

LONG ISLAND POWER AUTHORITY
(A Component Unit of the State of New York)

Quarterly Unaudited Financial Report

For the six-month period ended June 30, 2017

LONG ISLAND POWER AUTHORITY
(A Component Unit of the State of New York)

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Introduction

The Long Island Power Authority (the Authority) is a component unit of New York State (State). The Authority became the retail supplier of electric service in the Counties of Nassau and Suffolk (with certain limited exceptions) and a portion of Queens County known as the Rockaways (Service Area), on May 28, 1998 by acquiring the transmission and distribution (T&D) system of the Long Island Lighting Company (LILCO) as a wholly-owned subsidiary of the Authority. As part of the acquisition, the Authority also acquired an undivided 18% interest in the Nine Mile Point Unit 2 (NMP2) generating facility, located in upstate New York, which is operated and managed by Exelon Corporation.

In order to assist the Authority in providing electric service to its customers, the Authority entered into operating agreements to provide the Authority with the operating personnel, and a significant portion of the power supply resources, necessary for the Authority to provide electric service in the Service Area.

Since the acquisition, the Authority has conducted business through its wholly owned subsidiary, LILCO, under the names LIPA and Power Supply Long Island, referred to collectively as the Authority. The Authority provides electric delivery service in the Service Area, which includes approximately 1.1 million customers. The population of the Service Area is approximately 2.9 million.

The Authority's role significantly changed as a result of the LIPA Reform Act (Reform Act), which was passed and codified as Chapter 173, Laws of New York, on June 21, 2013 by the New York State Assembly and Senate. The Reform Act is divided into two parts, Part A and Part B. Part A addresses the reorganization of the Authority and substantially changed its operating responsibilities. Under the Authority's new business model, PSEG Long Island is the Authority's service provider pursuant to the Amended and Restated Operations Services Agreement (A&R OSA). Under the A&R OSA, the PSEG Long Island management company is the contracting entity with the Authority. PSEG Long Island is a wholly owned subsidiary of Public Service Enterprise Group (PSEG). The A&R OSA provides for the operation, maintenance and related services for the T&D system. PSEG Long Island is paid a management fee and may earn incentives related to specified performance metrics. Essentially all costs of operating and maintaining the Authority's T&D system incurred by PSEG Long Island are passed through to and paid for by the Authority.

The Authority also has a contract with PSEG Energy Resources and Trade LLC (PSEG ER&T) to provide for services related to fuel and power supply management and certain commodity activities. Separately from its contract with PSEG ER&T, the Authority maintains power purchase agreements with third party power generators.

Part B of the Reform Act created the Securitization Law which established the Utility Debt Securitization Authority (UDSA). The Securitization Law's sole purpose was to provide a legislative foundation for the UDSA's issuance of restructuring bonds to allow the Authority to retire a portion of its outstanding indebtedness and provide savings to the Authority's customers on a net present value basis. The restructuring bonds are to be repaid by an irrevocable, nonbypassable restructuring charge on all the Authority's customers. The UDSA has a governing body separate from that of the Authority and has no commercial operations.

Overview of the Consolidated Financial Statements

The Authority is engaged in business type activities and follows financial reporting for enterprise funds. The Authority's financial statements are prepared on an accrual basis in accordance with generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

The Authority's reporting entity is comprised of itself and (i) its operating subsidiary the Long Island Lighting Company (LILCO), a wholly owned subsidiary of the Authority doing business as "LIPA" and Power Supply Long Island, and (ii) the UDSA. All significant transactions between the Authority, LIPA and the UDSA have been eliminated. The Authority and its blended component units are referred to collectively as the "Authority" in the consolidated financial statements.

The Management's Discussion and Analysis of the Authority's financial performance provides an overview of the Authority's financial information for the six-month period ended June 30, 2017 compared to 2016. The unaudited quarterly financial statements should be read in conjunction with the annual audited financial statements, which may be found on the Authority's website at www.lipower.org.

Contacting the Long Island Power Authority

This financial report is designed to provide the Authority's bondholders, customers, and other interested parties with a general overview of the Authority's finances and to demonstrate its accountability for the funds it receives. If you have any questions about this report or need additional information, contact the Authority at 333 Earle Ovington Blvd., Suite 403, Uniondale, New York 11553, or visit the Authority's website at www.lipower.org.

LONG ISLAND POWER AUTHORITY
(A Component Unit of the State of New York)

Consolidated Statements of Net Position

June 30, 2017 and December 31, 2016

(Amounts in thousands)

Assets and Deferred Outflows of Resources	2017 (unaudited)	2016 (audited)
Current assets:		
Cash and cash equivalents	\$ 172,293	562,156
Restricted cash - working capital requirements	232,968	207,045
Restricted cash	73,175	88,572
Investments	287,023	219,212
Counterparty collateral – posted by the Authority	20,733	8,365
Accounts receivable (less allowance for doubtful accounts of \$37,332 and \$37,716 at June 30, 2017 and December 31, 2016, respectively)	479,522	484,781
Other receivables	87,798	113,154
Fuel inventory	105,460	103,894
Material and supplies inventory	47,496	46,771
Regulatory assets to be recovered within one year	196,051	151,012
Prepayments and other current assets	101,976	54,222
Total current assets	1,804,495	2,039,184
Noncurrent assets:		
Restricted cash and cash equivalents	53,624	76,733
Restricted investments	366,722	394,239
Utility plant and property and equipment, net	7,907,814	7,768,551
Nuclear decommissioning trust	125,050	115,800
Other long-term receivables	28,121	28,285
Unrealized charges	144,646	136,131
Financial derivatives	2,996	2,846
Prepayments	1,637	3,215
Regulatory assets for future recovery	1,126,112	1,148,239
Acquisition adjustment (net of accumulated amortization)	1,045,073	1,100,760
Total noncurrent assets	10,801,795	10,774,799
Deferred outflows of resources:		
Deferred defeasance costs on debt refunding	258,383	273,558
Accumulated decrease in fair value of commodity derivatives	7,409	11,740
Pensions	1,481	1,481
Total deferred outflows of resources	267,273	286,779
Total assets and deferred outflows of resources	\$ 12,873,563	13,100,762

LONG ISLAND POWER AUTHORITY
(A Component Unit of the State of New York)

Consolidated Statements of Net Position

June 30, 2017 and December 31, 2016

(Amounts in thousands)

Liabilities, Deferred Inflows and Net Position	2017 (unaudited)	2016 (audited)
Current liabilities:		
Short-term debt	\$ 518,125	405,625
Current maturities of long-term debt	71,335	117,250
Current maturities of UDSA debt	100,620	72,598
Current portion of capital lease obligation	183,082	195,959
Accounts payable and accrued expenses	450,843	445,566
Regulatory liabilities payable in one year	7,266	12,100
Commodity derivative instruments	5,679	11,569
Accrued payments in lieu of taxes	6,086	10,729
Accrued interest	43,560	48,042
Customer deposits	38,158	37,701
Total current liabilities	1,424,754	1,357,139
Noncurrent liabilities:		
Long-term debt	3,369,051	3,396,020
Long-term UDSA debt	4,278,181	4,360,731
Capital lease obligations	1,930,197	2,021,284
Borrowings	79,789	82,241
A&R Operations Services Agreement-employee retirement benefit	591,576	580,720
Financial derivative instruments	148,513	149,496
Commodity derivative instruments	13,608	2,324
Asset retirement obligation	67,583	66,487
Long-term liabilities and unrealized credits	64,601	69,933
Claims and damages	32,878	41,430
Total noncurrent liabilities	10,575,977	10,770,666
Deferred inflows of resources:		
Regulatory credits - grants	502,213	502,213
Accumulated increase in fair value of financial derivatives	2,995	2,846
Pensions	1,499	1,499
Accumulated increase in fair value of Nine Mile Point 2 Trust	14,348	9,353
Accumulated increase in fair value of OPEB Account	7,283	1,980
Total deferred inflows of resources	528,338	517,891
Net position:		
Net investment in capital assets	(95,152)	(115,699)
Restricted	65,458	73,879
Unrestricted	374,188	496,886
Total net position	344,494	455,066
Total liabilities, deferred inflows of resources and net position	\$ 12,873,563	13,100,762

LONG ISLAND POWER AUTHORITY
(A Component Unit of the State of New York)

Consolidated Statements of Revenues, Expenses, and Changes in Net Position

Six-month period ended June 30, 2017 and 2016

(unaudited)

(Amounts in thousands)

	2017	2016
Operating revenues – electric sales	\$ 1,566,323	1,483,646
Operating expenses:		
Operations – power supply charge (a)	734,333	701,051
Operations - power supply charge-property tax related (b)	105,625	108,571
Operations and maintenance	314,345	264,478
Storm restoration	44,529	63,506
General and administrative	15,313	14,301
Depreciation and amortization	154,797	142,986
Payments in lieu of taxes and assessments	161,587	160,941
Total operating expenses	1,530,529	1,455,834
Operating income	35,794	27,813
Nonoperating revenues and expenses:		
Other income, net:		
Investment income	2,864	5,094
Grant income	3,724	9,179
Carrying charges on regulatory assets	12,941	13,519
Other	2,134	1,699
Total other income, net	21,663	29,491
Interest charges and (credits):		
Interest on long-term debt	170,946	164,382
Other interest	13,777	17,317
Other interest amortizations	(13,291)	(3,114)
Allowance for borrowed funds used during construction	(3,403)	(3,360)
Total interest charges and (credits)	168,029	175,225
Change in net position	(110,572)	(117,921)
Net position, beginning of year	455,066	481,499
Net position, end of period	\$ 344,494	363,578

- (a) National Grid Power Supply Agreement (PSA) and Nine Mile Point 2 (NMP2) operating costs have been reclassified in 2016 from Operations and Maintenance to Power Supply Charge for comparative presentation purposes.
- (b) Pass through taxes related to the PSA, NMP2 and certain other long term operating agreements for 2016 have been reclassified to Power Supply Charge for comparative presentation purposes.

LONG ISLAND POWER AUTHORITY
(A Component Unit of the State of New York)
Consolidated Statements of Cash Flows
Six-month period ended June 30, 2017 and 2016
(unaudited)
(Amounts in thousands)

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
Operating revenues received	\$ 1,625,635	1,495,087
Paid to suppliers and employees:		
Operations and maintenance	(272,603)	(226,326)
Operations – power supply charge (a)	(830,632)	(812,277)
Power supply charge-property tax related (b)	(105,625)	(108,561)
Payments in lieu of taxes	(259,293)	(254,159)
Collateral on commodity derivative transactions, net	(11,489)	38,234
PSEG Long Island Pension funding	(17,100)	(11,800)
Net cash provided by operating activities	<u>128,893</u>	<u>120,198</u>
Cash flows from investing activities:		
Earnings received on investments	10,914	4,569
Restricted cash	12,583	2,735
Sales of restricted investment securities	27,517	—
Purchases of investment securities	(67,811)	(10,686)
Other	—	277
Net cash used in investing activities	<u>(16,797)</u>	<u>(3,105)</u>
Cash flows from noncapital financing related activities:		
Grant proceeds	1,919	16,110
Proceeds from credit facility draws and commercial paper program	130,000	170,625
Repayment of credit facility draws and commercial paper program	(17,500)	—
Net cash provided by noncapital related activities	<u>114,419</u>	<u>186,735</u>
Cash flows from capital and related financing activities:		
Capital expenditures	(326,374)	(237,676)
Proceeds from insurance recoveries	—	49,580
Proceeds from the issuance of long-term debt - UDSA	—	783,288
Debt issuance costs	(259)	(4,713)
Other interest costs	(13,870)	(16,349)
Interest paid	(97,084)	(80,254)
Redemption of long-term debt - LIPA	(46,385)	(873,351)
Redemption of long-term debt - UDSA	(32,790)	(30,000)
Interest paid - UDSA	(99,616)	(73,738)
Net cash used in capital and related financing activities	<u>(616,378)</u>	<u>(483,213)</u>
Net decrease in cash and cash equivalents	(389,863)	(179,385)
Cash and cash equivalents at beginning of year	<u>562,156</u>	<u>600,698</u>
Cash and cash equivalents at end of period	<u>\$ 172,293</u>	<u>421,313</u>
Reconciliation to net cash provided by operating activities:		
Operating income	\$ 35,794	27,813
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	154,797	142,986
Other post-employment benefit non-cash expense	18,100	19,237
Nuclear fuel burned	6,856	4,538
Shoreham and VBA surcharges	19,888	19,726
Accretion of asset retirement obligation	1,797	1,765
Changes in operating assets and liabilities:		
Accounts receivable, net	29,708	50,683
Regulatory assets and liabilities	(89,661)	(122,674)
Fuel and material and supplies inventory	(2,291)	14,004
Accounts payable, accrued expenses and other	(46,095)	(37,880)
Net cash provided by operating activities	<u>\$ 128,893</u>	<u>120,198</u>

- (a) National Grid Power Supply Agreement (PSA) and Nine Mile Point 2 (NMP2) operating costs have been reclassified in 2016 from Operations and Maintenance to Power Supply Charge for comparative presentation purposes.
- (b) Pass through taxes related to the PSA, NMP2 and certain other long term operating agreements for 2016 have been reclassified to Power Supply Charge for comparative presentation purposes.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)

Six-Month Period ended June 30, 2017 Compared to 2016

The change in net position for the six-month period ended June 30, 2017 was \$7 million more favorable than the six-month period of 2016.

Operating Revenues

Operating revenue increased \$83 million compared to the six-month period of 2016, resulting from rate changes effective January 1, 2017, consistent with the approved Three Year Rate Plan. In the 2017 approved budget, revenue was projected to grow to reflect anticipated (i) increases in the Power Supply Charge; (ii) increases in operating expenses to support new programs to maintain reliability, improve system resiliency and customer satisfaction; (iii) increases in property tax assessments; and (iv) increases in debt service, including fixed obligation coverage to support the Authority's capital improvement plan.

Operating Expenses

Effective January 1, 2017, the Power Supply Charge includes costs associated with the National Grid Power Supply Agreement (PSA) and operation and maintenance costs associated with the Authority's 18% interest in the Nine Mile Point 2 (NMP2) nuclear generating station. These changes were made to be more consistent with how other New York electric utilities classify generation capacity costs. To achieve conformity and comparability, the prior year amounts related to the PSA and NMP2 have been reclassified in the financial statements from operating costs to the Power Supply Charge. Power supply costs, including those related to pass through property taxes, increased \$30 million when compared to the same six-month period of 2016 due to an increase in natural gas and oil prices.

Operations and maintenance expense increased \$50 million compared to the same six-month period of 2016 due to higher costs related to increased tree trimming to improve system resiliency. Also contributing to the increase was a lower level of storm activity (see below), which results in higher labor cost allocations to operating areas such as customer and business services.

Storm restoration expense decreased \$19 million when compared to the same six-month period of 2016 due to a lower level of storm activity. The Authority experienced seven storms through June 2017, two of which required mutual assistance, compared with nine storms through June 2016, four of which required mutual assistance.

Depreciation and amortization increased \$12 million when compared to the same six-month period of 2016 primarily due to increased utility plant assets placed in service.

Nonoperating Expenses

Other income decreased \$8 million compared to the same six-month period of 2016 primarily due to the receipt in the prior year of a Federal Emergency Management Agency grant related to a reimbursable storm event.

Interest charges decreased \$7 million compared to the same six-month period of 2016 due to the interest savings resulting from the 2016 refunding of long term bonds.

Liquidity and Capital Resources

The Authority adopted a policy that it should at all times maintain cash on hand and available credit equivalent to at least 120 days of operating expenses. As of June 30, 2017 and December 31, 2016, the Authority's available sources of liquidity for operating purposes and capital program funding, as displayed below, achieved the policy target.

	(amounts in thousands)	
	June 30, 2017	December 31, 2016
Operating liquidity		
Unrestricted cash and cash equivalents	\$324,078	652,370
OPEB account cash, cash equivalents & investments	135,240	128,998
PSEG LI Working Capital requirements	232,968	207,045
Total operating liquidity	692,286	988,413
Available credit		
General Revenue Notes - Revolving Credit Facility	220,000	337,500
General Revenue Commercial Paper	186,875	169,375
Subordinated Revenue Commercial Paper	50,000	50,000
Total available credit	456,875	556,875
Total cash, cash equivalents, investments & available credit	\$1,149,161	1,545,288
Restricted cash		
FEMA - restricted	\$420,347	470,972
UDSA	73,175	88,572
Total restricted cash	\$493,522	559,544
Days cash & available credit on hand	147	197

Financing Activities

The Authority's consolidated debt at June 30, 2017 and December 31, 2016 is comprised of the following:

	(amounts in thousands)	
	June 30, 2017	December 31, 2016
Long-term debt:		
General Revenue Bonds	\$ 3,289,262	3,356,972
Unamortized premiums	151,124	156,298
Less: Current maturities	(71,335)	(117,250)
	<u>\$ 3,369,051</u>	<u>3,396,020</u>
UDSA Restructuring Bonds	\$ 3,932,739	3,965,529
Unamortized premiums	446,062	467,800
Less: Current maturities	(100,620)	(72,598)
	<u>\$ 4,278,181</u>	<u>4,360,731</u>
Short-term debt:		
General revenue commercial paper notes	\$ 138,125	155,625
Subordinated commercial paper notes	250,000	250,000
General revenue notes - revolving credit facility	130,000	—
	<u>\$ 518,125</u>	<u>405,625</u>

Regulatory Assets and Liabilities

The table below are the Authority's costs to be recovered or returned in a future period (regulatory assets or liabilities). Amounts to be recovered within the one year period showed an increase totaling \$45 million from December 31, 2016 to June 30, 2017 due primarily to the increase in the Power Supply Charge recovery. Fixed capacity costs related to long-term purchased power agreements are recognized seasonally to appropriately match to the period of higher capacity requirements resulting in a higher deferral during the first half of the year.

	(amounts in thousands)	
	June 30, 2017	December 31, 2016
Regulatory assets to be recovered within one year		
Operations services agreement – employee retirement benefits	\$ 58,000	54,199
Shoreham property tax settlement	47,093	43,498
Power supply charge	44,577	9,400
Employee benefit plan settlement	21,634	21,634
Revenue decoupling mechanism	15,315	15,024
New York State assessment	3,158	1,330
Debt issuance costs	3,209	3,209
Southampton visual benefit assessment	1,007	948
Distributed energy resources	2,058	1,770
Balance of Regulatory assets to be recovered within one year	\$ 196,051	151,012
Regulatory assets for future recovery		
Operations services agreement – employee retirement benefits	\$ 390,859	423,050
Shoreham property tax settlement	413,919	424,396
Employee benefit plan settlement	162,254	173,070
Power supply charge	49,074	44,649
Delivery service adjustment	70,319	41,841
Debt issuance costs	31,583	33,004
Southampton visual benefit assessment	8,104	8,229
Balance of Regulatory assets for future recovery	\$ 1,126,112	1,148,239
Regulatory liabilities payable within one year		
Delivery service adjustment	\$ 7,266	12,100
Balance of Regulatory liabilities payable within one year	\$ 7,266	12,100