November 1, 2005

Randy P. Trusley, WT 5C-K

AUDIT REPORT 2005-057F – REVIEW OF CONTROLS OVER TENNESSEE VALLEY AUTHORITY’S (TVA) ASSET RETIREMENT OBLIGATION BALANCES

As part of our annual audit plan, we audited the asset retirement obligation (ARO) controls relied on by management to ensure the ARO balances in the TVA financial statements are accurate and complete.

Effective October 1, 2002, TVA adopted Financial Accounting Standards Board Statement No.143 (FAS 143), Accounting for Asset Retirement Obligations. This statement requires, among other things, the recognition of a liability for “legal obligations” associated with the retirement of long-lived assets resulting from the acquisition, construction, development, and/or normal operation of long-lived assets.

As of June 30, 2005, the balance in the ARO approximated $1.8 billion and consisted primarily of the estimated costs to decommission the nuclear and fossil plants at the end of their useful life. Controls over the balance in this and other related ARO accounts included quarterly reconciliations of the general ledger balances and underlying support for the cost estimates maintained in a worksheet format for each plant. We tested the reconciliations and determined the controls over the ARO process were operating effectively to ensure balances were accurately stated, in all material respects, in TVA’s June 30, 2005, financial statements. Our objectives, scope, and methodology are attached.

Information contained in this report may be subject to public disclosure. Please advise us of any sensitive information in this report which you recommend be withheld.

No response to this report is necessary. If you have questions, please call David S. Shields, Auditor, at (865) 632-3354 or Louise B. Beck, Manager, Financial and Operational Audits, at (865) 632-2622. We appreciate the courtesy and cooperation received from your staff during the audit.

Ben R. Wagner
Assistant Inspector General
(Audits and Inspections)
ET 3C-K

DSS:SDB
cc: See page 2
cc (Attachment):
  R. Don Holden, WT 5C-K
  Andrew W. Holmes, WT 5C-K
  Tom D. Kilgore, ET 12A-K
  Richard W. Moore, ET 4C-K
  Michael E. Rescoe, ET 12A-K
  Ellen Robinson, ET 12A-K
  OIG File No. 2005-057F
OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to test controls relied on by management to ensure asset retirement obligation (ARO) balances in Tennessee Valley Authority’s (TVA) financial statements are accurate and complete. The scope of the audit addressed controls in place as of June 30, 2005. The audit did not address the accuracy or reasonableness of the estimated costs to retire the long-lived assets or the discount rate used to account for the obligation under FAS 143.

We assessed the controls by:

- Interviewing employees in the Chief Financial Officer’s Organization.
- Reviewing a draft of TVA accounting white paper – Asset Retirement Obligations (SFAS #143).
- Reviewing Statement of Financial Accounting Standards No. 71 and 143.
- Tracing amounts in the reconciliation to the general ledger and supporting worksheets for the retirement of long-lived assets associated with the fossil plants, combustion turbines, Bellefonte diesel generator, and nuclear plants.
- Verifying the mathematical accuracy of the worksheets supporting the reconciliation.

This audit was performed in accordance with generally accepted government auditing standards. Although we did not test for compliance with laws and regulations, nothing came to our attention during the audit that indicated noncompliance with applicable laws or regulations.