Tennessee Valley Authority
Form 10-Q
December 15, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13, 15(d), OR 37 OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2008

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ____ to ____

Commission file number 000-52313

TENNESSEE VALLEY AUTHORITY
(Exact name of registrant as specified in its charter)

A corporate agency of the United States created by an act of Congress (State or other jurisdiction of incorporation or organization)	62-0474417 (IRS Employer Identification No.)
400 W. Summit Hill Drive Knoxville, Tennessee (Address of principal executive offices)	37902 (Zip Code)

(865) 632-2101
(Registrant’s telephone number, including area code)

None
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13, 15(d), or 37 of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer o
Non-accelerated filer x (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No x

Explanatory Note

In this Quarterly Report on Form 10-Q for the three and nine months ended June 30, 2008 ("Quarterly Report"), the Tennessee Valley Authority ("TVA") is restating the financial statements as of and for the quarter ended June 30, 2007, primarily to restate revenue associated with an accounting error in the financial statements included in the Quarterly Report for the quarterly period ended June 30, 2007 (the "Original 10-Q"). The error was discovered during TVA's review of its unbilled revenue estimation process.

TVA is primarily a wholesale provider of power to distributor customers ("distributors") that resell the power to end users at retail rates. Under TVA's end-use billing arrangements with distributors, TVA relies on distributors to report their end-use sales. Because of the delay between the wholesale delivery of power to the distributor and the report of end-use sales to TVA, TVA must estimate the unbilled revenue at the end of each financial reporting period. In September 2006, TVA implemented a change in methodology for estimating unbilled revenue for electricity sales which resulted in an increase of $232 million in unbilled revenue (2.6 percent of operating revenue) for 2006.

The estimation process implemented in September 2006 utilized the distributors' average rates and an estimate of the number of days of revenue outstanding to reflect the delay in reporting the end-use sales to TVA ("days outstanding"). The number of days outstanding was derived using a procedure similar to a cross-correlation calculation that compared the monthly retail load to the monthly wholesale load. The intent was to reflect in the unbilled estimate the end-use sales that would be reported that month by distributors plus any remaining sales that would not be reported until the following month due to the delay between wholesale delivery and end-use reporting.

TVA has determined that the process implemented in September 2006 overestimated the days outstanding and that this overestimation resulted in an error in recording unbilled revenue and unbilled receivables. The previous unbilled process also failed to consider the annual true-up of each distributor's reported distribution losses. The annual true-up reconciles total end-use kilowatt-hour ("kWh") sales and revenue reported by each distributor with the kWh sales recorded for each distributor at wholesale.

TVA has used a new process for estimating unbilled revenue for the three and nine months ended June 30, 2007 in this Form 10-Q. This process carries over only the portion of sales from the distributor's meter read date to the month-end. Those sales, along with the current month sales, are then priced at rates based on each distributor's customer and product mix. Additionally, the true-up component has been added to the unbilled calculation to reflect any timing differences that occur between the retail and wholesale billing cycles. Due to the new process, an adjustment was made to increase revenue for the three month and nine month periods ended June 30, 2007, by $26 million and $22 million, respectively.

The restatement of unbilled revenue also affected TVA's fuel cost adjustment ("FCA") calculation. The FCA is a mechanism by which TVA collects the direct cost of fuel used in its generating facilities and also the energy costs of purchased power used to serve power demand. Implementation of the FCA occurred in October 2006 as a joint effort between TVA and its customers. The goal of the FCA is timely recovery of fuel-related expenses to reduce the volatility driven by fuel and purchased power markets. Under TVA's FCA methodology, adjustments to rates are based primarily on the difference between forecasted and actual expenses for the upcoming quarter, as well as the difference between forecasted and actual revenues for the upcoming quarter. Because the FCA adjustments are forward-looking, there is typically a difference between what is collected in rates and what actual expense is realized over the course of the quarter. This difference is added to or subtracted from a deferred account on TVA's balance sheet.

The restatement of unbilled revenue changed TVA's forecasted revenues, and since forecasted revenues are a major component of the FCA calculation, the change in forecasted revenues required a restatement of the amounts in TVA's deferred FCA account. The FCA deferred balance at September 30, 2007, was restated within the filing of the Amendment No. 2 to TVA's Annual Report on Form 10-K for the fiscal year ended September 30, 2007 (the "Annual Report").

The unbilled revenue error also affected the application of distributor prepayments. The balance in the distributors' unbilled accounts receivable is offset by the advance collections of those distributors who make prepayments for their power. As a result of the change in unbilled revenue, the balances in the unbilled receivable and advance collections accounts were also adjusted. The adjustment related to distributor prepayments at September 30, 2007, was restated within the filing of the Annual Report.

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In light of the need for this restatement, TVA has identified a material weakness in its internal control over financial reporting related to its unbilled revenue calculation. To rectify the material weakness, TVA used the new method of calculating the unbilled revenue estimate described above for all periods presented in this Quarterly Report. As remediation of the control occurred prior to the filing of this Quarterly Report, remediation is considered effective as of June 30, 2008. See Part 1, Item 4, Controls and Procedures, for additional information regarding controls and procedures related to this material weakness.

TVA has also included in the appropriate periods in its restated financial statements other miscellaneous adjustments that were deemed to be not material by management, either individually or in the aggregate, and therefore were corrected in the period in which they were identified. These adjustments are described in more detail in Note 2.

The effects of these restatements and miscellaneous adjustments on TVA's quarterly financial statements as of and for the quarter, and nine months ended June 30, 2007, are described in Note 2. The restatements had no impact on TVA's cash or cash equivalents.

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FORWARD-LOOKING INFORMATION

This Quarterly Report on Form 10-Q ("Quarterly Report") contains forward-looking statements relating to future events and future performance. All statements other than those that are purely historical may be forward-looking statements.

In certain cases, forward-looking statements can be identified by the use of words such as "may," "will," "should," "expect," "anticipate," "believe," "intend," "project," "plan," "predict," "assume," "forecast," "estimate," "objective," "possible," "proba "potential," or other similar expressions.

Examples of forward-looking statements include, but are not limited to

- Statements regarding strategic objectives;
- Projections regarding potential rate actions;
- Forecasts of costs of certain asset retirement obligations;
- Estimates regarding power and energy forecasts
- Expectations about the adequacy of TVA's funding of its pension plans, nuclear decommissioning trust, and asset retirement trust;
- The anticipated results of TVA's Extended Power Uprate project at Browns Ferry Nuclear Plant;
- TVA's plan to reduce the growth in peak demand by up to 1,400 megawatts by the end of 2012;
- TVA's plans to borrow under its credit facility with the U.S. Treasury during 2009;
- TVA's plans to continue using short-term debt to meet current obligations;
- The anticipated cost and timetable for placing Watts Bar Unit 2 in service;

Although the Tennessee Valley Authority ("TVA") believes that the assumptions underlying the forward-looking statements are reasonable, TVA does not guarantee the accuracy of these statements. Numerous factors could cause actual results to differ materially from those in the forward-looking statements. These factors include, among other things:

- New laws, regulations, and administrative orders, especially those related to:
  - TVA's protected service area,
  - The sole authority of the TVA board of directors to set power rates,
  - Various environmental matters including laws, regulations, and administrative orders restricting emissions and preferring certain fuels or generation sources over others,
  - The licensing, operation, and decommissioning of nuclear generating facilities;
  - TVA's management of the Tennessee River system,
  - TVA's credit rating, and
  - TVA's debt ceiling;
- Loss of customers;
- Performance of TVA's generation and transmission assets;
- Disruption of fuel supplies, which may result from, among other things, weather conditions, production or transportation difficulties, labor challenges, or environmental regulations affecting TVA's fuel suppliers;
- Purchased power price volatility;
- Events at facilities not owned by TVA that affect the supply of water to TVA's generation facilities;
- Compliance with existing environmental laws and regulations;
- Significant delays or cost overruns in construction of generation and transmission assets;
- Inability to obtain regulatory approval for the construction of generation assets;
- Significant changes in demand for electricity;
- Legal and administrative proceedings, including awards of damages and amounts paid in settlements;

- Weather conditions, including drought;
- Failure of TVA's transmission facilities or the transmission facilities of other utilities;
- Events at any nuclear facility, even one that is not operated by or licensed to TVA;
- Catastrophic events such as fires, earthquakes, floods, tornadoes, pandemics, wars, terrorist activities, and other similar events, especially if these events occur in or near TVA's service area;
- Reliability of purchased power providers, fuel suppliers, and other counterparties;
- Changes in the market price of commodities such as coal, uranium, natural gas, fuel oil, construction materials, electricity, and emission allowances;
- Changes in the prices of equity securities, debt securities, and other investments;
- Changes in interest rates;
- Creditworthiness of TVA, its counterparties, and its customers;
- Rising pension costs and health care expenses;

- Increases in TVA's financial liability for decommissioning its nuclear facilities and retiring other assets;
- Unplanned contributions to TVA's pension or other postretirement benefit plans or to TVA's nuclear decommissioning trust;
- Limitations on TVA's ability to borrow money;
- Changes in the economy;
- Ineffectiveness of TVA's disclosure controls and procedures and its internal control over financial reporting;
- Changes in accounting standards;
- The loss of TVA's ability to use regulatory accounting;
- Problems attracting and retaining skilled workers;
- Changes in technology;
- Changes in TVA's plans for allocating its financial resources among projects;
- Differences between estimates of revenues and expenses and actual revenues and expenses incurred;
- Volatility in financial markets;
- Changes in the market for TVA securities;
- Unforeseeable events; and

Additionally, other risks that may cause actual results to differ materially from the predicted results are set forth in Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, and in Part II, Item 1A, Risk Factors in this Quarterly Report, and in Item 1A, Risk Factors and Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations in TVA's Annual Report on Form 10-K, as amended, for the fiscal year ended September 30, 2007 ("Annual Report"), and in other filings TVA makes from time to time with the Securities and Exchange Commission ("SEC"). New factors emerge from time to time, and it is not possible for management to predict all such factors or to assess the extent to which any factor or combination of factors may impact TVA's business or cause results to differ materially from those contained in any forward-looking statement.

TVA undertakes no obligation to update any forward-looking statement to reflect developments that occur after the statement is made.

GENERAL INFORMATION

Fiscal Year

Unless otherwise indicated, years (2008, 2007, etc.) in this Quarterly Report refer to TVA's fiscal years ended September 30.

Notes

References to "Notes" are to the Notes to Financial Statements contained in Part I, Item 1, Financial Statements in this Quarterly Report.

Available Information

TVA's Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and all amendments to those reports are made available on TVA's web site, free of charge, as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. TVA's web site is www.tva.gov. Information contained on TVA's web site shall not be deemed to be incorporated into, or to be a part of, this Quarterly Report. In addition, the public may read and copy any reports or other information that TVA files with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. TVA's SEC reports are also available to the public without charge from the web site maintained by the SEC at www.sec.gov.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

TENNESSEE VALLEY AUTHORITY

STATEMENTS OF INCOME (UNAUDITED)

(in millions)

	Three months ended June 30		Nine months ended June 30	
	2008	2007 (As Restated)	2008	2007 (As Restated)
Operating revenues				
Sales of electricity				
Municipalities and cooperatives	$ 2,125	$ 1,889	$ 6,110	$ 5,549
Industries directly served	361	304	1,135	907
Federal agencies and other	31	29	89	80
Other revenue	35	43	96	114
Operating revenues	2,552	2,265	7,430	6,650
Revenue capitalized during precommercial operations	–	(23)	–	(23)
Net operating revenues	2,552	2,242	7,430	6,627
Operating expenses				
Fuel and purchased power	1,013	790	2,908	2,370
Operating and maintenance	575	571	1,714	1,687
Depreciation, amortization, and accretion	394	366	1,176	1,096
Tax equivalents	122	109	359	326
Loss on asset impairment	7	1	7	18
Total operating expenses	2,111	1,837	6,164	5,497
Operating income	441	405	1,266	1,130
Other income, net (Note 1)	7	16	8	51
Unrealized gain on derivative contracts, net (Note 1)	–	98	–	129
Interest expense				
Interest on debt and leaseback obligations	347	346	1,028	1,045
Amortization of debt discount, issue, and reacquisition costs, net	5	4	15	14

Allowance for funds used during construction and nuclear fuel expenditures	(4)	(45)	(12)	(144)
Net interest expense	348	305	1,031	915
Net income	$ 100	$ 214	$ 243	$ 395

The accompanying Notes are an integral part of these financial statements.

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TENNESSEE VALLEY AUTHORITY
BALANCE SHEETS
(in millions)

ASSETS	June 30 2008 (Unaudited)	September 30 2007
Current assets		
Cash and cash equivalents	$ 300	$ 165
Restricted cash and investments (Note 1)	122	150
Accounts receivable, net (Note 1)	1,383	1,458
Inventories and other, net	844	663
Total current assets	2,649	2,436
Property, plant, and equipment		
Completed plant	39,823	38,811
Less accumulated depreciation	(16,708)	(15,937)
Net completed plant	23,115	22,874
Construction in progress	1,725	1,286
Nuclear fuel and capital leases	731	672
Total property, plant, and equipment, net	25,571	24,832
Investment funds	1,045	1,169
Regulatory and other long-term assets (Note 1)		
Deferred nuclear generating units	2,836	3,130
Other regulatory assets	2,080	1,790
Subtotal	4,916	4,920
Other long-term assets	1,357	375
Total regulatory and other long-term assets	6,273	5,295
Total assets	$ 35,538	$ 33,732
LIABILITIES AND PROPRIETARY CAPITAL		
Current liabilities		
Accounts payable and accrued liabilities	$ 1,143	$ 1,205
Collateral funds held	148	157
Accrued interest	311	406
Current portion of leaseback obligations	41	43
Current portion of energy prepayment obligations	106	106
Short-term debt, net	456	1,422
Current maturities of long-term debt (Note 4)	2,030	90
Total current liabilities	4,235	3,429
Other liabilities		
Other liabilities	2,182	2,067

Regulatory liabilities (Note 1)	1,248	83
Asset retirement obligations	2,280	2,189
Leaseback obligations	990	1,029
Energy prepayment obligations (Note 1)	953	1,032
Total other liabilities	7,653	6,400
Long-term debt, net (Note 4)	20,681	21,099
Total liabilities	32,569	30,928
Commitments and contingencies		
Proprietary capital		
Appropriation investment	4,728	4,743
Retained earnings	1,999	1,763
Accumulated other comprehensive loss (Note 3)	(67)	(19)
Accumulated net expense of stewardship programs	(3,691)	(3,683)
Total proprietary capital	2,969	2,804
Total liabilities and proprietary capital	$ 35,538	$ 33,732

The accompanying Notes are an integral part of these financial statements.

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TENNESSEE VALLEY AUTHORITY
STATEMENTS OF CASH FLOWS (UNAUDITED)
For the nine months ended June 30
(in millions)

	2008	2007 (As Restated)
Cash flows from operating activities		
Net income	$ 243	$ 395
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation, amortization, and accretion	1,191	1,126
Nuclear refueling outage amortization	77	62
Loss on asset impairment	7	18
Amortization of nuclear fuel	136	94
Non-cash retirement benefit expense	106	151
Net unrealized gain on derivative contracts	–	(129)
Prepayment credits applied to revenue	(79)	(79)
Fuel cost adjustment deferral	12	(111)
Other, net	67	10
Changes in current assets and liabilities		
Accounts receivable, net	96	100
Inventories and other, net	(94)	(162)
Accounts payable and accrued liabilities	(53)	(31)
Accrued interest	(95)	(140)
Pension contributions	(56)	(56)
Refueling outage costs	(145)	(90)
Other, net	(2)	43
Net cash provided by operating activities	1,411	1,201
Cash flows from investing activities		
Construction expenditures	(1,552)	(1,151)
Combustion turbine asset acquisitions	–	(100)
Nuclear fuel expenditures	(253)	(109)
Change in restricted cash and investments	10	14
Proceeds from investments, net	3	2
Loans and other receivables		
Advances	(6)	(7)
Repayments	9	13
Proceeds from sale of receivables/loans	–	2
Other, net	1	1
Net cash used in investing activities	(1,788)	(1,335)
Cash flows from financing activities		
Long-term debt		
Issues	2,105	36
Redemptions and repurchases	(539)	(469)
Short-term (redemptions)/borrowings, net	(966)	234

Payments on leaseback financing		(34)		(27)
Payments on equipment financing		(7)		(7)
Payments from other financing		–		(1)
Financing costs, net		(17)		(1)
Payments to U.S. Treasury		(30)		(30)
Net cash provided by (used in) financing activities		512		(265)
Net change in cash and cash equivalents		135		(399)
Cash and cash equivalents at beginning of period		165		536
Cash and cash equivalents at end of period	$	300	$	137

The accompanying Notes are an integral part of these financial statements.

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TENNESSEE VALLEY AUTHORITY

STATEMENTS OF CHANGES IN PROPRIETARY CAPITAL

For the three months ended June 30, 2008 and 2007
(in millions)

	Appropriation Investment	Retained Earnings of Power Program	Accumulated Other Comprehensive Income (Loss)	Accumulated Net Expense of Nonpower Programs	Total	Comprehensive Income (Loss)
Balance at March 31, 2007 (Unaudited) (Restated)	$ 4,753	$ 1,524	$ 6	$ (3,676)	$ 2,607	
Net income (loss) (Restated)	–	218	–	(4)	214	$ 214
Return on Power Facility Appropriation Investment	–	(5)	–	–	(5)	–
Other comprehensive income (Note 3)	–	–	(25)	–	(25)	(25)
Return of Power Facility Appropriation Investment	(5)	–	–	–	(5)	–
Balance at June 30, 2007 (Unaudited) (Restated)	$ 4,748	$ 1,737	$ (19)	$ (3,680)	$ 2,786	$ 189
Balance at March 31, 2008 (Unaudited) (Restated)	$ 4,733	$ 1,900	$ (67)	$ (3,687)	$ 2,879	
Net income (loss)	–	104	–	(4)	100	$ 100
Return on Power Facility Appropriation Investment	–	(5)	–	–	(5)	–
Other comprehensive income (Note 3)	–	–	–	–	–	–
Return of Power Facility Appropriation Investment	(5)	–	–	–	(5)	–
Balance at June 30, 2008 (Unaudited)	$ 4,728	$ 1,999	$ (67)	$ (3,691)	$ 2,969	$ 100

For the nine months ended June 30, 2008 and 2007

	Appropriation Investment	Retained Earnings of Power Program	Accumulated Other Comprehensive Income (Loss)	Accumulated Net Expense of Nonpower Programs	Total	Comprehensive Income (Loss)

Balance at September 30, 2006 (Restated)	$ 4,763	$ 1,349	$ 43	$ (3,672)	$ 2,483	
Net income (loss) (Restated)	–	403	–	(8)	395	$ 395
Return on Power Facility Appropriation Investment	–	(15)	–	–	(15)	–
Accumulated other comprehensive income (Note 3)	–	–	(62)	–	(62)	(62)
Return of Power Facility Appropriation Investment	(15)	–	–	–	(15)	–
Balance at June 30, 2007 (Unaudited) (Restated)	$ 4,748	$ 1,737	$ (19)	$ (3,680)	$ 2,786	$ 333
Balance at September 30, 2007 (Restated)	$ 4,743	$ 1,763	$ (19)	$ (3,683)	$ 2,804	
Net income (loss)	–	251	–	(8)	243	$ 243
Return on Power Facility Appropriation Investment	–	(15)	–	–	(15)	–
Accumulated other comprehensive income (Note 3)	–	–	(48)	–	(48)	(48)
Return of Power Facility Appropriation Investment	(15)	–	–	–	(15)	–
Balance at June 30, 2008 (Unaudited)	$ 4,728	$ 1,999	$ (67)	$ (3,691)	$ 2,969	$ 195

The accompanying Notes are an integral part of these financial statements.

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NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in millions except where noted)

1. Summary of Significant Accounting Policies

General

The Tennessee Valley Authority ("TVA") is a wholly-owned corporate agency and instrumentality of the United States. TVA was created by the U.S. Congress in 1933 by virtue of the Tennessee Valley Authority Act of 1933, as amended, 16 U.S.C. §§ 831-831ee (as amended, the "TVA Act"). TVA was created to improve navigation on the Tennessee River, reduce flood damage, provide agricultural and industrial development, and provide electric power to the Tennessee Valley region. TVA manages the Tennessee River and its tributaries for multiple river-system purposes, such as navigation; flood damage reduction; power generation; environmental stewardship; shoreline use; and water supply for power plant operations, consumer use, recreation, and industry.

Substantially all TVA revenues and assets are attributable to the power program. TVA provides power in most of Tennessee, northern Alabama, northeastern Mississippi, and southwestern Kentucky and in portions of northern Georgia, western North Carolina, and southwestern Virginia to a population of approximately nine million people. The power program has historically been separate and distinct from the stewardship programs. The power program is required to be self-supporting from power revenues and proceeds from power financings, such as proceeds from the issuance of bonds, notes, and other evidences of indebtedness ("Bonds"). Although TVA does not currently receive congressional appropriations, it is required to make annual payments to the U.S. Treasury in repayment of, and as a return on, the government's appropriation investment in TVA power facilities (the "Power Facility Appropriation Investment"). Before 2000, most of the funding for TVA's stewardship programs was provided by congressional appropriations. These programs are now funded with power revenues except for certain stewardship activities that generate various revenues and user fees. These activities related to stewardship properties do not meet the criteria of an operating segment pursuant to Statement of Financial Accounting Standards ("SFAS") No. 131, "Disclosures About Segments of an Enterprise and Related Information." Accordingly, stewardship assets and properties are included as part of the power program, TVA's only operating segment.

Power rates are established by the TVA board of directors ("TVA Board") as authorized by the TVA Act. The TVA Act requires TVA to charge rates for power that will produce gross revenues sufficient to provide funds for operation, maintenance, and administration of its power system; payments to states and counties in lieu of taxes ("tax equivalent payments"); debt service on outstanding indebtedness; payments to the U.S. Treasury in repayment of and as a return on the Power Facility Appropriation Investment; and such additional margin as the TVA Board may consider desirable for investment in power system assets, retirement of outstanding Bonds in advance of maturity, additional reduction of the Power Facility Appropriation Investment, and other purposes connected with TVA's power business. In setting TVA's rates, the TVA Board is charged by the TVA Act to have due regard for the primary objectives of the TVA Act, including the objective that power shall be sold at rates as low as are feasible. Power rates set by the TVA Board are not subject to the prior approval of or subsequent review by any state or federal regulatory body.

Basis of Presentation

TVA prepares its interim financial statements in conformity with generally accepted accounting principles ("GAAP") accepted in the United States for interim financial information. Accordingly, TVA's interim financial statements do not include all of the information and notes required by GAAP for complete financial statements. Because the accompanying interim financial statements do not include all of the information and footnotes required by GAAP for complete financial statements, they should be read in conjunction with the audited financial statements for the year ended September 30, 2007, and the notes thereto, which are contained in TVA's 10K/A No.2.

The amounts included in the accompanying interim financial statements are unaudited but, in the opinion of TVA management, reflect all adjustments, which consist solely of normal recurring adjustments, necessary to fairly present TVA's financial position and results of operations for the interim periods. Due to seasonal weather variations and the timing of planned maintenance and refueling outages of electric generating units, the results of operations for interim periods are not necessarily indicative of amounts expected for the entire year.

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Use of Estimates

In preparing financial statements that conform to GAAP, management must make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the amounts of revenues and expenses reflected during the reporting period. Actual results could differ from those estimates.

Fiscal Year

TVA's fiscal year ends September 30. Unless otherwise indicated, years (2008, 2007, etc.) refer to TVA's fiscal years.

Restricted Cash and Investments

As of June 30, 2008, and September 30, 2007, TVA had $122 million and $150 million, respectively, in Restricted cash and investments on its Balance Sheets primarily related to collateral posted with TVA by a swap counterparty in accordance with certain credit terms included in the swap agreement. This resulted in the funds being reported in Restricted cash and investments.

Accounts Receivable

Accounts receivable primarily consist of amounts due from customers for power sales. The table below summarizes the types and amounts of receivables.

Accounts Receivable

	At June 30 2008	At September 30 2007
Power receivables billed	$ 229	$ 316
Power receivables unbilled	973	986
Fuel cost adjustment-current	121	132
Total power receivables	1,323	1,434
Other receivables	62	26
Allowance for uncollectible accounts	(2)	(2)
Net accounts receivable	$ 1,383	$ 1,458

Cost-Based Regulation

Regulatory assets and regulatory liabilities are classified under the provisions of SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation" ("SFAS No. 71"), and are included in Accounts receivable, net, Deferred nuclear generating units, Other regulatory assets, and Regulatory liabilities and as an offset to Property, plant, and equipment on the June 30, 2008, and September 30, 2007, Balance Sheets.

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TVA's regulatory assets and liabilities are summarized in the table below.

TVA Regulatory Assets and Liabilities

	At June 30 2008	At September 30 2007
Regulatory Assets:		
Unfunded benefit costs	$ 907	$ 973
Nuclear decommissioning costs	611	419
Debt reacquisition costs	201	210
Deferred losses relating to TVA's financial trading program	–	8
Deferred outage costs	164	96
Deferred capital lease asset costs	55	66
Unrealized losses on certain swap and swaption contracts	125	–
Fuel cost adjustment: long-term	17	18
Subtotal	2,080	1,790
Deferred nuclear generating units	2,836	3,130
Subtotal	4,916	4,920
Fuel cost adjustment receivable: short-term	121	132
Total	$ 5,037	$ 5,052
Regulatory Liabilities:		
Unrealized gains on coal purchase contracts	$ 1,080	$ 16
Capital lease liabilities	52	67
Deferred gains relating to TVA's financial trading program	116	–
Subtotal	1,248	83
Accrued tax equivalents	24	4
Reserve for future generation	71	74
Total	$ 1,343	$ 161

Subsequent to the third quarter of 2008, commodity prices have become variable. The following table reflects the effect of market conditions on natural gas and fuel oil commodities as shown by the changes in the Deferred gains relating to TVA's financial trading program and market conditions on coal commodities as shown by the changes in Unrealized gains on coal purchase contracts on TVA's balance sheets at September 30, 2008 and November 30, 2008:

Market Conditions on Natural Gas and Fuel Oil Commodities

	Regulatory Liabilities*		
	June 30 2008	September 30 2008	November 30 2008
Deferred gains (losses) relating to TVA's financial trading program	$ 116	$ (146)*	$ (218)*
Unrealized gains on coal purchase contracts	1,080	813	516

* As of June 30, 2008, Deferred gains (losses) relating to TVA's financial trading program were shown in Regulatory liabilities within the Balance Sheet presentation. Due to market fluctuations, the valuations as of September 30, 2008, and November 30, 2008, are listed as Deferred (losses) relating to TVA financial trading program, which are shown as Regulatory assets with in the Balance Sheet presentation.

In the first quarter of 2008, TVA began using regulatory accounting treatment to defer the unrealized mark-to-market gains and losses on certain swap and swaption contracts to reflect that the gain or loss is included in the ratemaking formula when these transactions actually settle. The value of swaps and swaptions is still recorded on TVA’s balance sheet with realized gains or losses on these contracts recorded in TVA's income statement. The deferred unrealized loss on the value of swaps and swaptions was $125 million for the first three quarters of 2008 and is included as a Regulatory asset on the June 30, 2008, Balance Sheet. See Swaps and Swaptions in this Note 1.

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On February 8, 2008, TVA finalized an agreement to purchase the Office of Power Complex (the major portion of TVA's Chattanooga Office Complex in Chattanooga, Tennessee) upon the expiration of the existing lease term on January 1, 2011. The purchase price is $22 million, payable on January 3, 2011. In accordance with Financial Accounting Standards Board ("FASB") Interpretation ("FIN") No. 26, "Accounting for Purchase of a Leased Asset by the Lessee during the Term of the Lease — an interpretation of FASB Statement No. 13," TVA increased the basis of the capital lease asset by $14 million, increased the capital lease regulatory asset by $1 million, and increased the capital lease obligation by $15 million.

TVA established a reserve for future generation funded by power customers which is also classified as a regulatory liability. Because of the nature of the reserve, it is considered as an offset to Property, plant, and equipment on the June 30, 2008, and September 30, 2007, Balance Sheets.

The FCA structure approved by the TVA Board in 2007 included a provision related to the current funding of the future expense TVA will incur for tax equivalent payments. As TVA records the fuel cost adjustment, the portion of the calculation that relates to a future liability for tax equivalent payments is recorded as a regulatory liability. The resulting liability of $24 million at June 30, 2008, and $4 million at September 30, 2007, is included in Accounts payable on the respective Balance Sheets.

Reserve for Future Generation

During the first quarter of 2007, TVA began collecting in rates amounts intended to fund future generation based on the need for additional generating capacity in TVA's service area. Because these amounts were intended to fund future costs, they were originally deferred as a regulatory liability. The funds were based on a predetermined rate applied to electricity sales approved as part of TVA's 2007 budget. Collections for the three months and nine months ended June 30, 2007, amounted to $19 million and $53 million, respectively. Total collections for the year ended September 30, 2007, amounted to $76 million. These amounts were recorded as a regulatory liability on the June 30, 2007, and September 30, 2007, Balance Sheets, respectively, as a component of Completed plant. Following the purchase of two combustion turbine facilities, these funds were applied as credits to Completed plant and are reflected on the September 30, 2007, Balance Sheet. The funds collected for future generation are being amortized to revenue in order to match revenue with the corresponding depreciation expense of the facilities on the Statement of Income. This revenue recognition process began when the facilities were placed into service. The reserve for future generation was not extended beyond 2007. The balance of the reserve for future generation was $71 million at June 30, 2008, and $74 million at September 30, 2007. TVA recognized revenue of $1 million during each of the first, second, and third quarters of 2008 consistent with the manner in which the related assets are being depreciated.

Other Long-Term Assets

Other long-term assets is comprised of the following:

Other Long-Term Assets

	June 30 2008	September 30 2007
Loans receivable, net	$ 78	$ 79
Currency swap valuation	199	280
Coal contract valuation	1,080	16

Total	$	1,357	$	375

TVA enters into coal contracts with volume options to protect against market prices. The $1,064 million increase in valuation of commodity contracts is related to increases in the price of this commodity.

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Energy Prepayment Obligations

Prior to 2005, TVA entered into sales agreements with 36 customers for 54.5 discounted energy units totaling approximately $55 million. Total credits applied to power billings on a cumulative basis from these arrangements through June 30, 2008, exceeded $30 million. Of this amount, over $1 million was recognized as revenue for the three months ended June 30, 2008, and 2007, respectively, and over $4 million was recognized as revenue for the nine months ended June 30, 2008, and 2007, respectively.

In November 2003, TVA, Memphis Light, Gas, and Water Division (“MLGW”), and the City of Memphis entered into agreements whereby MLGW prepaid a portion of its power requirements for 15 years. The amount of the prepayment was $1.5 billion. The prepayment credits are being applied to reduce MLGW’s monthly power bill on a straight-line basis over the same 15-year period. Total credits applied to power billings on a cumulative basis through June 30, 2008, exceeded $465 million. Of this amount, $25 million was recognized as revenue for the three months ended June 30, 2008, and 2007, respectively, and $75 million was recognized as revenue for the nine months ended June 30, 2008, and 2007, respectively. These amounts were based on the ratio of kilowatt-hours of electricity delivered to the total kilowatt-hours under contract.

At June 30, 2008, and September 30, 2007, obligations for these energy prepayments were $1,059 million and $1,138 million, respectively. These amounts are included in Energy prepayment obligations and Current portion of energy prepayment obligations on the June 30, 2008, and September 30, 2007, Balance Sheets.

Asset Retirement Obligations

In accordance with the provisions of SFAS No. 143, “Accounting for Asset Retirement Obligations,” TVA recognizes the fair value of legal obligations associated with the retirement of certain tangible long-lived assets. The fair value of the liability is added to the book value of the associated asset. The liability increases due to the passage of time (accretion expense), based on the time value of money, until the obligations settle. Subsequent to the initial recognition, the future liability is adjusted for any periodic revisions to the expected cost of the retirement obligation (changes in estimates to future cash flows) and for accretion of the liability due to the passage of time.

During the third quarter of 2008, TVA’s total asset retirement obligation (“ARO”) increased $31 million due to accretion expense. The nuclear accretion expense of $23 million was deferred and charged to a regulatory asset in accordance with SFAS No. 71. The remaining accretion expense of $8 million, related to coal-fired and gas/oil combustion turbine plants, asbestos, and polychlorinated biphenyls (“PCBs”), was expensed during the third quarter of 2008. During the third quarter of 2007, TVA’s total ARO increased $30 million. The increase was comprised of $7 million in new AROs plus $23 million in ARO expense (accretion of the liability).

During the first nine months of 2008, TVA’s total ARO increased $91 million due to accretion expense, $69 million related to nuclear ARO accretion, and $22 million related to non-nuclear ARO accretion. For the first nine months of 2007, TVA’s total ARO increased $157 million. The increase was comprised of $90 million in new AROs plus $67 million in ARO expense (accretion of the liability).

Reconciliation of Asset Retirement Obligation Liability

	Three Months Ended June 30		Nine Months Ended June 30	
	2008	2007	2008	2007

Balance at beginning of period	$ 2,249	$ 2,112	$ 2,189	$ 1,985
Changes in nuclear estimates to future cash flows	–	7	–	89
Non-nuclear additional obligations	–	–	–	1
	–	7	–	90
Add: ARO (accretion) expense				
Nuclear accretion (recorded as a regulatory asset)	23	16	69	46
Non-nuclear accretion (charged to expense)	8	7	22	21
	31	23	91	67
Balance at end of period	$ 2,280	$ 2,142	$ 2,280	$ 2,142

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Other Income, Net

Other income, net is comprised of the following:

Other Income, Net

	Three Months Ended June 30		Nine Months Ended June 30	
	2008	2007 As Restated	2008	2007 As Restated
Interest income	$ 3	$ 7	$ 13	$ 26
External services	5	6	10	14
Unrealized (losses) gains on investments	(2)	2	(25)	4
Claims settlement	–	–	8	–
Miscellaneous	1	1	2	7
Total other income, net	$ 7	$ 16	$ 8	$ 51

Allowance for Funds Used During Construction

TVA capitalizes interest as an allowance for funds used during construction ("AFUDC"), based on the average interest rate of TVA's outstanding debt. The allowance is applicable to construction in progress related to certain projects and certain nuclear fuel inventories. TVA continues to capitalize a portion of current interest costs associated with funds invested in most nuclear fuel inventories, but since October 1, 2007, interest on funds invested in capital projects has been capitalized only for projects with (1) an expected total project cost of $1 billion or more, and (2) an estimated construction period of at least three years in duration. The adoption of this new criteria has greatly reduced the number of qualifying projects, which was approximately 800 at September 30, 2007. Only one project — Watts Bar Nuclear Plant Unit 2 — met the new AFUDC criteria during the nine months ending June 30, 2008. The accumulated balance of costs for qualifying projects, which is used to calculate AFUDC, averaged approximately $3 billion for the year ended September 30, 2007. By contrast, the accumulated balance of costs for qualifying construction projects averaged approximately $51 million for the nine months ended June 30, 2008.

Swaps and Swaptions

From time to time TVA has entered into call monetization transactions using swaptions to hedge the value of call provisions on certain of its Bond issues. A swaption essentially grants a third party an option to enter into a swap agreement with TVA under which TVA receives a floating rate of interest and pays the third party a fixed rate of interest equal to the interest rate on the Bond issue whose call provision TVA monetized.

These call monetization transactions result in long-term liabilities until such time as TVA repurchases the option or until the option matures. These liabilities are marked to market each quarter. In accordance with the accounting policy that was in effect on September 30, 2007, the changes in the value of these liabilities were reported as unrealized gains or losses through TVA's income statement in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133"). The volatility of the valuations resulted in the recognition of sizable amounts of non-cash expense or income, which affected net income.

The TVA Board approved, beginning in 2008, the utilization of regulatory accounting treatment for swaps and swaptions related to call monetization transactions. This reflects that the effects of these transactions are included in ratemaking when they actually settle. This treatment removes the non-cash impacts to TVA's earnings that result from marking the value of these instruments to market each quarter. The value of the swaps and swaptions will still be recorded on TVA's balance sheet, and any interest expense impacts will continue to be reflected in TVA's income statement. The deferred unrealized gain on the value of the swaps and swaptions was $74 million for the third quarter of 2008, and the deferred unrealized loss for the first nine months of 2008 was $125 million. The deferred unrealized loss of $125 million is included as a Regulatory asset on the June 30, 2008, Balance Sheet.

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Impact of New Accounting Standards and Interpretations

Accounting for Planned Major Maintenance Activities. On September 8, 2006, FASB released FASB Staff Position ("FSP") AUG AIR-1, "Accounting for Planned Major Maintenance Activities." The FSP addresses the accounting for planned major maintenance activities and amends certain provisions in the American Institute of Certified Public Accountants Industry Audit Guide, "Audits of Airlines," and Accounting Principles Board Opinion No. 28, "Interim Financial Reporting." The guidance in this FSP states that entities should adopt an accounting method that recognizes overhaul expenses in the appropriate period. The following accounting methods are most often employed/permitted: direct expensing method; built-in overhaul method; or deferral method. The guidance in this FSP is applicable to entities in all industries and must be applied to the first fiscal year beginning after December 15, 2006. TVA adopted this guidance for 2008. Except for the recording of certain regulatory assets, TVA's policy is to expense maintenance costs as incurred (direct expensing method). Therefore, the adoption of this FSP did not have a material impact on TVA's results of operations or financial position.

Fair Value Measurements. In September 2006, FASB issued SFAS No. 157, "Fair Value Measurements." ("SFAS No. 157"). SFAS No. 157 provides guidance for using fair value to measure assets and liabilities that currently require fair value measurement. SFAS No. 157 also responds to investors' requests for expanded information about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. SFAS No. 157 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. SFAS No. 157 establishes a fair value hierarchy that prioritizes the information used to develop measurement assumptions. Provisions of SFAS No. 157 were to be effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. However, in February 2008, FASB issued FSP FAS 157-2, "Effective Date of FASB Statement No. 157," ("SFAS No. 157-2"), which delays the effective date of SFAS No. 157 for nonfinancial assets and nonfinancial liabilities except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis. This FSP delays the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of this FSP. TVA will implement SFAS No. 157 in the first quarter of 2009, and will utilize the deferral portion of FSP FAS 157-2 for all nonfinancial assets and liabilities within its scope. In October 2008, the FASB issued FSP No. FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active," ("FSP FAS 157-3"). FSP FAS 157-3 clarifies the application of SFAS No. 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. The guidance emphasizes that determining fair value in an inactive market depends on the facts and circumstances and may require the use of significant judgment. FSP FAS 157-3 is effective upon issuance, including prior periods for which financial statements have not been issued, and will become effective for TVA at upon its implementation of SFAS No. 157 during the first quarter of 2009. TVA is evaluating the requirements of SFAS No. 157 and the related FSP's and has not yet determined the impact of their implementation, which may or may not be material to TVA's results of operations or financial position.

Fair Value Option. In February 2007, FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities — Including an amendment of FASB Statement No. 115," ("SFAS No. 159"). This statement permits an entity to choose to measure many financial instruments and certain other items at fair value. The fair value option established by SFAS No.159 permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity will report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Most of the provisions in SFAS No. 159 are elective. The provisions of SFAS No. 159 are effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of the previous fiscal year provided that the entity makes that choice in the first 120 days of that fiscal year and also elects to apply the provisions of SFAS No. 157. SFAS No.

159 will become effective for TVA during the first quarter of 2009. TVA is evaluating the requirements of this statement and has not yet determined the potential impact of its implementation, which may or may not be material to TVA's results of operations or financial position.

Offsetting Amounts. On April 30, 2007, FASB issued FSP FIN No. 39-1, "Amendment of FASB Interpretation No. 39," which addresses certain modifications to FASB Interpretation No. 39, "Offsetting of Amounts Related to Certain Contracts." This FSP replaces the terms "conditional contracts" and "exchange contracts" with the term "derivative instruments" as defined in SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." The FSP also permits a reporting entity to offset fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) against fair value amounts recognized for derivative instruments executed with the same counterparty under the same master netting arrangement. The guidance in the FSP is effective for fiscal years beginning after November 15, 2007, with early application permitted. At this time, TVA is evaluating the requirements of this guidance and has not yet determined the potential impact of its implementation, which may or may not be material to TVA's financial position.

Business Combinations. In December 2007, FASB issued SFAS No. 141R, "Business Combinations," ("SFAS No. 141R"). This statement establishes principles and requirements for determining how an enterprise recognizes and measures the fair value of certain assets and liabilities acquired in a business combination, including non-controlling interests, contingent consideration, and certain acquired contingencies. SFAS No. 141R also requires acquisition-related transaction expenses and restructuring costs to be expensed as incurred rather than capitalized as a component of the business combination. The provisions of SFAS No. 141R are effective as of the beginning of an entity's first fiscal year that begins on or after December 15, 2008. Early adoption is prohibited. SFAS No. 141R will become effective for TVA as of October 1, 2009. TVA expects that SFAS No. 141R could have an impact on accounting for any businesses acquired after the effective date of this pronouncement.
Derivative Instruments and Hedging Activities. In March 2008, FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities — an amendment of FASB Statement No. 133," ("SFAS No. 161") which establishes, among other things, the disclosure requirements for derivative instruments and hedging activities. SFAS No. 161 amends and expands the disclosure requirements of SFAS No. 133. The effective date of adoption for TVA is the second quarter of 2009.

Hierarchy of Generally Accepted Accounting Principles. In May 2008, FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles," ("SFAS No. 162"). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements. SFAS No. 162 is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, "The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles." The implementation of SFAS No. 162 is not expected to have a material impact on TVA's consolidated financial position and results of operations.

Employers' Disclosures about Postretirement Benefit Plan Assets. On October 29, 2008, FASB issued FSP No.132 (R)-a, "Employers' Disclosures about Pensions and Other Postretirement Benefits," to require that an employer disclose the following information about the fair value of plan assets: 1) the level within the fair value hierarchy in which fair value measurements of plan assets fall; 2) information about the inputs and valuation techniques used to measure the fair value of plan assets; and 3) a reconciliation of beginning and ending balances for fair value measurements of plan assets using significant unobservable inputs. The final FSP will be effective for fiscal years ending after December 15, 2009, with early application permitted. At initial adoption, application of the FSP would not be required for earlier periods that are presented for comparative purposes. TVA is currently evaluating the potential impact of adopting this FSP on its disclosures in the financial statements.

2. Restatement

The accompanying financial statements as of and for the three and nine months ended June 30, 2007, have been restated. TVA determined that the method implemented to estimate unbilled revenues in September 2006 had resulted in errors in unbilled revenue presented in TVA's financial statements for the fiscal years ended September 30, 2006, and 2007, and the quarterly periods ended December 31, 2006, March 31, 2007, June 30, 2007, December 31, 2007, and March 31, 2008. There was no effect on periods prior to the three months ended September 30, 2006.

Under TVA's end-use billing arrangements with its distributor customers ("distributors"), TVA relies on the distributors to report their end-use sales. Because of the delay between the wholesale delivery of power to the customer and the report of end-use sales to TVA, TVA must estimate the unbilled revenue at the end of each financial reporting period. In September 2006, TVA implemented a change in methodology for estimating unbilled revenue for electricity sales which resulted in an increase of $232 million in unbilled revenue (or 2.6 percent of operating revenues) for 2006.

The estimation process implemented in September 2006 utilized the distributors' average rates and an estimate of the number of days of revenue outstanding to reflect the delay in reporting the end-use sales to TVA ("days outstanding"). The number of days outstanding was derived using a procedure similar to a cross-correlation calculation that compared the monthly retail load to the monthly wholesale load. The intent was to reflect in the unbilled estimate the end-use sales that would be reported that month by distributors plus any remaining sales that would not be reported until the following month due to the delay between wholesale delivery and end-use reporting.

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TVA has determined that the process implemented in September 2006 overestimated the days outstanding and that this overestimation of days outstanding resulted in an error in recording unbilled revenue and unbilled receivables. The previous unbilled method also failed to consider the annual true-up of each distributor's reported distribution losses. The annual true-up reconciles total end-use kilowatt-hour ("kWh") sales and revenue reported by each distributor with the kWh sales recorded for each distributor at wholesale.

TVA has used a new process for estimating unbilled revenues for the three and nine months ended June 30, 2008, and June 30, 2007. This process carries over only the portion of sales from the distributor's meter read date to the month-end. Those sales, along with the current month sales, are then priced at rates based on each distributor's customer and product mix. Additionally, a true-up component has been added to the unbilled calculation to reflect any timing differences that occur between the retail and wholesale billing cycles. Due to the new process, an adjustment was made to increase revenue for the three month and nine month periods ended June 30, 2007, by $26 million and $22 million, respectively.

The restatement of unbilled revenue also affected TVA's fuel cost adjustment ("FCA") calculation. The FCA is a mechanism by which TVA collects the direct cost of fuel used in its generating facilities and also the energy costs of purchased power used to serve power demand. Implementation of the FCA occurred in October 2006 as a joint effort between TVA and its customers. The goal of the FCA is timely recovery of fuel-related expenses to reduce the volatility driven by fuel and purchased power markets. Under TVA's FCA methodology, adjustments to rates are based primarily on the difference between forecasted and actual expenses for the upcoming quarter, as well as the difference between forecasted and actual revenues for the upcoming quarter. Because the FCA adjustments are forward-looking, there is typically a difference between what is collected in rates and what actual expense is realized over the course of the quarter. This difference is added to or subtracted from a deferred account on TVA's balance sheet.

The restatement of unbilled revenue changed TVA's forecasted revenues, and since forecasted revenues are a major component of the FCA calculation, the change in forecasted revenues required a restatement of the amounts in TVA's deferred FCA account. The FCA deferred balance at September 30, 2007, was restated within the filing of the Annual Report.

The unbilled revenue error also affected the application of distributor prepayments. The balance in the distributors' unbilled accounts receivable is offset by a reduction in the advance collections of those distributors who make prepayments for their power. As a result of the change in unbilled revenue, the balances in the unbilled receivable and advance collections accounts were also adjusted. The adjustment related to distributor prepayments at September 30, 2007, was restated within the filing of the Annual Report.

TVA has evaluated these errors and determined that the impact was an overstatement of net income for the fiscal year ended September 30, 2006, and understatements of net income for the fiscal year ended September 30, 2007, and the three months ended December 31, 2008, and 2007, the six months ended March 31, 2008, and 2007, and the nine months ended June 30, 2007. The changes to the financial statements for the respective years primarily involves accounts receivable and retained earnings on the balance sheets, and operating revenues and net income on the statements of income. The errors and restatements have no impact on cash and cash equivalents.

TVA has also included in the appropriate periods in its restated financial statements other miscellaneous adjustments that were previously deemed to be immaterial by management, either individually or in the aggregate, and therefore were corrected in the period in which they were identified. These adjustments are described in more detail below. References in the "Note" column correspond to lines on the Statements of Income following this table. Accordingly, previously reported amounts are being restated to properly reflect the accounting for these items as follows:

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Statements of Income
Summary of Restatements
For the Three and Nine Months Ended June 30, 2007

Line Item	Description of Adjustment	Three Months 2007	Note	Nine Months 2007	Note
Operating revenues	Unbilled revenue adjustments	$ 26		$ 22	
	Revenue capitalized during pre-commercial plant operation	(23)		(23)	
	Reclassification of expenses previously netted with revenue	3		8	
		6	I07-1	7	I07-5
Operating expenses	Fuel cost adjustment	6		14	
	Revenue capitalized during pre-commercial plant operation	(23)		(23)	
	Reclassification of operating expenses to asset impairment (O&M)	(1)		(23)	
	Reclassification of operating expenses to asset impairment (Asset Impairment)	1		23	
	Loss on asset impairment from audit adjustments	–		(5)	
	Change in period for depreciation expense	–		(8)	
	Intercompany charges reclassification	(14)		(11)	
	Financing cost interest reclassification	(12)		(36)	
	Reclassification of expenses previously netted with revenue	4		11	
		(39)	I07-2	(58)	I07-6
Operating income		45		65	
Other income/expense	Additional legal reserve	–		3	
	Intercompany charges reclassification	(14)		(11)	
	Reclassification of other income previously reported as revenue	1		3	
		(13)	I07-3	(5)	I07-7
Interest expense	Financing cost interest reclassification	12	I07-4	36	I07-8
Net income		$ 20		$ 24	

Accordingly, previously reported amounts are being restated to properly reflect the accounting for these items as follows:

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Statements of Income

The following table summarizes the statements of income for the periods indicated, giving effect to the restatement adjustments described above and showing previously reported amounts and restated amounts for the three and nine months ended June 30, 2007.

Statements of Income

	For the Three Months Ended June 30, 2007				For the Nine Months Ended June 30, 2007			
	As Previously Reported	Increase (Decrease)	Note	As Restated	As Previously Reported	Increase (Decrease)	Note	As Restated
Operating revenues								
Sales of electricity								
Municipalities and cooperatives	$ 1,863	26		$ 1,889	$ 5,527	22		$ 5,549
Industries directly served	304	–		304	907	–		907
Federal agencies and other	29	–		29	80	–		80
Other revenue	40	3		43	106	8		114
Operating revenues	2,236	29		2,265	6,620	30		6,650
Revenue capitalized during pre-commercial plant operations	–	(23)		(23)	–	(23)		(23)
Net operating revenues	2,236	6	I07-1	2,242	6,620	7	I07-5	6,627
Operating expenses								
Fuel and purchased power	779	11		790	2,342	28		2,370
Operating and maintenance	621	(50)		571	1,782	(95)		1,687
Depreciation, amortization, and accretion	366	–		366	1,104	(8)		1,096
Tax equivalents	110	(1)		109	327	(1)		326
Loss on asset impairment	–	1		1	–	18		18
Total operating expenses	1,876	(39)	I07-2	1,837	5,555	(58)	I07-6	5,497
Operating income	360	45		405	1,065	65		1,130
Other income (expense), net	29	(13)	I07-3	16	56	(5)	I07-7	51
	98	–		98	129	–		129

Unrealized gain on derivative contracts, net								
Interest expense								
Interest on debt and leaseback obligations	334	12		346	1,009	36		1,045
Amortization of debt discount, issue, and reacquisition costs, net	4	–		4	14	–		14
Allowance for funds used during construction and nuclear fuel expenditures	(45)	–		(45)	(144)	–		(144)
Net interest expense	293	12	I07-4	305	879	36	I07-8	915
Net income	$ 194	$ 20		$ 214	$ 371	$ 24		$ 395

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Statements of Cash Flows

The following table summarizes the statements of cash flows for the periods indicated, giving effect to the restatement adjustments described above and showing previously reported amounts and restated amounts for the nine months ended June 30, 2007.

Statement of Cash Flows

	June 30, 2007		
	As Previously Reported	Increase (Decrease)	As Restated
Cash flows from operating activities			
Net income	$ 371	$ 24	$ 395
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation, amortization, and accretion	1,134	(8)	1,126
Nuclear refueling outage amortization	62	–	62
Loss on asset impairment	23	(5)	18
Amortization of nuclear fuel	94	–	94
Non-cash retirement benefit expense	151	–	151
Net unrealized gain on derivative contracts	(129)	–	(129)
Prepayment credits applied to revenue	(79)	–	(79)
Fuel cost adjustment deferral	(126)	15	(111)
Other, net	13	(3)	10
Changes in current assets and liabilities			
Accounts receivable, net	122	(22)	100
Inventories and other	(162)	–	(162)
Accounts payable and accrued liabilities	(119)	88	(31)
Accrued interest	(140)	–	(140)
Pension contributions	(56)	–	(56)
Refueling outage costs	(90)	–	(90)
Other, net	43	–	43
Net cash provided by operating activities	1,112	89	1,201
Cash flows from investing activities			
Construction expenditures	(1,041)	(110)	(1,151)
Combustion turbine asset acquisitions	(100)	–	(100)
Nuclear fuel expenditures	(130)	21	(109)
Change in restricted cash and investments	14	–	14
Proceeds from investments, net	2	–	2
Loans and other receivables		–	
Advances	(7)	–	(7)
Repayments	13	–	13
Proceeds from sale of receivables/loans	2	–	2
Other, net	1	–	1
Net cash used in investing activities	(1,246)	(89)	(1,335)