

**LONG ISLAND POWER AUTHORITY
MINUTES OF THE 150th MEETING
HELD ON DECEMBER 20, 2002**

Pursuant to notice dated December 13, 2002, the Long Island Power Authority (the "Authority") was convened for the one hundred and fiftieth time at 10:15 AM at the Omni Teleconference Center in Uniondale, NY.

The following Trustees of the Authority were present:

**Richard M. Kessel, Chairman
Howard Steinberg, Deputy Chairman
Michael Affrunti
Nancy A. Akeson
Harvey Auerbach
Thomas A. Doherty
James Herrmann
Vincent Polimeni
Jonathan Sinnreich**

Also representing the Authority were Stanley Klimberg, General Counsel, Edward Grilli, Chief of Staff, Seth Hulkower, Chief Operating Officer, Anastasia Song, Acting Chief Financial Officer, Richard Bolbrock, Vice President – Power Markets, Christopher Furlong, Director of Customer Relations, Bert Cunningham, Vice President - Communications, Bruce Germano, Vice President – Retail

Services, Edward P. Murphy, Jr., Chief Administrative Officer, 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 stated with regret that Thomas Doherty is leaving the Board, and this will be his last meeting. The Chairman noted that Trustee Doherty is a friend, a terrific person and a valuable resource for LIPA who has led it through some difficult times. The Chairman stated that he wishes Trustee Doherty had been with LIPA since 1987, as LIPA could have benefited then from his wise advice. Chairman Kessel congratulated Trustee Doherty and wished him well.

Trustee Doherty stated that his more than seven years on the Board have been an honor and a rewarding experience. He added that when he first joined the Board there were many questions concerning LIPA's future, including whether to acquire more than \$7 billion in assets and liabilities, and this acquisition was accomplished with great professionalism and integrity. He noted that LIPA has delivered on the Governor's promise to provide a 20 percent rate reduction, and LIPA saved the ratepayers more than a quarter billion dollars, while running a sound financial entity with positive cash flow.

Trustee Doherty indicated that the electric system's reliability has been enhanced due to the commitment of the Board to capital improvements for new

generating plants and improvements of the transmission and distribution facilities. He stated that LIPA can take a great deal of pride in where it stands today, and he wishes everyone continued success.

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

619. APPOINTMENT OF ACTING DEPUTY CHAIRMAN FOR THE DECEMBER 20, 2002 MEETING OF THE BOARD OF TRUSTEES OF THE LONG ISLAND POWER AUTHORITY

RESOLVED, that Trustee Thomas A. Doherty is appointed as the Acting Deputy Chairman for the Long Island Power Authority Board of Trustees for its meeting of December 20, 2002.

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Chairman Kessel stated that the first item on the agenda is approval of the minutes of the November 25 Board meeting. Upon motion duly made and seconded, the following resolution was approved unanimously:

620. APPROVAL OF MINUTES AND RATIFICATION OF ACTIONS TAKEN AT THE NOVEMBER 25, 2002 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 25, 2002, 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.

* * *

Chairman Kessel stated that the next item on the agenda is Board consideration of a resolution for LIPA to take all appropriate actions to track and recover from KeySpan the costs to LIPA arising from KeySpan's overstatement of LIPA's revenues. The Chairman indicated that LIPA has several operating agreements with affiliates of KeySpan Corporation, pursuant to which KeySpan is to provide LIPA with accurate and timely financial information. He continued that KeySpan recently admitted, after LIPA repeatedly expressed concerns, that one of its affiliates, among other errors, had consistently "double counted" certain components of LIPA's electric service revenues, which resulted in the overstatement of LIPA's revenues by approximately \$60 million for the period of January 1, 2002 through September 30, 2002 and by \$700,000 for the year 2001.

Chairman Kessel stated that as a result of KeySpan's errors, LIPA has had to undertake the following actions: launched an independent review by LIPA's external auditor, PricewaterhouseCoopers; retained the specialized firm of Virchow Krause & Co., LLP to augment the audit with a broader review of KeySpan's controls, contract management and reporting systems as they affect the quality of information reported to LIPA; directed KeySpan's internal auditing department to conduct a full review of the matter; began a full review of all of the KeySpan/LIPA contracts; and suspended the closing of LIPA's financial books.

Chairman Kessel stated that KeySpan has indicated its general agreement to reimburse LIPA for the costs due to KeySpan's errors. He indicated that KeySpan should be accountable for all costs and effects borne by LIPA arising from KeySpan's errors. The Chairman continued that he recommends that LIPA

take all necessary actions to track, identify and recover from KeySpan any and all direct and indirect costs, including any increased costs of financing or other adverse effects, arising from KeySpan's errors.

Ms. Song stated that two separate audits were launched in connection with the revenue misstatement and the results are expected by mid-January. She continued that LIPA will notify the appropriate entities of the results. She added that LIPA has not closed its books since September, pending review and correction after intensive analysis by the financial staff in January.

Ms. Song stated that KeySpan's errors are grievous, have significantly harmed LIPA's credibility in the financial community and put LIPA in very difficult financial straits. She indicated that despite the errors, LIPA hopes to show positive net income for 2002, due largely to the fact that LIPA was suspicious of KeySpan's figures and its repeated denials and LIPA husbanded its financial resources so that it would not end the year in the red. She added that LIPA's cash position is strong and LIPA has worked diligently with the rating agencies, which take the matter seriously.

Ms. Song explained that the proposed resolution would allow LIPA to segregate and have KeySpan pay for all of the direct and indirect costs, including the costs for the diversion of LIPA's staff from its day-to-day operations and costs associated with higher financing costs. She stated that she supports the proposed resolution, and she noted that the Board will have to look at options in

the spring after the audits of the errors and the broader audit of KeySpan's operations are completed.

Deputy Chairman Steinberg stated that it is clear KeySpan is in material breach and may have caused irreparable harm to LIPA. He continued that he hopes it is clear that LIPA is authorized to take any means necessary in order to protect its financial condition, including preemptive actions such as litigation, if necessary.

Chairman Kessel stated that LIPA is not waiting until the spring to move ahead. The Chairman continued that teams are looking into all aspects of the matter, including legal issues regarding the errors, and all other options, such as changing or canceling contracts. He indicated that LIPA would begin the process of segregating the costs to be paid by KeySpan.

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

621. RESOLUTION REGARDING TRACKING AND RECOVERY OF COSTS TO LIPA IN CONNECTION WITH KEYSpan'S OVERSTATEMENT OF LIPA REVENUES

WHEREAS, pursuant to its operating agreements with affiliates of KeySpan Corporation ("KeySpan"), including the Management Services Agreement under which KeySpan Electric Services LLC provides day-to-day management of LIPA's electric transmission and distribution system, and the Energy Management Agreement under which KeySpan Energy Trading Services LLC purchases fuel used at KeySpan Generation LLC's on-Island power plants to generate electricity for LIPA and purchases and sells capacity and energy, which services under these agreements are on LIPA's behalf and subject to LIPA's supervision and

policy direction, LIPA relies on KeySpan to provide accurate and timely financial information that is reflected in LIPA's reported financial statements; and

WHEREAS, KeySpan has admitted that one of its affiliates, among other errors, had consistently "double count[ed]" certain components of LIPA's electric service revenues that it reported to LIPA, and that such errors resulted in the overstatement of LIPA's revenues, although such admission occurred only after LIPA repeatedly expressed concerns to KeySpan regarding the accuracy of the LIPA revenue figures that KeySpan provided to LIPA; and

WHEREAS, KeySpan has informed LIPA that, based upon an extensive internal review completed by its management, as well as reviews completed by both its internal audit department and its external auditors, KeySpan has concluded that as a result of its errors, KeySpan has overstated LIPA's revenues by approximately \$60 million for the period January 1 through September 30, 2002 and by \$700,000 for the year 2001; and

WHEREAS, as a result of KeySpan's admitted errors, LIPA has had to undertake the following actions, among others: launched an independent review of this matter by LIPA's external auditor, PricewaterhouseCoopers; retained another specialized professional firm, Virchow Krause & Co., LLP, to augment this auditing effort with a broader review of KeySpan's controls and contract management and reporting systems as they affect the quality of information reported to LIPA; directed KeySpan's internal auditing department to conduct a full review of the matter and report its findings to LIPA; began a full review of all KeySpan/LIPA contracts; and suspended the closing of LIPA's financial books until the above audit matters are closed to LIPA's satisfaction; and

WHEREAS, LIPA intends to complete its investigation as soon as possible and then to consult with PricewaterhouseCoopers and Virchow Krause & Co., LLP to evaluate the results of these inquiries and to assess the potential impact of KeySpan's errors on LIPA; and

WHEREAS, on December 11, 2002, Standard & Poor's Rating Services placed its ratings on LIPA's debt on "Credit Watch negative" based on "concerns that LIPA's financial performance could be impaired as a result of KeySpan Corp.'s ... overstatement of LIPA's revenues for 2002"; and

WHEREAS, KeySpan has recognized that LIPA has incurred and will incur costs due to KeySpan's errors in overstating LIPA's revenues, and KeySpan has indicated its general agreement to reimburse LIPA for such costs; and

WHEREAS, LIPA intends to hold KeySpan accountable for any and all costs, both direct or indirect, and internal or external to LIPA, including any increased costs of financing, and any other adverse effects borne by LIPA, arising from KeySpan's errors in overstating LIPA's revenues;

NOW, THEREFORE, BE IT RESOLVED, that LIPA shall take all actions necessary or appropriate to track, identify and obtain recovery from KeySpan of any and all costs, both direct or indirect, and internal or external to LIPA, including any increased costs of financing, and any other adverse effects borne by LIPA, arising from KeySpan's errors in overstating LIPA's revenues; and be it further

RESOLVED, that the Chairman and/or his designees are authorized to perform such further acts and deeds as may be necessary, convenient or appropriate, in their judgment, to carry out the foregoing resolutions.

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Chairman Kessel stated that the next item on the agenda is Board consideration of a resolution authorizing the Chairman or his designees to execute and effect a lease and related agreements to facilitate the development of a second generating facility in the Village of Freeport pursuant to prior Board resolutions. The Chairman continued that LIPA has engaged in discussions and negotiations with the Village of Freeport regarding the construction of two 45 MW gas-fired units, one to be developed and owned by Freeport and the other by a developer to be selected by Freeport. He indicated that pursuant to prior Board resolutions, it is appropriate for LIPA to lease property from Freeport for the second unit, and enter into related agreements with Freeport, including with respect to the selection of another developer for installation of new generation to replace the unit that was to be developed by PPL Global, and LIPA is hopeful that the units will be available for next summer.

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

**622. AUTHORIZATION FOR ENTRY INTO LEASE AND RELATED AGREEMENTS
IN CONNECTION WITH FREEPORT ENERGY PROJECT**

RESOLVED, that for the reasons set forth in the accompanying Memorandum, the Chairman or his designees be and hereby are authorized to execute and effect a lease and other related agreements and arrangements, and to perform such further acts and deeds as may be necessary, convenient, or appropriate, in the judgment of the Chairman or his designees, to facilitate development of new, gas-fired generation to be installed by a developer, to be selected by LIPA, in lieu of a second unit at the Freeport energy project site that was to be developed and owned by PPL Global but from which project PPL Global has withdrawn; and be it further

RESOLVED, that all actions taken by the Chairman and/or his designees with respect to the project referred to in the preceding resolutions are hereby in all respects ratified and approved.

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Chairman Kessel stated that the next item on the agenda is Board consideration of a resolution authorizing the Chairman to engage Farrell Fritz, P.C. to provide legal services to the Authority and LIPA. The Chairman indicated that Lazer, Aptheker, Feldman, Rosella & Yedid, P.C. has represented the Authority and LIPA in important and complex real estate matters, including those in connection with LIPA's fast track power projects. He further indicated that Mr. Lawrence Feldman, who had been the partner in charge of these matters, has recently moved to Farrell Fritz. The Chairman continued that Mr. Feldman has substantial experience that will be needed in the future and cannot easily be duplicated, and therefore Farrell Fritz should be engaged. He added that LIPA will continue to use the excellent services of the Lazer, Aptheker firm as needed.

Trustee Sinnreich stated that he is well acquainted with Mr. Feldman and the Lazer, Aptheker firm, and they are all first rate lawyers who will serve the Authority and LIPA well.

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

623. ENGAGEMENT OF LAW FIRM

RESOLVED, that the Chairman be, and hereby is, authorized to engage Farrell Fritz, P.C. to provide legal services to the Authority and LIPA.

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Chairman Kessel stated that LIPA normally tries to release its budget as early as possible in December, but due to the KeySpan errors the budget has been delayed. The Chairman continued that it would be inappropriate to vote today on the proposed 2003 operating budget and 2003-04 capital budgets, since they are just now being released for the Board's and public's review. He continued that a budget hearing will be held on January 15, 2003, and there will be opportunities for Board members to raise questions and to make amendments.

Chairman Kessel commended LIPA's staff and budget team led by Ms. Song and Mr. Feldman for their work to develop LIPA's budgets. The Chairman indicated that the budgets were prepared under very difficult circumstances,

including the KeySpan errors which affected LIPA's expected net income and created concerns in the financial community.

Chairman Kessel stated that the budget is strong under the circumstances and does two important things, namely, it protects LIPA's ratepayers and the Long Island economy by avoiding a full pass-through of excess fuel and purchased power costs, and it meets the needs of the financial community to ensure LIPA's financial strength. He indicated that the total budgeted operating expenses are \$2.546 billion and operating revenues are \$2.566 billion, a revenue increase of approximately 5.9 percent. He further indicated that this budget projects a positive net income balance of \$20 million, which LIPA will now dedicate itself to reach each year.

Chairman Kessel indicated that the capital budgets are \$252 million for 2003 and \$239.6 million for 2004, which represent a decrease from the 2002 capital budget due largely to the \$331 million cost of the ten fast track units for 2002. He stated that LIPA will continue to invest significant amounts to improve the reliability of the electric system on Long Island, which has improved significantly compared to the former LILCO. He noted that even the lower numbers for 2003 and 2004 are about twice the original projections.

Chairman Kessel stated that he recommends that LIPA's base rates be frozen for another year, and that about 3 percent be added to the current 5.8 percent fuel surcharge. He continued that the surcharge amount is driven not just by higher oil and natural gas prices, but also by the need to increase the

infrastructure on Long Island for power purchases in order to meet the growing demand. He stated that the ten fast track units built last summer kept the lights on in 2002, and LIPA will continue to introduce some similar projects for 2003 on a smaller scale. He indicated that there is every reason to believe that peak growth in 2003 could equal that of last summer, which was 150 MW.

Chairman Kessel reiterated that the proposed fuel surcharge increase does not impact base rates, and he noted that the approximate 3 percent increase for this year will amount to about \$2.80 per month for the average residential customer. He indicated that he regrets the need to increase the surcharge, but LIPA cannot afford to put its financial integrity into jeopardy, as in the case of Nassau County. He further indicated that an increase of about 12 percent in the surcharge, equating to about \$11.20 per month for the average residential customer, would result if LIPA were to pass through all of its excess fuel costs, but LIPA has chosen to continue to absorb a portion of those costs to protect its customers and Long Island's economy. He indicated that the cost of fuel and purchased power for 2003 is projected to be \$1.109 billion, an approximate 8.8 percent increase from 2001.

Chairman Kessel stated that electric sales are projected to increase by approximately 304,500 megawatt hours, a 1.6 percent increase from the 2002 budgeted level and 2.1 percent more than the 2002 projected normalized level. The Chairman continued that commercial and industrial sales are projected to grow by 1.8 percent, and residential sales are projected to grow by 1.4 percent.

Chairman Kessel indicated that LIPA will spend \$34 million on its Clean Energy Program, including conservation and alternative technology programs. The Chairman stated that Governor Pataki deserves tremendous credit for putting LIPA on the right course in 1998 by having LIPA set aside \$170 million for the Clean Energy Program, which is working very well.

Chairman Kessel stated that the Clean Energy Program alone does not remove the need for more on-Island generation. He also noted that LIPA faces continuing opposition from Connecticut to the operation of the Cross-Sound Cable, and that Northeast Utilities is making it difficult to repair the NUSCO cable that failed after an anchor dragging incident. The Chairman emphasized that additional on-Island generation will be critical if the Cross-Sound Cable is not operational.

Chairman Kessel indicated that the budget also recognizes that LIPA needs to change the operation of its fuel adjustment clause, which involves a one year lag in LIPA's recovery of costs incurred for fuel and purchased power. He stated that public hearings will be held in February 2003 concerning LIPA's proposal to increase the fuel surcharge and to start recovering excess fuel costs in the same year as they are incurred, while continuing to absorb some of those costs. He stated that a real time fuel adjustment will make LIPA a much stronger financial entity.

Chairman Kessel thanked Trustee Polimeni who raised the matter of real time fuel cost recovery several years ago. The Chairman also thanked Ms. Song,

Mr. Feldman and others who have worked on the proposed tariff revisions for the fuel adjustment clause.

Chairman Kessel stated that LIPA should be proud of its strong financial position in the face of absorbing fuel costs and limiting increases in the fuel surcharge. He indicated that the \$2.80 per month increase hardly compares to the tax increases in both Nassau and Suffolk Counties, and LIPA continues to perform excellently.

Mr. Feldman stated that LIPA will hold workshops for the Trustees in January to explain the budget and fuel surcharge proposals. He thanked the budget and financial staffs for their efforts in preparing the budgets.

Trustee Sinnreich stated that the proposed budget contains \$20 million in non-cost performance incentive payments to KeySpan, and KeySpan's poor performance in connection with its financial reporting should be considered when LIPA decides, to the extent allowable, whether or not to reduce or withhold performance incentive payments to KeySpan. Chairman Kessel indicated that LIPA is currently withholding some money from KeySpan.

Trustee Sinnreich indicated that Northeast Utilities' treatment of LIPA in connection with the NUSCO cable will be remembered in the context of future proposals by that company to do work for LIPA. Chairman Kessel indicated that the cable is important for Long Island's reliability, but it is far more important for reliability in Southwestern Connecticut, where there are significant transmission

limitations which may have led to blackouts had it not been for LIPA exporting power over the cable. The Chairman stated that he will advise Northeast Utilities in writing of the importance of the cable.

Chairman Kessel stated that the next item on the agenda is the Operations Report, to be delivered by Mr. Hulkower. Mr. Hulkower reported that LIPA is promoting Internet self-service options for its customers, which can be accessed via the LIPA website. He indicated that LIPA customers may access information concerning LIPA programs that they are enrolled in as well as programs they can enroll in.

Mr. Hulkower indicated that a customer may immediately access a great deal of information and services via the on-line services, including billing and payment history, on-line payment, direct debits, account history, usage information, on-line meter reading services and the balanced billing option. He further indicated that LIPA's longer term objective is to move to a paperless billing system, which would save approximately seventy-five cents per bill. He added that LIPA mails out more than 850,000 bills per month, for which a savings will add up quickly. He stated that the program is in its infancy, but there are 18,000 customers already in the process of registering via the website.

Chairman Kessel stated that LIPA recently announced that in January, LIPA will begin to separate its electric bills from KeySpan gas bills. He noted that the gas portion of the bill is typically double the electric portion on a twelve month basis, and LIPA's uncollectibles may be reduced as a result.

Chairman Kessel stated that bills are to be separated because people need to know what they are paying for each commodity, which will help customers better manage their electric usage and avoid confusion.

Deputy Chairman Steinberg stated that LIPA should encourage greater use by customers of the on-line capabilities, including passing through savings to customers as an incentive. He asked whether LIPA has ensured that proper security systems are in place. Mr. Hulkower responded that part of the delay in introducing the program was due to LIPA making sure that the security system is in order, and LIPA is currently deciding how to entice customers to use the program.

Trustee Akeson asked whether LIPA will split the gas and electric bills in terms of envelopes. Chairman Kessel answered that two separate bills will be sent in separate postage paid return envelopes. He added that there is no better consumer education program for energy conservation than to split the bills.

Chairman Kessel stated that Mr. Furlong, who is the head of LIPA's customer service department and has worked for the State for 37 years, mostly with the Public Service Commission, will be retiring. The Chairman continued that Mr. Furlong was originally loaned to LIPA from the PSC for a year and is still with LIPA five years later. He stated that Mr. Furlong is a qualified and capable person in the area of customer service and customer relations, and is a valuable asset to LIPA who will be missed.

Chairman Kessel stated that he wished to offer a resolution on behalf of the LIPA staff and Board commending Mr. Furlong for his extraordinary service to LIPA, and his helping to build what is today a very successful customer relations department.

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

624. RESOLUTION COMMENDING MR. CHRISTOPHER FURLONG

RESOLVED, that the Long Island Power Authority commends Mr. Christopher Furlong for his outstanding service to LIPA and his helping to build a very successful Customer Relations Department at LIPA.

* * *

Mr. Furlong stated that it has been a pleasure to work with the Chairman, the staff and the Board, and he has enjoyed every minute of it.

Chairman Kessel entertained a motion to go into executive session to discuss litigation and personnel issues.

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

625. EXECUTIVE SESSION - PURSUANT TO SECTION 105 OF THE PUBLIC OFFICERS LAW

RESOLVED, that pursuant to Section 105 of the Public Officers Law, the Trustees of the Long Island Power Authority shall convene in Executive Session for the purpose of discussing litigation and personnel matters.

* * *

At 11:27 AM the open session of the Board of Trustees was temporarily adjourned and an executive session of the Board of Trustees was convened.

At 12:10 PM the executive session was adjourned and the open session was reconvened.

After noting that no votes were taken in the executive session, Chairman Kessel entertained a motion to adjourn. Upon motion duly made and seconded, the Board voted unanimously to adjourn the meeting at 12:14 PM.

Respectfully submitted,

Stanley B. Klimberg