that contains audited financial statements and an opinion letter from the independent auditors. TVA’s Annual Report includes comparative financial information, and in 1990, TVA began publishing quarterly financial statements reviewed by independent auditors. In 2003, TVA began including its complete Information Statement with its annual report. In December 2006, TVA filed its first Annual Report (10-K) with the SEC and now files all annual reports (“10-Ks”), quarterly reports (“10-Qs”), and current reports (“8-Ks”) with the SEC.

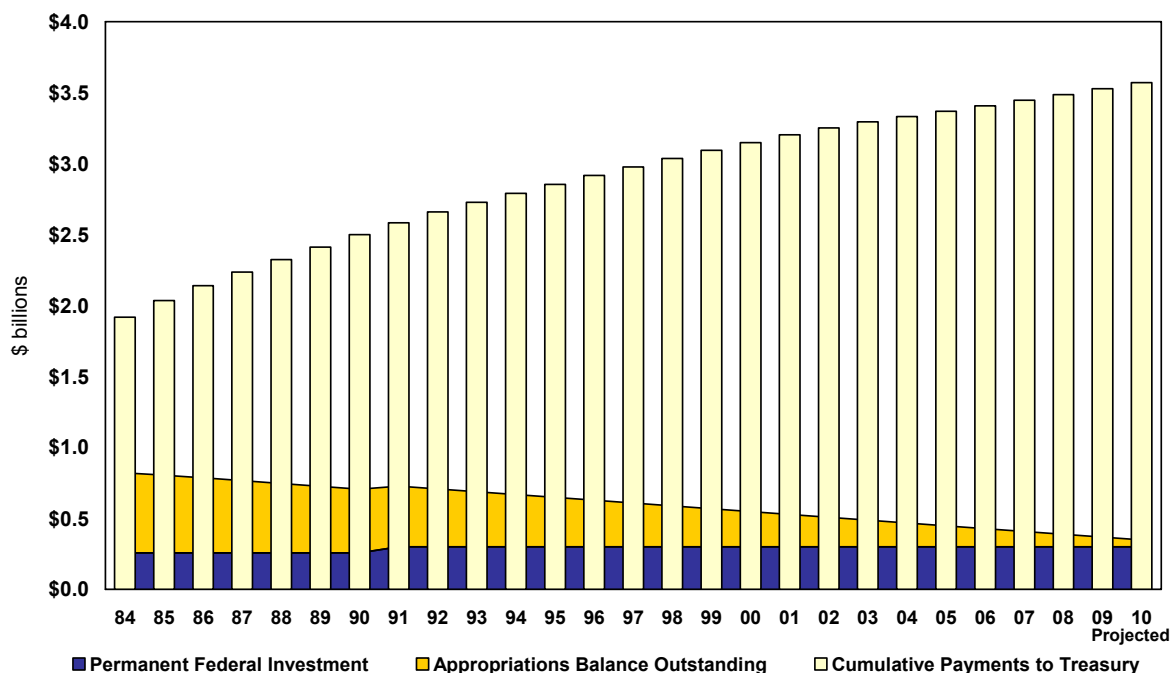
#### **Monthly Reporting Process**

Internal financial performance reporting is done on a monthly basis at all levels within the enterprise and on a weekly basis within some business units. The monthly financial performance reports contain explanations of actual-versus-budget and prior-year spending for each line item on the cash flow statement and statement of capital expenditures. In addition, the income statement contains explanations on actual versus budget for the current fiscal year. The reports also include a balance sheet analysis detailing significant changes during the reporting period and non-financial performance indicators comparing actual results versus targets. TVA also performs agency-wide financial forecasts on a monthly basis in order to anticipate and respond to events that may have a significant impact on financial performance during the year.

#### **Financing the Business**

For more than 40 years, TVA’s power program has provided a positive cash flow to taxpayers by repaying the government’s appropriation investment in the TVA power program along with a yearly return payment. Through 2010, these payments are expected to total an estimated \$3.6 billion on the federal government’s investment of \$1.4 billion. Under the TVA Act, the government will retain permanent equity in TVA.

### Power Program Appropriation Repayment



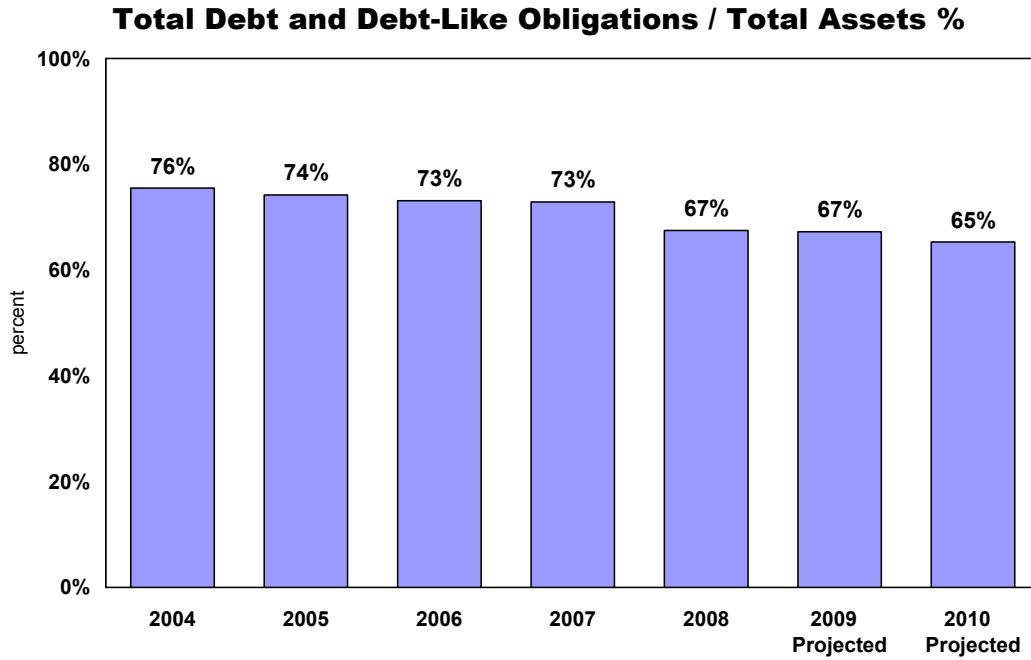
TVA uses a Debt Service Coverage (“DSC”) methodology for calculating its revenue requirement. The DSC methodology provides for recovery of normal operating costs, debt service (i.e., both annual principal and interest payments), and other required costs (i.e., decommissioning, pension contributions) necessary to maintain TVA’s credit quality. TVA also uses a cost of service methodology. Several components in the revenue requirement changed significantly from FY 2004 to FY 2007. Many of these costs, such as fuel and purchased power expense, and nuclear security measures, experienced increases that are largely beyond the control of TVA.

#### Financial Health

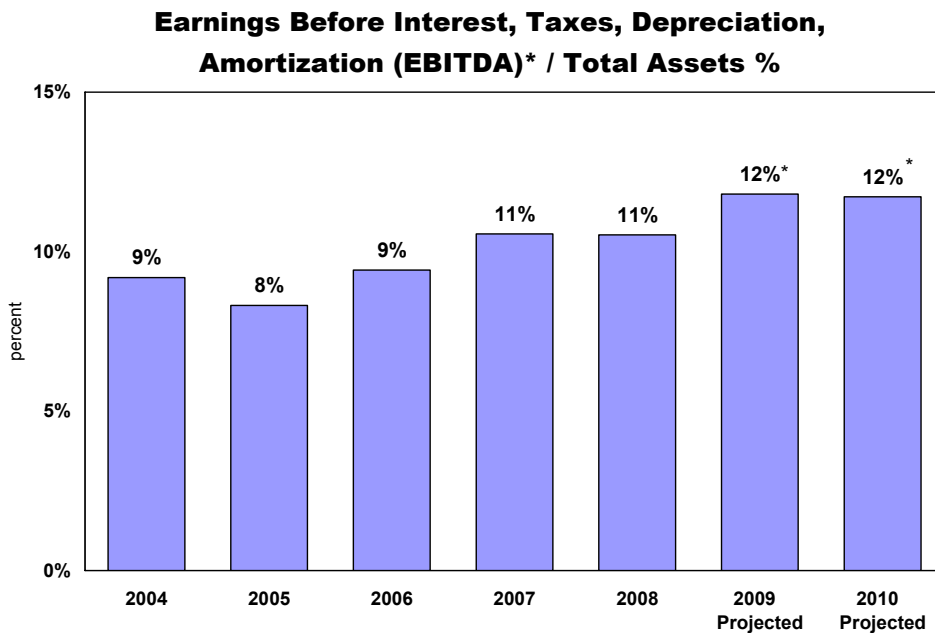
TVA’s financial information includes estimates with significant uncertainty relative to the weather, the economy, fuel prices, etc. which are subject to changing conditions. TVA is self-funded from the sale of electricity and financings that provide capital for the power program. Unlike investor-owned utilities that issue stock, TVA’s sources of capital are more limited. Maintaining TVA’s AAA credit rating is a key component of TVA’s financial strategy. This strategy is centered on applying sound decision criteria to new investments; retiring debt before the associated assets are retired; improving the balance sheet by improving the ratio of financing obligations to total assets; and improving cash return on total assets for the purpose of debt payment, asset investment and investments to improve environmental performance. TVA plans to continue to make decisions necessary to further sound financial performance. TVA’s liquidity is enhanced by several factors. The TVA Board has the ability to adjust rates on a quarterly basis, if needed. Additionally, the fundamentals of TVA’s business and high credit rating allow ready access to capital markets when needed, while TVA’s discount-note program provides TVA the short-term capital it needs to fund daily operations. TVA plans to:

- Invest in new capital projects and leases when economically justified or needed to meet regulatory requirements, such as clean air compliance;
- Pay down new financial obligations through revenue or savings generated from the investments they were used to fund; and
- Retire financial obligations before the value of the associated assets in the portfolio is depleted.

These actions will allow TVA to maintain a balance of financing obligations that is manageable and commensurate with its level of assets. TVA will track its financial health by measuring Total Debt and Debt-Like Obligations as a percent of Total Assets.



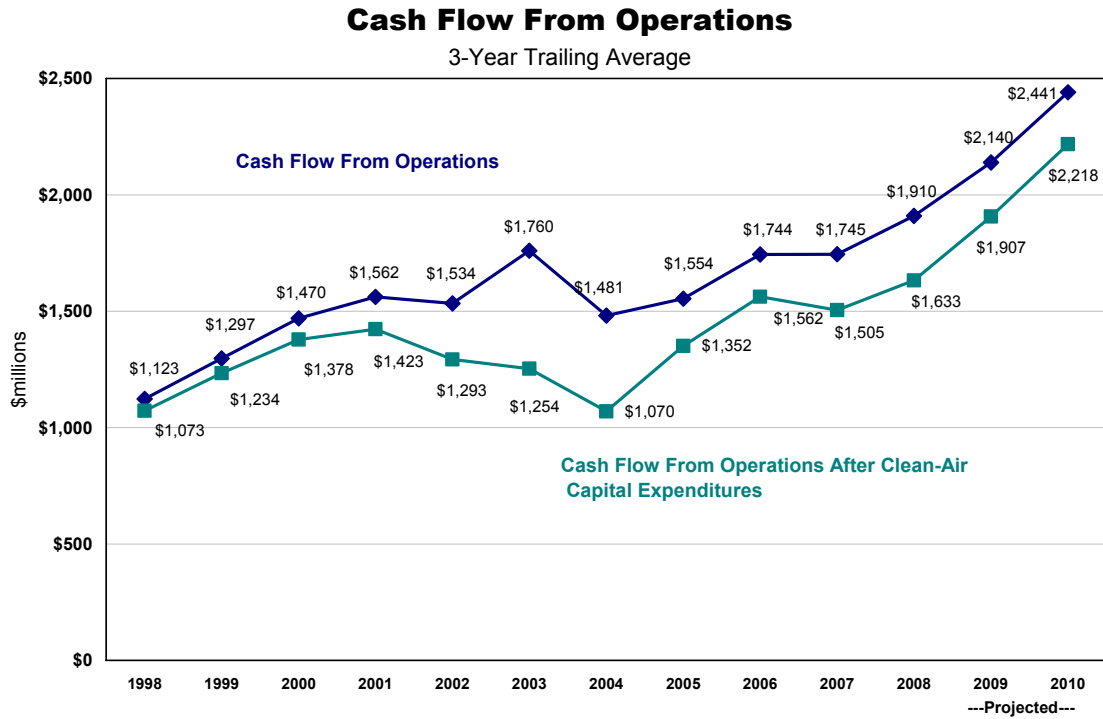
In addition to sound criteria for new investments, improving non-fuel O&M expenses is a central component of TVA's operations strategy and a key aspect of achieving cash return on assets. TVA intends to achieve top-quartile performance in non-fuel O&M expenses. The measure of this goal will be a ratio of Earnings before Taxes, Interest, and Depreciation and Amortization ("EBITDA") to Total Assets. See Appendix for a reconciliation of EBITDA, which is a non-GAAP measure, to the most directly comparable GAAP measure.



\*See Appendix for a reconciliation of EBITDA to the most directly comparable GAAP measure.

**Cash Flow from Operations (3-Year Trailing Average)**

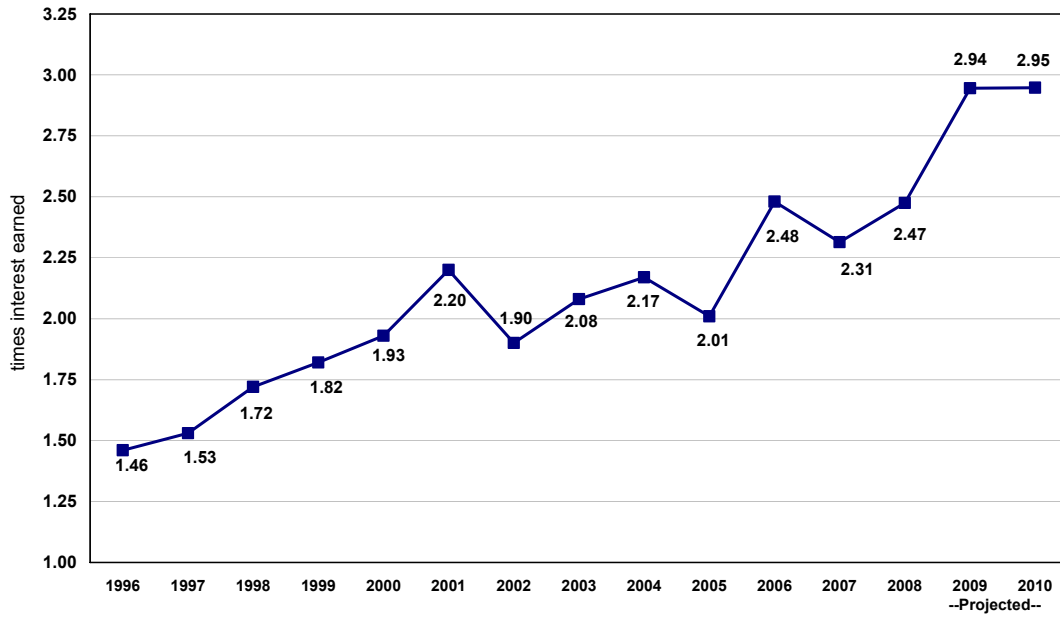
The amount of cash that TVA generates from its operations during the year – operating cash flow – is one of the best ways to measure TVA’s ability to meet its short-term obligations. Because power revenues and cash flow are greatly affected from year to year by weather and economic conditions, TVA uses a three-year average cash flow to provide a measure of its financial health.



**Interest Coverage**

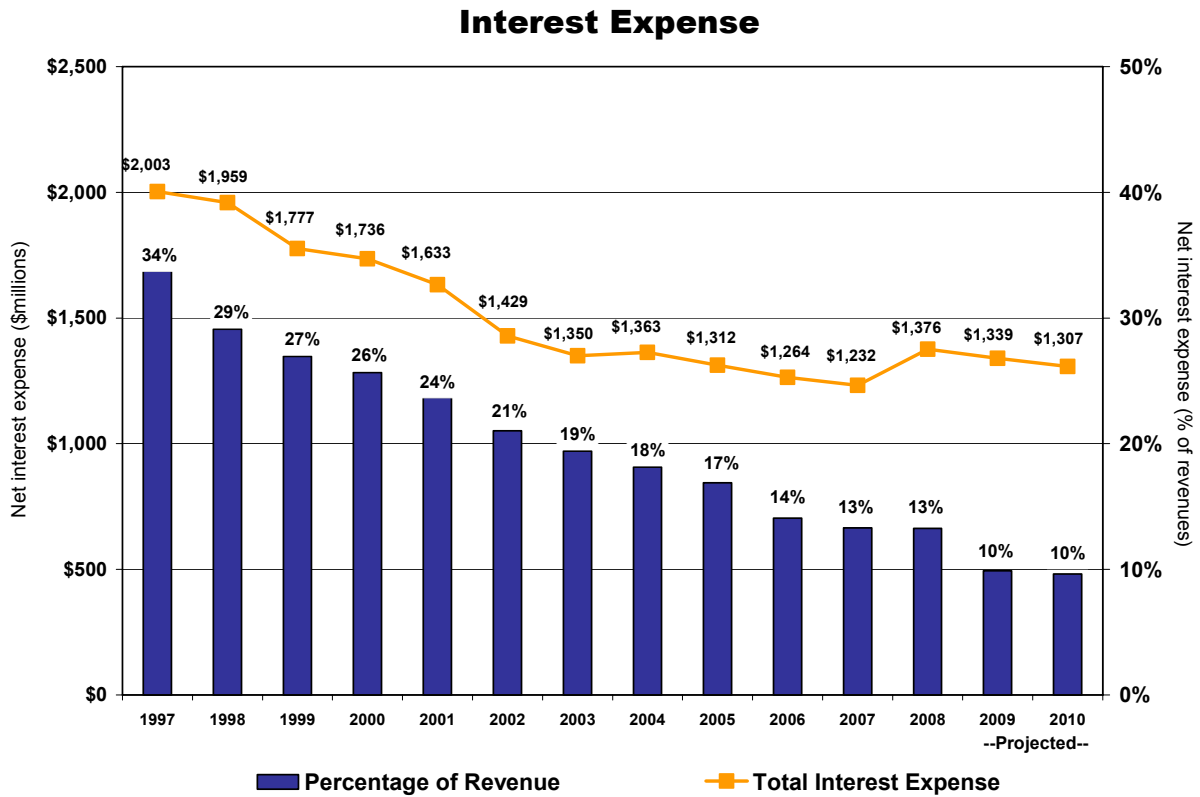
TVA’s ability to service its statutory debt, measured by the degree to which annual cash flow covers interest obligations, has also improved over the past several years as annual cash flow has generally increased and debt has been reduced.

### Interest Coverage Ratio



### Interest Expense

TVA intends to continue to manage fixed costs including interest expense. Annual interest expense was more than \$2 billion at its peak. This amount has declined 31 percent, to \$1.4 billion in 2008. In 1997, annual net interest expense as a percentage of total revenues was 34 percent. That figure has been reduced to only 13 percent of revenues for 2008 and is expected to decrease to 10 percent in 2009 and 2010.

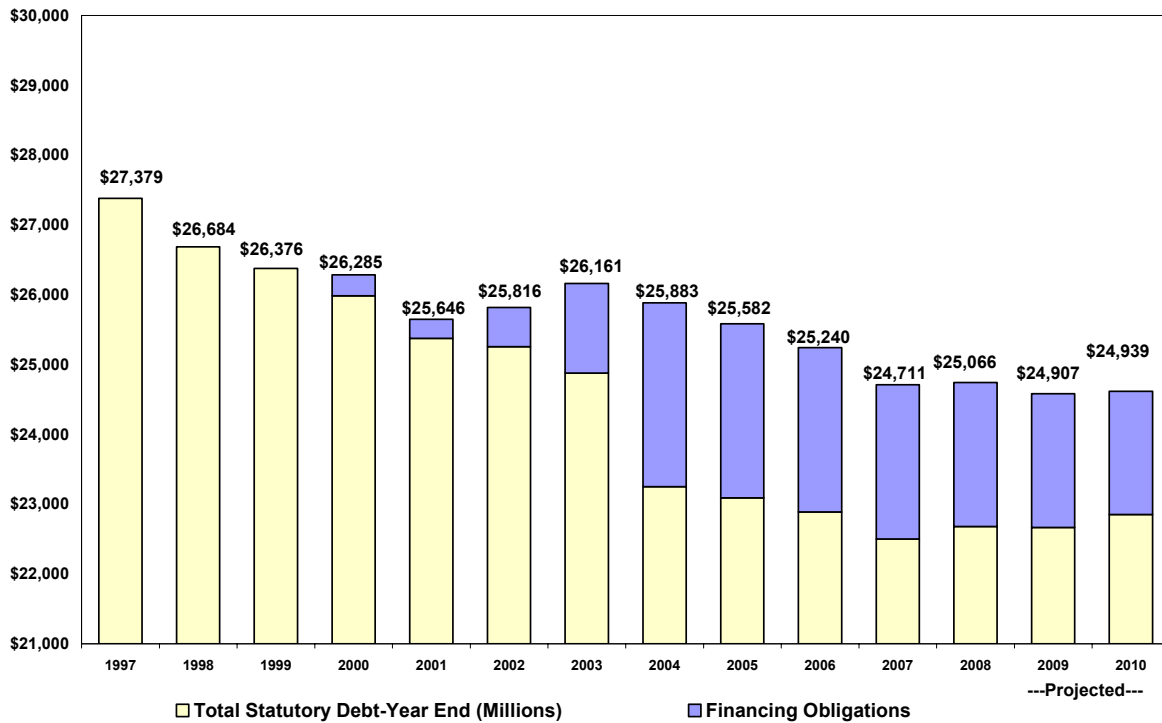


**Financing Obligations**

From 1997 through 2008, TVA has reduced its Total Debt and Debt-Like Obligations, which include both statutory debt and alternative financing mechanisms such as certain lease obligations and prepaid energy obligations, by nearly \$2.3 billion. This includes a net reduction of statutory debt of approximately \$4.7 billion during that same period.



**Total Debt and Debt-Like Obligations at Year End**  
(in millions)



**Credit Facilities**

The TVA Board has approved TVA entering into a credit facility or facilities not to (collectively) exceed \$5 billion. Thus far, TVA has entered into two such facilities, which allow TVA to borrow up to \$2.25 billion. This is not intended to be used as a tool to manage daily cash operations or as a primary source of funding. Any outstanding obligations on the facilities count towards TVA’s statutory debt limitation. TVA has not borrowed any money under the credit facilities.

In December 2008, TVA and the U.S. Treasury replaced a \$150 million note with a memorandum of understanding under which the U.S. Treasury provided TVA with a \$150 million credit facility. There were no outstanding borrowings under the facility at March 31, 2009.

**Risk Management**

As the power industry continues to change, companies across all aspects of the industry are exposed to new challenges and new risks. TVA meets these challenges by managing risk in order to keep power rates in the Tennessee Valley as low as feasible. Other industry participants, such as investor-owned utilities, energy marketers, and independent power producers, seek to increase shareholder wealth and sometimes accept higher risk in order to maximize profit.

**Power Supply & Fuels**

The Power Supply & Fuels group manages TVA’s fuel and purchased power portfolio (which is expected to be \$6 billion in FY2010). This is done in part through buying and selling power in the wholesale electricity market, with the goal of ensuring the optimum utilization of TVA’s system assets, thus supporting TVA’s objective of providing reliable and affordable power. The Fuels Supply group also manages the supply of natural gas, coal, and fuel oil for the fossil fleet. It also purchases natural gas for the combustion turbine generation units and the energy conversion agreements. The Fuels Supply group is responsible for buying coal and fuel oil for meeting system requirements or, on rare occasions, selling surplus fuel in the coal and fuel oil markets.

## 4. Expanded Electronic Government

Information technology ("IT") is a critical tool for TVA. The reliability and safeguarding of information, information systems, and telecommunications equipment is a top priority. TVA is committed to the continuous improvement of the agency's IT systems. TVA directs its efforts at developing and maintaining IT solutions to serve the interests of our stakeholders, and most importantly, serving the citizens of the Tennessee Valley. As the initiatives described in this report illustrate, TVA's resources are focused on developing and maintaining solutions that provide innovative business solutions through IT. The result has been an improvement in both TVA's business processes and its community relationships.

TVA also supplies the public with electronic information about the power program, the river system, campground reservations, financial stability, environmental impacts, employment opportunities, and other topics of interest.

TVA's expanded Electronic Government initiatives fall into six specific areas:

Major Process Improvements include: Implementation of Federal Information Security Management Act, NERC Critical Infrastructure Protection standards, NRC cyber security, Federal Desktop Core Configuration, agency-wide cyber security governance, access and identity management, vulnerability management, control system security, Online Connection, Enterprise-Wide Supply Chain, Enterprise Asset Management, Contractor Workforce Management, Electronic Corrective Action Program, Primavera Project Scheduling (P3e), Enterprise Performance Management, and TVA Enterprise Lessons Learned Database.

Financial e-Government initiatives include: Financial Systems Replacement, TVA Information Factory, and Self-Service Solutions.

Financial e-Government Applications include:

- Ninety-nine percent (99 percent) of all dollars are disbursed electronically.
- Ninety-seven percent (97 percent) of all payment transactions (payroll, vendor, and other) are electronic.
- A Web-based Cash Management System is used to record and account for all funds received by TVA.
- A Web-based payment system is used by distributors and directly served customers in the Automated Clearing House Program or Prepayment Program.
- A Web-based Vendor Invoice Query System allows vendors to see, via the Internet, the status of their invoices, as well as the payment date and check number.
- A Web-based system is used to auction short-term discount notes among TVA's selling-group members in a competitive, fees-inclusive environment, allocating the discount notes by the lowest rate bid being awarded first.

Customer-Centered Initiatives include: Real Time Pricing Applications and e-Distributor Annual Reporting.

Citizen-Centered Initiatives include: Recreation use of TVA reservoirs and TVA's external Web site. The following are examples of information available on TVA's site and routinely requested by the public:

- General TVA information data, such as the history and leadership biographies;
- Employment opportunities, including tips on applying for positions within TVA;
- Overviews of the TVA power system, including fossil fuel generation, hydroelectric power, nuclear energy and transmission;
- Environmental management data, such as air emissions and water quality ratings for plants or reservoirs, as well as federal environmental standards and scientific papers authored within TVA;
- Land management issues;
- TVA's Clean Water, Clean Marina, and Clean Boating campaigns, with links to resources such as EPA;
- Valley precipitation and stream-flow data for recreational users and commercial barge traffic;
- Highlights of the Spring Sport Fish Survey, of interest to local anglers;
- Opening and closing dates for TVA campgrounds;
- Financial news and information, including TVA's Annual Report, as well as an automatic e-mail alert system for investors interested in TVA financial news; and
- Links to TVA's Web site for TVA's retiree community.

TVA has also established an Environmental Information Center ("EIC"), a single source for answers to questions about a variety of environmental topics. The EIC may be accessed either via telephone during business hours or electronically via e-mail. The environmental topics normally addressed by the EIC include:

- Recreation, including boating, hunting, fishing, and camping;
- Shoreline actions and issues;
- Permitting procedures;
- Reservoir land plan information;
- Water quality;
- Archaeological information;
- Natural resources information;
- Environmental education;
- Sport fishing; and
- Other environmental issues

If an inquiry is outside the EIC's area of expertise, it is provided to the appropriate TVA organization for a response.

Major IT Initiatives include: HSPD-12, DNSSec, control system network segmentation, intrusion prevention system, centralized security monitoring, network access control, security information and event management, Governance Risk Compliance tool, Enterprise Systems Program, Unified Communications Strategy, Enterprise Information Management Strategy, Enterprise Document Management, and Service Level Management.

## 5. Budget and Performance Integration

### Integrated Performance Management – “Winning Performance”

The enterprise-wide performance management program, called Winning Performance, uses a process-based methodology tracked by a balanced scorecard to: *establish priorities for key objectives, measure and report performance in the key areas, provide line-of-sight between priorities and individual activities, and link individual compensation to company-wide results.* Winning Performance enables TVA to stay on top of strategic situations and ensure that new challenges and issues are addressed. It helps measure TVA’s performance and it identifies the areas of commitment for employees, financial health, and company resources.

### Measuring Winning Performance

#### The Balanced Scorecard

The balanced scorecard is the measure of TVA’s success. It gives employees monthly and yearly status updates on how TVA is meeting its critical objectives as a company and as Strategic Business Units (“SBUs”). The metrics are balanced between customers, people, financial, and assets / operations and reflect TVA’s overall performance. Six SBUs and many individual Business Units (“BUs”) have metrics that align with and support the TVA level scorecard. In addition, these scorecards are accompanied by variance analysis and action plans to ensure the SBUs and BUs are working toward the company’s overall goals. The TVA scorecard, which outlines the performance of the company as a whole, is distributed monthly to employees through InsideTVA (the company newsletter), posters and bulletin boards, and in individual SBU and BU newsletters. The information also is available on TVA’s intranet.

TVA Balanced Scorecard								
FY 2009								
Customers	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Retail Price (¢ / kWh Sales)</a>						8.40		
<a href="#">TVA Delivered Cost of Power Excluding FCA Costs (\$ / MWh Sales)</a>						35.89		
<a href="#">TVA Fuel Cost Adjustment Costs (\$ / MWh Sales)</a>						33.85		
<a href="#">TVA Economic Health Index (Percent)*</a>						100		
<a href="#">TVA Participation in Energy Efficiency &amp; Peak Shaving Initiatives (Percent)*</a>						98		
<a href="#">TVA Customer Satisfaction Survey (% Satisfied)*</a>						82		
<a href="#">TVA Connection Point Interruptions (Interruptions / Connection Point)</a>	20%						1.12	0.78
People	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Cultural Health Index*</a>						66.3		
<a href="#">TVA Safe Workplace (Injuries / Hours Worked)</a>						1.62		
Financial	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Debt-like Obligations / Asset Value (Percent)</a>						67.3		
<a href="#">TVA Funds From Operations / Interest (Ratio)</a>						2.6		
<a href="#">TVA Net Cash Flow from Operations less Investing (\$ Millions)*</a>	35%						Budget less Revenue Adjustment	Budget Exceed Budget by \$50M
Assets / Operations	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Key Environmental Metrics (Index)*</a>						100		
<a href="#">TVA Megawatt Demand Reduction (MW Reduced)</a>						154	162	170
<a href="#">TVA Demand Reduction (\$ / kW Reduced)*</a>	10%					643	611	582
<a href="#">TVA Equivalent Availability Factor - Coal, CC &amp; Nuclear (Percent)</a>	35%					85.8	87.1	88.0

### Translating TVA’s Strategic Plan into Operational Terms

TVA’s mission and strategic objectives are translated into operational terms to align the actions of management and employees. Defining the critical success factors (“CSFs”) is the first step. CSFs define the key factors and capabilities needed to generate sustainable performance consistent with the business themes of the mission and the priorities identified by the Strategic Plan.

Performance goals identify specific, tangible objectives for measuring achievement. TVA develops a strategy in the context of the mission, maps the strategy into operational initiatives, and ultimately develops performance plans for each part of the organization and scorecards for measuring success.

# Performance Goals and Results

## Goal 1: Supplying Low-Cost, Reliable Power

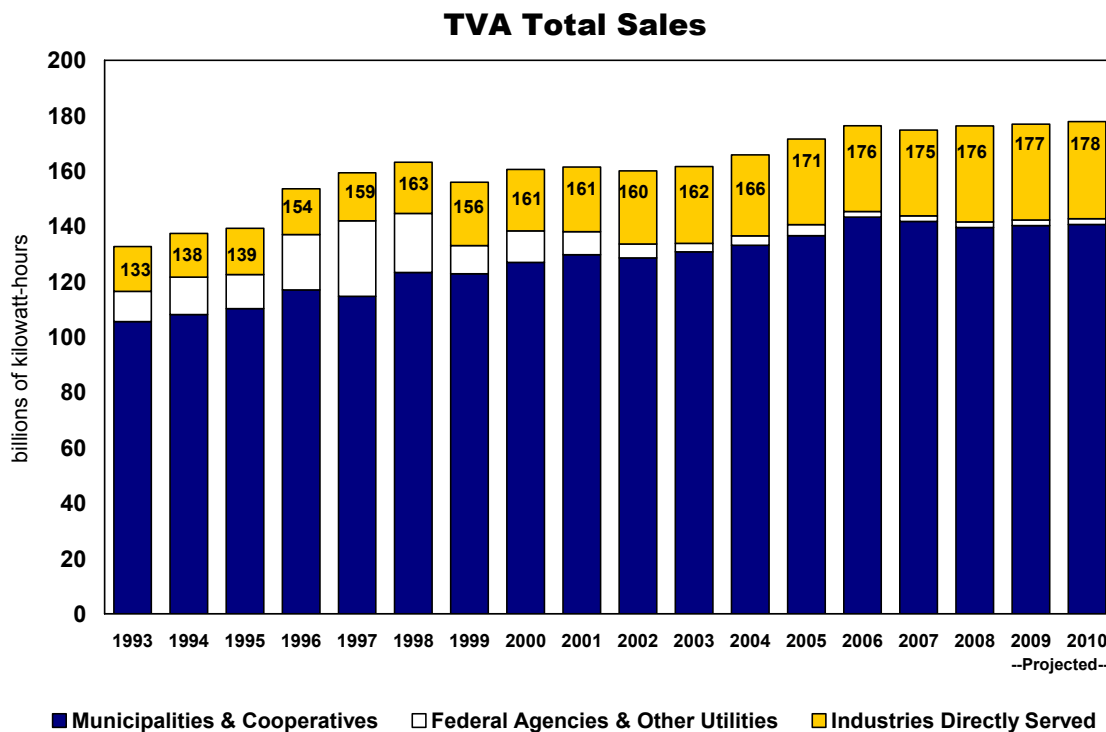
### Power Sales and Revenue

The Tennessee Valley Authority sells electricity to three main customer groups:

Distributors: TVA delivers power to wholesale customers, which include municipal utility companies and cooperatives, who resell that power to consumers. The municipal utilities make up the largest block of TVA customers. Cooperatives are customer-owned companies, many of which were originally formed to bring electricity to the farthest reaches of the Tennessee Valley. These municipal and cooperative distributors represent the majority of TVA's business. The Tennessee Valley Public Power Association is an organization that represents their interests.

Directly Served Customers: TVA also sells power to directly served customers, consisting primarily of federal agencies and customers with large or unusual loads.

Off-System Customers: TVA is authorized under the TVA Act to sell power under exchange power agreements to certain neighboring systems. Sales to these companies typically represent less than 1 percent of TVA's total power sales.



Note: TVA is currently experiencing less demand for power than projected.

### Demand in the Valley

In 2008, TVA sold 176 billion kilowatt-hours of electricity and is estimated to sell 177 billion kilowatt-hours in 2009, and 178 billion kilowatt-hours in 2010. Most of TVA's sales growth in the past several years has come from customers who are municipal and cooperative distributors of TVA power, which has offset reduced demand from federal agencies and other customers. Demand for electricity in the TVA region grew at 2 percent annually from 1995 through 2008. By 2010, the population of the TVA service region is expected to surpass 9 million, growing at a rate slightly higher than the national average.

<b>TVA System Capability</b>		
<i>Net summer dependable (MW) at September 30, 2008</i>		
<b>Fossil</b>	<b>14,469</b>	<b>39%</b>
<b>Nuclear</b>	<b>6,671</b>	<b>18%</b>
<b>Hydro</b>	<b>5,503</b>	<b>15%</b>
<b>Combustion Turbine (owned or leased)</b>	<b>7,266</b>	<b>20%</b>
<b>Power Purchase Agreements</b>	<b>2,789</b>	<b>8%</b>
<b>Other*</b>	<b><u>16</u></b>	<b><u>&lt;1%</u></b>
<b>Capacity**</b>	<b>36,714</b>	<b>100%</b>

\* Other includes 13 MW of Diesel Generator capacity and 3 MW of Renewable Resources Owned by TVA.

\*\*Includes 440 MW of capacity contracted by TVA from the two-unit Red Hills Generation Plant owned by Choctaw Generation, LP. Hydro capacity represented includes pumped-storage.

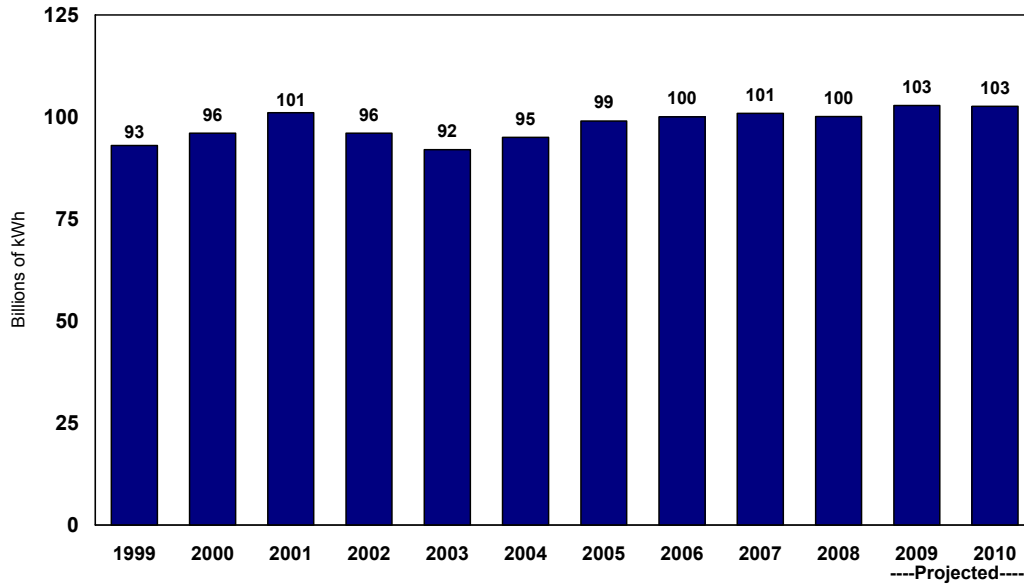
### **Operational Performance**

TVA is the largest public power provider in the nation and ranks among the largest generators of power in the country. TVA plays a vital role as a public power provider, dedicated to protecting the public interest in a rapidly changing industry. In recognition of the vital role it plays and its status as a public power entity, TVA is committed to excellence in operational performance and efficiency. TVA's commitment to operational excellence includes operating in an environmentally responsible manner. TVA is making appropriate investments in clean-air controls to further protect the environment of the Tennessee Valley.

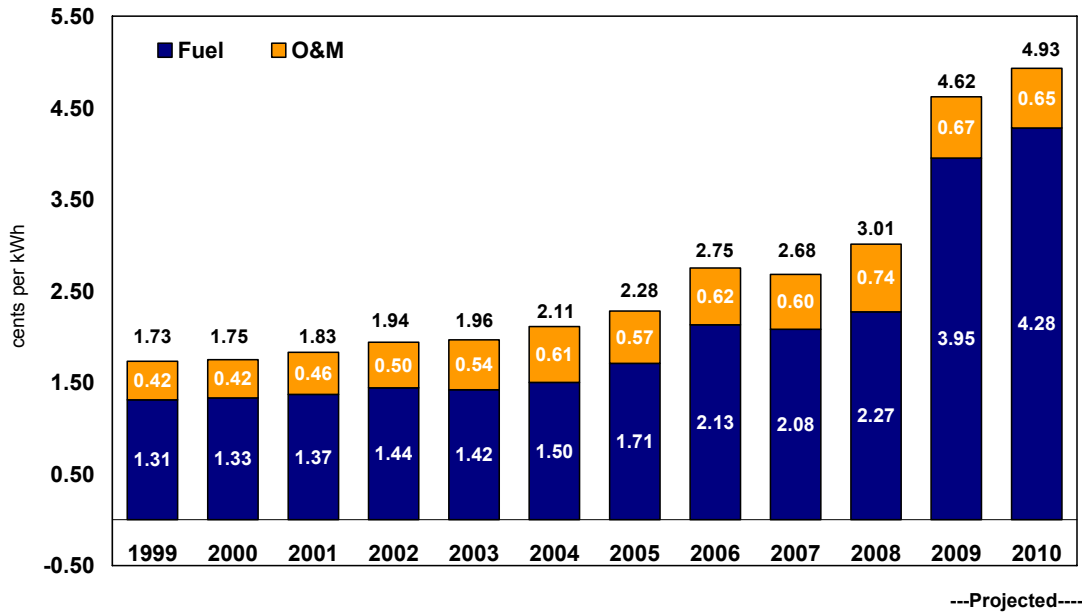
#### Fossil Power Highlights

The mainstay of TVA's power production portfolio is its fleet of 11 coal-fired fossil plants, which represent a combined 14,469 megawatts of net summer capability. TVA's fossil system also includes 87 simple-cycle combustion turbine units at eight different plant sites and six natural gas combined-cycle units. The simple-cycle combustion turbine sites are peaking sites that are designed to start quickly and help meet demand for electricity during peak operating periods. TVA's total fossil-system production expense on a per-kilowatt-hour basis is expected to increase in 2010 due to higher fuel costs. Operation and maintenance costs are projected to decrease. Several of TVA fossil plants set continuous-run records and received awards for efficiency and reliability.

### TVA Fossil Power Generation



### Fossil Power Production Expense

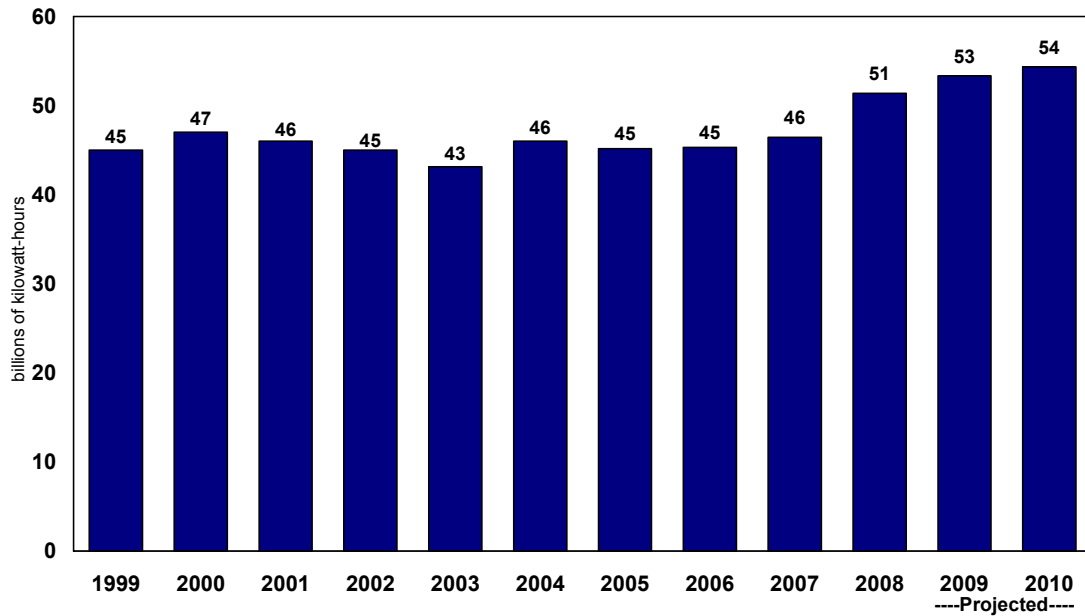


Note: TVA is experiencing increased coal costs as well as other significant levels of uncertainty primarily relating to the weather and the economy.

#### Nuclear Power Group Highlights

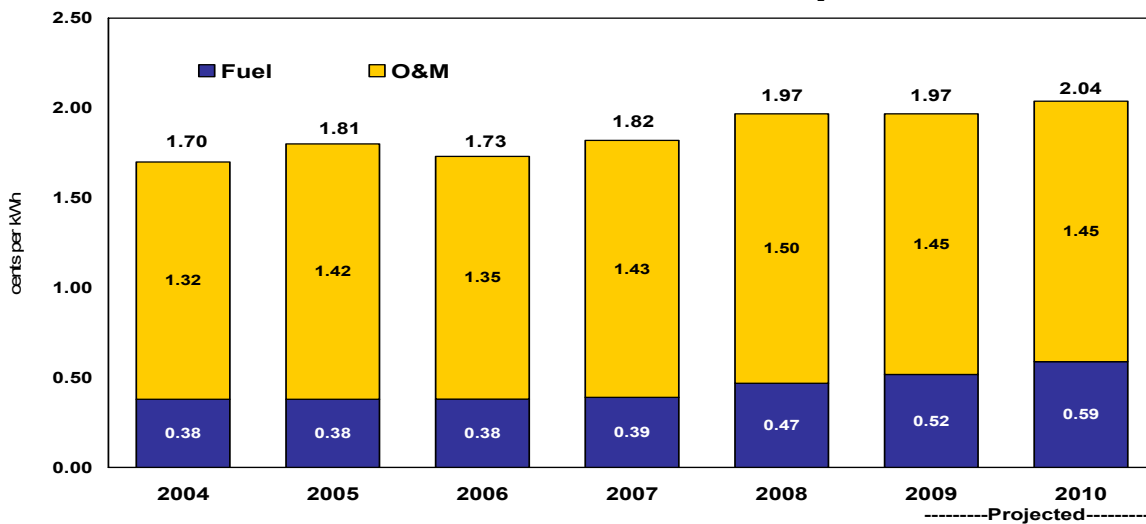
TVA's nuclear operations are critical to meet the region's power needs. In 2010, TVA's nuclear units are expected to generate 54 billion kilowatt-hours of electricity, which should represent approximately 33 percent of TVA's total net generation.

### TVA Nuclear Generation



TVA's total nuclear production expense on a per-kilowatt-hour basis is expected to increase in 2010 due to higher fuel costs. Operation and maintenance costs are projected to decrease.

### Nuclear Power Production Expense



#### Hydro Power Highlights

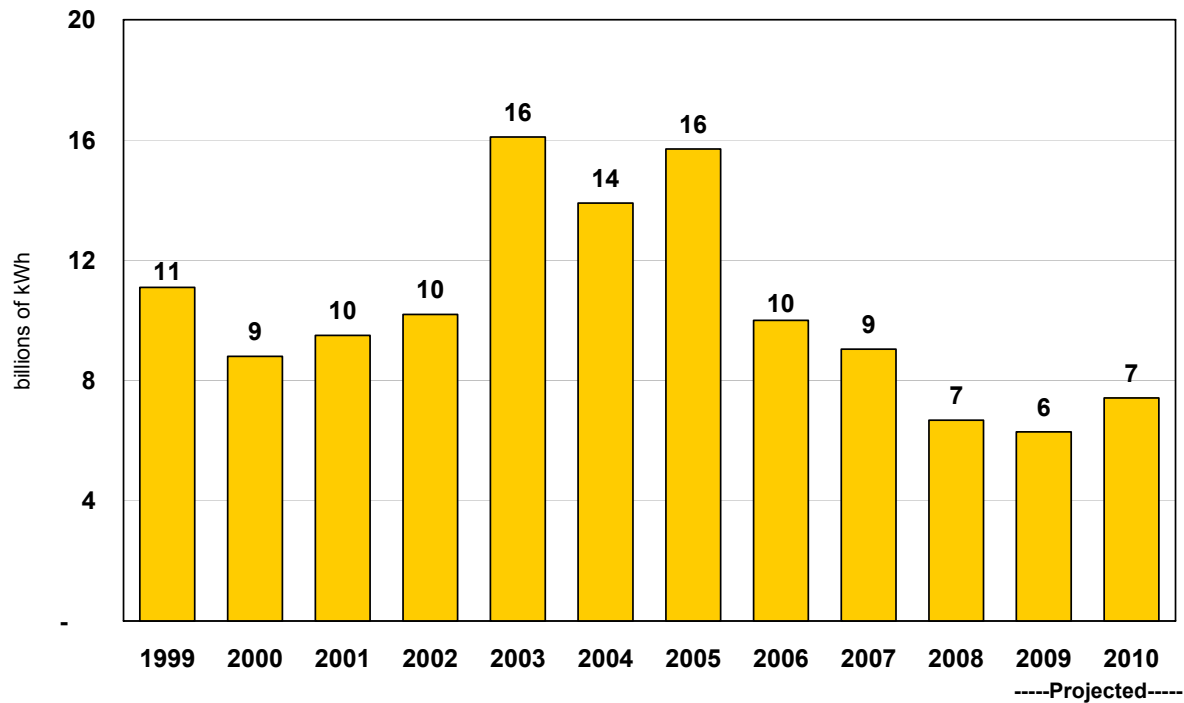
In 2008, TVA's integrated hydropower system of dams and pumped-storage units generated approximately 6.7 billion kilowatt-hours of electricity – approximately 4 percent of TVA's total net generation, and in 2010 it is estimated to produce approximately 7.4 billion kilowatt-hours – approximately 4.5 percent of TVA's total net generation. Generation in FY 2008 decreased 26.1 percent from FY 2007 due to below normal rainfall and run-off levels. In FY 2009, the historic drought conditions continued and are expected to keep hydro production lower until at least 2010. While hydropower represents a smaller amount of total net generation than other sources, hydropower represents a very important element in TVA's total portfolio.

TVA's hydro facilities have very low operating costs and can be used as base-load, intermediate, or peaking units,



depending on water availability and system needs. TVA's Raccoon Mountain pumped-storage facility allows TVA to store electricity in the form of potential energy by using inexpensive off-peak electricity to pump water to a mountain-top reservoir. This water is then used to generate electricity on-peak when power is more expensive or otherwise unavailable.

### TVA Hydro-System Net Power Generation



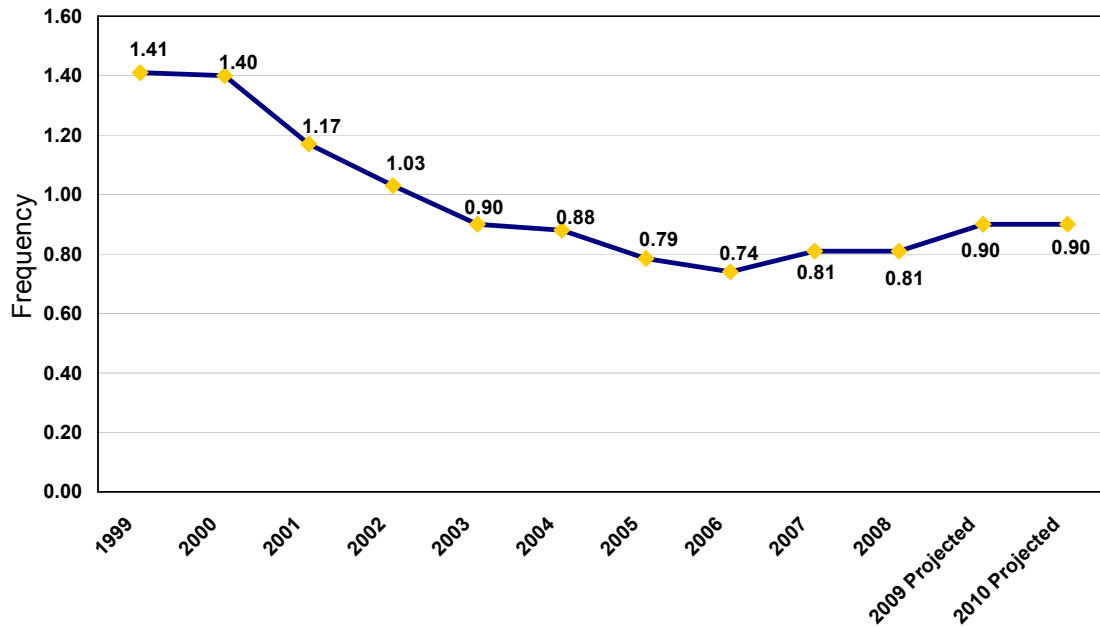
### TVA Transmission Highlights

The TVA transmission system, one of the largest in North America, delivered nearly 176 billion kilowatt-hours of electricity sales in 2008 and maintained 99.999 percent reliability over the past nine years for delivering electricity to customers. In 2010, the transmission system is expected to deliver nearly 178 billion kilowatt-hours of electricity sales. This system is comprised of approximately 15,860 circuit miles of transmission lines, including 2,400 miles of extra-high-voltage (500,000 volt) transmission lines, 487 substations, power switchyards and switching stations, 1,070 individual interchange and customer connection points, and 260,000 right-of-way acres.

The TVA transmission organization offers transmission services, similar to those offered by other transmission operators, in accordance with standards of conduct that separate its transmission functions from TVA's marketing functions.

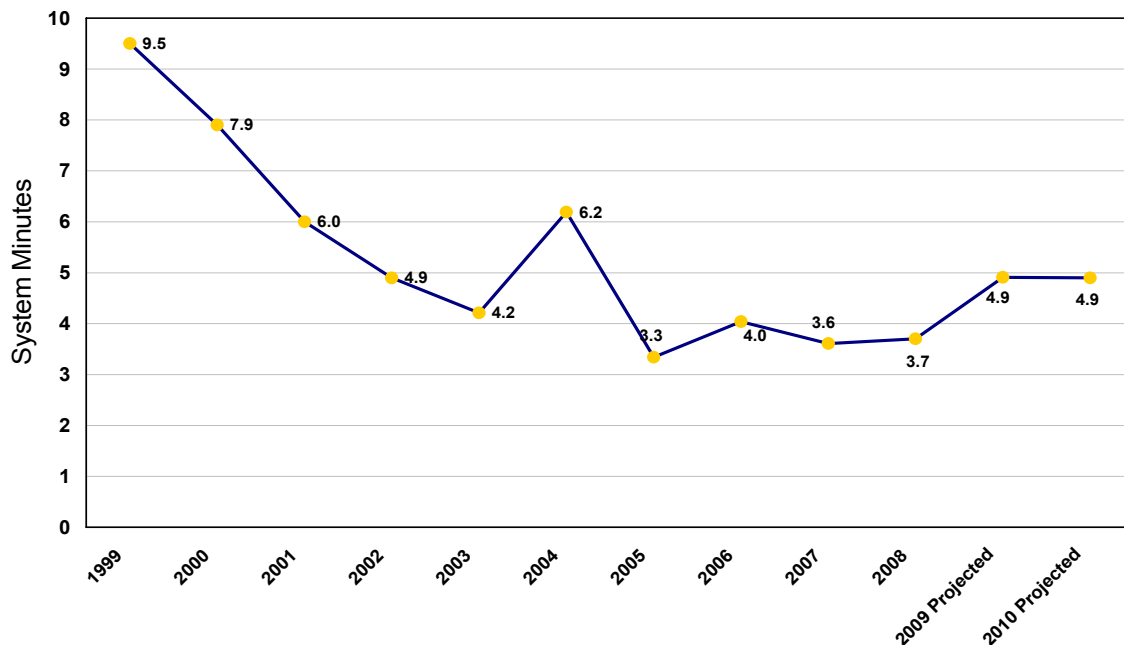
Connection point interruptions are driven primarily by weather, and it can be particularly difficult to reduce the number of interruptions across large transmission systems such as TVA's, which has thousands of miles of lines crossing rural areas. However, the impact of lightning strikes on TVA's transmission system, the single-largest cause of transmission interruptions in the TVA region, has been reduced by investing in more than 160 lightning mitigation projects. These projects have helped reduce connection point interruptions caused by lightning by more than 53 percent since 1995.

### Connection Point Interruptions



Another measure of reliability is Load Not Served (“LNS”), which is a measure of the magnitude and duration of interruptions that affect TVA customers. LNS applies to interruptions that exceed one minute and is calculated by multiplying the percentage of total load not served (in megawatt-hours) by the number of minutes in the fiscal year. TVA is taking proactive steps to maintain an improved level of LNS by (1) working on its transmission preventative maintenance program, (2) identifying equipment that is nearing the end of its service life and replacing it before failure and (3) rapid recovery from interruptions.

### Load Not Served (LNS)



**TVA and Security**

TVA takes seriously the safety and security of its employees, facilities, and the public. TVA is committed to doing even more to ensure that its facilities and processes are secure and that its operations will continue uninterrupted. TVA has developed a color-coded system of levels of security, and TVA has implemented an Agency Emergency Response Plan to provide a Valley-wide response to emergency threats requiring integrated action, from predicted severe weather to terrorist activity. Other measures TVA has implemented include tighter restrictions on access to TVA facilities, an increased presence of TVA Police ("TVAP") officers and contract security officers, and physical barriers around some facilities. TVA also has established agreements with state emergency management agencies to provide support from local law-enforcement agencies, highway patrol, Department of Transportation, and National Guard units.

## Goal 2: Environmental Stewardship and Supporting a Thriving River System

As a regional resource development agency, TVA is charged with stewardship of the natural resources of the Tennessee River watershed. TVA manages the Tennessee River system to provide public benefits including navigation, flood damage reduction, power production, water supply, and recreation. TVA involves the public in its environmental decision-making. Improvements in environmental performance are driven through a systematic, standardized approach based on TVA's Environmental Management System ("EMS"). Due to the increasing level and complexity of environmental requirements and expectations, TVA completed a new high-level environmental policy to align with and execute the direction in the Strategic Plan. The Environmental Policy was approved by the TVA Board on May 19, 2008, and is intended to be an integrated framework which provides policy-level guidance to carry out TVA's mission.

In light of increasing national focus on renewable and clean energy and TVA's desire to reduce its environmental footprint, on May 19, 2008, the TVA Board approved guiding principles for an Energy Efficiency and Demand Response Plan and a Renewable and Clean Energy Assessment.

The Energy Efficiency and Demand Response Plan seeks to slow the current rate of growth in the region's power demand by providing opportunities for residential, business, and industrial consumer groups to use energy more efficiently. In the short term, the plan proposes reducing the growth in peak demand by up to 1,400 megawatts by the end of the 2012 fiscal year.

The Renewable and Clean Energy Assessment strives to add clean energy resources to TVA's generating mix to help reduce carbon emissions while minimizing costs and maintaining a reliable power supply. The assessment proposes to review TVA's generation mix and identify a road map for pursuing additional renewable and clean energy supply in the region, and recommends consideration of different sources of renewable energy and a reduction in carbon intensity in TVA's generation mix, along with additional energy conservation by everyone who uses electricity.

### River System

TVA has federal jurisdiction for managing America's fifth-largest river system, the Tennessee River and its tributaries, to deliver multiple benefits, including year-round navigation, reduced flood damage, affordable and reliable electricity, recreation opportunities, adequate water supply, improved water quality, and economic growth. TVA has direct stewardship responsibility for 293,000 acres of public land, 11,000 miles of shoreline, and 650,000 acres of reservoir water surface available for recreation and other purposes. TVA reservoirs and public lands provide outdoor recreation opportunities for millions of visitors each year.

Navigation on the Tennessee River—made possible by the system of dams and locks operated by TVA—provides significant contributions to the regional economy. TVA also manages the river system to provide water for hydro generation and cooling water for TVA nuclear and fossil power plants. Other water supply activities include issuing permits for water intake structures and promoting regional water supply planning and project implementation.

TVA has installed and is upgrading equipment at its dams to provide the flows and oxygen levels needed for a healthy aquatic community in tailwaters (the areas immediately downstream from dams). In managing the watershed, TVA balances water quality protection with other demands for water use and implements a number of activities such as the Targeted Watershed Initiative Program, Tennessee Valley Clean Marina Initiative, Tennessee Growth Readiness Program, Strategic Partnership Initiative, and Shoreline Stabilization Program. TVA performs year-round monitoring and analysis of the 41,000-square-mile watershed and reports to the people of the Valley on the health of the river system.

### TVA and Air Quality in the Tennessee Valley

The latest annual air-quality trends report issued by the Environmental Protection Agency ("EPA") shows air quality in the nation has steadily improved since 1990 for all six principal pollutants: sulfur dioxide, nitrogen dioxide, ozone, carbon monoxide, particulate matter, and lead. Air quality data for the Tennessee Valley region also shows reductions in all of these pollutants. TVA is significantly reducing emissions from its coal-fired plants while continuing to supply affordable, reliable electric power. Over the past several years, TVA has made notable efforts to enhance its environmental performance, and TVA is continuing to make further improvements. By the end of this decade, TVA expects to have spent about \$5.5 billion on clean air controls at its 11 coal-fired power plants.

### Goal 3: Stimulating Economic Growth

Demonstrating leadership in sustainable economic development in the Tennessee Valley means helping communities recruit and retain quality jobs and making the Valley a better place to live and work.

TVA Economic Development's goal is to be a source for economic development information and services across the seven-state Tennessee Valley region. TVA's effective partnerships with its customers and communities have helped produce quality jobs and resulted in significant capital investments in new and existing companies. Economic development efforts are performed in partnership with various private and public organizations, including regional and state agencies. TVA helps meet the needs of its stakeholders to achieve the bigger picture of regional economic development that results in a better life for Tennessee Valley residents today and into the future. TVA's innovative programs and services combine to create powerful tools for sustainable economic development. These programs and services include the following:

#### **Global Business and Community Development**

##### Industrial Recruiting Services

TVA works with distributor customers and local, state, and regional economic development organizations to recruit industrial prospects through an integrated package of economic development resources.

##### Regional Development

A regional development specialist with economic development expertise is assigned to serve counties in a specific TVA region to create, sustain, and foster job growth.

##### Community Development

TVA helps communities increase their competitiveness in attracting investment and creating jobs by delivering training to local community leaders and by providing economic and market research that better prepares them for receiving industrial prospect visits, being competitive and taking advantage of opportunities.

#### **Business Resources**

##### Existing Industry Support

An array of products and services are geared to meet the expansion and retention needs of existing industries. These include financial support, technical services, and industry consulting services.

##### Economic Development Loan Fund

These funds are designed to stimulate job creation and leverage capital investment in the TVA power service region. The loan funds are open to primary manufacturing companies and other institutions in the Valley, including TVA customers, communities, and nonprofit economic development corporations.

##### Special Opportunities Counties ("SOC") Loan Fund

This revolving loan fund is available to the Valley's most economically distressed counties. Loans are made to assist with industrial expansion, job creation, and site/building improvements.

##### Business Incubation Network

Business incubators provide the support that many companies need to survive the challenging early stages of business start-up. Over the years, TVA has provided financial and technical assistance to help communities establish incubators where clients can share services, equipment, and building space.

##### Consumer Connection

Consumer Connection is an economic development program that links Valley communities with business opportunities, expansions, and retentions.

##### Valley Business Ventures

TVA helps the Tennessee Valley's high-growth sectors of woman-owned and minority-owned businesses to increase their job creation and capital investment opportunities.

#### **Technical Services**

##### Engineering and Design Assistance

TVA offers general engineering design services to help industrial prospects make sound location decisions.

Appalachian Regional Commission Project Administration

TVA serves as the basic agency to administer grants for the Appalachian Regional Commission in the Tennessee Valley.

## Budget Overview

### Power Program

TVA's power program is entirely self-financing and does not receive any federal appropriations. The power program budget is, however, included in the Consolidated Budget of the United States Government. TVA is experiencing increased coal costs as well as other significant levels of uncertainty relative to the weather, the economy and other factors. TVA's financial information includes estimates which are subject to these changing conditions.

TVA projects revenue to exceed \$13 billion in FY 2010, including the estimated impacts of the 2008 rate adjustments and fuel cost adjustment related to the recovery of fuel and purchased power expense increases. In FY 2010, TVA projects to invest \$2.2 billion in capital projects for the power system, including \$223 million for clean air projects and \$267 million for transmission system projects. TVA's debt and debt-like obligations increased by \$355 million in FY 2008 and are expected to decrease by \$159 million in FY 2009 and increase by \$32 million in FY 2010.

TVA power sales have increased an average of two percent annually during the past decade. To keep pace with this growth, TVA has added 8,497 megawatts of generating capacity over the past ten years and entered into purchase power agreements with independent power generators. TVA has also upgraded its transmission system to maintain reliability and added new customer delivery points to serve the growing load. With power demand in the Valley expected to grow at approximately 1.3 percent annually through 2028, TVA will continue to explore the full range of options available to meet the growing demand. Between 2006 and 2008, the TVA Board authorized the purchase of three combustion-turbine generating plants and one combined-cycle plant, executed a fifteen-year operating lease on a second combined-cycle plant and approved construction of a third for 2010 operations. Excluding the future 2010 construction, these actions added an additional 1,791 megawatts of winter peaking capacity and 2,373 megawatts of intermediate capacity to the TVA system. Additionally, Browns Ferry Nuclear Plant Unit 1 returned to service in May of 2007 and currently supplies additional generating capacity of approximately 1,150 megawatts with an eventual expected supply of 1,280 megawatts. On August 1, 2007, the TVA Board approved completing the construction of Watts Bar Unit 2. When completed, Watts Bar Unit 2 is expected to provide 1,180 megawatts of capacity.

TVA's 2010 annual interest expense is expected to be \$696 million lower than in 1997. As mentioned, annual net interest expense that once consumed 34 percent of TVA's revenue has been reduced to only 13 percent in 2008 and is expected to drop to 10 percent in 2009 and 2010.

### Water and Land Stewardship

TVA meets its obligation to operate and maintain its system of dams, reservoirs, and adjacent lands. Based on the provisions in the Energy and Water Development Appropriations Act of 1998, TVA funds its traditional essential water and land stewardship activities with power revenues, user fees, and sources other than appropriations. No appropriations have been received by TVA for Water and Land Stewardship since FY 1999, and none are requested for FY 2010. Long-term TVA funding levels for these activities are expected to continue at about the same level as in FY 1999. FY 2008 stewardship expenditures were approximately \$130 million, and FY 2010 funding of this program is estimated at \$86 million.

## Budget Details

### TVA Operating Budget

(millions of dollars)

	FY 2008 Actual	FY 2009 Estimate	FY 2010 Estimate
Revenue	\$ 10,382	\$ 13,543	\$ 13,567
Operating Expenses			
Fuel & Purchased Power	(4,176)	(6,650)	(6,508)
Operating, Maintenance, & Other	(2,307)	(2,555)	(2,620)
Depreciation & Amortization	(1,224)	(1,474)	(1,528)
Tax Equivalents*	<u>(491)</u>	<u>(627)</u>	<u>(669)</u>
Total Operating Expenses	<u>(8,198)</u>	<u>(11,306)</u>	<u>(11,325)</u>
Operating Income	2,184	2,237	2,242
Other Income	9	33	36
Interest Expense	<u>(1,376)</u>	<u>(1,339)</u>	<u>(1,307)</u>
Net Income	<u>\$ 817</u>	<u>\$ 931</u>	<u>\$ 971</u>

\* Tax equivalents are based on the prior year's base revenue and current year FCA revenue.

Note 1: Included budget estimates are subject to change by the TVA Board. The TVA Board is scheduled to approve the FY2010 budget in August of 2009.

Note 2: The above budget information include estimates with significant uncertainty relative to the weather, the economy, fuel prices, etc. which are subject to changing conditions.



## Budget Details

(continued)

### Capital Budget & Cash Flow

(millions of dollars)

	FY 2008 Actual	FY 2009 Estimate	FY 2010 Estimate
Operating Activities			
Net Income	\$ 817	\$ 931	\$ 971
Items not requiring cash	<u>1,140</u>	<u>1,743</u>	<u>1,720</u>
Total Cash Provided from Operating Activities	1,957	2,674	2,691
Cash Used in Capital Budget			
Capital Projects			
Nuclear	(143)	(142)	(140)
Fossil	(282)	(212)	(221)
Hydro	(56)	(48)	(47)
Transmission	(81)	(32)	(45)
Other Capital	<u>(73)</u>	<u>(109)</u>	<u>(78)</u>
Subtotal	(635)	(543)	(531)
Clean Air	(277)	(232)	(223)
Watts Bar Unit 2	(245)	(649)	(681)
Capacity Expansion	<u>(827)</u>	<u>(665)</u>	<u>(773)</u>
Total Capital Projects	(1,984)	(2,089)	(2,208)
Other Sources (Requirements)	<u>(112)</u>	<u>(530)</u>	<u>(625)</u>
Total Cash Used in Capital Budget	(2,096)	(2,619)	(2,833)
Cash Payments to U.S. Treasury	<u>(40)</u>	<u>(42)</u>	<u>(43)</u>
<b>Net Cash Available for Statutory Debt Reduction/(Increase)</b>	<b><u>\$ (179)</u></b>	<b><u>\$ 13</u></b>	<b><u>\$ (185)</u></b>
<b>Reduction/ (Increase) in Debt and Debt-Like Obligations</b>	<b><u>\$ (355)</u></b>	<b><u>\$ 159</u></b>	<b><u>\$ (32)</u></b>
Receipts Less Disbursements*	\$ 273	\$ (196)	\$ 47

\*For Federal reporting purposes Payments to U.S. Treasury are not considered disbursements.

Note 1: Included budget estimates are subject to change by the TVA Board. The TVA Board is scheduled to approve the FY2010 budget in August of 2009.

Note 2: The above budget information include estimates with significant uncertainty relative to the weather, the economy, fuel prices, etc. which are subject to changing conditions.

## **Program Assessment Rating Tool (PART) - Status Update**

### ***Power Program***

TVA's power program is entirely self financing and does not receive any federal appropriations. The power program budget is, however, included in the Consolidated Budget of the United States Government. TVA is the fifth-largest electric supplier in the country, generating power from a diverse mix of coal-fired, hydro-electric, nuclear, and combustion-turbine plants to meet the electricity needs of nearly nine million people.

In the 2004 PART assessment, TVA received solid ratings for its Operational Performance, Strategic Planning, Program Management, and Program Results. In particular, the Program Management section received a 91 percent rating, with an overall average rating of 74 percent for the entire assessment.

### ***Stewardship Programs - Water and Land***

TVA serves the Tennessee Valley region, which includes parts of seven states, through its management of the nation's largest public power system and the nation's fifth-largest river system, the Tennessee River. The dams and locks are operated as a fully integrated system to deliver multipurpose outputs. Public lands are managed to provide flood control, wildlife habitat, and recreation benefits.

TVA meets its obligation to operate and maintain the system of dams, reservoirs, and adjacent lands. Based on the authority provided in the Energy and Water Development Appropriations Act of 1998, TVA funds its traditional essential water and land stewardship activities with power revenues, user fees, and sources other than appropriations. No appropriations have been received by TVA for Water and Land Stewardship since FY 1999, and none is being requested for FY 2010. Long-term TVA funding levels for these activities are expected to continue at about the same level as in FY 1999. FY 2008 stewardship expenditures were approximately \$130 million, and FY 2010 funding of this program is estimated at \$86 million.

### ***NO<sub>x</sub> Emission Reduction***

The TVA NO<sub>x</sub> emissions-reduction program is designed to remove nitrogen oxide compounds from emissions produced at TVA coal plants in compliance with all NO<sub>x</sub>-related Clean Air Act regulations at the lowest overall cost to TVA ratepayers. The program's activities involve construction of selective catalytic reduction (SCR) and selective non-catalytic reduction ("SNCR") equipment at coal plants as well as monitoring NO<sub>x</sub> emissions for regulatory compliance. Since 1995, TVA has reduced its NO<sub>x</sub> emissions during the summer by 82 percent by installing various controls and has plans for further reductions going forward which include operation of NO<sub>x</sub> controls year-around beginning in October 2008. This will be achieved at the same time energy demand continues to grow in the Tennessee Valley region.

In 2007, OMB gave TVA's NO<sub>x</sub> Emissions Reduction PART an average overall 95 percent rating for the entire assessment and stated that, "TVA has been largely effective in achieving its annual and long-term goals to meet NO<sub>x</sub> reduction targets and comply with Clean Air Act mandates." OMB also gave TVA an "Effective" performance rating for the program. This is the highest rating a program can achieve. Programs rated Effective set ambitious goals, achieve results, are well-managed and improve efficiency.

In 2005, TVA installed SNCR systems on two units to demonstrate long-term technology capability, and continues to operate the SNCR on one of the units. In 2007, TVA began operating the High Energy Reagent Technology ("HERT") system on two additional units. HERT is similar to SNCR technology but has higher removal capabilities. Similar HERT equipment is planned for installation on five additional units in 2009, and TVA has announced plans to install SCRs at John Sevier by 2015. In October 2008, TVA began operating installed NO<sub>x</sub> control equipment year round (except for maintenance outages).

*Tennessee Valley Authority*

**GPRRA Annual Performance Plan**  
for FY 2010

*Submitted*  
**June 2008**



## Foreword

The Tennessee Valley Authority's Strategic Plan was approved by the TVA Board of Directors on May 31, 2007. TVA's Board and executive leadership recognized the need to articulate TVA's overall strategic direction for the next decade as a result of market trends, a new national energy policy, rising fuel costs and other changes since the previously issued strategic plan. The Strategic Plan outlines actions TVA must accomplish to align with this direction. The Strategic Plan also identifies aspects of TVA's current business structure that must be fine-tuned for TVA to strengthen its ability to continue to serve the people of the Tennessee Valley region.

This document is TVA's GPRA Annual Performance Plan for FY 2010. It contains the specific information that is required by the Government Performance and Results Act. This FY 2010 GPRA Annual Performance Plan builds upon the strategic objectives and critical success factors identified in the Strategic Plan and describe the metrics that will be used to monitor TVA's performance toward achieving successful implementation of its strategy.

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## 1. TVA Mission Statement

The mission of TVA is to improve the quality of life in the Tennessee Valley through its work in three key areas: energy, the environment, and economic development. TVA provides reliable, competitive power; manages the Tennessee River system and associated lands to meet multiple needs; and partners with Valley communities and states for economic development. For nearly 75 years, TVA's unique mission has served as the foundation of its business endeavors and provided the context for its business objectives and internal processes.

### Energy

#### ***Provide electric power to the Tennessee Valley***

- TVA supplies reliable, affordable electricity to the Tennessee Valley. It strives to meet the changing needs of power distributor customers and directly served industrial customers for electricity and related products and services in a dynamic marketplace.

### Environment

#### ***Act as steward of the Valley's water resources and associated public lands***

- To fulfill its environmental stewardship mission, TVA manages water resources and associated public lands in the Valley for the benefit of the region and the nation. It manages the Tennessee River system and associated public lands to reduce flood damage, maintain navigation, support power production and recreational uses, improve water quality and supply, and protect shoreline resources.

### Economic Development

#### ***Serve as a catalyst for sustainable economic development***

- TVA works with its power distributor customers; state, regional, and local economic development organizations; and other federal agencies to build partnerships that help bring jobs to the Tennessee Valley and make the economy stronger to benefit the people of the region.

## 2. Strategic Objectives and Critical Success Factors

In its 2007 Strategic Plan, TVA identified five broad strategic objectives on which it will focus as it moves forward, and twenty-four corresponding critical success factors that support those objectives. These strategic objectives, along with their corresponding critical success factors, are as follows:

**CUSTOMER:** Maintain power reliability, provide competitive rates, and build trust with TVA's customers

### Critical Success Factors:

- Strengthen relationships and trust by being responsive to stakeholder needs
- Develop a portfolio of product and pricing structures that more accurately reflect the costs of serving load at different times and levels of use.
- Partner with distributors and directly served customers to encourage conservation, promote energy efficiency, and reduce peak demand
- Partner with customers to limit volatility in rates and participate in power supply through shared generation ownership
- Assist states, communities, and distributors in sustaining economic development programs

**PEOPLE:** Build pride in TVA's performance and reputation

### Critical Success Factors:

- Safeguard the health and safety of employees and the public
- Strengthen workforce knowledge and skills and management processes to motivate performance and successfully implement the strategic objectives
- Treat employees, customers, and other stakeholders with integrity and respect
- Communicate clearly and consistently

**FINANCIAL:** Adhere to a set of sound guiding financial principles to improve TVA's fiscal performance

### Critical Success Factors:

- Apply sound economic and financing practices to new investments
- Pay financing obligations before assets are fully depreciated
- Strengthen TVA's balance sheet by improving the ratio of financing obligations to total assets
- Improve TVA's cash return on total assets in order to service debt, preserve existing assets, reinvest in new assets, and improve environmental performance
- Achieve top-quartile performance in non-fuel operation and maintenance ("O&M") expenses and then hold increases to be less than unit sales growth ("kWhs")

**ASSETS:** Use TVA's assets to meet market demand and deliver public value

Critical Success Factors:

- Balance TVA's production capabilities and load by adding assets (buy, build or through long-term contracts) and encouraging the use of energy in ways that reduce the need for new generation
- Preserve, maintain, repower or retire existing assets where appropriate
- Manage land and water resources to provide multiple benefits to the Valley
- Reduce fuel supply risk with a diverse portfolio of generation assets

**OPERATIONS:** Improve performance to be recognized as an industry leader

Critical Success Factors:

- Deliver reliable electric power generation and transmissions products and services
- Benchmark the industry's best performers to develop metrics for top-quartile performance
- Make nuclear safety the overriding priority for each nuclear facility and for each individual associated with it
- Continue to reduce the impacts of TVA's operations on the environment
- Serve as a responsible steward of the Tennessee River system
- Apply science and technological innovation to improve operational performance

### 3. Program Evaluations - Tracking Progress Against the Goals

#### 3.1 Corporate Level Metrics

The 2007 Strategic Plan outlined the Board of Directors' policy-level direction for TVA over the next decade and highlighted several actions that are needed for successful implementation of the strategy. In support of the strategic objectives and critical success factors outlined in the Strategic Plan, fourteen corporate-level metrics are in place to monitor TVA's performance toward achieving successful implementation of its strategy (Exhibit 1). These metrics will be reviewed and systematically updated to maintain alignment with the strategic focus. TVA's scorecard, with its performance metrics, clearly demonstrates that no one single organizational unit has complete responsibility for implementing strategy.

The TVA-wide performance metrics are as follows:

- (1) **Retail Price (¢ / kWh Sales )** = distributor reported retail power revenue and directly served power revenue divided by distributor reported retail power sales and directly served power sales

*Calculation:*

$$\frac{\text{Distributor reported power revenue} + \text{Directly Served power revenue}}{\text{Distributor reported sales} + \text{Directly Served power sales}}$$



- (2) **Delivered Cost of Power Excluding FCA Costs (\$ / MWh Sales)** = TVA's total costs in dollars per MWh of power sold to customers

*Calculation:*

$$\frac{\text{Total Income Statement Expenses (Excluding FCA Costs) +/- Other Income, net}}{\text{Total Sales Volume (MWh)}}$$

- (3) **Fuel Cost Adjustment Costs (\$ / MWh Sales)** = TVA's FCA expenses per MWh of power sold

*Calculation:*

$$\frac{\text{FCA Costs}}{\text{Total Sales Volume (MWh)}}$$

- (4) **Economic Health Index (Percent)** = percentage growth of the weighted average wage of jobs created and/or retained in the Valley as compared to the percentage growth of the weighted average wage of all states in the Southeast

*Calculation:*

$$\frac{\text{TVA Project Average Wage}}{\text{Southeastern Average Wage}}$$

- (5) **Participation in Energy Efficiency & Peak Shaving Initiatives (Percent)** = quarterly measure of distributors' participation in DSM programs and pilots

*Calculation:*

$$\frac{\text{\# of Distributor Customers Participating in DSM initiatives}}{\text{Total \# of Distributors}}$$

- (6) **Customer Satisfaction Survey (% Satisfied)** = quarterly measure of distributors' and directly served customers' satisfaction with TVA in a variety of areas including wholesale/retail supplier, performance of local TVA customer service staff, and power quality and reliability of transmission service, pricing, contracts, and power supply mix

*Calculation:*

$$\left[ \left( \sum \text{PD survey questions ( \% satisfied )} \right) * \left( 1/14 \right) * \left( 0.85 \right) \right] + \left[ \left( \sum \text{DSI survey questions ( \% satisfied )} \right) * \left( 1/13 \right) * \left( 0.15 \right) \right]$$

- (7) **Connection Point Interruptions (Interruptions / Connection Points)** = tracks interruptions of power, including momentary, at connection points caused by the transmission system

*Calculation:*

$$\frac{\text{Number of interruptions}}{\text{Number of connection points}}$$

- (8) **Cultural Health Index** = measures alignment, capability and engagement of the employee work force

*Calculation:*

Measured by the percent favorable responses (agree or strongly agree) on the Cultural Health Index. Item favorabilities are averaged within each respective dimension (alignment, capability, engagement). The CHI score is the average of the dimension favorability averages.

- (9) **Safe Workplace (Injuries / Hours Worked)** = a rate-based measure of employee safety as measured by the number of OSHA recordable injuries resulting in either a fatality, days away from work/lost time, restricted duty / job transfer, medical treatment, loss of consciousness, other significant work-related injury/illness diagnosed by a physician or other licensed health care professional per 200,000 employee-hours worked by both TVA employees and Staff Augmentation contractors

*Calculation:*

$$\frac{\text{ORIR} \times 200,000}{\text{Number of Hours worked during time period}}$$

NOTE: Hearing loss events are reported as recordable injuries on the OSHA 300 Log, but are excluded from the TVA Winning Performance Safe Workplace indicator.

- (10) **Debt-like Obligations / Asset Value (Percent)** = TVA's flexibility in a competitive market place

*Calculation:*

$$\frac{\text{Statutory debt} + \text{lease obligations} + \text{prepaid energy obligations}}{\text{Total Assets}}$$

- (11) **Funds From Operations / Interest (Ratio)** = credit quality

*Calculation:*

$$\frac{(\text{Net Income} + \text{Depreciation} + [\text{Other Non-Cash Items} - \text{AFUDC}] - \text{Changes in Working Capital} + [\text{Interest Expense} + \text{AFUDC}] + \text{Industry Defined Pension Adjustment})}{([\text{Interest Expense} + \text{AFUDC}] + \text{Industry Defined Pension Adjustment})}$$

- (12) **Net Cash Flow from Operations less Investing (\$ Millions)** = management's ability to control net cash flow (in millions) during the year by focusing attention on both cash inflows and outflows being balanced throughout the year

*Calculation:*

$$(\text{Cash Flow from Operations}) + (\text{Investing Cash Flow}) - (\text{Net Cash Flow from Change in FCA Deferral Account})$$

- (13) **Key Environmental Metrics (Index)** = a composite of the following environmental performance factors: Air (3 elements); Water (2 elements); Clean Water Act Nonconformances, Notices of Violation, and Office Recyclables (1 element each)

*Calculation:*

The sum of 6 element scores. The 6 elements are: CO<sub>2</sub>, NO<sub>x</sub>, SO<sub>2</sub>, CWA nonconformances, Notices of Violation, and office recyclables. The 6 element scores are the result of percent of target performance met. This percentage is determined by dividing the actual performance by the target or vice versa based on whether the preferred performance is declining or increasing. If threshold performance is achieved, the appropriate number of points are obtained. The maximum number of points which can be achieved are the points assigned to meeting the stretch performance.

- (14) **Megawatt Demand Reduction (MW Reduced)** = total incremental megawatt (MW) demand reduction potential from TVA-initiated energy efficiency and demand reduction activities, programs, projects, and pilots

*Calculation:*

[ ( Individual product kW impacts ) \* ( FY 09 individual product installations ) / 1000 ] + [ ( Individual FY 09 project kW impacts ) / 1000 ] + ( Individual FY 09 pilot kW impacts ) / 1000 ] + FY 09 Demand Response MW reduction

- (15) **Demand Reduction (\$ / kW Reduced)** = quarterly measure of cumulative annual expenditures for energy efficiency and demand response activities divided by cumulative annual demand reduction potential identified

*Calculation:*

$$\frac{\text{YTD EE\&DR Expenditures}_{\text{qtr}}}{\text{Monthly potential demand reduction reported YTD}_{\text{qtr}}}$$

- (16) **Equivalent Availability Factor - Coal, CC, & Nuclear (Percent)** = a ratio of actual available generation from all TVA Coal, Combined Cycle & Nuclear generating assets in a given period compared to maximum availability

*Calculation:*

$$\frac{\sum \text{ of all Coal, Combined Cycle \& Nuclear units } ((\text{AVH} * \text{NMC}) - \text{MWhL} - \text{SchMWhL}) * 100}{\sum \text{ of all Coal, Combined Cycle \& Nuclear units } (\text{PH} * \text{NMC})}$$

AVH = Available Hours (Includes Economic Load Reduction and Not in Demand Hours)

PH = Period Hours

NMC = Net Maximum Capacity = Winter NDC for Thermal Units

MWhL = MWh Losses due to forced outage or derating

SchMWhL = MWh Losses due to scheduled outages (planned or maintenance) or derating

### 3.2 The Winning Performance Process

The Winning Performance process keeps TVA focused on the strategic objectives. It identifies the things that must be accomplished to be successful, measures and tracks our performance in these areas, and provides the incentives and feedback to employees to see the direct connection. Employees' involvement in Winning Performance enables them to understand how

their day-to-day performance contributes to TVA's performance and success.

TVA's Winning Performance Team Incentive Plan ("WPTIP") is a pay-for-performance program similar in structure to incentivized performance-based profit-sharing programs used by private companies. The program is based on the principle that operational and process improvements, reduced costs, and improved revenues can be obtained by applying appropriate management focus and offering appropriate monetary incentives.

Employees can see how their work contributes to the direction set by their SBU's performance plan and how that contributes to TVA's overall successful implementation of the agency's strategy (Exhibit 2). Additionally, employees have line-of-sight from their individual performance objectives, developed as a part of the Integrated Performance Management process, to TVA's strategic objectives and critical success factors.

All full time employees are eligible to participate in WPTIP, except those approved by the Board of Directors or delegate(s) to participate in the Executive Annual Incentive Program. WPTIP is a compensation plan (lump sum payment) tied to performance results based on scorecard metrics at the TVA, SBU, and BU levels. The SBUs are Fossil Power Group, Nuclear Generation, Development and Construction, Nuclear Power Group, Power Supply & Fuels, Power System Operations, and River Operations. For FY 2009, the payouts are expected to be funded through the financial benefits incurred by TVA's improved performance when the targets on the TVA, SBU, and BU scorecards are achieved.

The TVA scorecard represents at least 30 percent of each employee's potential payout. The remaining potential employee payout is tied to the performance of an employee's SBU or BU scorecards, whichever is applicable. Corporate organizations are incented based off of a weighted average of TVA's SBU and BU scorecards as they support multiple groups. Executives also have performance incentives linked to the same scorecards.

### **3.3 TVA's Balanced Scorecard**

The TVA, SBU, and BU scorecards contain targets at three levels, corresponding to different incentive payouts: Threshold, Target, and Stretch.

The scorecard basis sheets contain the year-to-date actual values of the metrics, as well as historical and future forecasts, where applicable. Adverse trends and improvement plans are discussed during normal reviews with executive management.

Performance is monitored on each of the metrics, and the scorecards are updated to reflect actual results and updated forecasts. These updates are available to employees through their organizations, in the monthly newsletter InsideTVA, and TVA's intranet.

## **4. Strategy Implementation**

### **4.1 TVA's Mission and Strategic Plan**

The five strategic objectives identified in the TVA Strategic Plan focus on the general steps TVA must take to preserve its core mission. The outcomes are areas that TVA must focus on to continue fulfilling its mission within the evolving business environment.

## 4.2 Principles of a Strategy Focused Organization

TVA follows the five Principles of a Strategy Focused Organization<sup>1</sup> to implement its strategy throughout the operations of the organization. The five principles have been successfully used by both public and private sectors and are defined as follows:

1. Mobilize the organization through visible, executive leadership. The TVA Board approves the strategic plan, budgets, and performance targets. Executive leadership endorses the Strategic Plan and takes responsibility for ensuring its operational implementation.
2. Translate the strategy into operational terms. A key vehicle for translating TVA's strategy into operational terms is TVA's Business Planning Process. These objectives translate strategy into operational terms by identifying TVA-level strategic objectives and critical success factors.
3. Align the organization around the strategy. TVA achieves strategy alignment by developing a balanced scorecard, which defines measurable corporate-level and ultimate business-unit goals consistent with the strategic plan.
4. Motivate to make strategy everyone's job. Strategic awareness is created by "line of sight" mapping—aligning individual performance goals with critical success factors and by TVA's balanced scorecard which ties incentive compensation to the achievement of goals.
5. Govern to make strategy a continual process. TVA, SBU, and BU scorecards are updated monthly as described in section 3.3.

## 4.3 Translating the Strategic Plan into Operational Terms

TVA's mission and strategic objectives must be translated into operational terms to align the actions of management and employees. Defining the critical success factors ("CSFs") is the first step. CSFs define the key factors and capabilities needed to generate sustainable performance consistent with the business themes of the mission and the priorities identified by the Strategic Plan.

Performance goals identify specific, tangible objectives for measuring achievement. TVA develops a strategy in the context of the mission, maps the strategy into operational initiatives, and ultimately develops performance plans for each part of the organization and scorecards for measuring success.

## 4.4 Annual Goals, Long Term Goals and the Strategic Plan

Developing corporate short-term and long-term plans are key to achieving the goals outlined in the Strategic Plan. TVA's Long-Term Plans cover a minimum of 5 years and maximum of 20 years. These plans include:

- Shorter Term (1-3 Year) Plans

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<sup>1</sup> Robert S. Kaplan and David P. Norton, The Strategy-Focused Organization, Harvard Business School Press, Cambridge, Massachusetts, 2000.

- Bi-Annual Power Supply Plan
- TVA Business Plans (3-year outlook with Quarterly reviews)
- Longer Term (5-20 Years) Plans
  - Bi-Annual Long-Term Power Supply Plan (20-year forecast)
  - Long-Range Financial Plans (10 years or more), and associated risk analyses
  - Capital Project Plans (5-year outlook)
  - Enterprise Risk Assessments (5-year outlook)

At a minimum, quarterly briefings are held with the Board of Directors, which include a review of corporate performance. The strategic issues, the scorecard and financial outlook are tracked and reviewed. Annually these reviews include 3-year trending and 3-year forecast.

## **5. Key Factors External to TVA that Could Significantly Affect the Achievement of General Goals**

Given the long lead times needed to build new generation and transmission facilities, the electricity business is subject to forecast error, and planning under uncertainty is inherent. Normal planning uncertainties include those associated with projections about:

- growth in the regional economy and its impact on electricity demand
- changes in the cost of fuel used to generate electricity
- changes in laws and regulations, particularly those related to environmental compliance, reliability, and security
- technological change
- changes in market interest rates
- change in operating and maintenance cost

In addition to these uncertainties in electric power planning, the electric utility industry continues to evolve in ways that could have wide-ranging impacts on TVA, the way it achieves its mission and its ability to achieve the goals outlined in the Strategic Plan. Given the potential for change in the industry and the high potential for significant forecast error, TVA planning evolves as more information becomes available.

## **6. Resources and Skills Needed To Achieve Goals**

### **6.1 Financial Resources**

The TVA Act gives the TVA Board both the authority and the requirement to set electric rates at a level to cover all power system costs while being responsible to the Act's objective that power be sold at rates as low as feasible. The Energy and Water Development Appropriations Bill of 1998 authorized TVA to use power revenues to pay for essential stewardship activities previously funded by federal appropriations.

### **6.2 Physical Resources**

TVA's success in carrying out its mission requires that TVA retain management and operational responsibility for the Tennessee River system and other federal assets crucial to its statutory responsibility.

### **6.3 Management and Human Resources**

TVA will need to maintain its existing skills and processes related to power supply, resource stewardship, and economic development while also developing a number of new processes and skills. Major initiatives include the following:

- Continued efforts across the organization to improve efficiency. The activities involved include not only benchmarking best-in-class performers, but also raising the bar on TVA's own performance related to reliability, forced outage rates, and overall cost.
- Continued training to develop a multi-skilled workforce to improve labor productivity.
- Developing new tools to support the development of products and services, including new methods for determining TVA's cost to provide different types of service and evaluating and quantifying risk.
- Developing new methods for evaluating future investments in generation that reflect the uncertainty in future revenue available to recover those investments.

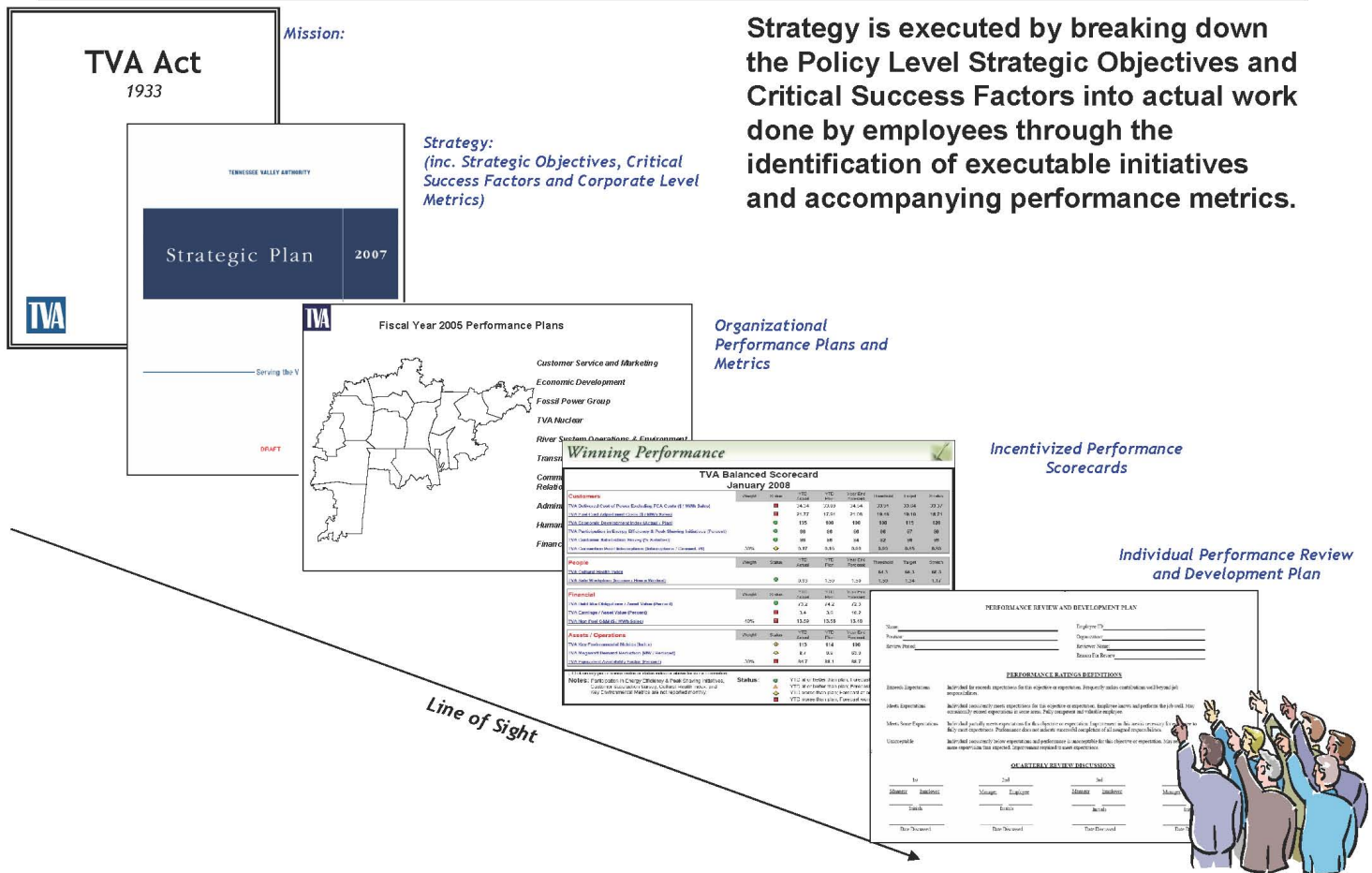
## Exhibit 1. TVA Strategic Plan Corporate Level Metrics

<b>TVA Balanced Scorecard</b>								
<b>FY 2009</b>								
<b>Customers</b>	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Retail Price (\$ / kWh Sales)</a>						8.40		
<a href="#">TVA Delivered Cost of Power Excluding FCA Costs (\$ / MWh Sales)</a>						35.89		
<a href="#">TVA Fuel Cost Adjustment Costs (\$ / MWh Sales)</a>						33.85		
<a href="#">TVA Economic Health Index (Percent)*</a>						100		
<a href="#">TVA Participation in Energy Efficiency &amp; Peak Shaving Initiatives (Percent)*</a>						98		
<a href="#">TVA Customer Satisfaction Survey (% Satisfied)*</a>						82		
<a href="#">TVA Connection Point Interruptions (Interruptions / Connection Point)</a>	20%						1.12	0.78
<b>People</b>	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Cultural Health Index*</a>						66.3		
<a href="#">TVA Safe Workplace (Injuries / Hours Worked)</a>						1.62		
<b>Financial</b>	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Debt-like Obligations / Asset Value (Percent)</a>						67.3		
<a href="#">TVA Funds From Operations / Interest (Ratio)</a>						2.6		
<a href="#">TVA Net Cash Flow from Operations less Investing (\$ Millions)*</a>	35%					Budget less Revenue Adjustment	Budget	Exceed Budget by \$50M
<b>Assets / Operations</b>	Weight	Status	Actual YTD	Plan YTD	Year End Forecast	Threshold	Target	Stretch
<a href="#">TVA Key Environmental Metrics (Index)*</a>						100		
<a href="#">TVA Megawatt Demand Reduction (MW Reduced)</a>						154	162	170
<a href="#">TVA Demand Reduction (\$ / kW Reduced)*</a>	10%					643	611	582
<a href="#">TVA Equivalent Availability Factor - Coal, CC &amp; Nuclear (Percent)</a>	35%					85.8	87.1	88.0



# Exhibit 2. Translating Strategy into Operational Terms

## Line Of Sight



## Appendix

EBITDA is a financial measure that, although commonly used, is not calculated and presented in accordance with U.S. generally accepted accounting principles ("GAAP"). EBITDA represents net income before interest, taxes, depreciation, and amortization. TVA presents EBITDA because it considers EBITDA an important indicator of TVA's fiscal health and performance. EBITDA should be considered in addition to, and not as a substitute for, TVA's other measures of performance that are reported in accordance with GAAP. A reconciliation of net income to EBITDA follows:

TENNESSEE VALLEY AUTHORITY							
Unaudited Reconciliation of Net Income to EBITDA							
(in millions)							
	2004	2005	2006	2007	2008	2009 Projected	2010 Projected
Net Income	\$ 386	\$ 85	\$ 113	\$ 423	\$ 817	\$ 931	\$ 971
Add back:							
Interest Expense	1,363	1,312	1,264	1,232	1,376	1,339	1,307
Tax Equivalents	338	365	376	451	491	627	669
Depreciation & Amortization	1,115	1,154	1,500	1,473	1,224	1,474	1,528
Total EBITDA	<u>\$ 3,202</u>	<u>\$ 2,916</u>	<u>\$ 3,253</u>	<u>\$ 3,579</u>	<u>\$ 3,908</u>	<u>\$ 4,371</u>	<u>\$ 4,475</u>



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