LONG ISLAND POWER AUTHORITY

MINUTES OF THE 138th MEETING

HELD ON NOVEMBER 29, 2001

Pursuant to notice dated November 23, 2001, the Long Island Power Authority (the “Authority") was convened for the one hundred and thirty-eighth time at 7:20 PM at Omni Teleconference Center in Uniondale, NY.

The following Trustees of the Authority were present:

Richard M. Kessel, Chairman
Patrick Foye, Deputy Chairman
Howard E. Steinberg, Deputy Chairman
Nancy A. Akeson
Thomas Doherty
Harriet Gilliam
James Hermann
Nancy Nugent
Vincent Polimeni
Jonathan Sinnreich

Also representing the Authority were Stanley Klimberg, General Counsel, Edward Grilli, Chief of Staff, Seth Hulkower, Chief Operating Officer, Edward Murphy, Jr., Chief Administrative Officer, Bert Cunningham, Vice President - Communications, Richard Bolbrock, Vice President - Power Markets, Christopher Furlong, Director of Customer Relations, 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. He welcomed Mr. James Hermann as a new LIPA Trustee, replacing former Trustee Michael Faltisheck.

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

Mr. Hulkower reported that LIPA is running well ahead of its projections and goals with regard to adding load and revenues. For 2001 LIPA expects to add approximately 38.7 megawatts of load against a goal of 32.5, and revenues of $16.1 million against a goal of $13.3 million. He pointed out that the biggest share of this growth is coming from the work of the major accounts organization, and he is very pleased with their results.

Mr. Hulkower stated that LIPA's Clean Energy Initiative is running close to target. He indicated that the annual energy savings goal is 44,503 megawatt hours for year-end, and that LIPA is very close to accomplishing that goal since the year-to-date energy savings is 44,176 megawatt hours.

Mr. Hulkower explained with regard to the Clean Energy Initiative, that some programs have been more successful than others. He noted that the

Lighting and Appliances program has been successful, but the Commercial Construction program is running behind. He pointed out that LIPA has approximately the same number of participants as expected in the Commercial Construction program, but they are not yielding as many megawatt hours as hoped. He indicated that LIPA will look into this matter.

Mr. Hulkower stated that LIPA is showing a marked increase in its accounts receivable, and LIPA is reducing the backlog that accumulated after collections were suspended for an approximate two-week period after September 11. He indicated that LIPA expects to be caught up by the first quarter of next year. Deputy Chairman Foye asked how this compares to KeySpan's experience on the gas side. Mr. Hulkower answered that LIPA's experience is directly parallel, and of a comparable percentage, since LIPA and KeySpan conduct the collections together and divide the receipts. Deputy Chairman Foye asked if gas and electric collections were suspended for the same period, and Mr. Hulkower responded yes.

Mr. Hulkower pointed out that LIPA still leads the State with respect to its reliability statistics, and there has been no change.

Chairman Kessel requested that LIPA's Controller, Kenneth Kane, present the Financial Report. With reference to the income statement, Mr. Kane reported that for the ten-month period ended October 31, 2001, LIPA has generated an excess of revenues over expenses amounting $63 million, as compared to a

budgeted amount of $164 million. He stated that the primary driver behind that difference was a change in the way LIPA reflects recovery of fuel costs that were deferred during 2000. He explained that the budget reflected a one hundred percent recovery of the cost, whereas LIPA is currently recovering only about forty percent through the 5.8 percent fuel surcharge. Mr. Kane pointed out that the Board, subsequent to the issuance of the budget, approved the 5.8 percent surcharge, and the budget numbers were not updated to reflect that event. He indicated that the revenue line shows a decrease of $112 million. He stated that LIPA would recognize revenue at an amount about equal to that recovered for the fuel costs, or approximately $96 million for the ten-month period ended October 2001. The remainder of the difference is the result of higher than budgeted Long Island Choice sales with a corresponding absence of a revenue component for fuel costs.

Mr. Kane highlighted that a significant item on the income statement is Fuel and Purchased Power expense, which was $21 million under budget. He noted that Long Island Choice sales contributed $18 million to this variance since LIPA did not incur fuel costs for those sales. He explained that since Long Island Choice customers choose to receive their energy from other providers, LIPA recovers transmission and distribution costs, not fuel costs, from those customers.

Mr. Kane further remarked with respect to Fuel and Purchased Power expense that LIPA has experienced costs higher than the budgeted $199 million,

$107 million of which has been deferred in accordance with LIPA's Fuel and Purchased Power Cost Adjustment (FPPCA) mechanism, leaving a net pricing variance of $92 million. He indicated that after adding the aforementioned $18 million contribution, the net variance is $74 million. He reported that $96 million was not recovered because it was written off at year-end 2000, in accordance with the Board's decision partially waiving the FPPCA mechanism.

Mr. Kane reported that the balance sheet shows no significant changes. He emphasized that LIPA's cash position is strong, noting there is $250 million in LIPA's Rate Stabilization Fund, leaving an unrestricted cash balance of $399 million as of November 16, 2001.

Chairman Kessel pointed out that while LIPA has over $700 million in cash, much of that amount is tied up in LIPA's Rate Stabilization Fund or the Shoreham credits. Chairman Kessel further emphasized that while LIPA is in a strong cash position, there are tremendous financial pressures to be faced.

Chairman Kessel clarified the issue of the fuel surcharge. He observed that LIPA's tariff requires an annual review of LIPA's fuel costs for the prior year, and that an adjustment be made to electric bills to recover those costs exceeding a baseline amount. He indicated that for the year 2000, LIPA's fuel costs exceeded the baseline by about $307 million. He stated that earlier this year LIPA held public hearings on a proposal that would effectively have LIPA absorb approximately sixty percent of the unrecovered year 2000 fuel costs with

approximately forty percent of the costs, or $126 million, being passed on to the customers.

Chairman Kessel reminded those present that if LIPA had followed its own rules and passed on one hundred percent of the unrecovered fuel costs, this would have resulted in a thirteen percent surcharge to the customers, and an increase in the average residential electric bill by more than eleven dollars per month. He stated that LIPA made a determination that Long Island and its economy would have been harmed by such an increase. He observed that LIPA decided to mitigate the surcharge by limiting it to 5.8 percent, or an approximate four-dollar per month increase in the average residential bill. The Chairman affirmed that the surcharge, which again corresponds to fuel costs for the year 2000, will remain in effect through February. He reemphasized that LIPA has undercollected and undercharged its customers by sixty percent, unlike almost every other utility across the country that charges customers dollar-for-dollar for higher fuel costs.

Chairman Kessel recounted that LIPA decided when it acquired LILCO to have a policy to assess fuel costs on a yearly basis, and to even out any recovery to avoid radical changes or "spiking" of customers' bills that could have been in excess of forty percent.

Chairman Kessel stated that LIPA's fuel costs this year will be significantly over budget, and have increased for most of this year. He noted that fuel costs

have begun to decrease towards the end of the year. The Chairman emphasized that LIPA is taking a hard look at its fuel costs, and that he has requested staff to accelerate the review and formulate strategies regarding LIPA's recovery of fuel costs for Board consideration in January or February of 2002.

Chairman Kessel stated that the Suffolk County Legislature has introduced and may have passed legislation calling for LIPA to repeal the fuel surcharge. He noted that such legislation is erroneous in assuming that the surcharge is based upon the fuel costs for 2001, since the surcharge is partially recovering costs incurred in 2000. He indicated that to date LIPA has recovered $83-84 million of the fuel costs for 2000, and that by March of 2002, approximately $126 million will have been recovered.

Chairman Kessel reiterated that in order to help the Long Island economy, LIPA has taken the unique approach among utilities by undercharging its customers. The Chairman recommended that the Suffolk County Legislature repeal its own surcharge imposed on LIPA electric customers in that County, which surcharge was recently passed without a public hearing. He observed that the Legislature passed that surcharge to plug a budget hole. He noted that surcharge is in the amount of one and one-half percent imposed on LIPA's customers as of March 2002, which will raise electric bills for the average customer by more than one dollar per month or approximately eighteen dollars per year. The Chairman stated it is incredible for the Suffolk County Legislature to call upon LIPA to repeal the surcharge for fuel costs for 2000, while

inappropriately imposing on LIPA customers a surcharge having nothing to do with electricity.

Chairman Kessel reported that he communicated with Suffolk County Executive Robert Gaffney and Presiding Officer Paul Tonna since the Board's last meeting. The Chairman stated that Mr. Gaffney has done an outstanding job dealing with severe budget problems in Suffolk County. However, the Chairman indicated he strongly disagrees with an approach that solves Suffolk County's budget problems on the backs of LIPA's ratepayers. He noted the possibilities that the surcharge may be increased by the Legislature if finances do not improve, and that other municipalities may also impose surcharges unrelated to electric costs. He indicated his hope that the Suffolk County Legislature will consider rescinding its surcharge. The Chairman indicated that he intends to attend a meeting of the Finance Committee of the Suffolk County Legislature scheduled for January.

Deputy Chairman Foye inquired whether the Suffolk County surcharge will be separately delineated on the LIPA bill. Chairman Kessel indicated that he has asked LIPA staff to look into this matter. The Chairman emphasized that it should, if allowable, be a separate line item in the bill.

Chairman Kessel stated that LIPA is in the final stages of the preparation of the budget for next year, and thanked the Finance Committee and the Board for their diligent work on the preparation of the budget. The Chairman stated that

while LIPA faces tremendous financial pressures, LIPA intends to fulfill its commitment to keep its electric rates frozen for five years. To accomplish this, the Chairman noted, LIPA must develop a stringent budget with cuts in a number of sensitive areas, and a current draft budget showing a deficit of $27 million must be revised to eliminate that deficit. He indicated that the budget to be presented to the Board for adoption at the next meeting will show a slight positive balance.

Chairman Kessel stated that the budget not only includes an operating budget for 2002, but a capital budget for 2002 and 2003. He noted that capital projects, while not operating expense items, must be paid for over time. He indicated that a significant portion of the capital costs for 2002 are interconnection costs related to the fast track power projects. He noted that more than $200 million of LIPA's capital budget for the next year will be spent on non-fast track projects, such as for the maintenance and upgrade of LIPA's T & D system, replacement of transformers and aggressive tree trimming.

Chairman Kessel indicated he has already advised the senior staff that the economy has worsened, and while it may not have as significant an impact on Long Island as other areas in the region, LIPA must be prepared for the worst. The Chairman identified two sources of tremendous financial pressure upon LIPA, the first being higher fuel costs. The Chairman advised that the 2002 budget numbers are based upon projections of increased fuel costs next year, especially for oil. The Chairman stated that the second pressure comes from the significant

costs associated with the necessary construction of a number of small generating plants on Long island to satisfy LIPA's resource needs, which costs include interconnection costs and the costs of purchased power from the plants.

Chairman Kessel reiterated that LIPA will make sacrifices to fulfill its obligation to meet the customers' expanding needs without raising rates, and unpopular decisions must be made. For example, the Chairman indicated that LIPA will not be able to increase its spending on clean energy next year by as much as he had hoped.

Chairman Kessel thanked Mr. Horowitz for his adept handling of "hedging" projects, which has helped the budget. Chairman Kessel noted he has requested that LIPA's department heads present ways to make additional cuts, large and small, to prepare for the worst next year. He indicated that as of January of 2002, the financial staff, led by Ms. Taylor, will track monthly expenditures in each department, so that no department will spend more than budgeted. He stated that the department heads will be responsible to keep spending within their budgets, and LIPA will stringently enforce this.

Chairman Kessel noted that LIPA's cash is restricted by requirements pertaining to, among other things, its bonds and Rate Stabilization Fund. Trustee Doherty observed that in the months of November and December of this year, LIPA will pay approximately $150 million for debt service. The Chairman

reemphasized that although the budget will be tight for next year, LIPA will live up to the Governor's and LIPA's commitments to freeze rates for a full five years, and expenses will have to be cut to fulfill the commitments to the public.

Chairman Kessel stated that he expects the final budget to be ready within ten days. He indicated copies will be provided to the Trustees, and the budget will be made public. He stated that, although not required, a public hearing on the budget will be held and public comment will be heard. He noted again that the budget will be discussed and presented for action at the next Board meeting on December 18, 2001.

Chairman Kessel commended Mr. Feldman, Ms. Taylor, Mr. Kane and the entire financial staff who worked non-stop over the last few weeks to assemble the budget. The Chairman further thanked the LIPA staff for cooperating by cutting budgets an additional fifteen percent after making initial cuts. He stressed the need for the public and customers to understand that LIPA is not immune from this difficult economy, which may not be apparent because LIPA has not raised rates, and LIPA has mitigated fuel costs.

Chairman Kessel indicated that LIPA's reliability is first in the State because of the terrific job of LIPA's employees and LIPA's significant expenditures on capital improvements. He credited the LIPA staff for paring down by more than $100 million the KeySpan proposed capital budget for LIPA. In sum,

he observed, LIPA seeks to maintain the programs that keep the system reliable, while ensuring cost efficiency.

Chairman Kessel indicated that the next item on the agenda is approval of the minutes of the November 13 Board meeting.

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

570. APPROVAL OF MINUTES AND RATIFICATION OF ACTIONS TAKEN AT THE NOVEMBER 13, 2001 SPECIAL MEETING OF THE BOARD OF TRUSTEES OF THE LONG ISLAND POWER AUTHORITY

RESOLVED, that the Minutes of the meeting of the Authority held on November 13, 2001, 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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As the next agenda item, Chairman Kessel asked the Board to approve a resolution authorizing the Chairman to engage Ruskin, Moscou, Evans & Faltischek, P.C., to provide legal services to LIPA. The Chairman stated that Mr. Kremer, one of the Authority's principal outside counsel, recently moved from Rivkin, Radler & Kremer, a law firm under contract with the Authority, to the firm of Ruskin, Moscou, Evans & Faltischek, P.C. The Chairman noted that Mr. Kremer has represented the Authority for many years, primarily in important and complex litigation matters, and that Mr. Kremer has substantial and unique expertise that

cannot be duplicated by another attorney. Chairman Kessel indicated that Mr. Kremer currently represents the Authority in a pending lawsuit on appeal involving Shoreham (<u>Town of Islip, et al. v. Long Island Power Authority</u>). The Chairman noted that the case has tremendous significance for LIPA and Suffolk County, and that it is necessary to engage Mr. Kremer's new firm in order to continue to utilize his valuable services.

Deputy Chairman Steinberg inquired as to whether the transfer of that case between firms would result in additional cost. Mr. Klimberg responded that while both firms would be retained to continue representation of LIPA, the same individuals would continue their work on the case, i.e., Mr. Kremer at Ruskin, Moscou, Evans & Faltischeck, P.C., and Mr. Krinick at Rivkin Radler. Mr. Klimberg indicated that Mr. Krinick will work with Mr. Kremer as he has done in connection with the prior litigation at Rivkin Radler. Deputy Chairman Steinberg requested that close attention be paid so that there is no duplication of legal bills, and Mr. Klimberg concurred.

Deputy Chairman Foye noted that Mr. Michael Faltischek, a former member of the Board, is a partner in the firm of Ruskin, Moscou, Evans & Faltischek. Deputy Chairman Foye complimented Mr. Kremer on the work that he has done for the Authority. Chairman Kessel remarked that an unfavorable decision in the <u>Islip</u> litigation currently on appeal would require Suffolk County and Brookhaven Town to forward almost $1.5 billion to LIPA. He stressed the importance of

maintaining the team that has represented LIPA to prevent a devastating effect on Suffolk County, Brookhaven Town and the Shoreham School District.

Upon motion duly made and seconded, the following resolution was approved, with Trustee Sinnreich abstaining:

571. ENGAGEMENT OF LAW FIRM

RESOLVED, that the Chairman be, and hereby is, authorized to engage Ruskin, Moscou, Evans & Faltischek, P.C. to provide legal services to the Authority and LIPA, effective July 16, 2001.

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Turning to the next agenda item, Chairman Kessel requested the Trustees to approve a resolution authorizing the Chairman to engage the Bank of New York to provide cash management and advisory services to LIPA to assist with the investment of the Nuclear Decommissioning Trust Funds with respect to LIPA's interest in the Nine Mile Two plant. He stated that in October 2001 the Authority issued a request for proposals for such services, drawing responses from six firms. The Chairman indicated that The Bank of New York was determined to be best suited to fulfill LIPA's needs.

Deputy Chairman Foye asked whether LIPA's share of the Nuclear Decommissioning Trust Funds is held directly by LIPA or through the joint

ownership of the Nine Mile Two plant. Mr. Hulkower indicated that it is held directly by LIPA, and he confirmed that a separate financial advisory consultant is needed by LIPA.

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

572. ENGAGEMENT OF CASH MANAGEMENT CONSULTANT

RESOLVED, that the Chairman be, and hereby is, authorized to engage The Bank of New York as Nuclear Decommissioning Trust Funds Cash Management and Advisory Consultant to The Long Island Power Authority.

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Finally, Chairman Kessel indicated that, as he mentioned at the last Board meeting, it is recommended that Ms. Kathleen Stella be appointed to be the new Secretary to the Board, effective November 8, 2001. The Chairman thanked Ms. Stella for the terrific job she has done for LIPA, most recently as the administrative assistant to Mr. Germano. The Chairman stressed the importance of promoting from within LIPA based upon merit. He stated that he wishes the former Secretary to the Board, Ms. Fama, luck in her new position at NASDAQ. Chairman Kessel also thanked LIPA's first Secretary to the Board, Ms. Leat, for the great job she did for LIPA, and for her valuable assistance during the transition. He also thanked Mr. Zarb, the former Chairman of LIPA, for his continued assistance and advice.

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

<u>573. APPOINTMENT TO OFFICE OF SECRETARY</u>

RESOLVED, that Kathleen Stella be, and hereby is, appointed to the Office of Secretary to the Long Island Power Authority ("Authority") Board of Trustees, effective November 8, 2001, until the earlier of her resignation or removal; and be it further

RESOLVED, that the incumbent of the Office of Secretary to the Authority Board of Trustees shall be an officer of the Authority within the meaning of the Authority's enabling legislation (Chapter 517 of the Laws of 1986), as amended, including Section 1020-bb of the Public Authorities Law, and all other applicable laws.

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Chairman Kessel entertained a motion to adjourn. Upon motion duly made and seconded, the Board voted unanimously to adjourn the meeting at 8:20 PM.

Respectfully submitted,

Stanley B. Klimberg