

**LONG ISLAND POWER AUTHORITY  
MINUTES OF THE 169th MEETING  
HELD ON MAY 26, 2005**

**Pursuant to notice dated May 19, 2005, the Long Island Power Authority (the "Authority") was convened for the one hundred and sixty-eighth time at 11:15 AM at the Nassau Community College Administration Building in Uniondale, NY.**

**The following Trustees of the Authority were present:**

**Richard M. Kessel, Chairman  
Patrick Foye, Deputy Chairman  
Howard Steinberg, Deputy Chairman  
Michael Affrunti  
Harvey Auerbach  
John Fabio  
Edna Gerrard  
Robert Maimoni  
Nancy Nugent  
James M. Shuart**

**Also representing the Authority were Stanley Klimberg, General Counsel, Edward Grilli, Chief of Staff, Seth Hulkower, Chief Operating Officer, Elizabeth McCarthy, Chief Financial Officer, Richard Bolbrock, Vice President – Power Markets, Bert Cunningham, Vice President – Communications, Bruce Germano, Vice President – Retail Services, Kenneth Kane, Controller, and Kathleen Stella, Secretary to the Board of Trustees.**

Upon determining that a quorum was present, Chairman Kessel called the meeting to order.

Chairman Kessel thanked Mr. Sean Fanelli and the administration of Nassau Community College for allowing LIPA to use its facility for this meeting. The Chairman continued that Nassau Community College is one of the greatest community colleges in the country. He indicated that he is a former member of the Board of Trustees of Nassau Community College, having served for nineteen years, and that was his first public job.

Chairman Kessel stated that the first item on the agenda is the adoption of the minutes of the Board's last meeting held on April 20, 2005.

Upon motion duly made and seconded, the following resolution was approved unanimously:

**738. APPROVAL OF MINUTES AND RATIFICATION OF ACTIONS TAKEN AT THE APRIL 20, 2005 MEETING OF THE BOARD OF TRUSTEES OF THE LONG ISLAND POWER AUTHORITY**

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**RESOLVED**, that the Minutes of the meeting of the Authority held on April 20, 2005 are hereby approved and all actions taken by the Trustees present at such meeting, as set forth in such Minutes, are hereby in all respects ratified and approved as actions of the Authority.

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**Chairman Kessel stated that he just came from the Hauppauge Industrial Association Annual Trade Show at Suffolk Community College, where LIPA has a great exhibit. He thanked Mr. Germano and LIPA's Retail Services staff who worked hard on LIPA's exhibit.**

**Chairman Kessel stated that LIPA's service continues to be of the highest quality. The Chairman continued that LIPA in conjunction with the IBEW just participated in Electric Safety Day, during which LIPA talked with hundreds of students from local schools about electric safety. He thanked Mr. Raghelli, Ms. Redmond and LIPA's staff for their help in putting the programs together.**

**Chairman Kessel stated that Long Island recently experienced very tough weather. The Chairman indicated that despite the brutal weather, LIPA crews worked continuously to restore service. He continued that he is proud LIPA leads the state in reliability. He stated that despite the weather, there were not many outages, which says a lot about the investment LIPA has made in the system. The Chairman continued that this is also a testament to LIPA's great work force, and to the commitment of the Board and Governor Pataki to LIPA.**

**Chairman Kessel stated that the price of oil continues to exert financial pressure on LIPA. The Chairman continued that LIPA is significantly over budget with respect to fuel costs, although LIPA's total operating expenses are below budget by about \$10 million. He thanked Mr. Grilli, Ms. McCarthy, Mr. Hulkower and LIPA's management for holding down costs.**

Chairman Kessel stated that the price of oil, which has moved parallel to the price of natural gas, fell to \$47 per barrel several weeks ago, but it is now back to \$51 per barrel. The Chairman continued that oil has risen by nearly \$2 per barrel within the last three days, and its volatility continues to impact LIPA. He indicated that LIPA will add 1.9 percent to its electric bills through LIPA's fuel surcharge, beginning June 8, 2005.

Chairman Kessel stated that the increase in bills negatively impacts LIPA's customers. The Chairman continued that the 1.9 percent increase is less than inflation and less than the increase in other energy prices on Long Island. He indicated it is extraordinary that LIPA has the financial strength to be able to hold the increase to less than 2 percent.

Chairman Kessel stated that heating costs increased by more than 20 percent over the winter, and gasoline costs at one point had risen by more than 25 percent since the beginning of 2005. The Chairman continued that any increase is bad news, but being able to hold it under 2 percent is very important, and reflects the wise financial decisions and hedging policies of the Authority.

Chairman Kessel stated that LIPA is the only utility in the region and possibly the country that not only announces a fuel cost increase in its bills, but also holds public hearings on the matter. The Chairman continued that most utilities increase their bills through their fuel adjustment clauses and never tell the public about it. He added that LIPA is run differently, and it is critically important to be honest with the public.

Chairman Kessel stated that although this is an automatic pass through that LIPA does not have to announce, he is announcing it, and LIPA will hold two public hearings to receive public comment. The Chairman continued that many utilities are raising bills, and their customers will not know this until one day they wake up and notice their bills are much higher.

Chairman Kessel stated that he hopes this will be the only increase that LIPA must institute this year, but if oil prices rise to the level of \$55 to \$60 per barrel, it will be difficult to hold this level. The Chairman indicated that LIPA will take another look at this in August and September, but based on LIPA's best projections and in view of LIPA's hedging practices and the budget, LIPA thinks it can get through the year with this minimal increase in bills.

Chairman Kessel stated that the upcoming weekend marks the seventh year of LIPA's ownership and operation of the electric system on Long Island. The Chairman continued that LIPA's bills are only approximately 7.5 percent higher than LILCO's were seven years ago. He indicated that LIPA's bills are somewhere between 30 and 40 percent less than if LILCO had continued ownership and operation of the electric system.

Chairman Kessel stated that LIPA has come a long way and has become the most reliable overhead utility in New York State. The Chairman continued that LIPA is at the top of every service survey in the country, and LIPA has a good relationship with its customers, great emergency responsiveness and one of the

leading clean energy programs anywhere in the world. He indicated that there is no better utility not only in terms of how it is operated and its finances, but also how people perceive it.

Deputy Chairman Steinberg stated that he was contacted by a member of a strategic planning board in Oregon who indicated that Oregon has problems similar to those that formerly existed on Long Island. He continued that Oregon has discussed LIPA as a model to follow, which is a nice compliment. Chairman Kessel stated that this is good to hear.

Trustee Fabio asked whether the dynamics of the greater oil demand in China and India, and the fact that refining capacity is less than it should, come into play to sustain higher oil prices. Chairman Kessel responded that increased usage in countries like China and India and the lack of refining capacity are forcing up oil prices. The Chairman continued that LIPA has commissioned a report from Pace Global Energy, and they have made that same point. He added that there are other factors as well that make for much volatility.

Chairman Kessel stated that since LIPA took over LILCO, the price of a barrel of oil has risen 230 percent, and there appears to be no relief. The Chairman continued that the answer is to aggressively find ways to produce electricity other than by oil or gas, and one example of LIPA doing this is the Neptune Project, which is fully permitted. He indicated that the Neptune Project will be on line in two summers, and it will allow LIPA to import 660 MW of electricity, a majority of which is not produced by oil or gas. He added that LIPA

just worked out an agreement with Nassau County Executive Suozzi and the Nassau County IDA that will allow for the use of IDA funds to lower the cost of that project.

Chairman Kessel stated that the economics of the offshore wind project are moving to a point where it is almost even with building a new oil or gas plant, due to the cost of fuel. The Chairman continued that the dependence on fossil fuels is a national problem. He added that LIPA is dealing with it on Long Island.

Chairman Kessel stated it is important to note that there will be huge increases in the cost of fuel going forward, and it is becoming a larger percentage of LIPA's budget. The Chairman continued that it is now close to sixty percent of LIPA's budget, and this is putting financial pressure on LIPA.

Chairman Kessel stated that he commends Mr. John Daly, who represents the IBEW clerical union, and the LIPA staff who work at the Call Center. The Chairman indicated that they do a great job.

Chairman Kessel stated that the next item on the agenda is the Operations Report, to be delivered by Mr. Hulkower.

Mr. Hulkower reported that the year-to-date statistics for Sales & Marketing Load and Revenue Growth and Retention are ahead of target, with 8.90 MW of load against a goal of 6.17 MW. He indicated that LIPA's projection for year end is running behind at 34.66 MW against a goal of 42.00 MW.

Mr. Hulkower stated that with respect to Clean Energy Initiatives, LIPA is running considerably ahead in terms of participants and MW reduction. He further reported that LIPA's arrears total \$77.7 million, which is down from \$86 million in October. He indicated that he will have a more detailed report on the matter at the June Board meeting.

Mr. Hulkower reported that the performance of the electric system in 2004 showed many improvements. He continued that LIPA's SAIFI improved 6 percent, CAIDI improved 4 percent and SAIDI, which is a combination of the time between interruptions and the length of interruptions, improved 10 percent. He added that LIPA's momentary interruptions are at a record low, and LIPA's reliability is in the first quartile for all three major indices.

Mr. Hulkower reported that LIPA's SAIFI at the end of 2004 was at 14.4 months between interruptions, which fell within the targeted band. He continued that LIPA's CAIDI is down to an all-time low of 62 minutes. He added that LIPA's SAIDI finished at 52 minutes per year.

Mr. Hulkower reported that LIPA's transmission substation reliability showed an improvement of approximately 5 percent. He continued that LIPA significantly reduced distribution outages by 49,000, due largely to LIPA's circuit improvement program. He added that animal contacts, burn-outs of taps and clamps, motor vehicle accidents and storm events decreased from 2003 to 2004.

Mr. Hulkower stated that the circuit improvement program, which targets the worst performing circuits, has yielded a 66 percent reliability improvement for those circuits within the past 20 years. He continued that tree trim programs prevented 500,000 customer interruptions over the last 10 years, and automatic sectionalizing prevented 2.5 million customer interruptions since 1994. He added that LIPA is replacing exit cables from the substations that may have been stressed over time, and LIPA is performing infrared scans of the transmission distribution lines to identify overloaded, overheated and vulnerable places.

Mr. Hulkower stated that LIPA will spend \$21.18 million on capital programs in 2006, which is a low. He indicated that capital expenditures will rise to about \$26 million through 2010.

Deputy Chairman Steinberg asked whether LIPA is deferring activities and expenditures from 2006 to 2007 and 2008. Mr. Hulkower responded that this is part of a planned program, and part of the reason for the increased cost over time is that costs are going up for everything. He indicated that LIPA is targeting its spending to stay within the targeted SAIFI band of 13 months to 15.5 months, and the decreased spending in 2006 is a function of the scheduled work.

Deputy Chairman Foye asked whether there are projected levels of improvement that go with the level of spending. Mr. Hulkower answered that the level of spending will keep LIPA's reliability within the targeted bands.

Trustee Nugent asked whether any of the improvements in the system were driven by the last blackout. Mr. Hulkower responded that there has been improvement from spending on the non-transmission side related to the blackout, and most of this will be completed this year. He added that there is more spending and improvement on the transmission side related to the blackout.

Mr. Hulkower reported that LIPA had 61,000 more customers with service interruptions in 2005 than 2004. He continued that in the first quarter of 2004 LIPA had the best performance in 34 years, and LIPA had two blizzards in the first quarter of 2005. He added that LIPA's targeted reliability programs are directed to especially problematic circuits, and the underground program is taking a look at LIPA's aging underground system.

Trustee Maimoni asked whether the underground facilities needing to be removed will be replaced by underground or above-ground lines. Mr. Hulkower answered that the underground lines will be replaced in kind.

Chairman Kessel stated that this is a good report, and it shows the work LIPA has done and continues to do in the reliability area.

Deputy Chairman Foye stated that LIPA should make sure the public knows of the dramatic improvement in the quality of service, in addition to the rate reductions. Chairman Kessel stated that LIPA should work on holding press conferences with the local press and community leaders on areas in which improvements have been made.

Trustee Affrunti asked what LIPA does after identifying poles that are in high risk areas for accidents. Mr. Hulkower answered that LIPA actually moves some away from the traffic flow. Trustee Affrunti asked whether LIPA first notifies the public emergency and highway departments to see if they will take corrective action to avoid the cost to LIPA of moving the poles. Mr. Hulkower answered that LIPA tries to work with the public works departments when they are laying out roads and when they are making modifications, but they have their own plans and coordination. Trustee Affrunti stated that sometimes those public improvements leave LIPA's poles more vulnerable, and LIPA should not bear the costs of correcting the situation.

Chairman Kessel stated that there have been a number of incidents, including one in North Merrick where road work ultimately put the pole in the street. The Chairman continued that LIPA moved the pole because it was a hazard. He added that LIPA will continue to work on this with the municipalities, with whom LIPA has a good relationship.

Chairman Kessel stated that the next item on the agenda is the Finance report, to be delivered by Ms. McCarthy.

Ms. McCarthy reported that for the four months ended April 30, 2005, LIPA had a deficit of \$185 million, which is \$13 million ahead of plan. She continued that revenues are essentially flat, which is on plan, but bundled residential, commercial and industrial sales are approximately 1.3 percent below plan. She

indicated that this is a result of lower than expected growth, which has been offset somewhat by higher average pricing. She reported that LIPA's Customer Choice Program had significant growth above plan. She stated that the rough weather essentially had no impact on revenues.

Ms. McCarthy reported that fuel and purchased power costs are approximately 4 percent or \$18 million below plan, due to lower bundled sales and lower commodity costs. She continued that LIPA expects the commodity costs to be above plan for the year.

Ms. McCarthy reported that PILOTs are approximately 6 percent higher than budget, due to higher than budgeted increases in school and town taxes. She continued that LIPA expects to be approximately \$5 million above budget for the year.

Ms. McCarthy stated that at the end of April, LIPA had \$445 million in cash invested in a number of different instruments, with approximately 95 percent held in instruments of three months or less.

Deputy Chairman Steinberg asked whether LIPA still projects a \$20 million excess of revenues over expenses. Ms. McCarthy answered that with the implementation of the surcharge increase, LIPA believes it will meet the \$20 million target.

Deputy Chairman Foye stated that the Finance and Audit Committee met for an hour and a half prior to this meeting and the financials were discussed in great detail. He continued that the Committee also discussed in detail the hedging program and a number of other issues.

Chairman Kessel stated that the next item on the agenda is Board consideration of a resolution authorizing the Chairman to engage Bear, Stearns & Co. to provide financial advisory services to the Long Island Power Authority. The Chairman continued that in March 2005, the Authority issued an RFP for experienced firms to act as Financial Advisor to the Authority, and five responses were received. He indicated that a selection committee comprised of Authority staff members carefully examined each proposal; and based on the written submissions, the oral presentations and an assessment of the Authority's needs, it was determined that Bear Stearns is best suited to fulfill those needs.

Chairman Kessel stated that some of the strengths of Bear Stearns include its in-depth working knowledge and understanding of the Authority, its debt and operations. The Chairman continued that the firm has previously provided substantial and valuable services to the Authority in connection with the acquisition of LILCO and related complex transactions, subsequent financings, the GPRA, and strategic organizational and governance matters, among others. He added that Bear Stearns demonstrated significant prior relevant experience in providing financial advisory services, and he recommends that Bear Stearns be selected as the Authority's Financial Advisor.

Trustee Auerbach stated that the Finance and Audit Committee discussed the matter earlier and had no concerns.

Deputy Chairman Foye asked if Ms. McCarthy could discuss the fees relative to what the Authority is currently paying. Ms McCarthy responded that the total amount of fees would be capped at \$100,000 above LIPA's current level of spending, and the fees could be approximately \$1 million below the current level, depending on the extent of transactions. Deputy Chairman Foye asked if the worst case scenario would be \$100,000 greater than current spending. Ms. McCarthy answered affirmatively. She indicated that the proposed fee structure has a base retainer and transaction fee up to a cap for certain types of transactions. She explained that the prior fee was a flat retainer, so the new capped fee would be \$100,000 above the prior flat retainer fee.

Upon motion duly made and seconded, the following resolution was approved, with Deputy Chairman Foye and Deputy Chairman Steinberg abstaining:

#### **739. ENGAGEMENT OF FINANCIAL ADVISOR**

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**RESOLVED**, that the Chairman be, and hereby is, authorized to engage Bear, Stearns & Co. Inc. as the Long Island Power Authority's Financial Advisor, with the contract term to be two years.

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Chairman Kessel stated that the next item on the agenda is Board consideration of a resolution adopting an addition to LIPA's tariff to charge customers for the installation and operation of remote meter reading equipment capable of providing usage and demand determinants without the need to gain access to the customer premises. The Chairman continued that in March 2005, LIPA issued a Notice of Proposed Rulemaking inviting public comment on LIPA staff's proposal to add provisions to LIPA's tariff that would provide for charges for remote meter reading services. He added that there would be a total one-time charge of \$127 per location, and daily recurring charges of \$1.40 for wireless cellular installations and \$.74 for telephone land-line installations.

Chairman Kessel stated that the benefits of remote meter reading include enhancing customer security, obviating the need for the customer to provide personnel to accompany the meter reader, and reducing the frequency of bills that are estimated. The Chairman indicated that public hearings were held in Nassau and Suffolk, and the public was given the opportunity to submit written comments by May 9, 2005. He added that no comments were received, and he urges the Board to adopt the new tariff.

Deputy Chairman Foye asked whether the one-time charge is the same for commercial as well as residential customers. Mr. Germano responded yes and noted that the charge is based on LIPA's cost to go out and do the work.

Deputy Chairman Steinberg asked whether the service requires somebody to enter the residential customer's premises to make changes at the meter.

Chairman Kessel answered that a site survey would be required initially, but the LIPA representative would not need to return. The Chairman continued that the new service offering is primarily for commercial customers, although it could be used by residential customers. He added that he has received complaints in connection with LIPA meter readers who have been denied access to a commercial facility by security personnel, and remote meter reading makes sense for those companies. He stated that LIPA intends to work with commercial and industrial customers to prevent any conflicts with security.

Deputy Chairman Steinberg asked if it would be optional for residential customers. Chairman Kessel answered that it would be optional for everyone. Mr. Germano indicated that it is based on the customer's request to LIPA, and otherwise if LIPA installs the service for its own purposes, LIPA will not charge the customer. Deputy Chairman Steinberg asked whether LIPA plans to notify all residential customers that remote meter reading is available at a charge. Mr. Germano answered that LIPA had not intended to do that.

Deputy Chairman Steinberg stated that it sounds like a good idea, and there are probably many customers who would not want people to come to their homes to read their meters. Mr. Germano answered that there is a high up front cost with relatively little benefit for residential customers. He added that it is mostly an access issue.

Trustee Fabio asked if a cost/benefit analysis was performed to determine what LIPA will save in terms of manpower. Mr. Germano answered that LIPA is

looking at the issue, but the cost to have meters read by people is significantly less, and there has not been wide scale deployment of automatic meter reading.

Deputy Chairman Foye asked if automatic meters are being installed in new homes. Mr. Germano answered that this has not occurred yet, but LIPA is currently looking at the issue.

Chairman Kessel stated it is important to note that the meter readers do a terrific job, and people actually like when they come. The Chairman indicated that he has received letters from senior citizens indicating they look forward to the visit by the meter reader.

Chairman Kessel stated that the automatic meter reading technology has been around a long time. The Chairman continued that he previously suggested to the Consumer Protection Board that electric meters be converted to read in dollars and cents, and this was not adopted.

Upon a motion duly made and seconded, the following motion was approved unanimously:

#### **740. APPROVAL OF TARIFF REVISIONS ESTABLISHING REMOTE METER READING SERVICE CHARGES**

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WHEREAS, the Long Island Power Authority staff issued a Proposal to add provisions to LIPA's Tariff establishing Remote Meter Reading ("RMR") service charges, including specified recurring and nonrecurring charges that are cost-based; and under the Proposal existing customers of RMR would be subject to

recurring charges but not nonrecurring charges; and neither recurring nor nonrecurring charges would apply to customers whose RMR equipment has been installed for LIPA's own programs, including the Peak Load Reduction Program; and

WHEREAS, following Public Notice in the State Register on March 16, 2005, two public hearings were held on May 3, 2005 and the public was afforded the opportunity to submit written comments by May 9, 2005; and no public comments have been received; and

WHEREAS, as discussed in the preceding Memorandum, the Proposal is in the public interest;

NOW, THEREFORE, BE IT RESOLVED, that the Proposal is hereby adopted and approved; and be it further

RESOLVED, that the attached Tariff leaves reflecting our action herein are approved.

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Chairman Kessel stated that the next item on the agenda is a report on LIPA's hedging program, to be delivered by Ms. McCarthy.

Ms. McCarthy stated that she will be presenting the report with Mr. Corey Horowitz, LIPA's Director of Risk Management. She reported that fuel and purchased power costs represent more than 50 percent of LIPA's operating costs, and since May 1998, residual fuel oil and natural gas costs have increased more than 200 percent and have experienced significant and growing volatility.

Ms. McCarthy reported that LIPA manages its fuel and purchased power costs through two mechanisms: first, through the application of LIPA's comprehensive Risk Management Program; and second, through the application of the Fuel and Purchased Power Cost Adjustment mechanism. She continued

that LIPA's goal is to minimize the impact of fuel and purchased power price volatility on customer bills, while maintaining LIPA's financial stability.

Mr. Horowitz reported that LIPA consumes residual fuel oil to produce electricity and the residual fuel oil market has moved up from \$30 per barrel to \$38. He noted that for crude oil and residual fuel oil, which is a refined product, there is great concern about the refining capacity in the United States and abroad. He added that this is reflected in the heating oil inventory numbers from the DOE and the unleaded gasoline inventory numbers.

Mr. Horowitz indicated that in January 2004, the budgeted level for residual fuel oil was approximately \$31, but immediately after establishing the budget, global events such as growth in China and India unfolded and the market started to oscillate. He added that in February 2005, the market exploded, due largely to concerns that OPEC's production capacity was diminishing, thereby reducing the ability to meet any additional demand shock.

Deputy Chairman Steinberg asked whether there are timing differences that account for the delta between the residual fuel oil and crude oil prices. Mr. Horowitz answered no. He continued that crude oil is globally traded, and the market is affected by global demand and currency rates.

Deputy Chairman Steinberg asked whether it is correct to link the need for the fuel surcharge to crude oil prices. Mr. Horowitz responded that crude oil prices will continue to rise and fall due to various economic factors, but residual

fuel oil is the commodity that LIPA hedges. Deputy Chairman Steinberg asked if residual fuel oil is less volatile than crude. Mr. Horowitz answered that the volatility is very similar to crude, but even though crude oil prices are coming down, there is a concern that crude oil cannot be refined fast enough to meet demand. He indicated that the risk of not being able to meet future demand has been reflected in the price of residual oil.

Chairman Kessel asked whether that also impacts the price of crude oil. Mr. Horowitz answered yes. He continued that heating oil prices moved up this winter, and there is still great concern that heating oil inventories are below last year's levels, and well below the five-year average. He indicated that if there is a very warm summer or very cold weather, the inventory will be very tight.

Chairman Kessel asked if the concern is still present. Mr. Horowitz answered affirmatively. He indicated that part of the reason crude oil prices spiked yesterday was that inventory growth actually flattened out this week.

Trustee Nugent asked where the refineries are located from which LIPA purchases residual fuel oil. Mr. Horowitz answered that they are scattered throughout the United States. Trustee Nugent asked if there were any new refineries built in the United States. Ms. McCarthy responded that there have been no new refineries constructed for 27 years. Mr. Horowitz indicated that part of the reason is the increased environmental compliance, and there is an approximate two-year lag to site and build a refinery to meet demand.

Mr. Horowitz reported that in the Risk Management Program LIPA tries to measure and control specific risk factors. He continued that LIPA isolates the risk factors and determines which risk factors LIPA can tolerate and reasonably control, such as transmission risk which can be managed by large investments in the transmission and distribution system. He added that some risks cannot be tolerated and LIPA chooses to transfer such risks to another entity, which is the basis for hedging.

Mr. Horowitz indicated that hedging provides a means to transfer risk to provide a range of expected financial results for LIPA. He continued that it reduces volatility of commodity prices and provides a level of protection in LIPA's financial budget. He added that it minimizes the variability of revenues and expenses, and as prices move hedge positions will generate cash to offset a shortfall in the revenues to meet expenses month by month.

Mr. Horowitz stated that LIPA does not speculate in the market. He continued that speculators or traders are specifically trying to profit from a very specific movement in the market, but LIPA tries to mitigate or limit the exposure to volatility of the commodity prices.

Mr. Horowitz reported that in 2002, the Authority adopted the LIPA Governing Policy for Energy Risk Management, which set forth a broad set of guidelines for overseeing the hedging program. He indicated that it described the commodities LIPA can hedge, the instruments LIPA can use, the volume limits, and the term for which LIPA is allowed to hedge. He added that one important

element of the policy was the establishment of the Executive Risk Management Committee (ERMC) that oversees and delegates authority to individuals inside LIPA to act within the hedging program.

Deputy Chairman Foye asked who is on the Committee. Ms. McCarthy responded that it consists of herself, Mr. Klimberg, Mr. Bolbrock, Mr. Hulkower and Mr. Grilli. Deputy Chairman Foye asked whether LIPA works with an outside consultant. Ms. McCarthy answered that Pace Global Energy advises and works with the ERMC.

Deputy Chairman Foye asked if the hedging program is disclosed in LIPA's financial statements. Ms. McCarthy responded that it is. Deputy Chairman Foye asked whether it is reviewed monthly with the Finance and Audit Committee. Ms. McCarthy answered yes.

Deputy Chairman Foye asked whether the hedging program is reviewed with the Comptroller. Ms McCarthy responded that there is no formal reporting, but LIPA provides financial statements. Chairman Kessel stated that LIPA actually discussed this with the Comptroller approximately one year ago. Deputy Chairman Foye stated that it was also discussed with KPMG, LIPA's independent auditor.

Deputy Chairman Steinberg asked whether the maximum level of financial risk taken by LIPA could be quantified. Ms McCarthy replied that LIPA hedges against a movement in its fuel costs that would impact bills, and measures risk

on this basis. Deputy Chairman Steinberg asked whether this means that LIPA is not taking financial risk regard the assets of the enterprise. Ms. McCarthy answered that LIPA is protecting against that, and LIPA has a credit limit set at \$40 million for each counterparty. She added that any time they encroach, LIPA has collateral calls.

Deputy Chairman Foye asked if the collateral calls had all been satisfied. Ms. McCarthy responded affirmatively and noted that LIPA moves collateral daily.

Deputy Chairman Steinberg asked whether LIPA imposes credit rating requirements. Ms. McCarthy responded affirmatively and noted that LIPA looks to the credit agencies and requires LIPA's counterparties to be rated A or above.

Mr. Horowitz stated that the ERMC adopted a policy control and procedures manual, which governs the activity in LIPA's Energy Risk Management Program. He indicated that the main business objective is to constrain LIPA's financial outcomes and levels of surcharge to its ratepayers. He added that subordinate to that is management of the energy inputs and the potentially unfavorable results of rising fuel prices, and then the enhancement of LIPA's revenues and position, where achievable.

Deputy Chairman Foye asked whether Mr. Horowitz reports on a daily basis to Ms. McCarthy. Mr. Horowitz answered that he provides a daily hedging report.

Mr. Horowitz reported that the ERMC also determines the projected fuel consumption going forward three fiscal years. He indicated that LIPA utilizes a Web-based system designed by Pace Global Energy to monitor the markets and manage LIPA's hedging position. He continued that the ERMC developed and established exposure boundaries for oil and natural gas price impacts on customer bills.

Mr. Horowitz stated that the ERMC established several different hedging protocols. He indicated that the first protocol is programmatic hedging, which is mandated accumulation of hedging positions on the 18 through 36 month horizon market over a 6 month period to remove some of the volatility. He continued that the second protocol is defensive hedging that relates back to the exposure boundaries. He indicated that third is the transaction decision protocol, which is discretionary and seeks to take out some of the volatility on a forward basis when favorable.

Mr. Horowitz reported that LIPA is at a 75 percent annualized hedge level for the balance of the year, 65 percent for 2006 and 55 percent for 2007. He continued that the protocols move every day as prices move. He added that LIPA enters the market programmatically and defensively at a very measured pace.

Mr. Horowitz reported that the residual fuel oil market is an over-the-counter market, where trading occurs principal-to-principal. He continued that it is not an exchange trading commodity where there is anonymity. He indicated

that LIPA is careful not to enter into millions of barrels of hedges in a short time, which would push the market away from LIPA.

Deputy Chairman Steinberg stated that he is surprised that LIPA is such a sizable player into the market. Mr. Horowitz responded that LIPA is a sizable player in the Northeast.

Deputy Chairman Foye asked whether this is because LIPA is a small component of the global world market, but a large component of the New York market. Mr. Horowitz responded yes. He indicated that LIPA's hedging could range on an annualized basis from 9 to 14 million barrels of oil and 45 to 60 million dekatherms of gas. He added that the numbers are doubled when looking forward to hedge two years.

Mr. Horowitz reported that for the four months ended April 30, LIPA received approximately \$25.5 million in cash from hedging. He continued that the current value of LIPA's position is around \$71 million. He added that since LIPA started the program, LIPA has realized income of \$127.4 million and a downward impact on customers' bills of approximately 5.1 percent.

Chairman Kessel highlighted that the hedging program has enabled LIPA to hold down bills by approximately 5 percent, which is important. Deputy Chairman Steinberg stated that this is a big success point.

Chairman Kessel stated that this is an excellent presentation and it is important for the Board and public to know LIPA's financial operations. The Chairman commended Ms. McCarthy, Mr. Horowitz and the others who worked on this complicated program.

Chairman Kessel acknowledged Mr. Ralph Raghelli, President of the IBEW, and asked if he could offer some remarks.

Mr. Raghelli stated that the report given by Mr. Hulkower is incredible and tells a wonderful story. He further stated that he wants to make the Board aware of significant productivity improvements that helped in the success story, in addition to LIPA's investment in the reliability of the transmission and distribution system. He indicated that the IBEW put crews on straight time on Saturdays and Sundays, bifurcated its workforce to reduce the amount of cross-training, and also revamped job classifications to provide classifications with lower rates. He stated that as a result, the IBEW has contributed towards improving reliability and holding down costs.

Mr. Raghelli stated that the IBEW also works in partnership with LIPA to do community outreach during Electric Safety Week, and the children speak well of LIPA which is a reflection of what they are hearing at home.

Chairman Kessel thanked Mr. Raghelli for his comments.

**Upon motion duly made and seconded, the Board voted unanimously to adjourn the meeting at 12:45 PM.**

**Respectfully submitted,**

**Stanley B. Klimberg**