NEW ISSUE—Full-Book-Entry

In the opinion of Bond Counsel to LIPA, under existing statutes and court decisions, and assuming compliance with the tax covenants referred to herein, interest on the Tax-Exempt Offered Securities is not included in gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and such interest is not treated as a preference item in calculating the Federal alternative minimum tax that may be imposed on individuals and corporations. Such interest, however, is included in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations by the Code. See "Tax Matters" in Part 1 of this Official Statement. It is also the opinion of Bond Counsel to LIPA that, under existing statutes, interest on all of the Offered Securities is exempt from personal income taxes imposed by the State of New York or any political subdivision thereof, and the Offered Securities are exempt from all taxation directly imposed thereon by or under the authority of the State of New York, except estate or gift taxes and taxes on transfers.

$3,449,527,638.05

LONG ISLAND POWER AUTHORITY

Electric System General Revenue Bonds, Series 1998A

Dated: As Shown on Inside Cover Page **Due: As Shown on Inside Cover Page**

The Electric System General Revenue Bonds, Series 1998A (the "Offered Securities") will be issued only as fully registered bonds registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York, which will act as securities depository for the Offered Securities under a book-entry-only system as described herein. Individual purchases of beneficial ownership interests may be made in the principal amount of $5,000 or any integral multiple thereof, in the case of the Current Interest Bonds, and at the initial offering price per $5,000 maturity amount or any integral multiple thereof in the case of the Capital Appreciation Bonds. Beneficial Owners of the Offered Securities will not receive physical delivery of bond certificates. United States Trust Company of New York, New York, New York, is the Trustee under the Resolution.

The Offered Securities are being issued for the purposes described herein.

Interest on the Current Interest Bonds is payable on December 1, 1998 and semiannually thereafter on each June 1 and December 1. Principal and accreted interest will be payable on the Capital Appreciation Bonds on the maturity date thereof.

The Offered Securities are subject to optional redemption and mandatory sinking fund redemption prior to maturity as described herein.

As described on the inside cover page and in this Official Statement, payment of the principal of and interest on certain of the Offered Securities on the regularly scheduled due dates for payment thereof will be insured by policies of municipal bond insurance to be issued simultaneously with the delivery of the Offered Securities.

MATURITY SCHEDULE—See Inside Cover Page

The Offered Securities are special obligations of LIPA payable principally from the revenues generated by the electric transmission and distribution system to be operated by LIPA Sub after the payment of operating expenses of the system. The Offered Securities shall not be debt of the State of New York or of any municipality, and neither the State of New York nor any municipality shall be liable thereon. LIPA shall not have the power to pledge the credit, the revenues or the taxing power of the State of New York or any municipality, and neither the credit, the revenues nor the taxing power of the State of New York or any municipality shall be, or shall be deemed to be, pledged to the payment of any of the Offered Securities. LIPA has no taxing power.

Bear, Stearns & Co. Inc.

Lehman Brothers **Morgan Stanley Dean Witter** **Salomon Smith Barney**

Artemis Capital Group, Inc. **First Albany Corporation** **Merrill Lynch & Co.**

J.P. Morgan & Co. **PaineWebber Incorporated**

ABN AMRO Inc. **Advest, Inc.** **M.R. Beal & Company**

J.C. Bradford & Co. **CIBC Oppenheimer** **Dain Rauscher, Inc.**

A.G. Edwards & Sons, Inc. **Fleet Securities, Inc.** **Raymond James & Associates, Inc.**

Key Capital Markets, Inc. **Lebenthal & Co., Inc.** **David Lerner Associates, Inc.**

Prudential Securities **Samuel A. Ramirez & Co., Inc.** **Roosevelt & Cross, Inc.**

William E. Simon & Sons Municipal Securities, Inc.

The Offered Securities are offered when, as and if issued and accepted by the Underwriters, subject to the approval of legality of Hawkins, Delafield & Wood, New York, New York, Bond Counsel. Certain legal matters with respect to this Official Statement will be passed upon for LIPA by Orrick, Herrington & Sutcliffe LLP, New York, New York, Disclosure Counsel to LIPA. Certain legal matters with respect to LIPA will be passed upon for LIPA by Stanley B. Klimberg, Esquire, General Counsel to LIPA, and by Winthrop, Stimson, Putnam & Roberts, New York, New York, Corporate Counsel to LIPA. Certain legal matters will be passed upon for the Underwriters by Nixon, Hargrave, Devans & Doyle LLP, New York, New York, Counsel to the Underwriters. It is expected that the Offered Securities will be available for delivery in book-entry-only form through The Depository Trust Company in New York, New York on or about May 28, 1998.

May 13, 1998

Current Interest Bonds Dated: May 1, 1998 **Due: December 1, as shown below**
Capital Appreciation Bonds Dated: Date of delivery thereof

$1,279,965,000 Serial Bonds

Maturity	Principal Amount	Interest Rate	Price or Yield	Maturity	Principal Amount	Interest Rate	Yield
1999	$45,880,000	4.50 %	3.90%	2007[1]	$ 8,830,000	4.60 %	4.65%
2000	47,945,000	4.10	100	2008[1]	22,440,000	4.625	4.70
2001	20,935,000	5.25	4.25	2008[1]	47,545,000	5.50	4.70
2001	28,975,000	4.25	100	2009[1]	8,290,000	4.70	4.73
2002	18,560,000	5.25	4.35	2009[1]	65,350,000	5.50	4.73
2002	33,680,000	4.30	4.35	2010[1]	12,170,000	4.75	4.78
2003[1]	54,660,000	4.30	100	2010[1]	65,450,000	5.50	4.78
2004[1]	40,555,000	5.25	4.40	2011[1]	81,800,000	5.50	4.83
2004[1]	16,455,000	4.375	4.40	2012[2]	86,300,000	5.50	4.89
2005[1]	37,660,000	5.25	4.50	2013[2]	91,045,000	5.50	4.93
2005[1]	22,200,000	4.50	100	2014[2]	56,665,000	5.25	4.93
2006[1]	47,490,000	5.50	4.60	2014[2]	39,385,000	5.00	5.10
2006[1]	15,350,000	4.50	4.60	2015[2]	100,995,000	5.00	5.15
2007[1]	57,310,000	6.00	4.65	2016[2]	106,045,000	5.125	5.20

$228,535,000 5.00% Term Bonds due December 1, 2018[2] Price 97.004% to Yield 5.24%
$66,035,000 5.30% Term Bonds due December 1, 2019[2] Price 100.000%
$465,060,000 5.125% Term Bonds due December 1, 2022[2] Price 97.613% to Yield 5.30%
$40,860,000 5.50% Term Bonds due December 1, 2023 Price 100.000%
$158,230,000 5.75% Term Bonds due December 1, 2024 Price 103.750%
$452,825,000 5.25% Term Bonds due December 1, 2026 Price 96.841% to Yield 5.47%
$587,225,000 5.50% Term Bonds due December 1, 2029 Price 98.965% to Yield 5.57%

(Accrued interest to be added.)

$145,792,638.05 Capital Appreciation Bonds[3]

Maturity	Aggregate Initial Offering Price	Approximate Yield to Maturity	Initial Offering Price Per $5,000 Maturity Amount	Maturity	Aggregate Initial Offering Price	Approximate Yield to Maturity	Initial Offering Price Per $5,000 Maturity Amount
2003	$10,201,250.95	4.40%	$3,934.15	2016	$4,970,233.70	5.25%	$1,916.05
2004	9,708,563.80	4.50	3,742.70	2017	4,692,416.30	5.28	1,808.95
2005	9,218,038.40	4.60	3,553.60	2018	4,454,157.40	5.28	1,717.10
2006	8,735,295.00	4.70	3,367.50	2019	4,227,960.60	5.28	1,629.90
2007	8,300,021.80	4.75	3,199.70	2020	3,995,667.90	5.30	1,540.35
2008	7,878,885.90	4.80	3,037.35	2021	3,792,038.90	5.30	1,461.85
2009	7,429,994.20	4.90	2,864.30	2022	3,598,785.90	5.30	1,387.35
2010	6,992,905.20	5.00	2,695.80	2023	3,415,390.10	5.30	1,316.65
2011	6,612,235.70	5.05	2,549.05	2024	3,241,332.70	5.30	1,249.55
2012	6,246,222.30	5.10	2,407.95	2025	3,076,094.90	5.30	1,185.85
2013	5,894,735.30	5.15	2,272.45	2026	2,919,287.60	5.30	1,125.40
2014	5,557,645.00	5.20	2,142.50	2027	2,770,521.70	5.30	1,068.05
2015	5,234,692.00	5.25	2,018.00	2028	2,628,264.80	5.30	1,013.60

(Without accrued interest.)

$25,000,000 5.94% Federally Taxable Bonds due December 1, 1999 Price 100%

(Accrued interest to be added.)

(1) Payment of principal and interest on these Current Interest Bonds will be insured by Ambac Assurance.
(2) Payment of principal and interest on these Current Interest Bonds will be insured by FSA.
(3) Payment of principal and interest on all of the Capital Appreciation Bonds will be insured by FSA.

See "Bond Insurance" in this Part 1.

LONG ISLAND POWER AUTHORITY

333 Earle Ovington Blvd.
Uniondale, New York 11553
Telephone: (516) 222-7700
Facsimile: (516) 222-9137

LIPA TRUSTEES

Richard M. Kessel—*Chairman*
Patrick Foye—*Deputy Chairman*

Michael Affrunti
Harvey Auerbach
Thomas A. Doherty
Michael L. Faltischek
Harriet A. Gilliam
Rupert H. Hopkins
Joseph F. Janoski
Robert R. McMillan
Nancy N. Miklos
Denise F. Molia
Vincent Polimeni
Jonathan Sinnreich

LIPA MANAGEMENT

Richard M. Kessel—*President and Chief Executive Officer*
Seth D. Hulkower—*Executive Director*
David P. Warren—*Chief Financial Officer*
Stanley B. Klimberg—*General Counsel*
Edward P. Murphy, Jr.—*Vice President and Controller*

Financial Advisor

Goldman, Sachs & Co.
New York, New York

Independent Consultant

Resource Management International, Inc.
New York, New York

Independent Accountant

Price Waterhouse LLP
New York, New York

Trustee

United States Trust Company of New York
New York, New York

State Regulatory Counsel

Adams, Dayter & Sheehan LLP
Albany, New York

Bond Counsel

Hawkins, Delafield & Wood
New York, New York

Corporate Counsel

Winthrop, Stimson, Putnam & Roberts
New York, New York

Disclosure Counsel

Orrick, Herrington & Sutcliffe LLP
New York, New York

Special Counsel

Rivkin, Radler & Kremer
Uniondale, New York

Federal Regulatory Counsel

Van Ness Feldman P.C.
Washington, D.C.

No dealer, broker, salesperson or other person has been authorized by LIPA or the Underwriters to give any information or to make any representation, other than the information and representations contained in this Official Statement, in connection with the offering of the Offered Securities, and, if given or made, such information or representations must not be relied upon as having been authorized by LIPA or the Underwriters. This Official Statement does not constitute an offer to sell or solicitation of an offer to buy any of the Offered Securities in any jurisdiction to any person to whom it is unlawful to make such offer or solicitation in such jurisdiction.

The information set forth herein has been furnished by LIPA, LILCO, FSA, Ambac Assurance and RMI and includes information obtained from other sources, all of which are believed to be reliable, but no representation as to the accuracy or completeness of such information is made by the Underwriters. The information and expressions of opinion contained herein are subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of LIPA, LILCO, FSA or Ambac Assurance or the matters covered by the report of RMI included as Appendix A to Part 2 of this Official Statement since the date hereof. Such information and expressions of opinion are made for the purpose of providing information to prospective investors and are not to be used for any other purpose or relied on by any other party.

This Official Statement contains statements which, to the extent they are not recitations of historical fact, constitute "forward-looking statements." In this respect, the words "estimate", "project", "anticipate", "expect", "intend", "believe" and similar expressions are intended to identify forward-looking statements. A number of important factors affecting LIPA's and LIPA Sub's business and financial results could cause actual results to differ materially from those stated in the forward-looking statements.

IN CONNECTION WITH THE OFFERING OF THE OFFERED SECURITIES, THE UNDERWRITERS MAY OVERALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE OFFERED SECURITIES AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

THIS OFFICIAL STATEMENT CONSISTS OF THE COVER PAGE, THE INSIDE COVER PAGE, THE TABLE OF CONTENTS, THE SUMMARY STATEMENT AND THIS PART 1, INCLUDING THE APPENDICES TO THIS PART 1 (ALL OF THE FOREGOING ARE REFERRED TO COLLECTIVELY AS "PART 1") AND THE ATTACHED PART 2, INCLUDING ALL APPENDICES THERETO (COLLECTIVELY, "PART 2"). BOTH THIS PART 1 AND PART 2 ARE DATED MAY 13, 1998. THIS PART 1, TOGETHER WITH PART 2, CONSTITUTE LIPA'S OFFICIAL STATEMENT RELATING TO THE OFFERED SECURITIES (AND ONLY SUCH OFFERED SECURITIES). BOTH PART 1 AND PART 2 MUST BE READ IN THEIR ENTIRETY.

SUMMARY STATEMENT

This Summary Statement is subject in all respects to more complete information contained in this Official Statement and should not be considered a complete statement of the facts material to making an investment decision. The offering of the Offered Securities to potential investors is made only by means of the entire Official Statement. Certain terms used herein are defined in Appendices C and E to Part 2 of this Official Statement.

The LIPA Transaction ..... The Long Island Power Authority (''LIPA'') is a corporate municipal instrumentality and political subdivision of the State of New York. LIPA's primary ongoing statutory purpose is to lower electric rates in a service area comprised of the New York Counties of Nassau and Suffolk (with certain limited exceptions) and in a small portion of Queens County known as the Rockaways. LIPA plans to reduce rates by becoming the provider of retail electric service in this service area by acquiring the Long Island Lighting Company (''LILCO'') as part of a series of interrelated merger and restructuring transactions involving LIPA, LILCO and KeySpan Energy Corporation (the parent holding company of The Brooklyn Union Gas Company). The acquisition of LILCO by LIPA is not dependent upon the LILCO/KeySpan merger.

Immediately prior to its acquisition by LIPA, LILCO will restructure itself by transferring to one or more new subsidiaries of BL Holding Corp, its newly formed parent, all of its fossil fuel electric generating units and its natural gas system. Upon the consummation of the merger transactions, LIPA, through its wholly owned subsidiary, LIPA Sub, will acquire and operate a system comprised of: (a) LILCO's current electric transmission and distribution system and (b) LILCO's existing 18% ownership interest in the Nine Mile Point 2 nuclear generating facility. LIPA (through LIPA Sub) also will acquire the Shoreham Regulatory Asset and will be responsible for certain liabilities of LILCO, including the payment of certain existing debt obligations of LILCO.

The total consideration to be paid by LIPA for the acquisition of LILCO is $6.295 billion, reflecting the purchase of LILCO's common stock, the redemption of certain preferred stock and the retention of certain debt.

The Purpose of the Offered Securities ..... The Offered Securities are being issued, as part of the Plan of Finance described below, to provide a portion of the funds necessary to pay (i) the cash purchase price of the LILCO

	common stock, (ii) the cost of redemption of certain shares of LILCO preferred stock, (iii) the cost of refunding all of the G&R Bonds, (iv) the cost of refinancing certain of the Debentures, (v) certain other costs and expenditures, (vi) the cost of making certain rebates and credits to LIPA Sub's customers, and (vii) costs relating to the issuance of the Offered Securities. The Offered Securities and the Initial Subordinated Indebtedness required to be delivered simultaneously therewith will be issued in an amount at least sufficient to fund the acquisition of LILCO so that upon delivery of the Offered Securities and the Initial Subordinated Indebtedness, LIPA (through LIPA Sub) will commence operations as the provider of retail electric service in its service area.
Plan of Finance	LIPA expects to issue fixed rate Bonds, including the Offered Securities, along with variable rate Subordinated Indebtedness, in three tranches during 1998. If completed as currently projected, LIPA's Plan of Finance (which is subject to change based on market conditions and other factors) would result in the issuance of approximately $5.5 billion of fixed rate Bonds and up to $1.5 billion of the variable rate Initial Subordinated Indebtedness. The Offered Securities and the variable rate Initial Subordinated Indebtedness, which are required to be issued at the same time as the Offered Securities, constitute the first tranche of the Plan of Finance. The remaining tranches assumed in the Plan of Finance are intended to refinance certain LILCO debt retained by LIPA Sub and are expected to be issued later in 1998. LIPA's future financing plans currently include financing necessary capital improvements and the funding of additional Shoreham Credits.
LIPA's Authority to Set Electric Rates	Under current New York law, LIPA is empowered to set rates for electric service in its service area without being required to obtain the approval of the New York State Public Service Commission (''PSC'') or any other State regulatory body. However, LIPA has agreed, in connection with the approval of the proposed merger transaction received from the Public Authorities Control Board (''PACB''), to certain conditions relating to rates including the condition that it will not impose any permanent increase in average customer rates over a 12 month period in excess of 2.5% without approval of the PSC.

LIPA's Initial Rate Structure...	LIPA has adopted an initial set of customer rates which include base rates, a fuel and purchased power cost adjustment clause, and certain riders and credits, and provide for surcharges. LIPA's initial rates result in system average revenue of 12.18 cents per kWh representing an immediate 20 percent reduction compared to LILCO's existing rates. This reduction is principally the result of the effective refinancing of a portion of LILCO's assets with LIPA's lower-cost tax-exempt debt, the exemption from Federal income tax of the net income of LIPA Sub, LIPA's share of the synergy savings from the LILCO/KeySpan merger and providing Shoreham Credits to the customers in LIPA Sub's service area.
Service Area	LIPA Sub's service area will be the same as LILCO's current service area: Nassau and Suffolk Counties (with certain limited exceptions) and the Rockaways area of Queens County. The service area includes over one million customers and had a 1997 peak load of approximately 4,140 MW. Approximately 49 percent of annual electric revenues are received from residential customers, with 48 percent coming from commercial/ industrial customers, and the balance from sales to other utilities and public authorities. LILCO's largest customer accounted for approximately one percent of LILCO's electric revenues, and LILCO's twenty largest customers accounted for approximately three percent of LILCO's electric revenues.
Transmission and Distribution Facilities	LIPA Sub's transmission system will include approximately 1,300 miles of overhead and underground lines with voltage levels ranging from 345kV to 23kV. There are 32 transmission substations to step down transmission voltage levels from 345kV or 138kV to 69kV, 33kV or 23kV. The distribution system has approximately 46,000 circuit miles of overhead lines, 10,400 circuit miles of underground lines and 149,000 line transformers.
Power Supply Resources	LIPA Sub's power supply resources will consist principally of various power purchase contracts. The principal power purchase contract is a Power Supply Agreement with a subsidiary of BL Holding Corp under which LIPA Sub obtains rights to and has obligations to pay for all of the capacity of LILCO's existing fossil fueled generation facilities and which entitles LIPA Sub to purchase all of the energy produced by such facilities for its own customers or

for resale to others. This Agreement has a fifteen year term and is renewable under similar terms. During 1997, 68% of the fuel for the generating units subject to the Agreement was natural gas and 32% was oil.

The only generation facility in which LIPA will have an ownership interest is LILCO's 18% interest in the 1,144 MW Nine Mile Point 2 nuclear unit operated by Niagara Mohawk Power Corporation and jointly owned by Niagara Mohawk and three other New York electric utilities in addition to LILCO.

LIPA's Plan of System Operation .....

LIPA plans to manage LIPA Sub's retail electric business and control costs through a senior management team supported by a small staff to minimize the size of its total work force.

The day-to-day operations of the electric system will be accomplished through three principal contracts: (i) a Management Services Agreement providing for operation of the transmission and distribution system, (ii) a Power Supply Agreement covering the supply of capacity from all of LILCO's current fossil fueled generating facilities and (iii) an Energy Management Agreement providing for the management of LIPA Sub's power supply resources and fuel procurement. Each such agreement will be with a subsidiary of BL Holding Corp which will employ management and other personnel currently performing these functions for LILCO. BL Holding Corp will guarantee the performance, and any payments, by said subsidiaries.

To assist LIPA's management in the supervision of these three principal agreements and to provide other functions requiring specific expertise, LIPA will employ outside consultants.

Independent Consultant's Report .....

LIPA has engaged Resource Management International, Inc. (''RMI''), an internationally recognized firm of engineers, economists and management consultants, for the purpose of conducting an evaluation of engineering, economic, system planning, operations, environmental and related matters for LIPA and LIPA Sub and preparing an estimate of the annual operating results for LIPA and LIPA Sub for the period June 1, 1998 through December 31, 2008 (the ''Study Period''). The Independent Consultant's Report also contains analyses of the sensitivity of estimated operating results to changes in certain key variables.

The Independent Consultant's Report relies on information from a variety of sources as well as a number of specific assumptions set forth in the Independent Consultant's Report. In the Independent Consultant's Report, RMI reaches a number of conclusions concerning the condition of the system and LIPA's ability to achieve its rate reductions and the operation and maintenance of the system. The Independent Consultant's Report is included as Appendix A to Part 2 of this Official Statement and must be read in its entirety.

Projected Revenues, Revenue Requirements and Debt Service Coverages ..... Exhibit 1 to the Independent Consultant's Report sets forth RMI's estimates for LIPA's revenues and revenue requirements for the Study Period and indicates that LIPA's debt service coverage on senior lien debt is estimated to be no less than 2.1x during the Study Period.

Accelerated Retirement of Shoreham Related Debt..... LIPA's Trustees have approved a plan which contemplates (but does not require) using excess cashflow from debt service coverage and favorable budget variances to accelerate the retirement of the portion of debt issued under the Plan of Finance relating to the $4.2 billion intangible asset principally attributable to the Shoreham Regulatory Asset (the Acquisition Adjustment reflected on LIPA's pro-forma consolidated balance sheet in Appendix B to Part 2 of this Official Statement). LIPA intends to effect the accelerated retirement of debt through a combination of (i) open market purchases and tender offers; (ii) cash defeasances; (iii) exercise of LIPA's optional redemption rights; and (iv) up to $850 million of additional scheduled amortization in the period ending December 1, 2013 in tranches two and/or three. LIPA estimates that implementation of this plan would enable it to retire this portion of the debt in approximately 16 years while amortizing the remaining debt under the Plan of Finance and future financings on a level debt service basis.

This accelerated debt retirement, if accomplished, will have a significant impact on the average life of LIPA's debt issued under the Plan of Finance maturing after December 1, 2013. LIPA presently estimates that more than $2 billion of excess cash flow will be available for the accelerated retirement of a portion of the approximately $3 billion of fixed rate Bonds and the variable rate Subordinated Indebtedness expected to mature after December 1, 2013. The potentially significantly shorter average life of Bonds maturing after

December 1, 2013, will affect, among other things, the cost effectiveness of bond insurance purchased in the secondary market for such Bonds.

Security and Sources of Payment for Bonds ..... The Offered Securities and all future Bonds issued on a parity therewith will be payable from and secured by the Trust Estate pledged under LIPA's Bond Resolution. The Trust Estate consists principally of the revenues generated by the operation of LIPA Sub's transmission and distribution system. The revenues are pledged (after the payment of operating expenses) by LIPA Sub to LIPA under the Financing Agreement and by LIPA to the Trustee and the holders of Bonds under the Bond Resolution.

Flow of Funds: The Bond Resolution contains a basic flow of funds, including a Rate Stabilization Fund, but does not require specific periodic advance deposits to be made into, or specific balances maintained in, the various funds and accounts. LIPA's financing plan contemplates the maintenance of the Rate Stabilization Fund at a minimum balance of $250 million.

Additional Bonds Test: After the issuance of the Bonds required to complete the Plan of Finance, the Bond Resolution requires compliance with a 1.2x historical or projected debt service coverage test on Bonds and other senior lien obligations as a condition to the issuance of additional Bonds. Such requirement will be eliminated once LIPA retires an amount equal to 25% of the Acquisition Debt net of the outstanding principal balance of the Promissory Notes. Refunding Bonds may be issued at any time without compliance with any coverage or savings test.

Rate Covenant: The Bond Resolution initially contains a rate covenant providing for 1.2x debt service coverage on Bonds and other senior lien obligations and 1.0x coverage of all other expenses. Such 1.2x coverage requirement will be reduced to 1.0x once LIPA retires an amount equal to 25% of the Acquisition Debt net of the outstanding balance of the Promissory Notes.

Competition and the LIPA Plan ..... LIPA has proposed a retail choice plan, Long Island Choice, intended to lead to full retail choice of power suppliers by 2003. Long Island Choice has been planned in a manner to make LIPA economically indifferent to whether a customer

selects LIPA or another power supplier to serve the customer's power needs. Power delivered to a LIPA retail customer will be delivered over LIPA's transmission and distribution system. LIPA plans to set its rates for delivery service to include all of its non-avoidable costs.

Potential Customer Loss ..... LIPA believes, and the Independent Consultant's Report concludes, based on the information and assumptions relied upon therein, that (i) LIPA's revenues available for debt service are not likely to be materially reduced by additional self-generation and (ii) new municipalization within the service area is unlikely to occur for economic reasons. The Independent Consultant's Report is included as Appendix A to Part 2 of this Official Statement and must be read in its entirety. LIPA further believes, based on opinions from counsel described in this Official Statement, that new municipalization is precluded by law.

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PART 1

of the

OFFICIAL STATEMENT

of the

LONG ISLAND POWER AUTHORITY

relating to its

$3,449,527,638.05

Electric System General Revenue Bonds, Series 1998A

INTRODUCTION

The Offered Securities are being issued by the Long Island Power Authority (''LIPA'') pursuant to the Long Island Power Authority Act, being title one-A of article five (§1020 *et seq.*) of the Public Authorities Law of the State of New York, as amended (the ''LIPA Act''), and the Electric System General Revenue Bond Resolution of LIPA adopted on May 13, 1998 (the ''Bond Resolution''), as supplemented by a resolution of LIPA adopted on May 13, 1998 authorizing the Offered Securities (the ''Supplemental Resolution''). The Bond Resolution, as supplemented by the Supplemental Resolution and as it may be further supplemented or amended in the future, is herein called the ''Resolution.''

LIPA will issue between $1,200,000,000 and $1,500,000,000 principal amount of its variable rate Electric System Subordinated Revenue Bonds in one or more series (collectively, the ''Initial Subordinated Indebtedness''). The Initial Subordinated Indebtedness is being issued pursuant to LIPA's Electric System General Subordinated Revenue Bond Resolution (the ''Subordinated Resolution''), and will be offered pursuant to a separate official statement of LIPA relating solely to the Initial Subordinated Indebtedness. The Offered Securities and the Initial Subordinated Indebtedness constitute the first of three tranches of financings contemplated by the Plan of Finance.

This Official Statement assumes for purposes of estimating the sources and uses of funds, debt service and the pro forma consolidated balance sheet that the Initial Subordinated Indebtedness will be $1,500,000,000. It is a condition to the issuance and delivery of the Offered Securities that the Offered Securities and the Initial Subordinated Indebtedness be issued and delivered simultaneously.

As used in the Official Statement, the term ''Bonds'' means the bonds issued by LIPA pursuant to the Resolution, all of which are on a parity, senior lien basis as to security and source of payment. The term ''Bonds'' does not include Subordinated Indebtedness. The term ''Subordinated Indebtedness'' means all bonds, notes or other evidence of indebtedness of LIPA issued by LIPA which are on a junior and subordinate basis to the Bonds as to security and source of payment. The Initial Subordinated Indebtedness is Subordinated Indebtedness as so defined. The Offered Securities are Bonds as defined above. See ''Appendix C—Glossary of Defined Terms'' and ''Appendix E—Summary of Operating Agreements—Definitions of Certain Terms'' for the definitions of certain capitalized terms.

Financial Security Assurance Inc. and Ambac Assurance Corporation (each, a ''Bond Insurer''), will each issue a policy of bond insurance (each, a ''Bond Insurance Policy'') insuring the portion of the Offered Securities indicated on the inside cover page of this Official Statement (all of the insured Offered Securities are herein referred to as the ''Insured Offered Securities'').

PURPOSE OF THE OFFERED SECURITIES AND THE INITIAL SUBORDINATED INDEBTEDNESS

General

The proceeds of the first tranche of the financing contemplated by the Plan of Finance will be used to complete the LIPA/LILCO Merger Transaction, which will permit LIPA (through LIPA Sub)

to commence business as the retail supplier of electricity in the Service Area. The table which follows shows the sources and uses of funds for the first tranche. See "Plan of Finance" in Part 2 of this Official Statement for a description of the uses of funds for each tranche of the Plan of Finance.

ESTIMATED SOURCES AND USES OF FUNDS
(millions of dollars)

Sources	
Principal Amount of Offered Securities	$3,449.5
Principal Amount of Initial Subordinated Indebtedness	1,500.0
Original Issue Premium	8.8
Accrued Interest	13.0
Other Contributed Funds	36.2
Total	$5,007.5
Uses	
Cash Purchase Price for Common Stock	$2,497.5
Preferred Stock Redemption	339.1
Redemption of G&R Bonds	1,217.8
Refinance Debentures	476.3
Shoreham Rebates and Credits	142.5
Capital Expenditures	135.0
Purchase of Interest Rate Hedge	64.9
Clean Energy and Rate Payer Advocacy Programs	21.0
Reimbursement of Advances	35.2
Accrued Interest	13.0
Credit Enhancement Fees, Underwriters' Discount and Costs of Issuance	65.2
Total	$5,007.5

LIPA anticipates completing the second and third tranches of the Plan of Finance in 1998 for the purpose of, among other things, refunding the portion of the Debentures and the NYSERDA Financing Notes not supported by Promissory Notes. The purpose of these refundings is to achieve debt service savings and replace certain "bullet" maturities with self-amortizing debt. After completion of the Plan of Finance, LIPA expects that it will, from time-to-time, issue additional Bonds or Subordinated Indebtedness to fund future capital expenditures for the T&D System and NMP2 and to fund additional Shoreham Credits.

Debt Service

The following table shows an estimate of LIPA's consolidated debt service requirements following the issuance of the Offered Securities and the Initial Subordinated Indebtedness (based on the assumptions in the footnotes to said table), including the debt service payable by LIPA Sub on the Debentures and NYSERDA Financing Notes. It also shows the amounts estimated to be paid to LIPA Sub by BL Holding Corp and one or more of its subsidiaries (the "Promissory Note Obligors") under the Promissory Notes that will be used by LIPA Sub to offset a portion of this debt service. If the second and third tranches of LIPA's Plan of Finance as described in the next paragraph are not completed, then this chart will represent LIPA's resulting debt service structure prior to any other future issuance by LIPA of Bonds or Subordinated Indebtedness.

ESTIMATED DEBT SERVICE AFTER ISSUANCE OF OFFERED SECURITIES AND INITIAL SUBORDINATED INDEBTEDNESS ($000)

Debt Service Accruing Through December 31	Offered Securities(1)		Initial Subordinated Indebtedness(2)		Debentures(3)		NYSERDA Financing Notes(4)		Less: Promissory Notes (5)		Total Net Debt Service		
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Total
1998	$ —	$ 101,071	$ —	$ 34,313	$ —	$ 77,905	$ —	$ 42,335	$ —	$ 38,801	$ —	$ 207,607	$ 207,607
1999	70,880	173,265	—	67,500	397,000	141,559	—	56,362	397,000	67,754	45,745	382,503	428,248
2000	47,945	169,715	—	67,500	36,000	111,264	—	56,362	—	38,773	83,755	379,177	462,932
2001	49,910	167,750	—	67,500	145,000	109,950	—	56,362	—	38,773	194,975	375,642	570,617
2002	52,240	165,419	—	67,500	—	100,888	—	56,362	—	38,773	52,425	364,131	416,556
2003	64,861	165,760	—	67,500	150,000	95,600	—	56,362	—	38,773	216,080	360,836	576,916
2004	66,719	163,907	—	67,500	59,000	88,248	—	56,362	—	38,773	127,203	351,356	478,559
2005	69,078	161,549	—	67,500	200,000	79,058	—	56,362	—	38,773	270,433	339,938	610,371
2006	71,575	159,056	—	67,500	—	71,933	29,375	56,362	27,215	38,773	75,038	330,368	405,407
2007	74,440	156,188	—	67,500	122,700	67,331	—	54,159	—	36,732	198,245	322,938	521,183
2008	77,864	152,764	—	67,500	—	62,730	—	54,159	—	36,732	78,448	315,437	393,884
2009	81,070	149,561	—	67,500	—	62,730	19,100	54,159	17,115	36,732	83,607	312,259	395,867
2010	84,613	146,014	—	67,500	—	62,730	—	52,669	—	35,397	85,093	308,631	393,723
2011	88,412	142,217	—	67,500	—	62,730	—	52,669	—	35,397	88,882	304,843	393,725
2012	92,546	138,084	—	67,500	—	62,730	17,200	52,669	—	35,397	110,173	300,756	410,929
2013	96,940	133,689	—	67,500	—	62,730	—	51,250	—	35,397	97,415	294,894	392,309
2014	101,608	129,018	—	67,500	—	62,730	—	51,250	—	35,397	102,195	290,114	392,309
2015	106,230	124,397	—	67,500	—	62,730	—	51,250	—	35,397	107,328	284,976	392,303
2016	111,015	119,612	—	67,500	—	62,730	150,000	46,188	—	35,397	262,851	274,394	537,245
2017	116,172	114,455	—	67,500	—	62,730	—	44,500	—	35,397	118,729	266,833	385,562
2018	121,509	109,119	—	67,500	—	62,730	—	44,500	—	35,397	124,971	260,587	385,558
2019	127,138	103,492	—	67,500	—	62,730	100,000	44,500	31,365	35,397	200,245	253,951	454,195
2020	133,316	97,310	—	67,500	—	62,730	200,000	33,775	90,505	30,784	247,905	241,036	488,940
2021	139,742	90,886	—	67,500	—	62,730	—	23,050	—	26,684	145,615	227,203	372,818
2022	146,514	84,112	—	67,500	451,000	62,730	200,000	17,391	37,635	26,235	766,614	214,360	980,974
2023	153,655	76,971	—	67,500	270,000	11,070	100,000	8,726	296,885	12,985	234,442	159,205	393,647
2024	161,471	69,155	—	67,500	—	—	50,000	4,142	2,240	706	217,637	147,282	364,919
2025	170,406	60,222	—	67,500	—	—	50,000	1,702	13,440	605	215,484	135,897	351,381
2026	179,034	51,594	—	67,500	—	—	—	—	—	—	188,487	125,234	313,721
2027	188,131	42,497	—	67,500	—	—	—	—	—	—	198,601	115,120	313,721
2028	198,183	32,439	—	67,500	—	—	—	—	—	—	209,294	104,429	313,723
2029	206,310	11,347	—	67,500	—	—	—	—	—	—	218,510	79,571	298,081
2030	—	—	348,100	67,500	—	—	—	—	—	—	350,600	67,500	418,100
2031	—	—	363,800	51,836	—	—	—	—	—	—	366,400	51,723	418,123
2032	—	—	380,100	35,465	—	—	—	—	—	—	382,800	35,235	418,035
2033	—	—	408,000	7,650	—	—	—	—	—	—	400,200	18,009	418,209
Totals	$3,449,528	$3,762,634	$1,500,000	$2,289,263	$1,830,700	$1,895,754	$915,675	$1,235,936	$913,400	$940,138	$6,866,424	$8,603,975	$15,470,399

Footnotes on next page.

Entries rounded to the nearest thousands. Totals may not add due to rounding.

(1) Interest on Capital Appreciation Bonds is shown in the year such Capital Appreciation Bonds mature.

(2) The Initial Subordinated Indebtedness (assumed to be issued in the principal amount of $1,500,000,000) will bear interest at variable rates. Principal maturities have been assumed as shown. Interest, including letter of credit and remarketing fees, has been assumed at a rate of 4.5% per annum.

(3) The Debentures are unsecured obligations which were obligations of LILCO and which will be obligations of LIPA Sub. It is expected that the Debentures not refinanced in the first tranche (other than the $667 million aggregate principal amount of Debentures due in 1999 and 2023 that will be the subject of an exchange offer by BL Holding Corp) will be refinanced from the proceeds of the second and third tranches expected to be issued in 1998.

(4) The NYSERDA Financing Notes were obligations of LILCO and will be obligations of LIPA Sub. Certain of the NYSERDA Financing Notes bear interest at fixed rates and certain bear interest at variable rates which are assumed to be 4.5% (including letter of credit and remarketing fees). It is expected that the NYSERDA Financing Notes for which there are no corresponding Promissory Notes will be refinanced from the proceeds of the second tranche.

(5) The Promissory Notes will be issued on the date of the closing of the LIPA/LILCO Merger Transaction by the Promissory Note Obligors to LIPA Sub and will evidence the obligation of the Promissory Note Obligors to pay to LIPA Sub, 30 days prior to the applicable due dates thereof, the principal of and interest on (i) $397,000,000 principal amount of the Debentures due on July 15, 1999 and $270,000,000 principal amount of the Debentures due on March 15, 2023 (each subject to later reduction, however, to reflect the amount of such Debentures exchanged pursuant to the BL Holding Corp exchange offer) and (ii) $246,400,000 aggregate principal amount of the NYSERDA Financing Notes due on various dates through 2025. The amounts shown reflect estimates of the principal amount of Promissory Notes that will be applicable to the NYSERDA Financing Notes. The actual amount of such Promissory Notes will be determined at the time of the LIPA/LILCO Merger Closing and will be subject to post-closing adjustment, which may decrease or increase the final amount of such Promissory Notes. It is not expected that such decreases or increases will be significant.

The following table shows an estimate of LIPA's debt service requirements (based on the assumptions in the footnotes to said table) following the completion of the second and third tranches (together with the amounts to be received by LIPA Sub from the Promissory Note Obligors under the Promissory Notes that will be used to offset a portion of this debt service). NO ASSURANCE CAN BE GIVEN, HOWEVER, THAT LIPA WILL, OR WILL BE ABLE TO, COMPLETE FULLY ITS PLAN OF FINANCE AS CURRENTLY ENVISIONED, OR THAT ALL OF THE DEBT ANTICIPATED TO BE REFINANCED WILL BE REFINANCED, OR THAT SUCH DEBT WILL BE REFINANCED ON THE TERMS ASSUMED IN THIS TABLE. The effects of not refinancing all debt anticipated to be refinanced would be that LIPA's annual debt service requirements will be substantially higher in certain years than would be the case if the Plan of Finance is completed as contemplated.

ESTIMATED DEBT SERVICE AFTER COMPLETION OF PLAN OF FINANCE
($000)

Debt Service Accruing Through December 31	Bonds (1) and (2)		Subordinated Indebtedness(1)		Debentures(3)		NYSERDA Financing Notes(4)		Less: Promissory Notes (5)		Total Net Debt Service		
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Total
1998	$ —	$ 127,739	$ —	$ 34,313	$ —	$ 25,561	$ —	$ 13,240	$ —	$ 38,801	$ —	$ 162,052	$ 162,052
1999	135,175	284,306	—	67,500	397,000	51,121	—	16,633	397,000	67,754	135,175	351,806	486,981
2000	115,075	277,928	—	67,500	—	22,140	—	16,633	—	38,773	115,075	345,428	460,503
2001	120,160	272,841	—	67,500	—	22,140	—	16,633	—	38,773	120,160	340,341	460,501
2002	125,935	267,068	—	67,500	—	22,140	—	16,633	—	38,773	125,935	334,568	460,503
2003	142,271	263,687	—	67,500	—	22,140	—	16,633	—	38,773	142,271	331,187	473,459
2004	148,084	257,887	—	67,500	—	22,140	—	16,633	—	38,773	148,084	325,387	473,470
2005	154,633	251,338	—	67,500	—	22,140	—	16,633	—	38,773	154,633	318,838	473,471
2006	161,660	244,310	—	67,500	—	22,140	27,215	16,633	27,215	38,773	161,660	311,810	473,470
2007	169,390	236,578	—	67,500	—	22,140	—	14,592	—	36,732	169,390	304,078	473,468
2008	177,989	227,980	—	67,500	—	22,140	—	14,592	—	36,732	177,989	295,480	473,468
2009	186,705	219,269	—	67,500	—	22,140	17,115	14,592	17,115	36,732	186,705	286,769	473,474
2010	196,158	209,806	—	67,500	—	22,140	—	13,257	—	35,397	196,158	277,306	473,464
2011	206,262	199,707	—	67,500	—	22,140	—	13,257	—	35,397	206,262	267,207	473,469
2012	217,176	188,798	—	67,500	—	22,140	—	13,257	—	35,397	217,176	256,298	473,474
2013	228,795	177,174	—	67,500	—	22,140	—	13,257	—	35,397	228,795	244,674	473,469
2014	126,078	164,790	—	67,500	—	22,140	—	13,257	—	35,397	126,078	232,290	358,368
2015	132,130	158,737	—	67,500	—	22,140	—	13,257	—	35,397	132,130	226,237	358,367
2016	138,445	152,424	—	67,500	—	22,140	—	13,257	—	35,397	138,445	219,924	358,369
2017	145,232	145,635	—	67,500	—	22,140	—	13,257	—	35,397	145,232	213,135	358,367
2018	152,309	138,561	—	67,500	—	22,140	—	13,257	—	35,397	152,309	206,061	358,371
2019	159,783	131,087	—	67,500	—	22,140	31,365	13,257	31,365	35,397	159,783	198,587	358,370
2020	167,821	123,044	—	67,500	—	22,140	90,505	8,644	90,505	30,784	167,821	190,544	358,364
2021	176,217	114,653	—	67,500	—	22,140	—	4,544	—	26,684	176,217	182,153	358,370
2022	185,069	105,800	—	67,500	—	22,140	37,635	4,095	37,635	26,235	185,069	173,300	358,368
2023	194,405	96,461	—	67,500	270,000	11,070	26,885	1,915	296,885	12,985	194,405	163,961	358,366
2024	204,546	86,323	—	67,500	—	—	2,240	706	2,240	706	204,546	153,823	358,369
2025	215,956	74,913	—	67,500	—	—	13,440	605	13,440	605	215,956	142,413	358,369
2026	227,204	63,666	—	67,500	—	—	—	—	—	—	227,204	131,166	358,370
2027	239,071	51,799	—	67,500	—	—	—	—	—	—	239,071	119,299	358,369
2028	252,048	38,812	—	67,500	—	—	—	—	—	—	252,048	106,312	358,360
2029	263,275	14,623	—	67,500	—	—	—	—	—	—	263,275	82,123	345,398
2030	—	—	348,100	67,500	—	—	—	—	—	—	348,100	67,500	415,600
2031	—	—	363,800	51,836	—	—	—	—	—	—	363,800	51,836	415,636
2032	—	—	380,100	35,465	—	—	—	—	—	—	380,100	35,465	415,565
2033	—	—	408,000	7,650	—	—	—	—	—	—	408,000	7,650	415,650
Totals	$5,465,058	$5,367,742	$1,500,000	$2,289,263	$667,000	$596,972	$246,400	$343,166	$913,400	$940,138	$6,965,058	$7,657,005	$14,622,063

Entries rounded to the nearest thousands. Totals may not add due to rounding.

(1) See the prior table entitled "Estimated Debt Service After Issuance of Offered Securities and Initial Subordinated Indebtedness."

(2) Tranches two and three are expected to consist only of fixed rate Bonds which are expected to be issued in 1998 in the principal amount of $863,960,000 and $1,151,570,000 respectively, and are assumed to bear interest at a rate equal to 6% per annum.

(3) Represents the entire $667 million aggregate principal amount of the Debentures maturing in 1999 and 2023, subject to later reduction if and to the extent that the BL Holding Corp exchange offer is successful.

(4) Represents the principal amount of the NYSERDA Financing Notes to be outstanding after the completion of the Plan of Finance. See footnotes 4 and 5 to the prior table.

(5) See footnote 5 to the prior table.

DESCRIPTION OF THE OFFERED SECURITIES

General

The Offered Securities will consist of Current Interest Bonds and Capital Appreciation Bonds, as described below.

Upon initial issuance, the Offered Securities will be available only in book-entry form. The Depository Trust Company, New York, New York (''DTC'') will act as securities depository for the Offered Securities, and the ownership of one fully registered bond for each maturity of the Offered Securities in the principal amount of such maturity will be registered in the name of Cede & Co., as nominee for DTC, and deposited with DTC. See Appendix H to Part 2 of this Official Statement for a description of DTC and its book-entry-only system.

Current Interest Bonds

The Current Interest Bonds will be dated May 1, 1998 and will mature at the times and in the principal amounts as set forth on the inside cover page of this Official Statement. Interest on the Current Interest Bonds will be payable semiannually on June 1 and December 1, commencing on December 1, 1998 (7 months' interest). The Current Interest Bonds will be offered in authorized denominations of $5,000 and integral multiples thereof (''Authorized Denominations'' of the Current Interest Bonds).

Capital Appreciation Bonds

The Capital Appreciation Bonds are serial bonds, will be dated the date of their delivery to the Underwriters, and will mature at the times and will be issued in minimum denominations (each of which accretes to an aggregate $5,000 principal and interest payable at maturity) as set forth in the column ''Initial Offering Price Per $5,000 Maturity Amount'' and integral multiples thereof (the ''Authorized Denominations'' of such Capital Appreciation Bonds), as set forth on the inside cover page of this Official Statement. Interest on the Capital Appreciation Bonds will not be payable currently.

For purposes of the Resolution, the amount of the Capital Appreciation Bonds deemed to be Outstanding for purposes of calculating the principal amount of any such Bonds and the principal amount of Bonds Outstanding in connection with the exercise of any voting right or privilege, the giving of any consent or direction or the taking of any other action that the Holders of the Bonds are entitled to take pursuant to the Resolution, shall be the accreted value thereof as of the next preceding June 1 or December 1. The accreted value of Capital Appreciation Bonds on any June 1 and December 1 is determined by computing the present worth on such date of $5,000 (per each minimum Authorized Denomination) payable at maturity, based upon the yield to maturity at which such Capital Appreciation Bonds were initially offered to the public as set forth on the inside cover page of this Official Statement and semi-annual compounding. Appendix 1 to this Part 1 sets forth the accreted values of the Capital Appreciation Bonds as of each June 1 and December 1 on the minimum Authorized Denominations specified above, until the maturity thereof. The accreted values of the Capital Appreciation Bonds for times other than those set forth in such Appendix will be interpolated on a straight line basis.

Redemption

Optional. The 5.00% Current Interest Serial Bonds due on December 1, 2014 and the Current Interest Serial and Term Bonds maturing on and after December 1, 2015 (except for the Current Interest Bonds maturing on December 1, 2029) are subject to redemption prior to maturity, at the

option of LIPA, on any date on and after June 1, 2008, in whole, or in part from time to time, and in any order of maturity selected by LIPA, at the following redemption prices (expressed as a percentage of the principal amount of the Current Interest Bonds to be redeemed), together with the interest accrued on such principal amount to the redemption date:

Period During Which Redeemed (both dates inclusive)	Redemption Price
June 1, 2008 through May 31, 2009	101%
June 1, 2009 through May 31, 2010	100½
June 1, 2010 and thereafter	100

The Current Interest Bonds maturing on December 1, 2029 are subject to optional redemption prior to maturity, at the option of LIPA, on any date on and after June 1, 2003, in whole, or in part from time to time, at a redemption price of 101% (expressed as a percentage of the principal amount of the Current Interest Bonds to be redeemed), together with the interest accrued on such principal amount to the redemption date.

The Current Interest Bonds maturing on December 1, 1999 through December 1, 2013 and the 5.25% Current Interest Serial Bonds due on December 1, 2014, are not subject to redemption prior to maturity.

The Capital Appreciation Bonds are not subject to redemption prior to maturity.

The Taxable Bonds are not subject to redemption prior to maturity.

Sinking Fund. The Current Interest Bonds which mature on December 1, 2018 are also subject to redemption in part on December 1 of the years and in the respective principal amounts set forth below at 100% of the principal amount thereof, plus accrued interest to the redemption date, from mandatory sinking fund installments which are required to be made in amounts sufficient to redeem on December 1 of each year the principal amount of such Current Interest Bonds specified for each of the years shown below:

Current Interest Bonds Due December 1, 2018	
Year	Principal Amount
2017	$111,480,000
2018 (maturity)	117,055,000

The Current Interest Bonds which mature on December 1, 2022 are also subject to redemption in part on December 1 of the years and in the respective principal amounts set forth below at 100% of the principal amount thereof, plus accrued interest to the redemption date, from mandatory sinking fund installments which are required to be made in amounts sufficient to redeem on December 1 of each year the principal amount of such Current Interest Bonds specified for each of the years shown below:

Current Interest Bonds Due December 1, 2022	
Year	Principal Amount
2019	$ 56,875,000
2020	129,320,000
2021	135,950,000
2022 (maturity)	142,915,000

The Current Interest Bonds which mature on December 1, 2026 are also subject to redemption in part on December 1 of the years and in the respective principal amounts set forth below at 100% of the principal amount thereof, plus accrued interest to the redemption date, from mandatory sinking fund installments which are required to be made in amounts sufficient to redeem on December 1 of each year the principal amount of such Current Interest Bonds specified for each of the years shown below:

Current Interest Bonds Due December 1, 2026	
Year	Principal Amount
2023	$109,380,000
2024	0
2025	167,330,000
2026 (maturity)	176,115,000

The Current Interest Bonds which mature on December 1, 2029 are also subject to redemption in part on December 1 of the years and in the respective principal amounts set forth below at 100% of the principal amount thereof, plus accrued interest to the redemption date, from mandatory sinking fund installments which are required to be made in amounts sufficient to redeem on December 1 of each year the principal amount of such Current Interest Bonds specified for each of the years shown below:

Current Interest Bonds Due December 1, 2029	
Year	Principal Amount
2027	$185,360,000
2028	195,555,000
2029 (maturity)	206,310,000

Credit Against Sinking Fund Installments. In the event a principal amount of term Current Interest Bonds of any maturity is deemed to be no longer Outstanding, except by a redemption from moneys credited to the Debt Service Fund as sinking fund installments, such principal amount shall be applied to reduce the remaining sinking fund installments for such term Current Interest Bonds in such order and amounts as is determined by LIPA.

Notice of Redemption

If any of the Offered Securities are to be redeemed (either optionally or as required to satisfy mandatory sinking fund installments), notice of such redemption is to be mailed by the Trustee to registered owners of such Offered Securities to be redeemed not less than 30 nor more than 45 days preceding each redemption date. Any notice of redemption may provide that such redemption is conditioned on, among other things, the availability of sufficient moneys on the redemption date.

The Trustee, so long as a book-entry-only system is used for determining ownership of the Offered Securities, shall send the notice to DTC or its nominee, or its successor, and, if less than all of the bonds of the Offered Securities of a maturity are to be redeemed, DTC and the Direct DTC Participants and, where appropriate, Indirect DTC Participants will determine the particular beneficial ownership interests of such Offered Securities of such maturity to be redeemed. Any failure of DTC or a Direct DTC Participant or, where appropriate, Indirect DTC Participants to do so, or to notify a Beneficial Owner of an Offered Bond of such redemption, will not affect the sufficiency or the validity

of the redemption of such Bond. LIPA can make no assurances that DTC, Direct DTC Participants, Indirect DTC Participants or other nominees of the Beneficial Owners of the Offered Securities to be redeemed will distribute such notices to the Beneficial Owners of such Bonds, or that they will do so on a timely basis. See "Book-Entry-Only System" in Appendix H to Part 2.

BOND INSURANCE

General

It is a condition to the issuance of all of the Offered Securities that each Bond Insurer issue its Bond Insurance Policy for the Insured Offered Securities that it is insuring. The Insured Offered Securities, and those that each Bond Insurer is insuring, are indicated on the inside cover page of this Part 1. Each Bond Insurer has agreed to issue its Bond Insurance Policy concurrently with the initial issuance of the Offered Securities.

There follows under this caption certain information concerning each Bond Insurer and its Bond Insurance Policy, which has been supplied by such Bond Insurer, as well as certain information relating to certain provisions of the Resolution relating thereto. No representation is made by LIPA or the Underwriters as to the accuracy, completeness or adequacy of such information, or as to the absence of material adverse changes in such information subsequent to the date hereof. Neither LIPA nor the Underwriters have made any independent investigation of each Bond Insurer or its Bond Insurance Policy, and reference should be made to the information set forth below and in Appendices 3 and 4 hereto for a description thereof. The Bond Insurance Policies do not constitute a part of the contract between LIPA and the holders of the Insured Offered Securities as evidenced by such Bonds or the Resolution. Except for payment of the premiums for the Bond Insurance Policies, LIPA has no responsibility whatsoever with respect to the Bond Insurance Policies, including the maintenance or enforcement thereof or collection of amounts payable thereunder.

So long as FSA and Ambac Assurance are not in default under their respective Bond Insurance Policies, they shall each be deemed to be the *sole* holder of their respective Insured Offered Securities for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the holders of the Insured Offered Securities are entitled to take under the provisions of the Bond Resolution pertaining to supplemental resolutions, amendments, defaults and remedies and the Trustee.

Financial Security Assurance Inc. Insured Offered Securities

The following information and the specimen bond insurance policy attached to this Part 1 as Appendix 3 has been furnished by Financial Security Assurance Inc. ("FSA") for use in this Official Statement.

FSA Insurance Policy

Concurrently with the issuance of the Offered Securities, FSA will issue its municipal bond insurance policy (the "FSA Insurance Policy") for the Current Interest Bonds maturing on December 1, 2012, 2013, 2014, 2015, 2016, 2018, 2019 and 2022, and all of the Capital Appreciation Bonds (the "FSA Insured Offered Securities"). The FSA Insurance Policy guarantees the scheduled payment of principal of and interest on the FSA Insured Offered Securities when due as set forth in the form of the FSA Insurance Policy included as Appendix 3 to this Official Statement.

THE FSA INSURANCE POLICY IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

Financial Security Assurance Inc.

FSA is a New York domiciled insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. (''Holdings''). Holdings is a New York Stock Exchange listed company whose major shareholders include Fund American Enterprises Holdings, Inc., The Tokio Marine and Fire Insurance Co., Ltd. and U S WEST Capital Corporation. The shareholders of Holdings are not liable for the obligations of FSA.

At December 31, 1997, FSA's total policyholders' surplus and contingency reserves were approximately $781,661,000 and its total unearned premium reserve was approximately $496,936,000 in accordance with statutory accounting principles. At December 31, 1997, FSA's total shareholders' equity was approximately $897,860,000 and its total net unearned premium reserve was approximately $422,073,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the SEC are hereby incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the FSA Insured Offered Securities.

Copies of such materials incorporated by reference will be provided upon request to FSA: 350 Park Avenue, New York, New York 10022, Attention: Communications Department (telephone (212) 826-0100).

The FSA Insurance Policy does not protect investors against changes in market value of the FSA Insured Offered Securities, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. FSA makes no representation regarding the FSA Insured Offered Securities or the advisability of investing in the FSA Insured Offered Securities. FSA makes no representation regarding this Official Statement, nor has it participated in the preparation thereof, except that FSA has provided to LIPA the information presented under this caption for inclusion in this Official Statement.

Ambac Assurance Corporation Insured Offered Securities

The following information and the specimen municipal bond insurance policy attached to this Part 1 as Appendix 4 has been furnished by Ambac Assurance Corporation (''Ambac Assurance'') for use in this Official Statement. Concurrently with the issuance of the Offered Securities, Ambac Assurance will issue its municipal bond insurance policy (the ''Ambac Assurance Municipal Bond Insurance Policy'') for the Current Interest Bonds maturing on December 1, 2003, 2004, 2005, 2006, 2007, 2008, 2009, 2010 and 2011 (the ''Ambac Assurance Insured Offered Securities'').

Ambac Assurance has made a commitment to issue an Ambac Assurance Municipal Bond Insurance Policy relating to the Ambac Assurance Insured Offered Securities effective as of the date of issuance of the Ambac Assurance Insured Offered Securities. A specimen copy of the Ambac Assurance Municipal Bond Insurance Policy is attached hereto as Appendix 4. Under the terms of the Ambac Assurance Municipal Bond Insurance Policy, Ambac Assurance will pay to the United States Trust Company of New York, in New York, New York or any successor thereto (the ''Insurance Trustee'') that portion of the principal of and interest on the Ambac Assurance

Insured Offered Securities which shall become Due for Payment but shall be unpaid by reason of Nonpayment by LIPA (as such terms are defined in the Ambac Assurance Municipal Bond Insurance Policy). Ambac Assurance will make such payments to the Insurance Trustee on the later of the date on which such principal and interest becomes Due for Payment or within one business day following the date on which Ambac Assurance shall have received notice of Nonpayment from the Trustee/Paying Agent. The insurance will extend for the term of the Ambac Assurance Insured Offered Securities and, once issued, cannot be canceled by Ambac Assurance.

The Ambac Assurance Municipal Bond Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Ambac Assurance Insured Offered Securities become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Ambac Assurance Insured Offered Securities, Ambac Assurance shall remain obligated to pay principal of and interest on outstanding Ambac Assurance Insured Offered Securities on the originally scheduled interest and principal payment dates including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Ambac Assurance Insured Offered Securities, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration.

In the event the Trustee/Paying Agent has notice that any payment of principal of or interest on an Ambac Assurance Insured Offered Security which has become Due for Payment and which is made to an Ambac Assurance Insured Offered Security Owner by or on behalf of LIPA has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such registered owner shall be entitled to payment from Ambac Assurance to the extent of such recovery if sufficient funds are not otherwise available.

The Ambac Assurance Municipal Bond Insurance Policy does not insure any risk other than Nonpayment, as defined in the Policy. Specifically, the Ambac Assurance Municipal Bond Insurance Policy does not cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity;
2. payment of any redemption, prepayment or acceleration premium; and
3. nonpayment of principal or interest caused by the insolvency or negligence of any Trustee or Paying Agent, if any.

If it becomes necessary to call upon the Ambac Assurance Municipal Bond Insurance Policy, payment of principal requires surrender of the Ambac Assurance Insured Offered Securities to the Insurance Trustee together with an appropriate instrument of assignment so as to permit ownership of such Ambac Assurance Insured Offered Securities to be registered in the name of Ambac Assurance to the extent of the payment under the Ambac Assurance Municipal Bond Insurance Policy. Payment of interest pursuant to the Ambac Assurance Municipal Bond Insurance Policy requires proof of Ambac Assurance Insured Offered Security owner entitlement to interest payments and an appropriate assignment of the Ambac Assurance Insured Offered Security owner's right to payment to Ambac Assurance.

Upon payment of the insurance benefits, Ambac Assurance will become the owner of the Ambac Assurance Insured Offered Security, appurtenant coupon, if any, or right to payment of

principal or interest on such Ambac Assurance Insured Offered Security and will be fully subrogated to the surrendering Ambac Assurance Insured Offered Security owner's rights to payment.

The insurance provided by the Ambac Assurance Municipal Bond Insurance Policy is not covered by the property/casualty insurance security fund specified by the insurance laws of the State of New York.

Ambac Assurance Corporation

Ambac Assurance is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin and licensed to do business in 50 states, the District of Columbia, the Territory of Guam and the Commonwealth of Puerto Rico, with admitted assets of approximately $2,879,000,000 (unaudited) and statutory capital of approximately $1,656,000,000 (unaudited) as of December 31, 1997. Statutory capital consists of Ambac Assurance's policyholders' surplus and statutory contingency reserve. S&P, Moody's and Fitch (all as hereinafter defined) have each assigned a triple-A claims-paying ability rating to Ambac Assurance.

Ambac Assurance has obtained a ruling from the Internal Revenue Service to the effect that the insuring of an obligation by Ambac Assurance will not affect the treatment for federal income tax purposes of interest on such obligation and that insurance proceeds representing maturing interest paid by Ambac Assurance under policy provisions substantially identical to those contained in its municipal bond insurance policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the issuer of the Ambac Assurance Insured Offered Securities.

Ambac Assurance makes no representation regarding the Ambac Assurance Insured Offered Securities or the advisability of investing in the Ambac Assurance Insured Offered Securities and makes no representation regarding, nor has it participated in the preparation of, the Official Statement other than the information supplied by Ambac Assurance and presented under the heading ''Bond Insurance—Ambac Assurance Corporation Insured Offered Securities''.

Available Information. The parent company of Ambac Assurance, Ambac Financial Group, Inc. (''Ambac Financial''), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the ''Exchange Act''), and in accordance therewith files reports, proxy statements and other information with the SEC. Such reports, proxy statements and other information may be inspected and copied at the public reference facilities maintained by the SEC at 450 Fifth Street, N.W., Washington, D.C. 20549 and at the SEC's regional offices at 7 World Trade Center, New York, New York 10048 and Northwestern Atrium Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. Copies of such material can be obtained from the public reference section of the SEC at 450 Fifth Street, N.W., Washington, D.C. 20549 at prescribed rates. In addition, the aforementioned material may also be inspected at the offices of the New York Stock Exchange, Inc. (the ''NYSE'') at 20 Broad Street, New York, New York 10005. Ambac Financial's Common Stock is listed on the NYSE.

Copies of Ambac Assurance's financial statements prepared in accordance with statutory accounting standards are available from Ambac Assurance. The address of Ambac Assurance's administrative offices and its telephone number are One State Street Plaza, 17th Floor, New York, New York 10004 and (212) 668-0340.

Incorporation of Certain Documents by Reference. The following documents filed by Ambac Financial with the SEC (File No. 1-10777) are incorporated by reference in this Official Statement:

(1) Ambac Financial's Annual Report on *Form 10-K* for the fiscal year ended December 31, 1997 and filed on March 31, 1998;

(2) Ambac Financial's Current Report on *Form 8-K* dated March 27, 1998 and filed on March 27, 1998; and

(3) Ambac Financial's Amendment to its Annual Report on *Form 10-K/A* for the fiscal year ended December 31, 1997 and filed on March 31, 1998;

All documents subsequently filed by Ambac Financial pursuant to the requirements of the Exchange Act after the date of this Official Statement will be available for inspection in the same manner as described above in "Available Information".

TAX MATTERS

Offered Securities—Federal Tax Matters

In the opinion of Hawkins, Delafield & Wood, New York, New York, Bond Counsel to LIPA ("Bond Counsel"), under existing statutes and court decisions, interest on the Tax-Exempt Offered Securities (i.e., all of the Offered Securities except for the Taxable Bonds indicated on the inside cover page) is not included in gross income for federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended to the date of initial issuance and delivery of the Tax-Exempt Offered Securities (as used in this section, the "Code"). Under the Code, interest on the Tax-Exempt Offered Securities is not treated as a preference item in calculating the federal alternative minimum tax that may be imposed on individuals and corporations; such interest, however, is included in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations by the Code. In rendering the foregoing opinions, Bond Counsel has assumed (i) the material accuracy of the representations, statements of intention and reasonable expectations and certifications of facts contained in the Arbitrage and Use of Proceeds Certificate delivered by LIPA and LIPA Sub with respect to the use of the proceeds of the Tax-Exempt Offered Securities and the investment of certain funds, and other matters affecting the non-inclusion of interest on the Tax-Exempt Offered Securities in gross income for federal income tax purposes under Section 103 of the Code and (ii) future compliance by LIPA and LIPA Sub with the procedures set forth in the Arbitrage and Use of Proceeds Certificate and the tax covenants. Furthermore, Bond Counsel expresses no opinion as to the effect of any action taken or not taken in reliance upon an opinion of counsel other than themselves on the exclusion from gross income for federal income tax purposes of interest on the Tax-Exempt Offered Securities, or under state and local tax laws.

Certain Requirements of the Code

The Code establishes certain requirements that must be met subsequent to the issuance and delivery of the Tax-Exempt Offered Securities in order that interest on the Tax-Exempt Offered Securities be and remain not included in gross income for federal income tax purposes under Section 103 of the Code. Noncompliance by LIPA or LIPA Sub with such requirements may require inclusion of interest on the Tax-Exempt Offered Securities in gross income retroactive to the date of issuance of the Tax-Exempt Offered Securities, regardless of when such noncompliance occurs or is ascertained. LIPA and LIPA Sub have covenanted that they will not take or omit to take or permit any person to

take or omit to take any action which would cause interest on the Tax-Exempt Offered Securities to be included in the gross income of any Tax-Exempt Offered Security owner for federal income tax purposes by reason of Section 103(b) of the Code as now in effect.

Certain Additional Federal Tax Consequences

The following is a brief discussion of certain federal income tax matters with respect to the Tax-Exempt Offered Securities under existing statutes. It does not address all aspects of federal taxation that may be relevant to a particular owner of a Tax-Exempt Offered Security. Prospective investors, particularly those who may be subject to special rules, are advised to consult their own tax advisors regarding the federal tax consequences of owning and disposing of the Tax-Exempt Offered Securities.

As noted above, interest on the Tax-Exempt Offered Securities must be taken into account in determining the tax liability of corporations subject to the federal alternative minimum tax imposed by Section 55 of the Code. Interest on the Tax-Exempt Offered Securities must also be taken into account in determining the tax liability of foreign corporations subject to the branch profits tax imposed by Section 884 of the Code.

Owners of Tax-Exempt Offered Bonds should be aware that the ownership of such obligations may result in collateral federal income tax consequences to various categories of persons, such as corporations (including S Corporations and certain foreign corporations), financial institutions, property and casualty insurance companies, individual recipients of Social Security or railroad retirement benefits and individuals otherwise eligible for the earned income tax credit, and to taxpayers deemed to have incurred or continued indebtedness to purchase or carry obligations the interest on which is not included in gross income for federal income tax purposes.

Owners of Tax-Exempt Offered Securities subject to any such taxes, or who might fall into any such category, should consult their own tax advisors as to the computation of any such tax and the applicability of these and other tax consequences.

Original Issue Discount

Bond Counsel is of the opinion that the original issue discount, if any, on the Tax-Exempt Offered Securities that is properly allocable to any owner thereof is not includable in gross income for federal income tax purposes to the same extent as the interest on the Tax-Exempt Offered Securities, as described above. Original issue discount is the excess, if any, of the sum of all payments provided by a maturity of Tax-Exempt Offered Securities (excluding certain ''qualified stated interest'' that is unconditionally payable at least annually at prescribed rates) over the ''issue price,'' generally equal to the initial public offering price of such maturity. In connection with the preceding sentence, all accreted interest on the Capital Appreciation Bonds is original issue discount and the ''initial public offering price'' refers to the initial offering price to the public (excluding bond houses, brokers or similar persons acting in the capacity of underwriters or wholesalers) at which a substantial amount of the Tax-Exempt Offered Securities comprising a maturity was first sold.

Under Section 1288 of the Code, original issue discount accrues in accordance with a constant interest method based on the compounding of interest, and an owner's adjusted basis in a Tax-Exempt Offered Security having original issue discount (a ''Discount Bond'') for purposes of determining gain or loss on disposition will be increased by the amount of any such accrual. A portion of the original issue discount that accrues in each year to an owner of a Discount Bond that is a corporation will be included in the calculation of the corporation's federal alternative minimum tax liability.

Consequently, corporate owners of a Discount Bond should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability even though such owners have not received a corresponding cash payment.

Owners of Discount Bonds should consult their own tax advisors with respect to treatment of original issue discount for federal income tax purposes, including various special rules relating thereto, and state and local tax consequences, in connection with the acquisition, ownership and disposition of Discount Bonds.

Bond Premium

In general, if an owner acquires a Tax-Exempt Offered Security for a purchase price (excluding accrued interest) or otherwise at a tax basis that reflects a premium over the sum of all amounts payable on the Bond after the acquisition date (excluding certain "qualified stated interest" that is unconditionally payable at least annually at prescribed rates), that Bond (a "Premium Bond") will have bond premium. In general, under Section 171 of the Code, an owner of a Premium Bond must amortize the bond premium over the remaining term of the Premium Bond, based on the owner's yield over the remaining term of the Premium Bond, determined on the basis of constant yield principles. An owner of a Premium Bond must amortize the bond premium by offsetting the qualified stated interest allocable to each interest accrual period, under the owner's regular method of accounting, against the bond premium allocable to that period. In the case of a tax-exempt bond, such as a Tax-Exempt Offered Security, that is a Premium Bond, if the bond premium allocable to an accrual period exceeds the qualified stated interest allocable to that accrual period, the excess is a nondeductible loss. Under certain circumstances, the owner of a Premium Bond may realize a taxable gain upon disposition of the Premium Bond even though it is sold or redeemed for an amount less than or equal to the owner's original acquisition cost.

The owner of any Premium Bond should consult its own tax advisors with respect to the treatment of bond premium for federal income tax purposes, including various special rules relating thereto, and state and local tax consequences, in connection with the acquisition, ownership, and disposition of such Premium Bond.

Certain Proposed Federal Tax Legislation

Legislation affecting municipal bonds is constantly being considered by the United States Congress. There can be no assurance that legislation enacted or proposed after the date of issuance of the Tax-Exempt Offered Securities will not have an adverse effect on the tax-exempt status or market price of the Tax-Exempt Offered Securities or on LIPA's ability to issue subsequent tax-exempt obligations and to complete the Plan of Finance.

In November 1997, Senator Murkowski introduced legislation (the "Murkowski Bill"), which was proposed to apply to sales of electric output after November 8, 1997 and which proposes: (i) to treat certain specified limited transactions involving electric output facilities (which includes transmission, distribution and generation facilities) as not giving rise to nonqualified private business use under Code Section 141(b) (8); and (ii) to permit an issuer which has issued tax-exempt bonds to finance an electric output facility to take certain actions to preserve the tax-exempt status of those bonds after it begins to participate in a defined open access plan for energy competition or transmission wheeling allowed by FERC. If enacted in its present form, the Murkowski Bill could be interpreted to have an adverse effect on the tax-exempt status of the tax-exempt obligations of LIPA issued to finance

output facilities, which would include the Offered Securities, including a retroactive adverse effect on any such obligations (including the Offered Securities), issued prior to the date of enactment of the Murkowski Bill. It is not possible to predict the effect or outcome of this proposed legislation. In introducing the Murkowski Bill, Sen. Murkowski stated "No one wants to see bonds issued to finance public power become retroactively taxable . . . [t]hat would cause havoc in the financial markets," and furthermore referred to the legislation as a "starting point for discussion." There can be no assurance that legislation enacted or proposed after the date of issuance of the Tax-Exempt Offered Securities, including, without limitation, the Murkowski Bill, will not have an adverse effect on the tax-exempt status or market price of the tax-exempt obligations of LIPA issued to finance output facilities, including the Offered Securities.

Taxable Bonds

The interest on the federally Taxable Bonds, which are indicated on the inside cover page of this Official Statement, is includable in gross income for federal income tax purposes.

Bond Premium on a Taxable Bond

In general, if an owner acquires a Taxable Bond for a purchase price (excluding accrued interest) or otherwise at a tax basis that reflects a premium over the sum of all amounts payable on the Bond after the acquisition date (excluding certain "qualified stated interest" that is unconditionally payable at least annually at prescribed rates), that Bond (a "Premium Taxable Bond") will have bond premium. In general, under Section 171 of the Code, an owner of a Premium Taxable Bond may either deduct the bond premium under Section 171(a)(1) or may elect under Section 171(c) of the Code to amortize that premium as "amortizable bond premium" over the remaining term of the Premium Taxable Bond, based on the owner's yield over the remaining term of the Premium Taxable Bond, determined on the basis of constant yield principles. An owner of a Premium Taxable Bond that so elects amortizes the amortizable bond premium by offsetting the qualified stated interest allocable to each interest accrual period, under the owner's regular method of accounting, against the bond premium allocable to that period. If the bond premium allocable to an accrual period exceeds the qualified stated interest allocable to that accrual period, the excess is treated as a bond premium deduction under Section 171(a)(1) of the Code, subject to certain limitations. Under certain circumstances, the owner of a Premium Taxable Bond may realize a taxable gain upon disposition of the Premium Taxable Bond even though it is sold or redeemed for an amount less than or equal to the owner's original acquisition cost.

Owners of a Premium Taxable Bond should consult their own tax advisors with respect to the treatment of bond premium for Federal Income tax purposes, including various special rules relating thereto, and state and local tax consequences, in connection with the acquisition, ownership, and disposition of Premium Taxable Bonds.

Backup Withholding and Information Reporting for U.S. Holders of Taxable Bonds

In general, information reporting requirements will apply to non-corporate U.S. Holders with respect to payments of the principal of, and interest on, a Taxable Bond and the proceeds of the sale of a Taxable Bond before maturity within the United States. Backup withholding at a rate of 31% will apply to such payments unless the U.S. Holder (i) is a corporation or other exempt recipient and, when required, demonstrates that fact, or (ii) provides a correct taxpayer identification number, certifies under penalties of perjury, when required, that such U.S. Holder is not subject to backup withholding and has not been notified by the IRS that it has failed to report all interest and dividends required to be shown on its United States federal income tax returns.

As used herein, the term "U.S. Holder" means a beneficial owner of a Taxable Bond that is for United States federal income tax purposes (w) a citizen or resident of the United States, (x) a corporation, partnership or other entity created or organized in or under the laws of the United States or of any political subdivision thereof, (y) an estate the income of which is subject to United States federal income taxation regardless of its source or (z) a trust whose administration is subject to the primary jurisdiction of a United States court and which has one or more United States fiduciaries who have the authority to control all substantial decisions of the trust.

New York State Tax Matters

It is also the opinion of Bond Counsel that, under existing statutes, interest on all the Offered Securities is exempt from personal income taxes imposed by the State of New York or any political subdivision thereof, and the Offered Securities are exempt from all taxation directly imposed thereon by or under the authority of the State of New York, except estate or gift taxes and taxes on transfers.

CORPORATE INCOME TAX RULINGS

As contemplated by the LIPA/LILCO Merger Agreement, LIPA together with LILCO and KeySpan have obtained a private letter ruling from the Internal Revenue Service ("IRS") containing two rulings on certain federal corporate income tax matters in connection with the acquisition of LILCO by LIPA. One of those rulings holds that the public utility income of LILCO after it becomes LIPA Sub will be excluded from LIPA Sub's gross income for federal income tax purposes, i.e., that such income will be exempt from federal income taxation. The other ruling holds that LILCO will not recognize any taxable gain under certain sections of the Code, either as a result of the acquisition of its stock by LIPA or as a result of LIPA Sub's public utility income becoming exempt from federal income tax. Both of these rulings are based on the facts presented to the IRS and are subject to certain conditions and qualifications.

Following LIPA's acquisition of all the stock of LILCO, the certificate of incorporation of LILCO will be amended to meet the requirements of the first ruling. This ruling provides that, because LIPA Sub's activities while it is a subsidiary of LIPA will be limited to its activities as a public electric utility, LIPA Sub's income, including any income attributable to regulatory assets, will be excluded from LIPA Sub's gross income while it is a wholly-owned subsidiary of LIPA. While the ruling exempts the public utility income of LIPA Sub from federal income tax, LIPA Sub will continue to file federal income tax returns as a separate, otherwise taxable corporation.

The other ruling holds that LILCO will not recognize gain as a result of either LIPA's acquisition of the LILCO stock and the amendment of LILCO's certificate of incorporation described above or the subsequent exclusion of LIPA Sub's income from federal income taxation. The ruling expresses no opinion as to the tax treatment of future actual or constructive dispositions of assets by LIPA Sub, including the application of the depreciation recapture rules of the Code (which may require the recognition of income on a disposition of depreciated assets even if the disposition is otherwise not taxable). Thus, if LIPA Sub sells or otherwise disposes of assets after it becomes a subsidiary of LIPA, the ruling may not apply to prevent the recognition of taxable gain or losses by LIPA Sub on such sales or dispositions.

The rulings are based in part on the conclusion of the IRS that LIPA Sub will not become an "integral part" of LIPA as a result of the transaction or at any time thereafter. That conclusion in turn was based on a number of representations by LIPA with respect to the absence of any financial or

other support for LIPA Sub from LIPA and other agencies of the State of New York. The ruling from the IRS provides expressly that, if "the facts and circumstances in the future are other than as contemplated" by the representations in the ruling, LIPA and LIPA Sub "should seek an appropriate supplemental ruling" from the IRS with respect to the presence or absence of state support for LILCO and the effect of such state support on the status of LIPA Sub and the original rulings. LIPA has covenanted that it shall not, nor shall it permit LIPA Sub to, do or omit to do any act that would result in the revocation of the rulings and a resultant material federal income tax liability.

The rulings described above are generally binding on the IRS, subject to a change in law, and are based upon the representations described above and the other facts presented to the IRS by LILCO and LIPA. If these representations or the facts of the transactions as presented to the IRS were incorrect in a material respect or omitted to present a material fact, the rulings could be revoked. LIPA is not aware of any facts or circumstances which would cause such representations or the facts as presented to be untrue or incomplete in any material respect. If the rulings were revoked, LIPA Sub could be subject to significant federal income tax liability unless LIPA Sub were otherwise exempt from federal taxation under applicable provisions of the Code.

PACB APPROVALS

On April 22, 1998, the PACB approved the issuance of the Offered Securities and the Initial Subordinated Indebtedness.

For a description of the PACB approvals of the LIPA/LILCO Merger, certain conditions of the PACB relating thereto and LIPA's plan to satisfy such conditions, see "Public Authorities Control Board" in Part 2 of this Official Statement.

UNDERWRITING

The underwriters listed on the cover page hereof (the "Underwriters") have jointly and severally agreed, subject to certain conditions, to purchase all, but not less than all, of the Tax Exempt Offered Securities from LIPA at an underwriters' discount of $21,137,780.34. The Underwriters will be obligated to purchase all of the Tax Exempt Offered Securities if any are purchased. The initial public offering prices of the Tax Exempt Offered Securities may be changed, from time to time, by the Underwriters.

J.P. Morgan Securities, Inc. (one of the Underwriters) has agreed, subject to certain conditions, to purchase all, but not less than all, of the Taxable Bonds at an Underwriter's discount of $31,250.00. J.P. Morgan Securities, Inc. will be obligated to purchase all of the Taxable Bonds if any are purchased. The initial public offering prices of the Taxable Bonds may be changed, from time to time, by J.P. Morgan Securities, Inc.

The Offered Securities may be offered and sold to certain dealers (including the Underwriters and other dealers depositing Offered Securities into investment trusts) at prices lower than such public offering prices.

It is a condition to the issuance and delivery of the Offered Securities that the Offered Securities and the Initial Subordinated Indebtedness be issued and delivered simultaneously.

OTHER RELATIONSHIPS

Certain of the Underwriters have provided, from time to time, financial advisory, investment or commercial banking services to LIPA, LILCO and/or KeySpan and their respective affiliates, for which such Underwriters have received and will receive customary fees and commissions. Bear, Stearns & Co. Inc., the representative of the Underwriters, served as financial advisor to LIPA from October 1995 through December 1997 and $4,000,000 of its compensation for the rendering of such services is contingent upon the completion of the LIPA/LILCO Merger Transaction. Merrill Lynch, Pierce, Fenner & Smith, Inc. served as financial advisor to KeySpan regarding the merger with LILCO and $9,000,000 of Merrill Lynch's fee for such services is contingent upon the consummation of the proposed LILCO/KeySpan merger. Certain of the Underwriters currently serve as remarketing agents for the variable rate debt issued by the New York State Energy Research and Development Authority for the benefit of LILCO and may serve as remarketing agents for LIPA Subordinated Indebtedness issued as variable rate debt.

In addition, in the ordinary course of sales, trading, brokerage and financing activities, certain of the Underwriters may at any time hold long or short positions and may trade or otherwise effect transactions, for their own account or the account of customers, in debt or equity securities or senior loans of LILCO and/or KeySpan and their respective affiliates.

CONTINUING DISCLOSURE CERTIFICATE

The Offered Securities will be subject to the Continuing Disclosure Certificate referred to under "Additional Information and Continuing Disclosure Undertakings for the Offered Securities" in Part 2 of this Official Statement. The Offered Securities being subject to the Continuing Disclosure Certificate is a condition precedent to the obligation of the Underwriters to purchase the Offered Securities.

CREDIT RATINGS

Offered Securities

It is a condition to the obligation of the Underwriters to purchase the Offered Securities that, at the date of delivery thereof to the Underwriters, (i) the Insured Offered Securities be rated "AAA" by Fitch IBCA, Inc. ("Fitch"), "Aaa" by Moody's Investors Services, Inc. ("Moody's") and "AAA" by Standard & Poor's Ratings Services, a division of the McGraw-Hill Companies, Inc. ("S&P") and (ii) the remainder of the Offered Securities be rated "A-" by Fitch, "Baa1" by Moody's and "A-" by S&P. The Insured Offered Securities are expected to be assigned such long-term ratings upon, and solely as a result of, the issuance of the Bond Insurance Policies relating thereto. See "Bond Insurance" and Appendices 3 and 4 to this Part 1.

General

The respective ratings by Fitch, Moody's and S&P of the Insured Offered Securities and the uninsured remainder of the Offered Securities reflect only the views of such organizations and any desired explanation of the significance of such ratings and any outlooks or other statements given by the rating agencies with respect thereto should be obtained from the rating agency furnishing the same, at the following addresses: Fitch IBCA, Inc., One State Street Plaza, New York, New York 10004, Moody's Investors Service, Inc., 99 Church Street, New York, New York 10007 and Standard & Poor's Ratings Services, 25 Broadway, New York, New York 10004. Generally, a rating agency bases

its rating and outlook (if any) on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance such ratings for either the Insured Offered Securities or the uninsured remainder of the Offered Securities will continue for any given period of time or that any of such ratings will not be revised downward or withdrawn entirely by any of the rating agencies if, in the judgment of such rating agency or agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Offered Securities.

APPROVAL OF LEGAL PROCEEDINGS

Hawkins, Delafield & Wood, New York, New York, Bond Counsel to LIPA, will render opinions with respect to the validity of the Offered Securities in substantially the form set forth in Appendix 2 to this Part 1. Certain legal matters with respect to this Official Statement will be passed upon for LIPA by Orrick, Herrington & Sutcliffe LLP, New York, New York, Disclosure Counsel to LIPA. Certain legal matters with respect to LIPA will be passed upon for LIPA by Stanley B. Klimberg, Esquire, General Counsel to LIPA, and by Winthrop, Stimson, Putnam & Roberts, New York, New York, Corporate Counsel to LIPA. In addition, certain legal matters will be passed upon for LIPA by Rivkin, Radler & Kremer, Uniondale, New York, Special Counsel to LIPA; Adams, Dayter & Sheehan, LLP, Albany, New York, State Regulatory Counsel to LIPA; and Van Ness Feldman P.C., Washington, D.C., Federal Regulatory Counsel to LIPA. Certain legal matters will be passed upon for the Underwriters by Nixon, Hargrave, Devans & Doyle LLP, New York, New York, Counsel to the Underwriters.

See "Public Authorities Control Board—Litigation Relating to PACB Merger Approval" in Part 2 of this Official Statement for a description of certain litigation in which LIPA and others are defendants and the opinions of litigation counsel to LIPA with respect to such litigation.

MISCELLANEOUS

This Official Statement (which consists of Part 1 and Part 2) includes, among other things, descriptions of (i) LIPA, LIPA Sub and their relationship and the T&D System and NMP2 and (ii) the terms of the Offered Securities, the Operating Agreements, the LIPA/LILCO Merger Agreement, the Resolution, the Continuing Disclosure Certificate, the Bond Insurers, the Bond Insurance Policies and certain provisions of the LIPA Act. Such descriptions are not complete and all such descriptions and references thereto are qualified by reference to each such document, copies of which may be obtained from LIPA.

The agreements with the holders of the Offered Securities are fully set forth in the Resolution. This Official Statement is not to be construed as a contract with the purchasers of the Offered Securities or of any other obligations of LIPA.

This Official Statement has been approved by the Trustees of LIPA and has been executed on behalf of LIPA by the Chairman of its Trustees pursuant to the authority of the Trustees.

LONG ISLAND POWER AUTHORITY

By: /s/ RICHARD M. KESSEL
Chairman

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APPENDIX 1

ACCRETED VALUE TABLES
(Per $5,000 Maturity Amount)

The following table illustrates the accretion of the Capital Appreciation Bonds, on the basis of semiannual compounding of the difference between the amounts payable at maturity and the initial public offering price per $5,000 maturity amount shown on the inside cover page. LIPA is not obligated to pay, or to provide for the payment of, any amounts on the Capital Appreciation Bonds prior to their date of maturity. *No representation is made that the accreted values presented below bear or will bear any relationship to the market prices of the Capital Appreciation Bonds. The market prices of the Capital Appreciation Bonds are expected to be more volatile than those of the Current Interest Bonds.*

ACCRETED VALUE TABLES
(Per $5,000 Maturity Amount)

Interest Accretion Date	Bonds Due December 1, 2003	2004	2005	2006	2007	2008	2009	2010	2011
December 1, 1998	4,022.15	3,828.30	3,636.70	3,447.95	3,277.00	3,111.50	2,935.65	2,764.35	2,614.50
June 1, 1999	4,110.65	3,914.45	3,720.35	3,529.00	3,354.85	3,186.15	3,007.55	2,833.45	2,680.55
December 1, 1999	4,201.05	4,002.55	3,805.90	3,611.90	3,434.50	3,262.65	3,081.25	2,904.30	2,748.20
June 1, 2000	4,293.50	4,092.60	3,893.45	3,696.80	3,516.10	3,340.95	3,156.75	2,976.90	2,817.60
December 1, 2000	4,387.95	4,184.65	3,983.00	3,783.65	3,599.60	3,421.10	3,234.10	3,051.35	2,888.75
June 1, 2001	4,484.50	4,278.80	4,074.60	3,872.60	3,685.05	3,503.20	3,313.30	3,127.60	2,961.70
December 1, 2001	4,583.15	4,375.10	4,168.35	3,963.60	3,772.60	3,587.30	3,394.50	3,205.80	3,036.50
June 1, 2002	4,684.00	4,473.55	4,264.20	4,056.75	3,862.20	3,673.40	3,477.65	3,285.95	3,113.15
December 1, 2002	4,787.05	4,574.20	4,362.30	4,152.05	3,953.90	3,761.55	3,562.85	3,368.10	3,191.75
June 1, 2003	4,892.35	4,677.10	4,462.60	4,249.65	4,047.85	3,851.85	3,650.15	3,452.30	3,272.35
December 1, 2003	5,000.00	4,782.35	4,565.25	4,349.50	4,143.95	3,944.30	3,739.60	3,538.60	3,355.00
June 1, 2004		4,889.95	4,670.25	4,451.75	4,242.40	4,038.95	3,831.20	3,627.10	3,439.70
December 1, 2004		5,000.00	4,777.65	4,556.35	4,343.15	4,135.90	3,925.05	3,717.75	3,526.55
June 1, 2005			4,887.55	4,663.40	4,446.30	4,235.15	4,021.25	3,810.70	3,615.60
December 1, 2005			5,000.00	4,773.00	4,551.90	4,336.80	4,119.75	3,905.95	3,706.90
June 1, 2006				4,885.15	4,660.00	4,440.85	4,220.70	4,003.60	3,800.50
December 1, 2006				5,000.00	4,770.70	4,547.45	4,324.10	4,103.70	3,896.45
June 1, 2007					4,884.00	4,656.60	4,430.05	4,206.30	3,994.85
December 1, 2007					5,000.00	4,768.35	4,538.60	4,311.45	4,095.70
June 1, 2008						4,882.80	4,649.75	4,419.25	4,199.15
December 1, 2008						5,000.00	4,763.70	4,529.75	4,305.15
June 1, 2009							4,880.40	4,642.95	4,413.85
December 1, 2009							5,000.00	4,759.05	4,525.30
June 1, 2010								4,878.00	4,639.60
December 1, 2010								5,000.00	4,756.75
June 1, 2011									4,876.85
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ACCRETED VALUE TABLES (continued)
(Per $5,000 Maturity Amount)

Interest Accretion Date	Bonds Due December 1, 2012	2013	2014	2015	2016	2017	2018	2019	2020
December 1, 1998	2,470.40	2,331.95	2,199.10	2,071.85	1,967.20	1,857.50	1,763.20	1,673.65	1,581.85
June 1, 1999	2,533.40	2,392.00	2,256.30	2,126.25	2,018.85	1,906.55	1,809.75	1,717.85	1,623.80
December 1, 1999	2,598.00	2,453.60	2,314.95	2,182.05	2,071.85	1,956.90	1,857.50	1,763.20	1,666.80
June 1, 2000	2,664.25	2,516.80	2,375.15	2,239.30	2,126.25	2,008.55	1,906.55	1,809.75	1,711.00
December 1, 2000	2,732.20	2,581.60	2,436.90	2,298.10	2,182.05	2,061.55	1,956.90	1,857.50	1,756.35
June 1, 2001	2,801.85	2,648.05	2,500.25	2,358.45	2,239.30	2,116.00	2,008.55	1,906.55	1,802.85
December 1, 2001	2,873.30	2,716.25	2,565.30	2,420.35	2,298.10	2,171.85	2,061.55	1,956.90	1,850.65
June 1, 2002	2,946.55	2,786.20	2,632.00	2,483.90	2,358.45	2,229.20	2,116.00	2,008.55	1,899.70
December 1, 2002	3,021.70	2,857.95	2,700.40	2,549.10	2,420.35	2,288.05	2,171.85	2,061.55	1,950.05
June 1, 2003	3,098.75	2,931.55	2,770.60	2,616.00	2,483.90	2,348.45	2,229.20	2,116.00	2,001.70
December 1, 2003	3,177.80	3,007.00	2,842.65	2,684.65	2,549.10	2,410.45	2,288.05	2,171.85	2,054.75
June 1, 2004	3,258.80	3,084.45	2,916.55	2,755.15	2,616.00	2,474.10	2,348.45	2,229.20	2,109.20
December 1, 2004	3,341.90	3,163.85	2,992.40	2,827.45	2,684.65	2,539.40	2,410.45	2,288.05	2,165.10
June 1, 2005	3,427.15	3,245.35	3,070.20	2,901.70	2,755.15	2,606.45	2,474.10	2,348.45	2,222.50
December 1, 2005	3,514.55	3,328.90	3,150.05	2,977.85	2,827.45	2,675.25	2,539.40	2,410.45	2,281.35
June 1, 2006	3,604.15	3,414.65	3,231.95	3,056.00	2,901.70	2,745.90	2,606.45	2,474.10	2,341.85
December 1, 2006	3,696.05	3,502.55	3,315.95	3,136.25	2,977.85	2,818.40	2,675.25	2,539.40	2,403.90
June 1, 2007	3,790.30	3,592.75	3,402.15	3,218.55	3,056.00	2,892.80	2,745.90	2,606.45	2,467.60
December 1, 2007	3,886.95	3,685.25	3,490.65	3,303.05	3,136.25	2,969.15	2,818.40	2,675.25	2,533.00
June 1, 2008	3,986.10	3,780.15	3,581.40	3,389.75	3,218.55	3,047.55	2,892.80	2,745.90	2,600.10
December 1, 2008	4,087.75	3,877.50	3,674.50	3,478.75	3,303.05	3,128.00	2,969.15	2,818.40	2,669.00
June 1, 2009	4,191.95	3,977.35	3,770.05	3,570.05	3,389.75	3,210.60	3,047.55	2,892.80	2,739.75
December 1, 2009	4,298.85	4,079.75	3,868.05	3,663.80	3,478.75	3,295.35	3,128.00	2,969.15	2,812.35
June 1, 2010	4,408.50	4,184.80	3,968.65	3,759.95	3,570.05	3,382.35	3,210.60	3,047.55	2,886.90
December 1, 2010	4,520.90	4,292.60	4,071.80	3,858.65	3,663.80	3,471.65	3,295.35	3,128.00	2,963.40
June 1, 2011	4,636.20	4,403.10	4,177.70	3,959.95	3,759.95	3,563.30	3,382.35	3,210.60	3,041.90
December 1, 2011	4,754.40	4,516.50	4,286.30	4,063.90	3,858.65	3,657.35	3,471.65	3,295.35	3,122.50
June 1, 2012	4,875.65	4,632.80	4,397.75	4,170.55	3,959.95	3,753.90	3,563.30	3,382.35	3,205.25
December 1, 2012	5,000.00	4,752.10	4,512.10	4,280.05	4,063.90	3,853.00	3,657.35	3,471.65	3,290.20
June 1, 2013		4,874.45	4,629.40	4,392.40	4,170.55	3,954.75	3,753.90	3,563.30	3,377.40
December 1, 2013		5,000.00	4,749.75	4,507.70	4,280.05	4,059.15	3,853.00	3,657.35	3,466.90
June 1, 2014			4,873.25	4,626.05	4,392.40	4,166.30	3,954.75	3,753.90	3,558.80
December 1, 2014			5,000.00	4,747.45	4,507.70	4,276.30	4,059.15	3,853.00	3,653.10
June 1, 2015				4,872.10	4,626.05	4,389.20	4,166.30	3,954.75	3,749.90
December 1, 2015				5,000.00	4,747.45	4,505.05	4,276.30	4,059.15	3,849.25
June 1, 2016					4,872.10	4,624.00	4,389.20	4,166.30	3,951.25
December 1, 2016					5,000.00	4,746.05	4,505.05	4,276.30	4,056.00
June 1, 2017						4,871.35	4,624.00	4,389.20	4,163.45
December 1, 2017						5,000.00	4,746.05	4,505.05	4,273.80
June 1, 2018							4,871.35	4,624.00	4,387.05
December 1, 2018							5,000.00	4,746.05	4,503.30
June 1, 2019								4,871.35	4,622.65
December 1, 2019								5,000.00	4,745.15
June 1, 2020									4,870.90
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ACCRETED VALUE TABLES (continued)
(Per $5,000 Maturity Amount)

Interest Accretion Date	Bonds Due December 1, 2021	2022	2023	2024	2025	2026	2027	2028
December 1, 1998	1,501.25	1,424.75	1,352.10	1,283.20	1,217.80	1,155.75	1,096.85	1,040.95
June 1, 1999	1,541.05	1,462.50	1,387.95	1,317.20	1,250.10	1,186.35	1,125.90	1,068.50
December 1, 1999	1,581.85	1,501.25	1,424.75	1,352.10	1,283.20	1,217.80	1,155.75	1,096.85
June 1, 2000	1,623.80	1,541.05	1,462.50	1,387.95	1,317.20	1,250.10	1,186.35	1,125.90
December 1, 2000	1,666.80	1,581.85	1,501.25	1,424.75	1,352.10	1,283.20	1,217.80	1,155.75
June 1, 2001	1,711.00	1,623.80	1,541.05	1,462.50	1,387.95	1,317.20	1,250.10	1,186.35
December 1, 2001	1,756.35	1,666.80	1,581.85	1,501.25	1,424.75	1,352.10	1,283.20	1,217.80
June 1, 2002	1,802.85	1,711.00	1,623.80	1,541.05	1,462.50	1,387.95	1,317.20	1,250.10
December 1, 2002	1,850.65	1,756.35	1,666.80	1,581.85	1,501.25	1,424.75	1,352.10	1,283.20
June 1, 2003	1,899.70	1,802.85	1,711.00	1,623.80	1,541.05	1,462.50	1,387.95	1,317.20
December 1, 2003	1,950.05	1,850.65	1,756.35	1,666.80	1,581.85	1,501.25	1,424.75	1,352.10
June 1, 2004	2,001.70	1,899.70	1,802.85	1,711.00	1,623.80	1,541.05	1,462.50	1,387.95
December 1, 2004	2,054.75	1,950.05	1,850.65	1,756.35	1,666.80	1,581.85	1,501.25	1,424.75
June 1, 2005	2,109.20	2,001.70	1,899.70	1,802.85	1,711.00	1,623.80	1,541.05	1,462.50
December 1, 2005	2,165.10	2,054.75	1,950.05	1,850.65	1,756.35	1,666.80	1,581.85	1,501.25
June 1, 2006	2,222.50	2,109.20	2,001.70	1,899.70	1,802.85	1,711.00	1,623.80	1,541.05
December 1, 2006	2,281.35	2,165.10	2,054.75	1,950.05	1,850.65	1,756.35	1,666.80	1,581.85
June 1, 2007	2,341.85	2,222.50	2,109.20	2,001.70	1,899.70	1,802.85	1,711.00	1,623.80
December 1, 2007	2,403.90	2,281.35	2,165.10	2,054.75	1,950.05	1,850.65	1,756.35	1,666.80
June 1, 2008	2,467.60	2,341.85	2,222.50	2,109.20	2,001.70	1,899.70	1,802.85	1,711.00
December 1, 2008	2,533.00	2,403.90	2,281.35	2,165.10	2,054.75	1,950.05	1,850.65	1,756.35
June 1, 2009	2,600.10	2,467.60	2,341.85	2,222.50	2,109.20	2,001.70	1,899.70	1,802.85
December 1, 2009	2,669.00	2,533.00	2,403.90	2,281.35	2,165.10	2,054.75	1,950.05	1,850.65
June 1, 2010	2,739.75	2,600.10	2,467.60	2,341.85	2,222.50	2,109.20	2,001.70	1,899.70
December 1, 2010	2,812.35	2,669.00	2,533.00	2,403.90	2,281.35	2,165.10	2,054.75	1,950.05
June 1, 2011	2,886.90	2,739.75	2,600.10	2,467.60	2,341.85	2,222.50	2,109.20	2,001.70
December 1, 2011	2,963.40	2,812.35	2,669.00	2,533.00	2,403.90	2,281.35	2,165.10	2,054.75
June 1, 2012	3,041.90	2,886.90	2,739.75	2,600.10	2,467.60	2,341.85	2,222.50	2,109.20
December 1, 2012	3,122.50	2,963.40	2,812.35	2,669.00	2,533.00	2,403.90	2,281.35	2,165.10
June 1, 2013	3,205.25	3,041.90	2,886.90	2,739.75	2,600.10	2,467.60	2,341.85	2,222.50
December 1, 2013	3,290.20	3,122.50	2,963.40	2,812.35	2,669.00	2,533.00	2,403.90	2,281.35
June 1, 2014	3,377.40	3,205.25	3,041.90	2,886.90	2,739.75	2,600.10	2,467.60	2,341.85
December 1, 2014	3,466.90	3,290.20	3,122.50	2,963.40	2,812.35	2,669.00	2,533.00	2,403.90
June 1, 2015	3,558.80	3,377.40	3,205.25	3,041.90	2,886.90	2,739.75	2,600.10	2,467.60
December 1, 2015	3,653.10	3,466.90	3,290.20	3,122.50	2,963.40	2,812.35	2,669.00	2,533.00
June 1, 2016	3,749.90	3,558.80	3,377.40	3,205.25	3,041.90	2,886.90	2,739.75	2,600.10
December 1, 2016	3,849.25	3,653.10	3,466.90	3,290.20	3,122.50	2,963.40	2,812.35	2,669.00
June 1, 2017	3,951.25	3,749.90	3,558.80	3,377.40	3,205.25	3,041.90	2,886.90	2,739.75
December 1, 2017	4,056.00	3,849.25	3,653.10	3,466.90	3,290.20	3,122.50	2,963.40	2,812.35
June 1, 2018	4,163.45	3,951.25	3,749.90	3,558.80	3,377.40	3,205.25	3,041.90	2,886.90
December 1, 2018	4,273.80	4,056.00	3,849.25	3,653.10	3,466.90	3,290.20	3,122.50	2.963.40
June 1, 2019	4,387.05	4,163.45	3,951.25	3,749.90	3,558.80	3,377.40	3,205.25	3,041.90
December 1, 2019	4,503.30	4,273.80	4,056.00	3,849.25	3,653.10	3,466.90	3,290.20	3,122.50
June 1, 2020	4,622.65	4,387.05	4,163.45	3,951.25	3,749.90	3,558.80	3,377.40	3,205.25
December 1, 2020	4,745.15	4,503.30	4,273.80	4,056.00	3,849.25	3,653.10	3,466.90	3,290.20
June 1, 2021	4,870.90	4,622.65	4,387.05	4,163.45	3,951.25	3,749.90	3,558.80	3,377.40
December 1, 2021	5,000.00	4,745.15	4,503.30	4,273.80	4,056.00	3,849.25	3,653.10	3,466.90
June 1, 2022		4,870.90	4,622.65	4,387.05	4,163.45	3,951.25	3,749.90	3,558.80
December 1, 2022		5,000.00	4,745.15	4,503.30	4,273.80	4,056.00	3,849.25	3,653.10
June 1, 2023			4,870.90	4,622.65	4,387.05	4,163.45	3,951.25	3,749.90
December 1, 2023			5,000.00	4,745.15	4,503.30	4,273.80	4,056.00	3,849.25
June 1, 2024				4,870.90	4,622.65	4,387.05	4,163.45	3,951.25
December 1, 2024				5,000.00	4,745.15	4,503.30	4,273.80	4,056.00
June 1, 2025					4,870.90	4,622.65	4,387.05	4,163.45
December 1, 2025					5,000.00	4,745.15	4,503.30	4,273.80
June 1, 2026						4,870.90	4,622.65	4,387.05
December 1, 2026						5,000.00	4,745.15	4,503.30
June 1, 2027							4,870.90	4,622.65
December 1, 2027							5,000.00	4,745.15
June 1, 2028								4,870.90
December 1, 2028								5,000.00

APPENDIX 2

Form of Opinion of Hawkins, Delafield & Wood
Relating to the Series 1998A Bonds

[Closing Date]

Long Island Power Authority
333 Earle Ovington Blvd.
Uniondale, NY 11553

Ladies and Gentlemen:

We have examined a certified record of proceedings relating to the issuance of $3,449,527,638.05 Electric System General Revenue Bonds, Series 1998A (the "Bonds") of the Long Island Power Authority (the "Authority"), a corporate municipal instrumentality of the State of New York (the "State") constituting a body corporate and politic and a political subdivision of the State.

The Bonds are issued under and pursuant to the Constitution and statutes of the State, including the Long Island Power Authority Act, being Title 1-a of Article 5 of the Public Authorities Law, Chapter 43-A of the Consolidated Laws of the State of New York, as amended (herein called the "Act"), and under and pursuant to proceedings of the Authority duly taken, including a resolution adopted by the Trustees of the Authority on May 13, 1998 entitled "Electric System General Revenue Bond Resolution" as supplemented by a resolution of said Trustees adopted on May 13, 1998 (collectively, the "Resolution").

The Bonds consist of Current Interest Bonds and Capital Appreciation Bonds, and are dated, mature, are payable, bear interest and are subject to redemption, all as provided in the Resolution.

We are of the opinion that:

1. The Authority is duly created and validly existing under the laws of the State, including the Constitution of the State and the Act. Under the laws of the State, including the Constitution of the State, and under the Constitution of the United States, the Act is valid with respect to all provisions thereof material to the subject matters of this opinion letter.

2. The Authority has the right and power under the Act to adopt the Resolution and to perform its obligations thereunder, including its rate covenant relating to the establishment and maintenance of System fees, rates, rents, charges and surcharges. The Authority has received all approvals of any governmental agency, board or commission necessary for the adoption of, or performance of its obligations under, the Resolution, including the approval of the New York State Public Authorities Control Board. The approval of the Public Authorities Control Board of the project being financed with the proceeds of the Bonds directs the Authority to obtain the approval of the New York State Public Service Commission prior to implementing certain rate increases.

3. The Resolution has been duly and lawfully adopted by the Authority, is in full force and effect, is valid and binding upon the Authority and is enforceable against the Authority in accordance with its terms. The Resolution creates the valid pledge which it purports to create of the Trust Estate (as defined in the Resolution), subject only to the provisions of the Resolution permitting the application thereof for the purposes and on the terms and conditions set forth in the Resolution.

4. The Bonds have been duly and validly authorized and issued in accordance with the laws of the State, including the Constitution of the State and the Act, and in accordance with the Resolution, and are valid and binding obligations of the Authority, enforceable against the Authority in accordance with their terms and the terms of the Resolution, payable solely from the Trust Estate as provided in the Resolution. The Authority has no taxing power, the Bonds are not debts of the State or of any municipality thereof, and the Bonds will not constitute a pledge of the credit, revenues or taxing power of the State or of any municipality thereof. The Authority reserves the right to issue additional bonds on the terms and conditions, and for the purposes, provided in the Resolution, on a parity of security and payment with the Bonds.

5. Any registration with, consent of, or approval by, any governmental agency, board, or commission that is necessary for the execution and delivery and the issuance of the Bonds has been obtained.

6. The adoption of the Resolution, compliance with all of the terms and conditions of the Resolution and the Bonds, and the execution and delivery of the Bonds, will not result in a violation of or be in conflict with any term or provision of any existing law, or of any approval by any governmental agency, board or commission necessary for the adoption of, or performance of the Authority's obligations under, the Resolution.

7. The Financing Agreement dated as of May 1, 1998, between the Authority and LIPA Acquisition Corp. (the ''Subsidiary'') has been duly authorized, executed and delivered by the Authority and the Subsidiary and is a valid and binding obligation of the parties thereto, enforceable against the Authority and the Subsidiary in accordance with its terms. You have received a separate opinion of Winthrop, Stimson, Putnam & Roberts, New York, New York, the Authority's Corporate Counsel, as to the due and valid creation and existence of the Subsidiary and as to certain other matters relating to the Subsidiary, all of which we have assumed, without further investigation, in rendering the opinions in this paragraph 7.

8. Under existing statutes, interest on the Bonds is exempt from personal income taxes imposed by the State or any political subdivision thereof, and the Bonds are exempt from all taxation directly imposed thereon by or under the authority of the State, except estate or gift taxes and taxes on transfers.

9. Under existing statutes and court decisions, interest on the Tax Exempt Bonds (i.e. all of the Bonds other than the Bonds maturing on December 1, 1999 in the principal amount of $25,000,000 and bearing interest at a rate of 5.94%) is not included in gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended to the date hereof (the ''Code''). Under the Code, interest on the Tax Exempt Bonds is not treated as a preference item in calculating alternative minimum taxable income for purposes of the alternative minimum tax applicable to individuals and corporations; such interest, however, is includable in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on corporations by the Code. In rendering the opinions in this paragraph 9, we have relied upon and assumed (i) the material accuracy of the representations, statements of intention and reasonable expectations, and certifications of fact contained in the Arbitrage and Use of Proceeds Certificate delivered on the date hereof by the Authority and the Subsidiary with respect to the use of proceeds of the Tax Exempt Bonds and the investment of certain funds, and other matters affecting the non-inclusion of interest on the Tax Exempt Bonds in gross income for Federal income tax purposes under Section 103 of the Code, and (ii) compliance by the Authority and the Subsidiary with procedures set forth in the Arbitrage and

Use of Proceeds Certificate and with tax covenants as to such tax matters. Under the Code, failure to comply with such procedures and covenants may cause the interest on the Tax Exempt Bonds to be included in gross income for Federal income tax purposes, retroactive to the date of issuance of the Tax Exempt Bonds, irrespective of the date on which such noncompliance occurs or is ascertained.

10. The original issue discount on the Current Interest Tax Exempt Bonds, if any, and on the Capital Appreciation Bonds that is properly allocable to any owner thereof is not includable in gross income for Federal income tax purposes to the same extent as interest on the Bonds. Original issue discount accrues in accordance with a constant interest method based on the compounding of interest, and an owner's adjusted basis in a Current Interest Bond having original issue discount and in a Capital Appreciation Bond for purposes of determining gain or loss on disposition will be increased by the amount of any such accrual.

The opinions expressed in paragraphs 2, 3, 4 and 7 above are subject to applicable bankruptcy, insolvency, reorganization, moratorium and other laws heretofore or hereafter enacted affecting creditors' rights, and are subject to the application of principles of equity relating to or affecting the enforcement of contractual obligations, whether such enforcement is considered in a proceeding in equity or at law.

Except as stated in paragraphs 8, 9 and 10 above, we express no opinion as to any Federal, state or local tax consequences arising with respect to the Bonds or the ownership or disposition thereof. Furthermore, we express no opinion as to the effect of any action taken or not taken in reliance upon an opinion of counsel other than ourselves on the exclusion from gross income for Federal income tax purposes of interest on the Bonds, or under State and local tax law.

We express no opinion as to the accuracy, adequacy or sufficiency of any financial or other information which has been or will be supplied to purchasers of the Bonds.

This opinion is issued as of the date hereof, and we assume no obligation to update, revise or supplement this opinion to reflect any facts or circumstances that may hereafter come to our attention, or any changes in law, or in interpretations thereof, that may hereafter occur, or for any other reason whatsoever.

Very truly yours,

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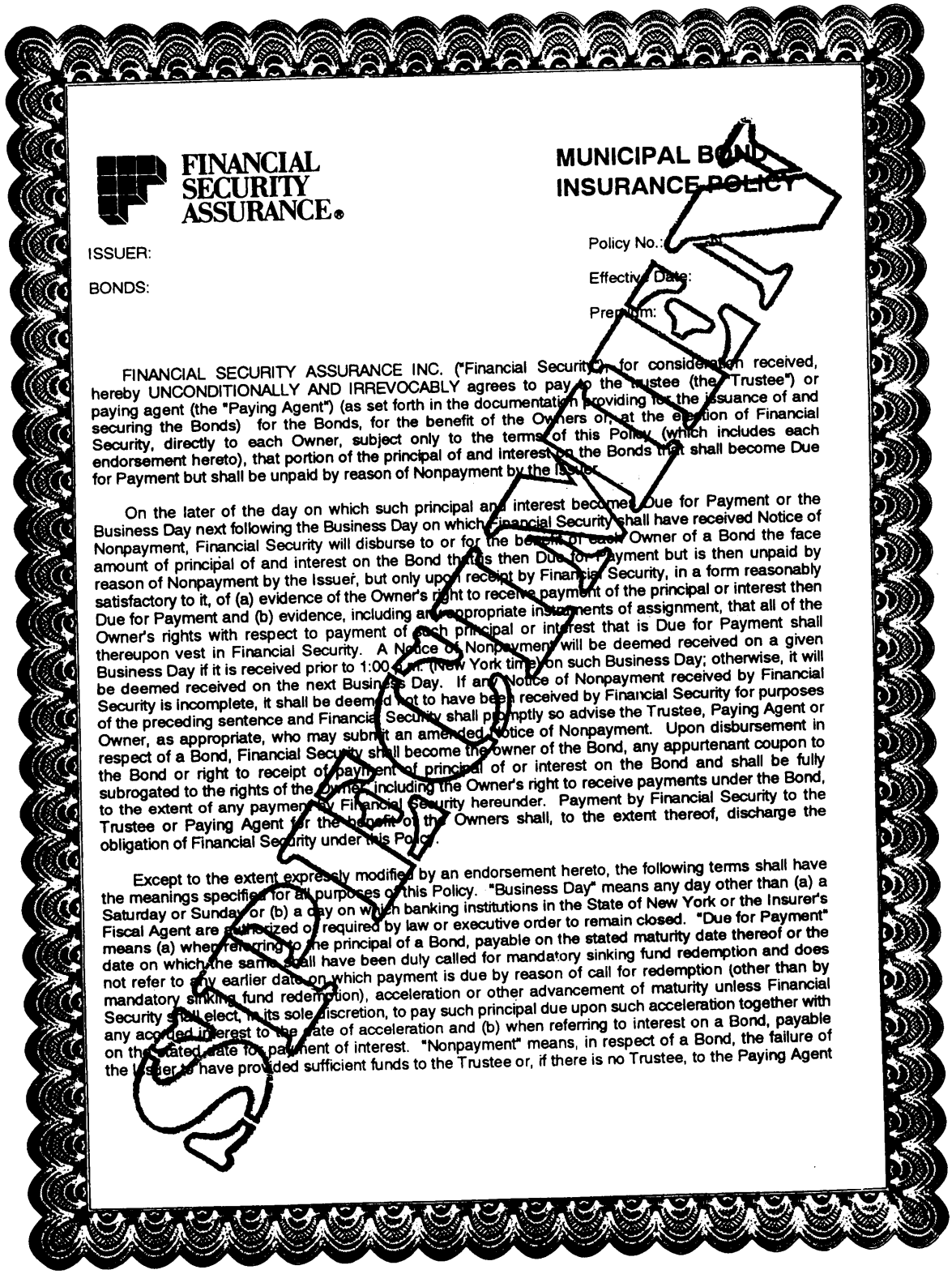

FINANCIAL SECURITY ASSURANCE®

MUNICIPAL BOND INSURANCE POLICY

ISSUER:

BONDS:

Policy No.:

Effective Date:

Premium:

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the Trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it, of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 p.m. (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal of or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent

SPECIMEN

for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment made to an Owner by or on behalf of the Issuer which has been recovered from such Owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction. "Notice" means telephonic or telecopied notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including, without limitation, the defense of fraud), whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

FINANCIAL SECURITY ASSURANCE INC.

By _____
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
350 Park Avenue, New York, N.Y. 10022-6022
(212) 826-0100

Form 500NY (5/90)

SPECIMEN

Ambac

Municipal Bond Insurance Policy

Ambac Assurance Corporation
c/o C T Corporation Systems
11 East Mifflin Street, Madison, Wisconsin 53703
Administrative Office:
One State Street Plaza, New York, New York 10004
Telephone: (212) 668-0340

Issuer:

Policy Number:

Bonds:

Premium:

Ambac Assurance Corporation (Ambac) A Wisconsin Stock Insurance Company

in consideration of the payment of the premium and subject to the terms of this Policy, hereby agrees to pay to United States Trust Company of New York, as trustee, or its successor (the "Insurance Trustee"), for the benefit of Bondholders, that portion of the principal of and interest on the above-described debt obligations (the "Bonds") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

Ambac will make such payments to the Insurance Trustee within one (1) business day following notification to Ambac of Nonpayment. Upon a Bondholder's presentation and surrender to the Insurance Trustee of such unpaid Bonds or appurtenant coupons, uncanceled and in bearer form and free of any adverse claim, the Insurance Trustee will disburse to the Bondholder the face amount of principal and interest which is then Due for Payment but is unpaid. Upon such disbursement, Ambac shall become the owner of the surrendered Bonds and coupons and shall be fully subrogated to all of the Bondholder's right to payment.

In cases where the Bonds are issuable only in a form whereby principal is payable to registered Bondholders or their assigns, the Insurance Trustee shall disburse principal to a Bondholder as aforesaid only upon presentation and surrender to the Insurance Trustee of the unpaid Bond, uncanceled and free of any adverse claim, together with an instrument of assignment, in form satisfactory to the Insurance Trustee, duly executed by the Bondholder or such Bondholder's duly authorized representative, so as to permit ownership of such Bond to be registered in the name of Ambac or its nominee. In cases where the Bonds are issuable only in a form whereby interest is payable to registered Bondholders or their assigns, the Insurance Trustee shall disburse interest to a Bondholder as aforesaid only upon presentation to the Insurance Trustee of proof that the claimant is the person entitled to the payment of interest on the Bond and delivery to the Insurance Trustee of an instrument of assignment, in form satisfactory to the Insurance Trustee, duly executed by the claimant Bondholder or such Bondholder's duly authorized representative, transferring to Ambac all rights under such Bond to receive the interest in respect of which the insurance disbursement was made. Ambac shall be subrogated to all the Bondholder's rights to payment on registered Bonds to the extent of the insurance disbursements so made.

In the event the trustee or paying agent for the Bonds has notice that any payment of principal of or interest on a Bond which has become Due for Payment and which is made to a Bondholder by or on behalf of the Issuer of the Bonds has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

As used herein, the term "Bondholder" means any person other than the Issuer who, at the time of Nonpayment, is the owner of a Bond or of a coupon appertaining to a Bond. As used herein, "Due for Payment", when referring to the principal of bonds, is when the stated maturity date or a mandatory redemption date for the application of a required sinking fund installment has been reached and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by application of required sinking fund installments), acceleration or other advancement of maturity and, when referring to interest on the Bonds, is when the stated date for payment of interest has been reached. As used herein, "Nonpayment" means the failure of the Issuer to have provided sufficient funds to the paying agent for payment in full of all principal of and interest on the Bonds which are Due for Payment.

This Policy is noncancelable. The premium on this Policy is not refundable for any reason, including payment of the Bonds prior to maturity. This Policy does not insure against loss of any prepayment or other acceleration payment which at any time may become due in respect of any Bond, other than at the sole option of Ambac, nor against any risk other than Nonpayment.

In witness whereof, Ambac has caused this Policy to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.

President

AMBAC ASSURANCE CORPORATION CORPORATE SEAL WISCONSIN

Secretary

Effective Date:

Authorized Representative

UNITED STATES TRUST COMPANY OF NEW YORK acknowledges that it has agreed to perform the duties of Insurance Trustee under this Policy.

Authorized Officer

Form No. 66-8005 (7/97)

SPECIMEN

Ambac

Endorsement

Ambac Assurance Corporation
c/o CT Corporation Systems
44 East Mifflin Street, Madison, Wisconsin 53703
Administrative Office:
One State Street Plaza, New York, New York 10004
Telephone: (212) 668-0340

Policy for:

Attached to and forming part of Policy No.:

Effective Date of Endorsement:

SPECIMEN

The insurance provided by this Policy is not covered by the property/casualty insurance security fund specified by the insurance laws of the State of New York.

Nothing herein contained shall be held to vary, alter, waive or extend any of the terms, conditions provisions, agreements or limitations of the above mentioned Policy other than as above stated.

In Witness Whereof, Ambac has caused this Endorsement to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.

Ambac Assurance Corporation

President

AMBAC ASSURANCE CORPORATION CORPORATE SEAL WISCONSIN

Secretary

Authorized Representative

Form No. 2B-0005 (7/97)

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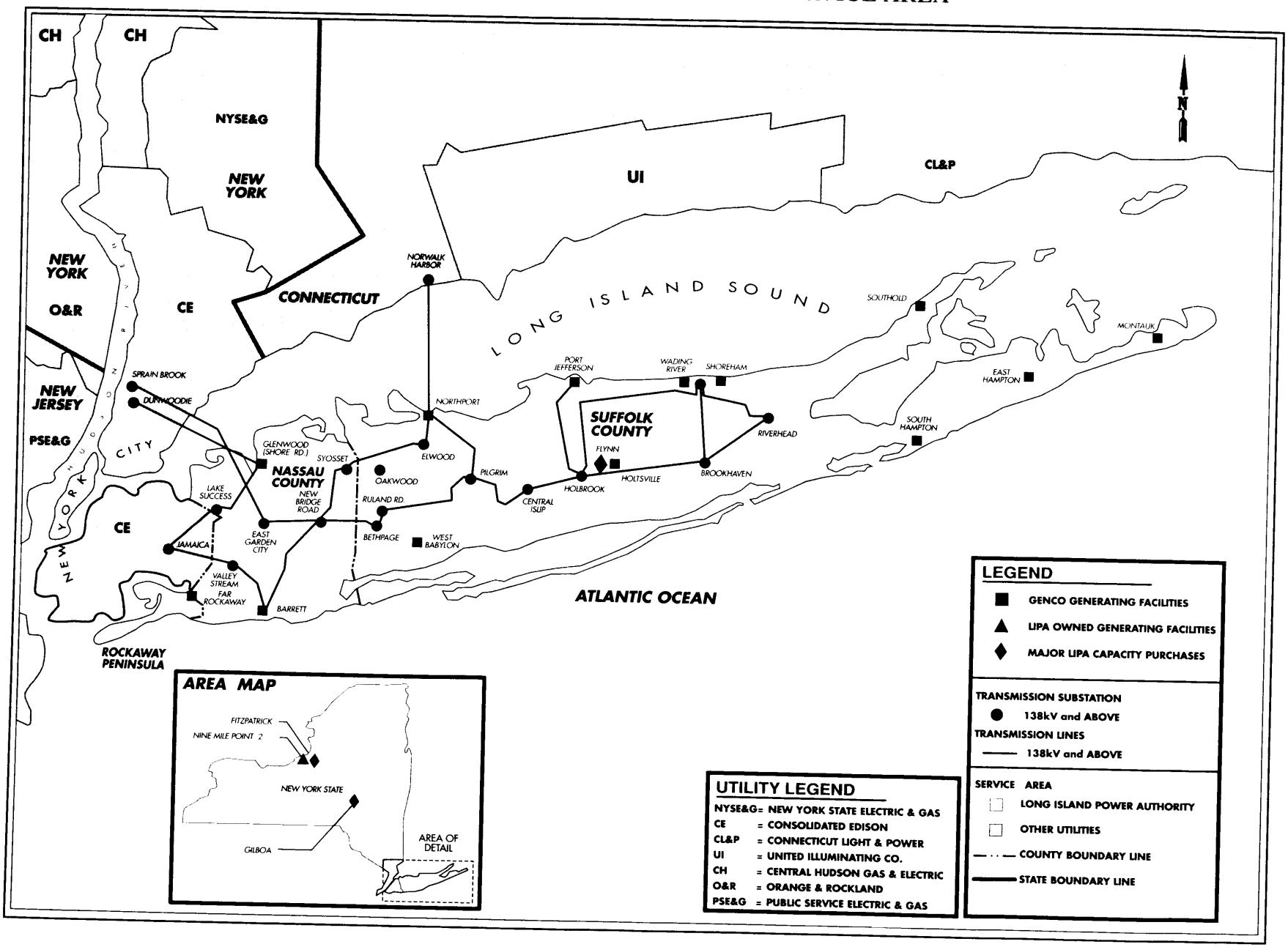
LONG ISLAND POWER AUTHORITY SERVICE AREA



PART 2

of the

OFFICIAL STATEMENT

of the

LONG ISLAND POWER AUTHORITY

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PART 2

of the

OFFICIAL STATEMENT

of the

LONG ISLAND POWER AUTHORITY

BACKGROUND

General

The purpose of this Part 2 is to describe, among other things, the Long Island Power Authority ("LIPA") and its wholly-owned subsidiary ("LIPA Sub") and the electric utility business LIPA (through LIPA Sub) will begin to conduct in its service area (the "Service Area") on Long Island, New York ("Long Island") commencing on the date of completion of the LIPA/LILCO Merger Transaction described below. The Service Area of LIPA is the same service area within which the Long Island Lighting Company ("LILCO") currently conducts its retail electric business, and includes two counties on Long Island—Nassau County ("Nassau County") and Suffolk County ("Suffolk County")—except for the Nassau County villages of Freeport and Rockville Centre and the Suffolk County village of Greenport, each of which has their individually owned municipal electric system, and a small portion of the Borough of Queens of The City of New York known as the Rockaways.

LIPA is a corporate municipal instrumentality and a political subdivision of the State of New York (the "State"), exercising essential governmental and public powers. LIPA was created by the State Legislature under and pursuant to the LIPA Act which was enacted in 1986 (being Title One-A of Article 5 (§1020 *et seq.*) of the Public Authorities Law of the State of New York, as amended) for two purposes: (i) to achieve the shutdown and decommissioning of the completed and fueled, but non-commercially operating, nuclear generating station then owned by LILCO located at Shoreham, Long Island and known as the Shoreham Nuclear Power Station ("Shoreham"); and (ii) to lower electric rates in the Service Area.

Shutdown and Decommissioning of Shoreham

A contract for the transfer by LILCO to LIPA of Shoreham was executed in 1989. The Nuclear Regulatory Commission ("NRC") approved the transfer of Shoreham to LIPA, and the transfer was completed in February 1992. In accordance with the requirements of the LIPA Act, physical decommissioning of Shoreham was completed in 1994 and its license was surrendered to the NRC in 1995.

With the approval of the New York State Public Service Commission ("PSC") in June 1989, LILCO recorded on its financial statements a regulatory asset approximately equal to its costs of Shoreham, less a disallowance required by the PSC for imprudent investment by LILCO in Shoreham. This regulatory asset, and the resulting ability of LILCO to recover it through its rates, was intended by the PSC to restore LILCO's debt to an investment grade rating following LILCO's abandonment of its investment in Shoreham. The costs relating to Shoreham paid by LIPA after the transfer of Shoreham to LIPA, including payments in lieu of taxes and decommissioning costs, were funded by LILCO and, as a result, were also recorded on LILCO's financial statements as a regulatory asset of LILCO. The regulatory assets described above, and other Shoreham-related items recorded on LILCO's financial statements, are referred to collectively in this Official Statement as the "Shoreham

Regulatory Asset." In 1989, the PSC approved the recovery by LILCO of the Shoreham Regulatory Asset through the rates of LILCO over a period of forty years. As of March 31, 1998, the balance of the Shoreham Regulatory Asset not yet recovered by LILCO in its rates was $4.7 billion.

THE LIPA/LILCO MERGER

Plan for Lowering Electric Rates in the Service Area

In order to fulfill the second of LIPA's purposes, in December of 1995, New York State Governor George E. Pataki announced a plan to lower electric rates in the Service Area. At that time LILCO had, and still has, among the highest electric utility rates in the continental United States (in large part the result of the recovery by LILCO through its rates of the Shoreham Regulatory Asset). As part of this plan to lower electric rates in the Service Area, Governor Pataki set forth the following six objectives: (i) deliver sustainable double digit electric rate reductions in the Service Area; (ii) maintain a high level of reliability in the supply of electric utility services in the Service Area; (iii) maximize private sector involvement in the supply of electric utility services in the Service Area; (iv) settle the currently pending Shoreham-related property tax litigation between LILCO and Suffolk County and certain local taxing jurisdictions in Suffolk (the "Shoreham Property Tax Litigation") without raising real property tax rates on Long Island (for a further description of the Shoreham Property Tax Litigation, see "Shoreham Tax Matters" in this Part 2); (v) introduce competition in the supply of electricity in the Service Area; and (vi) end LILCO's monopoly position in the Service Area.

The LIPA/LILCO Merger

As of June 26, 1997, LIPA and LILCO entered into an Agreement and Plan of Merger (the "LIPA/LILCO Merger Agreement") pursuant to which LIPA will acquire all of the outstanding common stock of LILCO. The LIPA/LILCO Merger Agreement is part of a series of interrelated merger and restructuring transactions involving LIPA, LILCO, BL Holding Corp, and KeySpan Energy Corporation ("KeySpan", the parent holding company for The Brooklyn Union Gas Company). Upon the completion of this series of transactions, LIPA acting through LIPA Sub will be the retail supplier of electricity in the Service Area. In connection with the LIPA/LILCO Merger Agreement, and in order to enable LIPA (acting through LIPA Sub) to supply electricity at retail, LIPA also entered into a Management Service Agreement (the "MSA"), a Power Supply Agreement (the "PSA") and an Energy Management Agreement (the "EMA") (these three agreements are collectively referred to as the "Operating Agreements"). Upon completion of the interrelated transactions, the Operating Agreements will each become an agreement between LIPA Sub and an individual BL Holding Corp subsidiary formed to carry out the particular agreement (individually referred to herein as a "BL Holding Corp Sub" and, collectively, as the "BL Holding Corp Subs"). The performance of each such BL Holding Corp Sub under its respective Operating Agreement as well as any payment obligations it may have under such agreement will be guaranteed by BL Holding Corp (see "LIPA's Retail Electric Service Business—Guarantees and Indemnities").

The transactions required by the LIPA/LILCO Merger Agreement (all of which are referred to in this Official Statement as the "LIPA/LILCO Merger Transaction") include, among others, the following:

(i) LILCO will form BL Holding Corp, which will be a new holding company, and will also form certain BL Holding Corp Subs (the "Transferee Subsidiaries") to which LILCO, in exchange for stock of BL Holding Corp, will transfer its present gas transmission, distribution and supply assets and operations, non-nuclear electric generating assets and common plant (the

"Transferred Assets"), together with certain liabilities (the "Transferred Liabilities"), leaving LILCO with the assets described under "LIPA Sub Assets and Liabilities" below;

(ii) LIPA will pay to LILCO's shareholders, from the proceeds of the first Bonds issued by LIPA and any Subordinated Indebtedness which may be issued in connection with such Bonds, a "Cash Purchase Price" of $2,497,500,000;

(iii) the current shareholders of LILCO will become shareholders of BL Holding Corp;

(iv) LIPA Acquisition Corp (a transitory subsidiary formed by LIPA to facilitate the acquisition of LILCO) will merge with and into LILCO, with the result that LILCO will be a wholly-owned subsidiary of LIPA (LIPA Sub);

(v) LIPA Sub will retain and own the assets and liabilities described under "LIPA Sub Assets and Liabilities" below;

(vi) the Promissory Note Obligors will issue and deliver to LIPA Sub the Promissory Notes (the principal amount of the Promissory Notes is subject to adjustment as provided in the LIPA/LILCO Merger Agreement); and

(vii) LIPA, acting through LIPA Sub, will commence business as the retail supplier of electricity in the Service Area. The consummation of the LIPA/LILCO Merger Transaction (the "LIPA/LILCO Merger Closing") is expected to occur on the date of issuance and delivery of LIPA's first tranche of financing. See "Appendix G—Summary of the LIPA/LILCO Merger Agreement."

It is anticipated that, upon the consummation of the merger transactions, LILCO's current common shareholders and KeySpan's current shareholders will each become shareholders of BL Holding Corp, the ultimate parent holding corporation for the Transferee Subsidiaries, KeySpan and any other BL Holding Corp Subs. Such merger transactions will be accomplished pursuant to the LILCO/KeySpan Combination, which was executed by LILCO and KeySpan at the same time as and in contemplation of the LIPA/LILCO Merger Agreement. The LILCO/KeySpan merger is expected to be consummated simultaneously with the transactions under the LIPA/LILCO Merger Agreement. If such merger does not occur, any obligations of BL Holding Corp in connection with the LIPA/LILCO Merger Agreement will continue, but its financial condition will reflect the fact that BL Holding Corp will not be the owner of KeySpan and its subsidiaries.

LIPA Sub Assets and Liabilities

At the time of the LIPA/LILCO Merger, LILCO's principal assets will consist of: (i) the physical assets of LILCO's electric transmission and distribution system and other items relating to said system (the "T&D System"); (ii) LILCO's 18% undivided ownership interest in Unit 2 of the Nine Mile Point Nuclear Station; (iii) certain agreements and contracts for power supply and transmission; (iv) certain regulatory assets of LILCO, including the Shoreham Regulatory Asset; (v) the Promissory Notes; (vi) certain cash, receivables, and other assets; (vii) all judgments, actions and claims of LILCO for refunds for property taxes, including the judgments and claims of LILCO relating to the Shoreham Property Tax Litigation; and (viii) the intangible assets of LILCO's former retail electric business, including the right to provide service in the Service Area (collectively, the "LIPA Sub Assets"). Upon the consummation of the LIPA/LILCO Merger, LIPA Sub will record various purchase accounting adjustments to give recognition to the fact that LIPA Sub is not subject to the regulatory jurisdiction of the PSC and is exempt from federal income tax. The primary result of these adjustments will be the elimination of the regulatory assets and liabilities of LILCO, including the Shoreham Regulatory Asset, and the elimination of LILCO's deferred federal income tax liability. The excess of the

acquisition costs over the original net book value of the transmission and distribution and nuclear assets and the fair value of the other net assets retained will appear on the balance sheet as the "Acquisition Adjustment." See "Appendix B—Unaudited Pro Forma Consolidated Balance Sheet of LIPA".

LIPA Sub will also retain the following liabilities of LILCO: (i) the obligations of LILCO to pay the principal of and interest on $1.186 billion principal amount of LILCO's outstanding first mortgage General and Refunding Bonds (the "G&R Bonds"), which will be legally defeased or otherwise redeemed by LIPA at the time of the LIPA/LILCO Merger Closing; (ii) the obligations of LILCO to pay the principal of and interest on $2.270 billion principal amount of LILCO's outstanding unsecured debentures (the "Debentures") of which approximately $439.3 million is expected to be refinanced by LIPA at the time of the LIPA/LILCO Merger Closing (assuming the Initial Subordinated is $1,500,000,000 and, if less, fewer Debentures will be refinanced from the proceeds of the first tranche of the Plan of Finance but more will be refinanced from the second tranche); (iii) the obligations of LILCO to pay the principal of and interest on notes issued by LILCO to secure tax-exempt bonds issued on behalf of LILCO by New York State Energy Research and Development Authority ("NYSERDA") outstanding in the amount of $915.7 million; (iv) the obligation to redeem and pay $339.1 million for all of LILCO's outstanding Preferred Stock (except Series AA which will be redeemed by LILCO at the time of the LIPA/LILCO Merger Closing), (v) certain customer deposits, payables and other liabilities, and (vi) all other liabilities, including environmental liabilities, of LILCO not otherwise transferred to or indemnified by a subsidiary of BL Holding Corp pursuant to the LIPA/LILCO Merger Agreement (collectively, the "LIPA Sub Liabilities").

The LIPA Sub Liabilities, together with the LIPA Sub Assets, are collectively referred to herein as the "LIPA Sub Assets and Liabilities".

LIPA Sub's ongoing obligations relating to the Debentures and the NYSERDA Financing Notes will be effectively reduced by payments received under the Promissory Notes related thereto. The LIPA/LILCO Merger Agreement provides that, except as LIPA may otherwise agree, if at any time during the term of the Promissory Notes, the long-term senior debt of BL Holding Corp is not rated at least "A" by two or more nationally recognized rating services, then BL Holding Corp is obligated to either: (i) deliver a letter of credit issued by a financial institution whose long-term senior debt is or would be rated "A" by at least two such rating services to secure the Promissory Notes; or (ii) economically defease the Promissory Notes by delivering to LIPA U.S. treasury securities sufficient, as determined by LIPA, to pay all amounts due in respect of the debt related to the Promissory Notes.

Pro Forma Balance Sheet

The following unaudited pro forma condensed consolidated balance sheet gives effect to the acquisition by LIPA of LILCO, after the transfer of the Transferred Assets and Transferred Liabilities, in a transaction to be accounted for as a purchase as if it had occurred at March 31, 1998. See "Appendix B—Unaudited Pro Forma Consolidated Balance Sheet of LIPA." Because the nature of the financial operations of LIPA and LIPA Sub will be fundamentally different from those of LILCO prior to the completion of the LIPA/LILCO Merger Transaction, LIPA does not believe that pro forma income statement information is relevant. See "Appendix A—Independent Consultant's Report" in this Part 2 for a projection of LIPA Sub's revenues and revenue requirements during the Study Period.

LIPA Unaudited Pro Forma Condensed Consolidated Balance Sheet(1)
After First Tranche
March 31, 1998
($ in millions)

Assets	
Utility Plant	
Transmission and Distribution	$1,356.5
Nuclear and Nuclear Fuel	679.8
Total Utility Plant	2,036.3
Current Assets	616.9
Promissory Notes	913.4
Shoreham Rebates and Credits Fund	142.5
Clean Energy and Rate Payers funds	21.0
Interest & Escrow funds	20.0
Deferred Charges and Other Investments	88.3
Acquisition Adjustment	4,180.8
Total Assets	$8,019.2

Capitalization and Liabilities	
Capitalization	
Revenue Bonds	$3,449.5
Subordinated Indebtedness	1,500.0
Debentures	1,830.7
NYSERDA Financing Notes	915.7
Premium on Retained Debt	158.7
Accumulated Deficit	(29.9)
Total Capitalization	7,824.7
Current Liabilities	174.8
Deferred Credits	19.7
Total Capitalization and Liabilities	$8,019.2

(1) See Appendix B for notes.

Basis for LIPA Rate Reductions

As described under "Rates and Charges" herein, on April 9, 1998, LIPA adopted base rates and charges which, together with the Shoreham Credits, result in an average system revenue of LIPA Sub of 12.18 cents per kWh. These base rates and charges are on average 20 percent lower than LILCO's current average system rates and charges. LIPA's initial base rates are expected to be maintained at this level for at least five years. Such reduction in the average system base rate is principally the result of the following factors: the effective refinancing of the LIPA Sub Assets with LIPA's lower-cost tax-exempt debt, exemption from federal income tax of the net income of LIPA Sub, synergy savings resulting from the merger of LILCO and KeySpan which LIPA has obtained in the LIPA/LILCO Merger Agreement, and the Shoreham Credits. If the LILCO/KeySpan merger does not take place, a portion of such anticipated synergy savings may not be realized. Further, if the Shoreham Property Tax Settlement Agreement is not entered into, a portion of such anticipated savings may not be realized as contemplated herein.

Further Information

See Appendix G for a brief description of the LIPA/LILCO Merger Agreement. Information regarding the LILCO/KeySpan Combination can be obtained from publicly available sources including the Joint Proxy Statement/Prospectus on Form S-4 filed by LILCO and KeySpan with the Securities and Exchange Commission relating to the LILCO/KeySpan Combination and subsequent filings related thereto. Neither this Joint Proxy Statement/Prospectus nor subsequent filings are to be considered a part of this Official Statement, and LIPA makes no representation as to their accuracy or completeness.

LIPA'S RETAIL ELECTRIC SERVICE BUSINESS

General

On the LIPA/LILCO Merger Closing Date, LIPA, acting by and through LIPA Sub, will commence business as the retail electric supplier in the Service Area.

Relationship of LIPA and LIPA Sub

LIPA Sub is a wholly-owned subsidiary of LIPA. The board of directors for LIPA Sub will be appointed by the Trustees of LIPA. Accordingly, LIPA Sub will be controlled by LIPA. The initial directors for LIPA Sub are expected to be the Trustees.

LIPA and LIPA Sub will be parties to a Financing Agreement dated as of May 1, 1998 (the "Financing Agreement") to provide for their respective duties and obligations relating to the financing and operation of the retail electric business in the Service Area. See Appendix D for a summary of the Financing Agreement.

Pursuant to the terms of the Financing Agreement, LIPA will issue all required debt, including the debt necessary to pay the Cash Purchase Price and complete the LIPA/LILCO Merger Transaction, to fund the Shoreham Rebates and Shoreham Credits and refund the G&R Bonds, the Debentures and the NYSERDA Financing Notes as described under "Plan of Finance." The proceeds of all such debt will be treated as being loaned to LIPA Sub which will repay such loans from the revenues it receives from such retail electric business. To secure the loans, LIPA Sub will pledge all of its revenues to LIPA which will, in turn, pledge such revenues as security for such debt.

Pursuant to the terms of the Financing Agreement, LIPA Sub, as the owner of the T&D System and as the party to the Operating Agreements, will conduct the retail electric business in the Service Area and will be the entity that is responsible for providing service to customers in the Service Area. LIPA will be responsible, however, for administering, monitoring and managing the performance by all parties to the Operating Agreements.

LIPA and LIPA Sub will also be parties to an Administrative Services Agreement which will set forth the terms and conditions under which LIPA will provide personnel, personnel-related services and other services necessary for LIPA Sub to provide electric service in the Service Area. For a further discussion of the Administrative Services Agreement, see "Long Island Power Authority—Management and Operations of the System."

LIPA's Plan for System Operation

LIPA will perform its duties and obligations with a senior management team, while minimizing its total work force. LIPA will oversee the operation of the T&D System with a staff of approximately 23 and through the support of outside financial, engineering, accounting, and legal advisors and consultants. LIPA will provide for the operation of the T&D System (including obtaining all necessary power supplies) by LIPA Sub through the Operating Agreements. At the time of the LIPA/LILCO Merger Closing, LIPA will assign its rights and obligations under the Operating Agreements to LIPA Sub; LILCO will assign its rights and obligations thereunder to separate operating subsidiaries of BL Holding Corp; and BL Holding Corp will guarantee performance of each of the Operating Agreements by its subsidiaries. Day-to-day operations and maintenance during the terms of the Operating Agreements are expected to be performed by the personnel who are currently performing these services.

LIPA will provide the continuity of policy making, rate setting, financial planning and management of the T&D System by maintaining the capability of its management team and in-house staff to administer the Operating Agreements and to make efficient use of outsourced services. A wide variety of skills and experience are required to establish policy, evaluate the T&D System needs, assess system operations and related matters. The requirements are periodic and vary in the level of effort required. Outsourcing some of these services enables LIPA to have the skills needed without the expense of committing to full-time positions.

Tasks to be performed through this outsourcing arrangement are expected to include, but are not limited to, the following: (i) review of actual costs incurred under the Operating Agreements; (ii) review of the incentive/disincentive compensation provisions under the Operating Agreements; (iii) review of the application of price escalation indices under the Operating Agreements; (iv) planning, implementing and monitoring Long Island Choice; (v) review of power and fuel purchases under the EMA; (vi) review and evaluation of annual operating and capital budgets; (vii) solicitations for new capacity and energy supplies; (viii) evaluation of ramp-down opportunities under the PSA; (ix) evaluation of generation purchase rights; and (x) review of system dispatch and off-system sales and purchases. RMI and Price Waterhouse LLP are under contract to LIPA to provide consulting services as required. LIPA will utilize these services, as well as the services of other outside consultants, for these tasks.

See "Long Island Power Authority—Management and Operations of the System," and "Appendix A—Independent Consultant's Report—Management and Operation of the System" in this Part 2.

Operating Agreements

MSA. The MSA provides for a BL Holding Corp Sub (the "Manager") to perform the day-to-day operation and maintenance of the T&D System, including, among other functions, transmission and distribution facility operation, customer service, billing and collection, meter reading, planning, engineering, and construction, all in accordance with policies and procedures adopted by LIPA Sub. LIPA Sub will engage the Manager as an independent contractor to furnish such services, and the Manager will not have any ownership or leasehold interest in the T&D System. All cash collected by the Manager for the account of LIPA Sub after the LIPA/LILCO Merger Closing Date will be deposited on each business day in bank accounts in such bank as LIPA may direct and upon such terms and conditions to be specified by LIPA. See "Billing and Collections" in this Part 2.

LIPA will exercise control over the performance of the T&D System through specific standards for performance and incentives to the Manager contained in the MSA. The primary standards of performance for the delivery of power are the frequency and duration of outages.

Annual monetary incentives under the MSA to the Manager can reach $4 million if the reliability targets are met or exceeded. The incentives are apportioned to each of four geographic districts of the T&D System, the performance of which are separately monitored. This incentive encourages the Manager to undertake measures across the T&D System that are reasonably anticipated to maintain or improve reliability. The operating budget which has been established for 1998 for the MSA provides for at least the level of labor LILCO has maintained in recent years, adjusted in accordance with relevant cost indices. The capital additions budget approved for 1998 under the MSA is at levels similar to those which have been expended in recent years, during which LILCO has undergone a significant improvement in reliability.

In addition to incentives for controlling costs, the MSA establishes customer service incentives for call answering and meter reading. When combined with reliability, these services comprise the key performance areas of concern to most utility customers. The objective of the call answering incentive is to improve customer call response times within a specified range. The monthly meter reading incentive targets a reduction in the number of estimated meter reads. The MSA also provides for a worker safety incentive payment to achieve and maintain lost-time accident levels below historical levels.

The term of the MSA is eight years. The provisions of the MSA provide that the management services for the T&D System performed by the Manager will be competitively bid in the sixth year of the MSA for a new management agreement beginning after the eighth year. See Appendix E for a summary of the MSA.

PSA. The PSA provides for the sale to LIPA Sub by a BL Holding Corp Sub (''GENCO'') of all of the capacity and, to the extent LIPA Sub requests, energy, from the existing oil and gas-fired generating plants on Long Island owned by LILCO prior to the LIPA/LILCO Merger Closing (the ''GENCO Generating Facilities''), which facilities will be transferred to GENCO as part of the LIPA/LILCO Merger Closing. Such sales of capacity and energy from the GENCO Generating Facilities will be made at cost-based wholesale rates approved by the Federal Energy Regulatory Commission (''FERC''). The initial rates have been accepted by FERC for implementation on the LIPA/LILCO Merger Closing Date, subject to the results of a hearing at a later date. The outcome of this FERC hearing can only result in the same rate level or a reduction in the rate level, not an increase in the rate. This rate may be modified in the future in accordance with the terms of the PSA for (i) agreed upon labor and expense indices applied to the base year; (ii) a return of and on net capital additions required for the GENCO Generating Facilities, which will require approval by LIPA; and (iii) reasonably incurred expenses that are outside the control of GENCO. This rate formula provides for the containment of GENCO costs.

In addition to cost control, the PSA provides incentives and penalties for GENCO to maintain the output capability of the Generating Facilities, as measured by annual industry-standard tests of operating capability, and to make capital improvements which benefit plant availability. These combined incentives and penalties may total as much as $4 million annually and are expected to provide a meaningful inducement for favorable performance. The FERC hearing will also review both the incentives and penalties, as well as the rate modification mechanism described in the previous paragraph.

The PSA provides LIPA Sub with all of the capacity from the GENCO Generating Facilities. However, LIPA Sub has no obligation to purchase energy from the GENCO Generating Facilities and is able to purchase energy on a least-cost basis from all available sources consistent with existing transmission interconnection limitations of the T&D System. The term of the PSA is for fifteen years and is renewable on similar terms. However, the PSA provides LIPA the option of electing to reduce or ''ramp-down'' the capacity it purchases from GENCO beginning in year seven of the PSA, in accordance with schedules set forth in the PSA. In years seven through ten of the PSA, if LIPA elects to ramp-down, GENCO is entitled to payment for 100 percent of the present value of the capacity charges otherwise payable over the remaining term of the PSA. If LIPA ramps-down the generation capacity in years 11 through 15 of the PSA, the capacity charges otherwise payable by LIPA will be reduced in accordance with a formula established in the PSA. If LIPA exercises its ramp-down option, GENCO may use any capacity released by LIPA to bid on new LIPA capacity requirements or to bid on LIPA's capacity requirements to replace other ramped-down capacity. If GENCO continues to

operate the ramped-down capacity, the PSA requires it to use reasonable efforts to market the capacity and energy from the ramped-down capacity and to share any profits with LIPA. Capacity and energy sold by GENCO from ramped-down capacity must be transported over the T&D System, and GENCO will be required to pay LIPA's standard transmission (and, if applicable, distribution) rates for this service. The PSA will be terminated in the event that LIPA exercises its right to purchase at fair market value all of the GENCO Generating Facilities in the fourth year after the Merger Closing, subject to certain conditions. See Appendix E for a summary of the PSA.

EMA. The EMA provides for a BL Holding Corp Sub (''Energy Manager'') to (i) procure and manage fuel supplies for LIPA Sub to fuel the GENCO Generating Facilities, (ii) perform off-system capacity and energy purchases on a least-cost basis to meet LIPA Sub's needs, and (iii) make off-system sales of output from the GENCO Generating Facilities and other power supplies either owned or under contract to LIPA Sub. LIPA Sub is entitled to two-thirds of the profit from any off-system energy sales arranged by Energy Manager. The term for the service provided in (i) above is fifteen years, and the term for the service provided in (ii) and (iii) above is eight years. The EMA also provides for a continuation of the present gas transportation rate for gas delivered over the gas distribution system to the GENCO Generating Facilities and to new generation resources for a period of 11.5 years, with cost-based adjustments to meet gas delivery system expansion needs. See Appendix E for a summary of the EMA.

The EMA provides for payment of the costs of sufficient professional and support staff for the Energy Manager to properly perform its functions thereunder. The EMA further provides incentives for control of the cost of fuel and electricity purchased on behalf of LIPA by the Energy Manager. Fuel and electricity purchase prices will be compared to regional price indices and the Energy Manager will receive a payment from LIPA, or be obligated to make a payment to LIPA, for fuel and/or purchased electricity costs which are below or above, respectively, specified tolerance bands of regional indices. The total fuel purchase incentive or disincentive can be no greater than $5 million annually and the electricity purchase incentive or disincentive can be no greater than $2 million annually. LIPA pays for actual fuel and electricity purchased.

The budgets for all of the above-described agreements have been established in recognition of past budgets and actual expenditures and capital improvement requirements incurred by LILCO in recent years. The Independent Consultant's Report states that this benchmarking to past costs, with adjustments for known or anticipated changes in circumstances, provides a reasonable basis for estimating the levels of future costs to be included in the budget for the MSA, PSA, and EMA.

Other Rights

Pursuant to certain other agreements between LIPA and LILCO, certain future rights are granted to LIPA. Subject to certain conditions, they include the right for 99 years to lease or purchase, at fair market value, parcels of land and to acquire unlimited access to, as well as appropriate easements at, Generating Facility Sites for the purpose of constructing new electric generating facilities to be owned by LIPA or its designee. Subject to LIPA's right of first refusal, BL Holding Corp and its subsidiaries will have the right to sell or lease property on or adjoining Generating Facility Sites to third parties. In addition, LIPA will acquire at the LIPA/LILCO Merger Closing for fair market value an appropriately sized parcel at Shoreham suitable as the terminus for a potential transmission cable under Long Island Sound and, after review, evaluation and comparison with other alternatives, the potential site of a new gas-fired combined cycle generating facility.

BL Holding Corp or its subsidiaries will own the common plant (such as administrative office buildings and computer systems) and will charge LIPA for its beneficial use through the Operating Agreements. BL Holding Corp has agreed to provide LIPA, for a period of 99 years, the right to enter into leases at fair market value for common plant or sub-contract for common services which it may assign to a subsequent manager of the T&D System. BL Holding Corp has also agreed for a period of 99 years not to compete with LIPA as a provider of transmission or distribution service on Long Island. BL Holding Corp and KeySpan have agreed that LIPA will share in synergy savings over the next ten years attributed to the LILCO/KeySpan combination, which savings have been agreed to in the rate structure under the MSA, EMA and the PSA. BL Holding Corp has agreed not to commence any tax certiorari case (until termination of the PSA) challenging certain property tax assessments relating to the GENCO Generating Facilities. See "Shoreham Tax Matters—Other Real Property Tax Matters."

Guarantees and Indemnities

At the LIPA/LILCO Merger Closing, BL Holding Corp will deliver to LIPA a Guaranty Agreement under which BL Holding Corp will absolutely and unconditionally guarantee to LIPA (a) the full and prompt payment when due of all amounts required to be credited or paid by BL Holding Corp Subs under the Operating Agreements and (b) the full and prompt performance of the covenants and agreements of these subsidiaries under the Operating Agreements. Upon certain reductions in the credit ratings of BL Holding Corp, LIPA has the right to have BL Holding Corp obtain letters of credit securing these undertakings and agreements.

At the LIPA/LILCO Merger Closing, the Transferee Subsidiaries and BL Holding Corp ("BHC Parties") will deliver a Liabilities Undertaking and Indemnification Agreement which will indemnify LIPA, LIPA Acquisition Corp and LIPA Sub ("LIPA Parties") and hold them harmless from a variety of specified liabilities in connection with the LIPA/LILCO Merger Transaction, including the following: (i) unpaid debts, liabilities or obligations relating to the Transferred Assets, including, without limitation, liabilities or obligations relating to the Transferred Assets resulting or arising from (a) claims for personal injury or property damage, or (b) non-performance of any contract, commitment or obligation imposed by law or otherwise; (ii) debts, liabilities or obligations incurred by BHC Parties after the LIPA/LILCO Merger Closing; (iii) liabilities resulting from non-performance by BHC Parties under the LIPA/LILCO Merger Agreement or the Operating Agreements; (iv) liabilities or obligations relating to or arising out of any filing or other submission by BHC Parties with any government authority; and (v) certain undisclosed liabilities.

LIPA Parties will deliver a similar Liabilities Undertaking and Indemnification Agreement which will indemnify BHC Parties and hold them harmless from a variety of specified liabilities in connection with the LIPA/LILCO Merger Transaction, including the following: (i) unpaid debts, liabilities or obligations relating to the Retained Assets, including, without limitation, liabilities or obligations relating to the Retained Assets resulting or arising from (a) claims for personal injury or property damage or (b) non-performance of any contract, commitment or obligation imposed by law or otherwise; (ii) debts, liabilities or obligations incurred by LIPA Parties after the LIPA/LILCO Merger Closing; and (iii) non-performance by LIPA Parties under the LIPA/LILCO Merger Agreement or the Operating Agreements.

In addition, to clarify and supplement the Liabilities Undertaking and Indemnification Agreement, prior to the LIPA/LILCO Merger Closing, BHC Parties and LIPA Parties will enter into an agreement to allocate between them certain liabilities (including environmental liabilities) arising from events

occurring prior to the LIPA/LILCO Merger Closing and relating to the business and operations to be conducted by LIPA Parties after the LIPA/LILCO Merger Closing (the "Retained Business") and to the business and operations to be conducted by BHC Parties after the LIPA/LILCO Merger Closing (the "Transferred Business").

BHC Parties will be responsible for all liabilities arising from all manufactured gas plant operations ("MGP Sites"), including those currently or formerly operated by LILCO or any of its predecessors, whether or not such MGP Sites relate to the Transferred Business or the Retained Business; all liabilities traceable to the Transferred Business; and certain scheduled liabilities. See "Environmental Matters" in this Part 2. Certain liabilities that are traceable to GENCO may be recovered by BHC Parties to the extent provided for under the PSA.

LIPA Parties will be responsible for all liabilities traceable to the Retained Business (including environmental liabilities discovered in the future which arise from events or circumstances occurring prior to the LIPA/LILCO Merger Closing) and certain scheduled liabilities. Notwithstanding the parties' contractual allocation of environmental liabilities, under certain circumstances LIPA could be liable for environmental costs related to Transferred Assets, if a BHC Party fails to satisfy such liability.

Liabilities that exist as of the LIPA/LILCO Merger Closing that are untraceable, including untraceable liabilities that arise out of common plant and/or shared services (whether known or unknown), will be allocated 51.1% to LIPA Parties and 48.9% to BHC Parties (of which 27.9% is allocable to GENCO). Such liabilities that arise from events or circumstances occurring after the LIPA/LILCO Merger Closing may be recovered by BHC Parties to the extent provided for under the PSA and MSA.

For purposes of allocations, a liability is traceable if it can be determined to have resulted from the activities of the Retained Business or the Transferred Business, or a percentage of each, based on available documentation, reasonable inferences, and other reasonable evidence.

PLAN OF FINANCE

General

The total consideration to be paid by LIPA for the acquisition of LILCO and the transactions related thereto is $6.295 billion, reflecting the Cash Purchase Price in exchange for the LILCO common stockholder's equity, the redemption of certain preferred stock and the retention of certain debt of LILCO which is discussed under "Retained Debt" immediately following. LIPA's initial plan of finance (the "Plan of Finance") anticipates funding the Cash Purchase Price, redeeming the preferred stock and refinancing such Retained Debt not supported by Promissory Notes, through the issuance of bonds in three tranches during 1998. The Plan of Finance also contemplates the issuance of additional debt as part of these three tranches to fund certain rebates and credits to its customers, certain capital expenditures and other initial costs, and costs of issuance relating to such additional debt. Following completion of the Plan of Finance, LIPA anticipates the issuance of additional Bonds on an annual basis as discussed under "Future Financing Activities" below.

Retained Debt

LIPA Sub will retain liability for all outstanding G&R Bonds (which LIPA will defease and refund as part of the first tranche of LIPA financings), all Debentures (except any LILCO 1999 and 2023 Debentures which are acquired by BL Holding Corp through an expected exchange offer and cancelled), and certain NYSERDA Financing Notes. This Official Statement assumes that the Initial

Subordinated Indebtedness will be issued in the principal amount of $1,500,000,000. If that is the case, approximately $439,300,000 of Debentures are expected to be refinanced as part of the first tranche of the LIPA financing. If the actual principal amount of the Initial Subordinated Indebtedness is less than $1,500,000,000, fewer Debentures will be refinanced from the proceeds of the first tranche of the financing and more will be refinanced as part of the second tranche. The debt retained is detailed in the table below.

LILCO DEBT RETAINED BY LIPA SUB

Debentures

Maturity	Amount ($000)	Interest Rate	Call Date	Redemption Price(3)	Promissory Notes(4)
1/15/00	$ 36,000	7.300%	NC	NA	NA
7/15//01	145,000	6.250	NC	NA	NA
3/15/03	150,000	7.050	NC	NA	NA
3/01/04	59,000	7.000	NC	NA	NA
6/01/05	200,000	7.125	NC	NA	NA
3/01/07(1)	142,000	7.500	3/01/98	103.54%	NA
7/15/19(1)	420,000	8.900	7/15/98	105.94	NA
11/01/22	451,000	9.000	11/1/02	104.19	NA
	$1,603,000				NA
7/15/99(2)	$ 397,000	7.300	NC	NA	$397,000
3/15/23(2)	270,000	8.200	3/15/03	104	270,000
	$ 667,000				$667,000
	$2,270,000				

NC = Non-callable NA = Not Applicable

(1) $439,300,000 is expected to be refinanced as part of the first tranche of the LIPA financings, assuming the issuance of $1,500,000,000 of Initial Subordinated Indebtedness.

(2) Subject to BL Holding Corp exchange offer described above.

(3) Declining upon later redemption date.

(4) The amount of retained LILCO 1999 and 2023 Debentures will vary depending on the success of BL Holding Corp's exchange offer. For purposes of this Official Statement, it has been assumed that none of such Debentures are tendered in the exchange offer. LIPA Sub will hold Promissory Notes which correspond to the 1999 and 2023 Debentures which are retained by LIPA Sub.

NYSERDA Financing Notes (1) and (2)

Maturity	Amount Outstanding ($000)	Interest Rate	Call Date	Redemption Price	Promissory Notes
12/01/06	$ 2,000	7.500%	Currently	100%	$ TBD
12/01/06	27,375	7.500	Currently	100	TBD
12/01/09	19,100	7.800	Currently	100	TBD
10/01/12	17,200	8.250	Currently	100	TBD
3/01/16	150,000	Variable	AIPD	100	TBD
9/01/19	50,000	7.150	6/15/02	102	TBD
9/01/19	50,000	7.150	6/15/02	102	TBD
6/01/20	100,000	7.150	6/15/02	102	TBD
12/01/20	100,000	7.150	6/15/02	102	TBD
2/01/22	50,000	7.150	6/15/02	102	TBD
2/01/22	50,000	7.150	6/15/02	102	TBD
8/01/22	50,000	6.900	1/21/03	102	TBD
8/01/22	50,000	6.900	1/21/03	102	TBD
11/01/23	50,000	Variable	AIPD	100	TBD
11/01/23	50,000	Variable	AIPD	100	TBD
10/01/24	50,000	Variable	AIPD	100	TBD
8/01/25	50,000	Variable	AIPD	100	TBD
	$915,675				$246,400(3)

AIPD = Any Interest Payment Date TBD = To Be Determined

(1) NYSERDA Financing Notes Series 1997A due 12/01/27 in the principal amount of $24,880,000 and bearing variable interest rates are to be transferred to BL Holding Corp or one of the BL Holding Corp Subs.

(2) The NYSERDA Financing Notes were issued pursuant to certain Participation Agreements between NYSERDA and LILCO to evidence the obligation of LILCO to repay debt service on NYSERDA bonds issued to finance LILCO projects. Certain of the

NYSERDA Financing Notes are currently supported by bank letters of credit which may be terminated at the time of the LIPA/LILCO Merger Transaction. As a precondition to the delivery of the Offered Securities, LIPA must obtain waivers of such termination rights or substitute letters of credit or refinance the NYSERDA Financing Notes.

(3) LIPA Sub will receive Promissory Notes estimated to be approximately $246,400,000 in aggregate principal amount. The amount of Promissory Notes delivered at the LIPA/LILCO Merger Closing will be determined in accordance with the terms of the LIPA/LILCO Merger Agreement and are subject to post closing audit adjustment. The interest rate and maturity of the Promissory Notes will match the NYSERDA Financing Notes to which the Promissory Notes are allocated in accordance with the LIPA/LILCO Merger Agreement.

LIPA Financings

LIPA anticipates that the first tranche of its financings under the Plan of Finance will be approximately $4.950 billion, comprised of $3.450 billion of long term fixed rate bonds and $1.500 billion of variable rate Subordinated Indebtedness supported by direct pay letters of credit from certain commercial banks. The estimated sources and uses of funds for each of the three tranches are summarized in the chart below. The number, size and timing of these tranches, the application of the proceeds of tranches two and three, and the principal amounts of fixed rate Bonds and variable rate Subordinated Indebtedness, are subject to change, depending on numerous factors, including market conditions.

Plan of Finance

Estimated Sources and Uses of Funds

	Tranche One	Tranche Two	Tranche Three	Total
Estimated Sources of Funds				
Fixed Rate Bonds	$3,449,527,638	$863,960,000	$1,151,570,000	$5,465,057,638
Variable Rate Subordinated Indebtedness	1,500,000,000	—	—	1,500,000,000
Original Issue Premium	8,776,638	—	—	8,776,638
Accrued Interest	12,994,870	—	—	12,994,870
Accrued Interest Paid by LILCO	36,212,529	—	—	36,212,529
Total	$5,007,511,675	$863,960,000	$1,151,570,000	$7,023,041,675
Estimated Uses of Funds				
Cash Purchase Price for Common Stock	$2,497,500,000			$2,497,500,000
Preferred Stock Redemption	339,100,000			339,100,000
Redemption of G&R Bonds	1,217,840,775	—	—	1,217,840,775
Refinance Debentures	476,290,880	$148,801,800	$1,140,349,108	1,765,441,788
Refinance NYSERDA Financing Notes		687,297,547		687,297,547
Shoreham Rebates and Credits	142,500,000			142,500,000
Capital Expenditures	135,000,000			135,000,000
Clean energy and rate payer advocacy programs	21,000,000			21,000,000
Purchase of Interest Rate Hedge(1)	64,924,912	—	—	64,924,912
Reimbursement of advances	35,159,949	—	—	35,159,949
Original issue discount	—	20,380,648	1,581,634	21,962,282
Accrued Interest	12,994,870	—	—	12,994,870
Credit Enhancement Fees, Underwriters' Discount and Costs of Issuance	65,200,289	7,480,005	9,639,258	82,319,552
Total	$5,007,511,675	$863,960,000	$1,151,570,000	$7,023,041,675

(1) LIPA will purchase from BUG/LILCO Hedge Fund L.P. an interest rate hedge previously entered into for LIPA's benefit.

ACCELERATED DEBT RETIREMENT

LIPA's Trustees have approved a plan which contemplates (but does not require) using excess cashflow from debt service coverage and favorable budget variances to accelerate the retirement of the portion of debt issued under the Plan of Finance relating to the $4.2 billion intangible asset principally attributable to the Shoreham Regulatory Asset (the Acquisition Adjustment reflected on LIPA's pro-forma consolidated balance sheet in Appendix B to Part 2 of this Official Statement). LIPA intends to effect the accelerated retirement of debt through a combination of (i) open market purchases and tender offers; (ii) cash defeasances; (iii) exercise of LIPA's optional redemption rights; and (iv) up to $850 million of additional scheduled amortization in the period ending December 1, 2013 in tranches two and/or three. LIPA estimates that implementation of this plan would enable it to retire this portion of the debt in approximately 16 years while amortizing the remaining debt under the Plan of Finance and future financings on a level debt service basis.

This accelerated debt retirement, if accomplished, will have a significant impact on the average life of LIPA's debt issued under the Plan of Finance maturing after December 1, 2013. LIPA presently estimates that more than $2 billion of excess cash flow will be available for the accelerated retirement of a portion of the approximately $3 billion of fixed rate Bonds and $1.5 billion of variable rate Subordinated Indebtedness expected to mature after December 1, 2013. The potentially significantly shorter average life of Bonds maturing after December 1, 2013, will affect, among other things, the cost effectiveness of bond insurance purchased in the secondary market for such Bonds.

FUTURE FINANCING ACTIVITIES

LIPA anticipates issuing debt in the future for a variety of purposes including the funding of capital expenditures for the T&D System and NMP2, refinancing Bonds or Subordinated Indebtedness to the extent economically attractive, funding future installments of the Shoreham Credits, and funding the Generation Purchase Option, if exercised.

Unless otherwise funded in whole or in part from revenues, LIPA anticipates the issuance of approximately $136 million to $156 million of Bonds during each full year of the Study Period for capital projects, which issuances are reflected in the Independent Consultant's Report attached as Appendix A to this Part 2. In addition, LIPA expects to issue $320 million of Bonds over the next four years to fund the Shoreham Credits, which issuances are also reflected in the Independent Consultant's Report attached as Appendix A to this Part 2.

If LIPA exercises its fair market value option to acquire the GENCO Generating Facilities during the fourth year after the acquisition, it is anticipated that such purchase would be funded through the issuance of LIPA Bonds. As of March 31, 1998, the net book value of the GENCO Generating Facilities was approximately $500 million. However, the exercise of this option will require PACB approval which under the LIPA Act will necessitate a determination, among other things, that such exercise is "financially feasible" and results generally in lower electric rates. The Independent Consultant's Report assumes that such option will not be exercised.

The Resolution permits the use of, and LIPA will evaluate the merits of using, various derivative products to hedge its ongoing exposure to interest rate risk or to minimize its costs of borrowing, including swap-based derivatives such as synthetic fixed or floating rate debt.

PROJECTED REVENUE REQUIREMENTS AND DEBT SERVICE COVERAGE

General

The Independent Consultant's Report dated April 27, 1998, attached as Appendix A to this Part 2, presents projections and forward looking statements related to LIPA's annual revenues and revenue requirements for the period June 1, 1998 through December 31, 2008 (the "Study Period"). RMI's projections are based in part upon the terms of the LIPA/LILCO Merger Agreement and the Operating Agreements, the related current capital requirements funded in accordance with the Plan of Finance and the future financing activities described above. These revenue estimates also reflect the rates adopted by LIPA on April 9, 1998 which, together with the Shoreham Credits, provide for an immediate average rate reduction of 20%.

THE PROJECTED OPERATING RESULTS FROM THE INDEPENDENT CONSULTANT'S REPORT ARE PRESENTED BELOW. THESE PROJECTIONS ARE PREDICATED UPON ASSUMPTIONS PRESENTED IN THE INDEPENDENT CONSULTANT'S REPORT. NEITHER RMI NOR LIPA MAKE ANY REPRESENTATION THAT THESE ASSUMPTIONS WILL, IN FACT, OCCUR. THESE PROJECTIONS MAY BE AFFECTED FAVORABLY OR UNFAVORABLY BY UNFORESEEN FUTURE EVENTS, AND THEREFORE, TO THE EXTENT CONDITIONS DIFFER FROM THOSE ASSUMED IN THE INDEPENDENT CONSULTANT'S REPORT, THE RESULTS THAT WILL BE ACHIEVED BY LIPA WILL VARY FROM THOSE PROJECTED. THE ASSUMPTIONS WHICH FORM THE BASIS FOR THESE PROJECTIONS AND THE CONCLUSIONS DRAWN BY RMI ARE DISCUSSED IN THE INDEPENDENT CONSULTANT'S REPORT WHICH MUST BE READ IN ITS ENTIRETY FOR AN UNDERSTANDING OF THE PROJECTIONS, ASSUMPTIONS, AND CONCLUSIONS.

Projected Operating Results
($000)

	1998(1)	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
RETAIL ELECTRICITY SALES (GWH)	10,047	16,678	16,960	17,257	17,466	17,701	17,880	18,060	18,277	18,483	18,670
REVENUE											
Retail Sales Revenues (Tariff Rates)(2)	$1,330,445	$2,118,010	$2,153,741	$2,191,524	$2,218,080	$2,270,370	$2,316,269	$2,362,968	$2,415,239	$2,466,937	$2,516,775
RICO Credit(3)	(38,387)	(60,000)	(25,000)	—	—	—	—	—	—	—	—
Shoreham Settlement Surcharge (Credit)(4)	(49,213)	(84,365)	(84,365)	(84,365)	(84,365)	(16,250)	24,595	33,439	42,282	51,126	51,126
Fuel and Purchased Power Cost Adjustment(5)	—	—	(1,001)	—	—	3,326	56,602	53,322	86,132	105,447	115,104
Total Retail Sales Revenues	$1,242,846	$1,973,646	$2,043,375	$2,107,159	$2,133,715	$2,257,446	$2,397,467	$2,449,728	$2,543,653	$2,623,510	$2,683,004
Miscellaneous Revenues(6)	5,133	9,186	9,587	10,008	10,453	10,817	11,196	11,592	12,004	12,434	12,882
Total Revenues	$1,247,979	$1,982,832	$2,052,962	$2,117,167	$2,144,168	$2,268,263	$2,408,663	$2,461,320	$2,555,657	$2,635,944	$2,695,887
REVENUE REQUIREMENTS											
Operating Expenses											
Nine Mile Point 2 Expenses(7)	$ 19,374	$ 35,478	$ 33,795	$ 35,097	$ 34,576	$ 35,868	$ 36,119	$ 37,444	$ 37,706	$ 39,106	$ 39,413
Fuel for GENCO Units(8)	174,196	276,442	292,051	307,282	290,243	295,869	305,791	317,283	326,873	336,921	317,768
Purchased Power Costs(9)	208,960	350,353	356,698	357,921	399,826	428,491	424,492	452,064	470,567	477,422	550,035
GENCO Power Costs(10)	177,735	307,062	310,881	315,943	320,633	324,702	329,940	336,516	344,880	358,341	376,359
Energy Management Services(11)	934	2,065	2,590	2,892	3,153	3,649	4,081	4,289	4,399	4,469	4,541
Total Power Supply Costs	$ 581,199	$ 971,401	$ 996,014	$1,019,134	$1,048,431	$1,088,578	$1,100,422	$1,147,597	$1,184,425	$1,216,259	$1,288,116
T&D Management Services(12)	$ 158,139	$ 268,022	$ 263,710	$ 271,211	$ 270,981	$ 271,318	$ 273,928	$ 278,803	$ 283,293	$ 290,943	$ 297,112
Other Operating and Maintenance Costs(13)	34,364	55,954	57,429	58,911	61,895	64,979	65,038	65,122	66,267	67,428	68,599
Total Operating Expenses	$ 773,702	$1,295,377	$1,317,154	$1,349,257	$1,381,307	$1,424,875	$1,439,388	$1,491,522	$1,533,984	$1,574,630	$1,653,826
Net Operating Revenue	$ 474,277	$ 687,454	$ 735,808	$ 767,910	$ 762,861	$ 843,388	$ 969,275	$ 969,798	$1,021,673	$1,061,314	$1,042,060
Other (Income) and Deductions											
Interest Income(14)	$ (8,264)	$ (18,405)	$ (16,751)	$ (16,505)	$ (16,285)	$ (16,258)	$ (19,610)	$ (19,188)	$ (19,961)	$ (20,466)	$ (19,739)
Funding for RICO Credit(15)	(36,401)	(56,896)	(23,707)	—	—	—	—	—	—	—	—
BL Holding Corp Promissory Notes Receipts(16)	(34,090)	(465,180)	(39,199)	(39,199)	(39,199)	(39,199)	(39,199)	(39,199)	(66,414)	(37,158)	(37,158)
Payments in Lieu of Taxes(17)	117,582	276,712	279,369	282,214	283,427	294,149	311,476	323,947	338,974	353,873	367,662
Total Other (Income) and Deductions	$ 38,828	$ (263,769)	$ 199,712	$ 226,510	$ 227,943	$ 238,692	$ 252,666	$ 265,560	$ 252,599	$ 296,249	$ 310,765
Debt Service Payments											
Base Level Senior Lien Debt(18)	$ 114,244	$ 367,875	$ 374,699	$ 383,649	$ 391,205	$ 413,627	$ 429,315	$ 445,020	$ 460,776	$ 476,655	$ 484,241
Mandatory Senior Debt Acceleration (19)	—	35,535	37,100	38,825	40,730	42,785	44,970	47,285	49,790	52,480	55,340
Total Senior Lien Debt	$ 114,244	$ 403,410	$ 411,799	$ 422,474	$ 431,935	$ 456,412	$ 474,285	$ 492,305	$ 510,566	$ 529,135	$ 539,581
Subordinate Debt(20)	33,750	67,500	67,500	67,500	67,500	67,500	67,500	67,500	67,500	67,500	67,500
Interest on Assumed LILCO Debentures(21)	14,763	—	—	—	—	—	—	—	—	—	—
Reimbursable Debt(22)	34,090	465,180	39,199	39,199	39,199	39,199	39,199	39,199	66,414	37,158	37,158
Total Scheduled Debt Service Payments	$ 196,847	$ 936,090	$ 518,498	$ 529,173	$ 538,634	$ 563,111	$ 580,984	$ 599,004	$ 644,480	$ 633,793	$ 644,239
Interest Savings on Defeased Debt(23)	$ —	$ —	$ (7,505)	$ (13,403)	$ (19,330)	$ (24,696)	$ (28,248)	$ (37,444)	$ (45,451)	$ (54,993)	$ (65,445)
Net Debt Service Payments	$ 196,847	$ 936,090	$ 510,993	$ 515,770	$ 519,303	$ 538,415	$ 552,736	$ 561,560	$ 599,029	$ 578,800	$ 578,793
Total Revenue Requirements	$1,009,377	$1,967,699	$2,027,859	$2,091,537	$2,128,554	$2,201,982	$2,244,790	$2,318,641	$2,385,612	$2,449,679	$2,543,385
Net Cash Flow from Operations	$ 238,602	$ 15,133	$ 25,103	$ 25,630	$ 15,614	$ 66,281	$ 163,873	$ 142,679	$ 170,045	$ 186,265	$ 152,502

Note: Totals may not add due to rounding.

Projected Operating Results
($000)

	1998(1)	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
CALCULATION OF RATE STABILIZATION FUND BALANCE											
Beginning Balance(24)	$ —	$ 288,602	$ 249,990	$ 250,004	$ 250,004	$ 250,013	$ 252,984	$ 252,992	$ 252,991	$ 252,995	$ 253,001
Initial Fund Deposit(25)	71,000	—	—	—	—	—	—	—	—	—	—
Net Accounts Payable(26)	(101,000)	—	—	—	—	—	—	—	—	—	—
Net Cash Flow from Operations(27)	238,602	15,133	25,103	25,630	15,614	66,281	163,873	142,679	170,045	186,265	152,502
Shoreham Settlement Bond Proceeds(28)	80,000	80,000	80,000	80,000	80,000	—	—	—	—	—	—
Draw for Optional Accelerated Principal Repayment(29)	—	(133,745)	(105,090)	(105,630)	(95,605)	(63,310)	(163,865)	(142,680)	(170,040)	(186,260)	(152,525)
Ending Balance(30)	$ 288,602	$ 249,990	$ 250,004	$ 250,004	$ 250,013	$ 252,984	$ 252,992	$ 252,991	$ 252,995	$ 253,001	$ 252,977
DEBT SERVICE COVERAGE											
Net Cash Flow from Operations(27)	$ 238,602	$ 15,133	$ 25,103	$ 25,630	$ 15,614	$ 66,281	$ 163,873	$ 142,679	$ 170,045	$ 186,265	$ 152,502
Add Back:											
Payments in Lieu of Taxes(17)	117,582	276,712	279,369	282,214	283,427	294,149	311,476	323,947	338,974	353,873	367,662
Shoreham Settlement Bond Proceeds(28)	80,000	80,000	80,000	80,000	80,000	—	—	—	—	—	—
Total Debt Service Payments(27)	196,847	936,090	518,498	529,173	538,634	563,111	580,984	599,004	644,480	633,793	644,239
Less Interest Savings on Defeased Debt(27)	—	—	(7,505)	(13,403)	(19,330)	(24,696)	(28,248)	(37,444)	(45,451)	(54,993)	(65,445)
Total Available for Coverage	$ 633,032	$1,307,936	$ 895,465	$ 903,614	$ 898,345	$ 898,845	$1,028,084	$1,028,186	$1,108,048	$1,118,939	$1,098,957
Senior Lien Debt Service(31)	$ 114,244	$ 403,410	$ 404,294	$ 409,071	$ 412,604	$ 431,716	$ 446,037	$ 454,861	$ 465,115	$ 474,142	$ 474,135
Coverage on LIPA Senior Lien Debt Service	5.5	3.2	2.2	2.2	2.2	2.1	2.3	2.3	2.4	2.4	2.3
Senior Lien and Subordinated Debt Service	$ 147,994	$ 470,910	$ 471,794	$ 476,571	$ 480,104	$ 499,216	$ 513,537	$ 522,361	$ 532,615	$ 541,642	$ 541,635
Coverage on Senior Lien and Subordinated Debt	4.3	2.8	1.9	1.9	1.9	1.8	2.0	2.0	2.1	2.1	2.0
Total Debt Service(32)	$ 196,847	$ 936,090	$ 510,993	$ 515,770	$ 519,303	$ 538,415	$ 552,736	$ 561,560	$ 599,029	$ 578,800	$ 578,793
Coverage on Total Debt	3.2	1.4	1.8	1.8	1.7	1.7	1.9	1.8	1.8	1.9	1.9

Note: Totals may not add due to rounding.

Projected Operating Results
($000)

ANALYSIS OF REVENUE	1998(1)	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Retail Electricity Sales (GWH)	10,047	16,678	16,960	17,257	17,466	17,701	17,880	18,060	18,277	18,483	18,670
Retail Sales Revenues (Tariff Rates)(33)	$1,330,445	$2,118,010	$2,153,741	$2,191,524	$2,218,080	$2,270,370	$2,316,269	$2,362,968	$2,415,239	$2,466,937	$2,516,775
Average Annual Revenue per kWh (cents)(34)	12.70	12.70	12.70	12.70	12.70	12.83	12.95	13.08	13.21	13.35	13.48
Year to Year Rate Increases		0.0%	0.0%	0.0%	0.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%
Percent Reduction from LILCO Rates(35)	16.6%	16.6%	16.6%	16.6%	16.6%	15.8%	14.9%	14.1%	13.2%	12.4%	11.5%

References in the following Notes to the Exhibit and to specific pages or locations refer to Exhibit 1 to Appendix A to Part 2 of this Official Statement.

NOTES:

(1) June 1 through December 31, 1998.
(2) Based on average revenue per kWh shown on Page 3 of this Exhibit.
(3) Paid in accordance to the settlement between LILCO and its ratepayers. Includes effect of gross receipts tax.
(4) Paid in accordance with the Shoreham Settlement. Includes effect of gross receipts tax
(5) Calculated in accordance with the FPPCA.
(6) These include revenues such as street light rents, late payment charges, and dishonored check charges.
(7) Includes nuclear fuel expense, operation and maintenance expense, and funding for decommissioning.
(8) LIPA's cost for oil and natural gas.
(9) Includes cost of purchased capacity and energy (excluding costs incurred under the PSA), and transmission costs net of wholesale wheeling revenues. These costs are paid directly by LIPA.
(10) In accordance with the PSA including an allowance for incentive payments.
(11) In accordance with the EMA including an allowance for incentive payments.
(12) In accordance with the MSA including an allowance for incentive payments.
(13) Includes general and administrative costs.
(14) Interest earnings on bond proceeds for construction purposes until the proceeds are spent and interest earnings on the Rate Stabilization Fund. Interest earnings rate assumed to be 5 percent per annum.
(15) BL Holding Corp provides the funds for the RICO Credit net of gross receipts tax.
(16) Receipts from BL Holding Corp Promissory Notes held by LIPA for repayment of certain assumed debt (see note 22).
(17) These include payments to various taxing jurisdictions for NMP2, the T&D System, and Shoreham property taxes, gross receipts taxes, and Metropolitan Transportation Authority surcharge.
(18) Includes the portion of the Bonds that are not accelerated (see note 19) and the Additional Bonds. Bonds issued during tranche 1 are assumed to bear interest at 5.72 percent. Bonds issued during tranches 2 and 3 are assumed to bear interest at 6.0 percent. Additional Bonds issued to finance the Shoreham Settlement are assumed to bear interest at 6.5 percent per year. All other Additional Bonds are assumed to bear interest at 6.25 percent per year.
(19) Scheduled accelerated payments of the Bonds. Please refer to the section entitled "ACCELERATED DEBT RETIREMENT" in the Official Statement.
(20) Variable rate debt assumed at 4.5 percent including line of credit and remarketing.
(21) Interest payments due on debentures assumed from LILCO prior to refinancing by LIPA.
(22) Debt for which BL Holding Corp is obligated to pay. Please refer to Part 1 of the Official Statement, "PURPOSE OF THE OFFERED SECURITIES AND THE INITIAL SUBORDINATED INDEBTEDNESS—Debt Service."
(23) The interest savings on principal that is paid early through the optional accelerated principal repayment (See Note 29).
(24) Ending balance from the prior year.
(25) Cash received at Closing.
(26) Contractual level of initial accounts payable.
(27) From Exhibit 1, page 1 of 4.
(28) Proceeds of Bonds and Additional Bonds issued to finance the Shoreham Settlement (see note 4).
(29) Amount to be applied to accelerated repayment of debt, as supplied by financial advisor, and as shown in the "Calculation of Rate Stabilization Fund Balance" section of this Exhibit.
(30) Balance in the Rate Stabilization Fund on December 31 of each year.
(31) Senior lien debt, less interest savings on defeased debt, from Exhibit 1, page 1 of 4.
(32) Includes senior lien debt, subordinated indebtedness, and reimbursable debt.
(33) Excludes impact of RICO Credit, Shoreham Settlement, and the FPPCA.
(34) Average unit revenue for 1998 is annualized.
(35) Rate reduction computed from LILCO's rates in effect July 16, 1997 (the date of the PACB's approval of the Agreements), which rates remain in effect today. Ten year average reduction is 15.1 percent. Both LILCO's rates and LIPA's rates exclude the impact of pass-through adjustments and RICO credits.

Note: Totals may not add due to rounding.

Conclusions

In its Independent Consultant's Report, RMI has drawn a number of conclusions which are restated below. THE CONCLUSIONS ARE DEPENDENT ON THE ANALYSES, INVESTIGATIONS, AND ASSUMPTIONS DISCUSSED IN THE INDEPENDENT CONSULTANT'S REPORT. THE INDEPENDENT CONSULTANT'S REPORT MUST BE READ IN ITS ENTIRETY BEFORE RELIANCE IS PLACED ON THE CONCLUSIONS CONTAINED THEREIN.

1. The Retained Assets, in combination with the common plant, the rights of LIPA under the Agreements (as defined in the Independent Consultant's Report, which Agreements include the LIPA/LILCO Merger Agreement and the Operating Agreements, among others), and the obligations of BL Holding Corp and its affiliates, provide LIPA with the facilities, labor, management, and related resources required to operate and maintain the T&D System in accordance with prudent utility practices and the requirements of the Resolution.

2. The reliability of the T&D System, as measured by the Customer Average Interruption Duration Index, has improved dramatically during the last three years as the result of programs undertaken by LILCO and is equal to or better than the corresponding reliability levels of the transmission and distribution systems of the other five large electric utilities in the State of New York with predominantly overhead electric transmission and distribution systems.

3. The T&D System is in good condition and, with maintenance and capital expenditures at levels reflected in Exhibit 1 to the Independent Consultant's Report, can be operated throughout the Study Period at levels of reliability consistent with those experienced by the T&D System in the past three years. With continued maintenance and capital expenditures in accordance with prudent utility practice, the T&D System can reasonably be expected to achieve levels of reliability beyond 2008 that are comparable to those experienced during the Study Period.

4. Based upon NRC documents, FERC Form 1 filings, LILCO and Niagara Mohawk Annual Reports to the PSC, and interviews with (i) LILCO NMP2 oversight staff; and (ii) the non-operating co-tenants' representatives, RMI is not aware of regulatory compliance or operational problems with NMP2 which would result in operating costs or capital expenditures materially different from those reflected in the estimated Operating Results as set forth in Exhibit 1 of the Independent Consultant's Report or which would jeopardize the operation of NMP2 through the end of its operating license.

5. LIPA's anticipated annual transfers to the NMP2 decommissioning fund, combined with the balances in such fund as of December 31, 1997, and interest accruals thereon, will be sufficient to satisfy LIPA's share of the forecast of NMP2 decommissioning costs prepared during 1995 on behalf of Niagara Mohawk by ABZ Inc.

6. NMP2's non-fuel operation and maintenance costs, as reflected in Exhibit 1 of the Independent Consultant's Report, are comparable to the costs incurred at nuclear plants of similar design and vintage and can be expected to remain within the range of peer group costs throughout the Study Period. With maintenance and capital expenditures in accordance with prudent utility practices, NMP2's non-fuel operation and maintenance costs can reasonably be expected to continue within this range, adjusted for general inflation rates, beyond 2008.

7. Existing and additional power supply resources will be available to reliably meet the electric capacity and energy requirements of the T&D System for the Study Period.

8. Based on FERC Form 1 filings, LILCO operations and maintenance reports, interviews with LILCO staff, and RMI's observations of the GENCO generating unit sites and facilities, RMI is not aware of regulatory compliance or operational problems with the GENCO generating units which would result in operating costs or capital expenditures materially different from those reflected in the estimated Operating Results shown in Exhibit 1 of the Independent Consultant's Report or which would jeopardize the operation of the GENCO generating units for the duration of the 15-year PSA.

9. With reasonable capital improvements and maintenance levels, as reflected in the estimated Operating Results, the GENCO facilities as a group will be able to operate near their present rated capacity and near their recent availability levels for the duration of the 15-year PSA.

10. In accordance with the provisions of the EMA, the Energy Manager will be able to secure sufficient natural gas and fuel oil supplies, transportation, and storage to deliver fuel to the GENCO generating units on behalf of LIPA as necessary to operate the GENCO plants at the rates of production, and at the times needed, to achieve the energy production assumed in the projected Operating Results in the Independent Consultant's Report.

11. The staff and management personnel employed by the Manager, GENCO, and the Energy Manager have, as a whole, extensive and varied experience operating and maintaining the Retained Assets and the GENCO facilities, are highly qualified to perform the duties required of them by LIPA, and will be able to fulfill their obligations under the Agreements (as defined in the Independent Consultant's Report, which Agreements include the LIPA/LILCO Merger Agreement and the Operating Agreements, among others).

12. Through a combination of its own staff, outsourced professional services, and the Trustees' guidance, LIPA will be able to provide appropriate policy, financial, and management control over the Manager, GENCO, and the Energy Manager to operate and maintain the T&D System in accordance with prudent utility practices and to secure adequate power supply resources for LIPA's customers, all at expenditure levels consistent, on average, with those reflected in the estimated Operating Results set forth in Exhibit 1 to the Independent Consultant's Report.

13. Incentives contained in the MSA provide an economic inducement for the Manager to maintain reliable service, read meters accurately and on a timely basis, answer customer calls promptly and respond effectively, and protect worker safety. When taken together, these incentives are expected to be sufficient to provide meaningful inducement to manage the T&D System and to successfully achieve the targeted levels of performance contained in the MSA.

14. LIPA can reasonably expect that there will be competition for the continuation of the types of services provided by the Manager under the MSA following its term, and that it will be able to retain a qualified manager of the T&D System at costs comparable to the fees paid the Manager under the MSA.

15. LIPA's implementation of a retail choice program will not adversely impact net revenues pledged to the repayment of the Bonds and the Subordinated Indebtedness.

16. Self-generation, in addition to that already in operation, is unlikely to result in a material reduction in LIPA's revenues available for debt service.

17. Formation of new municipal utilities on Long Island are not expected to occur due to the risk and expense of undertaking such municipalization efforts and the lack of reasonable expectation of electric customer rate savings from municipalization, as compared to the Average System Rates to be charged by LIPA.

18. Conversion of existing electric end uses to natural gas is not likely to occur at levels that will materially affect the estimate of LIPA's annual capacity and energy requirements shown in Exhibits 7 and 8 of the Independent Consultant's Report.

19. Based upon information provided by LILCO and independent review performed by and on behalf of RMI, expected insurance proceeds and indemnification by BL Holding Corp, together with other available moneys, provide LIPA access to funding levels consistent with prudent utility practice to remove environmental liabilities arising during the Study Period associated with the Retained Assets which are known or suspected at the time of Closing.

20. The fuel and purchased power cost adjustment clause provides an effective and consistent mechanism for recovering fuel, purchased power, and load reduction program cost variations from LIPA's electric customers.

21. Revenues from the sale of electricity and from other sources will be sufficient to meet LIPA's annual revenue requirements, including debt service and debt service coverage requirements on the Bonds and the Subordinated Indebtedness during the Study Period.

22. Absent emergency conditions and extraordinary unforeseeable events, LIPA is expected to achieve average rate reductions of no less than 14 percent over a ten year period commencing on the date when LIPA begins providing electric service, when measured against LILCO's base rates in effect July 16, 1997. These reductions exclude the impacts of pass-through adjustments, such as those associated with the proposed Shoreham Settlement, the RICO Credit and the fuel and purchase power cost adjustment clause.

23. As shown in Exhibit 1 to the Independent Consultant's Report, LIPA is not expected to implement an increase in average customer rates exceeding 2.5 percent over a 12 month period, within the Study Period.

24. LIPA will be able to comply with the conditions of the July 16, 1997, PACB resolution approving the LIPA/LILCO Merger Agreement.

25. The assumptions upon which the estimated Operating Results shown in Exhibit 1 of the Independent Consultant's Report are based are reasonable for the purposes for which they have been relied on.

SECURITY AND SOURCES OF PAYMENT FOR THE BONDS

The Manager is required to operate the T&D System in accordance with the MSA. Under the MSA, the Manager is required to bill and collect such fees, rates, rents and charges for the use and services of the T&D System as are established by LIPA in accordance with the Bond Resolution and the LIPA Act. See "Billing and Collections."

Pursuant to the LIPA/LILCO Merger Agreement, LIPA Sub will own the T&D System after the LIPA/LILCO Merger Closing. Accordingly, the Financing Agreement contains covenants as to the operation and maintenance of the T&D System, and the Resolution contains covenants of LIPA to enforce the Financing Agreement and assigns to the Trustee certain of LIPA's rights and interests under the Financing Agreement, including the right to bring actions and proceedings for the enforcement of the Financing Agreement.

Pledge of Trust Estate

The Resolution pledges the Trust Estate for the payment of the Bonds and all Parity Obligations subject to the provisions of the Resolution, the LIPA Act and the Financing Agreement permitting certain applications of the Trust Estate and subject to the prior payment of Operating Expenses.

The Resolution authorizes the application of Revenues to certain purposes free and clear of the lien of the pledge. These applications include payment of Operating Expenses from the Operating Expense Fund prior to the deposit of Revenues in the Debt Service Fund. In addition, the Resolution provides that amounts on deposit in the Rate Stabilization Fund may be used for any lawful purpose of LIPA, and amounts retained in the Revenue Fund may be used for any lawful purpose of LIPA or LIPA Sub, as determined by LIPA.

The principal items in the Trust Estate pledged by the Resolution include:

(i) all payments received by LIPA from LIPA Sub under the Financing Agreement, and all rights to receive the same;

(ii) all Revenues and all right, title and interest of LIPA in and to Revenues, and all rights of LIPA to receive the same;

(iii) the proceeds of sale of Bonds until expended for the purposes authorized by the Supplemental Resolution authorizing such Bonds; and

(iv) all funds, accounts and subaccounts established by the Resolution, including securities credited thereto and investment earnings thereon.

LIPA covenants in the Resolution that it will not, and will not permit LIPA Sub to, issue any bonds, notes or other evidences or indebtedness or otherwise incur any indebtedness, other than Bonds or Parity Obligations, secured by a pledge of or other lien or charge on the Trust Estate which is prior to or of equal rank or priority with the pledge made by the Resolution, and that it will not create or cause to be created any lien or charge on the Trust Estate which is prior to or of equal rank or priority with the pledge made by the Resolution.

Payment of Revenues Pursuant to Financing Agreement

Under the Financing Agreement, LIPA Sub transfers to LIPA all of its right, title and interest in and to the Revenues, including all right to collect and receive the same, subject to the provisions of the Financing Agreement and the Resolution providing for the application of Revenues, and consents to the assignment by LIPA to the Trustee of its interest therein.

Revenues are defined in the Resolution to mean all revenues, rates, fees, charges, surcharges, rents, proceeds from the sale of LIPA Sub assets, proceeds of insurance, and other income and receipts, as derived in cash, directly or indirectly from any of LIPA Sub's operations, by or for the account of LIPA or LIPA Sub including but not limited to all payments received by LIPA or LIPA Sub with respect to Promissory Notes, any guaranty of performance under any System Agreement and all

dividends received by LIPA as a result of ownership of any stock or other evidence of an equity interest in LIPA Sub; provided, however, that Revenues shall not include (i) any Transition Charge, (ii) any such income or receipts attributable directly or indirectly to the ownership or operation of any Separately Financed Project, or (iii) any federal or State grant moneys the receipt of which is conditioned upon their expenditure for a particular purpose unless LIPA determines that such moneys constitute Revenues. Revenues also do not include any amounts, or amounts from any sources, as may be specified from time to time by Supplemental Resolution; provided, however, that at such time the applicable additional Bonds tests of the Resolution will be satisfied (whether or not the tests are then required to be met for other purposes) without regard to such amounts. Transition Charge means any rates, fees, charges or surcharges relating to the T&D System or the customers thereof established by irrevocable rate order or other action or instrument, and applicable to or by LIPA or LIPA Sub, in conjunction with the issuance of debt or other securities under a separate resolution, indenture or similar instrument (other than the Resolution) to the extent such rates, fees, charges or surcharges are pledged or otherwise encumbered or conveyed as security for such debt or other securities.

Funds

The Resolution establishes the following Funds: the Construction Fund; the Revenue Fund; the Operating Expense Fund; the Debt Service Fund; the Parity Contract Obligations Fund; the Subordinated Indebtedness Fund; the Subsidiary Unsecured Debt Fund; the PILOTs Fund; and the Rate Stabilization Fund, all to be held by or on behalf of LIPA with the exception of the Debt Service Fund, which is to be held by the Trustee.

Flow of Funds

LIPA is required by the Resolution, as promptly as practicable after receipt thereof by LIPA, to deposit all Revenues in the Revenue Fund. Amounts on deposit from time to time in the Revenue Fund shall be withdrawn and deposited in the following order of priority:

FIRST: to the Operating Expense Fund, the amount determined by LIPA from time to time to be deposited to pay, or to be set aside therein as a reserve for the payment of, Operating Expenses;

SECOND: (A) to the Debt Service Fund, the amounts required to pay or provide for the payment of the Principal Installments and Redemption Price of and interest on Bonds and Parity Reimbursement Obligations; and

(B) to the Parity Contract Obligations Fund, the amount determined by LIPA to be required to be deposited therein to pay or provide for the payment of Parity Contract Obligations;

THIRD: if such amounts are not expected by LIPA to be required to be deposited thereafter for purposes of paragraphs FIRST and SECOND, to the Subordinated Indebtedness Fund, the amount determined by LIPA to be required to be deposited therein to pay or provide for the payment of Subordinated Indebtedness;

FOURTH: if such amounts are not expected by LIPA to be required thereafter for purposes of paragraphs FIRST, SECOND or THIRD above, to the Subsidiary Unsecured Debt Fund, the amount determined by LIPA to be required to be deposited therein to pay or provide for the payment of Outstanding Subsidiary Unsecured Debt (including the Debentures and NYSERDA Financing Notes);

FIFTH: if such amounts are not expected by LIPA to be required thereafter for purposes of paragraphs FIRST, SECOND, THIRD or FOURTH, to the PILOTs Fund, the amount determined by LIPA to be required to be deposited in such Fund to pay or provide for the payment of PILOTs; and

SIXTH: if such amounts are not expected by LIPA to be required thereafter for purposes of paragraphs FIRST, SECOND, THIRD, FOURTH or FIFTH, to the Rate Stabilization Fund, the amount determined by LIPA to be deposited therein to provide for any payments or deposits from Revenues thereafter.

Any moneys remaining in the Revenue Fund may be used for any lawful purpose of LIPA or LIPA Sub, as determined by LIPA, including, but not limited to, the purchase or redemption of any bonds, notes or other obligations of LIPA or LIPA Sub.

Rate Covenant

LIPA covenants in the Resolution to establish and maintain System fees, rates, rents, charges and surcharges sufficient in each Fiscal Year so that Revenues reasonably expected to be produced in such Fiscal Year will be at least equal to the sum of:

(i) 120% (except, after LIPA retires, other than from the proceeds of Bonds or Subordinated Indebtedness, an amount equal to 25% of the Acquisition Debt net of the then outstanding balance of the Promissory Notes, 100%) of Debt Service, and amounts under all Parity Contract Obligations, payable by LIPA in such Fiscal Year;

(ii) 100% of the Operating Expenses payable in such Fiscal Year;

(iii) 100% of the amount necessary to pay all PILOTs payable in such Fiscal Year; and

(iv) 100% of the amount necessary to pay other Required Deposits, all other payments required pursuant to the Resolution and the Financing Agreement, and all other payments required for the System, for such Fiscal Year;

If at any time such fees, rates, rents, charges and surcharges are or will be insufficient to meet the rate covenant, it will not constitute an Event of Default if and to the extent LIPA promptly takes action reasonably expected by LIPA to cure or avoid any such deficiency or to cause the same to be cured or avoided. In addition, the failure in any Fiscal Year to comply with the covenant in clauses (i) (but only to the extent of the excess, if any, over 100% of Debt Service and amounts under all Parity Contract Obligations), (iii) and (iv) above (the "non-debt service and operating expense rate covenant"), will not constitute an Event of Default if LIPA retains a Rate Consultant and a Consulting Engineer for the purpose of reviewing System fees, rates, rents, charges and surcharges and reviewing the System Budget and complies with the following sentence. If the Rate Consultant (relying upon a certificate of the Consulting Engineer) is of the opinion that a schedule of fees, rates, rents, charges and surcharges for the T&D System which would provide funds to meet the requirements specified in the non-debt service and operating expense rate covenant is impracticable at that time and LIPA therefore cannot comply with the non-debt service and operating expense rate covenant, then LIPA will fix and establish such schedule of System fees, rates, rents, charges and surcharges as is recommended in such certificate by the Rate Consultant to comply as nearly as practicable with the non-debt service and operating expense rate covenant, and in such event the failure of LIPA to comply with the non-debt service and operating expense rate will not constitute an Event of Default.

For purposes of the rate covenant, at any time, (i) Revenues includes any amounts withdrawn or expected to be withdrawn thereafter in any Fiscal Year from the Rate Stabilization Fund which were

either (a) on deposit therein prior to such Fiscal Year or (b) proceeds of Bonds or Subordinated Indebtedness issued to fund the Shoreham Credits, (ii) Revenues do not include any proceeds from the sale of Subsidiary assets or proceeds of insurance, and (iii) Debt Service, Parity Contract Obligations, PILOTs and other Required Deposits will not include any amounts expected by LIPA to be paid from any funds, other than Revenues, reasonably expected by LIPA to be available therefor (including without limitation the anticipated receipt of proceeds of sale of Bonds or Subordinated Indebtedness, or moneys not a part of the Trust Estate, expected by LIPA to be used to pay the principal of Bonds, Parity Contract Obligations, Outstanding Subsidiary Unsecured Debt or Subordinated Indebtedness, other than proceeds of Bonds or Subordinated Indebtedness issued to fund the Shoreham Credits), which expectations, if included in a resolution of LIPA or Certificate of an Authorized Representative, will be conclusive.

In addition, LIPA covenants in the Resolution to review, or cause LIPA Sub to review, the adequacy of System fees, rates, rents, charges and surcharges at least annually. Except to the extent required by law, LIPA covenants not to permit LIPA Sub to furnish or supply or cause to be furnished or supplied any product, use or service of the System free of charge (or at a nominal charge) to any person, firm or corporation, public or private, unless LIPA determines that other adequate consideration has been, or is expected to be, received in connection therewith, and to cause LIPA Sub to enforce or cause to be enforced the payment of any and all amounts owing to LIPA Sub for use of the System in accordance with the Financing Agreement.

Additional Bonds Test

The Resolution requires that, as a condition to the delivery of additional Bonds, except Refunding Bonds, LIPA shall deliver to the Trustee the Certificate referred to in either subparagraph (A) or (B), unless not required as described below, as follows:

(A) A Certificate of any Authorized Representative of LIPA setting forth (i) the Revenues for any 12 consecutive calendar months out of the 18 calendar months immediately preceding the month in which such Bonds are to be issued, (ii) the Debt Service, and the amount payable under all Parity Contract Obligations, during such 12 month period for which Revenues are set forth pursuant to clause (i), excluding in each case any amount thereof paid from sources other than Revenues, and (iii) the sum of the Required Deposits for such 12 month period (excluding Required Deposits for the payment of Outstanding Bonds and Parity Obligations), and showing that the amount set forth in clause (i) is at least equal to the sum of (x) 120% of the amount set forth in clause (ii) and (y) 100% of the amount set forth in (iii).

(B) A Certificate of a Rate Consultant setting forth (i) the estimated Revenues for each of the full Fiscal Years in the period beginning with the Fiscal Year in which such Bonds are authenticated and delivered and ending with the fifth full Fiscal Year after such date of authentication and delivery, (ii) the estimated Debt Service, and estimated amounts payable under all Parity Contract Obligations, during each Fiscal Year for which Revenues are estimated pursuant to clause (i), (iii) the projected Debt Service, and projected amounts payable under Parity Contract Obligations, projected to be required for any purpose during each Fiscal Year for which Revenues are estimated pursuant to clause (i), and (iv) the sum of the estimated and projected Required Deposits for each such Fiscal Year (excluding Required Deposits for the payment of Outstanding Bonds and Parity Obligations), and showing that for each such Fiscal Year the amount set forth in clause (i) is at least equal to the sum of (x) 120% of the sum of the amounts set forth in clauses (ii) and (iii), and (y) 100% of the amount set forth in clause (iv). The Rate Consultant may base its estimates and projections upon such factors as it shall consider reasonable, a statement to which effect shall be included in the Certificate.

For purposes of the additional Bonds tests, at any time, (i) Revenues includes any amounts withdrawn or expected to be withdrawn thereafter in any Fiscal Year from the Rate Stabilization Fund which were either (a) on deposit therein prior to such Fiscal Year or (b) proceeds of Bonds or Subordinated Indebtedness issued to fund the Shoreham Credits, (ii) Revenues do not include any proceeds from the sale of LIPA Sub assets or proceeds of insurance, and (iii) Debt Service, Parity Contract Obligations and other Required Deposits will not include any amounts expected by LIPA to be paid from any funds, other than Revenues, reasonably expected by LIPA to be available therefor (including without limitation the anticipated receipt of proceeds of sale of Bonds or Subordinated Indebtedness, or moneys not a part of the Trust Estate, expected by LIPA to be used to pay the principal of Bonds, Parity Contract Obligations, Outstanding Subsidiary Unsecured Debt or Subordinated Indebtedness, other than proceeds of Bonds or Subordinated Indebtedness issued to fund the Shoreham Credits), which expectations, if included in a resolution of LIPA or Certificate of an Authorized Representative, will be conclusive.

The above provisions shall not apply, (i) to the initial Series of Bonds issued under the Resolution, (ii) to any Bonds constituting Acquisition Debt, (iii) to any Bonds for any of the purposes described above under the heading ''Plan of Finance,'' and (iv) at any time after LIPA first shall have retired, other than from proceeds of Bonds or Subordinated Indebtedness, an amount equal to 25% of the Acquisition Debt net of the then outstanding balance of the Promissory Notes.

Subordinated Indebtedness; Acceleration of Initial Subordinated Indebtedness

There is no limit or test for the issuance of Subordinated Indebtedness under the Resolution.

The Subordinated Resolution provides that Subordinated Indebtedness shall not be subject to acceleration of principal or interest except to the extent provided in the supplemental resolution authorizing the issuance thereof. The supplemental resolution authorizing the Initial Subordinated Indebtedness provides that if an event of default occurs under a reimbursement agreement relating to any credit facility (initially, a letter of credit) supporting any series of Initial Subordinated Indebtedness, the related issuer of such credit facility shall have the right to direct the trustee for the Initial Subordinated Indebtedness under the Subordinated Resolution (the ''Subordinated Indebtedness Trustee'') to declare, and upon such direction the Subordinated Indebtedness Trustee shall declare, the principal of all Initial Subordinated Indebtedness of the related series (but no Initial Subordinated Indebtedness of any other series) then outstanding, and the interest accrued thereon, to be due and payable immediately, and upon any such declaration the same shall become and be immediately due and payable. At any time thereafter, such credit facility issuer may direct the Subordinated Indebtedness Trustee to rescind, and upon such direction the Subordinated Indebtedness Trustee shall rescind, any such declaration and annul such default. The Initial Subordinated Indebtedness of each series shall not be subject to acceleration of principal or interest, whether by the Subordinated Indebtedness Trustee or the holders thereof, except as described above in this paragraph.

It will be a condition to the issuance and delivery of the Offered Securities that the Initial Subordinated Indebtedness be issued and delivered simultaneously with the Offered Securities. The Initial Subordinated Indebtedness will be supported by certain direct pay letters of credit having initial terms of three years. The reimbursement agreement relating to such letters of credit provides that, in the event of a default under the reimbursement agreement, the Initial Subordinated Indebtedness may be declared immediately due and payable. Such accelerations would not cause an acceleration of the Offered Securities or affect the priority of the application of Revenues to the payment of the Offered

Securities. In such an event any amounts then available under the Resolution after the payment of Operating Expenses and debt service on any Bonds, including the Offered Securities, and Parity Contract Obligations could be required to be applied to the payment of Initial Subordinated Indebtedness.

LONG ISLAND POWER AUTHORITY

LIPA is a corporate municipal instrumentality and a political subdivision of the State created by the LIPA Act which was enacted in 1986.

The LIPA Act

Pursuant to the LIPA Act, LIPA has all of the powers necessary or convenient to carry out the purposes and provisions of the LIPA Act including, without limitation, to (i) acquire the assets or securities of LILCO; (ii) acquire real or personal property; (iii) enter into agreements or contracts consistent with the exercise of its powers; (iv) borrow money, issue notes, bonds or other obligations and secure its obligations by mortgage or pledge of its property; (v) create or acquire one or more wholly owned subsidiaries; (vi) set its rates and charges; and (vii) make inquiries, investigations and studies necessary to carry out its objectives.

LIPA may enter into agreements to purchase power from the Power Authority of the State of New York (''NYPA''), the State, any State agency, any municipality, any private entity or any other available source (excluding Canada unless negotiated through NYPA) at such price as may be negotiated. LIPA is specifically authorized to provide and maintain generating and transmission facilities and enter into management agreements for the operation of all or any of the property or facilities owned by it. Finally, LIPA may transfer any of its assets to one or more private utilities or municipal gas or electric agencies for such consideration and upon such terms as LIPA may determine to be in the best interest of the gas and electric ratepayers in the Service Area. The LIPA Act permits LIPA to file a petition under Chapter 9 of Title 11 of the United States Bankruptcy Code or take other similar action for the adjustment of its debts. LIPA Sub as a corporation may file a petition under Chapter 7 or Chapter 11 of Title 11 of the United States Bankruptcy Code.

The LIPA Act requires that any resolution authorizing the issuance of bonds contain a covenant by LIPA that it will at all times maintain rates, fees or charges sufficient to pay, and that any contracts entered into by LIPA for the sale, transmission or distribution of electricity shall contain rates, fees or charges sufficient to pay, the costs of operation and maintenance of the facilities owned or operated by LIPA, payments in lieu of taxes, renewals, replacements and capital additions, the principal of and interest on any obligations issued pursuant to such resolution as they become due and payable, and to establish or maintain any reserves or other funds or accounts required or established by or pursuant to the terms of such resolution.

Trustees

LIPA is governed by a fifteen-member board of Trustees who are required under the LIPA Act to be residents of LIPA's Service Area. The Governor appoints nine of the Trustees. Of the six remaining, three are appointed by the Majority Leader of the New York State Senate, and three are appointed by the Speaker of the New York State Assembly. A chairman of the Trustees is also appointed by and serves at the pleasure of the Governor. Each Trustee serves for a staggered term of four years. Pursuant to the LIPA Act the Trustees and the officers of LIPA are not subject to any personal or civil liability resulting from the exercise, carrying out or advocacy of any of LIPA's purposes or powers. Trustees

are entitled to reimbursement for reasonable expenses in the performance of their duties. The By-laws and other instruments of LIPA and LIPA Sub provide for the indemnification of the Trustees, officers and employees of LIPA and the directors, officers and employees of LIPA Sub.

Management and Operations of the System

Administrative Services Agreement. LIPA and LIPA Sub will be parties to an Administrative Services Agreement, dated as of May 1, 1998 (the "Administrative Services Agreement"), which sets forth the terms and conditions under which LIPA will provide personnel, personnel-related services and other services (including management, supervisory, payroll and other services) necessary for LIPA Sub to provide electric service in the Service Area. Except for services of the type and nature provided to LIPA Sub by outside independent agents, attorneys and consultants and for any other services provided under agreements approved by LIPA, LIPA Sub will meet its personnel and personnel-related needs exclusively through the Administrative Services Agreement. The Administrative Services Agreement may be amended from time to time to reflect the changing needs of LIPA and LIPA Sub.

Under the Administrative Services Agreement, the services to be provided by LIPA include, but are not limited to: (i) performance of LIPA Sub's duties and obligations and enforcing its rights under any existing and future contracts between LIPA Sub and any other person, including, but not limited to, the MSA, EMA and PSA, (ii) coordination of services for which LIPA Sub contracts, (iii) coordination of negotiations and studies authorized by LIPA Sub for any project for the supply of power and energy or the provision of transmission capacity to LIPA Sub, (iv) reviewing invoices, (v) disbursement of all funds of LIPA Sub, (vi) preparation of construction and operating budgets on behalf of LIPA Sub, (vii) provision or coordination of all other accounting matters and preparation of billings to, and collection from, LIPA Sub's customers, (viii) coordination of all other matters arising under any agreements relating to any project that LIPA Sub might undertake, (ix) securing information from any persons required to fulfill LIPA Sub's obligations under any agreements arising from the Administrative Services Agreement, the agreements referred to in clauses (i) and (viii), and any project LIPA Sub might undertake, (x) provision or coordination of rate matters, and (xi) provision or coordination of such other services as LIPA Sub determines are required to carry out its business in an economical and efficient manner.

Management. LIPA will manage the performance and cost of electric service on Long Island with a senior management team, while minimizing its total work force and maximizing private sector involvement. LIPA has adopted an organizational structure which provides for eight senior management positions: (i) a chairman, president and chief executive officer; (ii) an executive director; (iii) a chief financial officer; (iv) a chief operating officer; (v) a vice president of power markets; (vi) a general counsel; (vii) a vice president of external affairs; and (viii) vice president and controller.

RMI in the Independent Consultant's Report has concluded, "The staff and management personnel employed by the Manager, GENCO, and the Energy Manager have, as a whole, extensive and varied experience operating and maintaining the Retained Assets and the GENCO facilities, are highly qualified to perform the duties required of them by LIPA, and will be able to fulfill their obligations under the Agreements, including the MSA, PSA, and EMA." RMI has also concluded, "Through a combination of its own staff, outsourced professional services, and the Trustees' guidance, LIPA will be able to provide appropriate policy, financial, and management control over the Manager, GENCO, and the Energy Manager to operate and maintain the T&D System in accordance with prudent utility practices and to secure adequate power supply resources for LIPA's customers, all at expenditure levels consistent, on average, with those reflected in the estimated Operating Results in

Exhibit 1." The Independent Consultant's Report must be read in its entirety for an understanding of the analyses, investigations, and assumptions upon which these conclusions are based.

The officers, and senior management of LIPA which are presently employed by LIPA, with information covering their background and experience, are listed below.

Richard M. Kessel (48) is the Chairman, President and Chief Executive Officer of LIPA. His current term as a LIPA Trustee expires September 7, 2000. Mr. Kessel has served as a LIPA Trustee since LIPA's inception. Mr. Kessel, who first served as LIPA Chairman from 1989 to 1995, was reappointed Chairman in April 1997. Mr. Kessel was appointed as Executive Director and Chairman of New York State's Consumer Protection Board in January 1984 and served until January 1995. Mr. Kessel served as an ex-officio member of Governor Cuomo's Advisory Commission on Liability Insurance. Since 1981, Mr. Kessel has been a member of the Board of Trustees of Nassau Community College. Mr. Kessel is a graduate of New York University. He received his Masters in Political Science from Columbia University.

Patrick Foye (41) is the Deputy Chairman of LIPA. Mr. Foye became a Trustee in September 1995, and his current term expires August 31, 1998. Effective in May, Mr. Foye has been appointed Executive Vice President of Apartment Investment and Management Company, a real estate investment trust and the nation's largest owner and manager of multifamily apartment properties. A partner since 1989 in the law firm of Skadden, Arps, Slate, Meagher & Flom LLP, Mr. Foye specializes in mergers and acquisitions, cross-border transactions, and privatization. Presently co-head of the firm's Privatization Group, Mr. Foye served as managing partner of the firm's offices in Moscow, Budapest, and Brussels from 1992 through 1994. Mr. Foye is a member of Governor Pataki's New York State Privatization Research Council. A frequent speaker on mergers and acquisition issues, Mr. Foye is a graduate of Fordham College and Fordham Law School.

Seth D. Hulkower (40) was appointed Executive Director of LIPA in July 1996. Prior to his appointment at LIPA, Mr. Hulkower was a Vice President of Merrill International Ltd., an energy project development and consulting company. Prior to Merrill International, Mr. Hulkower was a Vice President of JFG Associates, Inc. a financial advisory and management consulting firm. He has also held positions with the consulting firm of Putnam, Hayes, & Bartlett, Inc., New England Power Company and Stone & Webster Engineering Company. Mr. Hulkower received his S.M. in Technology and Policy from the Massachusetts Institute of Technology and his B.S. in Mechanical Engineering and B.A. in Economics from Tufts University.

David P. Warren (44) is the Chief Financial Officer of LIPA. He joined LIPA in January 1998. He is responsible for all financial activities of LIPA including the management of LIPA's proposed Plan of Finance. Prior to his current position, Mr. Warren was Deputy Treasurer of the State of Connecticut where he administered the State's public finance program. Before entering the public sector, Mr. Warren was a vice president in public finance at CS First Boston. Mr. Warren holds a Master's degree in Public and Private Management from the Yale School of Management and a B.A. from Wesleyan University.

Stanley B. Klimberg (53) is the General Counsel of LIPA. He joined LIPA in 1987 as its General Counsel and Acting Executive Director. Before joining LIPA, Mr. Klimberg was General Counsel of the New York State Energy Office from 1979-1987, and before that he was Assistant General Counsel and Staff Counsel of the New York State Public Service Commission. Mr. Klimberg received his law degree (J.D.) from the New York University School of Law and his undergraduate degree (B.A.) in history with high honors from Lehigh University.

Edward P. Murphy, Jr. (54) is Vice President and Controller of LIPA. He joined LIPA in April 1998. Prior to LIPA, Mr. Murphy held several management positions at Brooklyn Union Gas Company. From 1995-1997, he was Vice President for Business Transformation. Mr. Murphy was Vice President for Public Affairs from 1988-1994. From 1982-1987, he served as General Auditor and was Budget Director from 1976-1982. Prior to this, Mr. Murphy held various positions in operations and accounting at Brooklyn Union. Mr. Murphy received his B.S. in Accounting from Clarkson University and attended the Executive Program in Business Administration at Columbia University.

BL HOLDING CORP AND ITS SUBSIDIARIES

General

BL Holding Corp will serve as the parent holding company of several operating companies (some of which may be limited liability companies), including the companies to which LILCO's gas assets, non-nuclear generating assets and common plant (along with related liabilities) are to be transferred as part of the LIPA/LILCO Merger Transaction. BL Holding Corp Subs will provide: (i) certain management services on behalf of LIPA with respect to the operation of the T & D System; (ii) electric capacity to LIPA from the GENCO Generating Facilities; and (iii) energy management services to purchase fuel and electric capacity and energy and manage the scheduling and sale of electric capacity and energy on behalf of LIPA. See "LIPA's Retail Electric Service Business—Operating Agreements" in this Part 2.

BL Holding Corp will also be the parent holding company of KeySpan.

Available Information Regarding LILCO and KeySpan

Additional information on LILCO and KeySpan may be obtained from LILCO's and KeySpan's respective annual reports on Form 10-K and quarterly reports on Form 10-Q as filed with the Securities and Exchange Commission (the "SEC") under the Securities Exchange Act of 1934, as amended (the "1934 Act").

Additional information on both LILCO and KeySpan may be obtained from the Joint Proxy Statement/Prospectus on Form S-4 filed by LILCO and KeySpan with the SEC.

None of this additional information is part of this Official Statement, and LIPA takes no responsibility for the accuracy or completeness thereof.

THE SYSTEM

Service Area

The LIPA Service Area consists of Nassau and Suffolk counties (with certain limited exceptions) and a small portion of Queens in New York City known as the Rockaways. The population of the Service Area was estimated by LILCO at 2.7 million as of January 1, 1997.

RMI reports that in 1997, 49 percent of LILCO's annual revenues were received from residential customers and 48 percent from commercial and industrial customers with the balance derived from sales to other utilities and public authorities. Individual commercial and industrial customers are relatively small with 45% of these customers having peak demand at less than 75kW. The Long Island Rail Road Company, the largest customer in the Service Area, accounted for less than two percent of total sales. See "Appendix A—Independent Consultant's Report—Description of the Service Area."

The Transmission and Distribution System

The T&D System is an integrated transmission and distribution system with electricity delivered to and from the Service Area over five transmission interconnections that will be owned in part by or under contract to LIPA Sub. Two of the T&D System's transmission interconnections are tied to Con Edison's transmission system in Queens, New York and three extend across Long Island Sound to Westchester County, New York or to Connecticut. These interconnections connect the T&D System to utilities outside of the Service Area and enable delivery of (i) capacity and energy produced by NMP2; (ii) additional capacity resources needed to meet the peak demands of LIPA's electric customers; (iii) favorably-priced energy to supplement or displace generation from generating resources within the Service Area; and (iv) excess generation from generating facilities within the Service Area to purchasers outside of the Service Area when market conditions merit.

LIPA Sub's transmission system includes approximately 1,300 miles of overhead and underground lines with voltage levels ranging from 345kV to 23kV. There are 32 transmission substations to step down transmission voltage levels from 345kV or 138kV to 69kV, 33kV or 23kV. The distribution system has 46,029 circuit miles of overhead lines and 10,354 circuit miles of underground lines and approximately 149,000 line transformers.

Nine Mile Point Nuclear Power Station, Unit 2

LIPA Sub will continue to own an 18 percent interest in NMP2, which is part of a two-unit nuclear power station located at a 900-acre site on Lake Ontario near the Town of Scriba, New York. NMP2 is rated at 1,144 MW of capacity and is owned by five co-tenants, including LILCO, under a Basic Agreement dated as of September 22, 1975, which provides for contractual rights, payments and other matters. Under an Operating Agreement among the co-tenants, dated December 29, 1992, Niagara Mohawk has the exclusive operational control of the operation and maintenance of NMP2 under the oversight of a Management Committee (comprised of the co-tenants) for policy making, planning, budgeting, and operational decisions of Niagara Mohawk related to NMP2. This Operating Agreement provides for a sharing of all costs relating to NMP2 by the co-tenants in proportion to their percentage interests in the unit.

RMI reports that NMP2 has generally exceeded average industry performance for the past five years with respect to annual capacity factor. Periodic outages for refueling are being extended to every 24 months rather than every 18 months to improve overall unit capacity factors. Planned and actual outage times have decreased due to improved outage management and fewer emergent problems. See "Appendix A—Independent Consultant's Report—Nine Mile Point Nuclear Power Station, Unit 2."

NMP2 is scheduled for decommissioning in 2026. LIPA's share of the decommissioning costs, based on a site specific study conducted in 1995, is estimated to be $145 million in 1996 dollars ($407 million in 2026 dollars). After the LIPA/LILCO Merger Closing, LIPA Sub will retain title to the balance in LILCO's external trust fund for the decommissioning of the contaminated portion of the NMP2 plant. The balance in the external trust fund as of December 31, 1997 is $17.7 million. LIPA has calculated that an annual contribution of approximately $3 million is required to fully fund the external trust fund to meet LIPA Sub's 18 percent share of the decommissioning costs of decommissioning the contaminated portion of NMP2 by the decommissioning date of 2026. LIPA Sub will also fund approximately $1.2 million annually in an internal fund to fund its share of the decommissioning the non-contaminated portion of NMP2. See, "Appendix A—Independent Consultant's Report—Nine Mile Point Nuclear Power Station, Unit 2."

In August 1997, the NRC issued a final policy statement on the restructuring and economic deregulation of the electric industry. In it, the NRC expressed concern over these developments' effect on the adequacy of decommissioning funds and on operational safety, and it mentioned a number of initiatives it was considering. With respect to joint ownership of nuclear plants, the NRC recognized the industry practice of sharing both plant operating and decommissioning expenses and plant output pro rata, and it favored continuation of that practice. It announced, however, reservation of "the right, in highly unusual situations where adequate protection of public health and safety would be compromised if such action were not taken, to consider imposing joint and several liability on co-owners of more than *de minimis* shares when one or more co-owners have defaulted."

In a subsequent letter, the Commission issued a letter order declining to reconsider or delay implementation of the August 1997 final policy statement, as a group of publicly owned systems had requested that it do. The Commission stated that the policy statement was not binding, did not alter private contractual arrangements, did not affect rights or obligations of licensees, is fully consistent with NRC precedent including the rule proposal above noted, was not intended to create additional uncertainty regarding liability and merely leaves open and gives notice of the possibility that under unusual circumstances the NRC may consider imposing joint and several liability.

Capital Improvement Plan

RMI reports that, during the period 1993 through 1997, LILCO expended an average of approximately $97 million per year on capital expenditures to the T&D System. Such expenditures focused on reliability improvements, capability expansion, new customers, replacements and public works. LIPA and the Manager have agreed on a capital budget of approximately $117 million for the first full year of operation to continue reliability improvements and expansion of service for the T&D System. The Independent Consultant estimates that annual capital expenditures for the T&D System during the Study Period will be $123 to $144 million per year.

Capital expenditures at NMP2 are for plant modifications and nuclear fuel purchases. The 18 percent share of capital expenditures for NMP2 over the past five years has averaged $4.7 million annually for plant modifications and $4.7 million annually for nuclear fuel purchases. The 18 percent share of the capital expenditures projected by Niagara Mohawk, the operating agent for NMP2, for LIPA Sub over the next five years is an average of $2.1 million annually for plant modifications. The annual expenses for capitalized nuclear fuel purchases are estimated by Niagara Mohawk to average $5.7 million during the Study Period. See, "Appendix A—Independent Consultant's Report—The Transmission and Distribution System" and—"Nine Mile Point Nuclear Power Station, Unit 2."

Loads

LIPA's Service Area is characterized by customer usage patterns and weather conditions that result in peak usage during the summer and relatively low annual load factors. LILCO reported that peak usage in the summer of 1997 was 4,140 MW. LILCO has estimated that peak load growth will range between 0.4 percent and 1.3 percent annually on a weather-normalized basis, averaging 0.9 percent over the 1998-2008 period. LILCO estimates that energy growth will range between 1.0 percent and 1.8 percent annually, averaging 1.3 percent over the 1998-2008 period. This load forecast assumes moderate economic growth in the Service Area, consistent with the general economic conditions and low levels of unemployment on Long Island. Residential sales are projected to grow at approximately 1.2 percent per year between 1998 and 2008, while commercial and industrial sales are expected to grow 1.5 percent per year.

The load forecasts prepared by LILCO take into account a price elasticity effect resulting from rate reductions that LIPA is implementing. In addition, LILCO has included in its forecasts the effects of LIPA's conservation program and further reductions resulting from cogeneration or similar installations designed to serve customer loads directly. See "Appendix A—Independent Consultant's Report—System Loads and Resources."

Power Supply

LIPA Sub will rely on existing power supply resources to meet the bulk of its capacity and energy resources during the 1998 through 2008 period. LIPA's 18% interest in NMP2 and its rights to the capacity of the GENCO Generating Facilities are expected to provide 4,178 MW of generating capacity, with on-island independent power producers providing an additional 350 MW of capacity under contract to LIPA Sub. Existing DSM resources and power purchase contracts with on-island municipal utilities and off-island sources are expected to provide 28 MW and 290 MW, respectively, of capacity, for total resources available to LIPA and LIPA Sub, before additional purchases or generation additions, of 4,846 MW during 1998. Taking into account the continuation of existing DSM resources and the availability of existing power supply contracts, existing resources available to LIPA are expected to aggregate 4,972 MW of capacity by the end of 2008.

To satisfy the capacity needs of its electric customers, LIPA Sub is expected to enter into additional power purchase agreements beginning in 1998. The Independent Consultant's Report assumes these agreements will provide an additional 150 MW of capacity during 1998, increasing to 200 MW during 2007, before decreasing to 50 MW in 2008. During 2003, LIPA Sub is assumed to contract for the output of a new 144 MW electric generating facility to be constructed within the Service Area, with an additional 144 MW facility to be available during 2005 and a 219 MW facility during 2008. With these resource additions, total capacity available to LIPA to meet the needs of its customers during 2008 is expected to be 5,529 MW.

Fuel Supply

The Independent Consultant's Report states that, in 1997, 68 percent of the fuel energy for electric generation in GENCO Generating Facilities came from natural gas, with the remainder from residual oil and distillate oils. The Energy Manager will procure fuel needed for generation by GENCO pursuant to the EMA. LIPA is to directly pay for fuel used at the GENCO Generating Facilities. The particular fuel used for generation will depend on generation plant fuel capability, fuel supply and transportation availability, and fuel cost. Most of the GENCO steam units can burn either natural gas or residual oil and certain units are required to burn lower sulfur residual oil or natural gas. Natural gas or distillate fuel is burned in the gas turbines.

LILCO shares eight gas delivery interconnections between its distribution system and the New York gas market. LILCO, Brooklyn Union Gas and Consolidated Edison have entered into the New York Facilities Agreement that provides for use of their joint systems to allow the three parties to receive gas from interstate pipelines connected to all three systems.

Oil is stored on site or at locations accessible by each generation facility. RMI reports that (1) LILCO's oil storage capacity has helped LILCO avoid a fuel oil supply disruption, and (2) conversion of additional generating units to burn natural gas is further reducing exposure to potential oil interruptions. See, "Appendix A—Independent Consultant's Report—Power Supply Agreement."

NMP2 has a contract in place with US Enrichment Corporation for enrichment services and all or part of NMP2's enriched product needs to 2002. See "Appendix A—Independent Consultant's Report —Nine Mile Point Nuclear Power Station, Unit 2."

RATES AND CHARGES

The LIPA Act

The LIPA Act requires that any bond resolution of LIPA contain a covenant that it will at all times maintain rates, fees or charges sufficient to pay the costs of operation and maintenance of facilities owned or operated by LIPA; payments in lieu of taxes; renewals, replacements and capital additions; the principal of and interest on any obligations issued pursuant to such resolution as the same become due and payable; and to establish or maintain any reserves or other funds or accounts required or established by or pursuant to the terms of such resolution.

Rate Covenant

The Rate Covenant satisfies the requirement of the LIPA Act referenced in the preceding paragraph. For a description of the Rate Covenant, see "Security and Sources of Payment for the Bonds—Rate Covenant."

LIPA's Authority to Set Electric Rates

Under current New York law, LIPA is empowered to set rates for electric service in its Service Area without being required by law to obtain the approval of the PSC or any other State regulatory body. However, LIPA has agreed, in connection with the approval of the LIPA/LILCO Merger Transaction by the PACB, that it will not impose any permanent increase, nor extend or reestablish any portion of a temporary rate increase, in average customer rates over a 12 month period in excess of 2.5% without approval of the PSC, following a full evidentiary hearing. Another of the PACB conditions requires that LIPA reduce average rates within the Service Area by no less than 14% over a ten year period commencing on the date when LIPA begins providing electric service when measured against LILCO's base rates in effect on July 16, 1997 (excluding the impact of the Shoreham tax settlement, but adjusted to reflect emergency conditions and extraordinary unforeseeable events).

The projected Operating Results set forth in Exhibit 1 to the Independent Consultant's Report demonstrate that, based on the assumptions set forth therein (including LIPA's interpretation of the PACB conditions) and absent emergency conditions and extraordinary unforeseeable events, LIPA is expected to achieve an average rate reduction of no less than 14% over the ten year period commencing on the date when LIPA begins providing electric service and that LIPA is not expected to need to increase average customer rates in excess of 2.5% over any 12 month period during the Study Period. For purposes of determining compliance with the 2.5% and 14% PACB conditions described in the preceding paragraph, LIPA has interpreted the PACB conditions as allowing the exclusion of increases in the cost of electricity paid by LIPA's customers related to the Shoreham settlement, other pass-through adjustments and any decreases related to the RICO credits. LIPA believes that it will be able to satisfy the 14% PACB condition and that it will be able to obtain any PSC approvals necessary to comply with its obligations under the LIPA Act and under the Resolution. If either the PSC or the PACB were to disagree with LIPA's interpretation of the PACB conditions, it may influence the timing and size of rate increases implemented by LIPA and/or require (i) the modification of that portion of the Plan of Finance which contemplates the accelerated retirement of debt (see "Accelerated Debt Retirement"), (ii) the withdrawal of funds from the Rate Stabilization Fund to avoid or minimize rate increases, or (iii) other action necessary to meet the conditions of the PACB approval.

The average system revenue requirement based on the initial base rates set by LIPA to be charged by LIPA Sub, versus LILCO's existing average system revenue requirements, are presented in the table below.

AVERAGE SYSTEM REVENUES AND REDUCTIONS(1)

	System Average		Nassau/Rockaway Customers		Suffolk County Customers	
	Cents per kWh	Percent Reduction	Cents per kWh	Percent Reduction	Cents Per kWh	Percent Reduction
LILCO's Current Average System Revenue Requirements	15.23	—	15.23	—	15.23	—
Less: LIPA Sub's Base Savings	(2.53)	16.6	(2.53)	16.6	(2.53)	16.6
Less: Shoreham Credits	(0.52)	3.4	(0.66)	4.3	(0.38)	2.5
LIPA Sub's Average System Revenue Requirements	12.18	20.0	12.04	20.9	12.32	19.1

(1) Reflects average revenues for all retail customers. All values exclude effects of RICO credits.

Rate Tariffs and Adjustments

LIPA's initial rates are largely based on LILCO's current rate design to avoid customer confusion and facilitate an efficient transition from LILCO billing to LIPA Sub billing. In addition, LIPA's rates include a fuel and purchased power cost adjustment ("FPPCA"), a PILOT payments recovery rider, the Shoreham Credits and provide for the Suffolk Surcharge.

LIPA's rates include the FPPCA to adjust rates to reflect significant changes in the cost of fuel, purchased power and related costs. The FPPCA is designed such that customers will not pay for average annual increases above an established base fuel and purchased power cost, or receive a credit for decreases below an established base cost, of less than one percent per year. Expenses for fuel and purchased power cost in excess of or below this level will be recovered from or returned to customers beginning the following year. Should fuel and purchased power costs increase in excess of five percent cumulatively over the original base cost, the FPPCA will recover, from that year forward, all costs in excess of the original base.

The LIPA Act requires LIPA to make payments in lieu of taxes ("PILOTs") to municipalities and school districts equal to the property taxes that would have been received by each such jurisdiction from LILCO if the acquisition by LIPA had not occurred, and to make PILOTs for certain New York State and local taxes which would otherwise have been imposed on LILCO. The PILOT payments recovery rider allows for LIPA rate adjustments to accommodate the State PILOTs.

For a description of the Shoreham Credits and the Suffolk Surcharge, see "Shoreham Tax Matters."

BILLING AND COLLECTIONS

General

LIPA Sub customers are billed on a cycle basis, some monthly, others bi-monthly. There are 20 billing cycles within each month.

LILCO's total customer base as of March 1998 was as follows:

Electric only	620,458
Gas only	44,640
Dual service	427,122

Allocation of Cash

The Manager will collect and process daily customer remittances for LIPA Sub. Cash and checks received each day will be deposited to a LIPA bank account for overnight clearing. The Manager will process receipts on a one day lag to determine the amount collected with respect to electric and gas service. Partial payments from dual service customers will be allocated to electric and gas based upon historic usage. On the morning of the second business day, the LIPA bank account will be swept to a separate LIPA account within the Revenue Fund and to a separate BL Holding Corp account based upon the prior five days' average of actual electric and gas receipts. Each week a reconciliation of actual electric and gas receipts versus the estimated allocation will be performed. Any over/under allocation of gas receipts to BL Holding Corp will be collected from/refunded to BL Holding Corp together with interest.

LIPA Sub will adopt current LILCO policies relating to collections, credit, connections and disconnections.

LILCO's revenue collection history over the last five years is as follows.

Year Ended December 31,	Total Accounts Receivable Write-offs ($000)	Total Revenues ($000)	Percent Written-off
1993	$19,041	$2,881,000	0.66%
1994	20,067	3,067,300	0.65
1995	16,437	3,075,100	0.53
1996	22,795	3,150,700	0.72
1997	21,986	3,147,700	0.70
AVERAGE	$20,065	$3,064,400	0.65%

Currently, LILCO does not separately track electric and gas accounts receivable write offs. Hence the figures above represent combined electric and gas information. LILCO management has advised LIPA that it believes the ratio of combined electric and gas receivables write-offs to total revenues is indicative of the ratio for electricity revenues. The projected Operating Results contained in the Independent Consultant's Report reflect a similar level of accounts receivable write-offs.

SHOREHAM TAX MATTERS

Background

Through February, 1992 Suffolk County and the following Suffolk County political subdivisions (collectively, the "Suffolk Taxing Jurisdictions"), the Town of Brookhaven, Shoreham-Wading River Central School District, Wading River Fire District and Shoreham-Wading River Library District, levied and received real estate taxes from LILCO on the Shoreham plant. When LIPA acquired the Shoreham plant in February 1992 it was obligated pursuant to the LIPA Act to make PILOTs. As part of the agreement between LILCO and LIPA providing for the transfer of Shoreham to LIPA, LILCO agreed to fund these payments by LIPA. LILCO has been charging rates in an amount sufficient to make these payments to LIPA. Both LILCO and LIPA contested the assessments, claiming the Shoreham plant was over assessed.

Tax Judgments and Actions

The New York Supreme Court for Suffolk County entered a judgment against Suffolk County and certain of its taxing jurisdictions in favor of LILCO ordering them to refund to LILCO taxes levied and collected from LILCO based on over assessments of Shoreham for the tax years 1976/77 through 1983/84 (excluding 1979/80), plus interest. Pursuant to this judgment, in January 1996 Suffolk County paid to LILCO $81 million.

On March 26, 1997 a judgment was entered in the Supreme Court, State of New York, Suffolk County, on behalf of LILCO against the Suffolk Taxing Jurisdictions ordering them to refund to LILCO property tax overpayments (resulting from over assessments of Shoreham) in an amount exceeding $868 million, including interest. The Court also determined that the Shoreham plant had a value of zero during the period LIPA has owned Shoreham. This judgment is currently on appeal to the Appellate Division of the State of New York.

The New York State Court of Appeals in a separate case has ruled that the LIPA Act does not prohibit LIPA from seeking refunds if it has overpaid PILOTs based on an over assessment of Shoreham. LIPA has made PILOT payments totaling over $327 million which it believes were based on such an over assessment. LIPA believes that it is entitled to a refund of these PILOTs, but has not yet brought a claim for this refund.

Potential Shoreham Property Tax Settlement Agreement

LIPA has proposed to enter into the Shoreham Property Tax Settlement Agreement (the "Shoreham Property Tax Settlement Agreement") with the Suffolk Taxing Jurisdictions and Nassau County. The Shoreham Property Tax Settlement Agreement would settle the Shoreham Property Tax Litigation and provide for refunds to be made to the ratepayers who have borne the expense of the overpayment of property taxes and PILOTs. Pursuant to the terms of the Shoreham Property Tax Settlement Agreement, LIPA would agree to (i) continue to make PILOTs for the Shoreham plant site on a declining basis until 2002; (ii) cause LIPA Sub not to seek to enforce the judgement in favor of LILCO which it will acquire as a result of the LIPA/LILCO Merger; and (iii) not make any claim for a refund of what LIPA believes is an overpayment by it of PILOTs, all in exchange for an agreement by the Suffolk Taxing Jurisdictions to pay $625 million. In order to assist the Suffolk Taxing Jurisdictions in funding the settlement, LIPA would agree to use reasonable efforts to issue bonds, the net proceeds of which will be used to fund the settlement. LIPA would advance such net proceeds to LIPA Sub, which would make a rebate in an amount of $62.5 million in the form of checks transmitted

to Nassau and Rockaways ratepayers (the "Shoreham Rebates"). LIPA Sub would also provide credits against the statements of ratepayers in Nassau County and the Rockaways totaling $50 million a year for five years and credits against the statements of ratepayers in Suffolk County totaling $30 million a year for five years (the "Shoreham Credits"). Both the Shoreham Rebates and the Shoreham Credits would be funded from the proceeds of Bonds to be repaid through a surcharge on the rates of Suffolk County ratepayers (the "Suffolk Surcharge").

LIPA is in negotiations with the Suffolk Taxing Jurisdictions and Nassau County with respect to the Shoreham Property Tax Settlement Agreement. No assurance can be given that the parties will ultimately agree to and execute the Shoreham Property Tax Settlement Agreement.

Other Real Property Tax Matters

All currently pending actions and claims by LILCO for refunds of real property taxes involving property other than Shoreham will also be retained by LIPA Sub as part of the LIPA/LILCO Merger Transaction. LIPA has committed to drop all such tax claims and not challenge any PILOTs relating to its transmission and distribution facilities unless the assessment (other than a generally applicable assessment) on its facilities is increased not in an appropriate proportion to the increase in value related to taxable capital additions affixed to the tax parcel between the last two tax status dates. BL Holding Corp and the BL Holding Corp Subs have agreed not to challenge any property tax relating to generating facilities or generating facility sites (provided the tax is included in the costs paid by LIPA related to such facilities or sites), unless the assessment (other than a generally applicable assessment) on such facilities is increased not in an appropriate proportion to the increase in value related to taxable capital additions affixed to the tax parcel between the last two tax status dates.

REBATES, CREDITS AND SUFFOLK SURCHARGE

As part of the acquisition of LILCO (and whether or not the Shoreham Property Tax Settlement Agreement is executed), LIPA intends to pay rebates in the form of checks to the ratepayers in the Service Area. Funds for the rebates will come from three sources: (i) approximately $82 million anticipated to be received from BL Holding Corp attributable to the class settlement of a civil lawsuit brought against LILCO under the federal Racketeer Influenced and Corrupt Organization Act ("RICO") relating to disclosures made by LILCO to the PSC concerning the construction and completion of Shoreham (the "RICO Rebates") (this source is subject, however, to court approval, following public hearings scheduled to be held in June 1998, of the necessary modification of the RICO settlement agreement to permit an accelerated, appropriately discounted payment by BL Holding Corp of the funds to be distributed pursuant to the settlement); (ii) $19 million attributable to the refund of Shoreham-related property taxes ("Shoreham Phase I Rebate"); and (iii) $62.5 million from the proceeds of Bonds which will be used to fund the Shoreham Rebates. Fifteen million dollars of the funds required for the Shoreham Phase I Rebate will be paid at the LIPA/LILCO Merger Closing to LIPA from funds provided by BL Holding Corp and the balance from monies carried on the balance sheet of LILCO at the time of its merger with LIPA Sub. Both the Shoreham Rebates and Shoreham Credits will be funded from the proceeds of LIPA Bonds to be issued from time-to-time to be repaid from the Suffolk Surcharge.

In the opinion of Adams, Dayter & Sheehan, LLP, State Regulatory Counsel to LIPA, (a) the Shoreham Rebates, Shoreham Credits and Suffolk Surcharge, as approved or provided for by LIPA in its actions adopting its initial rates, are within LIPA's authority under the LIPA Act and LIPA's

approval is rational and not arbitrary and capricious; (b) in the event the Suffolk Surcharge is invalidated by a court of competent jurisdiction in a final adjudication, LIPA possesses the legal authority under the LIPA Act to recover in its retail rates those monies refunded/credited to customers constituting the Shoreham Rebates and Shoreham Credits that would not otherwise be recovered by LIPA; and (c) in the event the Suffolk Surcharge is invalidated by a court of competent jurisdiction in a final adjudication, LIPA possesses the legal authority under the LIPA Act to recover in its retail rates the debt service costs on the Bonds issued to fund the Shoreham Rebates and Shoreham Credits that would otherwise not be recovered by LIPA.

COMPETITION AND THE LIPA PLAN

General

Fostering competition in wholesale and retail electric power markets has become a significant policy goal in many states, including New York, as well as at the federal level. The fostering of competition has been accompanied by, and requires, separating power supply services and costs from electric transmission and distribution services and costs. In New York and many other states, there have been legislative and regulatory actions to promote competition in the supply of power by requiring, among other things, that utilities sell all or part of their non-nuclear generating plants. Federal regulation of transmission has been the focus of increasing action and attention as transmission is viewed as the vehicle for delivery of competitively priced generation to wholesale and retail customers. In general, transmission and distribution is viewed as an inherently monopoly function that must remain regulated.

The LIPA/LILCO Merger Transaction accomplishes the disaggregation of ownership of power supply (with the exception of the 18% interest in NMP2) from the provision of transmission and distribution services in the Service Area. Through the LIPA/LILCO Merger Transaction, the ownership and operation of the transmission and distribution system on Long Island will become LIPA's business and responsibility, while the on-island generating resources will be owned by GENCO. LIPA Sub will continue to own an 18% interest in NMP2, which is not on Long Island and which is operated by Niagara Mohawk.

As discussed below, LIPA has taken several actions to promote an orderly transition to greater competition in power supply and retail customer choice in the power supply markets in the service Area. Retail choice (sometimes called customer choice, retail wheeling, or retail open access) refers to a process by which retail customers choose among competitive suppliers for electric capacity, energy, and ancillary services. The delivery of capacity and energy is provided by the owner and operator of the local transmission and distribution system. Key issues that have surfaced in the movement to retail choice include the level of rate reductions accompanying the restructuring of individual utilities, recovery of stranded investments, and the timetable and methods for implementation of customer choice.

The PSC is in the process of implementing retail competition and industry restructuring for regulated investor-owned utilities through a combination of generic rule-makings and utility-specific restructuring proceedings. Neither LILCO nor LIPA is subject to these proceedings before the PSC, although LIPA has taken these restructuring actions into consideration in establishing its own retail choice plan.

LIPA can make no prediction as to what effect, if any, State or Federal law providing for retail competition will have on its plans for implementing retail competition. See "Certain Factors Affecting the Electric Utility Industry".

Phase-In of Competition on Long Island

Transmission constraints between Long Island and other utility systems significantly limit power supply competition compared to other utilities. LIPA's customer power demands and existing power supply commitments are approximately in balance at present. The power supply resources on Long Island, along with the existing transmission interconnections to Con Ed and other utilities, are sufficient to meet Long Island's present needs. At peak periods, when capacity is most valuable, Long Island can only import approximately 1,000 MW of the approximately 5,000 MW required to meet its peak load and reserve obligations. This contrasts with the situation of most of the other utilities in the State and the rest of the country which have more available transmission access and interconnections. Long Island's significant transmission constraints create substantial market power in the owner of the existing on-island generating facilities. In recognition of this situation, LIPA is taking a two-pronged approach to introducing competition in power supply on Long Island by: (i) maintaining, through the PSA, cost controls on, and the federal rate regulation of, the on-island generation to be owned by GENCO for at least the next 15 years, and (ii) allowing new generation (or energy efficiency and load control) sources to compete initially for new load developing after the LIPA/LILCO Merger Closing Date and, eventually, all retail load. At the same time, as discussed below, LIPA will be permitting increasing numbers of retail customers to choose among these competing sources of power supply.

LIPA's Steps to Create Opportunities for Competition in Power Supply to Long Island

With respect to controlling LIPA's power supply costs, the PSA guarantees LIPA's access to all of GENCO's on-island generating facilities under a cost-based rate that is regulated by the FERC while providing for specified limits on rate adjustments and for LIPA's cost oversight of GENCO's capital costs. The PSA is structured to recognize the relatively low capacity costs of Genco's Generating Facilities and the moderately high operating costs of such Facilities. LIPA Sub will not be required to purchase energy from the GENCO plants and may buy lower cost energy whenever it is available, given the transmission constraints mentioned above and the on-island generation operating requirements to maintain system reliability. Under the EMA, the Energy Manager, on LIPA Sub's behalf, will purchase, on a least-cost basis, the fuel used to generate energy in GENCO's plants.

LIPA's activities to encourage the development of competition in power supply will develop along with LIPA's requirement to meet its growing demands on Long Island. LIPA plans to meet that need through competitive solicitations for generation supply and transmission facilities. LIPA has committed to the following steps to enhance the opportunity for new competitive power supply development on Long Island:

(i) The LIPA/LILCO Merger Agreement provides that LIPA will acquire on the LIPA/LILCO Closing Date, a parcel of land at the Shoreham site suitable for (a) the interconnection of an underwater transmission line to the mainland with an anticipated capacity of 600 MW, and (b) up to 600 MW of combined cycle, gas-fired generation. LIPA has not made a decision as to the use of the site.

(ii) Under a separate agreement, LIPA has a 99 year right to acquire, for its own use or use by a designee, land at each of GENCO's existing generation sites for the construction of new generating facilities.

(iii) LIPA has adopted a Clean Energy Policy Statement which encourages the development and acquisition of clean energy resources, including generation from renewable and efficient generation resources and energy conservation efforts. In its recently adopted retail rate order, LIPA committed $32 million in the first year and $11 million to $17 million per year in energy efficiency funding in subsequent years to the development and acquisition of such resources. LIPA is interested in continuing to fund clean energy resources at the $32 million annual level, and (with input from LIPA's clean energy advisory panel) LIPA will be investigating long term funding mechanisms to accomplish this objective.

(iv) LIPA Sub has secured the existing LILCO intracompany gas transportation rate for the delivery of gas over the local gas distribution system for existing GENCO and new generating plants built on Long Island.

(v) Under the agreements, LIPA Sub has a right to purchase the GENCO Generating Facilities in the fourth year of the PSA at their then fair market value. If LIPA exercises its option to purchase these facilities, it may be required by the PACB conditions to then sell them to third parties.

(vi) In the seventh year of the PSA, LIPA Sub may begin to ramp down the amount of capacity purchased from GENCO up to a maximum reduction of approximately 1500 MW by the fifteenth year of the contract. GENCO is entitled to a declining percentage of the present value of the capacity charges that would have been recovered absent the reduction under a formula which, commencing in the eleventh year, reduces the percentage of such value the later a decision is exercised.

(vii) As discussed in "Certain Factors Affecting the Electric Utility Industry," FERC has adopted rules ("Order No. 888") that require jurisdictional public utilities to file a tariff ("OATT") providing non-discriminatory open access transmission services to other eligible entities seeking use of the interstate transmission system on rates, terms and conditions comparable to the transmission provider's own use. LIPA is not directly subject to Order No. 888. However, LIPA has undertaken a voluntary commitment to file an open-access transmission tariff that substantially conforms to the provisions of Order No. 888, as modified on rehearing, and FERC has made the filing of that tariff a condition to FERC's approval of the transfer to LIPA of LILCO's transmission assets. LIPA intends to seek a declaratory ruling from FERC that the filing of LIPA's OATT will entitle LIPA to open access transmission service from other FERC-jurisdictional transmission owners. In addition, as part of its commitment to file an OATT, LIPA will be required to establish an open access same time information system ("OASIS") and to adopt a code of conduct as required under FERC Order No. 889.

(viii) As discussed in "Certain Factors Affecting the Electric Utility Industry," the member systems of the New York Power Pool have submitted a proposal to FERC for the formation of an independent system operator ("ISO") which would operate the electric transmission system in the State of New York. LIPA is currently evaluating the feasibility of LIPA Sub participating in the ISO.

(ix) LIPA is coordinating the detailed evaluation of the feasibility of developing a new transmission cable under Long Island Sound. This evaluation is being undertaken to enable comparison of new on-island and off-island power resources to meet future customer power supply needs. LIPA has issued a request for proposals and on March 16, 1998 received proposals from three consortia to evaluate the technical, environmental and economic feasibility of interconnecting Long Island with Connecticut or other areas. The most likely path for a new cable is from the Shoreham site to Connecticut. LIPA is seeking a firm that would commit to

developing the new transmission line at the bid cost if LIPA decides to authorize the use of on-island rights held by it to interconnect the transmission project to the LIPA T&D System. LIPA will make that decision after issuing a solicitation for on-island or off-island generation and clean energy resources to meet its anticipated load growth in the Service Area by 2005. If LIPA determines as a result of the generating resource solicitation that the cost of off-island resources, including the cost of transmission over the proposed new cable, is less than on-island alternatives, it intends to authorize the construction of a new line using the Shoreham site as a terminus of the line.

LIPA's Plan For Retail Choice

LIPA's effort at creating competition in power supply resources is to gradually create a competitive retail market for power supply. LIPA has adopted a customer retail choice plan intended to lead to full choice among power suppliers by all retail customers by 2003. Under the retail choice plan, LIPA will, within one year after the LIPA/LILCO Merger Closing Date, provide customers representing an aggregate load of 100 MW the option of selecting competitive suppliers of electric capacity and energy. This initial phase of the retail choice plan, anticipated to begin by May 1, 1999, will be evenly split between residential customers and nonresidential customers. Approximately 25,000 residential customers will be eligible to participate. Customers who participate in this initial phase of the retail choice plan will receive a credit on their monthly electric bills based on the cost of power supply that LIPA avoids because of implementation of the plan. Participating customers who are able to contract for competitive power supplies at a cost lower than the credit offered by LIPA will experience an overall reduction in their electric bills. As part of the initial phase of the retail choice plan, LIPA will evaluate and resolve various issues related to program implementation, including, appropriate near-term market mechanisms and various administrative details, such as customer enrollment, metering, billing, and information systems. Following an evaluation of the initial phase, LIPA expects to expand the retail choice plan consistent with the development of long-term solutions to the implementation issues, including means to accommodate Internal Revenue Service regulations concerning tax-exempt financing.

Under the retail choice plan, LIPA will be the provider of last resort (''POLR'') responsible for offering supply at reasonable prices to any customers unwilling or unable to arrange for alternative power suppliers. LIPA's POLR responsibility will necessitate the adoption of flexible power supply arrangements to accommodate uncertain levels of customer loads. These arrangements may include capacity options and direct market sales or purchases.

Regardless of a customer's choice of electricity supplier, LIPA will remain the sole provider of transmission and distribution services to customers in the Service Area. LIPA plans to set its rates for delivery service to include all costs that are not avoidable once customers choose alternative suppliers, with the intent that LIPA be kept revenue neutral. Costs that LIPA will not be able to avoid, and therefore will be included in the rates for delivery service, include its debt service obligations and any long-term power purchase contracts, among other items. Accordingly, LIPA will continue to recover all costs needed for safe and reliable T&D System operation and to meet its financial obligations, regardless of the degree of customer participation in LIPA's retail choice program.

CERTAIN FACTORS RELATING TO POTENTIAL CUSTOMER LOSS

The Independent Consultant's Report has identified several sources of competition to LIPA that could reduce LIPA's load below its load projections. These challenges come from self-generation, municipalization, lapsed franchises and gas competition.

Self-Generation

The Independent Consultant's Report addresses various self-generation alternatives available to customers, including micro-turbines and fuel cells. The Independent Consultant's Report states that the Service Area does not generally contain large industrial customers of the type often found in other large utility service territories. The economics of self-generation depends on the displacement of capacity and energy purchases from utility supply. Therefore, self-generation is most attractive to customers who are high load factor energy users, such as hospitals, or manufacturers with multiple shift operations. There are few such customers of significant size on Long Island. The Independent Consultant's Report presents the results of evaluation of the practicality of, and approximate cost for, typical Long Island commercial and residential customers self-generating using emerging small, gas-fired generation technology. The evaluation is based on fuel supply and transportation conditions, anticipated LIPA back-up power supply rates, and other assumptions described in "Appendix A—Independent Consultant's Report—Security of Customer Revenue—Self Generation". The Report explains that the estimated cost of self generation for these customers, combined with the practical obstacles to installing on-site generation, is expected to preclude self-generation from being installed by any meaningful number of customers within the Service Area. Consequently, if there is to be a serious threat of revenue loss due to customer self-generation, it would involve either (i) the installation of generating plants with capacity larger than the individual customer loads, with the sale of excess generating output into the power supply market, or (ii) installation of very small generating plants to serve the typically smaller customer load within the Service Area. See "Appendix A—Independent Consultant's Report—Security of Customer Revenue."

Municipalization

LILCO's existing electric rates within the Service Area have caused some local governments to consider municipalization as a means to lower the cost of electric service. To date, seven villages have either authorized proceedings to conduct, or have conducted, voter referenda authorizing the villages to create municipal electric utilities to replace LILCO's services if it is determined to be economic to do so. If municipalization were to occur within any of these villages, it would require condemnation of the T&D System facilities, or construction of duplicate electric transmission and distribution facilities.

In the opinion of Adams, Dayter & Sheehan, LLP, LIPA's State Regulatory Counsel, after the LIPA/LILCO Merger (i) a municipality may not legally condemn LIPA Sub's electric distribution or other facilities in order to serve LIPA Sub's customers, and (ii) a municipality may not legally construct its own electric facilities to serve LIPA Sub's customers.

In 1998 the Attorney General of the State of New York rendered an informal opinion to the County Attorney for Suffolk County that a municipality in the LIPA Service Area may not condemn the distribution system, facilities or other assets of LILCO or LIPA and use them to operate a municipal utility. In the Attorney General's opinion such an action "clearly is inconsistent with and preempted by" the LIPA Act.

The Independent Consultant's Report concludes that formation of new municipal utilities on Long Island is not expected to occur due to the risk and expense of undertaking such municipalization efforts and the lack of reasonable expectation of electric customer rate savings from municipalization, as compared to the average system rates to be charged by LIPA. The Independent Consultant's Report

must be read in its entirety for an understanding of the analyses, investigations, and assumptions upon which these conclusions are based. See "Appendix A—Independent Consultant's Report—Security of Customer Revenue."

Lapsed Franchises

LILCO has advised LIPA that its franchises to operate its retail electric business and install and maintain the facilities and equipment related thereto have lapsed in certain municipalities in the Service Area. Accordingly, LIPA Sub, when it acquires the T&D System, will not have franchises to operate in these parts of the Service Area. In the opinion of Adams, Dayter & Sheehan, LLP such municipalities may not decline to grant LIPA a franchise (unless LIPA fails to agree to reasonable terms and conditions), and if the municipalities do decline to grant LIPA a franchise, LIPA may condemn the franchise.

Gas Competition

In reviewing the forecast of electric loads within the Service Area in preparing the Independent Consultant's Report, RMI considered the potential impact on such forecast from the conversion of existing electric appliances and other end uses to natural gas. Several factors influence a customer's decision to make such a conversion, including (i) access to the local gas distribution network; (ii) the cost of natural gas versus electricity; (iii) the cost of conversion to natural gas end use, including the price of the gas appliance and the installation of in-house gas piping; (iv) the maturity of the gas appliance technology; and (v) non-economic factors, such as perceptions of safety and performance.

The levels of end uses most vulnerable to conversion are generally sufficiently low that the loss of such sales, if it were to occur, would not have a material impact on total LIPA revenue. See the Independent Consultant's Report in Appendix A for further discussion.

PUBLIC AUTHORITIES CONTROL BOARD

The PACB

LIPA is required by the LIPA Act to obtain certain approvals of the PACB. The PACB consists of five members appointed by the Governor of the State of New York. One of the members is appointed upon the recommendation of the Majority Leader of the State Senate, one upon the recommendation of the Speaker of the State Assembly, one upon the recommendation of the Minority Leader of the State Senate and one upon the recommendation of the Minority Leader of the State Assembly. The two members of the PACB appointed by the Governor upon the recommendations of the Minority Leaders of the Senate and the Assembly do not vote. The unanimous vote of the voting members of the PACB is required to authorize action by the PACB.

Statutory Requirement for PACB Approval of LIPA Projects

Pursuant to the LIPA Act, LIPA may not undertake any "project" without PACB approval. A "project" of LIPA is defined to mean an action undertaken by LIPA that: (i) causes LIPA to issue bonds, notes or other obligations, or shares in any subsidiary corporation; (ii) significantly modifies the use of an asset valued at more than one million dollars owned by LIPA or involves the sale, lease

or other disposition of such an asset; or (iii) commits LIPA to a contract or agreement with a total consideration of greater than one million dollars and does not involve the day-to-day operations of LIPA.

The LIPA Act provides that the PACB shall only approve a proposed project of LIPA upon the PACB's determination that: (i) the project is financially feasible; (ii) the project does not materially adversely affect overall real property taxes in the Service Area; (iii) the project is anticipated to result generally in lower utility rates; and (iv) the project will not materially adversely affect overall real property taxes or utility rates in other areas of the State.

Approval of LIPA/LILCO Merger

On July 16, 1997, the PACB adopted a resolution (the "PACB Merger Resolution") which approved the execution and delivery of all agreements required for the consummation of the LIPA/LILCO Merger Transaction, including, but not limited to, execution, delivery and implementation of the LIPA/LILCO Merger Agreement, the MSA, the EMA, the PSA and all other agreements contemplated thereby. The PACB further made its approval subject to certain conditions (the "PACB Conditions"), which were accepted by LIPA by a resolution of the Trustees adopted unanimously on August 21, 1997. Two of those conditions relate to the establishment of rates, and are described herein under the caption "Rates and Charges—LIPA's Authority to Set Electric Rates." The PACB conditions, and the actions taken by LIPA to date and LIPA's plans to comply with such conditions, are described in the Independent Consultant's Report under the heading "Public Authorities Control Board Approval."

Bond Approval

On April 22, 1998, the PACB unanimously adopted a resolution approving the issuance of up to $5,238,000,000 of bonds relating to the first tranche of financing anticipated under the Plan of Finance, and the execution, delivery and implementation of agreements necessary to implement such financing.

Litigation Relating to PACB Merger Approval

Suffolk County brought a suit against LIPA and others seeking a judgment, among other things, (i) annulling and vacating the acceptance by LIPA of the PACB Conditions, (ii) directing that LIPA take no further action to acquire the stock or assets of LILCO unless and until such acquisition has been lawfully approved by the PACB in the manner provided by law, and (iii) pending such approval, declaring that all or any actions taken by LIPA to implement or carry out the PACB Conditions are null and void.

The case was argued on March 13, 1998. A decision was rendered on March 24, 1998 which held for LIPA on all of the substantive issues. In discussing the action, the court ruled that LIPA's acceptance of the conditions imposed by the PACB falls "smoothly within the LIPA Act's statutory framework." The court further held that LIPA did not act arbitrarily, capriciously or irrationally and the conditions it accepted were aimed at achieving the explicit goal of the LIPA Act. LIPA cannot predict if this decision will be appealed. In the opinion of Rivkin, Radler & Kremer, LIPA's counsel in this litigation, "While it is not possible to predict the outcome of any litigation with certainty, including this litigation, it is our opinion as litigation counsel to the Authority, that the Authority will prevail in any final adjudication of those claims raised in this litigation challenging the legality of certain acts taken by the Authority."

New York Public Interest Research Group, Inc., the Citizens Advisory Panel and two individuals commenced a proceeding in November 1997 in Albany County Supreme Court challenging the PACB Merger Resolution and seeking its annulment. Petitioners' sole argument is that the PACB was required to perform an environmental review under the State Environmental Quality Review Act ("SEQRA") of the LIPA Agreements before issuing the PACB Merger Resolution. The PACB, LIPA, LILCO, and the Brooklyn Union Gas Company have moved to dismiss the lawsuit on the grounds that the PACB Merger Resolution was exempt from SEQRA pursuant to certain provisions of the LIPA Act and SEQRA. The case was argued in December 1997, and the parties are waiting for a decision of the court. In the opinion of Adams, Dayter & Sheehan, LLP, LIPA's counsel in this litigation, based on the explicit SEQRA exemption language of Section 1020-s(2) of the LIPA Act and Section 8-0105(5)(ii) of the Environmental Conservation Law, the courts' decision construing those provisions in *Matter of Citizens for an Orderly Energy Policy* v. *Cuomo*, 159 AD2d 141 (3d Dept., 1990), *affirmed* 78 NY2d 398 (1991) and *Village of Atlantic Beach* v. *Gavalas*, 81 NY2d 322 (1993), and with the recognition that it is not possible to predict the outcome of any litigation with certainty, the PACB Merger Resolution will be upheld in all respects in the final adjudication of this litigation.

ACTIONS BY SUFFOLK COUNTY LEGISLATURE

The Suffolk County Legislature has appropriated $800,000 for the purposes of preventing the LIPA/LILCO Merger Transaction from taking place and monitoring LIPA. To that end, Suffolk County commenced the proceeding described under "Public Authorities Control Board—Litigation Relating to PACB Merger Approval."

The Suffolk County Legislature has also adopted by a vote of 12-0 with six abstentions a resolution which would place on the November 1998 ballot a referendum asking the voters of Suffolk County to approve the enactment of a charter law entitled "A CHARTER LAW DIRECTING TRUE AND HONEST ACTIVE OPPOSITION TO LIPA/LILCO BUG TRANSACTION." The stated purpose of this charter law is to ensure that Suffolk County, acting through its elected officials, continues active opposition to the LIPA/LILCO merger. If enacted by a majority of the voters voting thereon at the November general election, this law would require, among other things, that Suffolk County actively oppose (including bringing necessary legal action), among other things, the request to the IRS for private letter rulings obtained by LIPA and LILCO in connection with the LIPA/LILCO Merger Transaction and the issuance by LIPA of bonds; the PSC and FERC proceedings to approve the LIPA/LILCO merger and the LILCO/KeySpan merger; and any approvals by the PACB of LIPA's bonds. This law would also require Suffolk County to seek (i) compliance by LIPA and the PACB with the terms and conditions of the LIPA Act, (ii) enforcement of retail competition to the maximum extent possible and (iii) disallowance of LILCO's recovery of the Shoreham Regulatory Asset. LIPA believes that the referendum, if placed on the ballot and passed, will not have a material adverse impact on LIPA's ability to complete the transactions contemplated by the Plan of Finance, to operate the System, or to set and collect rates sufficient to meet its obligations in the future.

The resolution has been vetoed by the County Executive of Suffolk County. Certain members of the Suffolk County Legislature have indicated that a vote may be held in the near future to override such veto. Twelve affirmative votes would be required for such override. LIPA can make no predictions as to whether such vote will be taken, or if taken, the result thereof.

CERTAIN FACTORS AFFECTING THE ELECTRIC UTILITY INDUSTRY

General

The electric utility industry has been, and in the future will be, affected by a number of factors which will have an impact on the business, affairs and financial condition of both public and private electric utilities, including LIPA.

One of the most significant of these factors is the efforts on both the national and local levels to restructure the electric utility industry from a heavily regulated monopoly to an industry in which there is open competition for power supply service on both the wholesale and retail level. For a description of expected retail competition in the electric utility industry and the response of LIPA thereto, see ''Competition and the LIPA Plan'' in this Part 2.

Electric utilities are also subject to increasing Federal, state and local statutory and regulatory requirements with respect to the siting and licensing of facilities, safety and security, air and water quality, land use and other environmental factors. The industry is subject to claims asserting health effects from electric and magnetic fields associated with power lines, home appliances and other sources.

LIPA cannot predict what effects these factors will have on the business, operations and financial condition of LIPA, but the effects could be significant. The following sections of this caption provide brief discussions of certain of these factors. However, these discussions do not purport to be comprehensive or definitive, and these matters are subject to change subsequent to the date of this Official Statement. Extensive information on the electric utility industry is, and will be, available from legislative and regulatory bodies and other sources in the public domain.

Energy Policy Act of 1992

The Energy Policy Act of 1992 (the ''Energy Policy Act'') made fundamental changes in the Federal regulation of the electric utility industry, particularly in the area of transmission access. The purpose of these changes, in part, was to bring about increased competition in the wholesale electric power supply market. In particular, the Energy Policy Act provides FERC with the authority, upon application by any person selling electricity, federal power marketing agency, or other power generator, to require a transmitting utility to provide transmission services to the applicant essentially on a cost-of-service basis. Municipally-owned electric utilities are ''transmitting utilities'' for purposes of these provisions of the Energy Policy Act. However, the Energy Policy Act specifically denied FERC the authority to mandate ''retail wheeling,'' under which a retail customer of one utility could obtain transmission services for the purpose of obtaining power from another utility or non-utility power generator.

Recent FERC Initiatives

On April 24, 1996, the FERC issued two final rules and a Notice of Proposed Rulemaking (''New NOPR'') that contain significant policy initiatives designed to open the market for generation of electricity to competition. The final rules effect significant changes in the regulation of transmission services provided by ''public utilities'' (as defined in the Federal Power Act) that own, operate or control interstate transmission facilities used to transmit power in interstate commerce (''jurisdictional utilities''). Neither LIPA nor LIPA Sub is a jurisdictional utility as so defined.

One of the final rules, Order No. 888, (i) requires all public utilities to provide open access transmission services on a non-discriminatory basis by requiring all such public utilities to file tariffs that offer other entities seeking use of the interstate transmission system the same transmission services they provide themselves, under comparable terms and conditions and (ii) contains a reciprocity provision that requires non-jurisdictional utilities (including municipal and consumer-owned utilities such as LIPA and LIPA Sub) that purchase transmission services under FERC-filed open access tariffs and that own or control transmission facilities to, in turn, provide open access service to the transmitting utility on rates, terms and conditions that are comparable to the service that the non-jurisdictional utility provides itself. Order No. 888 also includes provisions which, in effect, would permit jurisdictional utilities to recover so-called ''stranded costs'' for generating and other facilities from wholesale customers of a utility who opt to purchase from other power suppliers.

The rates that LIPA charges for transmission service under its Open Access Transmission Tariff (''OATT''), when filed, including the calculation of any stranded cost charge, are not subject to direct regulation by the FERC under Part II of the Federal Power Act (''FPA''). However, the FERC will review the rates to ensure that the entire OATT meets FERC's comparability standards. A prospective customer seeking service under the OATT may challenge the rate or stranded cost charge quoted by LIPA to the customer by filing an application to the FERC for an order requiring LIPA to provide transmission service under Sections 211 and 212 of the FPA. FERC has discretion to entertain such an application, but it has not established a policy with respect to whether it would do so where FERC has approved a nonjurisdictional utility's OATT for comparability purposes.

The other final rule, Order No. 889, requires standards of conduct for utilities that offer open access transmission services to ensure that transmission owners and their affiliates do not have an unfair competitive advantage in using transmission to sell power. To this end, Order No. 889(i) requires those utilities to establish an electronic OASIS to share transmission-related information (including information about available capacity) on a real-time basis, and to require that those utilities also obtain information about their transmission systems for their own wholesale power transactions, such as available capacity, in the same way that their competitors do—via an OASIS, and (ii) promulgated standards of conduct to ensure that utilities functionally separate their transmission and wholesale power merchant functions to prevent self-dealing.

Additionally, the New NOPR proposes the replacement of the network and point-to-point single tariff in Order No. 888 with a ''capacity reservation tariff'' that would allow FERC-jurisdictional utilities and all other power market participants to reserve firm rights to transfer power between designated receipt and delivery points. LIPA is unable to predict whether the New NOPR will be adopted in its current form, and if adopted, what effect it would have on LIPA.

In the Spring of 1997, FERC issued its orders on rehearing of Order Nos. 888 and 889. In these orders FERC upheld the bulk of its rulings in Order Nos. 888 and 889, while making changes to certain aspects of those rules to implement its open-access policies. Public utilities were required to submit revised tariffs to FERC during the summer of 1997 to reflect FERC's orders on rehearing. In November 1997, FERC issued further orders on rehearing affirming, with certain clarifications, its previous orders. Certain aspects of Order Nos. 888 and 889 have been appealed to the U.S. Court of Appeals.

LIPA is not directly subject to the new rules nor would LIPA be subject to the rules proposed in the New NOPR. However, LIPA is subject to the reciprocity provision in Order No. 888, described above. Moreover, LIPA has undertaken a voluntary commitment to file an OATT that substantially

conforms to the provisions of Order No. 888, as modified on rehearing, and FERC has made the filing of that tariff a condition to FERC's approval of the transfer to LIPA of LILCO's transmission assets. Among the requirements that LIPA's OATT must satisfy under Order No. 888 is the requirement that LIPA's proposed rates for transmission and ancillary services are comparable to the rates that LIPA charges itself for those services. In addition, as part of its commitment to file an OATT, LIPA will be required to establish an OASIS and to adopt a code of conduct as required under Order 889, as modified on rehearing.

Under Part II of the Federal Power Act, ''public utilities'' are subject to regulation by FERC. A ''public utility'' includes any person or entity that owns, controls, or operates facilities used for the transmission of electric energy in interstate commerce or for the sale of electric energy at wholesale in interstate commerce. However, under Part II of the Federal Power Act a ''public utility'' does not include a state or any political subdivision of a state, or any agency, authority, or instrumentality of any one or more of the foregoing. As a corporate municipal instrumentality and political subdivision of the State of New York, LIPA, and, indirectly, LIPA Sub, are largely exempt from FERC regulation as ''public utilities'' under Part II of the Federal Power Act. Notwithstanding this exemption, LIPA is subject to the authority of FERC to order interconnection of its facilities pursuant to Section 210 of the FPA, and the authority of FERC to order ''transmitting utilities'' to provide transmission services in accordance with sections 211 and 212 of the Federal Power Act as amended by the Energy Policy Act. As noted above, FERC has required LIPA to file an OATT as a condition to FERC's approval of assets from LILCO under Section 203 of the FPA.

Clinton Administration's Comprehensive Electric Competition Plan

On March 25, 1998, the Clinton Administration issued a proposal to restructure the electric power industry. The proposal, which has been sent to the Congress but is not yet in the form of legislation, consists of a number of energy and environmental policy initiatives. The proposal would require all utilities to permit all retail customers to purchase power from the supplier of their choice by January 1, 2003. States and self-regulated utilities can opt out of this mandate if they determine, through a public proceeding, that consumers would be better served through another approach, including retaining the current system. The proposal retains a state's primary authority over stranded cost recovery, but provides the FERC with backup authority in the case where a state lacks authority to collect stranded costs. The proposal would make FERC's open access transmission rules applicable to all municipal utilities, and clarify FERC's authority to order retail transmission in a system other than the one in which the end use customer is located. The proposal would grandfather all outstanding tax-exempt bonds from private use limitations, but eliminate tax-exempt financing for new generation and transmission facilities. In addition, the proposal contains provisions that would promote consumer protection, transmission reliability and access, and environmentally friendly energy technologies. LIPA does not know whether this or any electricity restructuring proposal will be enacted into law or what form it may ultimately take. There can therefore be no assurance as to the effect of any such legislation on LIPA.

Congressional Restructuring Proposals

Congress is considering a number of pending bills to modify federal laws affecting the electric industry. Bills have been introduced in the current Congress to provide retail electric customers with the right to choose their power suppliers. LIPA cannot predict whether such legislation will be adopted and, if adopted, what effect it would have on LIPA.

New York State Electric Utility Industry Restructuring Matters

Public Service Commission Competitive Opportunities Proceeding. On March 19, 1993, the PSC commenced a proceeding to investigate issues related to a future regulatory regime for New York's electric industry in light of increasing competitive opportunities. The second phase of this proceeding, which commenced in August 1994, concerns issues related to potential restructuring of the industry from a regulated monopoly service to a more competitive framework.

The PSC issued an Opinion and Order on May 20, 1996 (''Order 96-12'') in the competitive opportunities proceeding which required each of the New York investor-owned electric utilities (except Niagara Mohawk and LILCO) to submit a restructuring plan to the PSC. In Order 96-12, the PSC set goals for the introduction of competition in New York State's generation and energy services sectors. The PSC's preferred industry structure would ultimately allow all customers retail access after a period of transition. The PSC anticipates both lower electricity prices and economic development to result from competition.

One of the key issues that must be addressed before competition is established in New York concerns stranded costs. Stranded (or strandable) costs are defined by the PSC as those costs incurred by utilities that may become unrecoverable during the transition from regulation to a competitive market for electricity. The investor-owned utilities contend that all prudent costs incurred to provide electric service should be recovered. The PSC stated in Order 96-12 that the utilities and independent power producers must mitigate potential stranded costs.

While not under the regulatory control of the PSC, LIPA has a significant interest in the outcome of Con Edison, NYSEG and other PSC restructuring proceedings. Any decision by the PSC relating to the future competitive structure of New York's electric industry could affect the manner in which LIPA operates.

Nuclear Plant Issues. In August 1997, the staff of the PSC issued a report in the context of the PSC's Competitive Opportunities Proceeding proposing, among other things, that beyond a transition period, which is generally the period covered by the individual restructuring agreements before the PSC, nuclear generation should operate on a competitive basis. The report also proposed that the sale of nuclear plants to third parties be the preferred means of determining the fair market value of marketable generation plants as it offers the greatest potential for mitigation of stranded costs and for the elimination of anti-competitive subsidies.

On March 20, 1998, the PSC initiated a proceeding to examine a number of issues raised by the staff report and the comments received in response thereto. In summary, the PSC (a) adopted as a rebuttable presumption the premise that nuclear power should be priced on a market basis to the same degree as power from other sources, with parties challenging that premise having to bear a substantial burden of persuasion, (b) characterized the proposals in the Staff report as by and large consistent in concept with the PSC's goal of a competitive, market-based electricity industry, (c) questioned staff's position that would leave funding and other decommissioning responsibilities with the sellers of nuclear power interests and (d) indicated interest in the potential for New York Nuclear Operating Company (NYNOC) to benefit customers through efficiency gains and directed pursuit of that matter in this nuclear generation proceeding or separately upon the filing of a formal NYNOC proposal. The proceeding is intended to be completed by the second quarter of 1999.

During 1997, NYPA, Con Edison, Niagara Mohawk and Rochester Gas and Electric Corporation (''RG&E''), the four utilities operating nuclear generating facilities in New York State, executed a joint announcement which expressed their desire to move forward with plans to form the New York Nuclear Operating Company (''NYNOC''), and stated that the four utilities will initiate the steps to

assure that NYNOC will have the necessary leadership, personnel and structure to operate the six nuclear units now operated independently by such utilities. The joint announcement also stated that during the transition phase, while necessary governmental approvals are sought, the utilities would continue with and add to the cooperative initiatives the companies have already begun. NYNOC, a limited liability company, would operate the six nuclear plants currently operated by the four entities to achieve economies of scale and increase cost effectiveness. The plants would continue to be owned, and the output of the plants marketed, by the respective owners of the plants. It is contemplated that NYNOC would obtain the NRC operating licenses for the plants, while other aspects of the NRC licenses would remain with the owners of the plants. It is uncertain what effect Niagara Mohawk's participation in such an arrangement will have on LIPA; nor can LIPA predict the effect on such an arrangement of the auction proposal in the staff report.

Independent System Operator Proposal. Pursuant to FERC Order No. 888, applicable to, among others, the seven investor-owned electric utilities (the ''IOUs'') in New York, which, along with NYPA, comprise the New York Power Pool (''NYPP''), the IOUs undertook, with NYPA, to develop an arrangement for providing non-discriminatory open-access transmission over all of the electric transmission lines in New York. As a result of this effort, the IOUs and the NYPA filed a proposal (as most recently revised in December 1997, the ''Proposal'') with FERC to provide open access to their transmission lines. Under the Proposal, the IOUs and the NYPA would form a not-for-profit corporation, the Independent System Operator (the ''ISO''), which would have responsibility for the operation of most of the transmission lines of the participants. The ISO would be responsible for scheduling the use of the lines by its members and others that wished to use the lines for transmission of electricity, and would be responsible for collecting fees from transmission customers. Each member and NYPA would retain ownership, and would be responsible for maintenance, of their respective transmission lines. The customers of the ISO, including the IOUs and NYPA, would pay fees to the ISO. Any member may withdraw from the arrangement contemplated by the Proposal, on 90-days' notice to the board of directors of the ISO but, in the case of an IOU, such withdrawal is conditioned upon the effectiveness of an ''open access'' transmission facilities tariff on file with FERC.

A significant feature of the ISO's tariff will be its use of a schedule of flexible transmission rates to take account of the cost of energy at its destination along the transmission network in meeting competing demands for the transmission facilities subject to the ISO's jurisdiction.

At first, the seven IOUs and NYPA would be the members of the ISO but any ''Market Participant'' (which would include any person engaged in the wholesale sale, transmission or purchase of electric energy) would be eligible to join. The ISO would be governed by a board of directors consisting of the executive director of the ISO and nine individuals selected by a selection committee composed of representatives of members, other interested parties and the PSC. No member of the board of directors would be able to own shares in or have a continuing business relationship with any Market Participant. The executive director of the ISO would be chosen by the other nine directors and would be responsible for the day-to-day operation of the ISO.

The Proposal also contemplates the formation of a separate not-for-profit corporation (the ''Reliability Council'') which will establish safety and reliability standards for all entities, including the ISO, engaging in electric power transactions on the ISO's transmission system. An executive committee consisting of thirteen members will govern the Reliability Council.

Certain members of the ISO have reserved the right to seek a determination of the United States Internal Revenue Service (the ''IRS'') that participation in the arrangement contemplated by the Proposal will not adversely affect the federal tax-exempt status of any obligations issued by such a

member nor adversely affect its ability to issue future federal tax-exempt obligations. FERC approval of the Proposal is pending.

IRS Regulations Affecting Transmission Systems

In January 1998, the IRS issued temporary regulations which, among other things, govern the use of transmission facilities, financed with tax-exempt debt. LIPA is continuing to analyze these temporary regulations, among other factors, to determine whether it is in its best interest to participate in the ISO. For a further description of the ISO, see ''System Loads and Resources— System Energy and Capacity Resources and Requirements—Independent System Operator'' in the Independent Consultant's Report attached to this Part 2 as Appendix A.

Environmental

Electric utilities are subject to continuing environmental regulation. Federal, state and local standards and procedures which regulate the environmental impact of electric utilities are subject to change. These changes may arise from continuing legislative, regulatory and judicial action regarding such standards and procedures. Consequently, there is no assurance that the LIPA's facilities will remain subject to the regulations currently in effect, will always be in compliance with future regulations or will always be able to obtain all required operating permits. An inability to comply with environmental standards could result in additional capital expenditures to comply, reduced operating levels or the complete shutdown of individual electric generating units, including NMP2 and those under contract to LIPA Sub under the PSA, not in compliance.

The United States Environmental Protection Agency (''EPA''), the states and local jurisdictions may issue new regulations governing emissions from many types of power plants. By the year 2000 or shortly thereafter, Clean Air Act regulation of electric utility emissions is likely to change significantly. The changes could affect the cost of purchased power from combustion turbines and other types of plants. If enacted, the new regulations may change existing cost assumptions for electric utilities. While it is too early to determine which of these provisions will be enacted, in what form, or what their effect will be, the changes may have a material impact on the cost of power generated at affected electric generating units. See also ''Environmental Matters'' in this Part 2.

Nuclear Plant Matters

The Energy Policy Act provides, among other things, that utilities with nuclear reactors will contribute an aggregate total of $150 million annually, based upon an assessment, for a period of 15 years, up to a total of $2.25 billion (in 1992 dollars), for the costs for the decommissioning and decontamination of the DOE nuclear fuel enrichment facilities.

In accordance with the Nuclear Waste Policy Act of 1982, Niagara Mohawk, as the operator of Nine Mile Point, in August 1995, entered into a contract with DOE, under which DOE, commencing not later than January 31, 1998, would accept and dispose of spent nuclear fuel. However, it appears unlikely that DOE will accept any spent nuclear fuel from Niagara Mohawk or others before 2010. The contract provides that Niagara Mohawk will pay quarterly to DOE a fee based on nuclear generation and sales of electricity from Nine Mile Point at a specified rate. LIPA's share of such fees is 18%.

The NRC has adopted decommissioning rules which require reactor operators to certify that sufficient funds will be available for decommissioning the contaminated portion of nuclear plant in the form of prepayments or external sinking funds, either of which must be segregated from the licensee's assets and outside its administrative control, or by the surety of insurance payable to a trust established

for decommissioning costs. LILCO established such an external decommissioning trust fund in 1990 to meet these regulatory requirements. LIPA expects that by the end of the expiration of NMP2's operating license in 2026, there will be funds in LIPA Sub's decommissioning trust fund sufficient to meet the current estimated costs for its 18% share of the decommissioning costs of Nine Mile Point 2. If the estimated NMP2 decommissioning costs should increase, based on future site specific studies or NRC regulatory changes, LIPA expects LIPA Sub to increase its contributions into the decommissioning trust fund to meet the revised requirements.

The Federal Low-Level Radioactive Waste Policy Act, as amended in 1985, requires states to join compacts or to individually develop their own low-level radioactive waste disposal site. In response to the Federal law, the State had decided to develop its own site because of the large volume of such waste generated in New York, and had committed to develop a plan for the management of the low-level radioactive waste in New York State during the interim period until the disposal facility was available. LIPA cannot predict when such a facility may be available.

Niagara Mohawk presently ships the low-level radioactive waste generated at Nine Mile Point to a disposal facility in Barnwell, South Carolina. During the period July 1, 1994, to June 30, 1995, the legislature of South Carolina denied access to the facility to out-of-region low-level radioactive waste generators, including those in New York State. LIPA cannot predict whether the Barnwell facility will be closed again to out-of-region low-level radioactive waste generators at some future date before the New York State disposal facility becomes available.

NMP2 has a spent fuel pool (''SFP'') to store the spent fuel assemblies discharged from normal plant operations. The SFP has a total designed capacity to house 4,049 spent fuel assemblies. There are 1,128 spent fuel assemblies currently residing in the NMP2 SFP.

SFP capacity will be reached in the year 2012. Therefore, starting in the time frame of 2008—2010, the operator of NMP2 is expected to focus on one of the following options available at that time for the management of its spent fuel.

1. Permanent Repository

   Based on DOE's current projection, the earliest available date for the permanent repository to begin receiving spent fuel will be in 2010. Based on the original DOE estimate, the repository will not begin to accept NMP2's spent fuel assemblies until 5 to 8 years after the starting of its operation. This will miss the critical date of 2012 needed by NMP2 even if DOE's schedule can be maintained.

2. Central Interim Storage

   Due to the extensive delay in the federal permanent repository development program, both the House and the Senate passed separate legislation in 1997 mandating DOE to construct a central interim spent fuel facility to fulfill this critical need. The two bills will be reviewed in 1998 by a conference committee to reconcile the differences. The resulting bill is expected to mandate DOE to build an interim facility to start operation before the year 2002. The total licensed capacity will be 40,000 metric tons of uranium and the license will be valid for 100 years. If this facility can be built and put into operation by the year 2002, NMP2's spent fuel storage needs would be met.

3. Additional Capacity

   If options 1 and 2 described above do not materialize as scheduled, NMP2 would need additional interim on-site storage capacity for, at least 1,000 bundles of spent fuel until either option 1 or option 2 become a reality. The technology for on-site spent fuel storage is well developed, and is in use at NMP2 and a number of nuclear plants in the United States.

Niagara Mohawk procures public liability and property insurance for NMP2, and LIPA Sub will reimburse Niagara Mohawk for its 18% share of those costs. The Price-Anderson Amendments Act mandates that nuclear power plants secure financial protection in the event of a nuclear accident. This protection must consist of two levels. The primary level provides liability insurance coverage of $200 million (the maximum amount available) in the event of a nuclear accident. If claims exceed that amount, a second level of protection is provided through a retrospective assessment of all licensed operating reactors. Currently, this ''secondary financial protection'' subjects each of the 110 presently licensed nuclear reactors in the United States to a retrospective assessment of up to $76 million for each nuclear incident, payable at a rate not to exceed $10 million per year. LIPA Sub's interest in NMP2 could expose it to a maximum potential loss of $13.6 million, per incident, through assessments of $1.8 million per year in the event of a serious nuclear accident at NMP2 or another licensed U.S. commercial nuclear reactor. These assessments are subject to periodic inflation indexing and to a 5% surcharge if funds prove insufficient to pay claims.

Niagara Mohawk has also procured $500 million primary nuclear property insurance with the Nuclear Insurance Pools and approximately $2.3 billion of additional protection (including decontamination costs) in excess of the primary layer through Nuclear Electric Insurance Limited (''NEIL''). Each member of NEIL, including LIPA, is also subject to retrospective premium adjustments in the event losses exceed accumulated reserves. For its share of NMP2, LIPA could be assessed up to approximately $1.6 million per loss. This level of insurance is in excess of the NRC required $1.06 billion of coverage.

LIPA Sub will obtain insurance coverage from NEIL for the extra expense incurred in purchasing replacement power during prolonged accidental outages. Under this program, should losses exceed the accumulated reserves of NEIL, each member, including LIPA Sub, would be liable for its share of deficiency. LIPA Sub's maximum liability per incident under the replacement power coverage, in the event of a deficiency, is approximately $0.7 million.

Year 2000

LIPA has been advised by LILCO that, with modifications to existing software and conversions to new software that are currently underway, the ''Year 2000'' issue will not pose significant operational problems for LILCO's computer systems. However, if such modifications and conversions are not made, or are not completed timely, the Year 2000 issue could have a material impact on the operations of LIPA Sub. The planned expenses for such modifications and conversions are reflected in the Projected Operating Results contained in the Independent Consultant's Report attached hereto as Appendix A.

ENVIRONMENTAL MATTERS

General

As discussed in ''LIPA's Retail Electric Service Business—Guarantees and Indemnities'' in this Part 2, at the LIPA/LILCO Merger Closing, BHC Parties will deliver a Liabilities Undertaking and Indemnification Agreement and LIPA Parties will deliver a similar Liabilities Undertaking and Indemnification Agreement which, taken together, will provide, generally, that environmental liabilities will be divided between BHC Parties and LIPA Parties on the basis of whether they relate to Transferred Assets or LIPA Sub Assets. In addition, to clarify and supplement these agreements, prior to the LIPA/LILCO Merger Closing, BHC Parties and LIPA Parties will enter into an agreement to allocate between them certain liabilities, including environmental liabilities, arising from events occurring prior to the LIPA/LILCO Merger Closing and relating to the business and operations to be

conducted by LIPA Parties after the LIPA/LILCO Merger Closing (the ''Retained Business'') and to the business and operations to be conducted by BHC Parties after the LIPA/LILCO Merger Closing (the ''Transferred Business'').

BHC Parties will be responsible for all liabilities arising from all manufactured gas plant operations (''MGP Sites''), including those currently or formerly operated by LILCO or any of its predecessors, whether or not such MGP Sites relate to the Transferred Business or the Retained Business; all environmental liabilities traceable to the Transferred Business; and certain scheduled environmental liabilities. Environmental liabilities that arise from the non-nuclear generating business may be recoverable by BHC Parties as part of the capacity charge under the PSA.

LIPA Parties will be responsible for all environmental liabilities traceable to the Retained Business and certain scheduled environmental liabilities. Notwithstanding the parties' contractual allocation of environmental liabilities, under certain circumstances LIPA could be liable for environmental costs related to Transferred Assets as the prior owner in the event the BHC Parties are unable to fulfill their contractual indemnity obligations.

A liability is traceable if it can be determined to have resulted from the activities of the Retained Business or the Transferred Business, or a percentage of each, based on available documentation, reasonable inferences, and other reasonable evidence. Environmental liabilities that exist as of the LIPA/LILCO Merger Closing that are untraceable, including untraceable liabilities that arise out of common and/or shared services (whether known or unknown) will be allocated 51.1% to LIPA Parties and 48.9% to BHC Parties (of which 27.9% represents GENCO's allocated amount).

On and after the LIPA/LILCO Merger Closing, LIPA and LIPA Sub will be subject to a number of Federal, state and local environmental laws and regulations governing the installation, operation and maintenance of electric transmission and distribution systems. For example, various waste management regulations and siting laws will be pertinent.

In the LIPA/LILCO Merger Agreement, BL Holding Corp has warranted to LIPA and LIPA Sub that the operations of LILCO relating to the LIPA Sub Assets are and have been in material compliance with all federal, state and local environmental laws and regulations and have all material environmental permits required for such operations; that there are no material environmental claims pending against LILCO or its properties; that they have no knowledge of any material release of hazardous materials by LILCO or any predecessor that could form the basis of a material claim; and that they have disclosed to LIPA or LIPA Sub all material facts concerning any environmental matters affecting LILCO with respect to the LIPA Sub Assets.

Environmental Matters Retained by LIPA Parties

Electromagnetic Fields. Electromagnetic fields (EMF) occur naturally and also are produced wherever there is electricity. These fields exist around power lines and other utility equipment. LILCO has advised LIPA that it is in compliance with all applicable regulatory standards and requirements concerning EMF. Although an extensive body of scientific literature has not shown an unsafe exposure level or a causal relationship between EMF exposure and adverse health effects, concern over the potential for adverse health effects will likely continue without final resolution for some time.

In addition to public concerns over exposure to EMF, concerns and litigation over property value diminishment have become more prevalent recently in the utility industry. There are four separate lawsuits which LIPA will assume from residential property owners alleging that the existence of EMF has diminished the value of their homes.

Long Island Sound Transmission Cables. During 1996, the Connecticut Department of Environmental Protection (''DEP'') issued a modification to an Administrative Consent Order (''ACO'') previously issued in connection with an investigation of an electric transmission cable system located under the Long Island Sound (''Sound Cable'') that, after the LIPA/LILCO Merger Closing, will be jointly owned by LIPA Sub and the Connecticut Light and Power Company (''Owners''). The modified ACO requires the Owners to submit to the DEP and DEC a series of reports and studies describing cable system condition, operation and repair practices, alternatives for cable improvements or replacement and environmental impacts associated with leaks of dielectric fluid into the Long Island Sound, which have occurred from time to time. LILCO has advised LIPA that it continues to compile required information and coordinate the activities necessary to perform these studies and, at the present time is unable to determine the costs it will incur to complete the requirements of the modified ACO or to comply with any additional requirements.

The Owners have reached an agreement in principle with the DEC regarding the terms and conditions of an ACO to be issued as a result of leaks of dielectric fluid from the Sound Cable. The ACO will formalize the DEC's authority to participate in and separately approve the reports and studies being prepared pursuant to the ACO issued by the DEP. In addition, the ACO will settle any DEC claim for natural resource damages in connection with historical releases of dielectric fluid from the Sound Cable.

In October 1995, the U.S. Attorney for the District of Connecticut had commenced an investigation regarding occasional releases of fluid from the Sound Cable, as well as associated operating and maintenance practices. The Owners have provided the U.S. Attorney with all requested documentation. LILCO has asserted that all activities associated with the response to occasional releases from the Sound Cable were consistent with legal and regulatory requirements.

In December 1996, a barge, owned and operated by a third party, dropped anchor, which then dragged over and damaged the Sound Cable, resulting in the release of dielectric fluid into Long Island Sound. Temporary clamps and leak abaters were installed on the cables to stop the leaks. Permanent repairs were completed in June 1997. The cost to repair the Sound Cable was approximately $17.8 million, for which there was $15 million of insurance coverage. The Owners filed a claim and answer in response to the maritime limitation proceeding instituted by the barge owner in the United States District Court, Eastern District of New York. The claim seeks recovery of the amounts paid by insurance carriers and recovery of the costs incurred for which there was no insurance coverage. Any costs not reimbursed by a third party or covered by insurance will be shared equally by the Owners.

Superfund Sites

Under Section 107(a) of the federal Comprehensive Environmental Response, Compensation and Liability Act (commonly referred to as the ''Superfund Legislation''), parties who arranged for disposal of hazardous substances are liable for costs incurred by the EPA in responding to a release or threat of release of the hazardous substances.

Metal Bank. The EPA has notified LILCO that it is one of many potentially responsible parties (''PRPs'') under CERCLA that may be liable for the remediation of a licensed disposal site located in Philadelphia, Pennsylvania, and operated by Metal Bank of America. LILCO and nine other PRPs, all of which are public utilities, completed performance of a Remedial Investigation and Feasibility Study (RI/FS), which was conducted under a consent order with the federal Environmental Protection Agency (''EPA''). In December 1997, the EPA issued its Record of Decision (ROD), setting forth the

final remedial action selected for the site. In the ROD, the EPA estimated that the present worth cost of the selected remedy for the site is $17.3 million. LILCO has advised LIPA that it cannot predict with reasonable certainty the actual cost of the selected remedy, who will implement the remedy, or the cost, if any, to LILCO. Under a PRP participation agreement, LILCO previously was responsible for 8.2% of the costs associated with the RI/FS. LILCO's allocable share of liability for the remediation activities has not yet been determined.

LILCO recorded a liability of $1.0 million representing its estimated share of the additional cost to remediate this site based upon its 8.2% responsibility under the RI/FS.

PCB Treatment Inc. LILCO has also been named a PRP for disposal sites in Kansas City, Kansas, and Kansas City, Missouri. The two sites were used by a company named PCB Treatment, Inc. from 1982 until 1987 for the storage, processing, and treatment of electric equipment, dielectric oils and materials containing PCBs. According to the EPA, the buildings and certain soil areas outside the buildings are contaminated with PCBs.

Certain of the PRPs, including LILCO and several other utilities, formed a group, signed a consent order, and have developed a work plan for investigating environmental conditions at the site. The EPA has provided LILCO with documents indicating that LILCO was responsible for less than 1% of the materials that were shipped to the Missouri site. The EPA has not yet completed compiling the documents for the Kansas site. LIPA is informed that LILCO is currently unable to determine its share of the cost to remediate these sites.

Liberty. The EPA notified LILCO that it is a PRP in a site located in Farmingdale, New York. Industrial operations took place at this site for at least fifty years. The PRP group has claimed that LILCO should absorb remediation expenses in the amount of approximately $100,000 associated with removing PCB-contaminated soils from a portion of the site which formerly contained electric transformers. LILCO has advised LIPA that it is currently unable to determine its share of costs of remediation at this site.

Osage. The EPA has notified LILCO that it is a PRP at the Osage Metals Site, a former scrap metal recycling facility located in Kansas City, Kansas. Osage had purchased capacitors scrap metal from PCB Treatment, Inc. Through the arrangements that LILCO made with PCB Treatment, Inc. to dispose of capacitors, LILCO is alleged to have arranged for disposal within the meaning of the federal Superfund law. A similar letter was sent to 861 parties who sent capacitors to PCB Treatment, Inc. The EPA is seeking to recover approximately $1.1 million it expended to conduct a removal action at the site.

Environmental Matters Which May Be Recoverable from LIPA Sub by BHC Parties through the PSA

Asbestos. Through the course of normal business operations, utility employees are exposed to hazardous materials. One of these hazardous materials is insulation containing asbestos. Most of LILCO's steam generating units were constructed with insulation containing asbestos. The presence of asbestos alone does not itself constitute a health risk if the asbestos is properly maintained and abated where required. Although LILCO has a program in place for asbestos containment and replacement, there have been a significant number of claims regarding impaired health from exposure to asbestos. LILCO has advised LIPA that it expects that many of the claims will be disposed of, i.e., settled or dismissed without payment; however, it also anticipates that claims of this nature may continue to arise in the future.

Asharoken. In March 1996, the Village of Asharoken filed a lawsuit against LILCO in the New York Supreme Court, Suffolk County (*Incorporated Village of Asharoken, New York, et al.* v. *Long Island Lighting Company*). The Village is seeking monetary damages and injunctive relief based upon theories of negligence, gross negligence and nuisance in connection with the LILCO design and construction of the Northport Power Plant which the Village alleges upset the littoral drift, thereby causing beach erosion. In November 1996, the court decided LILCO's motion to dismiss the lawsuit, dismissing two of the three causes of action. The court limited monetary damages on the surviving continuous nuisance claim to three years prior to the commencement of the action. LILCO has advised LIPA that its liability, if any, resulting from this proceeding cannot yet be determined. However, LILCO does not believe that this proceeding will have a material adverse effect on its financial position, cash flows or results of operations.

Environmental Matters Which Are Currently Untraceable or Not Yet Allocated and For Which LIPA Sub Could Have Responsibility

Superfund Sites.

Syosset. In February 1994, a lawsuit was filed in the United States District Court for the Eastern District of New York by the Town of Oyster Bay (Town), against LILCO and nine other PRPs. The Town is seeking indemnification for remediation and investigation costs that have been or will be incurred for a federal Superfund site in Syosset, New York, which served as a Town-owned and operated landfill between 1933 and 1975. In a Record of Decision issued in September 1990, the EPA set forth a remedial design plan, the cost of which was estimated at $27 million and is reflected in the Town's lawsuit. In an Administrative Consent Decree entered into between the EPA and the Town in December 1990, the town agreed to undertake remediation at the site. LILCO has advised LIPA that it is participating in a joint PRP defense effort with several other defendants. Liability, if imposed, would be joint and several. An agreement in principal has been reached between LILCO, certain other defendants, the State of New York and the Town; any settlement is subject to court approval and if approved would not have a material adverse effect on its financial position, cash flows or results of operations.

Port Washington. In 1989, the EPA notified LILCO that it was a PRP for a landfill in Port Washington, New York. LILCO has advised LIPA that it does not believe that it sent any materials to the site that contributed to the contamination which requires remediation and has therefore declined the EPA's requests to participate in the pending investigation and remediation activities at the property. Following that response, LILCO has not received further communications regarding this site.

Blydenburgh. The New York State Office of the Attorney General has notified LILCO that it may be responsible for the disposal of wastes and/or for the generation of hazardous substances that may have been disposed of at the Blydenburgh Superfund site, also known as the Islip Municipal Sanitary Landfill. The Islip landfill operated from 1927 through 1990. The State has incurred approximately $15 million in costs for investigation and remediation of environmental conditions at the landfill. LILCO received a Request for Information concerning LILCO's historical waste management practices and a tolling agreement, which if executed by LILCO, will commit the State not to commence legal action until after March 18, 1999. During the tolling period the State will continue its investigation to determine whether LILCO is liable for investigation and remediation response costs. LILCO has not yet completed a review of its records to determine whether its historical waste management practices are connected with the Islip landfill's operations.

Storage Facilities. As a result of petroleum leaks from underground storage facilities and other historical occurrences, LILCO is required to investigate and, in certain cases, remediate affected soil and groundwater conditions at several facilities within its service territory. The aggregate costs of such remediation work are estimated at between $3 million and $5 million.

Huntington/East Northport. The New York State Department of Environmental Conservation has notified LILCO, pursuant to the State superfund program, that its records indicated LILCO may be responsible for the disposal of waste at this municipal landfill property. LILCO conducted a search of its corporate records and did not locate any information concerning waste disposal practices associated with this landfill. LILCO has advised LIPA that it is currently unable to determine its share, if any, of the costs to investigate and remediate this site.

Riverhead Lawsuit. In June 1996, a lawsuit was commenced against LILCO in the New York Supreme Court, Suffolk County (*Town of Riverhead, et al.* v. *Long Island Lighting Company*), in which the plaintiffs seek monetary damages and injunctive relief based upon theories of nuisance, breach of contract, and breach of the public trust in connection with LILCO's construction of the Shoreham Nuclear Power Station and LILCO's diversion and maintenance of the Wading River Creek. The plaintiffs allege that the diversion of the Wading River Creek and the construction of the Shoreham Nuclear Power Station have caused negative environmental impacts on surrounding areas. The plaintiffs also allege that LILCO has contractual obligations to perform annual maintenance dredging of the Wading River Creek and beach replenishment of certain beach front property. In September 1996, LILCO filed a motion to dismiss the complaint on numerous grounds. In January 1997, the plaintiffs cross-moved for an order seeking partial summary judgment. The Court issued an Order dated August 26, 1997 which denied both motions except that it dismissed Plaintiff's cause of action alleging violation of the Public Trust Doctrine and prohibited the Town of Riverhead from suing in its sovereign capacity. The parties have filed notices of intent to appeal this order and discovery has commenced. LILCO's liability, if any, resulting from this proceeding cannot yet be determined. However, LILCO has advised LIPA that it does not believe that this proceeding will have a material adverse effect on its financial position, cash flows or results of operations.

REGULATION

The operations of LIPA will be subject to regulation by various State and Federal agencies, discussions of which appear in other parts of this Official Statement. The principal agencies having a regulatory impact on LIPA and the conduct of its activities are as follows:

New York State

Public Authorities Control Board. Any action constituting a "project" as defined in the LIPA Act is subject to the approval of the PACB. See "Public Authorities Control Board."

Public Service Commission. The PSC is the principal agency in the State regulating the generation, transmission and sale of electric power and energy. It has no statutory jurisdiction over rates for power generated, transmitted or distributed by LIPA but does regulate the rates of New York State's investor-owned utilities and certain municipal systems to which LIPA sells power. The PSC is empowered by the New York Public Service Law to issue Certificates of Environmental Compatibility and Public Need ("Certificates") prior to the construction of power transmission lines of certain capacities and lengths. Under the Act, LIPA is empowered to set rates for electric service in its Service

Area without obtaining the approval of the PSC or any other State regulatory body. See, however, "Rates and Charges—LIPA's Authority to Set Electric Rates."

State Board on Electric Generation Siting and the Environment. The New York State Board on Electric Generation Siting and the Environment is empowered to issue certificates for the construction of major electric generating facilities in New York.

Department of Environmental Conservation. Before any Federal license or permit can be issued for any activity involving a discharge into navigable waters, the DEC must certify that the discharge will comply with the State water quality standards (or waive certification). Certain aspects of the DEC's regulatory authority over pollutant discharge permits, air quality permits and hazardous waste regulation arise from delegation of such authority to the State by Federal legislation.

Federal

Nuclear Regulatory Commission. The NRC regulates the construction and operation of nuclear power plants. An operating license is required for the operation of any nuclear power plant. In addition, the NRC prescribes various operating standards and other rules.

Federal Energy Regulatory Commission. Under Part II of the Federal Power Act, FERC regulates the rates, terms and conditions of (i) the sale for resale of electric power by "public utilities"; and (ii) the provision of transmission service in interstate commerce by public utilities. Neither LIPA nor LIPA Sub is a "public utility" under the Federal Power Act. Although the rates, terms and conditions under which LIPA provides transmission service are not subject to general FERC jurisdiction, FERC may order LIPA to provide transmission service to individual customers meeting the requirements of Sections 211 and 212 of the Federal Power Act on rates, terms and conditions comparable to those of LIPA for LIPA's own use of its system.

In addition, LIPA has committed to file an open-access transmission tariff containing rates, terms and conditions that conform to the requirements of Order No. 888, as modified on rehearing, and FERC has imposed as a condition on its approval of the transfer of LILCO's transmission assets to LIPA the filing of such a tariff. As part of its commitment to file an open-access transmission tariff, LIPA will also be required to establish an OASIS and to adopt a code of conduct as required under Order 889, as modified on rehearing.

LILCO requires the approval of FERC under Section 203 of the Federal Power Act to dispose of its "jurisdictional facilities" (basically, its transmission facilities) before transferring them to LIPA. On February 12, 1998, FERC issued an order authorizing that disposition, conditioned as discussed above. No request for rehearing of that order has been filed with the FERC.

The rates charged by GENCO to LIPA Sub are subject to FERC approval under Sections 205 and 206 of the Federal Power Act. On February 12, 1998, FERC issued an order permitting those rates to go into effect subject to refund in the event that, after a hearing, the rates are found by FERC to be excessive. As a result, the outcome of that proceeding will be that the rates charged by GENCO to LIPA Sub will either remain at the same level as proposed or be reduced. However, FERC retains the ability in future proceedings, either on its own motion or upon a complaint filed with FERC, to modify GENCO's rates, either upward or downward, if FERC finds that the public interest requires it to do so. On April 23, 1998, FERC issued an order denying a request for reopening of the February 12 order requested by Suffolk County. In the April 23 order, FERC also clarified that the parties may address at a hearing the non-rate terms and conditions of the PSA including the 15 year term of the PSA.

Environmental Protection Agency. The Environmental Protection Agency (''EPA'') is the principal agency of the Federal government regulating air, water and land quality. However, with respect to nuclear facilities, the NRC reviews environmental impacts as part of its permit and licensing proceedings. LIPA is subject to EPA rules requiring the securing of routine discharge permits for non-radiological emissions and effluents from all LIPA facilities.

Department of Energy. The Economic Regulatory Administration of DOE is authorized to issue Presidential permits for international transmission interconnections.

United States Army Corps of Engineers. The United States Army Corps of Engineers is authorized to approve construction undertaken in connection with a power plant or transmission line which affects navigation, involves dredging or filling in navigable waters, or involves crossing of navigable streams.

INSURANCE AND LIABILITY MANAGEMENT

In the opinion of Meyers-Reynolds & Associates, Inc., Oklahoma City, Oklahoma, nationally recognized insurance consultant to LIPA, the insurance coverages expected to be in place on the LIPA/LILCO Merger Closing Date satisfy the insurance requirements of the Resolution and the Financing Agreement and provide insurance coverages for LIPA, LIPA Sub and its assets in accordance with prudent utility practice.

For a discussion of LIPA's and LIPA Sub's insurance coverage with respect to NMP2, see ''Certain Factors Affecting the Electric Utility Industry—Nuclear Plant Matters.''

LITIGATION

LIPA

There is no litigation pending or threatened in any court (either State or Federal) to restrain or enjoin the issuance or delivery of the Offered Securities or questioning the creation, organization or existence of LIPA, the title to office of the Trustees or officers of LIPA, the validity or enforceability of the Resolution, Financing Agreement, the pledge of the Trust Estate, the proceedings for the authorization, execution, authentication and delivery of the Offered Securities or the validity of the Offered Securities. For a discussion of certain proceedings relating to the LIPA/LILCO Merger Transaction see ''LIPA's Retail Electric Service Business—Guarantees and Indemnities'' and ''Public Authorities Control Board—Litigation Relating to PACB Merger Approval.''

Existing LILCO Litigation

Pending before federal and state courts, the federal Equal Employment Opportunity Commission and the New York State Division of Human Rights are charges by several individuals alleging, in separate actions, that LILCO discriminated against them, or that they were the subject of harassment, on various grounds.

The Civil Rights Bureau of the New York Attorney General's office has subpoenaed LILCO for the production of documents to aid in its investigation as to whether LILCO has engaged in discriminatory practices based upon age. No charges have been filed and the Attorney General has not made any further inquiry for the past several years.

LILCO has estimated that any costs to LILCO resulting from these matters would not have a material adverse effect on its financial position, cash flows or results of operations.

In May 1995, eight participants of LILCO's Retirement Income Plan (RIP) filed a lawsuit against the Company, the RIP and Robert X. Kelleher, the Plan Administrator, in the United States District Court for the Eastern District of New York (Becher, et al. v. Long Island Lighting Company, et al.). In January 1996, the Court ordered that this action be maintained as a class action. This proceeding arose in connection with the plaintiffs' withdrawal, approximately 25 years ago, of contributions made to the RIP, thereby resulting in a reduction of their pension benefits. The plaintiffs are now seeking, among other things, to have these reduced benefits restored to their pension accounts. LILCO's liability, if any, resulting from this proceeding cannot yet be determined. In November 1997, LILCO filed a motion for partial summary judgment with the District Court. The Court has not yet ruled on LILCO's motion. However, LILCO maintains that the plaintiff's claims are without merit and intends to defend against said claims.

See, also "Environmental Matters."

LILCO is also involved in numerous actions arising from the ordinary conduct of its business. LIPA believes that such litigation, in the aggregate, will not have a material adverse effect on the business or affairs of LIPA Sub after the LIPA/LILCO Merger Transaction.

Possible Future Litigation

The transactions described in this Official Statement, including the contemplated financings, have been the subject of criticism by various individuals and organizations which have publicly stated that additional litigation may be initiated challenging one or more aspects of the transactions described in this Official Statement.

PROPOSED LEGISLATION

A bill has been introduced in the State Legislature titled the "Ratepayer Protection and Utility Competition Act of 1998." The bill provides that any municipality could acquire all or part of LILCO or its successors, and LIPA would be required to "fully cooperate with and assist" in such acquisition. The bill would establish 21 single member districts for the election of the LIPA trustees, with one additional trustee appointed by the governor. In addition, the bill would establish the Long Island Energy Efficiency and Renewable Energy Fund, containing $120 million in contributions from power generators in the Service Area, to provide energy efficiency and renewable energy programs.

LIPA is unable to predict whether this bill will be enacted into law or, if enacted, what its effect on LIPA would be.

AGREEMENT OF NEW YORK STATE

In the LIPA Act, the State pledges to and agrees with the holders of any obligations issued under the LIPA Act and the parties to any contracts with LIPA that the State will not limit or alter the rights vested in LIPA until such obligations together with the interest thereon are fully met and discharged and/or such contracts are fully performed on the part of LIPA, provided that nothing therein contained shall preclude such limitation or alteration if and when adequate provision shall be made by law for

the protection of the holders of such obligations of LIPA, or those entering into such contracts with LIPA. LIPA, as agent for the State, is authorized to include such pledge and agreement by the State in all agreements with the holders of such obligations and in all such contracts. LIPA has included such pledge in the Resolution.

ADDITIONAL INFORMATION AND CONTINUING DISCLOSURE UNDERTAKINGS FOR THE OFFERED SECURITIES

Pursuant to the Continuing Disclosure Certificate dated as of the date of the closing of the sale of the Offered Securities (the "Continuing Disclosure Certificate"), a form of which is attached hereto as Appendix F, LIPA will provide for the benefit of the holders of the Offered Securities certain financial information and operating data relating to LIPA by the dates specified in the Continuing Disclosure Undertaking (the "Annual Report"), and provide notices of the occurrence of certain enumerated events with respect to the Offered Securities, if material. The Annual Report will be filed by or on behalf of LIPA with each Nationally Recognized Municipal Securities Information Repository and with the State Information Depository, if any, established by the State. The notices of such material events would be filed by or on behalf of LIPA with each Nationally Recognized Municipal Securities Information Repository or with the Municipal Securities Rulemaking Board, with such State Information Depository, if any, and with the Trustee. The specific nature of the information to be contained in the Annual Report and the notices of material events is set forth in the form of the Continuing Disclosure Certificate which is included in its entirety in Appendix F hereto. LIPA's undertakings in the Continuing Disclosure Certificate are being made in order to assist the Underwriters in complying with Securities and Exchange Commission Rule 15c2-12.

LEGALITY FOR INVESTMENT

The LIPA Act provides that the Offered Securities will be legal investments for public officers and bodies of the State of New York and all municipalities, insurance companies and associations and other persons carrying on an insurance business, banks, bankers, trust companies, savings banks and savings associations, including savings and loan associations, building and loan associations, investment companies, and other persons carrying on a banking business, all trusts, estates and guardianships, and all other persons whatsoever who are now or may hereafter be authorized to invest in bonds or other obligations of the State of New York, may properly and legally invest funds, including capital in their control or belonging to them. Under the LIPA Act, the Offered Securities are also securities which may be deposited with and may be received by all public officers and bodies of the State and all municipalities for any purpose for which the deposit of bonds or other obligations of the State is now or may hereafter by authorized.

FINANCIAL ADVISOR

LIPA has retained Goldman, Sachs & Co., New York, New York ("Goldman Sachs") as its financial advisor in connection with the acquisition and financings contemplated by LIPA's Plan of Finance. Although Goldman Sachs has assisted in the preparation of the Official Statement, Goldman Sachs is not obligated to undertake, and has not undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information contained in this Official Statement. A portion of Goldman Sachs' fees for acting as financial advisor is contingent upon the issuance of the Offered Securities.

INDEPENDENT CONSULTANT

Resource Management International, Inc. (''RMI'') has been retained by LIPA as its independent consultant. RMI is an internationally recognized firm of approximately 350 engineers, economists and management consultants headquartered in Sacramento, California. RMI is a wholly-owned subsidiary of the Metzler Group, Inc., a publicly traded holding company, which focuses on consulting services to the utility industry. RMI has prepared its Independent Consultant's Report dated April 27, 1998, which is attached to this Part 2 as Appendix A. The majority of RMI's fees for acting as LIPA's independent consultant are not contingent upon the issuance of the Offered Securities. **THE REPORT OF RMI MUST BE READ IN ITS ENTIRETY.**

APPENDIX A

Long Island Power Authority

Electric System General Revenue Bonds
and
Electric System Subordinated Revenue Bonds

Independent Consultant's Report

April 27, 1998

RESOURCE MANAGEMENT INTERNATIONAL, INC.

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RMI

RESOURCE MANAGEMENT
INTERNATIONAL

April 27, 1998

Long Island Power Authority
Board of Trustees
333 Earle Ovington Boulevard
Suite 403
Uniondale, New York

Chairman and Members of the Board of Trustees:

Resource Management International, Inc. (''RMI'') has been retained by the Long Island Power Authority (''LIPA'') in connection with the proposed issuance by LIPA of the Electric System General Revenue Bonds and the Electric System Subordinated Revenue Bonds for the purpose of financing, among other things, the acquisition by LIPA of the Long Island Lighting Company (''LILCO'').

RMI submits this report (the ''Independent Consultant's Report'') stating its findings, assumptions, and conclusions. RMI consents to the inclusion of, and references to, the Independent Consultant's Report in LIPA's Official Statement relating to the proposed bond offering.

In preparation of the Independent Consultant's Report, RMI conducted an evaluation of the engineering, economic, system planning, operations, environmental, and related matters supporting an estimate of the annual operating results of LIPA for the period June 1, 1998 through December 31, 2008. For purposes of this assignment, RMI has made investigations and analyses, including discussions with staff and representatives of LIPA and LILCO, among others, and examinations of reports and projections prepared by consultants and advisors to LIPA, which RMI deemed necessary and appropriate to reach its conclusions. The Independent Consultant's Report attached hereto must be read in its entirety.

Respectfully submitted,

/s/ RONALD O. NICHOLS
Ronald O. Nichols
Senior Vice President

750 LEXINGTON AVENUE, 15TH FLOOR • NEW YORK, NY 10022-1200
(212) 223-3468 • FAX (212) 223-3509 • www.rmiinc.com

With Offices Worldwide

LONG ISLAND POWER AUTHORITY
ELECTRIC SYSTEM GENERAL REVENUE BONDS
AND
ELECTRIC SYSTEM SUBORDINATED REVENUE BONDS

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INTRODUCTION

Presented herein is the report of Resource Management International, Inc. (''RMI'') resulting from RMI's analysis and investigations regarding the proposed issuance by the Long Island Power Authority (''LIPA'') of approximately $7 billion aggregate principal amount of Electric System General Revenue Bonds (the ''Bonds'') and Electric System Subordinated Revenue Bonds (the ''Subordinated Indebtedness'') in accordance with the plan of finance adopted by LIPA's Board of Trustees (the ''Plan of Finance''). The Bonds and Subordinated Indebtedness are being issued pursuant to LIPA's Electric System General Revenue Bond Resolution (the ''General Bond Resolution'') and LIPA's Electric System General Subordinated Revenue Bond Resolution (the ''Subordinated Bond Resolution''), respectively. The Bonds and Subordinated Indebtedness are being issued for the purpose of financing, among other things, the acquisition of the Long Island Lighting Company (''LILCO'') by LIPA through the purchase of LILCO's common stock, the redemption of LILCO's preferred stock, and the refinancing of certain LILCO debt retained by a subsidiary to be created by LIPA (''LIPA Sub'').

Additional series of bonds, notes, or other obligations on a parity with the Bonds (the ''Additional Bonds'') are assumed to be issued by LIPA to finance, among other uses, future capital expenditures and a proposed property tax settlement. A more complete description of the Bonds, the Subordinated Indebtedness, and the Additional Bonds, including the Plan of Finance, is contained in the section entitled ''PLAN OF FINANCE'' in LIPA's Official Statement to which this report is appended (the ''Official Statement'').

RMI is an internationally recognized firm of engineers, economists and management consultants headquartered in Sacramento, California. RMI is a wholly-owned subsidiary of the Metzler Group, Inc., a publicly traded holding company, which provides consulting services to the utility industry. RMI's staff of approximately 350 professionals is engaged primarily in providing services within the energy (including electric and gas utilities, independent power producers, and power marketers), water resources, and telecommunications industries. Typical services include power marketing analysis, transmission and distribution system planning and design, generation facilities review and evaluation, rate and pricing studies, environmental assessments, conservation and demand-side management (''DSM'') program development and evaluation, strategic planning, marketing studies, and related services.

RMI has assisted LIPA in the analysis and planning of the LIPA acquisition and has advised LIPA in connection with various actions and proposals of LIPA discussed herein, including, but not limited to, participation in preparation of the Management Services Agreement (the ''MSA''), Power Supply Agreement (the ''PSA''), and Energy Management Agreement (the ''EMA'') described herein. RMI also assisted LIPA in developing its rates, the proposed Long Island Choice program, its open access transmission tariff, and the negotiation with LILCO of initial capital and operating budgets under the Agreements, as hereinafter defined. RMI is currently serving as the Consulting Engineer and Rate Consultant to LIPA.

RMI has been retained by LIPA in connection with the issuance of the Bonds and the Subordinated Indebtedness to evaluate the engineering, economic, system planning, operations, environmental, and related matters supporting the preparation of an estimate of the annual operating results (the ''Operating Results'') of LIPA for the period June 1, 1998 through December 31, 2008 (the ''Study Period'') shown in Exhibit 1 to this report. For purposes of this assignment, RMI has made investigations and analyses, including, but not limited to, discussions with staff and

representatives of LIPA, LILCO, Niagara Mohawk Power Corporation (''Niagara Mohawk''), the Federal Energy Regulatory Commission (''FERC''), the New York State Public Service Commission (''NYPSC''), New York Public Authorities Control Board (the ''PACB''), the New York State Department of Environmental Conservation (''NYSDEC''), the United States Nuclear Regulatory Commission (''NRC''), the United States Environmental Protection Agency (''EPA''), the Power Authority of the State of New York (the ''New York Power Authority'' or ''NYPA''), and examinations of reports and projections prepared by consultants and advisors to LIPA, which RMI deemed necessary and appropriate to reach its conclusions. RMI's investigations and analyses were conducted with particular emphasis on consideration of those items of major potential economic, financial, environmental, and operational impact on the future operations of LIPA. This report (the ''Independent Consultant's Report'' or the ''Report'') summarizes RMI's findings and presents certain technical and economic information concerning LIPA, LIPA Sub, LILCO, the Bonds and the Subordinated Indebtedness. The Official Statement to which this Independent Consultant's Report is appended should be read in its entirety for additional information on LIPA, LIPA Sub, LILCO, the Bonds and the Subordinated Indebtedness.

LONG ISLAND POWER AUTHORITY

LIPA is a corporate municipal instrumentality and political subdivision of the State of New York authorized under the Long Island Power Authority Act (the ''LIPA Act''). LIPA was created primarily for the purpose of acquiring, by agreement or condemnation, all or any part of the securities or assets of LILCO, an electric and natural gas utility, with the intent of providing safe and reliable electric service at rates lower than would have been charged by LILCO absent the acquisition by LIPA.

The LIPA Act further authorizes the LIPA Board of Trustees (the ''Trustees'' or ''Board'') to set rates and charges for electric service after conducting public hearings. The LIPA Act provides that LIPA is generally not subject to regulation by the NYPSC, including rate regulation. However, LIPA is subject to special provisions contained in the PACB resolution, dated July 16, 1997, approving LIPA's acquisition of LILCO. Information on the conditions established by the PACB relative to the acquisition of LILCO and agreed to by the Trustees are discussed in the section entitled ''PUBLIC AUTHORITIES CONTROL BOARD APPROVAL'' of this Report.

With the exception of certain conditions under Sections 211 and 212 of the Federal Power Act (''FPA''), LIPA's rates and charges for wholesale power sales and for transmission service over its electric system are exempt from FERC regulation. Under Section 211, any electric utility, federal power marketing agency, or any other person or entity generating electric energy for sale for resale may apply to FERC for an order under Section 211 requiring a transmitting utility, including LIPA, to provide transmission services (including any enlargement of transmission capacity necessary to provide such services) to the applicant. FERC may issue an order requiring such transmission service to be provided at non-discriminatory rates and charges if it finds such order meets the requirements of Sections 211 and 212 and would otherwise be in the public interest. In partial recognition of the Section 211 requirements, LIPA will adopt an open access, non-discriminatory transmission tariff under FERC Order No. 888 which will provide access to LIPA's transmission system by third-parties. Please see the section in this Report entitled ''UTILITY RATES AND CHARGES—Open Access Transmission Tariff'' for additional information on LIPA's open access transmission tariff.

OVERVIEW OF THE TRANSACTION

LIPA, LILCO, and KeySpan Energy Corporation (''KeySpan'', the parent holding company of Brooklyn Union Gas Company) entered into the Agreement and Plan of Merger, dated June 26, 1997, which includes a number of definitive agreements (collectively, the ''Agreements''), including the key provisions for the acquisition by LIPA of all of LILCO's outstanding common stock. Following the effective date of the acquisition of LILCO's common stock (the ''Closing Date'' or ''Closing''), LILCO will exist and operate as a subsidiary of LIPA. For purposes of this Report, LIPA and LIPA Sub are collectively referred to as ''LIPA'' following the Closing.

Immediately prior to the Closing Date, LILCO will transfer certain assets (the ''Transferred Assets'') to one or more subsidiaries of BL Holding Corporation (''BL Holding Corp''), a holding company to be formed in connection with the merger of LILCO and KeySpan (See ''The LILCO/KeySpan Combination'' in this section). Assets not transferred to BL Holding Corp (the ''Retained Assets'') will be retained by LIPA through its acquisition of LILCO. The Retained Assets will consist of (i) the electric transmission and distribution system owned by LILCO at the Closing Date, including assets, facilities, equipment, and contractual arrangements used to provide the transmission and distribution of electrical capacity and energy to electric customers within the area served by LILCO (the ''T&D System''); (ii) LILCO's existing 18 percent ownership interest in the Nine Mile Point Nuclear Power Station, Unit 2 (''NMP2''), located in upstate New York; (iii) certain assets consisting primarily of the Shoreham Regulatory Asset, working capital, and accounts receivable; and (iv) Shoreham Nuclear Power Station (''Shoreham'') property tax claims and other tax claims and tax certiorari matters.

The Transferred Assets to be owned by BL Holding Corp will include (i) all non-nuclear generating facilities; (ii) all natural gas utility assets and agreements; (iii) all common plant; (iv) certain materials, inventory, and supplies held by LILCO prior to the Closing; (v) all vehicles owned or leased by LILCO, except those used primarily in the T&D System; (vi) real estate parcels used for or required in connection with existing on-island generating facilities, as well as certain other parcels; (vii) all equipment, except that used primarily in the T&D System; (vii) all rights of LILCO in nitrogen oxide (''NOx'') and sulfur dioxide (''SO2'') emission allowances; (ix) all tax benefits associated with the payment of any accrued liability prior to the Closing Date; and (x) all other assets identified in the Agreements, relating primarily to intellectual property, rights in certain actions and suits, and governmental authorizations applicable to the gas system and on-island generating facilities.

For more complete information on the acquisition of LILCO, including the Retained Assets and the Transferred Assets, please see the section entitled ''THE LIPA/LILCO MERGER'' in the Official Statement.

The LILCO/KeySpan Combination

LILCO and KeySpan announced the proposed merger of the two companies on December 29, 1996 (the ''LILCO/KeySpan Combination ''). The LILCO/KeySpan Combination provides for the business combination of LILCO and KeySpan and the formation of BL Holding Corp as a holding company to manage their combined businesses. Effective with the Closing Date, the Transferred Assets from LILCO will be owned by one or more subsidiaries created by BL Holding Corp pursuant to the Agreements. The LILCO/KeySpan Combination is related to, but not contingent upon, LIPA's acquisition of LILCO and is expected to occur concurrently with the Closing Date.

Agreement and Plan of Merger

The Agreements are comprised of agreements and schedules that provide for the management, operation, and maintenance of the Retained Assets and for related services. Key components of the Agreements are summarized below.

Management Services Agreement

The MSA provides for a subsidiary of BL Holding Corp (the "Manager") to (i) perform the day-to-day operation and maintenance of the T&D System in accordance with policies established by LIPA and (ii) administer and manage LIPA's interest in NMP2 using employees and management currently employed by LILCO. The MSA has a term of eight years. The MSA mandates that in the sixth year, LIPA will seek competitive proposals for a new management contract effective at the expiration of the MSA. The MSA does not grant any rights of control or ownership of the T&D System or NMP2 to the Manager, BL Holding Corp, or its subsidiaries, other than those rights necessary for the routine operation and maintenance of the T&D System and for the management and administration of LIPA's interest in NMP2. For additional information on the MSA, please see the section entitled "TRANSMISSION AND DISTRIBUTION SYSTEM—Management and Operation" in this Report and Appendix E of the Official Statement.

Power Supply Agreement

The PSA provides that a subsidiary of BL Holding Corp ("GENCO"), formed to own all of the existing oil and natural gas-fired generating facilities on Long Island presently owned by LILCO, will sell to LIPA all of the capacity of such generating facilities. However, the PSA does not obligate LIPA to make energy purchases from GENCO. The PSA has a term of 15 years and contains provisions which provide LIPA the opportunity to reduce its obligation to purchase generating capacity from GENCO under a "rampdown" schedule beginning in the seventh year of the PSA, subject to continuation of certain capacity-related payments. LIPA has the option to renew the PSA at the end of the 15-year period on terms consistent with the original PSA for all capacity which has not been ramped down. For additional information regarding the PSA, please see the section entitled "POWER SUPPLY AGREEMENT" in this Report and Appendix E in the Official Statement.

Energy Management Agreement

The EMA provides that a subsidiary of BL Holding Corp (the "Energy Manager") will (i) procure and manage fuel supplies for LIPA to fuel the GENCO generating facilities, (ii) perform off-system capacity and energy purchases on a least-cost basis to meet LIPA's needs, and (iii) make off-system sales of output from the GENCO generating facilities and other power supplies either owned or under contract to LIPA. LIPA is entitled to two-thirds of the profit from any off-system energy sales arranged by Energy Manager. The term for the service provided in (i) above is fifteen years, and the term for the service provided in (ii) and (iii) above is eight years. Schedule F (Grant of Future Rights) of the Agreements, provides for a continuation of the existing intra-company gas transportation rate for a period of 11.5 years for gas delivered over the gas distribution system to the GENCO plants and to new generation resources above a minimum unit size established by LIPA. For additional information regarding the EMA, please see Appendix E to the Official Statement.

Other Agreements

In addition to the agreements summarized above, the Agreements include (i) the Generation Purchase Right Agreement which provides LIPA with the right to acquire all GENCO generation facilities in the fourth year of the PSA; (ii) the Grant of Future Rights, including rights to the

acquisition of additional generating sites; and (iii) other rights integral to the acquisition, management, and operation of the T&D System, LIPA's interest in NMP2, and LIPA's ability to provide electric service to its customers. For more information on these agreements and rights, please see Appendix E to the Official Statement.

The Agreements provide that, as of the Closing Date, BL Holding Corp and its subsidiaries will execute and deliver promissory notes (the "Promissory Notes") in connection with certain LILCO debt retained by LIPA. The aggregate principal amount of the Promissory Notes will be equal to the excess, if any, of the indebtedness of LILCO outstanding on the Closing Date over the portion of the LILCO debt for which LIPA is to be financially responsible. The rates and maturities of the Promissory Notes will correspond to the rates and maturities on the LILCO debt retained by LIPA and are to be adjusted to require payment by BL Holding Corp thirty days prior to the corresponding payment dates on this debt.

Summary of Financing Plan

The Bonds and the Subordinated Indebtedness are expected to aggregate approximately $7 billion and will be used to (i) acquire LILCO's common stock; (ii) redeem LILCO's preferred stock; (iii) refinance LILCO's General and Refunding Bonds; (iv) fund the initial installment of a Shoreham property tax settlement; (v) fund initial capital expenditures; (vi) purchase an interest rate hedge from BUG/LILCO Hedge Fund L.L.P.; (vii) reimburse the State of New York (the "State") for advances made to LIPA; and (viii) pay the costs of issuance. The Plan of Finance contemplates issuing the Bonds in three tranches during 1998.

Following the issuance of the Bonds and the Subordinated Indebtedness in connection with the acquisition of LILCO, LIPA expects to fund approximately 100 percent of its annual capital requirements, together with the funding of the remaining balance of the Shoreham property tax settlement, through the issuance of Additional Bonds. These Additional Bonds are expected to be issued beginning in 1999 and each year thereafter. For additional information regarding LIPA's Plan of Finance, please see the section entitled "PLAN OF FINANCE—LIPA Financings" in the Official Statement.

Security of Customer Revenues

The Bonds and the Subordinated Indebtedness will be secured by a pledge of the net revenues received by LIPA from the sale of electricity and other services, and will not be an obligation of the State or any other governmental entity. In evaluating LIPA's future customer revenues, RMI considered changes now occurring in the electric utility industry, including movement toward retail customer choice of power suppliers, the availability of dispersed electric generating facilities suitable for small commercial or industrial installations, and efforts by communities on Long Island to form municipal electric utilities, among other factors. For more information on the security of LIPA's revenue, please see the section entitled "SECURITY OF CUSTOMER REVENUE" in this Report.

DESCRIPTION OF THE SERVICE AREA

The map following Part 1 of the Official Statement provides an illustration of the area to be served by LIPA (the "Service Area") and the location of major facilities of the Retained Assets and GENCO. These and other characteristics are described below.

Geographic Area

The Service Area encompasses the bulk of Long Island in New York State, and is comprised of Nassau and Suffolk Counties and the Rockaway Peninsula in Queens County, an area of approximately 1,230 square miles, excluding areas served by three existing municipal utilities: the villages of Freeport, Greenport, and Rockville Centre. Suffolk County is the easternmost county within the Service Area and covers an area of approximately 911 square miles, followed by Nassau County with a 287 square mile area, and the Rockaway Peninsula with an area of approximately 32 square miles. The Service Area is bounded by the Atlantic Ocean on the south and east, by the Long Island Sound on the north, and by portions of New York City on the west. The population of the Service Area was estimated to be approximately 2.7 million as of January 1, 1997.

Climatic Factors

Long Island experiences seasonal conditions typical of the northeast United States. Summers are usually hot with high temperatures in excess of 90F. Winters include snow and icing conditions that can be damaging to overhead power lines. In addition, the Service Area experiences severe storms, including nor'easters and hurricanes, that can be particularly damaging due to Long Island's coastal location. In response to these conditions, the T&D System has been constructed and maintained to minimize damage from high winds, and LILCO has developed storm response procedures designed to restore service expeditiously. Please see the section entitled "THE TRANSMISSION AND DISTRIBUTION SYSTEM—Storm Restoration Program" in this Report for a description of LILCO's storm response procedures.

Regional Economy

Once considered a "bedroom community" of New York City, Long Island has evolved into a significant regional economy that benefits from its proximity to Manhattan, but also generates its own income, employment, and regional output. Prior to the 1980's, the Long Island economy was dominated by the activities of several large defense contractors, including Grumman, Baton AIL, Fairchild Republic, and Sperry. In less than ten years, however, all four of these large defense companies have either discontinued operations on Long Island or have significantly downsized their operations. Defense activity, which was once the mainstay of the economy, is not likely to regain its prior dominance on Long Island, and the region is unlikely to attract any large industrial customers in the foreseeable future.

Future economic gains on Long Island are likely to be based, in part, on the effective utilization of the region's current assets, such as:

- highly skilled labor force;
- close proximity to New York City;
- diverse institutions of higher education;
- location advantages for European markets;
- strong, diversified technology base;

- core research institutions, such as Brookhaven National laboratory, Cold Spring Harbor Laboratory, and medical research centers, such as North Shore Hospital; and
- suburban life style.

Long Island's residential market is relatively affluent. Long Island is ranked highly in economic characteristics among the metropolitan statistical areas throughout the United States. According to the *Long Island Business News*, Long Island ranks first in the United States in:

- median household effective buying income;
- the percentage of households having income of $50,000 or more; and
- the percentage of household incomes of $150,000 and over.

The Long Island economy benefits from low unemployment (approximately 3.8 percent in 1997), high average personal income, and a strong service-based economy. Annual new housing starts have grown from 4,500 in 1994 to 5,800 in 1997. Office vacancy has declined from a peak of nearly 16 percent in 1995 to approximately 10.5 percent at year-end 1997. The decline in unemployment and office space vacancy as well as the gain in new housing starts has occurred despite the decline in manufacturing activity on Long Island. Recent historical electric sales reflect this trend, revealing a modest decline in sales to manufacturing customers in recent years, while sales to customers in retail and service sectors have increased. Please see the section entitled "SYSTEM LOADS AND RESOURCES—System Capacity and Energy Requirements" in this Report for additional information on historical capacity and energy sales within the Service Area.

Customer Base

Approximately 99 percent of LIPA's total sales revenues are projected to be from electric sales to retail customers. LIPA expects to serve over one million retail electric customers, of which approximately 927,000 will be residential and 106,000 commercial and industrial. Approximately 49 percent of annual electric revenues are expected to be received from residential customers, with 48 percent expected to come from commercial and industrial customers, and the balance from sales to other utilities and public authorities.

Although commercial and industrial customers provide a significant portion of annual electric sales revenues, these customers account for only 10 percent of the retail electric customers served by LIPA. In general, individual commercial and industrial customers are relatively small, with approximately 45 percent of these customers having peak demands less than 75 kilowatts ("kW"). Furthermore, the Service Area does not contain traditional "industrial" loads, and customers served under this rate classification are primarily large commercial customers. The single largest customer in the Service Area accounts for less than two percent of total electric sales. Overall, the 20 largest electric customers, in aggregate, accounted for less than four percent of total retail energy sales and revenues during 1997. Although a decline in manufacturing has reduced base load energy requirements within the Service Area, the remaining service-dominated economy is believed to represent a more stable economic base, with less risk of loss of load.

In addition to its retail customers, LIPA will make wholesale sales (sales for resale) to other electric utilities, including the three existing municipally-owned electric utilities on Long Island (the villages of Greenport, Freeport, and Rockville Centre). These villages rely primarily upon their own generation and purchases from the New York Power Authority for their power supply. LILCO has historically sold only minimal amounts of energy directly to these villages for resale, a situation that is likely to continue under LIPA ownership.

LIPA will also provide electric transmission service to NYPA for the delivery of NYPA capacity and energy to the three municipal utilities and other NYPA-power recipients on Long Island, including the Suffolk County Electrical Agency ("SCEA") and the Nassau County Public Utility Agency ("NCPUA"). Please see the section in this Report entitled "SECURITY OF CUSTOMER REVENUE —Long Island Electrical Agencies" for a discussion concerning SCEA and NCPUA.

Historical Sales and Revenues

Exhibit 2 of this Report provides summary information on LILCO's annual energy sales and retail electric revenues during the 1993 through 1997 period. Also included in Exhibit 2 is information on numbers of retail electric customers for this historical period. LILCO's annual electric sales during 1997, unadjusted for weather normalization, were less than one percent higher than 1993 sales levels, in part the result of additional cogeneration and NYPA power deliveries during this period. The relatively mild weather during the 1997 summer season also impacted this modest increase in sales.

THE TRANSMISSION AND DISTRIBUTION SYSTEM

Description of Facilities

The T&D System is an integrated electric transmission and distribution system consisting of overhead and underground facilities, vehicles, equipment, contractual arrangements, land parcels, easements, and other assets used to provide the transmission and distribution of electric capacity and energy to and within the Service Area. Key components of the T&D System are summarized below.

Transmission Interconnections

Electricity is transmitted to and from the Service Area over five transmission interconnections which will be owned in part or will be under contract to LIPA. These interconnections tie the T&D System to other utilities and enable delivery of (i) capacity and energy produced by NMP2; (ii) additional off-system capacity resources needed to meet the peak demands of the electric customers; (iii) favorably-priced energy to supplement or displace generation from on-island generating resources; and (iv) excess generation from on-island generating facilities to off-island purchasers when conditions merit. Table 1 provides summary information on the transmission interconnections.

TABLE 1

SERVICE AREA TRANSMISSION INTERCONNECTIONS

Name	Off-System Terminal Location	Interconnecting Utility (1)(2)	Voltage Level (3)
Dunwoodie to Shore Road	Westchester County, NY	Con Edison	345kV
East Garden City to Sprainbrook	Westchester County, NY	NYPA	345kV
Northport to Norwalk Harbor	Norwalk, CT	CL&P	138kV
Jamaica to Lake Success	Queens, NY	Con Edison	138kV
Jamaica to Valley Stream	Queens, NY	Con Edison	138kV

(1) These utilities own the portion of the interconnections not owned by LIPA, except for the interconnection with NYPA, which is owned entirely by NYPA.

(2) Con Edison = Consolidated Edison Company of New York, Inc.; CP&L = Connecticut Light and Power.

(3) Kilovolt or "kV".

Two of the T&D System's transmission interconnections are tied to the Con Edison transmission system in Queens County, New York. LIPA will own these facilities to the border of Nassau County and Queens County, at which point ownership transfers to Con Edison. The three remaining interconnections extend under water across Long Island Sound to New York or Connecticut. One of these lines, the East Garden City to Sprainbrook line is owned entirely by NYPA (the "NYPA Line") and will be used by LIPA under the terms of the current contract between LILCO and NYPA. The other two interconnections will be owned by LIPA from their termination points on Long Island to the middle of Long Island Sound, at which point ownership is held by the interconnecting utility.

The agreement between LILCO and NYPA for the NYPA Line provides that LILCO will reimburse NYPA for the costs it incurs in connection with the NYPA Line, including, but not limited to, debt service, reserves, and operation and maintenance expenses, in return for the use of the capacity of the line. LILCO was initially allocated the full capacity of the NYPA Line and to the extent that NYPA allocates capacity to other parties, LILCO's payment obligations are proportionately reduced, with such other parties making payments pursuant to rates under NYPA's Open Access Tariff. In the past, NYPA has allocated capacity of the NYPA Line to certain loads served by NYPA in the Service Area when there has been insufficient capacity to serve such loads on another transmission line jointly owned by LILCO and Con Edison. This practice is expected to continue after the Closing.

Transmission Facilities

The transmission facilities permit the transmission of capacity and energy from the transmission interconnections and the on-island generating facilities owned by GENCO and other power suppliers to LIPA's electric distribution system. The transmission system includes approximately 1,300 miles of overhead and underground lines. Table 2 provides a summary of LIPA's transmission line statistics, inclusive of transmission lines associated with LIPA's off-system transmission interconnections.

TABLE 2

CIRCUIT MILES OF TRANSMISSION LINE(1)

Voltage Level	Overhead	Underground	Total
345kV	—	8	8
138kV	218	116	334
69kV	635	55	690
33kV	97	3	100
23kV	133	53	186
Total	1,083	235	1,318

(1) Miles of line as of December 31, 1997.

The on-island transmission system has been constructed following standards similar to those employed by other major electric utilities in the Northeast and includes wood poles, steel poles, and lattice steel towers. Many of the existing transmission structures include distribution circuits and/or connections for telephone, cable television, or fiber optics. In addition, certain T&D System facilities have been installed on structures owned by Bell Atlantic pursuant to a joint-use agreement.

Thirty-two transmission substations are in service and utilized on the T&D System. The combined capability of these substations is approximately 6,838 million volt amperes ("MVA"). The transmission system also includes transformation equipment at 13 generating sites used to step up the

generation voltage to transmission levels. With the exception of certain facilities at the GENCO generating facilities (e.g., auxiliary and starting transformers), transformation equipment at these sites is included in the Retained Assets and will be owned by LIPA following the Closing.

Distribution Facilities

The distribution system consists of 13-thousand volt (''kilovolt'' or ''kV'') and 4-kV facilities. These facilities are a combination of overhead, underground, and network equipment. There are 146 substations throughout the Service Area that step the voltage down from transmission to distribution levels. These distribution substations have a combined transformation capability of approximately 5,759 MVA. The distribution system also includes approximately 56,000 circuit miles of overhead and underground line and approximately 149,000 line transformers with a total capacity of 7,500 MVA. Table 3 provides a summary of LIPA's distribution line statistics.

TABLE 3

CIRCUIT MILES OF DISTRIBUTION LINES

Type of Construction	Circuit Miles(1)
Overhead	46,029
Underground	10,354
Total	56,383

(1) Miles of lines as of December 31, 1997

Condition of Facilities

During January 1998, RMI conducted on-site observations of the principal and representative facilities comprising the T&D System. These observations consisted of visual examinations of facilities which RMI deemed adequate to allow it to assess the general condition of the facilities. In addition to field observations, RMI reviewed historical operation and maintenance records for the T&D System to assess past performance levels and examined written maintenance procedures to evaluate the adequacy of existing maintenance practices. RMI also reviewed the 1998 T&D System capital and operating budgets agreed to by LIPA and the Manager to assess the adequacy of budgeted expenditures to maintain historical T&D System reliability levels. Based on the observations and assessments conducted by RMI and the measured reliability of the T&D System as discussed further below, the T&D System is considered to be in good condition.

Three submarine cables installed across Long Island Sound form part of the interconnection between the T&D System and other utility systems. The Dunwoodie to Shore Road line, a 345-kV cable designated as Y-50 and placed in operation in August 1978, is owned jointly with Con Edison. This cable is of pipe-type construction in which dielectric fluid is circulated to cool the conductors and maintain the electrical insulation. A second interconnection, the NYPA Line, was installed in 1991 and is designated the Y-49 line. The eight-mile, 345-kV submarine portion of this line extends from Westchester County to Nassau County and is constructed of self-contained dielectric fluid-filled cables that operate under high pressure. The land-based portions of the NYPA line are of conventional pipe-type construction. This line connects to the T&D System at the East Garden City substation. A third interconnection is the Northport to Norwalk Harbor line, a 138-kV submarine cable installed in 1969,

that extends approximately twelve miles under the Long Island Sound from the Northport generating station in Suffolk County to Connecticut. LIPA will have ownership of this line to the New York-Connecticut state boundary. This dielectric fluid-filled cable system has periodically incurred damage from ship and barge anchors, most recently in 1996. The damage from these incidents has been repaired and the cable is in operation. The interconnections appear to be in good operating condition.

Since 1992, LILCO has pursued a program to improve the reliability and quality of electric service within the Service Area. For the distribution system, this program has focused on four major areas, consisting of (i) circuit improvements; (ii) distribution system automation; (iii) underground feeder exit replacement; and (iv) pole replacement. For the transmission system, this program has focused on (i) circuit improvements; (ii) substation reliability improvements; and (iii) pole replacements. The programs undertaken for the T&D System have resulted in material reductions in the frequency of customer outages and helped to mitigate increases in the duration of these outages.

Two key industry standard criteria for measuring transmission and distribution system reliability are:

1. **System Average Interruption Frequency Index ("SAIFI"),** which is derived by dividing the total number of customers affected or interrupted during the year by the total number of customers served; and

2. **Customer Average Interruption Duration Index ("CAIDI"),** which is derived by dividing the total number of customer hour duration of interruptions during the year by the total number of customers affected.

The MSA establishes incentive measures for the Manager to maintain SAIFI and CAIDI indices for the T&D System within prescribed levels. Information on these incentives may be found in Appendix E of the Official Statement. Figures 1-A and 1-B compare the historical T&D System reliability, as measured by these two indices, to (i) the system-wide average incentive levels under the MSA; and (ii) the average performance of the five other investor-owned electric utilities in New York State with predominately overhead distribution systems. The utilities included in this comparison are:

- Central Hudson Gas & Electric Corporation
- Niagara Mohawk Power Corporation
- New York State Electric & Gas Corporation
- Orange and Rockland Utilities Incorporated
- Rochester Gas and Electric Corporation

Con Edison has been excluded from Figures 1-A and 1-B because much of its system is of underground construction and therefore not subject to the potential for damage typical of above-ground systems. The results graphically depicted in Figures 1-A and 1-B represent a system-wide average for the T&D System, whereas the specific MSA incentives are tied to performance within four distinct operating districts of the T&D System. For both SAIFI and CAIDI, a low value is favorable and, for SAIFI, indicates less frequent service interruptions, and, for CAIDI, indicates a shorter average duration of the outages which have occurred. Consistent with industry practice, the statistics shown in Figures 1-A and 1-B exclude the effects of major storms.

FIGURE 1-A

AVERAGE NUMBER OF OUTAGES PER CUSTOMER PER YEAR (SAIFI)

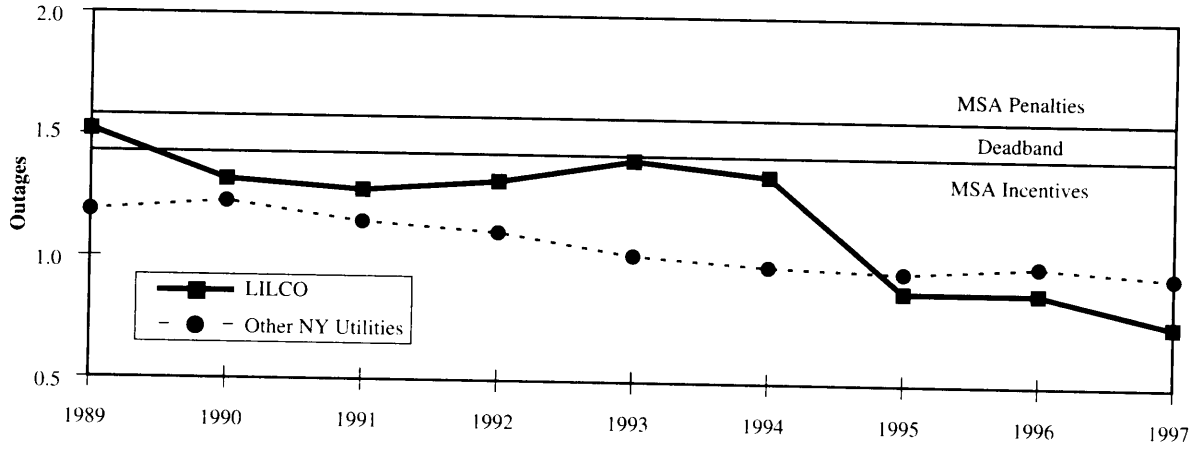
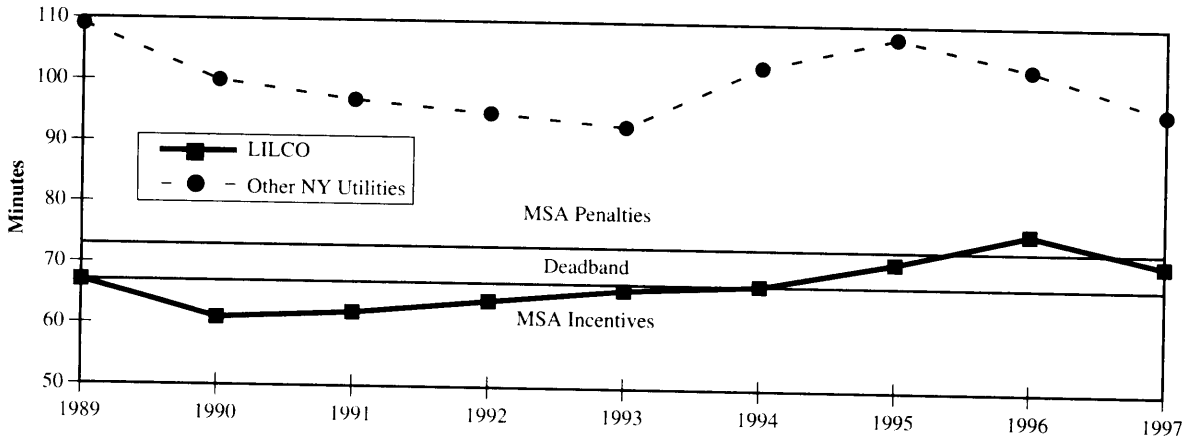


FIGURE 1-B

AVERAGE TOTAL ANNUAL OUTAGE TIME PER CUSTOMER (CAIDI)



As Figure 1-A illustrates, from 1989 through 1997 the average annual number of outages per customer has declined substantially. The T&D System's performance since 1995 compares very favorably to the other large electric utilities in the State. Over this same period, the duration of these interruptions, as measured by CAIDI and as shown in Figure 1-B, while climbing slightly until 1996, declined in 1997, and ranks as the best among the comparable electric utilities in New York State. Long Island is exposed to high winds and periodic icing conditions and has a high concentration of heavily treed rights-of-way. Achieving levels of reliability above the levels experienced by comparable New York State utilities, while facing these adverse conditions, is evidence of the emphasis LILCO has placed on reliability of service in programs and budgets. As discussed under "CAPITAL EXPENDITURES" in this section, LILCO increased capital expenditures for the T&D System by an average of approximately $9 million annually during the 1994 through 1997 period, as compared to the average for 1992 and 1993, reflecting, in part, greater expenditures for reliability improvements.

The capital budgets reflected in the projected Operating Results in this Report provide for similar continued levels to help support system reliability improvements.

Management and Operation

Pursuant to the MSA, LIPA will rely on the Manager to operate and maintain the T&D System in accordance with policies established by LIPA. The Manager's responsibilities under the MSA include, but are not limited to, (i) the day-to-day operation, and maintenance of the T&D System, including emergency repairs, customer service, billings, and meter readings; (ii) routine facility additions and improvements, including customer connections, procurement of goods and services from third-parties, and inventory management; (iii) preparing and monitoring budgets, load and energy forecasts, and power resource models and plans; and (iv) maintaining an operation and maintenance manual for the T&D System. In addition to complying with all applicable laws and prudent utility practices, the Manager must also comply with T&D System policies and procedures established by LIPA.

LIPA will be responsible for, among other things, (i) setting rates and charges; (ii) line extension policies; (iii) service rules and regulations; (iv) approval of long-term strategic plans; (v) determination of customer service programs; (vi) approval of annual budgets; (vii) approval of the Manager's load forecast and power resource models and plans; (viii) determination of all energy efficiency, conservation and load management policies and plans, (ix) governmental relations and reporting; (x) overall legal responsibilities; (xi) oversight of the Manager's operations and performance, and (xii) community and public relations. LIPA will also have the right to approve the appointment of key personnel of the Manager who report directly to a designated LIPA representative.

In exchange for the services rendered under the MSA, the Manager will be entitled to receive an annual service fee as compensation. The service fee will be paid on a monthly basis and will be calculated based on five components, consisting of a (i) fixed direct fee; (ii) third-party cost reimbursement component; (iii) variable payment; (iv) cost incentive fee; and (v) non-cost performance component. In addition to the service fee, the Manager will be reimbursed for all approved third-party costs and will be paid or reimbursed for certain capital and unforeseeable costs.

Under the MSA, the cost incentive fee is payable annually when actual costs are less than the total cost budget. The non-cost performance incentive component of the MSA applies when LILCO's performance meets certain threshold levels of system reliability, worker safety, and customer service. The fee structure is also subject to disincentives when actual costs exceed the budget and where the performance is below threshold minimums.

For a more complete description of the MSA, please see Appendix E of the Official Statement.

Storm Restoration Program

Under the terms of the MSA, the Manager will continue the storm response and storm restoration programs which LILCO has used historically. LILCO has cross-trained its gas utility and generation staff to perform electric transmission and distribution emergency restoration services in response to storm damage to increase the availability of field forces to restore service. The MSA provides for the GENCO staff and the gas system employees of BL Holding Corp to continue to be cross-trained and available for emergency storm response services associated with the T&D System.

LILCO has also historically relied upon standard electric utility industry mutual aid programs wherein neighboring and regional utilities provide emergency assistance to one another in the event of

outages from major storms. The Manager will continue using such mutual aid assistance arrangements on behalf of LIPA.

Table 4 presents the total cost of major storm damage within the Service Area over the past five years.

TABLE 4
MAJOR STORM EXPENDITURES FOR THE T&D SYSTEM
($000)

Year	
1993	$19,794
1994	12,791
1995	14,400
1996	16,732
1997	8,478

The average cost of major storm damage to the T&D System has been approximately $14.4 million over the past five years. LIPA intends to provide a combination of reserves and insurance to provide for the funding of major storm damage restoration. Under the MSA, $4 million annually is budgeted for the Manager to provide storm restoration services and is included in the estimated Operating Results presented in Exhibit 1 of this Report. In addition, LIPA has included in revenue requirements an annual storm restoration reserve contribution of $10 million, which is twice the historic level of reserves maintained by LILCO for this purpose. Finally, LIPA has informed RMI that it intends to maintain property damage insurance which will provide approximately $40 million to $50 million of insurance coverage for storm and other property damage. An allowance for the insurance premiums for such coverage is included in the estimated Operating Results in Exhibit 1 in this Report.

Capital Expenditures

During the period 1993 through 1997, LILCO spent an average of approximately $97 million per year on additions and improvements to the T&D System. These improvements and additions included moneys for reliability enhancements, capability expansion, new customer connections, facility replacements, and public works projects.

In accordance with the terms of the MSA, LIPA and the Manager have agreed to a capital budget for the T&D System for 1998. The 1998 capital budget provides for a continuation of the historical programs to improve reliability and quality of electric service, as well as appropriate levels of expenditure for capability expansion, new customers, facility placements, and public work projects that are comparable to historical levels. Table 5 provides a breakdown of the 1998 capital budget by principal activity, together with information on the historical level of expenditures during the 1993 through 1997 period.

TABLE 5

T&D SYSTEM CAPITAL EXPENDITURES
(Millions of Dollars)

Expenditure Category	Historical					Budget
	1993	1994	1995	1996	1997	1998(2)(3)
Reliability	$30	$34	$ 40	$33	$ 42	$ 47
Expanded Capability(1)	13	9	16	15	12	12
New Customers	12	14	19	19	24	20
Replacements	24	29	31	25	19	26
Public Works	4	6	5	5	3	2
Total(4)	$84	$92	$111	$97	$100	$107

(1) Increase in capacity of overhead and underground lines and substations.
(2) Amounts shown for 1998 exclude allowance for funds used during construction and certain other costs totalling approximately $10 million annually that have been included historically.
(3) Represents 12-months of expenditures.
(4) Amounts may not total exactly due to rounding.

LIPA anticipates that future T&D System capital expenditures, in the aggregate, will be comparable to the expenditure levels reflected in the 1998 T&D System budget, adjusted for inflation and customer growth. T&D System capital expenditures will be subject to LIPA's annual approval process under the terms of the MSA. Exhibit 3, "Estimated Capital Expenditures," includes RMI's estimate of LIPA's T&D System capital expenditures for the Study Period. Please see the section entitled "FINANCING REQUIREMENTS—Capital Expenditures" of this Report for more details.

Environmental Review

Under the terms of the Agreements, the Retained Assets will include approximately 260 properties, consisting of approximately 2,205 parcels of land, and 40,000 easements on properties owned by others. RMI reviewed information on liabilities associated with the environmental investigation and remediation activities currently required, or that will be required, in connection with the T&D System properties to be owned by LIPA. In addition to these liabilities, liabilities may accrue to LIPA in connection with certain Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") Superfund sites which allege a nexus to LILCO's historical operations, liabilities associated with common facilities, and liabilities associated with being an operator under CERCLA for easements granted to LIPA for the T&D System.

RMI reviewed reports, data, and other documentation provided by LILCO concerning remediation efforts at five T&D System properties and eight Superfund sites and other miscellaneous environmental liabilities. The majority of the known or suspected environmental liabilities associated with existing LILCO property pertain to contamination from past manufactured gas plant ("MGP") sites related to historical gas utility operations and are not LIPA's responsibility. BL Holding Corp is providing LIPA with complete indemnification for all liabilities arising from all MGP operations. As a result of this indemnification, no reserves for the remediation of the MGP sites resulting from gas plant operations have been included in the estimate of LIPA's annual Operating Results.

Because detailed information on environmental conditions at a majority of the properties has not previously been required by LILCO, RMI has commissioned, through a subcontractor retained on behalf of LIPA, an environmental site assessment of the T&D System and other Retained Assets. In

addition, RMI is undertaking an independent review of estimates prepared by LILCO of environmental liability, including those for Superfund liabilities. The environmental site assessment performed by RMI's subcontractor uses the American Society for Testing and Measurement evaluation method, which includes literature research of past activity and limited on-site surface inspection of certain sites, locations, and rights-of-way. No physical soil or ground water sampling nor any other physical sampling or testing has been undertaken to verify the potential presence or concentration of contaminants.

This preliminary assessment was undertaken as a means to determine the potential extent of environmental liability which may exist. Absent a complete evaluation of all property to which LIPA has rights, there can be no assurance that environmental liabilities do not exist, nor that the preliminary assessment of locations addressed in the evaluation will identify environmental contamination which may exist.

Based upon the known Superfund sites, the preliminary environmental assessment described above, and discussion with and representations by LILCO, RMI is unaware of any environmental liabilities of a magnitude which would materially negatively impact the Operating Results presented in Exhibit 1 of this Report. As shown in Exhibit 1, and as discussed under the section "OPERATING RESULTS" in this Report, the rate stabilization fund to be created by LIPA (the "Rate Stabilization Fund") is estimated to maintain a significant balance in each year, even after substantial accelerated payment of LIPA debt. To the extent unanticipated environmental liabilities arise which are the responsibility of LIPA and associated remediation costs are incurred, LIPA is expected to use insurance proceeds and other available funds for the payment of such remediation and related costs.

Health and Safety

As a basis for assessing the adequacy of LILCO's health and safety programs, RMI reviewed Occupational Safety and Health Administration ("OSHA") citations, OSHA 200 Logs, and LILCO's Corporate Quality Assurance Department safety-related audit reports and health and safety program documents. In addition, RMI interviewed LILCO's safety program manager, an industrial hygiene representative from LILCO's Environmental Engineering Department, an attorney representing LILCO's Human Resources Department, and health department representatives from both Nassau and Suffolk Counties.

Based on RMI's review, it appears that LILCO's health and safety program is designed and implemented to meet basic OSHA and local government requirements. Historically, worker injury and accident rates have been slightly better than the industry averages reported by the Bureau of Labor Statistics and on a par with National Safety Council members participating in the "Occupational Safety Health Award Program." Furthermore, during 1997, LILCO recorded its best safety performance ever. LILCO's health and safety management program is generally typical of programs found at utilities with similar operations. These programs are expected to be continued by the Manager under LIPA's ownership. The budget levels adopted under the MSA are consistent with the continuation of a health and safety program of the type LILCO has previously conducted to safeguard workplace safety.

POWER SUPPLY AGREEMENT

The PSA provides for GENCO to supply LIPA with all of the capacity of the electric generation facilities on Long Island presently owned by LILCO, which facilities will be transferred to GENCO at

Closing. The GENCO facilities consist of 53 fossil fuel generating units at 13 sites on Long Island. These steam, combustion turbine, and internal combustion generating units operate using oil, natural gas, or both, and have a dependable maximum net capability (''DMNC'') of 3,973 megawatt (''MW'') based on average DMNC test results for 1993-1997. DMNC represents the maximum rate of production of the generating facilities, as determined through periodic testing in accordance with New York Power Pool (''NYPP'') procedures. Descriptive information for these facilities is summarized in Exhibit 4 of this Report.

Although the GENCO facilities will be operated and maintained by GENCO, the Energy Manager, under the EMA, will be responsible, on behalf of LIPA, for procuring fuel for the GENCO facilities and for dispatching all power resources owned by, or under contract to, LIPA. The PSA has a term of 15 years and may be renewed by LIPA at the end of this period on terms comparable to the original PSA.

LIPA and GENCO have agreed to certain fixed and variable rates for the initial year of the PSA and to a formula for adjustment of these charges through the term of the PSA. These rates are subject to the jurisdiction of the FERC, which has approved the rates to become effective at Closing, subject to refund. These rates are the basis for the GENCO-supplied portion of the power supply costs included in the estimated Operating Results in this Report. LIPA and GENCO expect to renegotiate the levels of the fixed and variable charges to become effective for successive five year periods beginning in 2004 and 2009, subject to FERC approval. Under the terms of the PSA, GENCO's capital expenditures for which LIPA is responsible are subject to approval by LIPA. LIPA will pay for approved GENCO capital expenditures through the depreciation accruals and return on investment included in the rates charged under the PSA. The PSA also provides for certain incentives and disincentives related to targeted performance levels by GENCO, including summer DMNC, summer availability, and efficiency levels (heat rate) of the generating facilities.

The PSA provides LIPA the option of electing to reduce or ''ramp-down'' the capacity it purchases from GENCO beginning in year seven of the PSA, in accordance with schedules set forth in the PSA. In years seven through ten of the PSA, if LIPA elects to ramp-down, GENCO is entitled to payment for 100 percent of the present value of the capacity charges otherwise payable over the remaining term of the PSA. If LIPA ramps-down the generation capacity in years 11 through 15 of the PSA, the capacity charges otherwise payable by LIPA will be reduced in accordance with a formula established in the PSA. If LIPA exercises its ramp-down option, GENCO may use any capacity released by LIPA to bid on new LIPA capacity requirements or to bid on LIPA's capacity requirements to replace other ramped-down capacity. If GENCO continues to operate the ramped-down capacity, the PSA requires it to use reasonable efforts to market the capacity and energy from the ramped-down capacity and to share any profits with LIPA. In the event of such power sales, the profits will take into consideration all costs which have been recovered by GENCO, including previous payments from LIPA. Capacity and energy sold by GENCO from ramped-down capacity must be transported over the T&D System and GENCO will be required to pay LIPA's standard transmission and distribution rates for this service. The PSA will be terminated in the event that LIPA exercises its generation purchase right under the Agreements. For a more complete description of the PSA, please see Appendix E of the Official Statement.

The GENCO capacity will comprise approximately 80 percent of LIPA's total capacity resources during 1998 and approximately 72 percent by the end of the Study Period. Nonetheless, while LIPA has the rights to all energy from the GENCO capacity, LIPA is not obligated under the PSA to purchase any specified amount of energy from GENCO and will procure energy resources from the lowest cost sources available. During 1997, the GENCO resources accounted for approximately 56

percent of the Service Area's energy requirements. Please see the section entitled "SYSTEM LOADS AND RESOURCES" in this Report for additional information on the operating history of the GENCO facilities.

Condition of Facilities

In July and November 1997, RMI representatives conducted field observations of the major GENCO facilities to observe their condition. These observations consisted of plant walk-throughs, discussions with plant staff, and a limited review of operating and maintenance records. This review was undertaken to determine the general condition of the generating facilities and to provide familiarity with the units in order to put the capital budget and operation and maintenance budgets in context. As a whole, the facilities that RMI observed were found to be in good operating condition, as evidenced by a reasonably constant DMNC and unit availability during recent years and taking into account their age and operating history. Under the PSA, GENCO is expected to implement an on-going capital improvement program to identify deteriorated equipment and replace it if appropriate.

Capital Expenditures

During the period 1993 through 1997, capital expenditures for the GENCO units averaged $32.7 million annually. A significant portion of these expenditures may be characterized as one-time, rather than recurring, in nature. These one-time expenditures include natural gas conversions to enable dual-fuel capability at existing oil-fired stream units and control system upgrades at other units. RMI expects the magnitude of such expenditures to diminish after completion of similar projects underway or planned. In December 1997, LIPA agreed to an annualized GENCO capital budget of approximately $25 million for calendar year 1998. The GENCO capital budget level agreed to by LIPA for 1998 was developed with consideration of historical spending for recurring items and specific one-time capital projects. The PSA provides for annual review of and approval by LIPA of the capital additions to the GENCO units. RMI expects the capital improvement program and associated budgets to enable GENCO to maintain the capacity ratings and availability of these generating facilities near recent historical levels, however, a slight decline in unit availability may occur as the generating units age.

Environmental Review

RMI's review of the regulatory requirements for GENCO's generating facilities consisted of a review of (i) the list of environmental permits and permit expiration dates provided by LILCO; (ii) key regulatory program compliance; (iii) discussions with state and county regulatory personnel; (iv) notices of violations, fines, and enforcement actions; and (v) LILCO's internal audit reports on environmental compliance. RMI also reviewed existing regulatory programs and requirements as well as programs and requirements that have been promulgated and approved, but not yet implemented. Based on this review, LILCO appears to hold all required environmental permits for its generating facilities and RMI is unaware of any environmental permits that are not held by LILCO and required for the operation of the generating facilities. LILCO appears to be in compliance with the conditions set forth by those permits, except for New York State opacity limits pertaining to the visibility of power plant air emissions. Although LILCO's exceedance of opacity limits ranked as the second lowest in the State during 1996, the latest year for which information is available, the NYSDEC has begun to more aggressively enforce opacity exceedances by all New York State utilities. LILCO is currently in negotiations with NYSDEC to resolve issues concerning its occasional exceedance of mandated opacity limits, which have generally occurred during start-up and shut down of certain generating facilities. LILCO advised RMI that it expected a NYSDEC Consent Order in this matter to

be completed near the end of the first quarter of 1998, but no such Consent Order has been issued as of the date of this Report. LILCO has advised RMI that it does not expect any significant operating limitations or capital expenditures to result from a Consent Order on this matter.

Table 6 provides a comparison of the GENCO facilities' emission levels during 1996, the latest year for which comparative data is available, and the emission levels experienced by the other large electric utilities in the State. Lower emission rates are favorable. As shown in Table 6, the GENCO facilities' emission levels are approximately one-half the average for utilities in New York State.

TABLE 6

COMPARISON OF AIR EMISSION LEVELS FOR 1996(1)
FOSSIL GENERATION UNITS
(Pounds per MWh)

	NOx Emission Rate	SO2 Emission Rate
Rochester Gas & Electric Corporation	4.93	33.52
New York State Electric & Gas Corporation	4.48	8.98
Niagara Mohawk Power Corporation	4.37	28.62
Central Hudson Gas & Electric Corporation	3.97	10.54
Orange & Rockland Utilities Incorporated	3.80	8.49
Consolidated Edison Company of New York	3.67	1.96
New York Power Authority	1.65	1.27
Long Island Lighting Company	**1.58**	**5.32**
New York State Average	3.49	10.73

(1) Most recent year for which data is available.

Fuel Supply

In 1997, approximately 68 percent of the fuel burned for electric generation in GENCO's units came from natural gas, with the balance from residual oil and distillate oils. The Energy Manager will procure fuel needed by GENCO for generation pursuant to the EMA. LIPA will pay directly for fuel purchased for the GENCO facilities. LILCO has historically purchased natural gas for the generating facilities through the spot market or through term contracts that are market price-based. Oil fuels have historically been purchased through contracts that are based on market prices at or near the time of delivery. These practices are expected to be continued by the Energy Manager. Oil fuels will be delivered via ship, barge, or truck, depending on the particular generation site. In 1997, LILCO purchased 53 percent of the natural gas used by the GENCO units on the spot market and 47 percent through term contracts. Thirty-four percent of oil requirements for the GENCO units were purchased from the spot market during 1997 and 66 percent through term contracts.

The particular fuel used for generation will depend on generation plant fuel capability, fuel supply and transportation availability, and fuel cost. Most of the GENCO steam units can burn either natural gas or residual oil, although some of these units may be limited to burning a single type of fuel due to emission constraints. Natural gas or distillate fuel is burned in the gas turbines. Table 7 summarizes historical fuel usage at the GENCO plants.

TABLE 7

HISTORICAL GENERATION FUEL USAGE
PERCENT OF TOTAL ANNUAL USE

Year	Natural Gas	Fuel Oil	
		Residual	Distillate
1993	36.8%	62.1%	1.1%
1994	48.0	50.3	1.7
1995	68.0	30.6	1.4
1996	52.6	45.5	1.9
1997	67.8	30.1	2.1

LIPA's estimated fuel costs for oil and natural gas are based on proprietary fuel price forecasts developed by LILCO for each type of fuel. To assess the reasonableness of LILCO's fuel price projections, RMI calculated the composite weighted average cost of fuel oil and natural gas by year for the Study Period. This average was derived by using a representative fixed weighting of the underlying prices to mitigate the influence of a changing mix of seasonal supplies or other factors. The resulting annual values were compared to assess the composite year-to-year changes in fuel prices. This comparison indicated an initial decline from 1997 price levels during 1998 and 1999 for natural gas, followed by annual increases averaging 2.1 percent per year through 2008. Weighted average oil prices are estimated to increase at approximately 1.5 percent annually. The weighted average prices track well with the expected changes in fuel prices based on an analysis by RMI of data projected by the United States Department of Energy ("DOE")—Energy Information Administration. In addition, the initial decline in gas prices forecast by LILCO is consistent with recent gas market price data that indicates a substantial drop in gas prices during the first quarter of 1998 from 1997 levels.

Gas Supply and Transportation

The deregulation of natural gas production and the partial deregulation of transportation in the United States and Canada have opened competitive markets for gas consumers. Major gas production regions that LIPA can access include the Gulf Coast and the Mid-continent regions in the United States and the province of Alberta in Canada. Gas in these supply regions can be purchased under term contracts, usually at market-based prices, or on the spot market. Numerous interstate pipelines and transCanada pipelines connect the New York-area market to these gas supply regions. Gas storage is available in the producing regions and near the New York market.

LILCO, KeySpan, and Con Edison have entered into the New York Facilities Agreement which provides for the use of their joint systems to allow the three parties to receive gas from interstate pipelines. LILCO shares seven gas delivery interconnections between its gas transmission system and the New York gas market.

Once gas reaches Long Island, it must move across the gas transmission and distribution system to the respective power plants. Pursuant to the Grant of Future Rights set forth in the Agreements, transportation over the on-island gas distribution system will be provided to LIPA on an interruptible basis at a price of $0.19 per million British thermal units ("MMBtu") for a period of 11.5 years. This rate will only be adjusted for capital improvements required to provide this service to LIPA and will be applied to gas transported to the GENCO facilities and to new generating capacity of a size above a minimum level established by LIPA that is constructed by or on behalf of LIPA. Generation plants are the lowest priority on the gas distribution system and these facilities are curtailed first during

supply delivery constraints. During periods of curtailment, most of the GENCO steam units, which comprise the main on-island electric capacity and energy resource, can switch to fuel oil to meet generation needs.

Oil Supply and Transportation

Oil is stored on site or at locations accessible to each GENCO facility. Residual fuel storage totals 2.8 million barrels. Distillate fuel storage capacity totals 277,000 barrels. This storage capacity, plus LILCO's oil management program, has helped LILCO avoid a fuel oil supply disruption. Conversion of additional GENCO units to burn natural gas in the future, if economic, will further reduce exposure to potential fuel oil interruptions.

NINE MILE POINT NUCLEAR POWER STATION, UNIT 2

NMP2 is part of a two-unit nuclear power station located at a 900-acre site on the south shore of Lake Ontario near the town of Scriba, New York. Niagara Mohawk is the operator and majority owner of NMP2. Stone & Webster Engineering Corporation was the architect engineer and constructor of the facility. NMP2 received its operating license from the NRC in July 1987, and initiated commercial operation in April 1988. NMP2's operating license expires in 2026. On January 8, 1998, LILCO obtained approval from the NRC for the indirect transfer of control of its ownership rights in NMP2 to LIPA. NMP2 is the second of two units at the Nine Mile Point Nuclear Power Station (''Nine Mile Point'') site. Unit 1 (''NMP1'') began commercial operation in 1969 and includes an older model reactor than NMP2. NMP1 and NMP2 are operated separately under different ownership interests. LIPA will have no ownership interest in NMP1. The Fitzpatrick Nuclear Power Plant (''Fitzpatrick''), owned and operated by NYPA, is located on a site adjacent to Nine Mile Point.

Description of Facility

NMP2 utilizes a General Electric Company boiling water reactor (''BWR'') and turbine generator. NMP2 was uprated to 1,144 MW of capacity following a turbine rotor replacement in 1995. Currently, NMP2's output is limited to 95 percent of core thermal power due to the unavailability of one of its two moisture separator reheaters. Niagara Mohawk has advised that this equipment is planned to be repaired during the refueling outage scheduled to commence May 2, 1998. NMP2's condenser water is cooled by a natural draft cooling tower, with makeup water from Lake Ontario.

Ownership Structure

NMP2 is owned by five co-tenants, as shown in Table 8, and is operated by Niagara Mohawk.

TABLE 8

OWNERSHIP OF NMP2

Name of Owner	Ownership Interest
Niagara Mohawk Power Corporation	41%
Long Island Lighting Company	18
New York State Electric & Gas Corporation	18
Rochester Gas & Electric Corporation	14
Central Hudson Gas & Electric Corporation	9
Total	100%

Ownership of NMP2 is governed by the Basic Agreement, dated September 22, 1975 (the ''Basic Agreement''), which outlines the participation of the NMP2 owners, including (i) contractual rights and payments for the nuclear site; (ii) Niagara Mohawk's authority with regard to construction of NMP2 and the co-tenants' obligation to reimburse Niagara Mohawk in accordance with their respective percentages; (iii) Niagara Mohawk's responsibility to obtain all permits and licenses; (iv) a construction agreement; and (v) an operating agreement. Additional key provisions of the Basic Agreement include (i) the term of the Basic Agreement, which extends from the date signed until decommissioning, unless termination is unanimously agreed upon by the co-tenants prior to this date; (ii) rights of Niagara Mohawk and the co-tenants with respect to capital improvements, (iii) provisions related to the damage, destruction, or condemnation of the nuclear plant; and (iv) assignment or transfer of a co-tenant's ownership percentage.

A new operating agreement (''NMP2 Operating Agreement'') was executed on December 29, 1992, and will be in effect until decommissioning in 2026, unless terminated with six months notice to all parties. The NMP2 Operating Agreement establishes a framework under which NMP2 will be operated, including (i) operating goals, establishment of a management committee (the ''Management Committee''), and establishment of an on-site owners' representative; (ii) a list of services to be provided by Niagara Mohawk as the operator; (iii) an outline of the co-tenants' responsibilities with regard to payment for operating costs; (iv) a framework for audit committee activities; (v) responsibility for fuel supply; (vi) insurance provisions; and (vii) measurement of NMP2 output.

The NMP2 Operating Agreement establishes provisions for the payment of each co-tenant's share of NMP2 costs and provides for the co-tenants to advance funds to Niagara Mohawk in proportion to their ownership interests in the event of the failure of a co-tenant to cover its share of NMP2 costs. The NMP2 Operating Agreement also provides that the Management Committee must approve annual operating and capital budgets and plans, which include annual operating goals and objectives for NMP2. The Management Committee is comprised of one representative from each co-tenant. Voting of the Management Committee is based on ownership percentage and a simple majority of ownership percentages is required for approval of matters brought before the Management Committee.

On August 28, 1997, NYPA, Con Edison, Niagara Mohawk, and Rochester Gas & Electric Corporation (''RG&E''), the four utilities operating nuclear generating facilities in the State, made a joint announcement that they would move forward with plans to form the New York Nuclear Operating Company (''NYNOC''). NYNOC, a limited liability company, would take over operation of the six nuclear plants (including NMP2) currently operated by these utilities, with the objective of achieving economies of scale and increased cost effectiveness. As presently envisioned, the plants would continue to be owned, and the output of the plants marketed, by the respective owners of the plants. It is contemplated that NYNOC would obtain the NRC operating licenses for the plants, while other aspects of the NRC licenses would remain with the plant owners.

The NMP2 Management Committee has taken a position in favor of supporting NYNOC and has budgeted funds to assist in the development of the concept. LIPA, as a member of the Management Committee, will have input into future NMP2 decisions regarding NYNOC.

Historical Unit Performance Levels

Over the past five years, NMP2 has generally exceeded average industry performance for annual capacity factors. Table 9 sets forth annual capacity factors and generation levels attributable to

LILCO's 18 percent share of NMP2 for the period 1993 through 1997. This table also presents comparative industry data for similar nuclear generating units.

TABLE 9

HISTORICAL NMP2 PERFORMANCE

Calendar Year	NMP2 Annual Net Generation (MWh)(1)	NMP2 Annual Net Capacity Factor(2)	NMP2 Three-Year Average Net Capacity Factor(3)	Industry Average Net Capacity Factor(4)
1993	1,294,794	78.4%	67.2%	74.6%
1994	1,504,065	90.8%	74.4%	77.9%
1995	1,305,662	76.5%	81.9%	79.6%
1996(5)	1,565,731	87.1%	84.8%	79.5%
1997	1,598,046	89.2%	84.3%	(6)

(1) LILCO's 18 percent share of total NMP2 output.
(2) Net capacity factor is a measure of the utilization of the NMP2's theoretical maximum annual output.
(3) The three-year average smooths the effects of refueling outages.
(4) Based on nuclear generating units with BWRs, as reported by the North American Electric Reliability Council.
(5) In 1995, the design electrical rating of NMP2 was increased from 1,062 MW to 1,144 MW.
(6) Industry data for 1997 is not available at the time of this Report.

NMP2's historical operating results have been favorable when compared to the average fuel and non-fuel operation and maintenance costs of other nuclear plants of similar design and vintage. Table 10 provides a comparison of this data for 1996, the latest year for which data is available. Nuclear plants shown in Table 10 were selected by identifying all plants with BWR's in the United States and narrowing the list to those plants with comparable capacity ratings and construction timeframes. Using this criteria, ten plants were selected for benchmarking against NMP2.

TABLE 10

COMPARATIVE NUCLEAR PLANT OPERATING STATISTICS 1996 RESULTS(1)

Facility	Production Cost ($/MWh)(2)	Fuel Cost ($/MWh)(3)	Capacity Factor (%)(3)
Limerick	14.14	4.53	86.81
Grand Gulf	15.37	5.27	89.07
NMP2	**15.85**	**5.26**	**87.10**
Susquehanna	16.22	5.59	87.99
Hope Creek	23.24	NDA	71.48
River Bend	23.76	6.54	83.23
Perry	26.42	9.63	71.10
Clinton	26.80	8.67	63.78
LaSalle	29.11	5.56	46.91
WNP-2	31.45	4.85	79.22
Fermi	36.67	12.34	61.73
Average (excluding NMP2)	24.32	7.00	82.81

(1) Most recent year for which data is available.
(2) Source: Utility Data Institute and *Inside NRC*. Excludes fuel costs.
(3) Source: *Nuclear Fuel*, JUNE 16, 1997.

Nuclear Fuel Supply and Disposal

NMP2 has a contract with US Enrichment Corporation for nuclear fuel enrichment services and for all or part of NMP2's enriched product needs to 2002. The NMP2 Fuel Committee, comprised of one representative from each co-tenant, has made the decision to use the spot market for the balance of future uranium and enrichment requirements beyond that covered by this contract. General Electric Company is under contract to supply fuel fabrication, core design, licensing, and core management services to 2006. Currently, there are three vendors offering fuel fabrication services to nuclear facilities with BWRs.

NMP2 undergoes periodic outages for refueling. Operating cycles, inclusive of refueling outages, are being lengthened to 24 months to improve overall NMP2 capacity factors. In addition to longer periods between refueling, NMP2 has demonstrated shorter refueling outage durations. Refueling outages are used to perform a major portion of NMP2's repairs and maintenance as well as refuel the reactor. Planned and actual outage times have decreased due to better outage management and fewer emergent problems. Shorter outage duration also tends to improve NMP2's capacity factor.

The NMP2 reactor core consists of 764 fuel assemblies. At each refueling outage, about a third of the oldest fuel assembles are replaced with fresh assemblies. The used assemblies are stored in the spent fuel pool adjacent to the reactor. Space must always be reserved in the pool to receive the off-loading of all assemblies in the core. The NMP2 spent fuel pool has a design capacity of 4,049 fuel assemblies. Storage racks for about one-half of this total are currently installed. The balance is scheduled to be installed in 2001. Currently, there are 1,128 fuel assemblies in the pool. Based on the planned 24-month operating cycle, NMP2 can operate into 2012 with existing and planned spent fuel racks.

Niagara Mohawk, along with all other nuclear utilities in the United States, executed a contract for disposal of spent nuclear fuel and/or high-level radioactive waste with the United States government in 1985. This contract required DOE to take title to and dispose of all spent nuclear fuel and high level waste of United States origin for civilian nuclear power reactors. For this service, NMP2's owners pay a fee of 1.0 mill per kilowatt hour (''kWh'') for all electricity generated by NMP2, less an amount to account for transmission losses. DOE was obligated to begin accepting fuel in 1998, but has failed to meet this commitment. Niagara Mohawk has joined other utilities in litigation over this contract as well as litigation to escrow the disposal fees.

The United States Court of Appeals ruled on November 14, 1997, that DOE had an unconditional obligation under the Nuclear Waste Policy Act of 1982 to begin disposal of used nuclear fuel. Despite this ruling, DOE maintains it will be unable to fulfill its obligation. On February 19, 1998, 41 utilities filed a petition in federal court requesting the court to order DOE to develop a program to accept and dispose of spent nuclear fuel beginning immediately. Separate legislation has passed each house of the United States Congress that mandates DOE build an interim central spent fuel storage facility, with operations to begin in 2002. A conference committee is expected to resolve differences in the two bills in early 1998. This legislation may provide a means for off-site disposal of NMP2's spent fuel.

The decommissioning cost estimate prepared on behalf of Niagara Mohawk for NMP2 in October 1995 includes an allowance for funds sufficient to construct and operate a dry waste fuel storage facility on site at NMP2. This cost estimate assumes that DOE will begin to accept NMP2 spent fuel during 2020 and that all NMP2 spent fuel will be accepted by DOE by the end of 2044.

Low-Level Radioactive Waste

The federal Low-Level Radioactive Waste Policy Act, as amended in 1985, requires states to join compacts or to individually develop their own low-level radioactive waste disposal site. In response to federal law New York State decided to develop its own low-level radioactive waste disposal site because of the large volume of waste generated in the State. The State expected this disposal facility to begin operation in 2001, although it does not appear likely a disposal facility will be available by this date, nor is it likely such a disposal facility will be available by the end of the Study Period.

Niagara Mohawk currently ships low-level radioactive waste generated at NMP2 to a disposal facility in Barnwell, South Carolina. During the period July 1, 1994 to June 30, 1995, the legislature of South Carolina denied access to the facility to out-of-region low-level radioactive waste generators, including New York State. RMI cannot predict whether the Barnwell facility will be closed again at some future date to out-of-region low-level radioactive waste generators before the New York State disposal facility becomes available.

Management and Oversight

Under the MSA, the Manager, at the direction of LIPA, is responsible for the administration and management of LIPA's interest in NMP2, including participation in meetings of the joint owners of NMP2. Historically, LILCO has staffed a NMP2 Oversight Division, comprised of five individuals whose purpose is to maintain knowledge of NMP2, the applicable regulatory requirements, its performance status, and its costs. This division coordinates timely support for all LILCO activities relating to NMP2 and works with the co-tenants to reduce NMP2 costs. After the Closing, this same staff will be employed by the Manager and will continue to perform this function in accordance with the provisions of the MSA, under the strategic and policy direction of LIPA. LIPA will designate an employee or outside advisor to work with the Manager's staff on NMP2 matters.

The NMP2 Operating Agreement provides for the retention of a person or organization to monitor activities related to NMP2 on behalf of the non-operating co-tenants and to provide assessments related to these activities. The non-operating co-tenants have retained MATS Incorporated (''MATS'') to perform these functions on their behalf. MATS is comprised of 10 individuals with technical and financial backgrounds located on-site at NMP2. MATS' responsibilities include (i) coordination of the on-site activities of the employees and agents of the non-operating co-tenants; (ii) representation, as appropriate, of the non-operating co-tenants' interests to Niagara Mohawk management and Niagara Mohawk operational managers; and (iii) communication of observations and assessments concerning the operation and maintenance of NMP2 to Niagara Mohawk. MATS may also serve as the non-operating co-tenants' representative on operation and maintenance committees and task forces established from time-to-time to inquire into issues related to the operation or performance of NMP2.

Niagara Mohawk prepares a capital and operating budget each year which is submitted to the Management Committee for review and approval. Niagara Mohawk has override authority over the Management Committee on capital expenditures it believes are required to meet regulatory and safety requirements. Cash calls are issued monthly to the co-tenants requesting weekly funding for the NMP2 ''Operations Account.'' In the event that any party fails to advance funds owed, all co-tenants are required to advance funds in proportion to their percentage ownership interest to cover the shortfall for up to three months. Longer term remedies to address the default of a party are handled by a meeting of the co-tenants. RMI is not aware of any instances of a NMP2 co-tenant not advancing funds when required by Niagara Mohawk.

Plant Operations

NMP2's physical condition is extensively monitored by Niagara Mohawk programs that are, in turn, monitored by the NRC. NMP2 maintenance practices and status are reviewed by the NRC as part of its inspection process. Ratings issued by the NRC, called Systematic Assessment of License Performance (''SALP''), are assessed by plant site, rather than individual unit, and constitute an assessment of operations, maintenance, plant support, and engineering functions at NMP1 and NMP2 combined.

Prior to 1993, Nine Mile Point was on the NRC ''Watch List'' for troubled plants. As shown in Table 11, Nine Mile Point has demonstrated an improving trend in SALP ratings until 1997. The decline in SALP rating for plant operations during 1997 appears to be attributable to a reactor overfill event at NMP1. Engineering also had problems solving certain technical issues with a motor operated valve program. Niagara Mohawk has reorganized its Nine Mile Point senior management positions to better address the deficiencies in the engineering area, and improvement in the SALP rating is a key goal in the 1998 business plan of Niagara Mohawk.

TABLE 11

NINE MILE POINT SALP RATINGS(1)

Year	Plant Operations	Engineering	Maintenance	Plant Support
1989	3	3	3	2
1990	3	3	3	2
1991	2	2	2	2
1992	2	2	2	2
1993	2	2	2	2
1995	1	2	2	2
1996	1	2	2	2
1997	2	2	2	2

(1) The NRC's rating system assigns a ''1'' for superior performance, a ''2'' for good performance, and a ''3'' for adequate performance. Ratings prior to 1993 were based on slightly different categories.

As noted in Table 11 above, Nine Mile Point received a rating of 2 in all four categories examined by the NRC. Nine Mile Point's SALP rating is viewed as an acceptable level of performance by the NRC.

The nuclear industry has an on-going program to identify and address safety issues that impact reactors with common designs. The NRC has issued ''generic issue letters'' to nuclear plant owners advising them of prospective safety issues and the measures that can be taken to mitigate or correct these problems. Niagara Mohawk has received generic issue letters related to potential safety issues at NMP2 and has formulated formal action plans for each of these letters. Activities identified in these action plans have been scheduled by Niagara Mohawk and are on track for completion.

One of the generic issues facing nuclear plants with BWRs, such as NMP2, involves the cracking of internal components of the reactor after about 10 years of operation. The cracking process proceeds slowly at a predictable rate, making the issue one of cost of inspection and repair, or replacement. Industry research has shown that the addition of hydrogen to the BWR feedwater can be expected to reduce stress corrosion cracking, which is the mechanism that has been determined to cause the

cracking problem. There has been no cracking observed at NMP2 through the end of March 1998 and Niagara Mohawk will be conducting reactor internal inspections during the May 1998 refueling outage. Approximately one-half of the world's BWR plant owners have committed to hydrogen water chemistry in an effort to prevent or mitigate this cracking problem. Niagara Mohawk has budgeted for, and is in the process of installing, hydrogen injection equipment at NMP2. The final effectiveness of this approach will only be known as BWRs go through future cycles of operation using this process.

Environmental Review

The list of environmental and regulatory permits required for the operation of NMP2, as provided by MATS and compared against the list contained in the Basic Agreement, was reviewed by RMI and found to be current. In addition, no significant environmental issues associated with the operation of NMP2 were discovered by RMI. RMI has commissioned, via subcontract, a Phase 1 review of the NMP2 property in accordance with standards established by the American Society for Testing and Materials. This review will assist in evaluating potential liabilities associated with the NMP2 property. While the review is ongoing, it is substantially complete and, as of the date of this Report, has not revealed any indications of environmental contamination at the NMP2 site.

During November 1997, Niagara Mohawk was awarded an International Standards Organization 14001 certificate. This certificate was issued in recognition of the conformance of Nine Mile Point's environmental management systems to the principals, policies, and procedures for corporate-wide environmental management established by the International Standards Organization. Nine Mile Point is the first nuclear generating facility in the United States to obtain this certification.

Capital Expenditures

During the last five years, LILCO's share of capital expenditures at NMP2 have averaged approximately $9.4 million per year for plant modifications and nuclear fuel. Table 12 provides a summary of LILCO's share of historical NMP2 capital expenditures during the 1993 through 1997 period.

TABLE 12

HISTORICAL NMP2 CAPITAL EXPENDITURES
LILCO'S 18 PERCENT SHARE
($000)

Year	Plant Modifications	Nuclear Fuel(1)	Total NMP2 Capital Expenditures
1993	$7,857	$5,615	$13,472
1994	5,919	7,164	13,083
1995	4,134	1,224	5,358
1996	3,785	8,895	12,680
1997	1,908	681	2,589

(1) Capital cost of nuclear fuel purchased during the year. Nuclear fuel expenditures are capitalized by LILCO and then expensed based on actual generation levels at NMP2.

LIPA's 18 percent share of NMP2's calendar year 1998 capital budget approximates $3.3 million for plant modifications and $10.5 million for nuclear fuel. Beginning in 1999, Niagara Mohawk expects the amount for plant modifications to decrease to approximately $1.8 million annually for LIPA's 18 percent share, due in part to the completion of NMP2's 1998 refueling cycle,

during which time major maintenance will be performed. The capital budget is expected to remain at generally this level through the remainder of the Study Period. This estimate reflects the recent downward trend in NMP2's capital expenditures and does not anticipate any new generic issues of significance that would materially impact capital expenditures. If new generic issues do arise for NMP2, or if NRC regulation intensifies, capital expenditures could be higher. Annual expenditures for nuclear fuel are estimated to average $5.7 million during the 1999 through 2008 period, reflecting the two year cycle between refueling periods. Estimated annual capital expenditures for LIPA's share of NMP2 are reflected in Exhibit 3, ''FINANCING REQUIREMENTS—Capital Expenditures,'' of this Report.

Decommissioning

The co-tenants expect to commence the decommissioning of NMP2 shortly after the planned cessation of operations in 2026. LIPA's share of the decommissioning costs, based on a site specific study conducted in 1995 by ABZ Inc. (''ABZ''), is estimated to be $145 million in 1996 dollars, or $407 million in 2026 dollars. ABZ is a nationally known engineering and consulting organization with extensive experience in the evaluation of nuclear power plant decommissioning alternatives and associated costs.

ABZ assumed a ''DECON'' method of decommissioning for NMP2 based upon current technology. This method provides for removal or decontamination of all equipment and structures necessary to permit release of the site property for unrestricted use. This is the method that was used for the completed decommissioning of the Fort St. Vrain nuclear facility in Colorado and for Shoreham. The actual costs incurred for the decommissioning of these plants were taken into account by ABZ in preparing its estimate for NMP2.

As noted earlier, it is anticipated that all spent fuel will be kept on site in dry storage until the year 2020, with annual transfers to an off-site DOE-administered waste disposal facility thereafter. ABZ's decommissioning cost estimate includes an allowance for annual on-site storage costs, waste transportation costs, and waste disposal costs at this DOE facility from 2020 through 2044, at which time all waste is expected to have been transferred to the DOE facility. Upon Closing, LIPA will gain title to LILCO's external trust fund for the decommissioning of the contaminated portion of NMP2. LIPA will also fund a separate decommissioning fund for the non-contaminated portion of NMP2. The balance in LILCO's external trust fund as of December 31, 1997 was approximately $17.7 million. LIPA has determined that an annual contribution of approximately $3.0 million will be required to fully fund the external trust fund by 2026 relative to its 18 percent share of NMP2 decommissioning costs. Total costs in 1996 dollars for decommissioning the contaminated portion of NMP2 are estimated to be $111 million. LIPA will establish an internal reserve fund to cover the non-radioactive decommissioning costs. LIPA has determined that an annual deposit of approximately $1.2 million will be necessary to fully fund LIPA's 18 percent share of the decommissioning of the non-contaminated portion of NMP2. The total estimated cost of LIPA's 18 percent share of NMP2's non-radioactive decommissioning costs in 1996 dollars is approximately $34 million.

SYSTEM LOADS AND RESOURCES

System Capacity and Energy Requirements

Electricity usage patterns and seasonal weather conditions in the Service Area result in maximum electrical demand during the summer season and relatively low load factors on an annual basis. Exhibit

6 sets forth historical annual peak demands and energy requirements for the period 1993 through 1997. Annual system load factors during this period ranged from 47.4 percent to 54.2 percent due, in large part, to variations in seasonal weather conditions.

LIPA's estimated peak demand and energy requirements for the Study Period are set forth in Exhibits 7 and 8. Peak demand growth is expected to range between 0.4 percent and 1.3 percent annually, averaging 0.9 percent over the 1998 to 2008 period. This growth rate would increase the summer peak demand from approximately 4,100 MW in 1998, net of the effects of DSM, to almost 4,500 MW in 2008. The projected growth rate is consistent with the historical demands that grew at an annual average rate of 1.1 percent from 1993 through 1997. Energy growth is estimated to range between 1 percent and 1.8 percent annually, averaging 1.3 percent over the same period. This projected rate of growth in energy compares to a modest annual increase in energy sales from 1993 through 1997. These projections of annual demand and energy requirements reflect the estimated impacts of the substantial rate reductions that LIPA will implement. Cumulatively, the price elasticity effect of these rate reductions (i.e. the change in consumption of energy resulting solely from the rate reductions) is estimated to add approximately 75 MW and 580 MWh in incremental demand and energy requirements, respectively, in 2008, the last year of the Study Period. Over the Study Period, annual residential sales are estimated to grow by approximately 1.2 percent and annual commercial energy sales approximately 1.5 percent.

Estimated demand and energy requirements take into account the effects of economic development power provided directly by NYPA and by NYPA through SCEA and NCPUA. Economic development power from NYPA is expected to remain constant over the next ten years due to the limited supply of inexpensive power available to NYPA that can be used to support economic development and limitations on available electric transmission import capacity. Please see the section entitled ''SECURITY OF CUSTOMER REVENUE—Long Island Electrical Agencies'' in this Report for a discussion of other matters related to SCEA and NCPUA.

Conservation Program Impacts

LIPA's estimate of annual demand and energy requirements takes into account the on-going effect of DSM programs expected to be implemented by LIPA from 1998 to 2008. During 1998, estimated peak demand reductions resulting from measures undertaken during 1998 are expected to be 28 MW. DSM reductions during the Study Period are estimated to increase to 181 MW by 2003 and decrease to 175 MW by 2008. Reductions in annual DSM savings result from the decreasing effectiveness of DSM measures installed during the 1998 through 2002 period. After 2002, DSM measures are expected to consist of peak load reduction programs which do not experience a deterioration in demand savings, except through the loss of participating customers. Further additions to the DSM measures will depend on the results of LIPA's Clean Energy Program, as described below, to be developed and implemented after the Closing.

In 1998, energy reductions from 1998 DSM programs are expected to be 11,000 MWh. Cumulative energy reductions from DSM programs installed starting in 1998 are expected to increase to 83,000 MWh in 2003 and decline to 62,000 MWh by 2008.

Estimated demand and energy savings from DSM are based on programs which target the following areas.

1. **General Residential and Commercial/Industrial Programs**—Assistance to customers to improve energy efficiency and lower electric bills, including energy audits, financial incentives, and efficiency improvement programs.

2. **Business Development Programs**—Assistance for businesses to invest in energy efficiency as a means to remain in, expand in, or relocate to the Service Area, and to residential customers to retain them as electric heat customers.

3. **Energy-Efficient Load Growth Programs**—Identification, evaluation, and promotion of energy efficient electric technologies, including education programs, outdoor security lighting fixtures, and electric vehicles.

4. **Peak Demand Reduction Programs**—Incentive payments to large commercial and industrial customers in exchange for them reducing their electric loads by a specified amount when requested or needed by LILCO.

5. **Low-Income Programs**—Joint efforts with local and State agencies for energy efficiency education, weatherization, and direct installation of energy-efficient refrigerators and fluorescent lighting.

Following the Closing, LIPA is expected to implement a "Clean Energy Program" consistent with a Clean Energy Policy Statement adopted by the Board in March 1998. Under this program, LIPA proposes to promote energy efficiency, renewable energy, and other efficient and environmentally preferred energy generation technologies. The objective of the Clean Energy Program is to support the development of energy efficiency and clean energy generation markets within the Service Area. To implement this program, LIPA has indicated its intent to establish a "Clean Energy Fund" and a "Clean Energy Advisory Panel." LIPA will establish a Clean Energy Fund with an initial balance of $32 million to support energy efficiency programs, cost-effective distributed generation, and renewable energy resource technologies, including the DSM programs listed above.

LIPA has proposed to work with a Clean Energy Advisory Panel to recommend, for consideration by the LIPA Board, a long-term funding mechanism for a Clean Energy Fund beyond the $32 million to be funded by LIPA in its first year of operation. With input from the Clean Energy Advisory Panel, LIPA will design specific programs to support energy efficiency and clean generation technologies. The programs are expected to include a combination of research and development, customer education, administration, and support for the Clean Energy Advisory Panel, and funding in support of the commercialization of preferred clean energy generation technologies.

In the projected Operating Results presented in this Report, the Clean Energy Fund provides funds for approximately $11 million in energy efficiency and load control in the first year of operations, increasing to approximately $17 million annually by the year 2002. The remainder of the $32 million in funds for the first year will be applied as determined by the Board, with input from the Clean Energy Advisory Panel.

Cogeneration Loads

Estimated demand and energy requirements for the Study Period reflect the effects of cogeneration currently installed by certain customers. Cogeneration is estimated to result in customer load reductions of approximately 90 MW and 464,000 MWh during 1998, increasing to 102 MW and 535,000 MWh by 2008. Cogeneration, which is used in whole or in part to directly serve customer loads, is distinguished from independent power producer ("IPP") facilities, which sell their output to LIPA as a supply resource.

System Import Constraints

Maximum import capability into the Service Area is nominally rated at 1,050 MW under typical conditions. This capability varies depending on electrical loads within and outside the Service Area and the availability of generating units and transmission capacity. The five major transmission lines which connect the T&D System with the Con Edison and NYPA systems to the west and with southern Connecticut to the north are shown on the map following Part 1 of the Official Statement.

The net import capability of the T&D System is derived by taking the total capability of the transmission lines and subtracting (i) the capability that is used to export power for Con Ed; and (ii) the capability owned by Con Ed which is used to import power. The 1,050 MW of typical import capability also takes into account the portion of the Northport to Norwalk Harbor line that can not be used for imports when the Northport and Norwalk Harbor generating units are operating and the portion of line capability that is reserved for emergency operations in order to maintain T&D System reliability.

LIPA has issued a request for proposals (the "Transmission RFP") to evaluate the feasibility of adding a new transmission interconnection to the Service Area. The availability of an additional interconnection would increase the maximum import capability to the Service Area and provide LIPA with access to additional power supply resources as well as promote increased competition between power sources within and outside its Service Area. Under the terms of the Transmission RFP, LIPA may authorize the successful proposer to proceed with the construction of an additional interconnection if LIPA considers it economically and environmentally desirable. LIPA has received three qualified responses to the Transmission RFP and expects to complete its review of these responses and select an evaluation contractor in May 1998. Neither the cost of additional off-island transmission interconnections nor potential savings in power supply costs from an additional interconnection are included in the projected Operating Results presented in this Report.

Existing Capacity and Energy Resources

LIPA is expected to rely on existing power supply resources, including the GENCO facilities and its share of NMP2, to meet the bulk of its capacity and energy requirements during the Study Period. Exhibit 6 of this Report sets forth the historical annual contribution of the GENCO facilities and NMP2 to the Service Area's capacity and energy requirements during the 1993 through 1997 period. Exhibit 9 provides additional information on the historical operating performance of the GENCO facilities. During the Study Period, NMP2 and the GENCO facilities are expected to be operated in a manner consistent with their historical operations.

In addition to NMP2 and the GENCO facilities, LIPA is expected to rely on existing power purchase agreements and other resources to meet its annual capacity and energy requirements. The Service Area's historical reliance on these resources is shown in Exhibit 10. Presented below is a description of LIPA's expected use of these resources during the Study Period.

New York Power Authority FitzPatrick and Gilboa Capacity

LIPA is expected to purchase 160 MW of summer peak capacity from NYPA's Fitzpatrick nuclear plant and receive an additional 25 MW of reserve credit from NYPA. LIPA is also expected to purchase 50 MW of capacity from NYPA's Blenheim-Gilboa pumped storage facility. These purchases are expected to continue throughout the Study Period.

Non-Dispatchable On-Island Independent Power Producers

LIPA is expected to purchase approximately 210 MW of summer peak capacity and associated energy from IPPs within the Service Area. These IPPs are mostly resource recovery or landfill gas facilities, are under contract at relatively high power purchase rates, and are not subject to dispatch or control by LIPA. The IPPs are assumed to operate through their contract expiration dates, which are set forth in Exhibit 10. These non-dispatchable resources represent less than five percent of LIPA's total capacity and can be readily accommodated in LIPA's total resource operations. In addition to the above, LIPA is expected to continue to purchase energy, without firm capacity, from a cogeneration facility at the State University of New York ("SUNY") at Stony Brook.

New York Power Authority, Richard M. Flynn Plant

LIPA is expected to continue to purchase the full 138 MW summer peak capability of NYPA's Richard M. Flynn ("Flynn") plant located in Holtsville, Suffolk County, New York. The Flynn plant is a combined cycle facility completed in May 1994, in response to a competitive bidding program by LILCO. LILCO has entered into a contract with NYPA which guarantees LILCO that the plant will have an overall equivalent availability of at least 90.42 percent and a minimum availability during LILCO's summer peak load periods of 90 percent. Actual plant availability above or below these levels results in an increase or decrease, respectively, in LILCO's fixed payments to NYPA for the Flynn plant. Unlike the other IPP contracts, NYPA's Flynn plant may be dispatched to meet least-cost system operation. The contract for this facility extends until 2014.

Purchases from On-Island Municipal Utilities

LIPA is expected to continue to purchase a total of 34 MW of summer peak capacity and associated energy from three municipal utilities within the Service Area. This capacity will typically be held as reserves and therefore only negligible amounts of energy are anticipated to be purchased under these contracts.

Firm Capacity Purchases

Firm capacity purchases during 1998 are expected to consist of a 100 MW summer capacity purchase commitment from an off-island supplier. Similar firm capacity purchases are anticipated throughout the Study Period.

NYPA Power for Jobs Program

NYPA's Power for Jobs is a program sponsored by the State that allocates a portion of the power from NYPA's Fitzpatrick nuclear facility and from competitively bid sources to specific qualified customers to promote job growth, job retention, and economic development. Program power is sold to the utilities serving the eligible recipients pursuant to sale for resale agreements at rates which reflect the cost of power to NYPA, plus a charge for transmission service. Under the present terms of the NYPA Power for Jobs program, LIPA will resell this power to the eligible recipients at the rates charged by NYPA, plus LIPA's applicable transmission and distribution charges, under three-year contracts.

Economy Energy

In addition to the above agreements, LIPA is expected to purchase economy energy from utilities outside of the Service Area. These purchases are made when the price of energy from these suppliers

falls below the incremental cost of generation from GENCO's electric generating facilities. During 1997, approximately nine percent of the Service Area's energy requirements were obtained through economy energy purchases.

LIPA's economy energy purchases are expected to be made through NYPP. NYPP is a tightly coordinated and centrally dispatched pool that matches regional loads with the least expensive statewide generating units available to meet those loads, subject to transmission constraints. Utilities participating in the economy interchange agreement currently split the difference between the marginal cost of producing power for the higher and lower cost utilities, with a share going to NYPP for operations. Generation within the Service Area is reduced when off-island economy power is available at a lower cost through NYPP.

System Energy and Capacity Resources and Requirements

The Service Area's historical capacity resources and requirements are set forth in Exhibit 6 of this Report. During the 1993 through 1997 period, over 90 percent of annual peak capacity requirements were supplied from resources within the Service Area, including existing GENCO capacity, non-dispatchable IPP capacity, and NYPA Flynn capacity. LILCO's total reserve margins during this five-year period ranged from a high of 35.5 percent to a low of 18.4 percent, primarily as a result of the impact of seasonal weather variations on annual peak demands.

The Service Area's historical annual energy balance is set forth in Exhibit 6. While power supply resources outside the Service Area accounted for less than 10 percent of total capacity resources, these resources have historically provided approximately 30 to 40 percent of total annual energy resources, due in part to economy energy purchased from NYPP and nuclear generation.

Historically, resource planning has been performed by LILCO using generation production models to compare existing power supply resources owned and under contract to the forecasted needs of LILCO's customers, including consideration of energy efficiency and DSM programs in place or proposed. LIPA is expected to employ a similar planning process, with new resource needs in the future expected to be sought through either negotiated arrangements or competitive solicitations in amounts to meet incremental system requirements.

Considering the restructuring of the utility industry and LIPA's retail choice program, discussed under "INDUSTRY RESTRUCTURING ISSUES" later in this Report, the power supply market will increasingly dictate decisions on resource additions to meet the needs of LIPA's customers. In the future it will likely be private developers, and their expectations of how the market will develop, who will determine the size, type, timing, and location of new generating facilities.

One of the factors that will influence the development of new generating facilities will be access to and use of local and State-wide electric transmission facilities. As described below, proposed changes to the operation and use of the New York State transmission system have been presented to FERC which could influence the development of new power supply resources.

Independent System Operator

Pursuant to FERC Order No. 888, applicable to, among others, the seven investor-owned electric utilities in New York, including LILCO, (the "IOUs"), which, along with NYPA, comprise NYPP, the IOUs and NYPA undertook development of an arrangement for providing non-discriminatory open-access transmission over all of the electric transmission lines in New York State. As a result of

this effort, the IOUs and NYPA (together, the "Participants") filed a proposal (as most recently revised in December 1997, the "Proposal") with FERC to provide open access to their transmission lines. Under the Proposal, the Participants would form a not-for-profit independent system operator (the "ISO"), which would have responsibility for the operation of most of the transmission lines of the Participants. The ISO would be responsible for scheduling the use of the lines by the Participants and others that wished to use the lines for transmission of electricity and would be responsible for collecting fees from transmission customers. Each Participant would retain ownership, and would be responsible for maintenance, of their respective transmission lines. The customers of the ISO, including the Participants, would pay fees to the ISO based on their usage of the transmission facilities.

A significant feature of the ISO's proposed tariff is its use of a flexible schedule of transmission rates to take account of the cost of energy at its destination along the transmission network in meeting competing demands for the transmission facilities subject to the ISO's jurisdiction. This pricing structure is expected to facilitate competition in the wholesale market for electric energy and reflect the economic cost of transmission congestion. Eventually this structure should provide an incentive to locate new generation facilities in areas where the local price of energy is high or to transmit energy from those areas where the local price is low. The relative value of various generation facilities may be modified as a result.

Under the Proposal, the Participants would initially be the only members of the ISO, but any "market participant" (which would include any person engaged in the wholesale sale, transmission, or purchase of electric energy) would be eligible to join. The ISO would be governed by a Board of Directors consisting of the Executive Director of the ISO and nine individuals selected by a Selection Committee composed of representatives of the other interested parties, and the NYPSC. The Executive Director of the ISO would be chosen by the other nine directors and would be responsible for the day-to-day operation of the ISO.

The Participants had requested FERC approval of the Proposal by no later than March 31, 1998, which would have allowed the ISO to commence operation by June 30, 1998. As of the date of this Report, FERC action on this proposal is pending.

Resource Evaluation

LIPA intends to encourage the development of all economical power supply options for the Service Area as a means of lowering the cost of electricity to its customers. An example of this effort is LIPA's program to assess the economic and technical feasibility of developing additional transmission interconnection capability to allow its customers to access other power supply markets. LIPA initiated this process in January 1998 with the issuance of the Transmission RFP for the evaluation and possible development of an additional transmission interconnection. This evaluation is scheduled to be completed in early 1999 to enable LIPA and its retail customers to comparatively evaluate power supplies outside of and within the Service Area.

The load forecast for the Service Area indicates a need for approximately 150 MW for the 1999 summer peak period. LILCO retains the responsibility for the need for new power resources until the Closing. LILCO has cooperated with LIPA in planning for the solicitation of this summer peak capacity.

LIPA has committed to the development of a retail choice program for its customers. The initial phase of this program is scheduled to begin in 1999, whereby customers may elect to receive their power from power suppliers other than LIPA. The initial program will be limited to an aggregate load

of 100 MW. Subsequently, the program will be ramped up to provide open access for all customers. Please see "INDUSTRY RESTRUCTURING ISSUES—LIPA's Plan for Retail Choice" in this Report for additional information on LIPA's retail choice program.

Until the retail choice program is implemented and a competitive power supply market has been firmly established, LIPA will rely upon traditional generation planning models to estimate the costs and performance of new supplies of capacity and energy to meet LIPA's future needs. For purposes of this Report, LIPA's power supply needs for the Study Period have been assessed based upon least-cost generation modeling to simulate operation of the NYPP and the power supply market within the Service Area.

As an indicator of the performance and cost of new power supply resources, several typical industry-standard and prototype technologies were considered by LIPA in the resource planning model, including gas turbine and combined cycle generating units and upgrades to existing GENCO generating units. The results of the resource planning analysis indicate that firm purchases from off-island sources of between 150 and 200 MW are expected until 2008, when these purchases drop to 50 MW. The capacity payments for these contracts are expected to be less expensive than the cost of building new combustion turbine capacity and therefore provide a lower cost alternative for meeting reserve requirements. Firm purchase contracts are limited to about 200 MW by transmission constraints. By the year 2008, the cost savings from firm purchase contracts are expected to decline as transmission costs increase due to an anticipated new State-wide transmission system structure and the tightening of the off-island capacity market.

Since import capability will be limited, it is expected that new capacity resources within the Service Area will be needed as early as 2003. The summer peak capability of new generation capacity additions are expected to be 144 MW from gas-fired combustion turbines added in 2003 and again in 2005, and 219 MW from gas-fired combined cycle capacity added in 2008. LIPA is assumed to be indifferent to the ownership of the new capacity and is expected to pay comparable rates for the capacity and energy produced by the units regardless of ownership, since it is assumed that market forces will keep this power competitively priced. The marketplace is likely to build at least as much capacity as is needed. Should market participants build more capacity than is needed, prices will decline as wholesale energy prices drop due to the increased competition for limited power sales.

The costs associated with incremental capacity additions, DSM program savings, firm power purchase contracts, NMP2, purchases under the PSA and EMA, and economy energy purchases were modeled as an estimate of the future results of the competitive power supply market. The results of this model are reflected in the fuel and purchased power cost projections contained in the estimated Operating Results shown in Exhibit 1 of this Report.

INDUSTRY RESTRUCTURING ISSUES

Competition is rapidly being introduced to the electric utility industry and New York is one of the states leading the nation in making the transition to a more competitive environment for electric utility service. While there are opportunities to introduce competition through the outsourcing of some administrative and other miscellaneous services, the primary focus in electric industry competition is power supply.

LIPA has indicated in documents pertaining to the acquisition of LILCO its intent to promote power supply competition within the Service Area. Consistent with this policy, LIPA contemplates promoting power supply competition at both the wholesale and retail levels. One objective of this policy is to transition to a structure where LIPA is indifferent as to who supplies power to its customers. Although LIPA will always remain the power supplier of last resort, it intends to implement

a program that will enable its customers to choose from alternative sources of power supply and that will encourage the participation of a diversified mix of new power suppliers within the Service Area. LIPA's program for retail choice is described below.

Retail Choice

Retail choice (sometimes called customer choice, retail wheeling, or retail open access) refers to a process by which retail customers choose among competitive suppliers for electric capacity, energy, and ancillary services. The delivery of capacity and energy is provided by the owner and operator of the local transmission and distribution system. Thus, the traditional vertically integrated electric business is unbundled into distinct power supply and electric transmission and distribution functions.

Utilities in the United States are beginning to adopt retail choice as a natural extension of wholesale market competition. Key issues, among many, that have surfaced in the movement to retail choice are the level of rate reductions, recovery of stranded investments, and the timetable for implementation of retail choice. In addition, the advent of market mechanisms, such as transmission ISOs and the creation of power exchanges, have been the subject of debate in most instances.

The issue of stranded cost recovery is of particular importance in conjunction with the movement to retail choice. Simply speaking, ''stranded costs'' include the costs of existing generation facilities and power supply contracts that are in excess of their market value. The market value of existing generating facilities is largely a function of the availability and cost of alternative capacity and energy supplies that can be reliably delivered to customers. The use of market value in the utility industry is a significant change from the traditional regulatory approach to setting rates, which is based on embedded, or historical, cost of service.

The NYPSC is in the process of implementing retail competition and industry restructuring through a combination of generic rule-makings and utility-specific restructuring proceedings. The plans that have been approved by the NYPSC, or are pending approval, address the recovery of investments that might be strandable during the transition to competition. Additionally, these plans include provisions for rate reductions during periods of transition to full retail choice. A brief summary of the restructuring plans of utilities in New York State is set forth in Exhibit 11.

LIPA's Plan For Retail Choice

LIPA has proposed a retail choice plan (called ''Long Island Choice'') intended to lead to full choice of power suppliers by all customers by 2003. Under Long Island Choice, LIPA will, within one year after Closing, provide customers representing an aggregate load of 100 MW the option of selecting competitive suppliers of electric capacity and energy. This initial phase of Long Island Choice, anticipated to begin as early as May 1, 1999, will be evenly split between residential customers and nonresidential customers. If fully subscribed, approximately 25,000 residential customers will be eligible to participate. Following an evaluation of the initial phase, LIPA expects to expand Long Island Choice consistent with the development of long-term solutions to the implementation issues, including means to accommodate Internal Revenue Service regulations concerning tax-exempt financing.

Under Long Island Choice, LIPA will be the provider of last resort (''POLR'') responsible for offering firm power supply at reasonable prices to any customers that are unwilling or unable to arrange for alternative power suppliers. LIPA's POLR responsibility will necessitate the adoption of flexible power supply arrangements to accommodate uncertain levels of customer loads. These arrangements may include capacity options and direct market sales or purchases.

Regardless of a customer's choice of electricity supplier, LIPA will remain the sole provider of transmission and distribution services to customers in the Service Area. LIPA plans to set its rates for delivery service to include all costs that are not avoidable once customers choose alternative suppliers, with the intent that LIPA be kept revenue neutral. Costs that LIPA will not be able to avoid, and therefore that will be incorporated in the rates for delivery service, include its debt service obligations, among other items. Accordingly, LIPA will continue to recover all costs needed for safe and reliable T&D System operation and to meet its financial obligations, regardless of the degree of customer participation in Long Island Choice.

FINANCING REQUIREMENTS

Capital Expenditures

Exhibit 3 provides a summary of LIPA's estimated annual capital expenditures during the Study Period. These capital expenditures consist primarily of LIPA's obligations with respect to the acquisition of LILCO and annual expenditures for capital improvements, additions, and replacements, and working capital requirements in connection with the Retained Assets. Capital expenditures associated with BL Holding Corp's use of the Transferred Assets are not included in Exhibit 3 and will be funded by BL Holding Corp through the compensation provisions of the MSA and PSA.

Financing Requirements

LIPA expects to utilize a portion of the proceeds of the Bonds and the Subordinated Indebtedness to fund LIPA's capital requirements during 1998 and to issue Additional Bonds to fund LIPA's capital expenditures during the 1999 through 2008 period. Exhibit 5 sets forth the estimated Bonds, Subordinated Indebtedness, and Additional Bonds to be issued during the Study Period, including the use of the proceeds from these issues.

MANAGEMENT AND OPERATION OF THE SYSTEM

LIPA will manage the performance and cost of electric service within the Service Area with a highly qualified senior management team, while minimizing its total work force. The day-to-day operations of the T&D System will be accomplished by contracts through the MSA, PSA, and EMA using management and other personnel currently performing these functions for LILCO. LIPA's ownership interest in NMP2 will also be managed in this manner through the MSA with oversight by LIPA. Certain functions currently performed by LILCO will be the responsibility of LIPA after Closing, including, but not limited to, (i) certain system planning; (ii) certain power marketing; (iii) DSM program definition; and (iv) financing activities. LIPA will use a combination of (i) a core group of senior managers; (ii) internal professional and administrative support staff; and (iii) outsourced services by specialists to meet the wide variety of skills and experience required to guide the management of the electric utility.

LIPA has adopted an organization which provides for senior management positions, including: (i) a chairman, president, and chief executive officer; (ii) an executive director; (iii) a chief financial officer; (iv) a vice president and controller; (v) a chief operating officer; (vi) a vice president of power markets; (vii) a vice president of governmental and external affairs, and (viii) a general counsel. LIPA has currently filled the positions of chairman, president and chief executive officer, executive director, chief financial officer, vice president and controller, and general counsel. LIPA expects to fully staff all senior management positions by early summer 1998.

In addition to the eight senior staff positions, LIPA will retain approximately 15 support personnel to assist in its day-to-day management activities. At present, seven of these positions have been filled by LIPA. LIPA has informed RMI that it expects to fill the remaining support staff positions by the third quarter, 1998. LIPA will rely on outside consultants and advisors to fulfill the duties of the support staff until such time as all planned positions are filled.

In addition to the above services, LIPA will utilize outside experts for those tasks or functions that require independent resources or, by their nature, are best performed by contractors. Examples of tasks to be performed through this outsourcing arrangement include, but are not limited to, the following:

- Review of actual costs incurred under the MSA, PSA, and EMA;
- Review of the incentive/disincentive compensation provisions under the MSA, PSA, and EMA;
- Review of the application of price escalation indices under the MSA, PSA, and EMA;
- Planning, implementation, and monitoring of Long Island Choice;
- Review of electricity and fuel purchases under the EMA;
- Review and evaluation of annual operating and capital budgets;
- Solicitations for new capacity and energy supplies;
- Evaluation of ramp-down opportunities under the PSA;
- Evaluation of generation purchase rights;
- Review of system dispatch and off-system sales and purchases; and
- Review of on-going programs to ensure compliance with applicable environmental, health, and safety requirements.

LIPA will provide the continuity of policy making, rate setting, financial planning, and management of the T&D System and NMP2 by maintaining capability on its management team and in-house staff to administer the MSA, PSA, and EMA, and by making efficient use of outsourced services.

Cost and Performance Control By LIPA

The Agreements are structured in a manner to provide LIPA control over the performance and cost of the T&D System and NMP2 without the requirement to directly provide the day-to-day operation and maintenance of these facilities. The MSA, PSA, and EMA establish the obligations of the contractors to perform T&D System operation and maintenance and provide for the cost effective management of NMP2, provide electric capacity from the GENCO generating facilities, and provide for the dispatching of the GENCO facilities, the acquisition and management of fuel supplies, and the management of other power supply resources, respectively.

Management Services Agreement

LIPA will exercise control over the performance of the T&D System through specific standards for performance and incentives to the Manager. The primary standards of performance for the delivery of power are the frequency and duration of outages, as described under the section entitled "TRANSMISSION AND DISTRIBUTION SYSTEM—Condition of Facilities" in this Report. Reliability standards established by LIPA in the MSA have generally been set at levels equal to or above the average levels LILCO has achieved in recent years.

Annual monetary incentives to the Manager under the MSA can reach $4 million by meeting or exceeding reliability targets. The incentives are apportioned to each of four geographic districts of the T&D System, the performance of which are separately monitored. This incentive encourages the Manager to undertake measures across the T&D System that are reasonably anticipated to maintain or improve reliability. The operating budget which has been established for 1998 to implement the MSA provides for at least the level of labor LILCO has maintained in recent years, adjusted in accordance with relevant cost indices. The capital additions budget approved for 1998 is at levels similar to those which have been expended in recent years, during which LILCO has undergone a significant improvement in reliability.

Budget expenditures for the operation and maintenance of the T&D System and NMP2 under the MSA consist of (i) ''Direct Costs'', which include the Manager's labor; (ii) ''Third Party Costs'', which are the costs of materials or services provided by others; and (iii) ''Other Costs'', which are those costs which are not able to be anticipated and are outside the control of the Manager. Direct Costs for 1998 have been set at a fixed annual amount based on historical levels, adjusted for known changes in circumstances. The Direct Cost portion of the budget will be adjusted solely by agreed-upon cost indices for the remaining seven years of the MSA. For 2006 through 2008, T&D System Direct Costs have been included in the estimated Operating Results based on estimated 2005 costs and assumed escalation in such costs.

Third Party Costs have been agreed to by LIPA for 1998 and are subject to advance approval every year, which provides LIPA with substantial cost control. Other Costs are those unexpected costs which any owner of a transmission and distribution system may encounter.

The MSA establishes customer service incentives for call answering and meter reading. When combined with reliability, these services comprise the key performance areas of concern to most utility customers. The call answering incentive will be developed based upon the results of the first year of operation under the MSA, with the objective of improving call response times within a specified range. The monthly meter reading incentive targets a reduction in the number of estimated meter reads. This incentive results in a $200,000 per month incentive, or payment obligation, during any month in which the number of estimated meter readings is below, or above, respectively, a specified tolerance band. The MSA also provides for a worker safety incentive payment to achieve and maintain lost-time accident levels below historical levels. This incentive can total $1 million annually.

Power Supply Agreement

The PSA provides for a FERC-regulated wholesale rate applicable to the electric generating capacity purchased by LIPA from GENCO. This rate is cost-based and has been adopted by FERC, subject to the results of a hearing to be held at a later date. The outcome of this FERC hearing can only result in the same rate level or a reduction in the rate level, but not an increase in the rate. This rate may be modified in the future in accordance with the terms of the PSA for (i) agreed upon labor and expense indices applied to the base year; (ii) capital expenditures required for the GENCO generating facilities, which will require approval by LIPA; and (iii) reasonably incurred expenses that are outside the control of GENCO. This rate formula provides for the containment of GENCO costs.

In addition to cost control, Appendix F of the PSA provides incentives and penalties for GENCO to maintain the output capability of its generating facilities, as measured by annual industry-standard tests of operating capability, and to make capital improvements which benefit plant availability. These combined incentives and penalties may total as much as $4 million annually and are expected to provide a meaningful inducement for favorable performance.

Energy Management Agreement

The EMA provides for payment of the costs of sufficient professional and support staff to procure fuel and energy for LIPA. The EMA further provides incentives for control of the cost of fuel and electricity purchased on behalf of LIPA by the Energy Manager. Fuel and electricity purchases will be compared to regional price indices and the Energy Manager will receive a payment from LIPA, or be obligated to make a payment to LIPA, for fuel and/or purchased electricity costs which are below or above, respectively, specified tolerance bands of regional indices. The total fuel purchase incentive or disincentive can be no greater than $5 million annually and the electricity purchase incentive or disincentive can be no greater than $2 million annually. LIPA pays for actual fuel and electricity purchases, therefore this level of incentive is expected to be sufficient to induce the Energy Manager to undertake purchases which compare favorably to regional prices for these commodities.

The budgets for all of the above-described agreements have been established in recognition of past budgets and actual expenditures and capital improvement requirements. This benchmarking to past costs is believed to provide a reasonable basis for estimating the levels of future costs to be included in the budget for the MSA, PSA, and EMA.

Other Mechanisms to Maintain Control of Cost of Service

The Agreements also provide LIPA the means to foster long-term competition in power supply and in T&D System management in the following ways:

- The "Grant of Future Rights" (Schedule F to the Agreements) enables LIPA to acquire or lease property for itself or other parties at or adjoining the existing GENCO generating sites. This right was obtained principally so that LIPA could make sites available to install generation to help create a competitive power supply market.
- The Generation Purchase Right Agreement grants LIPA the right, in the fourth year of the Agreements, to acquire all of LILCO's existing generation at fair market value.
- LIPA has a 99-year right to lease common property owned by BL Holding Corp that is needed for the operation and maintenance of the T&D System for use by a subsequent Manager.
- BL Holding Corp cannot compete with LIPA for transmission and distribution services within the Service Area. Any capacity and energy sold by GENCO or its affiliates within the Service Area must be delivered over LIPA's T&D System. This provision was established to enable LIPA to recover all of the charges it would otherwise receive for the use of the T&D System in the event power from the GENCO facilities not otherwise used by LIPA is sold outside the Service Area or into an authorized retail choice market within the Service Area.

UTILITY RATES AND CHARGES

LILCO's retail rates prior to Closing generally reflect traditional rate design and include daily service charges, block rate and time-of-use energy charges, demand charges for larger commercial and industrial customers, and several energy-based or percentage-based riders. Time-of-use rates are offered in both the residential and commercial customer classes. Economic development and load retention incentives are provided to a small number of commercial customers. A real-time pricing experiment is in place for six large commercial users.

LIPA's Proposed Rates

In January 1998, LIPA released its proposal to implement reductions in retail rates. Public hearings were held in March 1998, to accept comments on the proposed rate reductions.

On April 9, 1998, the Trustees approved new retail rates which will become effective at Closing. These new retail rates are designed to produce average revenues from retail electric sales ("Average System Rate") of 12.70 cents per kWh, excluding the effects of the Shoreham property tax settlement credit, as described later in this Report. When the Shoreham property tax settlement credits are taken into account, the rates adopted by the Board represent a 20 percent reduction from LILCO's existing base electric rates (excluding RICO credits)(1). LIPA's rates are expected to be maintained at this initial level through 2002. LIPA's rates also include the adjustment clauses described below.

LIPA's rates reflect equal across-the-board percentage reductions from LILCO's existing base rates for all customers receiving standard tariff service. These reductions are expected to approximate $250 annually for an average residential customer and total $498 million annually for all retail customers. Table 13 provides a summary of the components of the rate reductions.

The existing RICO credit mechanism, which is part of a settlement arising from a class action suit filed against LILCO (the "RICO Credit"), returns $60 million per year to ratepayers through May 2000. Pursuant to the Agreements, following Closing, LILCO and LIPA will jointly petition the Federal District Court, which is supervising the settlement, to authorize a one-time discounted payment in place of the ongoing refund mechanism. Until such time as the court authorizes the one-time payment, it is expected that LIPA will continue to include the existing RICO Credit in its rates, with full compensation from BL Holding Corp.

TABLE 13

AVERAGE SYSTEM RATES AND REDUCTIONS(1)

	System Average		Nassau/Rockaway Customers		Suffolk County Customers	
	Cents/ kWh	Percent Reduction	Cents/ kWh	Percent Reduction	Cents/ KWh	Percent Reduction
LILCO Current Average System Rates	15.23	—	15.23	—	15.23	—
Less: LIPA Base Savings(2)	(2.53)	16.6	(2.53)	16.6	(2.53)	16.6
Less: Shoreham Credits	(0.52)	3.4	(0.66)	4.3	(0.38)	2.5
LIPA Average System Rates	12.18	20.0	12.04	20.9	12.32	19.1

(1) Reflects average revenues for all retail customers.
(2) Reduction in average revenues per kWh resulting under the rates adopted by the Board.

An important element of LIPA's rates is the implementation of a settlement of the Shoreham property tax litigation and payment-in-lieu-of-tax ("PILOT") potential claims (the "Shoreham Settlement"). The Shoreham Settlement will account for a greater level of rate savings in Nassau County and the Rockaway Peninsula as compared with Suffolk County. The Shoreham Settlement relates primarily to a court ruling in 1996 that Suffolk County, Brookhaven Township, and some of the municipal taxing jurisdictions in Suffolk County had overtaxed LILCO for Shoreham and to the potential claim by LIPA for overpayment of PILOTs. The amount of the judgment, with interest

(1) BL Holding Corp will assume responsibility for payments to customers of remaining obligations resulting from a civil lawsuit brought against LILCO under the federal Racketeer Influenced and Corrupt Organization Act ("RICO") which alleged that LILCO had made inadequate disclosures before the NYPSC concerning the construction of nuclear generating facilities.

thereon, exceeds $868 million and the potential claims by LIPA for PILOT overpayments is approximately $327 million. Since LILCO had already collected these amounts from its customers through its electric rates, any money that LILCO received from this judgment was to be returned to ratepayers. The Shoreham Settlement will reduce the overall amount to be paid by Suffolk County and the municipal taxing jurisdictions to $625 million. To assist Suffolk County and the municipal taxing jurisdictions in funding this settlement, the Shoreham Settlement will be financed by LIPA and recovered from ratepayers in Suffolk County over the life of the Bonds and the Subordinated Indebtedness. Customers in Nassau County and the Rockaway Peninsula will collectively receive an up-front, one-time payment of $62.5 million, plus $50 million per year for five years through their electric rates, which represents their portion of the Shoreham Settlement. Customers in Suffolk County will collectively receive a refund of $30 million per year for five years through their electric rates so as not to create too large a rate differential within the Service Area (together with the annual refund received by customers in Nassau County and the Rockaway Peninsula, the ''Shoreham Credits''). For additional information on the Shoreham Settlement, please see the section entitled ''SHOREHAM TAX MATTERS'' in the Official Statement.

The rates adopted by LIPA are based in large part on LILCO's current rate designs to avoid potential confusion on the part of customers and to allow for a smooth and timely transition from LILCO billing to LIPA billing. In addition to the basic tariffs, LIPA's rates include a fuel and purchased power cost adjustment clause (the ''FPPCA''), a PILOT payment recovery rider, a Shoreham property tax adjustment rider, and a rider applicable to the RICO credit, all as described below. Miscellaneous service charges, pole attachment charges, and rental rates will be maintained at their existing levels without reductions.

Fuel and Purchased Power Cost Adjustment Clause

The FPPCA will apply to all service classifications and will be used to adjust rates in response to significant changes in the cost of fuel, purchased power, and load reduction program costs. Such costs will be determined on the basis of actual results and any adjustments will be applied prospectively. Exhibit 1 shows the estimated revenues that will be recovered through the FPPCA based upon the fuel and purchased power cost forecast incorporated in the estimated Operating Results.

Shoreham Property Tax Settlement Rider

LIPA's rates include a new rider to implement the Shoreham Settlement. The rider describes the calculation of percentage factors to be applied to bills, including the FPPCA. Separate factors will be established for Nassau County and the Rockaway Peninsula, and for Suffolk County to accomplish the goals of the Shoreham Settlement.

PILOT Payments Recovery Rider

LIPA's rates include a revenue tax factor to collect gross receipts taxes to be paid by LIPA in the form of PILOTs. Gross receipts taxes vary within the Service Area according to taxing jurisdiction. This rider is designed to recover the applicable gross receipts tax from each ratepayer. The PILOT payments recovery rider will also accommodate the Metropolitan Transportation Authority Temporary Surcharge that LIPA will pay as a PILOT.

RCAR Rider

The Ratepayer Class Action Refund (''RCAR'') Rider provides for the application of the RICO Credit on customer electric bills. The RICO Credit will be applied as a percentage of customer electric bills.

Regional Comparison

Table 14 provides a comparison of average revenues per kWh by revenue classification for LIPA and the seven investor-owned electric utilities in New York State, including LILCO. This table illustrates that LIPA's rate reduction will reduce the gap between the rates paid by electric consumers within the Service Area and the present retail rates of these other utilities. For example, compared to 1996 rates, the gap for the industrial classification will be cut in half on average, while the gap for the residential classification will be reduced by about 90 percent.

The comparisons shown in Table 14 do not take into account proposed or anticipated rate reductions that the New York State investor-owned utilities expect to implement as part of industry restructuring activities. Please see Exhibit 11 of this Report for information on the restructuring plans of these New York State utilities.

TABLE 14

COMPARISON OF AVERAGE UNIT REVENUES
(Cents per kWh)(1)

	Rate Classification		
	Residential	Commercial	Industrial
Long Island Lighting Company	16.73	14.36	13.42
Consolidated Edison Company of New York	16.50	12.90	12.40
New York State Electric & Gas Corporation	13.80	11.70	8.10
Long Island Power Authority(2)	13.38	11.49	10.74(3)
Orange & Rockland Utilities Incorporated	12.80	9.80	8.20
Niagara Mohawk Power Corporation	12.40	10.70	5.10
Rochester Gas & Electric Corporation	12.00	10.50	7.80
Central Hudson Gas & Electric Corporation	11.20	8.20	5.70

(1) Reflects average revenues per kWh for calendar year 1996. Source: Federal Energy Information Administration, Form 861. These revenues do not reflect reductions approved or expected to be approved by the NYPSC as part of utility restructuring plans. Please see Exhibit 11 for information on the structuring plans of the New York State utilities.

(2) Reflects the 20 percent rate reduction to be implemented at Closing, including the Shoreham Credits.

(3) The Service Area has little traditional ''industrial'' load. For LIPA, this rate classification applies primarily to large commercial customers.

Open Access Transmission Tariff

On April 24, 1996, FERC issued a ruling and regulations in Order No. 888 (since updated) requiring public utilities subject to FERC rate regulation under Section 205 of the FPA to provide open access transmission service to all ''Eligible Customers'', as defined in Order No. 888. Order No. 888 required such utilities to provide transmission service on a comparable basis to the means by which the transmission provider uses the transmission system for its own wholesale purposes and to file open access transmission tariffs with FERC in a prescribed format. FERC does not have authority to require municipal utilities, such as LIPA, to file open access tariffs with FERC. However, FERC adopted a reciprocity requirement for jurisdictional utilities giving them the right to demand, as a condition of providing such transmission service, that non-jurisdictional utility transmission customers that own, operate, or control transmission facilities provide the jurisdictional utility with comparable transmission service over the non-jurisdictional facilities.

In connection with LILCO's application to FERC to transfer its transmission facilities and other FERC jurisdictional facilities to LIPA, LIPA indicated that it intends to adopt an open access, non-discriminatory transmission tariff consistent with FERC's requirements. In FERC's order dated February 10, 1998, approving the transfer of these facilities to LIPA, FERC required LIPA to file an open access transmission tariff as a condition of approval of the transfer. The open access transmission tariff, with certain limited exceptions, would govern LIPA's provision of transmission service over its transmission system.

OPERATING RESULTS

Historical Revenues and Operating Expenses

Presented in Exhibit 12 of this Report, are LILCO's electric revenues and expenses for the calendar year 1993 through 1997 period, excluding annual depreciation accruals, interest expense, income taxes, and other non-operating expenditures. Historical revenue requirements for LILCO cannot be compared directly with LIPA's estimated revenue requirements set forth in Exhibit 1 due to differences in the recognition of costs. However, trends in sales, costs, and revenues provide an indication of the stability of LILCO's historical operating results.

Estimated Operating Results

LIPA's estimated Operating Results for the Study Period are shown in Exhibit 1 of this Report. Estimated operating revenues shown in Exhibit 1 have been based on the demand and energy forecast discussed earlier and reflect a continuation of the rates recently adopted by the Board through 2002, with assumed annual increases of one percent per year thereafter. Annual operating revenues also take into account the effects of the FPPCA, the Shoreham Settlement, the RICO Credit, and miscellaneous operating revenues.

Estimated revenue requirements shown in Exhibit 1 include annual operating expenses, PILOTs, annual debt service payments, promissory notes receipts, earnings on invested funds, and optional debt prepayment. Estimated operating expenses have been developed based on the terms of the Agreements and the budgets adopted or approved for 1998. Estimated PILOTs reflect a continuation of recent historical tax levels applicable to the Retained Assets and incorporate annual escalation rates consistent with LILCO's historical experience. Annual debt service payments are based on debt service schedules provided by LIPA's financial advisor for the Bonds, Subordinated Indebtedness and Additional Bonds and LILCO debt assumed by LIPA. Promissory notes receipts represent payments by BL Holding Corp equal to the annual debt service payments on certain LILCO debt assumed by LIPA. Earnings on invested funds were developed based on estimated cash fund balances and are treated as an offset to annual revenue requirements.

Page 1 of Exhibit 1 presents LIPA's estimated Operating Results for the Study Period. Annual revenues are expected to be sufficient throughout the Study Period to meet annual revenue requirements and provide funds available for other purposes. These available funds, after satisfaction of annual revenue requirements, are expected to be used in whole or part for the prepayment of a portion of LIPA's outstanding Bonds. Optional prepayment of LIPA debt has been incorporated based on schedules provided by LIPA's financial advisor. Interest savings resulting from the prepayment of the Bonds are included in Exhibit 1 as a reduction in annual debt service requirements.

Page 2 of Exhibit 1 illustrates the calculation of LIPA's annual Rate Stabilization Fund balance. Net cash flow from operations will flow into the Rate Stabilization Fund, as will the proceeds of Bonds issued to finance the Shoreham Settlement. This fund will be used to mitigate future increases in LIPA's retail electric rates, among other uses, and is expected to be maintained at a level of approximately $250 million on an annual basis.

Also included on page 2 of Exhibit 1 is a calculation of annual debt service coverage during the Study Period. LIPA's General Bond Resolution and Subordinated Bond Resolution contain covenants that obligate LIPA to make PILOTs to State and local taxing jurisdictions. The priority of payments under the Bond Resolution also specifies that payments of PILOTs will be subordinate to debt service. RMI's calculation of debt service coverages shown on page 2 of Exhibit 1 are consistent with this priority of payments.

Annual debt service coverage on LIPA's outstanding Bonds and Additional Bonds is estimated to range from 2.1 to 5.5 during the Study Period. Combined coverage levels for the Bonds, the Additional Bonds, and Subordinated Indebtedness are expected to range from 1.8 to 4.3, and for LIPA's total annual debt service, inclusive of LILCO debt assumed by LIPA, from 1.4 to 3.2 during the Study Period.

Page 3 of Exhibit 1 presents LIPA's average revenues per kWh under the rates adopted April 9, 1998, by the Trustees without the inclusion of the Shoreham Credits. As shown on page 3, these rates represent a reduction from LILCO's existing base electric rates of 16.6 percent during 1998. This reduction increases to 20 percent with the Shoreham Credits.

Sensitivity of Results

To assess the sensitivity of the Operating Results to changes in key variables, RMI evaluated the impact of five cases, each of which address variables that are largely beyond LIPA's control and which could adversely affect net cash flow available from operations during the Study Period. The selection of these sensitivity cases is not an indication of expectation of their occurrence. The variables selected include fuel costs, system capacity and energy requirements, rates of increase in non-fuel costs, changes in interest rates, and loss of the highest fixed cost power supply source serving LIPA.

Presented below is a description of the sensitivity analyses performed by RMI. In all cases, the rates initially charged by LIPA are assumed to equal those adopted by the Trustees on April 9, 1998, which reflect a 20 percent reduction from LILCO's existing base electric rates, inclusive of the Shoreham Credits. These rates are assumed to be held constant by LIPA through 2002, after which annual increases of 1.0 percent per year are included through 2008. In each of the sensitivity analyses, all of the financial and operating variables have been held at the levels reflected in the Base Case (as presented in Exhibit 1) except for those specifically discussed below. In addition, each of the sensitivity cases assumes the optional accelerated prepayment of Bonds in accordance with LIPA's estimated financial capacity to do so.

Case 1—Base Case: The Base Case represents the estimate of future Operating Results presented in Exhibit 1 of this Report. The Base Case provides a reference case from which to measure the changes in estimated Operating Results associated with the sensitivity analyses.

Case 2—Higher Fuel Cost: Under the Higher Fuel Cost case, LIPA's power supply costs have been modeled using commodity prices for fuel which reflect an immediate 9.1 percent increase for

natural gas and 4.1 percent increase for fuel oil, with future price level changes tracking the Base Case annual percentage change. Under this case, the added cost of fuel and purchased power is expected to be subject to recovery in accordance with the provisions of the FPPCA.

Case 3—Lower Load Forecast: The Lower Load Forecast case reflects average annual growth in electric sales of approximately 1.0 percent. This growth rate compares to the 1.3 percent per year average increase incorporated in the Base Case. The lower growth rate reflected in this sensitivity case was based on an analysis of historical sales levels and is representative of the load forecast variance that has occurred historically.

Case 4—Higher Escalation Rate: The Base Case incorporates an annual escalation rate of 2.7 percent for many cost elements. In the Higher Escalation Rate case, an escalation rate of 3.7 percent has been used to test the sensitivity of the estimated Operating Results to changes in the rate of escalation. This rate change does not affect costs associated with the estimation of fuel and purchased power costs, but does affect certain costs occurring under the MSA and PSA, as well as non-fuel and purchased power costs under the EMA. In addition, certain other costs included in the estimate of annual Operating Results are affected by the increase in escalation rates.

Case 5—Higher Assumed Interest Rates: This sensitivity case measures an increase of 100 basis points in the interest rate on all Bonds issued after the first tranche and an increase of 100 basis points in the interest rate on the Subordinated Indebtedness.

Case 6—Closure of NMP2: The Closure of NMP2 case reflects the permanent, unforeseen closure of NMP2 beginning January 1, 2000. This case assumes that purchased power would initially be imported using the transmission interconnection capacity freed up by the closure of NMP2. Subsequently, a combined cycle generating unit is assumed to be constructed near the NMP2 site in 2004. This case also assumes that non-fuel operation and maintenance costs for NMP2 continue through 2002, followed by the implementation of an accelerated decommissioning program in 2004.

Table 15 provides a comparison of key differences between the estimated Operating Results shown in Exhibit 1 for the Base Case and for the sensitivity cases.

TABLE 15
COMPARISON OF SENSITIVITY RESULTS
(Millions of Dollars)(1)

	Bonds			Total Debt(5)	
	Cumulative Optional Accelerated Debt(2)	Average Coverage Ratio(3)	Minimum Coverage Ratio(4)	Average Coverage Ratio(3)	Minimum Coverage Ratio(4)
Case 1—Base Case	1,318	2.4	2.1	1.8	1.4
Case 2—Higher Fuel Cost	1,243	2.4	2.1	1.7	1.4
Case 3—Lower Load Forecast	904	2.3	2.0	1.7	1.4
Case 4—Higher Escalation Rate	965	2.4	2.1	1.7	1.4
Case 5—Higher Assumed Interest Rate	866	2.3	2.0	1.7	1.4
Case 6—Closure of NMP2	1,386	2.5	2.1	1.8	1.4

(1) All amounts are totals for the period June 1998 through December 2008, unless otherwise noted. All cases reflect the 20 percent reduction from current LILCO base electric rates, inclusive of the

Shoreham Credits, approved by the Trustees on April 9, 1998, which are assumed to be held constant through 2002 and increased by one percent per year thereafter through 2008.

(2) Cumulative amount of unscheduled debt repayment made during the June 1998 through December 2008 period.

(3) Average debt service coverage for the period from June 1, 1998, through December 31, 2008.

(4) Minimum debt service coverage in any single year.

(5) Includes Bonds, Subordinated Indebtedness, Additional Bonds, and LILCO debt retained by LIPA Sub.

SECURITY OF CUSTOMER REVENUE

As competition in the electric utility industry becomes a reality, customers are expected to increasingly focus on rate comparisons in assessing the reasonableness of the cost of retail electric service. As discussed previously, LIPA's adopted rate reductions will substantially close the gap between LILCO's existing rates and the existing rates of the other New York State investor-owned utilities. This change alone will improve LIPA's revenue security by reducing the potential economic benefits of any measures LIPA's customers might consider in an effort to reduce their costs of electricity. Nevertheless, as other utilities reduce their rates under restructuring plans, increased customer focus on electricity costs warrants a careful consideration of the potential customers may have to either leave the T&D System or otherwise avoid the fixed costs of the T&D System.

Potential threats to LIPA's revenue security arise from actions or events which could reduce the long-term sale of capacity and energy which support the payment of LIPA's fixed costs. The potential conditions which could result in a reduction in LIPA's electric sales include (i) a permanent decline in individual customer demand and energy requirements; and (ii) customers permanently leaving the T&D System as a result of self-generation, direct bypass, or other measures. These conditions are described below.

Load Forecast Variance

Short run variations in customer capacity and energy sales are highly related to fluctuations in weather, whereas long run variations are highly related to changes in local, regional, and national economies. The load forecast upon which LIPA's revenue estimate has been based was developed taking into account normalized weather conditions. This approach restates historical electricity sales for variations in ''normal'' weather patterns and forecasted capacity and energy sales reflect customer usage levels under normal weather conditions. Although actual weather conditions, and therefore electricity sales, will vary from ''normal'' conditions on a year-to-year basis, the normalized load forecast should, over time, provide a reasonable approximation of actual capacity and energy sales during the forecast period.

Economic activity has a long-term effect on annual electricity sales due to the multi-year duration of most economic cycles, the relative slowness by which the cycles change, and the effect of economic conditions on consumer spending habits. The effects of economic activity within the Service Area have been incorporated in the load forecast through the use of an econometric model which considers population levels, personal income levels, economic activity, new housing starts, and related factors.

The cost of electricity may also impact LIPA's long-term electricity sales, particularly with large customers. Theoretically, electricity prices that are too high or that increase significantly over a short period of time could cause some customers to leave the Service Area or to permanently change their

electric usage patterns. Electric rates within the Service Area, however, have been extraordinarily high for over a decade and it is reasonable to expect that any loss of customers or change in usage patterns that would occur due to price have already taken place. Coupled with the substantial rate reduction the Trustees adopted on April 9, 1998, which will reduce average customer electric bills by 20 percent, it is highly unlikely that the cost of electricity within the Service Area after the Closing will contribute to a long-term reduction in estimated demand and energy sales.

Service Area Franchises

LILCO has advised LIPA that certain of LILCO's electric service franchises have lapsed and have not been renewed. LIPA's legal counsel has advised LIPA that municipalities may not decline to grant LIPA a franchise, unless LIPA fails to agree to reasonable terms and conditions. If the municipalities do decline to grant LIPA a franchise, LIPA may condemn the franchise. Consequently, the past or future expiration of LILCO's franchise agreements is not expected to have an impact on LIPA's long-term capacity and energy sales.

Gas Competition for Electric Load

In reviewing the forecast of electric loads within the Service Area, RMI gave consideration to the potential for impact to such forecast by the conversion of existing electric appliances and other electric end uses to natural gas. Several factors influence a customer's decision to make such a conversion, including (i) access to the local gas distribution network; (ii) the cost of natural gas versus electricity; (iii) the cost of conversion to natural gas end use, including the price of the gas appliance and the installation of in-house gas piping; (iv) the maturity of the gas appliance technology; and (v) non-economic factors, such as perceptions of safety and performance.

Electric space heating, central air conditioning, water heating, cooking, and clothes drying are typically the end uses which are theoretically considered most vulnerable to conversion to natural gas. According to saturation data developed by LILCO, electric clothes dryers and ranges are the only end uses within the Service Area with saturation levels in excess of 50 percent (61 percent and 52 percent, respectively). Electric space heating (5 percent saturation), electric water heating (12 percent saturation), and electric central air conditioning (21 percent saturation) are used in such small amounts that even if a significant percentage of such end uses converted to natural gas, the conversion would have a relatively minor impact on LIPA's annual operating revenues. However, the cost of converting individual homes or businesses to natural gas, which would include both the incremental cost of new end use appliances or equipment as well as the cost of connecting to the gas system and installing gas piping within the home or business, is likely to preclude the wide spread conversion of these end uses to natural gas.

In response to the conditions imposed by the PACB in approving LIPA's acquisition of LILCO, BL Holding Corp has agreed to invest $1.3 billion in energy-related and economic development projects and infrastructure projects in the counties of Queens, Nassau, and Suffolk over a 10 year period following the Closing. However, based on historical spending levels, a significant portion of this sum may be accounted for by normal capital expenditures by BL Holding Corp in gas system infrastructure improvements, and therefore should not stimulate additional conversions of electric load to natural gas. BL Holding Corp has not yet announced its plans for the methods to be used to comply with this PACB condition.

Retail Choice

The Long Island Choice plan has been developed in a manner that will make LIPA economically indifferent as to whether a customer selects LIPA or another power supplier to serve the customer's power supply needs. Under this plan, LIPA will be providing all of its customers with the option of selecting a party other than LIPA as their power supplier. Under any circumstance of retail choice, power delivered to a LIPA retail customer will continue to be delivered over the T&D System. LIPA's retail choice plan is designed to protect LIPA's ability to fully recover revenues to pay its fixed costs. LIPA will adopt unbundled retail rates under which the costs of power supply that can be avoided as a result of retail choice will be separated from the cost of delivering that power supply to the customer. Should a customer select an alternative power supplier, the customer will pay for all of LIPA's costs, other than incremental power supply costs, in the delivery charge. Consequently, to the extent a customer selects a power supplier other than LIPA, LIPA's obligation to supply power to such customer will be eliminated, as will the costs associated with power supply service to that customer.

LIPA intends to offer to continue to provide capacity to customers where marketers are unable to secure sufficient or more economical capacity. Over time, incremental growth in LIPA's power supply requirements are expected to be increasingly served by the competitive market. Under this structure, LIPA is not expected to encounter revenue loss without a corresponding reduction in its power supply cost obligation.

Self-Generation

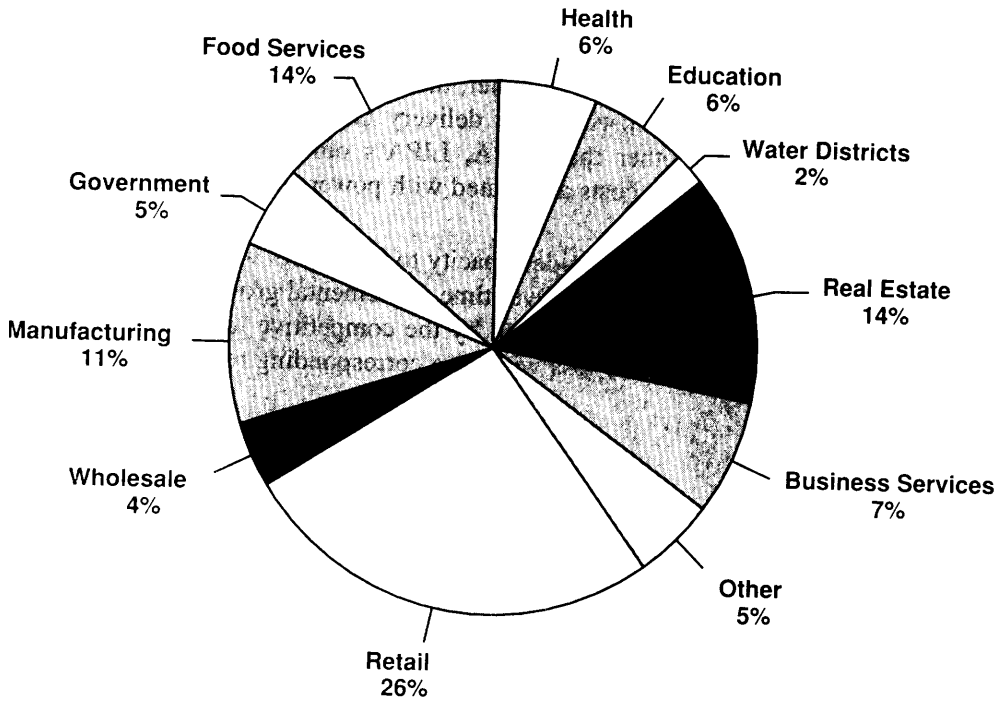
Customers could reduce LIPA's role of supplying and delivering electric capacity and energy through the installation of their own generating facilities. The economics of self-generation are greatly influenced by the characteristics of the capacity and energy sales displaced by the customer's generation. Self-generation is most attractive to customers who are high load factor energy users and can spread the fixed costs of self-generation over a large volume of energy usage. There are few customers of this nature within the Service Area. Exhibit 13 provides a summary of the peak demand and annual energy usage of the 20 largest electric users in the Service Area during 1997. As shown in Exhibit 13, the 20 largest customers during 1997 had combined energy sales and revenues of less than four percent of total energy sales and revenues, indicating that even the largest customers in the Service Area are generally not major, high load factor customers. Customers with low load factors face the burden of allocating substantial fixed capital costs and fixed annual operation and maintenance costs associated with self-generation over a relatively low total annual energy use. Such customers are generally not good candidates for self-generation.

Figure 2 shows the distribution of the Service Area's historical commercial and industrial customer mix by type of business. The most likely high load factor customer will be within the manufacturing and health segments, which together comprise only 17 percent of total commercial and industrial electric revenue. Based on information provided by LILCO for 1997, these customers represented approximately $200 million of annual revenue, or less than 10 percent of the total for the year. In addition, power supply costs are less than 30 percent of total annual revenue requirements. Therefore, power supply-associated revenues from the combined manufacturing and health sectors would approximate $60 million per year. Only a portion of the costs covered by this revenue would theoretically be subject to being stranded, even if the entire customer group elected to self-generate. The remaining commercial and industrial customers are expected to have lower load factors and consequently even lower likelihood of self-generation. Without large, single electric loads to serve,

there are few opportunities within the Service Area for the loss of significant electric sales through individual customer self-generation.

FIGURE 2

DISTRIBUTION OF REVENUE FROM COMMERCIAL AND INDUSTRIAL CUSTOMERS



Absent large individual customer loads, the principal opportunities for self-generation are expected to involve either the (i) installation of generating plants with capacity larger than the individual customer loads, with the sale of excess generating output into the power supply market; or (ii) installation of very small generating plants to serve the typically smaller customer load within the Service Area. In the 20 years since the passage of the Public Utility Regulatory Policies Act of 1978, which created the opportunity to sell excess co-generation output into the power supply market, only three significant cogeneration facilities have been constructed within the Service Area. These facilities were constructed to supply the individual customer's electrical needs, with excess electric output sold to LILCO. A total of approximately 201 MW of such capacity has been constructed within the Service Area in the past 20 years, with the last plant starting operation in 1996. Since 1993, approximately 53 MW of self-generation capacity has been installed on Long Island, of which 42 MW is the SUNY plant at StonyBrook. Therefore, other than this single plant, only 11 MW, or an average of about 2 MW per year, of self-generation has been installed in the Service Area. This represents less than four one-hundredths of one percent of peak demand per year lost to self-generation. This self-generation, other than the unique StonyBrook co-generation plant, also has represented an average annual incremental loss of less than seven one-hundredths of one percent of annual energy requirements. Given the long history of high electric rates within the Service Area, LIPA's recently adopted rate reduction of 20 percent is likely to decrease the prospect of additional projects of this type being developed.

Based on the profile of electric users within the Service Area, self-generation, if it is to occur, would likely be limited to the evolving small power generation technology. There are a number of potential situations in which customers could meet some or all of their power supply needs with their own generation resources. These situations include:

- residential users meeting their needs with small distributed generation sources, such as photo voltaic power generating units, gas-fired "micro-turbines, "gas-fueled fuel cells, or similar emerging technologies;
- commercial or industrial users installing commercial scale small generation to serve their needs; and
- groups of commercial and/or industrial customers within proximity to one another jointly installing larger scale generation to serve their collective needs (referred to herein as "cluster" self-generation).

These three situations address the range of circumstances in which the typically smaller customers can elect to provide their own power supply without forming a utility. In conjunction with the development of this Report, RMI performed quantitative evaluations of the cost of each of the above alternatives. These evaluations were based upon the current cost of generation equipment of the size that generally matches the individual or "cluster" of customers, present fuel costs, assumed cost of capital and term for debt repayment, and the cost of acquiring either back-up power supply from LIPA or installing redundant generating capacity to provide back-up power supply at or near utility-grade levels of reliability.

Several power generation equipment vendors are seeking to enter the market of what is referred to as "micro-turbines," which, in presently available technology, are sized in the 75 kW to 200 kW range. This technology has recently become commercially available at costs which vendors claim are competitive with the cost of utility-supplied power sources. For purposes of RMI's evaluation, the target size of customers, or cluster of customers, was assumed to be in the 75 kW to 1,000 kW level. This micro-turbine technology was used as a example of the cost and performance of generation which would be installed by small customers, or groups of small customers. The following three scenarios are expected to reasonably cover the range of situations where a small to medium-sized customer or adjoining groups of customers might seek to install their own generation as a means to reduce their electric costs:

- Scenario 1—One micro-turbine unit with non-firm gas supply, stand-by power provided by LIPA, and no fuel oil backup. The likely application for this scenario is a commercial building seeking more energy self-sufficiency with utility back-up power supply.
- Scenario 2—Two micro-turbine units (to provide redundancy and allow disconnection from the grid, non-firm gas supply, no stand-by power, and fuel oil back-up. This scenario provides for a "disconnect from the grid" approach to be totally self sufficient.
- Scenario 3—Five micro-turbine units, with non-firm gas supply, no stand-by power, and fuel oil back-up. This scenario is the same as 2, but includes larger installed capacity in order to serve a cluster of users, such as a small commercial office park or a small housing subdivision, to achieve some economies of scale. This scenario is expected to be representative of the costs to serve the largest commercial and/or industrial customers, or blocks of residential customers if such situation could be achieved, without the need to create a municipal utility.

Table 16 summarizes the estimated cost of power under each scenario.

TABLE 16

COMPARISON OF SELF-GENERATION POWER SUPPLY COSTS TO LIPA AVERAGE SYSTEM RATE
(Costs in 1998 Dollars per kWh)

Scenario	Gas	Oil	O&M Costs	Capital Costs	Taxes	Stand-By Power	Total Cost	LIPA Average System Rate(1)	Increase Over LIPA Average System Rate
1	$0.071	$0.000	$0.007	$0.017	$0.009	$0.050	$0.154	$0.122	$0.032
2	0.071	0.004	0.010	0.038	0.020	—	0.143	0.122	0.021
3	0.071	0.004	0.006	0.023	0.012	—	0.116	0.122	(0.006)

(1) Rounded from 12.18 cents per kWh.

The costs set forth in Table 16 are based on the assumption that the customer would not be responsible for any of LIPA's stranded costs caused by its actions. To the extent legal recourse exists for LIPA to recover all or a portion of any of its stranded costs, the effective cost of self-generation to customers within the Service Area would be even higher than the estimates shown in Table 16.

In addition to its cost, the following issues would mitigate against self-generation occurring on a wide scale basis within the Service Area:

- Capital Commitment: Self-generation requires a significant capital commitment, with a likely term of debt or payback on investment of at least 10 to 15 years. This commitment is likely to be a major obstacle to widespread self-generation and would require substantial demonstrable, sustained net savings for customers to opt for the inconvenience of self-generation. The above estimates suggest adequate levels of savings are not available.
- Relatively Large Capacity: The size of most of the generation technologies with reasonable fuel efficiency and reliability as a sole, or primary, source of power supply is larger than needed to serve a single residence or small business. As an example, the micro-turbine equipment which is presently becoming available is generally being manufactured at a capacity of 75 kW or greater, as compared to the average peak demand for a residential dwelling of 5 kW to 15 kW. Small commercial customers under the present LILCO tariff are customers with 7 kW peak demand and below. Consequently, in most cases, individual customers would need to combine with other customers to aggregate their loads. This raises legal questions as to the creation of a local "utility." Furthermore, the effort required for multiple customers to jointly finance or contract for the equipment, construct a miniature distribution system, establish individual customer submetering and billing, and other practical problems would likely be an obstacle to the joint use of generation equipment.
- Fuel Supply: If there were significant numbers of customers switching to gas-fueled generation, such gas use could be subject to interruption in the event of winter heating season delivery constraints. If a customer elected to completely disconnect from the LIPA T&D System, the potential for gas supply interruptions would require the generating units to be capable of operating on back-up fuel supply, thereby increasing the cost and complexity of this option.

Because self-generation would likely result in cost increases, and considering the above pragmatic obstacles to self-generation, it is unlikely additional self-generation will be installed in any meaningful numbers within the Service Area.

Municipalization

The final means by which retail electric customers could seek to change their relationship with LIPA is through the formation of a municipal utility or other form of local government-owned utility organization. Other than opting for retail choice or self-generation, this is the only other means for electric utility customers within the Service Area to obtain power supply, and perhaps other utility services, from a party other than LIPA.

Historically, electric rates within the Service Area have caused some local governments to consider municipalization as a means to lower the cost of electric service. Some villages have conducted voter referenda authorizing the creation of municipal electric utilities to replace LILCO if such action was determined to be economic. The villages of Westhampton Dunes, Lynbrook, Farmingdale, and Hempstead have so voted. Other villages, such as Islandia, Southold, Malverne, and Manorhaven and the City of Glen Cove are in the process of performing studies to assess the feasibility of municipalization. However, making a policy decision to consider municipalization and studying the prospect are actions far short of creating a new municipal utility.

As explained in the Official Statement, LIPA's legal counsel has advised LIPA that it has the sole authority to purchase LILCO's securities or assets under the LIPA Act and that local municipalization within the Service Area would be counter to a State-legislated solution to reduce electric rates to all consumers within the Service Area. As also explained in the Official Statement under the section entitled "CERTAIN FACTORS RELATING TO POTENTIAL CUSTOMER LOSS," the State Attorney General has rendered an informal opinion to the County Attorney of Suffolk County which concludes that the acquisition of LIPA's assets through condemnation is preempted by the LIPA Act. Furthermore, LIPA's legal counsel has also advised LIPA that the LIPA Act similarly precludes local governments from constructing their own facilities in order to serve LIPA customers.

Even if a municipality could legally condemn LIPA's assets, there is considerable question as to the ability of a municipality to acquire the assets using tax-exempt financing. LIPA's legal counsel has advised RMI that LIPA has a unique exception under the Federal Internal Revenue Code allowing it to acquire LILCO's existing electric assets without complying with certain restrictions generally applicable to the acquisition of electric utility property previously used by a private utility. Restrictions generally applicable would include the need to obtain State "volume cap" as a condition to the issuance of tax exempt bonds for the purpose of financing the acquisition of such property. LIPA's legal counsel has advised RMI that the limited amounts of volume cap would significantly constrain the ability of municipalities in the Service Area to issue tax-exempt debt for the purpose of acquiring the utility assets currently owned by LILCO and being acquired by LIPA.

Another obstacle to municipalization is FERC Order No. 888. Under FERC Order No. 888, which established open access transmission service, FERC has stated that it will assert jurisdiction to preclude municipal entities from forming utilities as a means of changing former retail customers to wholesale customers to avoid costs otherwise allocable to retail customers. FERC proposes the application of a "revenue loss" formula in which the net present value of costs which would have been paid by the retail customer would be due and payable to the prior local utility service provider in the form of a fee. If a municipality could acquire LIPA's local distribution system through condemnation for fair market value using taxable financing and had the continuing obligation to pay for fixed regulatory assets and any stranded generation costs, there is no likely opportunity for cost savings to the municipality's customers.

Notwithstanding the legal barriers, RMI has prepared an estimate of the cost of creating a municipal utility through the installation of a duplicative distribution system to assess the cost effectiveness of this alternative. This analysis was based on replicating a system with facilities similar to an existing Long Island municipal utility as a proxy for the mix of residential, commercial, and industrial customers, as well as the required distribution facilities per customer. The capital costs of the system were based on a ''replacement cost new'' estimate for the existing utility, with other costs per customer for operation and maintenance, customer accounting and service, billing, administrative and general, and miscellaneous costs using public domain data as a proxy. Power supply was assumed to be purchased at market prices from Long Island generating resources and delivery was assumed to be made without the use of LIPA's T&D System.

Average system revenue requirements for this ''proxy'' municipal utility are estimated at approximately 12.50 cents per kWh during 1998, or slightly higher than LIPA's Average System Rate of 12.18 cents per kWh. However, there are a number of optimistic assumptions used in this estimate, many of which, if changed, would result in a higher cost, including:

- No allowance was included for the recovery of LIPA's stranded costs resulting from retail customers shifting to wholesale customers.
- No costs were included for removing the existing distribution system when a duplicative system was installed;
- No allowance was included for separation costs to reconfigure the distribution system at the municipal utility's borders;
- The replacement cost assumes a mix of overhead and underground transmission and distribution facilities, when it is likely that more of the facilities would be required to be underground at higher costs; and
- No allowance for higher per customer costs for administration, management, or common facilities associated with the likely smaller size of the individual utility.

Although it is difficult to generically estimate the cost of the above four areas of added costs, it is not unreasonable to expect that the cumulative impact could easily add 30 to 50 percent to the above estimate of average system revenue requirements under municipalization. This evaluation suggests that municipalization would likely have a cost significantly higher than the rates LIPA will offer immediately. The LIPA rates will be applied at no risk to the municipality, with no financing requirement or associated risk, no land use or permitting challenges associated with the construction of a duplicative distribution system, and no risk of power supply costs being higher than anticipated. Based on this evaluation, it is unlikely there would be any economic basis for municipalization within the Service Area which would impact LIPA's revenues.

Long Island Electrical Agencies

SCEA is a municipal power agency created by Suffolk County, New York, in 1983 for the purpose of purchasing gas or electric energy from state, municipal, or other entities for resale to gas and electric consumers within its boundaries. SCEA purchases limited amounts of hydropower and economic development power from NYPA for resale to residential customers and commercial and industrial customers, respectively. Pursuant to an agreement entered into by LILCO and SCEA on November 14, 1985, and subsequently amended, power purchased from NYPA by SCEA is transmitted, distributed, and billed by LILCO. This agreement will be assumed by LIPA following the

Closing. For calendar year 1997, energy purchased by SCEA from NYPA and resold to Suffolk County electric consumers was less than 0.4 percent of LILCO's retail electric sales for the same period.

The legal status and services provided by NCPUA are identical in all material aspects to SCEA. Since 1986, NCPUA has purchased limited amounts of hydropower from NYPA for resale to residential customers in Nassau County. In accordance with an agreement dated November 14, 1985, and subsequently amended, between LILCO and NCPUA, LILCO transmits, distributes, and bills for the NYPA power purchased by NCPUA. LIPA will assume this agreement following the Closing. During 1997, the energy purchased by NCPUA and delivered to Nassau County residential users approximated 0.35 percent of LILCO's total annual energy sales.

On January 17, 1996, SCEA applied for an order from FERC requiring LILCO to provide firm network transmission service, as well as certain ancillary, billing, and collection services. SCEA is seeking transmission service to wheel SCEA-purchased electricity at 100 percent load factor from designated points of receipt on the T&D System to the homes of residential consumers presently receiving full requirements service from LILCO. In a December 31, 1996 "Proposed Order Directing Transmission Services and Ordering Further Procedures," FERC ordered LILCO to provide transmission services to the extent necessary to accommodate SCEA's proposed sale of 200 MW of power to residential customers to which it was providing electric service on the date of enactment of the Energy Policy Act (October 24, 1992). FERC also ordered further proceedings to establish the rates, terms, and conditions of such service. LILCO and SCEA have not reached agreement on the rates, terms, and conditions of such service and have referred their various disputes to FERC. The matter is still pending and it is not certain when FERC will act on the matter or what action it will take. LIPA will succeed to LILCO's interest in the case upon Closing.

On March 3, 1998, LIPA received a letter from NCPUA requesting, under Section 211 of the FPA, firm transmission service for up to 300 MW of firm capacity and energy to be delivered to unspecified customers in Nassau County.

PUBLIC AUTHORITIES CONTROL BOARD APPROVAL

The LIPA Act provides that LIPA may not undertake any "project" without the approval of the PACB. Approval by the PACB is to be conditioned on its determination that the project (i) is financially feasible; (ii) does not materially adversely affect real property taxes within the Service Area; (iii) is expected to result in lower utility rates in the Service Area; and (iv) will not adversely affect the real property taxes and utility rates in other areas of the state.

As defined in the LIPA Act, the Agreements constitute a "project" and are therefore subject to PACB approval. The PACB reviewed the Agreements and detailed supporting analysis and data and granted its unanimous approval on July 16, 1997, subject to certain conditions established by the PACB. These conditions are restated below from the PACB July 16, 1997, resolution approving the Agreement. This approval was granted subject to the following conditions:

> *1. "No later than one year after the date of this resolution but prior to the issuance of any debt, LIPA will establish a plan for open access to the electric distribution system in the LIPA service territory, which plan will include a schedule providing that within ten years of the date of this resolution all customers in the LIPA service territory, will be entitled to receive electric service from power suppliers other than LIPA. LIPA will establish and implement this plan according to the following guidelines:*

(a) All customer classes must experience cost reductions in approximately the same proportions

(b) Customers within localized load pockets must experience cost reductions commensurate with other customers in their classes

(c) The safety and reliability of the electric system must not be impaired

(d) LIPA must remain the electric provider of last resort, at just and reasonable rates

(e) If LIPA purchases LILCO's generating facilities, or develops generating facilities of its own, it must subsequently divest itself of such facilities, unless such divestiture is not financially sound or any such facility is needed to meet LIPA's obligations as the provider of last resort

(f) All customer protections existing at the date of this resolution, at a minimum, must be maintained

(g) Residential customers must receive standardized bills and standardized contracts

(h) Access to the distribution system will be limited in a manner that restricts the importation of electricity from power systems with high emissions of regulated air contaminants

(i) LIPA's workforce must be protected against any unfair impacts of a transition to competition; and

(j) Energy efficiency programs must be maintained.

2. "LIPA commits that if LIPA exercises the generation purchase right agreement and the power supply agreement providing for the purchase by LIPA from NEWCO of the generating assets of NEWCO, it will not purchase such assets at a price greater than book value.

3. "Prior to the consummation of the Acquisition Agreement, LIPA will enter into a contract with NEWCO in which NEWCO is obligated to invest over a ten year period no fewer than $1.3 billion in energy-related and economic development projects, and natural gas infrastructure projects, in the counties of Queens, Nassau and Suffolk. Such contract shall provide that barring extraordinary circumstances a substantial portion of such investment will be toward natural gas infrastructure improvements.

4. "LIPA will guarantee that, over a ten year period commencing on the date when LIPA begins providing electric service, average rates within the LIPA service territory will be reduced by no less than fourteen percent when measured against LILCO's base rates at the date of this resolution. The fourteen percent savings must not include the impact of the Shoreham tax settlement. The fourteen percent average rate reduction may be adjusted to reflect emergency conditions and extraordinary unforeseeable events including a percipitous (sic) rise in oil prices. As part of this guarantee, a contract between LIPA and NEWCO will provide that no less than two percent cost savings to LIPA's customers must result from the Amended and Restated Agreement and Plan of Exchange and Merger.

5. "LIPA will not implement an increase in average customer rates exceeding two and one half percent over a twelve month period, nor will LIPA extend or reestablish any portion of a temporary rate increase over two and one half percent, without approval of the Public Service Commission following a full evidentiary hearing."

On April 22, 1998, following the submission to the PACB by LIPA of a description of the measures that have been or will be taken by LIPA to comply with the PACB conditions, the PACB

approved LIPA's issuance of the first tranche of its Plan of Finance. For additional information on the PACB and its approval of the Agreements, please see the section entitled "PUBLIC AUTHORITIES CONTROL BOARD" in the Official Statement.

Compliance With PACB Conditions

LIPA's acquisition of LILCO, together with its plans for retail choice, have been structured to ensure compliance with the PACB conditions. Presented below is a brief description of LIPA's efforts to comply with several of these conditions:

Open Access

LIPA's plan for offering open access (retail choice) is described under the section in this Report entitled "INDUSTRY RESTRUCTURING ISSUES—LIPA's Plan for Retail Choice." This plan provides for:

- A framework for retail choice, with an allocation of 100 MW of customer load that will have an opportunity for choice of power supplier beginning in the first year after Closing and unlimited access for retail choice for all customers by 2003;
- Power suppliers will be required to be certified by LIPA to meet certain experience and performance requirements and LIPA will serve as "provider of last resort" to provide continued safety and reliability of T&D System operations;
- Residential customers will be provided standardized bills and contracts for services (i) through LIPA's power supplier certification program; and (ii) by all billing being coordinated through LIPA;
- The T&D System workforce employed by the Manager is protected contractually under the terms of the MSA; and
- LIPA has committed to increasing the funding for energy efficiency and clean energy generation technology compared to historical expenditures by LILCO, beginning with a $32 million initial annual funding level, which is nearly three times that funded by LILCO in recent years.

Generation Purchase Right Agreement

Under the Agreements, LIPA has a right to purchase the GENCO generating facilities in the fourth year of the Agreements at their fair market value. The Generation Purchase Right Agreement specifically provides for the terms of the PSA to be considered in determining fair market value of the generation assets. The PSA provides LIPA the right to purchase capacity from GENCO at cost-based rates for up to 15 years, at LIPA's option. The cost-based rates result in capacity costs under the PSA directly reflecting the depreciated book value of the GENCO facilities. To minimize customer costs, LIPA would be expected to exercise the option to purchase the GENCO generation assets only if there were alternative costs of power supplies available in the market, after accounting for the cost of acquiring the GENCO facilities, which would provide electric capacity at lower costs than available under the PSA. In this event, the value established by the market would be below the book value-based capacity payment LIPA makes to GENCO under the PSA.

Average Rate Reduction of At Least 14 Percent

Exhibit 1 of this Report shows that, over a ten-year period commencing on the date when LIPA begins providing electric service, LIPA is expected to achieve average rate reductions of approximately 15.1 percent when measured against LILCO's base retail rates in effect July 16, 1997

(the date of the PACB resolution approving the Agreements). These reductions exclude the impacts of the Shoreham Settlement, the RICO credits, and pass-through adjustments, such at the FPPCA.

NYPSC Approval of Certain Rate Increases

The estimated Operating Results shown in Exhibit 1 reflect annual operating revenues which assume that the rates adopted by the Board on April 9, 1998, will be held constant through 2002 and will increase by one percent per year thereafter through 2008. The revenues computed on this basis are estimated to be sufficient to meet all of LIPA's annual revenue requirements, including debt service payments on the Bonds, Subordinated Indebtedness, and Additional Bonds, and provide optional prepayment of a portion of the Bonds. These Operating Results are achieved without the need to increase LIPA's retail rates by more than the PACB's 2.5 percent threshold during any 12-month period.

PRINCIPAL ASSUMPTIONS AND CONSIDERATIONS

The results of the analyses performed in the preparation of this Independent Consultant's Report and the conclusions presented herein are predicated upon the general condition that the assumptions presented herein are reasonable and will continue, as stated, for the period covered by the analyses, without major modification or change. Although RMI believes the assumptions made are reasonable, RMI makes no representation that the assumed conditions will, in fact, occur. In this connection, RMI's conclusions may be affected favorably or unfavorably by unforeseen future events, and therefore, to the extent conditions differ from those assumed herein, the results that will be achieved by LIPA will vary from those forecast. In addition, RMI's studies, analyses, investigations, and projections have been based upon its understanding of certain documents and information provided to RMI by LIPA, LIPA's legal, financial, and accounting advisors, LILCO, and others, and include, but are not limited to, the documents listed in Exhibit 14 to this Report. While RMI believes these sources to be reliable, except as otherwise noted herein, they have not been independently verified for either accuracy or validity, and no assurances are offered with respect thereto. To the best of RMI's knowledge, the data and summaries presented herein accurately reflect the information furnished to RMI by LIPA, LIPA's legal, financial, and accounting advisors, LILCO, and others. Further, RMI has assumed that all contracts, agreements, or ordinances which have been relied upon in the conduct of its investigations will be fully enforceable in accordance with their terms and conditions. RMI makes no representations or warranties, and provides no opinion concerning the enforceability or legal interpretations of such contractual and legal requirements.

The assumptions on which this Independent Consultant's Report is based include, but are not limited to, the following:

1. LIPA will issue the Bonds, the Subordinated Indebtedness, and the Additional Bonds as necessary to complete the purchase of LILCO, the refinancing of LILCO debt retained by LIPA Sub, and such other purposes as set forth in Exhibit 5. The Bonds and the Subordinated Indebtedness will require debt service payments as set forth in Exhibit 1.

2. LIPA, through a subsidiary of LIPA, will purchase all outstanding shares of LILCO common stock in accordance with the terms of the Agreements.

3. BL Holding Corp and its subsidiaries will carry out their obligations in accordance with the terms of the Agreements and the Promissory Notes.

4. LIPA will fund repairs, renewals, and replacements to the T&D System, and the Manager will make such repairs, renewals, and replacements in accordance with prudent utility practices and the MSA, as may be required to continue the safe and reliable operation of the T&D System.

5. New power supply resources will be available at the times and in the amounts shown in Exhibits 7 and 8 to meet the electric capacity and energy requirements of LIPA's customers, with adequate reserves for reliability.

6. LIPA's capacity and energy requirements, including the impacts of DSM, will increase as projected in Exhibits 7 and 8.

7. LIPA will retain staff, advisors, and consultants, as necessary, to carry out its responsibilities for financing, contract administration, planning, public relations, and other matters in connection with the ownership, operation, and maintenance of the Retained Assets.

8. LIPA, Suffolk County, and the other Shoreham taxing jurisdictions will implement the terms of the Shoreham Settlement as discussed in the section entitled "RATES AND CHARGES —Shoreham Tax Matters" in the Official Statement and as reflected in LIPA's retail rates.

9. LIPA will approve reasonable capital expenditures by GENCO, and GENCO will make repairs, renewals, and replacements in accordance with prudent utility practice and the PSA, as may be required to continue the reliable operation of GENCO's generating facilities.

10. All NMP2 co-tenants will provide operating and capital funds in a timely manner as needed to maintain the reliable, cost effective operation of NMP2 and to meet applicable regulations, including environmental and safety standards.

11. LILCO will indemnify LIPA against all liabilities arising from all MGP operations and LIPA will have no financial responsibility for the remediation or other correction of contamination from any MGP site operation, nor liabilities associated with environmental contamination on, or emanating from, previous LILCO gas system properties or facilities.

12. Natural gas transportation facilities to deliver gas to and within the Service Area will be maintained, improved, and expanded to enable operation of the on-island generating facilities as forecast by LILCO in its resource planning calculations and as provided in the PSA for the GENCO facilities, as well as for the IPPs and NYPA Flynn plant, for the Study Period.

13. LIPA will incur fuel and purchased power expenses, including escalation thereon, as set forth in Exhibit 1.

14. Third party costs, PILOTs, incentive payments, and escalation rates for labor and other costs, as applicable, associated with the MSA, PSA, and EMA will be as reflected in Exhibit 1.

15. At Closing, LIPA will gain title to the balance of $17.7 million in LILCO's external decommissioning fund for the contaminated portion of NMP2.

16. LIPA's share of NMP2 decommissioning costs will increase from ABZ's estimate of 1996 costs at 3.0 percent per year and will be funded through annual deposits by LIPA of approximately $3.0 million and $1.2 million for the contaminated and non-contaminated portions, respectively, of NMP2. Annual earnings on the decommissioning funds held by or on-behalf of LIPA will average 5.0 percent.

17. LIPA will establish and maintain the Rate Stabilization Fund at the levels shown in Exhibit 1 of this Report. The Rate Stabilization Fund will be funded through cash available at Closing, net revenues from operations, and proceeds of Bonds and Additional Bonds issued to finance the Shoreham Settlement.

18. The Rate Stabilization Fund will be used for the purposes and in the amounts shown in Exhibit 1 of this Report for the Study Period.

19. LIPA will earn interest on its available funds as reflected in Exhibit 1.

20. LIPA will adopt electric rates that provide debt service coverage levels at least equal to the minimum requirements set forth in the General Bond Resolution.

21. Consistent with LIPA's understanding of the PACB conditions, increases in the cost of electricity paid by LIPA's customers related to the Shoreham Settlement, the RICO Credit, and pass-through adjustments, such as the FPPCA, will not be considered in determination of LIPA's rate increases, or average rate reductions, for the purposes of compliance with certain conditions established by the PACB in its July 16, 1997 resolution, which require ten-year average rate reductions of no less than 14 percent, and require the approval of the NYPSC for rate increases during any 12-month period in excess of 2.5 percent.

22. GENCO will obtain final approval from FERC for the PSA, including the rates accepted by FERC subject to refund as of February 12, 1998.

23. Upon expiration or termination of the MSA and the EMA, LIPA will lease, purchase, or otherwise obtain rights to the use of the common facilities owned by BL Holding Corp. and used by the Manager and the Energy Manager to carry out their duties under the MSA and EMA, respectively, at costs which will be at or below the costs for such use reflected in the charges for the MSA and EMA.

24. LIPA will adopt a final customer choice plan consistent with the principles described in the section "INDUSTRY RESTRUCTURING ISSUES—LIPA's Plan for Retail Choice" in this Report.

25. There will be no changes in applicable federal, State, or local laws that will establish new limits on the operation and maintenance of the GENCO or NYPA Flynn generating facilities during the Study Period.

26. LIPA will maintain regulations, policies, procedures, and rates and charges which will preclude the shifting of fixed costs among retail customers or rate classes as a result of individual customers or groups of customers electing to select power suppliers other than LIPA.

27. LIPA will retain the FPPCA through at least the end of the Study Period and will use it to recover variations in the average cost of fuel, purchased power, and load reduction program costs from LIPA's electric customers.

28. There will be no changes in regulations or policies of federal, State, or local agencies with jurisdiction over NMP2 that will cause new capital additions or operation and maintenance costs to exceed the estimated amounts of such costs reflected in Exhibit 1 of this Report.

29. Niagara Mohawk will be successful in maintaining the recent historical annual capacity factors at NMP2 and in addressing all generic issues, including the reactor internals crackling issue, within the NMP2 plant modification budget forecast. NMP2's regulatory performance will be sufficient to make increased NRC regulation of NMP2 unnecessary.

30. The Participant's Proposal to form the ISO will be approved by FERC in substantially the form submitted to FERC.

31. LIPA will not be precluded from being the sole supplier of electric transmission and distribution services due to the lapse or expiration of LILCO's electric service franchises prior to Closing.

32. The LILCO/KeySpan Combination will occur on or immediately after the Closing Date.

33. LIPA will issue the Bonds, and the Subordinated Indebtedness in the amounts and at the times shown in Exhibit 5 of this Report and annual debt service payments on the Bonds and the Subordinated Indebtedness will be as estimated by LIPA's financial advisor and shown in Exhibit 1.

34. LIPA will realize earnings on its invested funds, including the decommissioning funds, equal to the interest rates provided by LIPA's financial advisor.

35. Any legislation enacted by the federal government that provides for the restructuring of the electric utility industry will not preclude the use of tax-exempt debt by LIPA for the acquisition of LILCO, the funding of the Shoreham Settlement, the funding of capital improvements, or for other purposes contemplated during the Study Period and will not preclude LIPA from owning or operating the Retained Assets as contemplated in this Report.

CONCLUSIONS

On the basis of the foregoing considerations and assumptions and studies and analyses, RMI concludes that:

1. The Retained Assets, in combination with the common plant, the rights of LIPA under the Agreements, and the obligations of BL Holding Corp and its affiliates, provide LIPA with the facilities, labor, management, and related resources required to operate and maintain the T&D System in accordance with prudent utility practices and the requirements of the General Bond Resolution and the Subordinated Bond Resolution.

2. The reliability of the T&D System, as measured by the Customer Average Interruption Duration Index, has improved dramatically during the last three years as the result of programs undertaken by LILCO and is equal to or better than the corresponding reliability levels of the transmission and distribution systems of the other five large electric utilities in the State of New York with predominately overhead electric transmission and distribution systems.

3. The T&D System is in good condition and, with maintenance and capital expenditures at levels reflected in Exhibit 1 of this Report, can be operated throughout the Study Period at levels of reliability consistent with those experienced by the T&D System in the past three years. With continued maintenance and capital expenditures in accordance with prudent utility practice, the T&D System can reasonably be expected to achieve levels of reliability beyond 2008 that are comparable to those experienced during the Study Period.

4. Based upon NRC documents, FERC Form 1 filings, LILCO and Niagara Mohawk Annual Reports to the NYPSC, and interviews with (i) LILCO NMP2 oversight staff; and (ii) the non-operating co-tenants' representatives, RMI is not aware of regulatory compliance or operational problems with NMP2 which would result in operating costs or capital expenditures materially different from those reflected in the estimated Operating Results as set forth in Exhibit 1 in this Report or which would jeopardize the operation of NMP2 through the end of its operating license.

5. LIPA's anticipated annual transfers to the NMP2 decommissioning fund, combined with the balances in such fund as of December 31, 1997, and interest accruals thereon, will be sufficient to satisfy LIPA's share of the forecast of NMP2 decommissioning costs prepared during 1995 on behalf of Niagara Mohawk by ABZ Inc.

6. NMP2's non-fuel operation and maintenance costs, as reflected in Exhibit 1 of this Report, are comparable to the costs incurred at nuclear plants of similar design and vintage and can be expected to remain within the range of peer group costs throughout the Study Period. With maintenance and capital expenditures in accordance with prudent utility practices, NMP2's non-

fuel operation and maintenance costs can reasonably be expected to continue within this range, adjusted for general inflation rates, beyond 2008.

7. Existing and additional power supply resources will be available to reliably meet the electric capacity and energy requirements of the T&D System for the Study Period.

8. Based on FERC Form 1 filings, LILCO operations and maintenance reports, interviews with LILCO staff, and RMI's observations of the GENCO generating unit sites and facilities, RMI is not aware of regulatory compliance or operational problems with the GENCO generating units which would result in operating costs or capital expenditures materially different from those reflected in the estimated Operating Results shown in Exhibit 1 of this Report or which would jeopardize the operation of the GENCO generating units for the duration of the 15 year PSA.

9. With reasonable capital improvements and maintenance levels, as reflected in the estimated Operating Results, the GENCO facilities as a group will be able to operate near their present rated capacity and near their recent availability levels for the duration of the 15-year PSA.

10. In accordance with the provisions of the EMA, the Energy Manager will to be able to secure sufficient natural gas and fuel oil supplies, transportation, and storage to deliver fuel to the GENCO generating units on behalf of LIPA as necessary to operate the GENCO plants at the rates of production, and at the times needed, to achieve the energy production assumed in the projected Operating Results in this Report.

11. The staff and management personnel employed by the Manager, GENCO, and the Energy Manager have, as a whole, extensive and varied experience operating and maintaining the Retained Assets and the GENCO facilities, are highly qualified to perform the duties required of them by LIPA, and will be able to fulfill their obligations under the Agreements, including the MSA, PSA, and EMA.

12. Through a combination of its own staff, outsourced professional services, and the Trustees' guidance, LIPA will be able to provide appropriate policy, financial, and management control over the Manager, GENCO, and Energy Manager to operate and maintain the T&D System in accordance with prudent utility practices and to secure adequate power supply resources for LIPA's customers, all at expenditure levels consistent, on average, with those reflected in the estimated Operating Results set forth in Exhibit 1.

13. Incentives contained in the MSA provide an economic inducement for the Manager to maintain reliable service, read meters accurately and on a timely basis, answer customer calls promptly and respond effectively, and protect worker safety. When taken together, these incentives are expected to be sufficient to provide meaningful inducement to manage the T&D System and to successfully achieve the targeted levels of performance contained in the MSA.

14. LIPA can reasonably expect that there will be competition for the continuation of the types of services provided by the Manager under the MSA following its term, and that it will be able to retain a qualified manager of the T&D System at costs comparable to the fees paid the Manager under the MSA.

15. LIPA's implementation of a retail choice program will not adversely impact net revenues pledged to the repayment of the Bonds and the Subordinated Indebtedness.

16. Self-generation, in addition to that already in operation, is unlikely to result in a material reduction in LIPA's revenues available for debt service.

17. Formation of new municipal utilities on Long Island is not expected to occur due to the risk and expense of undertaking such municipalization efforts and the lack of reasonable

expectation of electric customer rate savings from municipalization, as compared to the Average System Rates to be charged by LIPA.

18. Conversion of existing electric end uses to natural gas is not likely to occur at levels that will materially affect the estimate of LIPA's annual capacity and energy requirements set forth in Exhibits 7 and 8.

19. Based upon information provided by LILCO and independent review performed by and on behalf of RMI, expected insurance proceeds and indemnification by BL Holding Corp, together with other available moneys, provide LIPA access to funding levels consistent with prudent utility practice to remove environmental liabilities arising during the Study Period associated with the Retained Assets which are known or suspected at the time of Closing.

20. The FPPCA provides an effective and consistent mechanism for recovering fuel, purchased power, and load reduction program cost variations from LIPA's electric customers.

21. Revenues from the sale of electricity and from other sources will be sufficient to meet LIPA's annual revenue requirements, including debt service and debt service coverage requirements on the Bonds and the Subordinated Indebtedness during the Study Period.

22. Absent emergency conditions and extraordinary unforeseeable events, LIPA is expected to achieve average rate reductions of no less than 14 percent over a ten year period commencing on the date when LIPA begins providing electric service, when measured against LILCO's base rates in effect July 16, 1997. These reductions exclude the impacts of pass-through adjustments such as those associated with the proposed Shoreham Settlement, the RICO Credit, and the FPPCA.

23. As shown in Exhibit 1, LIPA is not expected to implement an increase in average customer rates exceeding 2.5 percent over a 12 month period, within the Study Period.

24. LIPA will be able to comply with the conditions of the July 16, 1997, PACB resolution approving the Agreements.

25. The assumptions upon which the estimated Operating Results shown in Exhibit 1 of this Report are based are reasonable for the purposes for which they have been relied on.

Exhibit 1

Long Island Power Authority
Projected Operating Results
($000)

	1998(1)	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
RETAIL ELECTRICITY SALES (GWH)	10,047	16,678	16,960	17,257	17,466	17,701	17,880	18,060	18,277	18,483	18,670
REVENUE											
Retail Sales Revenues (Tariff Rates)(2)	$1,330,445	$2,118,010	$2,153,741	$2,191,524	$2,218,080	$2,270,370	$2,316,269	$2,362,968	$2,415,239	$2,466,937	$2,516,775
RICO Credit(3)	(38,387)	(60,000)	(25,000)	—	—	—	—	—	—	—	—
Shoreham Settlement Surcharge (Credit)(4)	(49,213)	(84,365)	(84,365)	(84,365)	(84,365)	(16,250)	24,595	33,439	42,282	51,126	51,126
Fuel and Purchased Power Cost Adjustment(5)	—	—	(1,001)	—	—	3,326	56,602	53,322	86,132	105,447	115,104
Total Retail Sales Revenues	$1,242,846	$1,973,646	$2,043,375	$2,107,159	$2,133,715	$2,257,446	$2,397,467	$2,449,728	$2,543,653	$2,623,510	$2,683,004
Miscellaneous Revenues(6)	5,133	9,186	9,587	10,008	10,453	10,817	11,196	11,592	12,004	12,434	12,882
Total Revenues	$1,247,979	$1,982,832	$2,052,962	$2,117,167	$2,144,168	$2,268,263	$2,408,663	$2,461,320	$2,555,657	$2,635,944	$2,695,887
REVENUE REQUIREMENTS											
Operating Expenses											
Nine Mile Point 2 Expenses(7)	$ 19,374	$ 35,478	$ 33,795	$ 35,097	$ 34,576	$ 35,868	$ 36,119	$ 37,444	$ 37,706	$ 39,106	$ 39,413
Fuel for GENCO Units(8)	174,196	276,442	292,051	307,282	290,243	295,869	305,791	317,283	326,873	336,921	317,768
Purchased Power Costs(9)	208,960	350,353	356,698	357,921	399,826	428,491	424,492	452,064	470,567	477,422	550,035
GENCO Power Costs(10)	177,735	307,062	310,881	315,943	320,633	324,702	329,940	336,516	344,880	358,341	376,359
Energy Management Services(11)	934	2,065	2,590	2,892	3,153	3,649	4,081	4,289	4,399	4,469	4,541
Total Power Supply Costs	$ 581,199	$ 971,401	$ 996,014	$1,019,134	$1,048,431	$1,088,578	$1,100,422	$1,147,597	$1,184,425	$1,216,259	$1,288,116
T&D Management Services(12)	$ 158,139	$ 268,022	$ 263,710	$ 271,211	$ 270,981	$ 271,318	$ 273,928	$ 278,803	$ 283,293	$ 290,943	$ 297,112
Other Operating and Maintenance Costs(13)	34,364	55,954	57,429	58,911	61,895	64,979	65,038	65,122	66,267	67,428	68,599
Total Operating Expenses	$ 773,702	$1,295,377	$1,317,154	$1,349,257	$1,381,307	$1,424,875	$1,439,388	$1,491,522	$1,533,984	$1,574,630	$1,653,826
Net Operating Revenue	$ 474,277	$ 687,454	$ 735,808	$ 767,910	$ 762,861	$ 843,388	$ 969,275	$ 969,798	$1,021,673	$1,061,314	$1,042,060
Other (Income) and Deductions											
Interest Income(14)	$ (8,264)	$ (18,405)	$ (16,751)	$ (16,505)	$ (16,285)	$ (16,258)	$ (19,610)	$ (19,188)	$ (19,961)	$ (20,466)	$ (19,739)
Funding for RICO Credit(15)	(36,401)	(56,896)	(23,707)	—	—	—	—	—	—	—	—
BL Holding Corp Promissory Notes Receipts(16)	(34,090)	(465,180)	(39,199)	(39,199)	(39,199)	(39,199)	(39,199)	(39,199)	(66,414)	(37,158)	(37,158)
Payments in Lieu of Taxes(17)	117,582	276,712	279,369	282,214	283,427	294,149	311,476	323,947	338,974	353,873	367,662
Total Other (Income) and Deductions	$ 38,828	$ (263,769)	$ 199,712	$ 226,510	$ 227,943	$ 238,692	$ 252,666	$ 265,560	$ 252,599	$ 296,249	$ 310,765
Debt Service Payments											
Base Level Senior Lien Debt(18)	$ 114,244	$ 367,875	$ 374,699	$ 383,649	$ 391,205	$ 413,627	$ 429,315	$ 445,020	$ 460,776	$ 476,655	$ 484,241
Mandatory Senior Debt Acceleration (19)	—	35,535	37,100	38,825	40,730	42,785	44,970	47,285	49,790	52,480	55,340
Total Senior Lien Debt	$ 114,244	$ 403,410	$ 411,799	$ 422,474	$ 431,935	$ 456,412	$ 474,285	$ 492,305	$ 510,566	$ 529,135	$ 539,581
Subordinate Debt(20)	33,750	67,500	67,500	67,500	67,500	67,500	67,500	67,500	67,500	67,500	67,500
Interest on Assumed LILCO Debentures(21)	14,763	—	—	—	—	—	—	—	—	—	—
Reimbursable Debt(22)	34,090	465,180	39,199	39,199	39,199	39,199	39,199	39,199	66,414	37,158	37,158
Total Scheduled Debt Service Payments	$ 196,847	$ 936,090	$ 518,498	$ 529,173	$ 538,634	$ 563,111	$ 580,984	$ 599,004	$ 644,480	$ 633,793	$ 644,239
Interest Savings on Defeased Debt(23)	$ —	$ —	$ (7,505)	$ (13,403)	$ (19,330)	$ (24,696)	$ (28,248)	$ (37,444)	$ (45,451)	$ (54,993)	$ (65,445)
Net Debt Service Payments	$ 196,847	$ 936,090	$ 510,993	$ 515,770	$ 519,303	$ 538,415	$ 552,736	$ 561,560	$ 599,029	$ 578,800	$ 578,793
Total Revenue Requirements	$1,009,377	$1,967,699	$2,027,859	$2,091,537	$2,128,554	$2,201,982	$2,244,790	$2,318,641	$2,385,612	$2,449,679	$2,543,385
Net Cash Flow from Operations	$ 238,602	$ 15,133	$ 25,103	$ 25,630	$ 15,614	$ 66,281	$ 163,873	$ 142,679	$ 170,045	$ 186,265	$ 152,502

Note: Totals may not add due to rounding.

Exhibit 1

Long Island Power Authority
Projected Operating Results
($000)

	1998(1)	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
CALCULATION OF RATE STABILIZATION FUND BALANCE											
Beginning Balance(24)	$ —	$ 288,602	$ 249,990	$ 250,004	$ 250,004	$ 250,013	$ 252,984	$ 252,992	$ 252,991	$ 252,995	$ 253,001
Initial Fund Deposit(25)	71,000	—	—	—	—	—	—	—	—	—	—
Net Accounts Payable(26)	(101,000)	—	—	—	—	—	—	—	—	—	—
Net Cash Flow from Operations(27)	238,602	15,133	25,103	25,630	15,614	66,281	163,873	142,679	170,045	186,265	152,502
Shoreham Settlement Bond Proceeds(28)	80,000	80,000	80,000	80,000	80,000	—	—	—	—	—	—
Draw for Optional Accelerated Principal Repayment(29)	—	(133,745)	(105,090)	(105,630)	(95,605)	(63,310)	(163,865)	(142,680)	(170,040)	(186,260)	(152,525)
Ending Balance(30)	$ 288,602	$ 249,990	$ 250,004	$ 250,004	$ 250,013	$ 252,984	$ 252,992	$ 252,991	$ 252,995	$ 253,001	$ 252,977
DEBT SERVICE COVERAGE											
Net Cash Flow from Operations(27)	$ 238,602	$ 15,133	$ 25,103	$ 25,630	$ 15,614	$ 66,281	$ 163,873	$ 142,679	$ 170,045	$ 186,265	$ 152,502
Add Back:											
Payments in Lieu of Taxes(17)	117,582	276,712	279,369	282,214	283,427	294,149	311,476	323,947	338,974	353,873	367,662
Shoreham Settlement Bond Proceeds(28)	80,000	80,000	80,000	80,000	80,000	—	—	—	—	—	—
Total Debt Service Payments(27)	196,847	936,090	518,498	529,173	538,634	563,111	580,984	599,004	644,480	633,793	644,239
Less Interest Savings on Defeased Debt(27)	—	—	(7,505)	(13,403)	(19,330)	(24,696)	(28,248)	(37,444)	(45,451)	(54,993)	(65,445)
Total Available for Coverage	$ 633,032	$1,307,936	$ 895,465	$ 903,614	$ 898,345	$ 898,845	$1,028,084	$1,028,186	$1,108,048	$1,118,939	$1,098,957
Senior Lien Debt Service(31)	$ 114,244	$ 403,410	$ 404,294	$ 409,071	$ 412,604	$ 431,716	$ 446,037	$ 454,861	$ 465,115	$ 474,142	$ 474,135
Coverage on LIPA Senior Lien Debt Service	5.5	3.2	2.2	2.2	2.2	2.1	2.3	2.3	2.4	2.4	2.3
Senior Lien and Subordinated Debt Service	$ 147,994	$ 470,910	$ 471,794	$ 476,571	$ 480,104	$ 499,216	$ 513,537	$ 522,361	$ 532,615	$ 541,642	$ 541,635
Coverage on Senior Lien and Subordinated Debt	4.3	2.8	1.9	1.9	1.9	1.8	2.0	2.0	2.1	2.1	2.0
Total Debt Service(32)	$ 196,847	$ 936,090	$ 510,993	$ 515,770	$ 519,303	$ 538,415	$ 552,736	$ 561,560	$ 599,029	$ 578,800	$ 578,793
Coverage on Total Debt	3.2	1.4	1.8	1.8	1.7	1.7	1.9	1.8	1.8	1.9	1.9

Note: Totals may not add due to rounding.

Exhibit 1

Long Island Power Authority
Projected Operating Results
($000)

	1998(1)	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
ANALYSIS OF REVENUE											
Retail Electricity Sales (GWH)	10,047	16,678	16,960	17,257	17,466	17,701	17,880	18,060	18,277	18,483	18,670
Retail Sales Revenues (Tariff Rates)(33)	$1,330,445	$2,118,010	$2,153,741	$2,191,524	$2,218,080	$2,270,370	$2,316,269	$2,362,968	$2,415,239	$2,466,937	$2,516,775
Average Annual Revenue per kWh (cents)(34)	12.70	12.70	12.70	12.70	12.70	12.83	12.95	13.08	13.21	13.35	13.48
Year to Year Rate Increases		0.0%	0.0%	0.0%	0.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%
Percent Reduction from LILCO Rates(35)	16.6%	16.6%	16.6%	16.6%	16.6%	15.8%	14.9%	14.1%	13.2%	12.4%	11.5%

Exhibit 1

Long Island Power Authority
Projected Operating Results

NOTES:

(1) June 1 through December 31, 1998.
(2) Based on average revenue per kWh shown on Page 3 of this Exhibit.
(3) Paid in accordance to the settlement between LILCO and its ratepayers. Includes effect of gross receipts tax.
(4) Paid in accordance with the Shoreham Settlement. Includes effect of gross receipts tax
(5) Calculated in accordance with the FPPCA.
(6) These include revenues such as street light rents, late payment charges, and dishonored check charges.
(7) Includes nuclear fuel expense, operation and maintenance expense, and funding for decommissioning.
(8) LIPA's cost for oil and natural gas.
(9) Includes cost of purchased capacity and energy (excluding costs incurred under the PSA), and transmission costs net of wholesale wheeling revenues. These costs are paid directly by LIPA.
(10) In accordance with the PSA including an allowance for incentive payments.
(11) In accordance with the EMA including an allowance for incentive payments.
(12) In accordance with the MSA including an allowance for incentive payments.
(13) Includes general and administrative costs.
(14) Interest earnings on bond proceeds for construction purposes until the proceeds are spent and interest earnings on the Rate Stabilization Fund. Interest earnings rate assumed to be 5 percent per annum.
(15) BL Holding Corp provides the funds for the RICO Credit net of gross receipts tax.
(16) Receipts from BL Holding Corp Promissory Notes held by LIPA for repayment of certain assumed debt (see note 22).
(17) These include payments to various taxing jurisdictions for NMP2, the T&D System, and Shoreham property taxes, gross receipts taxes and Metropolitan Transportation Authority surcharge.
(18) Includes the portion of the Bonds that are not accelerated (see note 19) and the Additional Bonds. Bonds issued during tranche 1 are assumed to bear interest at 5.72 percent. Bonds issued during tranches 2 and 3 are assumed to bear interest at 6.0 percent. Additional Bonds issued to finance the Shoreham Settlement are assumed to bear interest at 6.5 percent per year. All other Additional Bonds are assumed to bear interest at 6.25 percent per year.
(19) Scheduled accelerated payments of the Bonds. Please refer to the section entitled "ACCELERATED DEBT RETIREMENT" in the Official Statement.
(20) Variable rate debt assumed at 4.5 percent including line of credit and remarketing.
(21) Interest payments due on debentures assumed from LILCO prior to refinancing by LIPA.
(22) Debt for which BL Holding Corp is obligated to pay. Please refer to Part 1 of the Official Statement, "PURPOSE OF THE OFFERED SECURITIES AND THE INITIAL SUBORDINATED INDEBTEDNESS—Debt Service."
(23) The interest savings on principal that is paid early through the optional accelerated principal repayment (See Note 29).
(24) Ending balance from the prior year.
(25) Cash received at Closing.
(26) Contractual level of initial accounts payable.
(27) From Exhibit 1, page 1 of 4.
(28) Proceeds of Bonds and Additional Bonds issued to finance the Shoreham Settlement (see note 4).
(29) Amount to be applied to accelerated repayment of debt, as supplied by financial advisor, and as shown in the "Calculation of Rate Stabilization Fund Balance" section of this Exhibit.
(30) Balance in the Rate Stabilization Fund on December 31 of each year.
(31) Senior lien debt, less interest savings on defeased debt, from Exhibit 1, page 1 of 4.
(32) Includes senior lien debt, subordinated indebtedness, and reimbursable debt.
(33) Excludes impact of RICO Credit, Shoreham Settlement, and the FPPCA.
(34) Average unit revenue for 1998 is annualized.
(35) Rate reduction computed from LILCO's rates in effect July 16, 1997 (the date of the PACB's approval of the Agreements), which rates remain in effect today. Ten year average reduction is 15.1 percent. Both LILCO's rates and LIPA's rates exclude the impact of pass-through adjustments and RICO credits.

Note: Totals may not add due to rounding.

Exhibit 2

LONG ISLAND LIGHTING COMPANY
HISTORICAL CUSTOMER STATISTICS(1)

	1993	1994	1995	1996	1997
Number of Customers(2)					
Residential					
General	835,214	837,605	844,837	851,523	858,443
Other	70,783	70,885	70,325	69,407	68,435
Total Residential	905,997	908,490	915,162	920,930	926,878
Commercial and Industrial					
Small General	46,009	46,067	46,110	46,066	46,548
Large General	41,526	41,437	42,427	43,122	43,533
Large General and Industrial	3,548	3,690	3,825	3,947	4,075
Space Heating	5,018	4,953	4,942	4,939	4,909
Other	6,153	6,343	6,365	6,414	6,493
Total Commercial and Industrial	102,254	102,490	103,669	104,488	105,557
Public Lighting	4,423	4,453	4,419	4,465	4,563
Other Sales to Public Authorities	125	127	127	127	127
Interdepartmental	—	—	—	—	—
Total Number of Customers	1,012,799	1,015,560	1,023,377	1,030,010	1,037,125
Sales of Electricity (MWh)(3)					
Residential					
General	6,058,376	6,061,692	6,112,456	6,134,366	6,181,087
Other	1,059,219	1,097,630	1,043,774	1,068,333	1,003,218
Total Residential	7,117,595	7,159,322	7,156,230	7,202,699	7,184,305
Commercial and Industrial					
Small General	337,020	343,880	335,945	325,061	325,270
Large General	2,764,067	2,765,227	2,801,241	2,766,609	2,778,588
Large General and Industrial	4,702,018	4,796,925	4,698,522	4,649,189	4,702,390
Space Heating	356,610	360,439	352,507	345,327	330,469
Other	97,219	127,665	147,605	156,171	200,109
Total Commercial and Industrial	8,256,934	8,394,136	8,335,820	8,242,357	8,336,826
Public Lighting	181,825	182,078	182,812	185,204	186,183
Other Sales to Public Authorities	267,786	274,445	277,132	256,023	229,807
Interdepartmental	6,492	8,716	3,129	8,236	4,186
Total Sales of Electricity	15,830,632	16,018,697	15,955,123	15,894,519	15,941,306

Exhibit 2

LONG ISLAND LIGHTING COMPANY
HISTORICAL CUSTOMER STATISTICS(1)

	1993	1994	1995	1996	1997
Revenues from Sales of Electricity ($000)(3)(4)					
Residential					
General	$ 995,723	$1,039,308	$1,048,142	$1,047,230	$1,058,795
Other	150,168	162,816	156,845	157,903	150,611
Total Residential	$1,145,891	$1,202,124	$1,204,987	$1,205,133	$1,209,407
Commercial and Industrial					
Small General	$ 58,044	$ 62,270	$ 60,806	$ 58,730	$ 59,096
Large General	423,187	442,064	447,471	440,344	442,698
Large General and Industrial	580,654	615,278	607,246	598,260	607,690
Space Heating	52,555	55,503	54,498	53,164	51,578
Other	18,047	21,307	23,993	24,002	30,263
Total Commercial and Industrial	$1,132,487	$1,196,422	$1,194,014	$1,174,500	$1,191,325
Public Lighting	$ 20,275	$ 20,868	$ 21,191	$ 21,488	$ 21,750
Other Sales to Public Authorities	29,285	31,609	31,280	29,025	26,348
Interdepartmental	308	408	142	366	203
Total Revenues from Sales of Electricity	$2,328,246	$2,451,431	$2,451,614	$2,430,512	$2,449,032
Average Revenue Per KWh Sold (Dollars/kWh)					
Residential					
General	$ 0.1644	$ 0.1715	$ 0.1715	$ 0.1707	$ 0.1713
Other	0.1418	0.1483	0.1503	0.1478	0.1501
Total Residential	$ 0.1610	$ 0.1679	$ 0.1684	$ 0.1673	$ 0.1683
Commercial and Industrial					
Small General	$ 0.1722	$ 0.1811	$ 0.1810	$ 0.1807	$ 0.1817
Large General	0.1531	0.1599	0.1597	0.1592	0.1593
Large General and Industrial	0.1235	0.1283	0.1292	0.1287	0.1292
Space Heating	0.1474	0.1540	0.1546	0.1540	0.1561
Other	0.1856	0.1669	0.1625	0.1537	0.1512
Total Commercial and Industrial	$ 0.1372	$ 0.1425	$ 0.1432	$ 0.1425	$ 0.1429
Public Lighting	$ 0.1115	$ 0.1146	$ 0.1159	$ 0.1160	$ 0.1168
Other Sales to Public Authorities	0.1094	0.1152	0.1129	0.1134	0.1147
Interdepartmental	0.0474	0.0468	0.0454	0.0444	0.0485
Total Average Revenue per KWh Sold	$ 0.1471	$ 0.1530	$ 0.1537	$ 0.1529	$ 0.1536

(1) Amounts may not total exactly due to rounding.
(2) Average number of customers.
(3) Excludes Sales for Resale.
(4) Excludes unbilled service and RICO Credit. Includes FPPCA revenues.

Exhibit 3

ESTIMATED CAPITAL EXPENDITURES
($000)

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Capital Improvements(1)											
T&D System	$ 68,259	$123,394	$129,805	$123,026	$122,981	$126,325	$129,761	$133,288	$136,912	$140,633	$144,454
NMP2(2)	1,931	3,524	11,947	4,122	11,796	4,139	11,850	4,139	11,850	4,139	11,850
Conservation/DSM (3)	2,957	4,927	4,747	5,515	4,345	—	—	—	—	—	—
Total Capital Improvements	$ 73,147	$131,845	$146,499	$132,663	$139,122	$130,464	$141,611	$137,427	$148,762	$144,772	$156,304
Increases in Working Capital	$ —	$ 4,412	$ 7,916	$ 3,652	$ 5,879	$ 4,738	$ 4,779	$ 5,026	$ 5,619	$ 6,282	$ 6,282
Acquisition Requirements											
Purchase of LILCO Common Stock	$2,497,500	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Redemption of LILCO Preferred Stock	339,100	—	—	—	—	—	—	—	—	—	—
Debt Refinancing	3,609,058	—	—	—	—	—	—	—	—	—	—
Total Acquisition Requirements	$6,445,658	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Shoreham Settlement	$ 109,167	$ 80,000	$ 80,000	$ 80,000	$ 80,000	$ 33,333	$ —	$ —	$ —	$ —	$ —
Deposit to Clean Energy Fund(4)	$ 20,000	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Deposit to Ratepayer Advocacy Fund	$ 1,000	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
New York State Reimbursement	$ 33,000	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Total Capital Expenditures(5)	$6,681,972	$216,257	$234,415	$216,315	$225,001	$168,535	$146,390	$142,453	$154,381	$151,054	$162,586

(1) Estimated values for 1998 assume seven months of ownership by LIPA.

(2) Eighteen percent share of total NMP2 capital expenditures. Includes the capital cost of nuclear fuel purchased in each year. Nuclear fuel purchases are capitalized and expensed based on generation levels at NMP2.

(3) Excludes conservation/DSM expenditures for program management and administration, and for load reduction program costs.

(4) Additional amounts beginning at approximately $12 million annually will be expensed by LIPA.

(5) Excludes the costs of issuance and other expenditures for the Bonds, the Subordinated Indebtedness, and the Additional Bonds.

Exhibit 4

GENCO GENERATING FACILITIES
SUMMARY DESCRIPTION

Facility	Nameplate Rating (MW)(1)	Summer Rating (MW)(2)	Fuel	Year of Commercial Operation	County
Steam Turbine					
E.F. Barrett 1,2	350	386	Gas, Oil	1956, 1963	Nassau
Far Rockaway 4	100	110	Gas, Oil	1953	Queens
Glenwood 4,5	200	223	Gas	1952, 1954	Nassau
Northport 2,4	750	771	Gas, Oil	1968-1977	Suffolk
Northport 1,3	750	750	Oil	1967-1972	Suffolk
Port Jefferson 3,4	350	385	Gas, Oil	1958, 1960	Suffolk
Subtotal	2,500	2,625			
Combustion Turbine					
E.F. Barrett 1-12	311	280	Gas, Oil	1970-1971	Nassau
Wading River	242	242	Oil	1989	Suffolk
East Hampton 1	21	20	Oil	1970	Suffolk
Glenwood 1-3	126	117	Oil	1967-1972	Nassau
Holtsville 1-10	567	510	Oil	1974-1975	Suffolk
Northport G-1	16	14	Oil	1967	Suffolk
Port Jefferson G-1	16	15	Oil	1966	Suffolk
Shoreham	72	67	Oil	1966, 1971	Suffolk
Southampton 1	12	11	Oil	1963	Suffolk
Southhold 1	14	13	Oil	1964	Suffolk
West Babylon 4	52	47	Oil	1971	Suffolk
Subtotal	1,449	1,336			
Internal Combustion					
East Hampton 2-4	6	6	Oil	1962	Suffolk
Montauk 2-4	6	6	Oil	1961	Suffolk
Subtotal	12	12			
Total	3,961	3,973			

(1) Source: LILCO's 1996 Annual Report to the NYPSC.

(2) Average DMNC for the period 1993 through 1997, adjusted to 93°F. Represents the combined rating for multiple unit stations

Exhibit 5

ESTIMATED FINANCING REQUIREMENTS
($000)

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Bonds(1)											
Capital Requirements(2)	$5,293,158	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Interest Rate Hedge	69,000	—	—	—	—	—	—	—	—	—	—
Issuance Costs(3)	175,676	—	—	—	—	—	—	—	—	—	—
Total Bonds	$5,537,834	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Subordinated Indebtedness											
Capital Requirements(2)	$1,484,000	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Issuance Costs(3)	16,000	—	—	—	—	—	—	—	—	—	—
Total Additional Bonds	$1,500,000	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Additional Bonds(4)											
Capital Requirements(2)(5)	$ —	$214,956	$224,752	$214,375	$215,350	$133,263	$136,739	$140,514	$144,730	$149,115	$153,936
Issuance Costs(3)	—	3,570	3,774	3,561	3,586	2,722	2,796	2,876	2,955	3,050	2,129
Total Bonds	$ —	$218,526	$228,526	$217,936	$218,936	$135,985	$139,535	$143,390	$147,685	$152,165	$156,065
Summary											
Capital Requirements(5)	$6,777,158	$214,956	$224,752	$214,375	$215,350	$133,263	$136,739	$140,514	$144,730	$149,115	$153,936
Interest Rate Hedge	69,000	—	—	—	—	—	—	—	—	—	—
Issuance Costs(3)	191,676	3,570	3,774	3,561	3,586	2,722	2,796	2,876	2,955	3,050	2,129
Total Issues	$7,037,834	$218,526	$228,526	$217,936	$218,936	$135,985	$139,535	$143,390	$147,685	$152,165	$156,065

(1) Bonds issued during the first three tranches, principally to finance the acquisition of LILCO, based upon the adopted Plan of Finance.

(2) Includes acquisition requirements, capital improvements, increases in working capital, Shoreham Settlement, and/or other related expenditures.

(3) Includes original issue discount, underwriter's discount, bond insurance, and/or other costs of issuance.

(4) Bonds issued principally to finance capital improvements and the Shoreham Settlement following the acquisition of LILCO.

(5) Excludes capital expenditures for NMP2 nuclear fuel purchases, which will be funded from net revenues.

Exhibit 6

HISTORICAL LOADS AND RESOURCES

	1993	1994	1995	1996	1997
Annual Peak Demand (Summer)(1)	3,967	3,882	4,077	3,610	4,140
Capacity (MW)(2)					
LILCO Generating Resources					
Steam	2,719	2,711	2,619	2,627	2,615
Nuclear(3)	188	187	203	205	205
Other	1,344	1,352	1,338	1,351	1,367
Total Generating Resources	4,251	4,250	4,160	4,183	4,187
Purchased Capacity(3)(4)	499	616	713	710	716
Total Capacity	4,750	4,866	4,873	4,893	4,903
Annual Reserve Margin					
MW	783	984	796	1,283	763
Percent	19.7%	25.3%	19.5%	35.5%	18.4%
Energy (MWh)					
Annual Energy Requirements					
Retail Requirements	17,232,766	17,302,091	17,266,798	17,179,744	17,197,532
Sales for Resale	304,057	372,083	620,021	527,360	418,584
Total Energy Requirements	17,536,823	17,674,174	17,886,819	17,707,104	17,616,116
LILCO Generating Resources					
Steam	9,084,524	8,365,488	9,256,730	8,606,806	9,549,059
Nuclear(3)	1,290,397	1,498,556	1,301,240	1,558,397	1,588,477
Other	138,659	170,021	185,523	154,212	245,222
Total Generating Resources	10,513,580	10,034,065	10,743,493	10,319,415	11,382,758
Purchased Energy(3)(4)	7,023,243	7,640,109	7,143,326	7,387,689	6,233,358
Total Energy Resources	17,536,823	17,674,174	17,886,819	17,707,104	17,616,116

(1) Includes firm sales for resale.
(2) Summer rating.
(3) Delivered to the T&D System.
(4) Includes non-utility generators, purchases, and credits.

Exhibit 7

ESTIMATED CAPACITY REQUIREMENTS AND RESOURCES
(MW)

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SYSTEM DEMAND											
Peak Demand(1)	4,220	4,290	4,355	4,425	4,485	4,540	4,590	4,640	4,695	4,750	4,795
Less: Cogeneration and NYPA Loads(2)	(90)	(91)	(92)	(93)	(96)	(97)	(98)	(99)	(100)	(101)	(102)
Net Demand after Cogeneration and NYPA Loads	4,130	4,199	4,263	4,332	4,389	4,443	4,492	4,541	4,595	4,649	4,693
Required Reserve Margin(3)	738	744	749	759	758	767	776	785	795	805	813
Required Minimum Capability	4,868	4,943	5,012	5,091	5,147	5,210	5,268	5,326	5,390	5,454	5,506
RESOURCES											
Generation											
GENCO Capacity	3,973	3,973	3,973	3,973	3,973	3,973	3,973	3,973	3,973	3,973	3,973
NMP2	205	205	205	205	205	205	205	205	205	205	205
Subtotal Generation	4,178	4,178	4,178	4,178	4,178	4,178	4,178	4,178	4,178	4,178	4,178
Non-Utility Generation											
Non-Dispatchable	212	212	212	212	212	212	212	212	212	212	212
Dispatchable (NYPA Flynn)	138	138	138	138	138	138	138	138	138	138	138
Subtotal Non-Utility Generation	350	350	350	350	350	350	350	350	350	350	350
Purchases											
Municipal Utilities	34	34	34	34	34	34	34	34	34	34	34
NYPA (Fitzpatrick)	160	160	160	160	160	160	160	160	160	160	160
NYPA (Gilboa)	50	50	50	50	50	50	50	50	50	50	50
NYPA (Power for Jobs)	21	43	64	64	64	64	—	—	—	—	—
NYPA (Reserve Credits)	25	25	25	25	25	25	25	25	25	25	25
Firm Purchases (4)	100	150	150	150	150	150	200	200	150	200	50
New Generation Capacity(5)	—	—	—	—	—	144	144	288	288	288	507
Subtotal Purchases	390	462	483	483	483	627	613	757	707	757	826
DSM	28	65	100	116	180	181	181	180	180	179	175
Total Capability	4,946	5,055	5,111	5,127	5,191	5,336	5,322	5,465	5,415	5,464	5,529
Reserve Margin (6)	19.9%	20.7%	20.4%	18.9%	19.1%	21.0%	19.3%	21.2%	18.6%	18.2%	18.5%

(1) Before effect of cogeneration and DSM.
(2) Includes customer cogeneration and loads served by NYPA.
(3) Equals 18 percent of net demand after cogeneration and NYPA loads, net of DSM.
(4) Assumed firm purchases from off-island suppliers.
(5) Assumed capacity purchases from new on-island generation units.
(6) Calculation of reserve margin excludes DSM in demand and resource.

Exhibit 8

ESTIMATED ENERGY REQUIREMENTS AND RESOURCES
(MWh)

	1998(1)	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
ENERGY REQUIREMENTS											
System Energy Requirements(2)	18,329,080	18,684,140	19,010,992	19,338,230	19,594,302	19,857,984	20,056,724	20,255,358	20,494,658	20,721,816	20,914,786
NYPA Loads(3)	(167,000)	(171,000)	(169,000)	(153,000)	(161,000)	(161,000)	(161,000)	(161,000)	(161,000)	(161,000)	(161,000)
Cogeneration Loads	(464,000)	(471,000)	(479,000)	(486,000)	(493,000)	(500,000)	(507,000)	(514,000)	(521,000)	(528,000)	(535,000)
Off-System Sales(4)	333,756	249,660	298,656	297,840	297,840	297,840	298,656	297,840	297,840	297,840	298,656
Total Energy Requirements	18,031,836	18,291,800	18,661,648	18,997,070	19,238,142	19,494,824	19,687,380	19,878,198	20,110,498	20,330,656	20,517,442
ENERGY RESOURCES											
Generation											
GENCO Capacity	8,746,547	8,966,973	9,603,502	9,973,384	9,126,417	9,354,021	9,165,174	9,233,922	9,289,112	9,344,555	8,666,367
NMP2	1,276,825	1,494,686	1,277,443	1,494,686	1,276,825	1,412,246	1,280,694	1,412,245	1,276,827	1,412,247	1,280,696
Subtotal Generation	10,023,372	10,461,659	10,880,945	11,468,070	10,403,242	10,766,267	10,445,868	10,646,167	10,565,939	10,756,802	9,947,063
Non-Utility Generation											
Non-Dispatchable	1,763,504	1,760,384	1,762,010	1,756,177	1,759,223	1,760,888	1,765,325	1,759,256	1,742,228	1,736,630	1,740,878
Dispatchable (NYPA Flynn)	1,173,590	1,167,575	1,123,528	1,177,427	1,147,052	974,900	1,175,735	1,193,964	1,149,546	1,179,189	1,159,008
Subtotal Non-Utility Generation	2,937,094	2,927,959	2,885,538	2,933,604	2,906,275	2,735,788	2,941,060	2,953,220	2,891,774	2,915,819	2,899,886
Purchases											
Municipal Purchases	—	—	—	—	—	—	—	—	—	—	—
NYPA Purchase-Fitzpatrick	2,071,584	1,868,048	1,787,098	1,784,024	1,613,585	1,637,786	1,692,333	1,557,897	1,590,649	1,584,748	1,593,923
NYPA Purchase-Gilboa	(19,826)	(17,395)	(13,273)	(11,244)	(15,459)	(13,053)	(15,021)	(13,259)	(16,834)	(15,033)	(16,684)
NYPA Upstate Surplus(5)	194,019	109,859	118,262	94,044	88,517	79,896	106,883	83,586	88,953	75,323	77,678
Net Economy and Supplemental(6)	2,397,346	2,440,485	2,365,975	2,002,509	3,592,885	3,452,737	3,838,453	3,825,541	4,330,563	4,162,920	4,205,796
Firm Purchases	417,247	472,185	590,103	663,063	570,097	725,406	561,914	689,760	529,620	706,160	349,460
New On-Island	—	—	—	—	—	26,997	33,890	55,286	50,834	66,917	1,398,320
Subtotal Purchases	5,060,370	4,873,182	4,848,165	4,532,396	5,849,625	5,909,769	6,218,452	6,198,811	6,573,785	6,581,035	7,608,493
DSM(7)	11,000	29,000	47,000	63,000	79,000	83,000	82,000	80,000	79,000	77,000	62,000
Total Resources	18,031,836	18,291,800	18,661,648	18,997,070	19,238,142	19,494,824	19,687,380	19,878,198	20,110,498	20,330,656	20,517,442

(1) Reflects the full twelve months of the year.
(2) Before the effect of cogeneration and loads served by NYPA.
(3) Customers in the Service Area receiving energy from NYPA under existing NYPA programs.
(4) Off-system sales, excluding economy energy sales included under "Net Economy and Supplemental" Purchases.
(5) Excess energy associated with the Fitzpatrick plant.
(6) Short-term purchases net of economy energy sales.
(7) DSM savings resulting from measures implemented during the Study Period.

Exhibit 9

HISTORICAL GENCO GENERATION
(GWh)(1)

Generating Facility	1993	1994	1995	1996	1997
Steam Turbine					
E.F. Barrett 1,2	1,992.5	1,727.3	1,874.1	1,599.5	1,735.0
Far Rockaway 4	102.5	326.6	467.2	230.9	244.0
Glenwood 4,5	194.0	536.2	885.2	519.3	509.0
Northport 1-4	5,206.8	4,456.2	5,015.3	5,044.1	5,416.0
Port Jefferson 3,4	1,588.7	1,319.2	1,015.0	1,213.0	1,645.0
Total Steam Turbine	9,084.5	8,365.5	9,256.8	8,606.8	9,549.0
Combustion Turbine(2)					
E.F. Barrett 1-12	62.2	50.6	78.2	29.4	77.0
Wading River	21.3	46.0	43.6	79.1	86.0
East Hampton 1	3.0	5.3	4.6	2.3	6.0
Glenwood 1-3	1.5	4.3	3.0	5.7	6.0
Holtsville 1-10	48.5	59.1	49.7	32.5	63.0
Northport G-1	—	0.2	—	—	—
Port Jefferson GT	—	0.2	0.2	0.2	—
Shoreham 1-2	—	0.6	1.5	2.1	3.0
Southampton 1	0.2	0.5	0.3	0.2	1.0
Southhold 1	—	—	—	0.2	—
West Babylon 4	1.1	1.4	2.8	1.7	2.0
Total Combustion Turbine(2)	137.9	168.2	183.9	153.5	244.0
Internal Combustion					
East Hampton 2-4	0.5	1.1	1.1	0.4	—
Montauk 2-4	0.3	0.7	0.5	0.3	—
Total Internal Combustion	0.8	1.8	1.6	0.7	—
Total GENCO Resources	9,223.2	8,535.5	9,442.3	8,761.0	9,793.0

(1) Source: LILCO. Amounts may not total exactly due to rounding.

(2) The output of some units is too small to include in the list, but is included in the totals.

Exhibit 10

EXISTING POWER PURCHASE AGREEMENTS(1)

Type of Resource	Contract Expiration	Summer Contract Capacity (MW)	Calendar Year Energy Purchases (MWh) 1993	1994	1995	1996	1997
Independent Power Producers							
NYPA Flynn(2)	2014	138.4(3)	—	745,878	1,165,289	1,095,048	1,186,047
Hempstead Resource Recovery	2009	70.0	545,462	550,546	552,796	553,968	558,741
Trigen NDEC Combined Cycle	2016	43.7	388,984	385,564	389,113	374,791	423,732
Gruman Combined Cycle	2004	38.3	301,879	307,397	302,490	301,431	352,660
Huntington Resource Recovery	2012	22.9	145,467	146,503	144,182	158,678	162,588
Babylon Resource Recovery	2008	14.7	110,205	97,801	105,261	107,647	109,677
SUNY-Stony Brook Cogeneration(4)	2015	—	—	—	109,941	142,680	109,200
Islip Resource Recovery(5)	2010	8.9	51,786	54,594	45,760	50,598	57,784
Oceanside Landfill	2006	3.0	30,364	27,389	23,355	19,942	18,040
Long Beach Resource Recovery	2008	2.5	7,859	5,623	10,958	9,533	2,657
Islip Landfill	2004	1.7	19,935	17,538	12,661	10,529	4,248
Yaphank Landfill	2008	2.7	16,049	12,418	8,138	2,572	13,325
Bethpage Landfill (Oyster Bay)	2010	1.3	9,473	8,496	5,954	5,167	4,518
Smithtown Landfill	2010	1.1	7,317	8,959	8,190	5,904	4,969
South Oaks Hospital	2005	0.2	4,671	4,664	5,144	4,354	4,235
Other(6)		0.9	18,774	16,716	4,749	1,499	1,687
Subtotal Independent Power Producers		350.3	1,658,225	2,390,086	2,893,981	2,844,341	3,014,108
Municipal Utilities							
Freeport		21.0	—	—	—	N/A(8)	N/A(8)
Greenport		5.0	—	—	—	N/A(8)	N/A(8)
Rockville Centre		8.0	100	100	—	N/A(8)	N/A(8)
Subtotal Municipal Utilities		34.0	100	100	—	500	730
NYPA Off-Island							
Fitzpatrick & Gilboa		210.0	758,000	1,499,000	1,737,000	1,749,000	1,670,994
Reserve Credit (7)		25.0	—	—	—	—	—
Subtotal NYPA Off-Island		235.0	758,000	1,499,000	1,737,000	1,749,000	1,670,994
Total Power Purchases		619.3	2,416,325	3,889,186	4,630,981	4,593,841	4,685,832

(1) Data from NYPSC Annual Reports, FERC Form 1, and "1996 Load & Capacity Data Report of the Member Electric Systems of the NYPP."
(2) Commercial generation began in 1994.
(3) Net dependable capacity was uprated from 135.6 MW based on 1996 DMNC test results.
(4) Commercial operation began in 1995.
(5) The contract for the Islip Resource Recovery was terminated in 1998.
(6) Various small contracts.
(7) Capacity only.
(8) Detail not available.

Exhibit 11

SUMMARY OF CUSTOMER CHOICE PLANS IN NEW YORK STATE

	Central Hudson Gas & Electric Corporation	Consolidated Edison Company of New York, Inc.	New York State Electric and Gas Corporation	Niagara Mohawk Power Corporation	Orange & Rockland Utilities, Inc.	Rochester Gas & Electric Corporation
Start of Retail Choice	No later than early 1998	Full Phase-In beginning June 1, 1998	Phase-In beginning with the Dairylea pilot during 11/97	Phase-In beginning with the Dairylea pilot during 11/97	Phase-In beginning with expansion of POWERPICK	Phase-In beginning July 1, 1998
Retail Access Available to all Customers	July 1, 2001	Year-end 2001	August 1999	Year-end 1999	May 1, 1999	July 1, 2002
Stranded Cost Recovery	Yes	Yes	Yes	Yes	Yes	Yes
Rate Reductions for Residential Customers(1)	Base Rate Freeze	10% phased in over 5 years	5%	3.2% phased in over 3 years	2.09% phased in over 2 years(2)	7.5% phased in over 5 years
Rate Reductions for Commercial Customers(1)	Base Rate Freeze	10% phased in over 5 years	5%	3.2% phased in over 3 years	2.09% phased in over 2 years(2)	7.5%-10% phased in over 5 years
Rate Reductions for Industrial Customers(1)	5%	25% for large industrial customers	22.6% phased in over 5 years	Up to 25% for some customers	12%(3)	11.2% phased in over 4 years(4)

(1) Unless specified otherwise, includes expected one percent reduction in State gross receipts tax.

(2) Excludes expected reduction in gross receipts tax.

(3) According to the Orange & Rockland Utilities, Inc. plan, large industrial customers will be provided with an opportunity to realize an average electric price of 6.0 cents/kWh. Achieving this average electric price implies a 12 percent reduction from current average prices for such customers. The company plans to provide about 8.5 percent of the reduction via scheduled rate reductions. The company expects that the balance (ie., about 3.5 percent) will be realized in participation in its expanding POWERPICK retail choice program. Excludes gross receipts tax impacts.

(4) Additionally, beginning July 1, 1999, and continuing through June 30, 2002, incremental manufacturing load will be served at an average rate of 4.5 cents per kWh.

Exhibit 12

LONG ISLAND LIGHTING COMPANY
HISTORICAL REVENUES AND EXPENSES
ELECTRIC OPERATIONS

($000)(1)

	1993	1994	1995	1996	1997(2)
Operating Revenues					
Sales of Electricity	$2,328,246	$2,451,431	$2,451,615	$2,430,511	$2,449,032
Sales for Resale	13,102	14,895	19,104	20,927	16,354
Other Operating Revenues	4,505	15,719	13,437	15,363	15,360
Total Operating Revenues	$2,345,853	$2,482,045	$2,484,156	$2,466,801	$2,480,747
Operating Expenses					
Power Supply					
Steam Power Production					
Fuel Expense	$ 264,682	$ 235,852	$ 236,480	$ 285,317	$ 305,916
Other Operation	36,609	35,084	26,713	25,785	23,987
Maintenance	29,728	26,485	25,751	21,442	25,456
Total Steam Power Production	$ 331,019	$ 297,421	$ 288,944	$ 332,544	$ 355,360
Nuclear Power Production					
Fuel Expense	$ 7,042	$ 8,205	$ 7,136	$ 8,049	$ 7,693
Other Operation	15,631	12,457	11,862	9,296	11,014
Maintenance	5,910	8,880	7,105	7,003	5,732
Total Nuclear Power Production	$ 28,583	$ 29,542	$ 26,103	$ 24,348	$ 24,439
Other Power Production					
Fuel Expense	$ 8,761	$ 10,392	$ 10,222	$ 10,809	$ 16,411
Other Operation	4,077	3,583	2,454	2,450	2,147
Maintenance	5,729	5,254	5,055	4,470	5,148
Total Other Power Production	$ 18,567	$ 19,229	$ 17,731	$ 17,729	$ 23,707
Other Power Supply					
Purchased Power	$ 250,262	$ 267,103	$ 266,702	$ 289,705	$ 279,638
Other	3,086	3,052	2,541	2,465	3,699
Total Other Power Supply	$ 253,348	$ 270,155	$ 269,243	$ 292,170	$ 283,337
Total Power Supply	$ 631,517	$ 616,347	$ 602,021	$ 666,791	$ 686,842
Transmission					
Operation	$ 55,247	$ 54,541	$ 57,967	$ 55,198	$ 56,328
Maintenance	4,646	4,877	4,948	5,215	4,977
Total Transmission	$ 59,893	$ 59,418	$ 62,915	$ 60,413	$ 61,305
Distribution					
Operation	$ 23,870	$ 19,832	$ 25,406	$ 27,288	$ 28,377
Maintenance	61,264	56,241	57,709	54,880	50,042
Total Distribution	$ 85,134	$ 76,073	$ 83,115	$ 82,168	$ 78,419
Customer					
Customer Accounts	$ 52,857	$ 58,338	$ 58,457	$ 58,651	$ 56,374
Customer Service and Information	26,449	25,027	20,655	21,990	19,123
Sales	—	1	558	826	1,219
Total Customer	$ 79,306	$ 83,366	$ 79,670	$ 81,467	$ 76,716
Administrative and General					
Operation	$ 136,883	$ 146,116	$ 136,871	$ 131,460	$ 145,550
Maintenance	4,489	5,838	5,463	4,997	3,563
Total Administrative and General	$ 141,372	$ 151,954	$ 142,334	$ 136,457	$ 149,113
Total Operating Expenses	$ 997,222	$ 987,158	$ 970,055	$1,027,296	$1,052,395

(1) Source: LILCO NYPSC Annual Report and FERC Form 1 except 1997.
(2) Source: LILCO. Amounts may not total exactly due to rounding.

Exhibit 13

SUMMARY OF 20 LARGEST ELECTRIC SALES ACCOUNTS(1)

Rank	Nature of Business	Annual MWh(2)	Non-Coincident kW(3)	Revenue(4) ($000s)	Annual Load Factor
1	Railroad	226,950	48,300	$ 25,430	54%
2	Health Services	55,700	9,300	6,860	68%
3	Government	33,500	6,825	4,450	56%
4	Health Services	27,050	5,850	3,465	53%
5	Government	21,625	3,775	2,865	65%
6	Government	20,425	4,200	3,210	56%
7	Communications	20,425	3,275	2,905	71%
8	Business Services	18,875	3,875	2,430	56%
9	Real Estate	18,625	3,450	2,640	62%
10	Real Estate	18,150	4,375	2,755	47%
11	Government	17,800	3,850	2,430	53%
12	Instruments and Related Products	17,075	3,625	2,375	54%
13	Educational Services	16,250	3,350	2,175	55%
14	Health Services	15,950	2,850	2,145	64%
15	Electronic & Other Electric Equipment	15,725	2,450	2,105	73%
16	Real Estate	15,550	3,075	2,215	58%
17	Depository Institutions	14,925	2,625	2,080	65%
18	Amusement & Recreation Services	14,750	3,725	2,160	45%
19	Finance, Taxation, & Monetary Policy	13,725	2,825	1,715	55%
20	Electronic & Other Electric Equipment	12,900	2,800	1,640	53%
	Total	615,975	124,400	$ 78,050	
	1997 System Totals	15,937,121		$2,448,829	
	Percent of Total System	3.9%		3.2%	

(1) All accounts (except for the largest) are for single meters.
(2) Rounded to the nearest 25 MWh.
(3) Rounded to the nearest 25 kW (15-minute demand).
(4) Rounded to the nearest $5,000.

Exhibit 14

PARTIAL LIST OF DOCUMENTS REVIEWED IN SUPPORT OF INDEPENDENT CONSULTANT'S REPORT

1. LILCO FERC Form 1 for 1993 though 1996
2. LILCO NYPSC Annual Reports for 1993 through 1996
3. NRC SALP Reports for NMP2
4. LILCO Retail Rate Application to the NYPSC—1993
5. LILCO Retail Rate Application to the NYPSC—September 1996
6. LILCO Annual Capital Expenditures Budgets—1993 through 1997
7. LILCO Actual Capital Expenditures—1993 through 1997
8. Niagara Mohawk NYPSC Annual Reports for 1993 through 1996
9. LILCO NYPSC Competitive Opportunities Proceeding Applications
10. Consolidated Edison (Con Ed) Competitive Opportunities Proceeding Application
11. LILCO Load Pocket Analysis for NYPSC Competitive Opportunities Proceeding, February 1996
12. New York Power Pool Independent System Operator petition to the FERC
13. LILCO 1996 Securities and Exchange Commission From 10-K
14. Site Investigation and Remediation Projects—Project Valuation for the Office of the Controller
15. General Operations Procedure GO-96. Environmental Policy and General Compliance Procedures. Rev. April 12, 1996
16. Corporate Quality Assurance Procedure 18.1. Rev. July 23, 1997
17. Personnel Training Plan. In NYS DEC Hazardous Waste and Solid Waste Management Permit: Container and Tank Storage Facility, Hicksville, NY. EPA ID NYD006866008. January 1996
18. Historic Review of MGP Plants on Long Island. By Atlantic Environmental Services, Inc., June 1996
19. Hazardous Waste Plan: LILCO Substations, Queens/Nassau District. Rev. March 24, 1997
20. General Operations Procedure GO-10326. Hazard Communication Program. Rev. April 18, 1997
21. Environmental Liabilities—Interim Report, issued by Apex Environmental, March 31, 1998
22. Consent Order #WC5191: State of Connecticut v. Connecticut Light and Power Company and Long Island Lighting Company
23. LILCO transmission and distribution system maintenance records
24. LILCO transmission and distribution system property records
25. Distribution System Reliability Program History—LILCO presentation
26. Standards on Reliability and Quality of Electric Service—LILCO, March 26, 1997
27. LILCO 1998 Distribution Lines Program
28. Resolution of the PACB approving LIPA's acquisition of LILCO
29. The Long Island Power Authority Act
30. Case 97-M-0567—Joint Petition of Long Island Lighting Company and the Brooklyn Union Gas Company for Authorization under Section 70 of the Public Service Law to transfer ownership to an unregulated holding company and other related approvals
31. State of New York Public Service Commission—Case 96-E-0909. In the Matter of Central Hudson Gas & Electric Corporation's Plans for Electric Rate/Restructuring pursuant to Opinion 96-12, Amended and Restated Settlement Agreement, Dated January 2, 1998
32. State of New York Public Service Commission—Case 96-E-0909. In the Matter of Central Hudson Gas & Electric Corporation's Plan for Electric Rate/Restructuring pursuant to Opinion 96-12, Order Adopting Terms of Settlement Subject to Modifications and Conditions, Issued and Effective February 19, 1998
33. State of New York Public Service Commission—Case 96-E-0897. In the matter of Consolidated Edison Company of New York Inc.'s Plans for (1) Electric Rate/Restructuring pursuant to Opinion No. 96-12; and (2) the formation of a Holding Company Pursuant to PSL, Sections 70, 108 and 110, and Certain Related Transactions, Amended and Restated Agreement and Settlement Dated September 19, 1997

Exhibit 14

PARTIAL LIST OF DOCUMENTS REVIEWED IN SUPPORT OF INDEPENDENT CONSULTANT'S REPORT

34. State of New York Public Service Commission—Case 96-E-0897. In the Matter of Consolidated Edison Company of New York Inc.'s Plans for (1) Electric Rate/Restructuring pursuant to Opinion No. 96-12; an (2) the formation of a Holding Company Pursuant to PSL, Sections 70, 108 and 110, and Certain Related Transactions, Opinion and Order Adopting Terms of Settlement subject to conditions and Understandings, Issued and Effective November 1, 1997
35. State of New York Public Service Commission—Case 96-E-0987. In the Matter of Consolidated Edison Company of New York Inc.'s Plans for (1) Electric Rate/Restructuring pursuant to Opinion No. 96-12; and (2) the formation of a Holding Company Pursuant to PSL, Sections 70, 108 and 110, and Certain Related Transactions, Order Approving Retail Access Rate Schedule and Retail Access Implementation Plan subject to modifications, Issued and Effective January 23, 1998
36. State of New York Public Service Commission—Case 96-E-0891. In the Matter of New York State Electric & Gas Corporation's Plans for Electric Rate/Restructuring pursuant to Opinion 96-12, Order Adopting Terms of Settlement subject to Modifications and Conditions, Issued and Effective January 27, 1998
37. State of New York Public Service Commission—Case 96-E-0091 and 94-E-0099. Niagara Mohawk Power Corporation, POWERCHOICE Settlement Agreement, Dated October 19, 1997
38. State of New York Public Service Commission—Case 96-E-0900. In the Matter of Orange and Rockland Utilities Inc.'s Plan for Electric Rate/Restructuring Pursuant to Opinion 96-12, Electric Rate and Restructuring Plan, Dated November 6, 1997
39. State of New York Public Service Commission—Case 96-E-0900. In the Matter of Orange and Rockland Utilities Inc.'s Plan for Electric Rate/Restructuring Pursuant to Opinion 96-12, Order Adopting Terms of Settlement, Issued and Effective November 26, 1997
40. State of New York Public Service Commission—Case 96-E-0898. In the Matter of Rochester Gas & Electric Corporation's Plan for Electric Rate/Restructuring Pursuant to Opinion 96-12, Amended and Restated Settlement Agreement, Dated October 23, 1997
41. State of New York Public Service Commission—Case 96-E-0898. In the Matter of Rochester Gas & Electric Corporation's Plan for Electric Rate/Restructuring Pursuant to Opinion 96-12, Opinion and Order Adopting Terms of Settlement Subject to Conditions and Changes, Issued and Effective November 26, 1997
42. State of New York Public Service Commission—Case 96-E-0898. In the Matter of Rochester Gas & Electric Corporation's Plan for Electric Rate/Restructuring Pursuant to Opinion 96-12, Opinion and Order Adopting Terms of Settlement Subject to Conditions and Changes, Issued and Effective January 4, 1998

APPENDIX B

Unaudited Pro Forma Consolidated Balance Sheet of LIPA

The following unaudited pro forma consolidated balance sheet gives effect to the acquisition by LIPA of LILCO, after the transfer of the Transferred Assets and Transferred Liabilities to BL Holding Corp, in a transaction to be accounted for as a purchase. The unaudited pro forma balance sheet is based on the unaudited allocated balance sheet of LILCO as of March 31, 1998. The allocation of the assets and liabilities of LILCO between the LIPA Sub Assets and Liabilities and the Transferred Assets and Transferred Liabilities was derived from information provided by LILCO Management. This allocation is subject to adjustment based upon the actual amounts of the LIPA Sub Assets and Liabilities at the closing and the results of the post closing audit.

Because the operations of LIPA and LIPA Sub will be fundamentally different from that of current LILCO, LIPA believes that pro forma income statement information is not relevant. See "Appendix A—Independent Consultant's Report" in this Part 2 for a projection of LIPA Sub's revenues and revenue requirements post-transaction. Additional information on LILCO and KeySpan may be obtained from the Joint Proxy Statement/Prospectus on Form S-4 filed by LILCO and KeySpan with the SEC. Such Form S-4 is not a part of this Official Statement. LIPA makes no representation as to its accuracy or completeness.

Long Island Power Authority
Unaudited Pro Forma Consolidated Balance Sheet
After First Tranche
March 31, 1998
(in millions)

	LIPA*	New LILCO	Pro-Forma Adjustments	Pro-Forma LIPA
Utility Plant				
Electric				
Transmission and distribution	$	$ 1,356.5		$1,356.5
Nuclear and nuclear fuel		679.8		679.8
Total Utility Plant	0.0	2,036.3		2,036.3
Regulatory Assets				
Shoreham Regulatory Assets		4,661.1	(4,661.1)(1)	
Regulatory tax asset		1,716.9	(1,716.9)(1)	
Other		262.7	(262.7)(1)	
Total Regulatory Assets	0.0	6,640.7		0.0
Other Long-term Investments				
Non Utility Property and Other Investments		17.9		17.9
Promissory Notes		1,013.4	(100.0)(5)	913.4
	0.0	1,031.3		931.3
Current Assets				
Cash and cash equivalents	0.5	75.0	35.2 (4)	110.7
Accounts receivable and accrued revenue		328.6		328.6
Fuel oil at average cost		32.2		32.2
Prepayments and other current assets	7.1	3.3		10.4
Total Current Assets	7.6	439.1		481.9
Designated Funds				
Shoreham Rebates and Credits fund			142.5 (4)	142.5
Clean Energy and Ratepayer Advocacy funds			21.0 (4)	21.0
Interest & Escrow Funds			20.0 (4)	20.0
Capital Expenditure fund			135.0 (4)	135.0
	0.0	0.0		318.5
Deferred Charges	0.0	78.6	(8.2)(4)	70.4
Acquisition Adjustment	0.0		4,180.8 (7)	4,180.8
Total Assets	$7.6	$10,226.0		$8,019.2

*At December 31, 1997; latest available information

See Accompanying Notes to Unaudited Pro-Forma Consolidated Balance Sheet

Long Island Power Authority
Unaudited Pro Forma Consolidated Balance Sheet
After First Tranche
March 31, 1998
(in millions)

	LIPA*	New LILCO	Pro-Forma Adjustments	Pro-Forma LIPA
Capitalization				
Revenue Bonds	$	$	$ 3,449.5 (4)	$3,449.5
Subordinated Indebtedness			1,500.0 (4)	1,500.0
General & Refunding Bonds		1,286.0	(1,286.0)(4)(5)	
Debentures		2,270.0	(439.3)(4)	1,830.7
NYSERDA Notes		915.7		915.7
Premium on Retained Debt			158.7 (6)	158.7
Total preferred stock, including current portion		339.1	(339.1)(3)	
Total common shareowners' equity		2,500.8	(2,500.8)(3)	
Accumulated Deficit	(29.9)			(29.9)
Total Capitalization	(29.9)	7,311.6		7,824.7
Regulatory Liabilities	0.0	395.2	(395.2)(1)	0.0
Current Liabilities				
Accounts payable and accrued expenses	37.5	101.7	13.0 (4)	152.2
Customer deposits		22.6		22.6
Total Current Liabilities	37.5	124.3		174.8
Deferred Credits				
Deferred federal income tax		2,377.9	(2,377.9)(2)	
Other		17.0	2.7 (1)	19.7
Total Deferred Credits	0.0	2,394.9		19.7
Total Capitalization and Liabilities	$ 7.6	$10,226.0		$8,019.2

*At December 31, 1997; latest available information

See Accompanying Notes to Unaudited Pro-Forma Consolidated Balance Sheet

Notes to Unaudited Pro Forma Balance Sheet

Note 1—The allocated balance sheet of LILCO, after giving effect to the transfer of the Transferred Assets and Transferred Liabilities to BL Holding Corp. (i.e., New LILCO), has been adjusted to give effect to the proposed transaction. The allocation of the assets and liabilities among New LILCO and BL Holding Corp was derived from information provided by LILCO management and are subject to adjustment pursuant to the LIPA/LILCO Merger Agreement.

The pro forma balance sheet has been prepared to reflect the acquisition by LIPA of the common stock of New LILCO for a purchase price of $2,497.5 million. Pro forma adjustments are made to reflect:

1. The elimination of regulatory assets and liabilities to reflect the fact that LIPA will not be subject to the jurisdiction of the New York Public Service Commission with the respect to the determination of its rates and charges.

2. The elimination of the deferred federal income tax liability to reflect the fact the LIPA Sub will be exempt from federal income tax.

3. The elimination of the common shareholder's equity accounts of New LILCO and the redemption of the preferred stock of New LILCO.

4. The issuance of $4,949.5 million of LIPA debt to complete the purchase acquisition; refinance $1,625.3 million of New LILCO Retained Debt, fund certain funds and pay the costs of the transaction.

5. The maturity on April 15, 1998 of $100 million of G&R Bonds and the elimination of the corresponding Promissory Notes.

6. The excess of the estimated fair value of the Retained Debt over its par amount of $111.6 million for the Debentures and $47.1 million for the NYSERDA Financing Notes.

7. To record the excess of the acquisition costs, including the fair value of the Retained Debt, over the original net book value of the transmission and distribution and nuclear assets and the fair value of the other net assets acquired (acquisition adjustment).

APPENDIX C

GLOSSARY OF DEFINED TERMS

The following terms, as used in Part 1, Part 2 and Appendices D and E of this Official Statement, have the respective meanings provided below. For additional definitions relating to the Operating Agreements, see Appendix E. These summary definitions do not purport to be complete or definitive and are qualified in their entirety by reference to the Resolution, the Financing Agreement, the MSA, the PSA and the EMA, copies of which are on file with the Trustee.

"Account" means one of the special accounts created and established pursuant to the Resolution.

"ACO" means administrative consent order.

"Acquisition Debt" means (i) all Bonds and Subordinated Indebtedness issued for the purposes of providing sufficient funds to acquire all outstanding LILCO common stock in accordance with the LIPA/LILCO Merger Agreement, pay a portion of the redemption price of certain preferred stock of LILCO in accordance with the LIPA/LILCO Merger Agreement, retire certain outstanding debt of LILCO, purchase certain interest rate hedges entered into in anticipation of the Bonds, and pay any fees and expenses incurred in conjunction with the foregoing, and (ii) all other Outstanding Subsidiary Unsecured Debt.

"Administrative Services Agreement" means the Administrative Services Agreement, dated as of May 1, 1998, between LIPA and LIPA Sub, as the same may be amended and supplemented.

"Agreement and Plan of Merger and Exchange" means the document executed by LILCO and Brooklyn Union, dated as of June 26, 1997.

"Annual Subsidiary Budget" means the annual budget of LIPA Sub, as amended or supplemented, adopted or in effect for a particular Fiscal Year, as provided in the Financing Agreement.

"Annual Report" means the report prepared for holders of the Offered Securities to provide certain financial information and operating data relating to LIPA no later than six months after the end of each of LIPA's fiscal years.

"Authority Budget" or "LIPA Budget" means the annual budget of LIPA, as amended or supplemented, adopted or in effect for a particular Fiscal Year, included as part of the System Budget as provided in the Resolution.

"Authority Expenses" means all Operating Expenses incurred by LIPA.

"Authority Obligations" means, collectively, all Bonds and other bonds, notes or other evidences of indebtedness for money borrowed by LIPA, Parity Reimbursement Obligations, Parity Contract Obligations and Subordinated Indebtedness, but shall not include debt of LIPA not secured by the Trust Estate.

"Authorized Denominations" means $5,000 in the case of Current Interest Bonds, and the amount accreting to $5,000 due at maturity in the case of Capital Appreciation Bonds, and in each case integral multiples thereof.

"Authorized Representative" means in the case of both LIPA and LIPA Sub, their respective Chairman, Chief Executive Officer, Executive Director, Chief Financial Officer, Controller or Chief Operating Officer, or such other person or persons so designated by resolution of LIPA or LIPA Sub, as the case may be.

"Basic Agreement" means the Basic Agreement, dated September 27, 1975, that specifies the ownership interests of NMP2.

"Beneficial Owner" shall have the meaning assigned thereto in Appendix H to this Official Statement.

"BHC Parties" means the Transferee Subsidiaries and BL Holding Corp.

"BL Holding Corp" means BL Holding Corp, a New York corporation.

"BL Holding Corp Sub" or **"BL Subsidiary"** means a subsidiary of the BL Holding Corp. constituting one of the Transferee Subsidiaries.

"Bond Counsel" means Hawkins, Delafield & Wood, New York, New York.

"Bond Counsel's Opinion" or **"Opinion of Bond Counsel"** means an opinion signed by any attorney or firm of attorneys of nationally recognized standing in the field of law relating to revenue bonds of municipalities and public agencies, selected by LIPA and reasonably satisfactory to the Trustee.

"Bond Payment Date" means each date on which interest or both a Principal Installment and interest shall be due and payable on any of the Outstanding Bonds or Parity Reimbursement Obligations according to their respective terms.

"Bond Year" means, with respect to any Bonds, the twelve-month period, if any, set forth in a Supplemental Resolution.

"Bondholder", **"Owner"** or **"Holder"** or words of similar import mean, when used with reference to a Bond, the person in whose name the Bond is registered on the registry books kept by the Trustee pursuant to the Resolution.

"Bonds" means all bonds, notes or other evidence of indebtedness of LIPA issued pursuant to the Resolution that are on a parity, senior lien basis as to security and source of payment.

"BU" or **"Brooklyn Union"** means The Brooklyn Union Gas Company, a New York corporation.

"BUG/LILCO Hedge Fund L.P." means the limited partnership which acquired the interest rate hedge to be purchased by LIPA as part of the LIPA/LILCO Merger.

"Capital Appreciation Bonds" means Offered Securities which pay interest only at maturity. The amount of interest accrued on any Capital Appreciation Bond as of any date prior to maturity will be the difference between the accreted value thereof and the initial Authorized Denomination thereof.

"Capital Improvement Bonds" means Bonds issued by LIPA each year for capital projects.

"Capital Lease" means any capital lease or other obligation (other than Bonds, G&R Bonds, Subordinated Indebtedness, Outstanding Subsidiary Unsecured Debt, Parity Contract Obligations, Subordinated Contract Obligations, Parity Reimbursement Obligations, Subordinated Reimbursement Obligations, or certain obligations issued for Separately Financed Projects), treated as debt under the accounting principles pursuant to which the books of account of LIPA or LIPA Sub, as the case may be, are kept and audited.

"Capitalized Interest" means that portion of the proceeds of any Bonds deposited in a sub-account established in the Capitalized Interest Account of the Debt Service Fund, and interest earnings thereon to the extent retained in such Account as provided in the Resolution, for the purpose of funding the payment of a portion of the interest on any Bonds.

"Cash Purchase Price" means the sum which LIPA will pay to the common shareholders of LILCO on the LIPA/LILCO Merger Closing Date.

"Certificate" means (i) a signed document attesting to or acknowledging the matters therein stated or setting forth matters to be determined pursuant to the Resolution, (ii) the report of an Accountant as to an audit or compliance called for by the Resolution, or (iii) any report of the Consulting Engineer or Rate Consultant as to any matter called for by the Resolution or the Financing Agreement.

"Certificates" means Certificates of Environmental Compatibility and Public Need.

"Clean Air Act" means the federal Clean Air Act of 1977, as amended.

"Code" means the Internal Revenue Code of 1986, as amended, or any successor thereto, as the same may be in effect from time to time.

"Construction Fund" means the fund by that name established pursuant to the Resolution.

"Consulting Engineer" means any independent engineer or firm of engineers of recognized standing selected by LIPA and may include an independent engineer or firm of engineers retained by LIPA or LIPA Sub in one or more other capacities.

"Costs" means costs of any System Improvements or any other purpose related to the System for which bonds, notes or other obligations of LIPA may be issued under the LIPA Act or under other applicable State statutory provisions (whether or not also classifiable as an Operating Expense), including but not limited to direct costs, incidental costs (including but not limited to legal, administrative, engineering, consulting and technical services, insurance and financing costs), working capital and reserves deemed necessary or desirable by LIPA Sub and approved by LIPA, and other costs properly attributable thereto including but not limited to the payment of principal, interest, and redemption, tender or purchase price of any (i) obligations issued by LIPA for the payment of any of such costs, (ii) Outstanding Subsidiary Unsecured Debt, (iii) obligations issued to pay Capitalized Interest or (iv) obligations issued to refund any obligations referred to in clauses (i) or (iii) or Outstanding Subsidiary Unsecured Debt referred to in clause (ii); all items of expense directly or indirectly payable or reimbursable and related to the authorization, sale and issuance of Bonds, including but not limited to printing costs, costs of preparation and reproduction of documents, filing and recording fees, initial fees and charges of any Fiduciary, legal fees and charges, fees and disbursements of consultants and professionals, costs of credit ratings, fees and charges for preparation, execution, transportation and safekeeping of Bonds, costs and expenses of refunding, premiums for the insurance of the payment of the Bonds and any other cost, charge or fee in connection with the original issuance of Bonds; termination payments under the Power Supply Agreement or other agreement of LIPA or LIPA Sub for power supply purposes; and termination payments under Financial Contracts.

"Credit Facility" means a letter of credit, revolving credit agreement, surety bond, insurance policy or similar obligation, arrangement or instrument issued by a bank, insurance company or other financial institution which provides for payment of all or a portion of the Principal Installments or interest due on any Bonds including through a reserve or similar fund.

"Current Interest Bonds" means Offered Securities which pay a fixed rate of interest semiannually.

"Customer Average Interruption Duration Index" or **"CAIDI"** means the total number of customer hour duration of interruptions during the year divided by the total number of customers affected.

"Debenture Indenture" means the Indenture, dated as of November 1, 1986, between LILCO and State Street Bank and Trust Company, as successor Trustee, and an Indenture, dated as of November 1, 1992, between LILCO and Chemical Bank, as Trustee, as amended and supplemented.

"Debentures" means certain unsecured obligations of LILCO retained as liabilities of LIPA Sub.

"Debt Service" for any Fiscal Year or part thereof means, as of any date of calculation, the sum of (i) with respect to any Outstanding Bonds, an amount equal to the sum of (a) interest payable during such Fiscal Year or part thereof on such Bonds, except to the extent that such interest is to be paid from amounts representing Capitalized Interest and (b) the Principal Installments of such Bonds payable during such Fiscal Year or part thereof and (ii) with respect to a Parity Reimbursement Obligation, an amount equal to the sum of (a) interest payable during such Fiscal Year or part thereof on such Parity Reimbursement Obligation and (b) the Principal Installments of such Parity Reimbursement Obligation payable during such Fiscal Year or part thereof. Such interest and Principal Installments shall be calculated on the assumption that (x) no such Bonds, or Parity Reimbursement Obligations Outstanding at the date of calculation will cease to be Outstanding except by reason of the payment thereof upon stated maturity or upon mandatory redemption by application of Sinking Fund Installments and (y) Variable Rate Bonds will bear interest at the greater of (A) the rate or rates which were assumed by LIPA in the Authority Budget for such Fiscal Year to be borne by Variable Rate Bonds during such Fiscal Year or (B) the average rate or rates borne on Variable Rate Bonds Outstanding during the twelve calendar months preceding the date of calculation, but at a rate not less than the rate or rates borne thereon as of such date of calculation; provided, however, that if LIPA has in connection with any Variable Rate Bonds entered into a Financial Contract which provides that LIPA is to pay to the Qualified Counterparty an amount determined based upon a fixed rate of interest on the Outstanding principal amount of such Variable Rate Bonds or that the Qualified Counterparty is to pay to LIPA an amount determined based upon the amount by which the rate at which such Variable Rate Bonds bear interest exceeds a stated rate of interest on all or any portion of such Variable Rate Bonds, it will be assumed that such Variable Rate Bond bears interest at the fixed rate of interest to be paid by LIPA or the rate in excess of which the Qualified Counterparty is to make payment to LIPA in accordance with such agreement.

"Debt Service Component," when used with reference to Supply Contracts with any entity, or Capital Leases, means that portion of any rates, fees, charges, surcharges or payments for the specific purpose of meeting principal and/or interest on that entity's obligations directly associated with that contract and payable to such entity regardless of delivery, and the principal and/or interest component of any Capital Lease.

"Debt Service Fund" means the fund by that name established pursuant to the Resolution.

"DEC" means the New York State Department of Environmental Conservation.

"Defeasance Obligations" means obligations of the type described in clause (ii), (iii) or (ix) of the definition of Investment Securities, which are not subject to redemption prior to maturity except at the option of the holder.

"DEP" means the Connecticut Department of Environmental Protection.

"Depositary" means any bank or trust company selected by LIPA Sub or LIPA, as the case may be, as a depositary of moneys to be held under the provisions of the Financing Agreement or the Resolution and may include the Trustee.

"Direct DTC Participants" shall have the meaning assigned thereto in Appendix H to this Official Statement.

"Disbursement Request" means the written request signed by an Authorized Representative of LIPA Sub and required to be delivered to LIPA pursuant to the Financing Agreement to effect disbursements from the Construction Fund.

"Discount Bond" means an Offered Bond having original issue discount.

"DOE" means the United States Department of Energy.

"DSM" means demand side management.

"DTC" means The Depository Trust Company or its successors.

"EMF" means electromagnetic fields.

"Energy Management Agreement" or **"EMA"** means the Energy Management Agreement, dated as of June 26, 1997, between LIPA and LILCO, and their respective successors and assigns, as the same may be amended and supplemented.

"Energy Policy Act" means the federal Energy Policy Act of 1992, as amended.

"EPA" means the United States Environmental Protection Agency.

"Event of Default" means any event specified in the Resolution as an "Event of Default."

"Federal Low-Level Radioactive Waste Policy Act" means the federal Low-Level Radioactive Waste Policy Act of 1985, as amended.

"Federal Power Act" means the federal Public Utilities Act of 1935, as amended.

"FERC" means the Federal Energy Regulatory Commission.

"Fiduciary" means the Trustee, any Paying Agent, any Depositary, or any Authenticating Agent.

"Financial Contract" means, to the extent from time to time permitted by law, any financial arrangement entered into by LIPA with respect to Bonds or Subordinated Indebtedness, and any financial arrangement entered into by LIPA or LIPA Sub with respect to Outstanding Subsidiary Unsecured Debt, for the purpose of moderating interest rate fluctuations or any other purpose, (i) which is entered into with an entity that is a Qualified Counterparty at the time the arrangement is entered into, and (ii) which is any of the following, or any combination thereof, or any option with respect thereto: a cap, floor or collar; forward rate; future rate; swap (such swap may be based on an amount equal either to the principal amount of such Bonds or Subordinated Indebtedness, or of such Outstanding Subsidiary Unsecured Debt, as the case may be, as may be designated or a notional

principal amount relating to all or a portion of the principal amount of such Bonds or Subordinated Indebtedness, or such Outstanding Subsidiary Unsecured Debt, as the case may be); asset, index, price or market-linked transaction or agreement; other exchange or rate protection transaction agreement; or other similar transaction (however designated).

"Financing Agreement" means the Financing Agreement, dated as of May 1, 1998, by and between LIPA and LIPA Sub to provide for their respective duties and obligations relating to the financing and operation of the retail electric business in the Service Area, as the same may be amended or supplemented.

"First Supplemental Resolution" means the resolution entitled the First Supplemental Resolution of LIPA, which authorizes the issuance of the Series 1998A Bonds.

"Fiscal Year" means the twelve-month period commencing on January 1 of each year; provided, however, that LIPA and LIPA Sub may, from time to time, mutually agree on a different twelve-month period as the Fiscal Year, in which case January 1, when with reference to Fiscal Year, shall be construed to mean the first day of the first calendar month of such different Fiscal Year.

"Fitch" means Fitch IBCA, Inc., formerly known as Fitch Investors Services, L.P. and its successors and their assigns.

"FPPCA" means fuel and purchased power cost adjustment.

"G&R Bonds" means any outstanding bonds under the General and Refunding Indenture, dated as of June 1, 1975, between LILCO and Manufacturers Hanover Trust Company, as supplemented and amended.

"Generating Facilities" or **"GENCO Generating Facilities"** means the existing oil and gas-fired generating plants on Long Island owned by LILCO prior to the Merger Closing.

"Generating Facility Sites" means each parcel of land upon which each existing GENCO Generating Facility is situated, as well as the land contiguous thereto, owned by GENCO as of March 19, 1997.

"Generation Purchase Right Agreement" means the Generation Purchase Right Agreement, dated as of June 26, 1997, by and between LILCO, as seller, and LIPA, as buyer, and their respective successors and assigns.

"Guaranty Agreement" or **"Guaranty"** means the Guaranty Agreement to be entered into prior to the Closing Date from the Guarantor to LIPA, as the same may be amended from time to time in accordance therewith.

"Independent Consultant's Report" means the Independent Consultant's Report contained in Appendix A to this Official Statement.

"Indirect DTC Participants" shall have the meaning assigned thereto in Appendix H to this Official Statement.

"Initial Subordinated Indebtedness" means the initial issue of variable rate Electric System Subordinated Revenue Bonds.

"Investment Securities" means and includes any of the following securities, if and to the extent the same are at the time legal investments by LIPA of the funds to be invested therein and conform to the policies set forth in any investment guidelines adopted by LIPA and in effect at the time of the making of such investment: (i) direct obligations of, or obligations guaranteed as to principal and interest by, any state or direct obligations of any agency, public authority or political subdivision thereof, provided such obligations are rated, at the time of purchase, in one of the three highest Rating Categories by a Rating Agency; (ii) (a) any bonds or other obligations which as to principal and interest constitute direct obligations of, or are guaranteed by the United States of America, including obligations of any agency thereof or corporation which has been or may be created pursuant to an Act of Congress as an agency or instrumentality of the United States of America to the extent unconditionally guaranteed by the United States of America or (b) any other receipt, certificate or other evidence of an ownership interest in obligations or in specified portions thereof (which may consist of specified portions of the interest thereon) of the character described in subclause (a) of this clause (ii); (iii) obligations of any agency, subdivision, department, division or instrumentality of the United States of America, or obligations fully guaranteed as to interest and principal by any agency, subdivision, department, division or instrumentality of the United States of America; (iv) banker's acceptances or certificates of deposit issued by a commercial bank with its principal place of business within the State and having capital and surplus of more than $100 million; (v) corporate securities, including commercial paper and fixed income obligations, which are, at the time of purchase, rated by a Rating Agency in one of its three highest Rating Categories for comparable types of obligations; (vi) repurchase agreements or other investment agreements collateralized by securities described in clause (ii) above with any registered broker/dealer or with any domestic commercial bank whose long-term debt obligations are rated "investment grade" by each Rating Agency, provided that (a) a specific written repurchase agreement governs the transaction, (b) the securities are held, free and clear of any lien, by the Trustee or an independent third party acting solely as agent for the Trustee, and such third party is either a direct member of the Federal Reserve Bank or a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than $25 million, and the Trustee shall have received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Trustee, (c) the repurchase agreement has a term of thirty days or less, or the Trustee will value the collateral securities no less frequently than monthly and will liquidate the collateral securities if any deficiency in the required collateral percentage is not restored within five business days of such valuation, and (d) the fair market value of the collateral securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 102%; (vii) investment agreements or guaranteed investment contracts with any financial institution whose senior long term debt obligations, or whose obligations under such an investment agreement or guaranteed investment contract, are guaranteed by a financial institution whose senior long term debt obligations, have a rating (at the time such agreement or contract is entered into) in one of the three highest Rating Categories for comparable types of obligations by a Rating Agency; (viii) money market funds rated in one of the three highest Rating Categories for comparable types of obligations by a Rating Agency; (ix) municipal obligations, the payment of principal and redemption price, if any, and interest on which is irrevocably secured by obligations of the type referred to in clauses (i), (ii) or (iii) above and which obligations have been deposited in an escrow arrangement which is irrevocably pledged to the payment of such municipal obligations and which municipal obligations are rated in the highest Rating Category by a Rating Agency, or any other municipal obligation rated in the highest Rating Category by a Rating Agency;

(x) obligations of any person or entity which shall be rated at the time of the investment in one of the three highest Rating Categories by a Rating Agency; and (xi) any other investment in which LIPA is permitted to invest under applicable law, notwithstanding any limitations set forth in clauses (i) through (x) above. Obligations of any Fiduciary or an affiliate thereof may be Investment Securities, provided that they otherwise qualify.

"IOU" means an investor-owned electric utility.

"IRS" means the United States Internal Revenue Service.

"Joint Proxy Statement/Prospectus" means the form of S-4 filed by LILCO and Brooklyn Union (prior to becoming a subsidiary of KeySpan) with the SEC relating to the LILCO/KeySpan Merger.

"Jurisdictional Utilities" means **"public utilities"** (as defined in the Federal Power Act) that own, operate or control interstate transmission facilities used to transmit power in interstate commerce.

"KeySpan" means KeySpan Energy Corporation, the parent holding company of Brooklyn Union.

"Liabilities Undertaking and Indemnification Agreement" means the agreement delivered at the LIPA/LILCO Merger Closing by the BHC Parties to indemnify the LIPA Parties and hold them harmless from a variety of specified liabilities in connection with the LIPA/LILCO Merger Transaction.

"LILCO" means the Long Island Lighting Company, a New York corporation.

"LILCO/KeySpan Combination" means the agreement entered into between LILCO and BU to combine their two companies through a series of steps which will result in BL Holding Corp being the parent company of both LILCO and KeySpan.

"LIPA" or **"Authority"** means the Long Island Power Authority, a corporate municipal instrumentality of the State of New York created under and by virtue of the LIPA Act.

"LIPA Acquisition Corp" means a transitory subsidiary of LIPA formed to facilitate the acquisition of LILCO by LIPA.

"LIPA Act" means the Long Island Power Authority Act, being Title 1-A of Article 5 (§1020 *et seq.*) of the Public Authorities Law of the State of New York, as amended.

"LIPA Parties" means LIPA, LIPA Acquisition Sub, LIPA Sub and LILCO as Surviving Corporation.

"LIPA Sub" or **"Subsidiary"** means LIPA Acquisition Corp. and, after the LIPA/LILCO Merger Closing, shall mean LILCO as the surviving corporation of such merger and a wholly-owned subsidiary of LIPA, and any successor or assignee permitted under the Financing Agreement.

"LIPA Sub Assets" or **"Subsidiary Assets"** means the assets of LILCO retained by LIPA Sub on the LIPA/LILCO Merger Closing Date.

"LIPA Sub Budget" or **"Subsidiary Budget"** means the annual budget of LIPA Sub, as amended or supplemented, adopted or in effect for a particular Fiscal Year as provided in the Financing Agreement.

"LIPA Sub Debentures" or **"Subsidiary Debentures"** means any "Bonds" as defined in the Debenture Indentures.

"LIPA Sub Expenses" or **"Subsidiary Expenses"** means all Operating Expenses incurred by LIPA Sub.

"LIPA Sub General Fund" or **"Subsidiary General Fund"** means the special fund by that name established by LIPA Sub and held by a bank, trust company or banking association designated by LIPA Sub to act as a depository for the general funds of LIPA Sub.

"LIPA Sub Liabilities" or **"Subsidiary Liabilities"** means the liabilities of LILCO retained by LIPA Sub as of the LIPA/LILCO Merger Closing Date.

"LIPA Sub Note" or **"Subsidiary Note"** means the promissory note or notes of LIPA Sub delivered in accordance with the Financing Agreement.

"LIPA Sub Unsecured Debt Fund" or **"Subsidiary Unsecured Debt Fund"** means the fund established in accordance with the Resolution for payment of the principal of and interest on Outstanding LIPA Sub Unsecured Debt, subject to the provisions of the Resolution.

"LIPA/LILCO Merger Agreement" or **"Merger Agreement"** means the Agreement and Plan of Merger, dated as of June 26, 1997, by and among BL Holding Corp, LILCO, LIPA and LIPA Sub.

"LIPA/LILCO Merger Closing" means the consummation of the LIPA/LILCO Merger Transaction.

"LIPA/LILCO Merger Closing Date" means the date on which the LIPA/LILCO Merger Transaction will be completed.

"LIPA/LILCO Merger Transaction" or **"LIPA/LILCO Merger"** means the merger and related transactions between LIPA and LILCO provided for by the LIPA/LILCO Merger Agreement.

"Long Island Choice" means the customer choice plan proposed by LIPA intended to lead to full choice of power suppliers for all of LIPA's customers by 2003.

"Management Committee" means the management committee (comprised of the co-tenants) which has oversight for policy making, planning, budgeting, and operational decisions made by Niagara Mohawk related to NMP2, under an Operating Agreement among the co-tenants, effective as of January 1, 1993.

"Management Services Agreement" or **"MSA"** means the Management Services Agreement, dated as of June 26, 1997, between LIPA and LILCO, and their respective successors and assigns, as the same may be amended and supplemented.

"Market Participant" means, originally, the seven IOUs and NYPA, but would include any person engaged in the wholesale sale, transmission or purchase of electric energy, under the proposal for the ISO.

"Merger Closing" means the completion of the LIPA/LILCO Merger.

"MGP Sites" means locations of manufactured gas plant operations.

"Moody's" means Moody's Investors Service and its successors and their assigns.

"New NOPR" means the Notice of Proposed Rulemaking issued by the FERC on April 24, 1996, which proposes replacement of the network and point-to-point single tariff in Order No. 888 with a capacity reservation tariff.

"New York Facilities Agreement" means the New York Facilities Agreement, dated as of January 1, 1994, by and among Consolidated Edison Company of New York, Brooklyn Union and LILCO relating to certain natural gas transmission facilities.

"New York Public Service Law" means the New York Public Service Law, as amended.

"NRC" means the Nuclear Regulatory Commission.

"Nuclear Waste Policy Act of 1982" means the federal Nuclear Waste Policy Act of 1982, as amended.

"NYNOC" means the New York Nuclear Operating Company, a planned company to be formed by the four utilities operating nuclear generating facilities in the State.

"NYPA" means the Power Authority of the State of New York.

"NYSERDA Financing Notes" means the notes of LILCO supporting the tax-exempt bonds issued on behalf of LILCO by the New York State Energy Research and Development Authority.

"OASIS" means an electronic "Open Access Same-time Information System", required by FERC Order No. 889, which is a system to share transmission-related information (including information about available capacity) on a real-time basis.

"OATT" means Open Access Transmission Tariff.

"Operating Agreements" means, collectively, the EMA, the MSA and the PSA.

"Operating Expense Fund" means the fund by that name established pursuant to the Resolution.

"Operating Expenses" means any and all current expenses of maintaining, repairing, operating and managing the System, including but not limited to the costs of supplies, fuel, fuel assemblies and components required for the operation of the System (including but not limited to any payments made under Supply Contracts other than the Debt Service Component thereof); payments relating to fuel or electricity hedging instruments; all payments under any System Agreements; all salaries, administrative, general, commercial, architectural, engineering, advertising, public notices, auditing, billing, collection and enforcement and legal expenses; insurance and surety bond premiums; consultants' fees and charges; payments to pension, retirement, health and hospitalization funds; any taxes which may lawfully be imposed on the System or the income or operation thereof or of LIPA Sub; costs of public hearings; ordinary and current rentals of equipment or other property; lease payments for real property or interests therein; expenses of maintenance and repair (including

replacements); expenses, liabilities and compensation of the Trustee or any other Fiduciary or depositary of LIPA or LIPA Sub funds; to the extent provided by by-law, agreement or other instrument of the Authority or LIPA Sub, indemnification of Fiduciaries, Trustees, officers and employees of LIPA, directors, officers and employees of LIPA Sub, and others and premiums for insurance related thereto; reasonable reserves for operation, maintenance and repair and for self-insurance; and all other expenses necessary, incidental or convenient for the efficient operation of the System; all costs and expenses associated with or arising out of the research, development (including feasibility and other studies, including but not limited to resource planning and studies and reports relating to demand side management) and/or implementation of any project, facility, system, task or measure related to the System including but not limited to demand side management programs, deemed desirable or necessary by LIPA or LIPA Sub; all other costs and expenses arising out of or in connection with the conduct of LIPA Sub's business or necessary, incidental or convenient for the efficient operation of LIPA Sub; and all expenses necessary, incidental or convenient for the efficient operation of LIPA and the performance of the obligations of LIPA under the Administrative Services Agreement. Notwithstanding the foregoing, Operating Expenses shall not include (i) any costs and expenses attributable to a Separately Financed Project, (ii) any costs or expenses for new construction or for reconstruction other than restoration of any part of the System to the condition of serviceability thereof when new, (iii) the Debt Service Component of any Supply Contract, (iv) to the extent so specified by LIPA, any incentive payments payable by LIPA Sub under any System Agreement, (v) any payments payable by LIPA Sub under any other agreement the terms of which specify that the same shall not constitute an Operating Expense under the Resolution, (vi) any allowance for depreciation, (vii) payment under any Capital Leases, or (viii) any PILOTs.

"Option Securities" means bonds, notes or other evidences of indebtedness which by their terms may be tendered by and at the option of the Holder thereof for purchase or payment by or on behalf of LIPA prior to the stated maturity thereof, or the maturities of which may be extended by and at the option of the Holder thereof.

"Outstanding" when used with reference to Parity Reimbursement Obligations, shall have the meaning given to such term in the agreement creating such Parity Reimbursement Obligations, and, when used with reference to Bonds, means, as of any date, all Bonds theretofore or thereupon being authenticated and delivered under the Resolution except: (a) any Bonds canceled by the Trustee at or prior to such date; (b) any Bonds the principal and Redemption Price, if any, of and interest on which have been paid in accordance with the terms thereof; (c) any Bonds in lieu of or in substitution for which other Bonds have been authenticated and delivered pursuant to the Resolution; and (d) any Bonds deemed to have been paid as provided in the Resolution.

"Outstanding LIPA Sub Unsecured Debt" or **"Outstanding Subsidiary Unsecured Debt"** means (i) any indebtedness of LIPA Sub outstanding as of the LIPA/LILCO Merger Closing Date, as described therein, consisting of (a) "Bonds" as defined in the Debenture Indentures, and (b) the NYSERDA Financing Notes, and (ii) Financial Contracts related to Outstanding Subsidiary Unsecured Debt and (iii) any reimbursement obligation relating to any letter of credit or other credit support for any indebtedness referred to in (i)(a) or (b) above.

"PACB" means the Public Authorities Control Board of the State of New York.

"Parity Contract Obligation" means the obligation of LIPA or LIPA Sub to pay the Debt Service Component of Supply Contracts from Revenues and secured by a pledge of and lien on the Trust Estate on a parity with the Bonds.

"Parity Contract Obligations Fund" means the fund by that name established pursuant to the Resolution from which amounts shall be applied for the payment of Parity Contract Obligations in accordance with the Resolution.

"Parity Obligations" means, collectively, all Parity Contract Obligations and Parity Reimbursement Obligations.

"Parity Reimbursement Obligation" shall have the meaning assigned thereto under the heading "Special Provisions Relating to Option Securities, Financial Contracts, Subordinated Credit Facilities, Parity Obligations and Subordinated Indebtedness" in Appendix D.

"Paying Agent" means any paying agent for any Bonds, and its successor or successors and any other person which may at any time be substituted in its place pursuant to the Resolution.

"PILOT" means any payment in lieu of taxes due and owing by LIPA or LIPA Sub in accordance with Section 1020-q of the LIPA Act or other applicable law.

"PILOTs Fund" means the fund by that name established by the Resolution, and used to make payments to the State or any municipality or other political subdivision of the State, which shall be entitled to receive PILOTs under the LIPA Act, subject to the provisions of the Resolution.

"POLR" means provider of last resort, designated as LIPA under Long Island Choice.

"Power Supply Agreement" or **"PSA"** means the Power Supply Agreement, dated as of June 26, 1997, between LIPA and LILCO, and their respective successors and assigns, as the same may be amended and supplemented.

"Price-Anderson Act" means the federal Price-Anderson Atomic Energy Damages Act of 1957, as amended.

"Principal Installment" means, as of any date of calculation and with respect to any Outstanding Bonds, (i) the principal amount of such Bonds (including (x) any amount designated in, or determined pursuant to, the applicable Supplemental Resolution, as the "principal amount" with respect to any Bonds which do not pay full current interest for all or any part of their term and (y) the principal amount of any Parity Reimbursement Obligation) due on a certain future date for which no Sinking Fund Installments have been established, or (ii) the unsatisfied balance of any Sinking Fund Installments due on a certain future date for such Bonds, or (iii) if such future dates coincide as to different Bonds, the sum of such principal amount of Bonds and of such unsatisfied balance of Sinking Fund Installments due on such future date.

"Promissory Note Obligor" means BL Holding Corp and one or more of its subsidiaries.

"Promissory Notes" means one or more promissory notes evidencing the obligation of the Promissary Note Obligor to pay to LIPA Sub amounts equal to the principal and interest when due on certain Debentures and certain NYSERDA Financing Notes.

"Property Tax Settlement", as used in the Resolution, means LIPA's program of rebates and credits to System customers in respect of the amounts otherwise payable by Suffolk County, the Town of Brookhaven and certain other municipalities within Suffolk County as refunds of taxes and payments in lieu of taxes relating to the Shoreham Nuclear Power Plant.

"PRP" means "potentially responsible party".

"PSC" means the New York State Public Service Commission.

"Public Utilities" means "public utilities" as defined in the Federal Power Act, and it includes any person or entity that owns, controls, or operates facilities used for the transmission of electric energy in interstate commerce or for the sale of electric energy at wholesale in interstate commerce, except a state or any political subdivision of a state, or any agency, authority, or instrumentality of any one or more of the foregoing.

"Qualified Counterparty" means an entity (i) whose senior long term debt obligations, other senior unsecured long term obligations, financial program rating, counterparty rating or claims paying ability are rated (at the time the subject Financial Contract is entered into) in any of the three highest Rating Categories from a nationally recognized statistical rating organization, (ii) whose payment obligations under a Financial Contract are guaranteed by an entity whose senior long term debt obligations, other senior unsecured long term obligations, financial program rating, counterparty rating or claims paying ability, are rated (at the time the subject Financial Contract is entered into) in any of the three highest Rating Categories from a nationally recognized statistical rating organization, or (iii) whose obligation, if any, to make payment to LIPA upon the termination of the subject Financial Contract is fully collateralized by Investment Securities of the type described in clause (ii) of the definition of Investment Securities; provided, however, that such obligation shall be deemed to be fully collateralized if the Investment Securities shall have a market value, determined periodically in accordance with the Financial Contract, that is not less than 102% of any termination payment.

"Rate Consultant" means the independent accountant or firm of independent accountants, or a management consultant or firm of management consultants, or independent engineer or firm of independent engineers which, in any case, shall be of recognized standing in the field of electric transmission and distribution system consulting selected by LIPA.

"Rate Covenant" means the covenants by LIPA in the Resolution to establish and maintain System fees, rates, rents, charges and surcharges.

"Rate Stabilization Fund" means the fund by that name established by the Resolution, and used for any lawful purpose of LIPA or LIPA Sub, including but not limited to making any deposits required by the Resolution to any Fund or Account, in accordance with the Resolution.

"Rating Agency" means each of Fitch, Moody's, and S&P, and their respective successors and assigns, in each case and at any time only if the same is then maintaining a rating on any Bonds at the request of LIPA.

"Rating Category" means a general rating category of an applicable Rating Agency or nationally recognized statistical rating organization without regard to any refinement or gradation of such rating by a numerical modifier or otherwise.

"Record Date" means, with respect to each scheduled payment of principal of, premium, if any, and interest on each Bond, the date specified as the "record date" therefor in the Supplemental Resolution authorizing such Bond.

"Redemption Price" means, when used with respect to a Bond or portion thereof, the principal amount thereof plus the applicable premium, if any, payable upon either optional or mandatory redemption thereof pursuant to the Resolution.

"Refunding Bond" means any Bond authenticated and delivered on original issuance pursuant to the Resolution for the purpose of refunding any Outstanding Bonds, or thereafter authenticated and delivered pursuant to the Resolution in lieu of or substitution for such Bond.

"Reimbursement Obligation" shall have the meaning provided under the heading "Special Provisions Relating to Option Securities, Financial Contracts, Subordinated Credit Facilities, Parity Obligations and Subordinated Indebtedness" in Appendix D.

"Reliability Council" means the separate not-for-profit which will establish safety and reliability standards for all entities, including the ISO, engaging in electric power transactions on the ISO's transmission system.

"Required Deposits" means the amount, if any, payable into the Operating Expense Fund, the Debt Service Fund, the Parity Contract Obligations Fund, the Subordinated Indebtedness Fund, LIPA Sub Unsecured Debt Fund and the PILOTs Fund, but in each case only to the extent such payments are required to be made from Revenues.

"Resolution" means the Electric System General Revenue Bond Resolution, of LIPA, as the same may be amended or supplemented by a Supplemental Resolution or Resolutions.

"Retained Assets" means the balance of LILCO's assets and properties to be retained by LILCO following its merger with LIPA Acquisition Corp.

"Retained Business" means the business and operations to be conducted by LIPA Parties after the LIPA/LILCO Merger Closing.

"Retained Debt" means the total long-term indebtedness of LILCO on the LIPA/LILCO Merger Closing Date that will be retained by LIPA Sub.

"Revenue Fund" means the fund into which Revenues are deposited by LIPA or by LIPA Sub, unless required by the Resolution to be deposited to any other Fund or Account, in accordance with the Resolution or the Financing Agreement.

"Revenues" means all revenues, rates, fees, charges, surcharges, rents, proceeds from the sale of LIPA Sub assets, proceeds of insurance, and other income and receipts, as derived in cash, directly or indirectly from any of LIPA Sub's operations, by or for the account of LIPA or LIPA Sub, including but not limited to (i) all payments received by LIPA or LIPA Sub with respect to the Promissory Notes, (ii) any guaranty of performance under any System Agreement and (iii) all dividends received by LIPA as a result of ownership of any stock or other evidences of an equity interest in LIPA Sub; provided, however, that Revenues shall not include (a) any Transition Charge, (b) any of the foregoing attributable directly or indirectly to the ownership or operation of any Separately Financed Project, or (c) any federal or State grant moneys the receipt of which is conditioned upon their expenditure for a particular purpose unless LIPA determines that such grant moneys shall constitute Revenues. Notwithstanding the foregoing, Revenues also shall not include any amounts, or amounts from any sources, as may be specified from time to time by a Supplemental Resolution; provided, however that at the time such Supplemental Resolution becomes effective the tests set forth in paragraph (e)(B) under the heading "Conditions Precedent to Delivery of Bonds" shall be satisfied without regard to either (i) such amounts or (ii) paragraph (e)(D) under the same heading.

"RG&E" means Rochester Gas and Electric Company.

"**RI/FS**" means Remedial Investigation and Feasibility Study.

"**RICO**" means the federal Racketeer Influenced and Corrupt Organization Act.

"**RMI**" or "**Consulting Engineer**" means Resource Management International, Inc., a wholly-owned subsidiary of the Metzler Group, Inc., and an independent consultant to LIPA and source of the Independent Consultant's Report.

"**S&P**" means Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc., and its successors and their assigns.

"**SALP Report**" means the Systematic Assessment of Licensee Performance Report delivered by the Regional Administrator of the NRC (concerning the two units at Nine Mile Point Station).

"**SEC**" means the United States Securities and Exchange Commission.

"**Separately Financed Project**" means any such project financed by revenues or other income derived solely from the ownership or operation of such Separately Financed Project or from other funds withdrawn from the Revenue Fund in accordance with the Resolution.

"**SEQRA**" means the New York State Environmental Quality Review Act, enacted in 1976, as amended.

"**Service Area**" or "**LIPA Service Area**" means the Counties of Suffolk and Nassau and that portion of the County of Queens constituting LILCO's electric franchise area as of the effective date of the LIPA Act. "Service Area" does not include the Villages of Freeport, Rockville Centre and Greenport.

"**Shoreham**" means the Shoreham Nuclear Power Station located at Shoreham, Long Island.

"**Shoreham Credits**" means credits to the bills of System ratepayers arising from the proposed settlement of the Shoreham Property Tax Litigation, currently proposed in each of the first five years in Nassau County and the Rockaways in the aggregate amount of $50 million per year and in Suffolk County in the aggregate amount of $30 million per year.

"**Shoreham Phase I Rebates**" means payments LIPA intends to make to the ratepayers in the Service Area related to $19 million attributable to the refund of Shoreham-related property taxes relating to over-assessments for the years prior to 1984.

"**Shoreham Property Tax Litigation**" means (i) the litigation initiated by LILCO against the Suffolk Taxing Jurisdictions resulting in a judgment in LILCO's favor, (the "Shoreham Phase II Judgement") ordering the Suffolk Taxing Jurisdictions to repay to LILCO $868 million (including interest) representing taxes levied and collected from LILCO based on over-assessments of Shoreham for the tax years 1984/85 through 1991/92 and (ii) the ability of LIPA to claim it is entitled to a refund from the Suffolk Taxing Jurisdictions of the approximately $327 million in PILOTs it has paid to the Suffolk Taxing Jurisdictions for the years 1992/93 through 1997/98 based on (a) a final court ruling that the LIPA Act does not prohibit an action by LIPA to recover PILOTs overpayments based upon an inflated assessed valuation of Shoreham and (b) the holding in the Shoreham Phase II Judgement to the effect that the value of Shoreham has been zero since before its acquisition by LIPA.

"**Shoreham Property Tax Settlement Agreement**" means the proposed agreement between LIPA and the Suffolk Taxing Jurisdictions to settle the Shoreham Property Tax Litigation and make

refunds to LILCO ratepayers who have borne the expense of overpayments of property taxes and PILOTs related to Shoreham.

"Shoreham Rebates" means payments LIPA intends to make to the ratepayers in the Service Area related to $62.5 million relating to the alleged over-assessment for the years 1984 through 1992.

"Shoreham Regulatory Asset" means the amount approved by the PSC for recovery of Shoreham related costs which have not yet been recovered through the rates of LILCO.

"Shoreham Site" means the location of the Shoreham nuclear power station.

"Sinking Fund Installment" means, as of any particular date of calculation, the amount required, as of such date of calculation, to be paid by LIPA on a future date for the retirement of Outstanding Bonds which are stated to mature subsequent to such future date, but does not include any amount payable by LIPA by reason only of the maturity of a Bond.

"Sound Cable" means the electric transmission cable system located under Long Island Sound that is jointly owned by LILCO and Connecticut Light and Power Company.

"Sound Cable Owners" means the owners of the Sound Cable, which are LILCO and the Connecticut Light and Power Company.

"State" means the State of New York.

"State Administrative Procedures Act" means the New York State Administrative Procedures Act, as amended.

"Study Period" means the period May 1, 1998 through December 31, 2008.

"Subordinated Contract Obligation" shall mean the Debt Service Component of a Supply Contract that does not constitute a Parity Contract Obligation.

"Subordinated Credit Facility" means a letter of credit, revolving credit agreement, standby purchase agreement, surety bond, insurance policy or similar obligation, arrangement or instrument issued by a bank, insurance company or other financial institution which (i) provides for payment of all or a portion of the principal of or interest on any Subordinated Indebtedness, (ii) provides funds for the purchase of any Bonds or Subordinated Indebtedness, or any portion of any thereof, or (iii) secures the payment by LIPA of its obligations under a Financial Contract relating to Bonds or Subordinated Indebtedness.

"Subordinated Indebtedness" means any bond, note or other evidence of indebtedness issued by LIPA in furtherance of its corporate purposes under the LIPA Act and secured by a pledge of the Trust Estate subordinate to the pledge thereof made by the Resolution in favor of the Bonds and Parity Obligations and otherwise as provided by the Resolution. Subordinated Indebtedness shall include, but shall not be limited to, Option Securities, Reimbursement Obligations other than Parity Reimbursement Obligations, and Financial Contracts to the extent provided by the Resolution.

"Subordinated Indebtedness Fund" means the fund established in accordance with the Resolution for payment of the principal and redemption price of and interest on Subordinated Indebtedness, subject to the provisions of the Resolution.

"Suffolk Surcharge" means the rate surcharge that LIPA intends to levy on ratepayers in Suffolk County to recover the costs associated with the bonds issued to fund the Shoreham Rebates and Shoreham Credits.

"Suffolk Taxing Jurisdictions" means, collectively, Suffolk County, the Town of Brookhaven, the Shoreham-Wading River Central School District, the Wading River Fire District, and the Shoreham-Wading River Library District.

"Supplemental Resolution" means a resolution of LIPA authorizing the issuance of a Series of Bonds or otherwise amending or supplementing the Resolution, adopted in accordance with the Resolution.

"Supply Contract" means any contract of LIPA or LIPA Sub with another entity for fuel, energy or power.

"System" means the Retained Assets and any System Improvements, but shall not include any Separately Financed Projects.

"System Agreements" means any agreements relating to the operation or maintenance of the System, the supply of power and energy to the System, and the provision of transmission and distribution services and capacity for the System, including, but not limited to, the Management Services Agreement, the Energy Management Agreement and the Power Supply Agreement.

"System Budget" means the combined Authority Budget and Subsidiary Budget, as amended or supplemented, adopted or in effect for a particular Fiscal Year, as provided in the Resolution and in the Financing Agreement.

"System Improvement" means any project, facility, system, equipment, or material related to or necessary or desirable in connection with the generation, production, transportation, transmission, distribution, delivery, storage, conservation, purchase or use of energy or fuel, whether owned jointly or singly by LIPA Sub, including any capacity or output in which LIPA Sub has an interest, heretofore or hereafter authorized by the LIPA Act or by other applicable State statutory provisions, including but not limited to demand side management programs; provided, however, that the term "System Improvement" shall not include any Separately Financed Project.

"System Manager" initially means, collectively, the BL Holding Corp Sub acting as Manager under the Management Services Agreement and the BL Holding Corp Sub acting as Energy Manager under the Energy Management Agreement, and thereafter means any person, company or entity who signs an agreement to operate some or all of System or System-related activities on behalf of LIPA Sub.

"T&D System" means the electric transmission and distribution system located in the Service Area which provides the means for transmitting and distributing electricity.

"Transferee Subsidiaries" means the various subsidiaries of BL Holding Corp to which the Transferred Assets are transferred.

"Transferred Assets" means LILCO's present gas transmission, distribution and supply assets and operations, non-nuclear generating assets, certain real estate and common plant.

"Transferred Business" means the business and operations to be conducted by BHC Parties after the Merger Closing.

"Transferred Liabilities" means liabilities associated with or traceable to the Transferred Assets or assumed by BL Holding Corp.

"Transition Charge" means any rates, fees, charges or surcharges relating to the System or the customers thereof established by irrevocable rate order or other action or instrument, and applicable to or by LIPA or LIPA Sub, in conjunction with the issuance of debt or other securities under a separate resolution, indenture or similar instrument (other than the Resolution) to the extent such rates, fees, charges or surcharges are pledged or otherwise encumbered or conveyed as security for such debt or other securities.

"Trust Estate" means collectively: (i) all payments received by LIPA from LIPA Sub under the Financing Agreement, and all rights to collect and receive the same; (ii) all Revenues and all right, title and interest of LIPA in and to the Revenues, including all rights of LIPA to collect and receive the same, including but not limited to (a) all payments received by LIPA with respect to the Promissory Notes and all right, title and interest of LIPA in and to the Promissory Notes, including all rights of LIPA to collect and receive amounts payable thereunder and (b) any dividends received by LIPA as a result of ownership of any common or preferred stock or other evidences or an equity interest of LIPA in LIPA Sub, and all rights to receive the same; (iii) the proceeds of sale of Bonds until expended for the purposes authorized by the Resolution; (iv) all Funds, Accounts and subaccounts established by the Resolution, including securities credited thereto and investment earnings thereon; and (v) all funds, moneys and securities and any and all other rights and interests in property, whether tangible or intangible, from time to time hereafter by delivery or by writing of any kind conveyed, mortgaged, pledged, assigned or transferred as and for additional security under the Resolution for the Bonds by LIPA, or by anyone on its behalf, or with its written consent, to the Trustee, which is authorized by the Resolution to receive any and all such property at any and all times, and to hold and apply the same subject to the terms of the Resolution.

"Trustee" means United States Trust Company of New York, New York, New York, and its successor or successors and any other person which may at any time be substituted in its place pursuant to the Resolution.

"Underwriters" means the underwriters listed on the cover page of this Official Statement.

SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION

Resolution to Constitute Contract

In consideration of the purchase and acceptance of the Bonds by those who shall hold the same from time to time, the provisions of the Resolution shall be deemed to be and shall constitute a contract between LIPA, the Trustee and the Holders from time to time of the Bonds; and the pledge made in the Resolution and the covenants and agreements therein set forth to be performed by or on behalf of LIPA shall be for the equal benefit, protection and security of the Holders of any and all the Bonds, each of which, regardless of the time or times of its issue or maturity, shall be of equal rank without preference, priority or distinction over any other thereof except as expressly provided in the Resolution.

Obligation of Bonds

The Bonds shall be special obligations of LIPA payable solely from the Trust Estate, and no other revenues or assets of LIPA shall be, or shall be deemed to be, pledged to the payment of the Bonds; provided, however, that nothing contained in the Resolution shall prevent the pledge of any Credit Facility relating to any particular Bonds, or the proceeds of such Credit Facility, to the payment of Bonds. The bonds, notes and other obligations of LIPA (including but not limited to the Bonds) shall not be a debt of the State or of any municipality, and neither the State nor any municipality shall be liable thereon. Neither the credit, the revenues nor the taxing power of the State or of any municipality shall be, or shall be deemed to be, pledged to the payment of any bonds, notes or other obligations of LIPA (including but not limited to the Bonds).

Conditions Precedent to Delivery of Bonds

Bonds may be issued pursuant to a Supplemental Resolution in such principal amount or amounts for each such Series as may be specified in such Supplemental Resolution. A Supplemental Resolution shall specify, among other things, the purpose or purposes for which such Bonds are being issued, the authorized principal amount and Series designation of such Bonds, the maturity date or dates and interest rate or rates of the Bonds and the forms of the Bonds which shall specify terms with respect to tender or redemption, if any. Such Bonds shall be delivered by LIPA under the Resolution upon the delivery of, among other things, a Supplemental Resolution authorizing such Bonds, a Counsel's Opinion with respect to the validity of the Bonds and a certificate of an Authorized Representative of LIPA to the effect that, upon delivery of the Bonds, LIPA will not be in default in the performance of the terms and provisions of the Resolution or of any of the Bonds, and a certificate of an Authorized Representative of LIPA Sub to the effect that LIPA Sub is not in default in the performance of any of the covenants, conditions, agreements or provisions contained in the Financing Agreement.

Except in the case of Refunding Bonds issued pursuant to the Resolution, the Trustee shall also receive the Certificate referred to in either paragraph (a) or (b) below, unless not required pursuant to subparagraph (d), as follows:

(a) A Certificate of an Authorized Representative of LIPA setting forth (i) the Revenues for any 12 consecutive calendar months out of the 18 calendar months immediately preceding the month in which such Bonds are to be issued, (ii) the Debt Service, and the amount payable under all Parity Contract Obligations, during such 12 month period for which Revenues are set forth pursuant to clause (i), excluding in each case any amount thereof paid from sources other than

Revenues, and (iii) the sum of the Required Deposits for such 12 month period (excluding Required Deposits for the payment of Outstanding Bonds and Parity Obligations), and showing that the amount set forth in clause (i) is at least equal to the sum of (x) 120% of the amount set forth in clause (ii) and (y) 100% of the amount set forth in (iii).

(b) A Certificate of a Rate Consultant setting forth (i) the estimated Revenues for each of the full Fiscal Years in the period beginning with the Fiscal Year in which such Bonds are authenticated and delivered and ending with the fifth full Fiscal Year after such date of authentication and delivery, (ii) the estimated Debt Service, and estimated amounts payable under all Parity Contract Obligations, during each Fiscal Year for which Revenues are estimated, (iii) the projected Debt Service, and projected amounts payable under Parity Contract Obligations, projected to be issued for any purpose during each Fiscal Year for which Revenues are estimated, and (iv) the sum of the estimated and projected Required Deposits for each such Fiscal Year (excluding Required Deposits for the payment of Outstanding Bonds and Parity Obligations), and showing that for each such Fiscal Year the amount set forth in clause (i) is at least equal to the sum of (x) 120% of the sum of the amounts set forth in clauses (ii) and (iii), and (y) 100% of the amount set forth in clause (iv). The Rate Consultant may base its estimates and projections upon such factors as it shall consider reasonable, a statement to which effect shall be included in such Certificate.

(c) For purposes of this section, (i) Revenues shall include any amounts withdrawn in any Fiscal Year from the Rate Stabilization Fund which were either (1) on deposit therein prior to such Fiscal Year or (2) proceeds of Bonds or Subordinated Indebtedness issued to fund the Shoreham Credits, (ii) Revenues shall not include any proceeds from the sale of LIPA Sub assets or proceeds of insurance, and (iii) any Debt Service, Parity Contract Obligations and Required Deposits shall not include any amounts thereof expected by LIPA to be paid from any funds, other than Revenues, reasonably expected by LIPA to be available therefor (including without limitation the anticipated receipt of proceeds of sale of Bonds or Subordinated Indebtedness, or moneys not a part of the Trust Estate, expected by LIPA to be used to pay the principal of Bonds, Parity Obligations, Outstanding LIPA Sub Unsecured Debt or Subordinated Indebtedness), which expectations, if included in a resolution of LIPA or Certificate of an Authorized Representative of LIPA filed with the Trustee, shall be conclusive.

(d) The provisions of this section shall not apply, (i) to the initial Series of Bonds issued under the Resolution, (ii) to any Bonds issued for any purposes described in the public offering statement issued by the Authority in connection with the initial Series of Bonds issued under the Resolution as part of the "Plan of Finance," in each such case if and to the extent not financed from the initial Series of Bonds issued under the Resolution, or (iv) at any time after LIPA shall have retired, other than from proceeds of Bonds or Subordinated Indebtedness, an amount equal to 25% of the Acquisition Debt net of the then outstanding balance of the Promissory Notes.

Any Supplemental Resolution may provide that (i) so long as a Credit Facility providing security (but not liquidity) is in full force and effect, and payment on the Credit Facility is not in default and the issuer of the Credit Facility is qualified to do business, the issuer of the Credit Facility shall be deemed to be the sole Owner of the Outstanding Bonds the payment of which such Credit Facility secures when the approval, consent or action of the Owners of such Bonds is required or may be exercised under the Resolution, or, in the alternative, that the approval, consent or action of the issuer of the Credit Facility shall be required in addition to the approval, consent or action of the applicable percentage of the Owners of Outstanding Bonds and including, without limitation, the Resolution and following an Event of Default, and (ii) in the event that the principal, sinking fund installments, if

any, and Redemption Price, if applicable, and interest due on any Outstanding Bonds shall be paid under the provisions of a Credit Facility, all covenants, agreements and other obligations of LIPA to the Owners of such Bonds shall continue to exist and such issuer of the Credit Facility shall be subrogated to the rights of such Owners in accordance with the terms of such Credit Facility.

Any Supplemental Resolution authorizing Bonds may delegate to any officers or employees of LIPA the determination of any details of such Bonds, within limitations which shall be set forth in such Supplemental Resolution. Any such determination shall be in writing, and each such written determination shall be deemed to be part of the Supplemental Resolution providing for the same.

Conditions Precedent to Delivery of Refunding Bonds

All Refunding Bonds shall be executed by LIPA for issuance and delivered to the Trustee, and thereupon shall be authenticated by the Trustee and delivered to LIPA or upon its order, but only upon the receipt by the Trustee of: (i) the documents required under the heading entitled "Conditions Precedent to Delivery of Bonds" and (ii) such documents, instructions, moneys and securities as are required by the provisions of the Resolution or any Supplemental Resolution adopted pursuant to the Resolution to cause the Bonds or portions thereof to be refunded to be paid or deemed to have been paid within the meaning and with the effect expressed in the Resolution.

Special Provisions Relating to Option Securities, Financial Contracts, Subordinated Credit Facilities, Parity Obligations and Subordinated Indebtedness

The Resolution provides that all Option Securities will be issued as Subordinated Indebtedness.

Payments to Qualified Counterparties under Financial Contracts shall constitute Subordinated Indebtedness, except that such payments under Financial Contracts relating to Outstanding LIPA Sub Unsecured Debt shall constitute Outstanding LIPA Sub Unsecured Debt.

In connection with any Bonds, LIPA may obtain or cause to be obtained one or more Credit Facilities and agree with the issuer of a Credit Facility to reimburse such issuer directly for amounts paid under the terms of such Credit Facility, together with interest thereon; provided, however, that no obligation to reimburse an issuer of a Credit Facility shall be created, for purposes of the Resolution, until amounts are paid under such Credit Facility. Such payments to reimburse the issuer of a Credit Facility are referred to as "Reimbursement Obligations." Any Reimbursement Obligation (a "Parity Reimbursement Obligation") may be secured by a pledge of and a lien on the Trust Estate on a parity with the lien created thereon by the Resolution. Any such Parity Reimbursement Obligation shall be deemed to be a part of the Series to which the Credit Facility which gave rise to such Parity Reimbursement Obligation relates.

Payments to reimburse the issuer of a Subordinated Credit Facility (a "Subordinated Reimbursement Obligation") shall constitute Subordinated Indebtedness.

With respect to any contract of LIPA or the LIPA Sub with another entity for fuel, energy or power (a "Supply Contract"), the obligation of LIPA or the LIPA Sub, as the case may be, to pay that portion of any rates, fees, charges, surcharges or payments for the specific purpose of meeting principal or interest or both on that entity's obligations directly associated with such contract and payable to such entity regardless of whether fuel or energy is delivered or made available for delivery and the principal and/or interest component of any Capital Lease, (such portion or component, the

"Debt Service Component") shall be (i) payable from Revenues and secured by a pledge of, and lien on, the Trust Estate on a parity with the lien created by the Resolution to secure the Bonds (a "Parity Contract Obligation") only if, when such Supply Contract or Capital Lease is entered into, LIPA shall have satisfied the test set forth above in either paragraph (a) or (b) under the heading "Conditions Precedent to Delivery of Bonds", subject to paragraph (d) under the same heading, with respect to such Debt Service Component or (ii) payable from funds withdrawn from the Revenue Fund as permitted by the Resolution, in all other events.

Separately Financed Project

Nothing in the Resolution shall prevent LIPA from authorizing and issuing bonds, notes, or other obligations or evidencing of indebtedness other than Bonds, for any purpose of LIPA authorized by the LIPA Act or by other applicable State statutory provisions, or from financing any such purpose from other available funds (such purpose being referred to in the Resolution as a "Separately Financed Project"), if the debt service on such bonds, notes, or other obligations or evidences of indebtedness, if any, and LIPA's share of any operating expenses related to such Separately Financed Project, are payable solely from the revenues or other income derived from the ownership or operation of such Separately Financed Project or from other funds withdrawn from the Revenue Fund as permitted by the Resolution, and may be secured by LIPA's or any LIPA subsidiary's ownership interest therein.

Pledge of Funds and Revenues

The Trust Estate is pledged for the payment of the Bonds and Parity Obligations in accordance with their terms and the provisions of the Resolution, subject only to the provisions of the Resolution, the LIPA Act and the Financing Agreement permitting the application thereof. As further security for the payment of the Bonds and Parity Obligations, LIPA assigns, transfers and pledges to the Trustee all of its rights and interests under and pursuant to the Financing Agreement (excluding rights to notice and other procedural rights, its rights to indemnification and rights and interests not material to Bondholders).

The Resolution establishes the following funds:

(1) Construction Fund, to be held by LIPA;

(2) Revenue Fund, to be held by LIPA;

(3) Operating Expense Fund, to be held by LIPA;

(4) Debt Service Fund, to be held by the Trustee;

(5) Parity Contract Obligations Fund, to be held by LIPA;

(6) Subordinated Indebtedness Fund, to be held by LIPA, except as may otherwise be permitted by the Resolution; and

(7) Subsidiary Unsecured Debt Fund, to be held by LIPA;

(8) PILOTs Fund, to be held by LIPA; and

(9) Rate Stabilization Fund, to be held by LIPA.

The Trustee shall, at the request of LIPA, establish within any Fund held by the Trustee such Accounts or sub-accounts. LIPA may do likewise with respect to any Fund held by it.

Construction Fund

The Resolution provides that LIPA shall deposit into the Construction Fund any amount required to be deposited therein pursuant to the Resolution or the Financing Agreement, and any other amounts received by LIPA for or in connection with the System and determined by LIPA to be deposited therein, which are not otherwise required to be applied in accordance with the Resolution. LIPA shall also deposit in the Construction Fund, the proceeds of insurance, if any, maintained by LIPA or LIPA Sub against physical loss of or damage to the System, or of contractors' performance bonds with respect thereto, pertaining to the period of acquisition or construction of System Improvements, to the extent not deposited to the Revenue Fund. Except as otherwise provided in the Resolution, amounts in the Construction Fund shall be expended only to pay Costs of System Improvements in the amounts, at the times, in the manner, and on other terms and conditions as determined by LIPA from time to time. To the extent that other moneys are not available therefor in any of the other Funds and Accounts established under the Resolution, amounts in the Construction Fund shall be applied to the payment of the Principal Installments of and interest on Bonds.

Revenue Fund

The Resolution provides that LIPA shall, as promptly as practicable after receipt thereof by LIPA, deposit all Revenues in the Revenue Fund, unless required by the Resolution to be deposited to any other Fund or Account. There shall also be deposited in the Revenue Fund all other amounts required by the Resolution or the Financing Agreement to be so deposited.

Payments Into Certain Funds

The Resolution provides that amounts on deposit from time to time in the Revenue Fund shall be withdrawn and deposited as follows and, as of any time, in the following order of priority:

FIRST: to the Operating Expense Fund, the amount determined by LIPA from time to time to be deposited thereto to pay, or to be set aside therein as a reserve for the payment of, Operating Expenses; and

SECOND: (A) to the Debt Service Fund, the amounts required to pay or provide for the payment of the Principal Installments and Redemption Price of and interest on Bonds and Parity Reimbursement Obligations; provided, however, that no such amount shall be required to be deposited therein in advance of one business day prior to the due date of any such payment;

(B) to the Parity Contract Obligations Fund, the amount determined by LIPA to be required to be deposited therein to pay or provide for the payment of Parity Contract Obligations provided, however, that no such amount shall be required to be deposited therein in advance of one business day prior to the due date of any such payment;

provided, however, that if the balance remaining to make all such deposits is less than sufficient to do so in full, deposits shall be made pro rata between the Debt Service Fund and the Parity Contract Obligations Fund in the same ratio that the amount required to be deposited thereto bears to the sum of the amount required to be deposited to each such Fund;

THIRD: if such amounts are not expected by LIPA to be required thereafter for purposes of paragraphs FIRST or SECOND above, to the Subordinated Indebtedness Fund, the amount determined by LIPA to be required to be deposited therein to pay or provide for the payment of principal and

redemption price of and interest on Subordinated Indebtedness in accordance with the Resolution; provided, however, that no such amount shall be required to be deposited therein in advance of one business day prior to the due date of any such payment;

FOURTH: if such amounts are not expected by LIPA to be required thereafter for purposes of paragraphs FIRST, SECOND or THIRD above, to the Subsidiary Unsecured Debt Fund, the amount determined by LIPA to be required to be deposited therein to pay or provide for the payment of Outstanding LIPA Sub Unsecured Debt in accordance with the Resolution;

FIFTH: if such amounts are not expected by LIPA to be required thereafter for purposes of paragraphs FIRST, SECOND, THIRD or FOURTH above, to the PILOTs Fund, the amount determined by LIPA to be required to be deposited in such Fund to pay or provide for the payment of PILOTs in accordance with the Resolution in accordance with the System Budget or the entire balance if less than sufficient; and

SIXTH: if such amounts are not expected by LIPA to be required thereafter for purposes of paragraphs FIRST, SECOND, THIRD, FOURTH or FIFTH above, to the Rate Stabilization Fund, the amount determined by LIPA to be deposited therein to provide for any payments or deposits from Revenues thereafter.

Any moneys remaining in the Revenue Fund at any time and not deposited as set forth above may be retained in the Revenue Fund or may be withdrawn and used for any lawful purpose of LIPA or LIPA Sub as determined by LIPA, including but not limited to the purchase or redemption of any bonds, notes or other obligations of LIPA or LIPA Sub and, to the extent specified by LIPA, the payment of any incentive payments payable by LIPA Sub under any System Agreements which are not payable as an Operating Expense; provided, however, that prior to any such withdrawal, LIPA shall have determined, taking into account, among other considerations, anticipated future receipts of Revenues and other moneys constituting part of the Trust Estate, that the moneys to be withdrawn are not needed for any other purpose provided in paragraphs FIRST through SIXTH set forth above. Amounts paid out or withdrawn pursuant to this paragraph shall be free and clear of the lien and pledge created by the Resolution unless deposited into any Fund or Account; provided, however, that to the extent amounts are paid out or withdrawn for the purpose of paying any expense of the Subsidiary, such amounts shall remain subject to the lien and pledge of the Resolution until such amounts are actually applied by LIPA or LIPA Sub to the payment of such expense.

Purchases of Bonds or Subordinated Indebtedness from amounts in the Revenue Fund shall be made at the direction of LIPA, with or without advertisement and with or without notice to other Holders of Bonds or Subordinated Indebtedness. Such purchases shall be made at such price or prices as determined by LIPA. If Sinking Fund Installments have been established for the maturities of Bonds purchased by LIPA, then LIPA shall direct the Trustee to credit the principal amount purchased against the applicable Sinking Fund Installments in such order and amounts as are determined by LIPA.

Operating Expense Fund

Amounts credited to the Operating Expense Fund shall be applied from time to time solely to the payment of Operating Expenses at the times, in the manner, and on the other terms and conditions as determined by LIPA from time to time. If and to the extent provided in a Supplemental Resolution

authorizing Bonds, amounts from the proceeds of such Bonds may be credited to the Operating Expense Fund and set aside therein as specified in the Supplemental Resolution for any purpose of such Fund.

Debt Service Fund

The Trustee shall for all Outstanding Bonds and Parity Reimbursement Obligations, pay (i) on each Bond Payment Date, (1) from the moneys on deposit in the Debt Service Fund the amounts required for the payment of the Principal Installments, if any, due on such Bond Payment Date and (2) from the moneys on deposit in the Debt Service Fund, including the moneys credited to the sub-account, if any, established for such Series in the Capitalized Interest Account, the interest due on such Bond Payment Date, and (ii) on any redemption date or date of purchase, the amounts required for the payment of accrued interest on Bonds to be redeemed or purchased on such date unless the payment of such accrued interest shall be otherwise provided.

As soon as practicable after the forty-fifth day preceding the due date of any Sinking Fund Installment, the Trustee shall proceed to call for redemption, pursuant to the Resolution, Bonds of the Series and maturity for which such Sinking Fund Installment was established in such amount as shall be necessary to complete the retirement of the principal amount specified for such Sinking Fund Installment of the Bonds of such Series and maturity. The Trustee shall so call such Bonds for redemption whether or not it then has moneys in the Debt Service Fund sufficient to pay the applicable Redemption Price thereof on the redemption date. The Trustee shall apply to the redemption of the Bonds on each such redemption date the amount required for the redemption of such Bonds.

Parity Contract Obligations Fund

The Resolution provides that amounts credited to the Parity Contract Obligations Fund shall be applied from time to time solely to pay or provide for the payment of Parity Contract Obligations at the times, in the manner, and on the other terms and conditions as determined by LIPA from time to time, subject to the Resolution which provides that if at any time any amount remains on deposit in the Parity Contract Obligations Fund which LIPA determines is not required thereafter for purposes thereof, such amount shall be transferred to the Revenue Fund.

Subordinated Indebtedness Fund

Amounts on deposit in the Subordinated Indebtedness Fund shall be applied by LIPA solely to pay or provide for the payment of the principal and redemption price of and interest on Subordinated Indebtedness, or as otherwise provided by the resolution of LIPA authorizing each issue of Subordinated Indebtedness, subject to the provisions set forth below under this heading.

If at any time the amounts in the Operating Expense Fund, Debt Service Fund or Parity Contract Obligations Fund shall be less than the current requirements thereof, LIPA shall withdraw from the Subordinated Indebtedness Fund and deposit in such other Funds the amounts necessary (or all the moneys in the Subordinated Indebtedness Fund, if less than the amounts necessary, applying available amounts in the order of priority and otherwise as specified in the Resolution), to make up such deficiency.

If at any time any amount remains on deposit in the Subordinated Indebtedness Fund which LIPA determines is not required thereafter for purposes thereof, such amount shall be transferred to the Revenue Fund.

Subsidiary Unsecured Debt Fund

Amounts on deposit in the Subsidiary Unsecured Debt Fund shall be applied by LIPA solely to the payment of the principal of and interest on Outstanding LIPA Sub Unsecured Debt, subject to the provisions below.

If at any time the amounts in the Operating Expense Fund, Debt Service Fund, Parity Contract Obligations Fund or Subordinated Indebtedness Fund shall be less than the current requirements thereof, LIPA shall withdraw from the Subsidiary Unsecured Debt Fund and deposit in such other Funds the amounts necessary (or all the moneys in said Fund, if less than the amounts necessary, applying available amounts in the order of priority and otherwise as specified in the Resolution), to make up such deficiency.

If at any time any amount remains on deposit in the Subsidiary Unsecured Debt Fund which LIPA determines is not required thereafter for purposes thereof, such amount shall be transferred to the Revenue Fund.

PILOTs Fund

Amounts on deposit in the PILOTs Fund shall be applied by LIPA, or paid to the LIPA Sub for application by LIPA Sub, solely to make payments to the State, or any municipality or other political subdivision of the State, which shall be entitled to receive PILOTs under the LIPA Act, at such times and in such amounts as LIPA shall determine to be required to make such payments, subject to the provisions below.

If at any time the amounts in the Operating Expense Fund, Debt Service Fund, Parity Contract Obligations Fund, Subordinated Indebtedness Fund or Subsidiary Unsecured Debt Fund shall be less than the current requirements thereof, LIPA shall withdraw from the PILOTs Fund and deposit in such other Funds the amounts necessary (or all the moneys in the PILOTs Fund, if less than the amounts necessary, applying available amounts in the order of priority and otherwise as specified in the Resolution), to make up such deficiency.

Amounts on deposit in the PILOTs Fund which LIPA may determine to be in excess of the amount required to be maintained therein for the purposes of such Fund shall be transferred to the Revenue Fund.

Rate Stabilization Fund

Amounts on deposit in the Rate Stabilization Fund may be used for any lawful purpose of LIPA or LIPA Sub, including but not limited to making any deposits required by the Resolution to any Fund or Account, as determined by LIPA; provided, however, that no such deposit to any such Fund or Account shall be required except as specified by the provisions below.

If at any time the amounts in the Operating Expense Fund, Debt Service Fund, Parity Contract Obligations Fund, Subordinated Indebtedness Fund, Subsidiary Unsecured Debt Fund or PILOTs Fund shall be less than the current requirements thereof, LIPA shall withdraw from the Rate Stabilization Fund and deposit in such other Funds the amounts necessary (or all the moneys in the Rate Stabilization Fund, if less than the amounts necessary, applying available amounts in the order of priority and otherwise as specified in the Resolution), to make up such deficiency.

Amounts on deposit in the Rate Stabilization Fund which LIPA may determine to be in excess of the amount required to be maintained therein for the purposes of such Fund shall be transferred to the Revenue Fund.

Investment of Certain Funds

Moneys held in all Funds and Accounts shall be invested and reinvested by LIPA or the Trustee, as the case may be, to the fullest extent practicable in Investment Securities which mature not later than at such times as shall be necessary to provide moneys when needed for payment to be made from such Funds and Accounts, subject, in the case of the Subordinated Indebtedness Fund and Subsidiary Unsecured Debt Fund, to the terms of any resolutions, indentures, or other instruments securing any issue of Subordinated Indebtedness or Outstanding Subsidiary Unsecured Debt, as the case may be. The Trustee shall make all such investments of moneys held by it in accordance with written instructions from any Authorized Representative of LIPA. In making any investment in any Investment Securities with moneys in any Fund or Account established under the Resolution, LIPA may, and may instruct the Trustee to, combine such moneys with moneys in any other Fund or Account, but solely for purposes of making such investment in such Investment Securities.

Interest (net of that which represents a return of accrued interest paid in connection with the purchase of any investment) and other investment earnings on any moneys or investments in the Funds and Accounts, other than the Construction Fund and Capitalized Interest Account, shall be paid into the Revenue Fund as and when received. Interest (net of that which represents a return of accrued interest paid in connection with the purchase of any investment) and other investment earnings on any moneys or investments in the Construction Fund and Capitalized Interest Account shall remain in such Fund or Account, respectively, unless LIPA elects to pay the same into the Revenue Fund.

Rate Covenants; Related Obligations

LIPA shall establish and maintain System fees, rates, rents, charges and surcharges sufficient in each Fiscal Year so that Revenues reasonably expected to be produced in such Fiscal Year will be at least equal to the sum of (i) 120% (except, after LIPA shall have retired, other than from proceeds of Bonds or Subordinated Indebtedness, an amount equal to 25% of the Acquisition Debt net of the then outstanding balance of the Promissory Notes, 100%) of Debt Service, and amounts under all Parity Contract Obligations, payable by LIPA in such Fiscal Year, (ii) 100% of the Operating Expenses payable in such Fiscal Year, (iii) 100% of the amount necessary to pay all PILOTs payable in such Fiscal Year, and (iv) 100% of the amount necessary to pay other Required Deposits, all other payments required pursuant to the Resolution and the Financing Agreement, and all other payments required for the System, for such Fiscal Year; provided, however, that if at any time such fees, rates, rents, charges and surcharges are or will be insufficient to meet the requirements of the Resolution, it shall not constitute a violation of the Resolution if and to the extent LIPA promptly takes action reasonably expected by LIPA to cure or avoid any such deficiency or to cause the same to be cured or avoided, or if LIPA complies with the provisions of the last paragraph set forth under this heading. Revenues shall include (i) any amount withdrawn or expected to be withdrawn thereafter in any Fiscal Year from the Rate Stabilization Fund which were either (a) on deposit therein prior to such Fiscal Year or (b) proceeds of Bonds or Subordinated Indebtedness issued to fund the Shoreham Credits, (ii) Revenues shall not include any proceeds from the sale of LIPA Sub assets or proceeds of insurance and (iii) Debt Service, Parity Contract Obligations, PILOTs and other Required Deposits shall not include any amounts thereof expected by LIPA to be paid from any funds, other than Revenues, reasonably expected by LIPA to be available therefor (including without limitation the anticipated receipt of proceeds of sale of Bonds or Subordinated Indebtedness, or moneys not a part of the Trust Estate,

expected by LIPA to be used to pay the principal of Bonds, Parity Contract Obligations, Outstanding LIPA Sub Unsecured Debt or Subordinated Indebtedness other than proceeds of Bonds or Subordinated Indebtedness issued to fund the Shoreham Credits), which expectations, if included in a resolution of LIPA or Certificate of an Authorized Representative, shall be conclusive.

LIPA shall review, or cause LIPA Sub to review, the adequacy of System fees, rates, rents, charges and surcharges at least annually. If such annual or more frequent review, or the report of the Rate Consultant pursuant to the Resolution, indicates that the rates, fees, rents, charges and surcharges are, or will be, insufficient to meet the requirements of the provisions stated in the preceding paragraph, LIPA shall promptly take, or cause LIPA Sub to take, the necessary action to cure or avoid any such deficiency, except as otherwise may be provided by the last paragraph under this heading.

Except to the extent required by law, LIPA will not permit LIPA Sub to furnish or supply or cause to be furnished or supplied any product, use or service of the System free of charge (or at a nominal charge) to any person, firm or corporation, public or private, unless and to the extent LIPA shall have determined that other adequate consideration has been or is expected to be received by LIPA Sub in connection therewith, and LIPA will cause LIPA Sub to enforce or cause to be enforced the payment of any and all amounts owing to LIPA Sub for use of the System in accordance with the Financing Agreement.

The failure in any Fiscal Year to comply with the covenant in clauses (i) (but only to the extent of the excess, if any, over 100% of Debt Service and amounts under all Parity Contract Obligations), (iii) and (iv) of the first sentence of the first paragraph above (the ''non-debt service and operating expense rate covenant'') shall not constitute an Event of Default if LIPA shall comply with the provisions contained in this paragraph. If LIPA shall fail in any Fiscal Year to comply with the non-debt service and operating expense rate covenant, LIPA shall retain a Rate Consultant and a Consulting Engineer for the purpose of reviewing System fees, rates, rents, charges and surcharges and reviewing the System Budget in the manner described in the Resolution. If the Rate Consultant (relying upon the certificate of the Consulting Engineer) shall be of the opinion, as shown by a certificate filed with the Trustee pursuant to the Resolution, that a schedule of fees, rates, rents, charges and surcharges for the System which would provide funds to meet the requirements specified in the non-debt service and operating expense rate covenant is impracticable at that time and LIPA therefore cannot comply with the non-debt service and operating expense rate covenant, then LIPA shall fix and establish such schedule of System fees, rates, rents, charges and surcharges as is recommended in such certificate by the Rate Consultant to comply as nearly as practicable with the non-debt service and operating expense rate covenant and in such event the failure of LIPA to comply with the non-debt service and operating expense rate covenant, shall not constitute an Event of Default. The Rate Consultant's certificate shall be accompanied by a certificate of the Consulting Engineer setting forth estimates of amounts required as provided by the Resolution for the then-current and the ensuing two Fiscal Years.

Tax Covenant

In the First Supplemental Resolution, LIPA has covenanted not to take or omit to take any action which would cause interest on any Series 1998 A Bond to be included in the gross income of any Owner thereof for Federal income tax purposes by reason of subsection (b) of Section 103 of the Internal Revenue Code of 1986 (Title 26 of the United States Code) as in effect on the date of original issuance of the Series 1998A Bonds (for purposes of this paragraph, the ''Code'') and, without limiting the generality of the foregoing, that no part of the proceeds of any Bonds or any other funds of LIPA

shall be used directly or indirectly to acquire any securities or obligations the acquisition of which would cause any Series 1998 A Bond to be an "arbitrage bond" as defined in section 148 of the Code and to be subject to treatment under subsection (b)(2) of Section 103 of the Code as an obligation not described in subsection (a) of said section. Notwithstanding any other provision of the Resolution to the contrary, upon the Authority's failure to observe, or refusal to comply with, this covenant, remedies are limited to specific performance and the Owners and Trustee shall not be entitled to any other rights and remedies provided under the Resolution.

The foregoing tax covenant does not apply to the Series 1998A Bonds maturing December 1, 1999 and bearing interest at a rate of 5.94%.

Consulting Engineer and Rate Consultant

Subject to the Resolution, LIPA shall employ or cause LIPA Sub to employ a Consulting Engineer and a Rate Consultant whose duties, respectively, shall be to make any certificates and perform any other acts required or permitted of the Consulting Engineer and the Rate Consultant under the Resolution or under the Financing Agreement.

Commencing with Fiscal Year 1999 and no less frequently than every other Fiscal Year thereafter, the Consulting Engineer and the Rate Consultant shall make an examination of, and shall report on, the properties and operations of the System. Such report shall be submitted to LIPA, LIPA Sub, and the Trustee no later than eight months after the close of the Fiscal Year to which such examination relates and shall set forth the following: (i) the Consulting Engineer's advice and recommendation as to the proper operation, maintenance and repair of the System during the ensuing two Fiscal Years, and an estimate of the amounts of money necessary for such purposes; (ii) the Consulting Engineer's advice and recommendations as to improvements which should be made during the ensuing two Fiscal Years, and an estimate of the amounts of money necessary for such purposes, showing the amount projected to be expended during such Fiscal Years from the proceeds of Bonds or Subordinated Indebtedness issued under or pursuant to the Resolution; (iii) the Rate Consultant's recommendation as to any necessary or advisable revisions of rates, fees, rents, charges and surcharges and such other advice and recommendation as it may deem desirable; and (iv) the Consulting Engineer's findings as to whether the System has been maintained in good repair and sound operating condition, and its estimate of the amount, if any, required to be expended to place such properties in such condition and the details of such expenditures and the approximate time required therefor.

LIPA covenants that if any such report shall set forth that the properties of the System have not been maintained in good repair and sound operating condition, it will cause LIPA Sub to promptly restore the properties to good repair and sound operating condition with all expedition practicable.

At any time after the expiration of the term of the initial Management Services Agreement LIPA may perform any duty or obligation of the Consulting Engineer or Rate Consultant for certain purposes as provided in the Resolution.

Further Assurance

At any and all times LIPA shall, so far as it may be authorized by law, pass, make, do, execute, acknowledge and deliver, all and every such further resolutions, acts, deeds, conveyances, assignments, transfers and assurances as may be necessary or desirable for better assuring, conveying, granting, pledging, assigning and confirming all and singular, the rights, assets, revenues and other moneys, securities, funds and property pledged or assigned by the Resolution, or intended so to be, or which LIPA may become bound to pledge or assign.

Indebtedness and Liens

The Resolution provides that LIPA shall not, and shall not permit or allow LIPA Sub to, issue any bonds, notes or other evidences of indebtedness or otherwise incur any indebtedness or contract obligations, other than Bonds or Parity Obligations, secured by a pledge of or other lien or charge on the Trust Estate which is prior to or of equal rank or priority with the pledge made by the Resolution. LIPA shall not create or cause to be created, and shall not permit or allow LIPA Sub to create or cause to be created, any lien or charge on the Trust Estate which is prior to or of equal rank or priority with the pledge made by the Resolution.

LIPA may issue either (i) Subordinated Indebtedness payable from the Subordinated Indebtedness Fund, secured by a pledge of and lien or charge on the Trust Estate, and further secured by an assignment of rights and interests under and pursuant to the Financing Agreement to the extent provided by the Resolution, in each case subject and subordinate in all respects to the pledge thereof and lien and charge thereon, or assignment thereof, as the case may be, created by the Resolution in favor of Bonds and Parity Obligations, or (ii) other bonds, notes or other evidences of indebtedness for borrowed money payable from funds withdrawn from the Revenue Fund as permitted by the Resolution.

Agreement of the State

The Resolution provides that, in accordance with Section 1020-o of the LIPA Act, LIPA, as agent for the State, agrees with the holders of obligations issued under the Resolution that the State will not limit or alter the rights vested in LIPA by the LIPA Act until such obligations together with the interest thereon are fully met and discharged, provided that nothing contained in the Resolution shall preclude such limitation or alteration if and when adequate provision shall be made by law for the protection of the Holders of such obligations of LIPA.

Annual System Budget

Prior to the beginning of each Fiscal Year commencing with Fiscal Year 1999, LIPA shall file with LIPA Sub and the Trustee an annual System Budget for the ensuing Fiscal Year which shall set forth in reasonable detail the estimated Revenues and Operating Expenses for the System for such year. Such annual System Budget shall include the LIPA Sub Budget (as such term is defined in the Financing Agreement) and the LIPA Budget and also may set forth such additional material as LIPA may determine. At the end of each quarter, LIPA shall review its estimates for such Fiscal Year, and in the event such estimates do not substantially correspond with actual Revenues or Operating Expenses, or if there are at any time during any such Fiscal Year extraordinary receipts or payments of unusual costs, LIPA shall prepare an amended annual System Budget for the remainder of the then current Fiscal Year. LIPA also may at any time adopt an amended annual System Budget for the remainder of the then-current Fiscal Year.

If for any reason LIPA shall not have adopted the System Budget by the time required by the Resolution, the System Budget for the then-current Fiscal Year shall be deemed to be the System Budget for the ensuing Fiscal Year until a new System Budget is adopted.

Deposits to Funds

The Resolution provides that LIPA will take such action as may be required to cause all Revenues to be deposited in the Revenue Fund (or, if so required by the Resolution, any other Fund or Account).

Enforcement and Amendment of Financing Agreement

LIPA shall enforce or cause to be enforced the provisions of the Financing Agreement and duly perform its covenants and agreements under the Financing Agreement. LIPA will not consent or agree to or permit any rescission of or amendment to or otherwise take any action under or in connection with the Financing Agreement except in accordance with the Resolution.

Amendments to Financing Agreement

Except as otherwise provided in the Resolution, the Financing Agreement may not be amended, changed, modified or terminated, nor may any provision thereof be waived, without the consent of the Holders of Outstanding Bonds as provided in the Resolution, if such amendment, change, modification, termination or waiver adversely affects the interest of the Holders of Outstanding Bonds in any material respect.

No such amendment, change, modification, termination or waiver shall take effect unless the prior written consent of (a) the Holders of at least a majority in principal amount of the Bonds then Outstanding, or (b) in case less than all Bonds then Outstanding are affected by the amendment, change, modification, termination or waiver, the Holders of not less than a majority in principal amount of the Bonds so affected and then Outstanding; provided, however, that if such amendment, change, modification, termination or waiver will, by its terms, not take effect so long as any specified Bonds remain Outstanding, the consent of the Holders of such Bonds shall not be required and such Bonds shall not be deemed to be Outstanding for the purpose of any such calculation of Outstanding Bonds.

For purposes of this section, any purchasers of the Bonds, whether purchasing as underwriters, for resale or otherwise, upon such purchase, may consent to an amendment, change, modification, termination or waiver permitted by this section with the same effect as a consent given by the Holders of such Bonds.

For the foregoing purposes, a Bond shall be deemed to be adversely affected by an amendment, change, modification, termination or waiver of the Financing Agreement if the same adversely affects or diminishes the rights of the Holder of such Bond in any material respect. The Trustee may in its discretion determine whether or not, in accordance with the foregoing provisions, any particular Bond would be adversely affected in any material respect by any amendment, change, modification, termination or waiver, and any such determination shall be binding and conclusive on LIPA and all Holders of Bonds.

For the foregoing purposes, the Trustee shall be entitled to rely upon an opinion of counsel, which counsel shall be satisfactory to the Trustee, with respect to whether any amendment, change, modification, termination or waiver adversely affects the interests of any Holders of Bonds then Outstanding in any material respect.

No Competitive Facilities

LIPA shall not construct, acquire or operate any plants, structures, facilities or properties which will provide electric transmission or distribution service in the Service Area (as defined in the LIPA Act) in competition with and not as part of the System unless such construction, acquisition or operation, in the judgment of LIPA, does not materially impair the ability of LIPA to comply with the rate covenant in the Resolution.

Disposition of Assets

LIPA shall not sell or otherwise dispose of, or encumber or grant a security interest in, any common or preferred stock or other evidence of LIPA's equity interest in LIPA Sub, unless LIPA or any subsidiary thereof shall thereupon own or effectively control the operation of the System. Except as provided by the Financing Agreement, LIPA shall not dispose of, or cause the disposition of, or permit to be disposed of, any real or personal properties of the System unless such disposal, in the judgment of LIPA, (i) is desirable in the conduct of the business of the System and (ii) does not materially impair the ability of LIPA to comply with the rate covenant in the Resolution.

Supplemental Resolutions; Amendments

LIPA may adopt (without the consent of any Holder) supplemental resolutions to, among others, authorize additional Bonds; to add to the restrictions contained in the Resolution upon the issuance of additional indebtedness; to add to covenants of LIPA contained in, or surrender any rights reserved to or conferred upon it by, the Resolution; to confirm any pledge under the Resolution or subject other property to the pledge; to permit qualification of the Resolution under, or add provisions permitted by, the Trust Indenture Act of 1939 or any similar Federal statute, and permit the qualification of the Bonds for sale under the securities laws of any state in the United States; to comply with such regulations and procedures as are from time to time in effect relating to establishing and maintaining a book-entry-only system; to comply with the requirements of any Rating Agency in order to maintain or improve a rating on the Bonds by such Rating Agency; to implement the last sentence of the definition of Revenues in the Resolution; to modify any provision of the Resolution, provided that such modification is effective upon or prior to the issuance of any Bonds affected or is effective only after all Bonds theretofore Outstanding cease to be Outstanding; to cure any ambiguity, supply any omission or to correct any defect or inconsistent provision in the Resolution; or to modify any provision provided that such modification shall not adversely affect the interests of the Bondholders in any material respect (and also provided that the Trustee consents thereto).

Any of the provisions of the Resolution may be amended by LIPA upon the written consent of the Holders of at least a majority in principal amount of the Bonds Outstanding at the time such consent is given, and in case less than all Bonds then Outstanding are affected by the modification or amendment, of the Holders of at least a majority in principal amount of such Outstanding Bonds that are or may be so affected; except that if such modification or amendment will, by its terms, not take effect so long as any particular Bonds remain Outstanding, the consent of the Holders of such Bonds shall not be required and such Bonds shall not be deemed to be Outstanding for the purpose of any calculation of Outstanding Bonds under the Resolution. No such modification or amendment shall permit a change in the terms of redemption or maturity of the principal of any Outstanding Bond or of any installment of interest thereon or a reduction in the principal amount or the Redemption Price thereof or in the rate of interest thereon without the consent of the Holder of such Bond, or shall reduce the percentages or otherwise affect the classes of Bonds the consent of the Holders of which is required to effect any such modification or amendment, or shall change or modify any of the rights or obligations of any Fiduciary without its written assent thereto. For the purposes of this paragraph, a Bond shall be deemed to be affected by a modification or amendment of the Resolution if the same materially and adversely affects or diminishes the rights of the Holder of such Bond.

Events of Default; Remedies Upon Default

Pursuant to the Resolution, any of the following events set forth in clauses (1) through (6) constitutes an "Event of Default" if: (1) LIPA defaults on the payment of Principal or the Redemption

Price of any Bond; or (2) LIPA defaults on the payment of any installment of interest on any Bond, and such default shall continue for a period of five (5) days; or (3) LIPA defaults in the performance or observance of any other of the covenants, agreements or conditions on its part in the Resolution, any Supplemental Resolution or in the Bonds contained, and such default shall continue for a period of sixty (60) days after written notice thereof (and stating that it is a "Notice of Default") to the Authority by the Trustee, or to both by the Holders of not less than sixty-six and two-thirds percent (66⅔%) of the principal amount of Bonds Outstanding, provided that if such default shall be such that it cannot be corrected within such sixty day period, it shall not constitute an Event of Default if corrective action is instituted within such period and diligently pursued until the failure is corrected; or (4) LIPA Sub defaults under the Financing Agreement and such default continues for a period of sixty (60) days after written notice thereof (and stating that it is a "Notice of Default") to the Authority by the Trustee, or to both by the Holders of not less than sixty-six and two-thirds percent (66⅔%) of the principal amount of Bonds Outstanding, provided that if such default shall be such that it cannot be corrected within such sixty day period, it shall not constitute an Event of Default if corrective action is instituted within such period and diligently pursued until the failure is corrected; or (5) if LIPA or LIPA Sub (a) files a petition seeking a composition of its indebtedness under the Federal bankruptcy laws, or under any other applicable law or statute of the United States of America or of the State; (b) consents to the appointment or taking possession by a receiver, liquidator, assignee, custodian, trustee, sequestrator or other similar official of LIPA or LIPA Sub or any substantial portion of either of their property; (c) makes any assignment for the benefit of creditors; or (d) admits in writing its inability generally to pay its debts generally as they become due; or (6) if (a) a decree or order for relief is entered by a court having jurisdiction of LIPA or LIPA Sub adjudging LIPA or LIPA Sub a bankrupt or insolvent or approving as properly filed a petition seeking reorganization, arrangement, adjustment or composition in respect of LIPA or LIPA Sub in an involuntary case under the Federal bankruptcy laws, or under any other applicable law or statute of the United States of America or of the State; (b) a receiver, liquidator, assignee, custodian, trustee, sequestrator or other similar official of LIPA or LIPA Sub or of any substantial portion of either of their property is appointed; or (c) the winding up or liquidation of its affairs is ordered and the continuance of any such decree or order unstayed and in effect for a period of sixty (60) consecutive days.

Upon an Event of Default, the Trustee may and, upon the written request of the Holders of not less than sixty-six and two-thirds percent (66-2/3%) of the principal amount of the Bonds Outstanding the Trustee shall declare the principal of all the Bonds then Outstanding to be due and payable immediately. Such declaration may be annulled or rescinded as described in the Resolution.

Under the Resolution LIPA covenants that upon an Event of Default, the books of record and account of LIPA shall at all times be subject to the inspection and use of the Trustee and of its agents and attorneys, and LIPA will, upon demand of the Trustee, account for all Revenues and other moneys, securities and funds pledged or held under the Resolution for such period as shall be stated in such demand. Upon a default, the Trustee may proceed to protect and enforce its rights and the rights of the Holders of the Bonds under the Resolution by a suit in equity or at law, whether for the specific performance of any covenant contained in the Resolution, in aid of the execution of any power granted therein, or for an accounting against LIPA as if LIPA were the trustee of an express trust, or in the enforcement of any other legal or equitable right as the Trustee. No Holder of any Bond shall have any right to institute any suit, action or proceeding at law or in equity for the enforcement of any provision of the Resolution or the execution of any trust under the Resolution or for any remedy under the Resolution, unless the Trustee has been requested by not less than sixty-six and two-thirds percent (66⅔%) in principal amount of the Bonds then Outstanding, and such Holders shall have offered the

Trustee adequate security and indemnity against the costs, expenses and liabilities to be incurred therein or thereby, and the Trustee has failed to commence such suit in the manner provided in the Resolution.

Defeasance

Bonds or any portion thereof for the payment or redemption of which moneys shall have been set aside and shall be held in trust by the Trustee (through deposit by LIPA of funds for such payment or redemption or otherwise) at the maturity or redemption date thereof shall be deemed to have been paid within the meaning of the Resolution and shall cease to be entitled to any lien, benefit or security under the Resolution either (A) as provided in the Supplemental Resolution authorizing their issuance or (B) if the following conditions are met: (i) in case any Bonds to be redeemed on any date prior to their maturity, LIPA shall have given to the Trustee instructions accepted in writing by the Trustee to mail as provided in the Resolution notice of redemption of such Bonds (other than Bonds which have been purchased by the Trustee at the direction of LIPA as provided prior to the mailing of such notice of redemption) on said date, (ii) there shall have been deposited with the Trustee either moneys in an amount which shall be sufficient, or Defeasance Obligations the principal installments of and/or the interest on which when due, without reinvestment, will provide moneys which, together with the moneys, if any, deposited with the Trustee at the same time, shall be sufficient, to pay when due the Principal Installments or Redemption Price, if applicable, and interest due and to become due on said Bonds or portion thereof on or prior to the redemption date or maturity date thereof, as the case may be, and (iii) in the event said Bonds are not to be redeemed within the next succeeding 60 days, LIPA shall have given the Trustee in form satisfactory to it irrevocable instructions to mail, as soon as practicable, a notice to the Holders of such Bonds that the deposit required by clause (ii) above has been made with the Trustee and that said Bonds or portion thereof (as the same thereafter may change) are deemed to have been paid in accordance with the Resolution and stating such maturity or redemption date (as the same thereafter may change) upon which moneys are to be available for the payment of the Principal Installments or Redemption Price, if applicable, on said Bonds or portion thereof (other than Bonds which have been purchased by the Trustee at the direction of LIPA as provided prior to the publication of the notice of redemption referred to above). The Trustee shall, as and to the extent necessary, apply moneys held by it pursuant to the Resolution to the retirement of said Bonds (or portions thereof) in amounts equal to the unsatisfied balances of any Sinking Fund Installments with respect to such Bonds (or portions thereof), all in the manner provided in the Resolution.

Unclaimed Moneys

Any moneys held by a Fiduciary in trust for the payment and discharge of the principal of or interest on any Bonds which remain unclaimed for two years after the date when such principal or interest, respectively, has become due and payable, either at their stated maturity dates or by call for earlier redemption, if such moneys were held by the Fiduciary at such date, or for two years after the date of deposit of such moneys if deposited with the Fiduciary after the said date when such principal or interest, as the case may be, becomes due and payable, shall, at the written request of LIPA, be repaid by the Fiduciary to LIPA, as its absolute property and free from trust, and the Fiduciary shall thereupon be released and discharged with respect thereto and the Bondholders shall look only to LIPA for the payment of such principal or interest, as the case may be. Notwithstanding the foregoing, any moneys held by a Fiduciary in trust for the payment and discharge of the principal of or interest on any Bonds which remain unclaimed after such moneys were to be applied to the payment of such principal or interest, as the case may be, in accordance with the Resolution may be applied in accordance with the provisions of the Abandoned Property Law of the State, being Chapter 1 of the Consolidated Laws of

the State, or any successor provision thereto, and upon such application, the Fiduciary shall thereupon be released and discharged with respect thereto and the Holders of Bonds shall look only to LIPA or the Comptroller of the State for the payment of such principal or interest, as the case may be. Before being required to make any such payment to LIPA or to apply such moneys in accordance with the Abandoned Property Law (or its successor) of the State, the Fiduciary shall, at the expense of LIPA, cause to be mailed to the Bondholders entitled to receive such moneys a notice that said moneys remain unclaimed and that, after a date named in said notice, which date shall be not less than 30 days after the date of the mailing, the balance of such moneys then unclaimed will be returned to LIPA or applied in accordance with the Abandoned Property Law (or its successor) of the State, as the case may be.

SUMMARY OF CERTAIN PROVISIONS OF THE FINANCING AGREEMENT

Agreement to Finance Acquisition of System and Cost of System Improvements

LIPA agrees to finance (i) the acquisition of all outstanding LILCO common stock in accordance with the LIPA/LILCO Merger Agreement, (ii) the payment of a portion of the redemption price of certain preferred stock of LILCO in accordance with the LIPA/LILCO Merger Agreement, (iii) the Property Tax Settlement, (iv) the retirement of certain outstanding debt of LILCO, (v) the purchase from BL Holding Corp. of certain interest rate hedges entered into in anticipation of the issuance of the Acquisition Debt, and (vi) the financing of capital expenditures relating to the System and other purposes of the initial Series of Bonds, and, thereafter, to use its best efforts to finance all or a part of the Cost of System Improvements, by the issuance of Authority Obligations from time to time in accordance with the Resolution, in each case unless and to the extent funded from other sources. LIPA and the LIPA Sub agree that the issuance of Authority Obligations, including the issuance of Authority Obligations for the purpose of refunding Authority Obligations or Outstanding LIPA Sub Unsecured Debt in accordance with the Financing Agreement and the Resolution, shall be deemed to constitute a loan to LIPA Sub. The obligation of LIPA Sub to repay such loan and to make payments in accordance with the Financing Agreement shall be evidenced by the delivery of the LIPA Sub Note.

Obligation to Make Payments to LIPA; Grant of Revenues and Certain Other Security to LIPA

On or before one business day prior to each due date for the payment of the principal of and redemption price, if any, or interest on, or other payments required under, Authority Obligations, until the same shall have been paid in full or provision for the payment thereof in full shall have been made in accordance with the Resolution or the provisions thereof, LIPA Sub shall make or cause to be made payments on LIPA Sub Note to LIPA in an amount which, when added to any moneys then on deposit under the Resolution and available therefor, including any dividends theretofore paid to LIPA and held thereunder, shall be equal to the amount payable on such due date with respect to the Authority Obligations, as provided in the Resolution, including amounts due for the payment of the principal of and sinking fund installments and premium, if any, and interest on the Bonds. The principal amount from time to time due and owing under the LIPA Sub Note and the scheduled amortization thereof and related interest rates (or the method of determining the same) shall be evidenced by the periodic delivery to LIPA Sub of a certificate of an Authorized Representative of LIPA setting forth the same.

Outstanding LIPA Sub Unsecured Debt shall be paid pursuant to and in accordance with the Resolution and the respective resolutions, indentures or similar instruments authorizing and providing for the issuance thereof.

LIPA Sub has granted and transferred to the LIPA all of its right, title and interest in and to the Revenues and the Promissory Notes, including all of its rights to collect and receive the same, subject only to the provisions of the Financing Agreement and the Resolution permitting the application thereof for or to the purposes and on the terms and conditions set forth in the Financing Agreement and the Resolution.

LIPA Sub has further pledged and assigned to LIPA, and granted to LIPA a security interest in, the System Agreements, subject however to the right and obligation of LIPA Sub to exercise its rights and to carry out its obligations and duties thereunder, and further subject to the terms of the Financing Agreement and the Resolution, the right and obligation to enforce or realize upon its rights and interests in the System Agreements.

Powers as to Grant, Conveyance and Transfer and as to Revenues of the System

LIPA Sub warrants and agrees that the Revenues, the System Agreements and other moneys, securities and funds and the rights under contracts so granted, conveyed, pledged and transferred are and will be free and clear of any pledge, lien, charge or encumbrance thereon or with respect thereto prior to, of equal rank with, the pledge created or authorized by the Resolution, and all corporate action on the part of LIPA Sub to that end has been duly and validly taken. LIPA Sub shall at all times, to the extent permitted by law, defend, preserve and protect the pledge of the Revenues, the System Agreements and other moneys, securities and funds and the rights under the contracts pledged under the Financing Agreement and the Resolution and all the rights of LIPA and the Bondholders under the Financing Agreement and the Resolution against all claims and demands of all persons whomsoever.

Subject to the provisions of the Financing Agreement, upon consummation of the merger of LIPA Sub with and into LILCO, LIPA Sub will be, and agrees that so long as any Authority Obligations remain outstanding it will at all times continue to be, the owner of the System.

LIPA Sub shall, so long as any Authority Obligations remain outstanding, perform all acts and duties required to be performed by it with respect to the System Agreements, and shall not permit any rescission or termination or amendment thereof, or otherwise take any action under or in connection with either, not expressly provided for by the terms thereof, which will in any manner impair or adversely affect the rights of LIPA Sub thereunder, or the rights or security of the holders of or parties to Authority Obligations under the provisions thereof or of the Resolution, and any action by LIPA Sub in violation of this covenant shall be null and void as to LIPA Sub.

Powers as to System and Collection of Revenues

The Financing Agreement provides that so long as any Authority Obligations remain outstanding, LIPA Sub will have or will use its best efforts to obtain good right and lawful authority to maintain, operate and improve the System; to impose and collect such fees, rates, rents and charges for the use or services of the System as are established from time to time by LIPA in accordance with the Resolution and the LIPA Act; and to demand and collect all Revenues becoming due to it for the use or services of the System.

State not Liable with Respect to LIPA Sub Note

The LIPA Sub Note and other obligations of LIPA Sub under the Financing Agreement shall not be a debt of the State or of any municipality, and neither the State nor any municipality shall be liable thereon. Neither the credit, the revenues nor the taxing power of the State or of any municipality shall be, or shall be deemed to be, pledged to the payment of the LIPA Sub Note or other obligations of LIPA Sub.

Payment From Construction Fund

The Costs incurred by LIPA Sub with respect to System Improvements shall be evidenced to LIPA by a certificate signed by an Authorized Representative of LIPA Sub. Each such certificate shall contain the information required to be set forth in a Disbursement Request. Upon receipt of such certificate LIPA shall pay or cause to be paid to the person entitled thereto amounts sufficient to pay all such certified Costs. Neither LIPA nor the Trustee shall be required to provide funds to pay the Costs of System Improvements from any source other than the Construction Fund and no such funds shall be required to be paid to LIPA Sub by LIPA or the Trustee in excess of the amounts set aside therefor in the Construction Fund.

Revenue Fund

The Financing Agreement provides that all Revenues, as promptly as practicable after receipt thereof by or on behalf of LIPA Sub, shall be deposited by LIPA Sub or by any System Manager into the Revenue Fund. LIPA Sub shall take such actions as it shall determine necessary and appropriate to assure that the System Manager complies with the applicable provisions of the Management Services Agreement and that the Energy Manager complies with the applicable provisions of the Energy Management Agreement relating to the application of moneys of the LIPA Sub.

Subsidiary General Fund

There shall be deposited in the Subsidiary General Fund all amounts received by LIPA Sub from LIPA or the Trustee pursuant to the Resolution for the purpose of paying LIPA Sub Expenses and any necessary and proper renewals, replacements and extensions of the System or, as provided in the Financing Agreement, PILOTs. All amounts in the Subsidiary General Fund shall be held in trust by LIPA Sub and applied only as provided in the Financing Agreement, in the LIPA Act or in the Resolution. Amounts on deposit in LIPA Sub General Fund shall be applied by LIPA Sub solely for the payment of LIPA Sub Expenses or any such renewals, replacements, extensions, or PILOTs.

Application of Revenues After Event of Default

LIPA Sub covenants that if an "Event of Default", as defined in the Resolution, shall occur, LIPA Sub, upon demand of the Trustee, shall pay over or cause to be paid over to the Trustee all moneys and securities then held by LIPA Sub or by any System Manager in the Subsidiary General Fund, and thereafter, as promptly as practical, the Revenues, for application in accordance with Section 1003 of the Resolution.

Rate Covenant

LIPA Sub and LIPA have covenanted and agreed that fees, rates, rents, charges and surcharges for the use of, or services furnished, rendered or made available by, the System shall be established by LIPA in accordance with the Resolution and the LIPA Act such that such fees, rates, rents, charges and surcharges shall be adequate, together with any other available funds, to provide for, among other things, (i) the timely payment of the Principal Installments of and interest on all Bonds, the principal of and interest on any other Authority Obligations payable from Revenues, and the principal of and interest on the Outstanding LIPA Sub Unsecured Debt, (ii) the proper operation and maintenance of the System, (iii) all other payments required for the System not otherwise provided for and (iv) all other payments required pursuant to the Financing Agreement and any System Agreements.

If the periodic review of System fees, rates, rents, charges and surcharges conducted by LIPA in accordance with the Resolution, or the report prepared pursuant to the Resolution, indicates that such rates, fees, rents, charges and surcharges are, or will be, insufficient to meet the requirements of Section 701 of the Resolution, LIPA Sub, in accordance with the directions, if any, of LIPA, shall promptly take and diligently pursue all necessary actions within its reasonable control to cure or avoid any such deficiency.

Except to the extent required by law, LIPA Sub will not furnish or supply or cause to be furnished or supplied any product, use or service of the System free of charge (or at a nominal charge) to any person, firm or corporation, public or private unless and to the extent LIPA shall have determined that other adequate consideration has been or is expected to be received by LIPA Sub in connection therewith, and LIPA Sub will use reasonable efforts to enforce or cause to be enforced the payment of any and all amounts owing to LIPA Sub for use of the System in accordance with the Financing Agreement.

Nothing contained in the Financing Agreement shall be deemed to limit or restrict the right or obligation of LIPA or LIPA Sub to comply with any covenant relating to rates to be charged for the use of, or services provided by, the System which may be made with the holders of or parties to Authority Obligations in accordance with the LIPA Act.

Compliance with Report as to System Condition

LIPA Sub covenants that if any report prepared in accordance with the Resolution shall set forth that the properties of the System have not been maintained in good repair and sound operating condition, it will restore the properties or cause the properties to be restored to good repair and sound operating condition as promptly as practicable.

Operation and Maintenance

LIPA Sub has covenanted that it shall, at all times:

(a) In accordance with the advice and recommendations set forth in the reports prepared from time to time in accordance with the Resolution, operate the System properly and in a sound and economical manner and shall maintain, preserve, and keep the same preserved and kept with the appurtenances and every part and parcel thereof, in good repair, working order and condition, and shall from time to time make, or cause to be made, all necessary and proper repairs, replacements, renewals and extensions so that at all times the operation of the System may be properly and advantageously conducted; provided, however, that nothing contained in the Financing Agreement shall require LIPA Sub to operate, maintain, preserve, repair, replace, renew or reconstruct any part of the System if, in the case of any part of the System having a market value of greater than $1 million, there shall be filed with LIPA Sub, LIPA and the Trustee a certificate of an Authorized Representative of LIPA Sub stating that in the opinion of LIPA Sub, abandonment of operation of such part of the System will not adversely affect the operation of the System or impair the ability of LIPA Sub and LIPA to comply with the provisions of the Financing Agreement and the rate covenant set forth in the Resolution;

(b) enforce the rules and regulations governing the operations, use and services of the System established from time to time by LIPA Sub or LIPA; and

(c) observe and perform all of the terms and conditions contained in the LIPA Act, and comply with all valid acts, rules, regulations, orders and directions of any legislative, executive, administrative or judicial body having competent jurisdiction of LIPA Sub or the System; provided, however, that the failure of LIPA Sub to comply with the covenant contained in this paragraph (c) for any period shall not constitute a default on its part so long as LIPA Sub (i) is taking reasonable and timely steps to permit compliance and (ii) LIPA Sub shall have delivered to the Trustee and to LIPA a Certificate of an Authorized Representative of LIPA Sub which (1) sets forth in reasonable detail the facts and circumstances attendant to such non-compliance, (2) sets forth the steps being taken by LIPA Sub to permit compliance, (3) sets forth the estimated date on which LIPA Sub will be in compliance and (4) states that in the opinion of such Authorized Representative such non-compliance during the period described will not adversely affect the operation of the System or the amount of Revenues to be derived therefrom.

Annual LIPA Sub Budget

Not less than thirty (30) days prior to the beginning of each Fiscal Year commencing with Fiscal Year 1998-1999, LIPA Sub shall file with LIPA and the Trustee an Annual LIPA Sub Budget for the ensuing Fiscal Year which shall set forth in reasonable detail the estimated Revenues, Subsidiary

Expenses and renewals, replacements and extensions for the System for such year. At the end of each quarter, LIPA Sub shall review its estimates for such Fiscal Year, and in the event such estimates do not substantially correspond with actual Revenues or Subsidiary Expenses, or if there are at any time during any such Fiscal Year extraordinary receipts or payments of unusual costs, LIPA Sub shall prepare an amended Annual LIPA Sub Budget for the remainder of the then current Fiscal Year. LIPA Sub also may at any time adopt an amended Annual LIPA Sub Budget for the remainder of the then current Fiscal Year.

Compliance with Agreements; Tax Exemption

LIPA Sub has covenanted with LIPA that it will take all such actions or refrain from taking all such actions, as the case may be, so as to comply with the terms and provisions of the Financing Agreement and the Resolution. LIPA has covenanted with LIPA Sub that it will take all such actions or refrain from taking any such actions, as the case may be, so as to comply with the terms and provisions of the Resolution and the Financing Agreement.

LIPA Sub has covenanted with LIPA, so long as any Bonds or other Authority Obligations, issued with the intent that the interest thereon not be included in gross income for Federal income tax purposes, shall be outstanding, that it will not take any action, or fail to take any action, which, if taken or not taken, as the case may be, would adversely affect the tax-exempt status of the interest payable on any such Bonds or other Authority Obligations.

Compliance with Resolution

LIPA Sub shall take all such actions and refrain from taking all such actions, as the case may be, and otherwise shall operate the System as shall ensure their compliance, and the compliance of LIPA, with the terms and provisions of the Resolution, or any other agreement entered into by LIPA in connection with the financing or operation of the System and which shall, by its terms, directly or indirectly apply to LIPA Sub.

Enforcement of Rules and Regulations

LIPA Sub shall enforce or cause any System Manager of the System to enforce the rules and regulations providing for discontinuance of or disconnection from the provision of electric service, for non-payment of fees, rates, rents or other charges imposed by LIPA and LIPA Sub, provided that such discontinuance or disconnection shall not be carried out except in the manner and upon notice consistent with the LIPA Act.

Books, Records and Accounts

Each of LIPA and LIPA Sub shall keep or cause to be kept, proper books of record and account in which complete and correct entries shall be made of all transactions relating to their corporate purposes under the LIPA Act and the Financing Agreement.

Liens

Until all Authority Obligations have been paid in full or provision has been made therefor in accordance with the Resolution, LIPA Sub shall not create, and, except to the extent permitted by the Financing Agreement and to the extent it has the power to do so, shall not permit to be created, any lien upon or pledge of the System, any real or personal properties comprising any part of the System,

or the Trust Estate including but not limited to the Revenues, except the lien and pledge thereon created by the Financing Agreement, the Resolution, and the LIPA Act.

Compliance with Law

LIPA and LIPA Sub have covenanted and agreed each for itself that it will observe and perform all of the terms and conditions contained in the LIPA Act, and comply with all valid laws, acts, rules, regulations, orders and directions of any legislative, executive, administrative or judicial body having competent jurisdiction over its property or affairs.

Insurance

LIPA Sub shall maintain or cause the System Manager to maintain with responsible insurers all insurance required and reasonably obtainable in the amounts and of the types customarily maintained by electric utilities consistent with prudent utility practice, to indemnify for loss of or damage to the System, and against public and other liabilities relating to the operations of LIPA Sub and the System. LIPA Sub shall also maintain or cause to be maintained any additional or other insurance which is required by the System Agreements. LIPA Sub may insure itself against any risk at the recommendation of an insurance consultant chosen by or acceptable to an Authorized Representative of LIPA Sub; provided, however, that LIPA Sub shall provide adequate funding of such self-insurance if and to the extent recommended by such insurance consultant.

Covenant Regarding Additional System Agreements

Any additional System Agreement executed by LIPA Sub shall contain such terms and conditions as will enable LIPA Sub to retain such overall supervision and control of the business, design, operating, management, transportation, maintenance, planning and research and development functions of the System as may be required by law, the Financing Agreement or the Resolution.

Limitations on Operating Expenses and Costs of Major Renewals and Replacements

LIPA Sub shall not incur or allow any System Manager to incur Operating Expenses or costs of major renewals, replacements and extensions for the System in any year in excess of the reasonable and necessary amount of such Operating Expenses or costs, respectively, and, except as may be necessary to respond to emergency conditions and to assure the continuing operation of the System, shall not expend any amount from the Operating Expense Fund for Operating Expenses or from the Construction Fund for costs of major renewals, replacements and extensions for the System for such year in excess of the respective amounts provided therefor in the Annual LIPA Sub Budget as originally adopted or as amended.

Maintenance of Existence

LIPA Sub covenants and agrees that during the term of the Financing Agreement it will maintain its existence as a corporation, will continue to be a corporation either organized under the laws of or duly qualified to do business in the State, will not dissolve or otherwise dispose of all or substantially all of its assets and will not consolidate with or merge into one or more other entities or permit one or more other entities to consolidate with or merge into it. LIPA Sub may, however, consolidate with or merge into one or more other entities or permit one or more other entities to consolidate with or merge into it, or sell or otherwise transfer to one or more other entities all or substantially all of its assets as an entirety and thereafter liquidate or dissolve if (a) LIPA Sub is the surviving, resulting or

transferee entity, or (b) in the event LIPA Sub is not the surviving, resulting or transferee entity, such entity (i) is solvent, and either organized under the laws of or duly qualified to do business subject to service or process in the State, (ii) assumes in writing all of the obligations of LIPA Sub as set forth in the Financing Agreement and (iii) is either LIPA or is wholly owned by LIPA, and (c), in either event, the Trustee shall have been furnished (1) an Opinion of Bond Counsel to the effect that under then existing statutes and court decisions, such consolidation, merger, sale or transfer does not adversely affect the exclusion of interest on any obligations of LIPA then outstanding the interest on which is excluded from gross income for federal income tax purposes, and (2) written confirmation from each Rating Agency to the effect that such consolidation, merger, sale or transfer, in and of itself, will not result in a withdrawal, suspension or downward revision of the rating assigned by such Rating Agency to the Bonds.

Disposition of Property

LIPA Sub may, with the approval of LIPA, dispose of properties if such disposal, in the judgment of LIPA Sub, (i) is desirable in the conduct of its business, (ii) is not disadvantageous in any material respect to the Holders of Authority Obligations and (iii) does not materially impair the ability of LIPA and LIPA Sub to comply with the Financing Agreement and the rate covenant set forth in the Resolution.

Competitive Facilities

LIPA Sub has covenanted that it will not construct, acquire, or operate, any plants, structures, facilities or properties which will provide electric service in the Service Area (as defined in the LIPA Act) unless the same are a part of the System.

Payment of Lawful Charges

LIPA Sub shall pay or cause to be paid, to the extent not paid by LIPA, all taxes and assessments or other municipal or governmental charges, if any, and all PILOTs to the extent not paid by LIPA, lawfully levied or assessed upon or in respect of the System, or upon any part thereof or upon the Revenues, when the same shall become due, and shall duly observe and comply in all material respects with all valid requirements of any municipal or governmental authority relative to any part of the System, and shall not create or suffer to be created any lien or charge upon the System or any part thereof or upon the Revenues therefrom, except the pledge and lien created by the Financing Agreement and by the Resolution for the payment of the principal and redemption price of and interest on, and other payments under, Authority Obligations. Nothing in the Resolution or the Financing Agreement shall be construed to prevent LIPA Sub or LIPA from entering into agreements to make PILOTs.

No Additional G&R Bonds

LIPA Sub covenants that it will not further amend or supplement the G&R Indenture or the Debenture Indentures, or take any other action, to allow the issuance of any additional G&R Bonds or any additional LIPA Sub Debentures other than bonds issued in lieu of or substitution therefor in accordance with the G&R Indenture and the Debenture Indentures. LIPA Sub agrees to take such further actions as may be required to close the G&R Indenture and the Debenture Indentures against the authentication and delivery on initial issuance of additional G&R Bonds and LIPA Sub Debentures, respectively.

Tax Rulings

The Subsidiary shall not do or omit to do any act that would result in (i) the revocation of the rulings that were issued by the Internal Revenue Service to the Authority, dated March 4, 1998, and (ii) a resultant material federal income tax liability.

Agreement of the State

In accordance with the LIPA Act, LIPA, as agent for the State, pledges to and agrees with the holders of any obligations issued under the Act and the parties to any contracts with LIPA thereunder that the State will not limit or alter the rights thereby vested in LIPA until such obligations together with the interest thereon are fully met and discharged and/or such contracts are fully performed on the part of LIPA, provided that nothing in the Financing Agreement shall preclude such limitation or alteration if and when adequate provision shall be made by law for the protection of the holders of such obligations of LIPA, or those entering into such contracts with LIPA.

Events of Default

An "event of default" means any one or more of the following events: (a) failure by LIPA Sub to make the payments required to be made to LIPA pursuant to the Financing Agreement; (b) failure by LIPA Sub to remit or cause to be remitted the Revenues, or any portion thereof, to the extent received by LIPA Sub, for deposit in the Revenue Fund; (c) failure of LIPA Sub to observe any covenant, term or condition of the Financing Agreement, provided that such failure shall have continued for a period of sixty (60) days after written notice, specifying such failure and requesting that it be remedied, is given to LIPA Sub by LIPA, unless LIPA shall agree in writing to an extension of such time prior to its expiration, and provided further that such extension shall not be unreasonable withheld if LIPA Sub has instituted and is diligently pursing corrective action within the applicable period; (d) if LIPA Sub files a petition seeking a composition of its indebtedness under the Federal bankruptcy laws, or under any other applicable law or statute of the United States of America or of the State; (2) consents to the appointment or taking possession by a receiver, liquidator, assignee, custodian, trustee, sequestrator or other similar official of LIPA Sub or any substantial portion of its property; (3) makes any assignment for the benefit of creditors; (4) admits in writing its inability to pay its debts generally as they become due; or (5) takes action in furtherance of any of the foregoing; (e) if (1) a decree or order for relief is entered by a court having jurisdiction of LIPA Sub adjudging LIPA Sub a bankrupt or insolvent or approving as properly filed a petition seeking reorganization, arrangement, adjustment or composition in respect of LIPA Sub in an involuntary case under the Federal bankruptcy laws, or under any other applicable law or statute of the United States of America or of the State; (2) a receiver, liquidator, assignee, custodian, trustee, sequestrator or other similar official of LIPA Sub or of any substantial portion of its property is appointed; or (3) the winding up or liquidation of its affairs is ordered and the continuance of any such decree or order unstayed and in effect for a period of sixty (60) consecutive days; or (f) the respective provisions of the LIPA Act pursuant to which the Resolution has been adopted or Authority Obligations have been issued or entered into, including, without limitation, those provisions pursuant to which the lien upon the Revenues has been created pursuant to the Financing Agreement and the Resolution and those provisions authorizing the establishment of LIPA Sub, shall be materially and adversely limited, altered or impaired by any legislative action or any formal judgment or the terms, conditions and security provided under the Financing Agreement, Authority Obligations and the Resolution shall be materially and adversely limited, altered or impaired by any legislative action or any final judgment.

Remedies

Whenever an event of default shall have occurred and be continuing, and written notice of the event of default, if required, shall have been given to LIPA Sub by LIPA or by the Trustee and the event of default shall not have been cured within the period provided therefor, LIPA and the Trustee may take whatever action at law or in equity to collect the payments then due and as they thereafter become due, and LIPA and the Trustee, so long as any Bonds are outstanding, may take whatever action at law or in equity to enforce performance and observance of any obligation, agreement or covenant of LIPA Sub under the Financing Agreement.

Termination

The Financing Agreement terminates and the covenants and other obligations contained in the Financing Agreement are discharged and satisfied, when (i) payment of all Authority Obligations has been made or provided for in accordance with the Resolution and (ii) either all payments required thereunder have been made in full, or provision for such payments satisfactory to LIPA and the Trustee has been made or LIPA pays or assumes all liabilities, obligations, duties, rights and powers of LIPA Sub thereunder.

Amendments to Agreement; Consents

The parties to the Financing Agreement may enter into any amendment, change or modification of the Financing Agreement (in writing, signed by each of the parties and consented to in writing if required by the Resolution); provided, the parties shall not enter into or consent to, any amendment, change or modification which materially adversely affects the rights of the Owners of the Bonds by modifying or revoking certain enumerated provisions of the Financing Agreement without first obtaining the consent of the holders of or parties to Authority Obligations in accordance with and to the extent provided by the provisions of the Resolution.

Indemnity by LIPA Sub

To the extent permitted by law, LIPA Sub releases and agrees to hold harmless and indemnify LIPA and its trustees, officers, officials, agents and employees from and against all, and agrees that LIPA and its trustees, officers, officials, agents and employees shall not be liable for any, (i) liabilities, suits, actions, claims, demands, damages, losses, expenses and costs of every kind and nature resulting from any action taken in accordance with, or permitted by the Financing Agreement, or the Resolution, or arising from or incurred by LIPA by reason of its incurrence of Authority Obligations pursuant to the Financing Agreement and the Resolution, or (ii) loss or damage to property or any injury to or death of any or all persons that may be occasioned by any cause whatsoever pertaining to the System arising by reason of or in connection with the presence on, in or about the premises of the System of any person; **provided, however,** that the indemnity shall be effective only to the extent of any loss or liability that may be sustained by LIPA or another party so indemnified by LIPA Sub in excess of net proceeds received from any insurance carried with respect to such loss or liability; and provided further that LIPA and LIPA Sub shall each provide waiver of rights of subrogation against the other in any insurance coverage obtained relating to the System.

Conflicts

The Financing Agreement provides that its provisions shall not change or in any manner alter the terms of the Resolution, or the security, rights or remedies of the Trustee or the holders or owners of Authority Obligations. In the event any provision of the Financing Agreement conflicts at any time, or in any manner, with the provisions of the Resolution or any Authority Obligations, the provisions of the Resolution or Authority Obligations shall be controlling and conflicting provisions of the Financing Agreement shall be disregarded.

APPENDIX E

SUMMARY OF OPERATING AGREEMENTS

Definitions Of Certain Terms

The following terms, as used in this Appendix E, have the respective meanings provided below. These summary definitions do not purport to be complete or definitive and are qualified in their entirety by reference to the Agreements, copies of which are on file with the Trustee. Capitalized terms which are used below but are not defined in this Appendix E shall have the definitions provided in Appendix C to this Official Statement.

"Affiliate" means any person, corporation or other entity directly or indirectly controlling or controlled by another person, corporation or other entity or under direct or indirect common control with such person, corporation or other entity.

"Ancillary Services" means the ancillary services required by NYPP/ISO from time to time to enable the NYPP/ISO to operate the transmission system in New York State in a secure and reliable manner.

"Annual T&D Budget" means such budget as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Summary of Certain Provisions of the Management Services Agreement—Annual T&D Budget and Five Year Planning Process").

"Applicable Law" means any law, rule, regulation, condition, requirement, guideline, ruling, ordinance or order of or any Legal Entitlement issued by, any Governmental Body and applicable from time to time to the performance of the obligations of the parties to an Agreement.

"Base Interest Rate" means the lesser of (1) the maximum rate of interest permitted by Applicable Law and (2) (a) for interest accruing during the first six months or less after the date on which a payment was payable under the Agreement, 6 month LIBOR, and (b) for interest accruing more than six months after the date on which such payment was payable under the Agreement, the Prime Rate plus 1.00%, in each case, as 6 month LIBOR or the Prime Rate as reported in the *Wall Street Journal* for each day.

"Billing Period" means each calendar month in each Contract Year, except that (1) the first Billing Period shall begin on the Closing Date and shall continue to the last day of the month in which the Closing Date occurs and (2) the last Billing Period shall end on the last day of the Term of the Agreement. Any computation made on the basis of a Billing Period shall be adjusted on a pro rata basis to take into account any Billing Period of less than the actual number of days in the month to which such Billing Period relates.

"BUG/LILCO Agreement" means the Amended and Restated Agreement and Plan of Exchange dated as of June 26, 1997, by and among the Guarantor, LILCO and Brooklyn Union.

"Business Day" means any day other than a Saturday, Sunday or Legal Holiday.

"Change of Control" means (i) the acquisition of beneficial ownership (within the meaning of Rule 13d-3 promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended (the "1934 Act")) of 35% or more of the outstanding shares of securities

the holders of which are generally entitled to vote for the election of directors of the Manager, the Energy Manager or the Guarantor, as the case may be (including securities convertible into, or exchangeable for, such securities or rights to acquire such securities or securities convertible into, or exchangeable for such securities, ''Voting Stock''), on a fully diluted basis, by any Person or group of Persons (within the meaning of Section 13 or 14 of the 1934 Act); (ii) any sale, transfer or other disposition of beneficial ownership of 35% or more of the outstanding shares of the Voting Stock, on a fully diluted basis, of the Manager, the Energy Manager or the Guarantor, as the case may be; (iii) any merger, consolidation, combination or similar transaction of the Manager, the Energy Manager or the Guarantor, as the case may be, with or into any other Person, whether or not the Manager, the Energy Manager or the Guarantor, as the case may be, is the surviving entity in any such transaction; (iv) any sale, lease, assignment, transfer or other disposition of the beneficial ownership in 35% or more of the property, business or assets of the Manager, the Energy Manager or the Guarantor, as the case may be; (v) a Person other than the current shareholders of the Manager, the Energy Manager or the Guarantor, as the case may be, obtains, directly or indirectly, the power to direct or cause the direction of the management or policies of the Manager, the Energy Manager or the Guarantor, as the case may be, whether through the ownership of capital stock, by contract or otherwise; (vi) during any period of 12 consecutive calendar months, when individuals who were directors of the Manager, the Energy Manager or the Guarantor, as the case may be, on the first day of such period cease to constitute a majority of the board of directors of the Manager, the Energy Manager or the Guarantor, as the case may be; or (vii) any liquidation, dissolution or winding up of the Energy Manager or the Guarantor, as the case may be.

''Closing Date'' means the date on which the merger of LIPA Sub and LILCO is completed.

''Common Facilities'' has the meaning attributed to that term in the FERC Uniform System of Accounts.

''Construction Work'' means the services to be provided and materials to be supplied by the Manager, relating to the design, procurement, construction, start-up and testing of the Major Capital Improvements and Public Works Improvements.

''Consulting Engineer'' means a nationally recognized consulting engineer or firm of consulting engineers, having experience with respect to the design, construction, testing, operation and maintenance of electricity transmission and distribution systems, which is designated as the Consulting Engineer for the purposes of the subject Agreement from time to time in writing by LIPA Sub.

''Contract Date'' means June 26, 1997.

''Contract Standards'' means the terms, conditions, requirements, methods, techniques, standards and practices of (1) Applicable Law, (2) the System Policies and Procedures, (3) the substantive requirements and standards and guidelines established by the NYSPSC that apply as of the Closing Date to the operation and maintenance of the T&D System, except to the extent otherwise directed by LIPA Sub, (4) Prudent Utility Practice, (5) the Performance Guarantees, (6) the Operation and Maintenance Manual, (7) applicable equipment manufacturer's specifications and reasonable recommendations, (8) applicable Insurance Requirements, and (9) any other term, condition or requirement specifically provided in this Agreement to be observed by the Manager.

''Contract Year'', except as LIPA Sub shall otherwise propose subject to the approval of the Manager, or the Energy Manager, as the case may be, which approval shall not be unreasonably

withheld, means the calendar year commencing on January 1 in any year and ending on December 31 of that year; *provided*, however, that the first Contract Year shall commence on the Closing Date and shall end on December 31 of that year, and the last Contract Year shall commence on January 1 prior to the date the Agreement expires or is terminated, whichever is appropriate, and shall end on the last day of the Term of the Agreement or the effective date of any termination, whichever is appropriate. Any computation made on the basis of a Contract Year shall be adjusted on a pro rata basis to take into account any Contract Year of less than 365/366 days.

"Cost Incentive Fee" means such fee as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budgets—Management Fee, Cost Incentive Fee and Non-cost Performance Incentives and Disincentives").

"Cost Substantiation" or **"Cost Substantiated"** means, with respect to any cost reasonably incurred or to be incurred by the Manager which is directly or indirectly chargeable in whole or in part to LIPA Sub as an Other Cost, a Major Capital Improvement Cost or a Public Works Improvement Cost under the MSA, the delivery to LIPA Sub of a certificate reasonably acceptable to LIPA Sub signed by an authorized engineering officer and an authorized financial officer of the Manager, certifying that it is true, complete and correct and setting forth the amount of such cost and the provisions of the MSA under which such cost is properly chargeable to LIPA Sub.

"Direct Cost Budget" means such budget as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Annual T&D Budget and Five Year Planning Budget Process—Annual T&D Budget Preparation").

"Direct Costs" means such costs as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Annual T&D Budget and Five Year Planning Budget Process—Annual T&D Budget Preparation").

"Dispatch" shall mean LIPA Sub's adjustment and control (which may be coordinated by NYPP/ISO) of the net electrical energy output of any component of the System Power Supply for the purpose of regulating the amount of Electricity delivered.

"Electricity" means the electrical energy (real and reactive) and capacity available from the System Power Supply.

"Electricity Customers" means the retail and wholesale customers of LIPA Sub located in the Service Area.

"Encumbrances" means any lien, lease, mortgage, security interest, charge, judgment, judicial award or encumbrance with respect to the T&D System (other than those associated with any retainage holdback on construction materials, supplies and equipment).

"Energy Manager" means a Transferee Subsidiary of BL Holding Corp and its successors or assigns expressly permitted pursuant to the EMA (as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—Miscellaneous Provisions—Assignment and Transfer").

"Energy Manager Fault" means any breach, failure of compliance, or nonperformance by the Energy Manager with its obligations under the Agreement or any negligence or willful misconduct by the Energy Manager under the EMA.

"Event of Default", as appropriate, means such events as defined in the EMA, the MSA or the PSA (and as summarized, with respect to the EMA, in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—Term: Events of Default," and as summarized, with respect to the MSA, in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Default, Termination for Cause and Dispute Resolution," and as summarized, with respect to the PSA, in this Appendix E, under the caption "Summary of Certain Provisions of the Power Supply Agreement—Term and Termination").

"Firm Gas Supply" means a type of natural gas supply delivered or transported to a City Gate which may not be interrupted except for "force majeure" events. Such gas may be interrupted on the gas distribution system serving LILCO's existing gas service area whenever its continued delivery would adversely affect the reliability of the gas distribution system serving LILCO's existing gas service area.

"Five-Year Planning Budget" means such budget as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Annual T&D Budget and Five Year Planning Budget Process—Annual T&D Budget Preparation").

"Fixed Direct Fee" means such fee as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Service Fee—Formula").

"Fuel" means the natural gas, oil, kerosene or other fossil fuel used for operating the GENCO Generating Facilities.

"Fuel Management Fee" means such fee as defined in the EMA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—Fuel Management—Fuel Management Fee").

"Fuel Purchase Performance Incentive/Disincentive" means the incentive payment to or disincentive payment from the Energy Manager calculated in accordance with an appendix to the EMA.

"Fuel Services" means those services required to be furnished and done for and relating to the delivery of Fuel to the GENCO Generating Facilities by the Energy Manager pursuant to the EMA subsequent to the Closing Date. A reference to "Fuel Services" shall mean "any part and all of the Fuel Services" unless the context otherwise requires.

"GENCO Generating Facilities" means the electric generating facilities owned by GENCO and under contract at any time with LIPA Sub under the Power Supply Agreement.

"Governmental Body" means any federal, State or local legislative, executive, judicial or other governmental board, agency, authority, commission, administration, court or other body, or any official thereof having jurisdiction with respect to any matter which is a subject of the Agreement other than LIPA.

"Guarantor" means BL Holding Corp and its successors and assigns permitted under the Guaranty Agreement.

"Incremental Internal Costs" means such costs as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Annual T&D Budget and Five Year Planning Budget Process—Other Costs").

"Insurance Requirement" means any rule, regulation, code, or requirement issued by any fire insurance rating bureau or any body having similar functions or by any insurance company which has issued a policy of construction work insurance or operation period insurance under the Agreement, as in effect during the term thereof.

"Interruptible Gas Supplies" means gas supplies that will be interrupted whenever the supplier recalls supplies pursuant to a negotiated supply contract and/or the interstate pipeline interrupts the transportation of such gas supply pursuant to its FERC approved tariff. Such gas supplies may also be interrupted for force majeure events.

"ISO" means the party or governing board responsible for the operation of transmission facilities and the dispatch of power generation facilities contemplated to succeed the New York Power Pool as part of the restructuring of the electric utility industry within the State of New York.

"Lien" means any and every lien against the T&D System, the T&D System Site, the Construction Work, the Operation and Maintenance Services or against any monies due or to become due from the Subsidiary to the Manager under the Agreement, for or on account of the Construction Work or the Operation and Maintenance Services.

"Loss-and-Expense" means any and all losses, liabilities, obligations, damages, delays, fines, penalties, judgments, deposits, costs, claims, demands, charges, assessments, taxes, or expenses, including all Fees-And-Costs.

"Major Capital Improvement" means any repair, replacement, improvement, alteration or addition to the T&D System or any part thereof (other than any repair, replacement, improvement, alteration or addition constituting routine maintenance of the T&D System) contained in the Major Capital Plan and Budget and that has a useful life at least equal to three years.

"Major Capital Improvement Cost" means the cost of any Major Capital Improvement which the Manager reasonably incurs under the Agreement and proves by Cost Substantiation including, without limitation, expenditures for material, equipment, incremental labor, and services supplied by architects, engineers and Subcontractors, and expenses related to managing and administering the Major Capital Improvement. "Major Capital Improvement Cost" shall not include amounts for an allowance for overhead, profit, or contingency.

"Major Capital Plan and Budget" means such plan and budget as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Major Capital Improvements—Major Capital Plan and Budget").

"Management Fee" means such fee as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budgets—Annual T&D Budget and Five Year Planning Budget Process—Direct Cost Budget").

"Manager Fault" means any breach, failure of compliance, or nonperformance by the Manager with its obligations under the MSA or any negligence or willful misconduct by the Manager under the MSA.

"Manager Indemnified Parties" means such parties as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary Certain Provisions of the Management Services Agreement—Indemnification").

"Monthly Fuel Payment" means such payment as defined in the EMA (and as summarized in this Appendix E, under the caption "Summary Certain Provisions of the Energy Management Agreement—Fuel Management—Monthly Fuel Payment").

"Monthly System Power Supply Management Fee" means such fee as defined in the EMA (and as summarized in Appendix E, under the caption "Summary Certain Provisions of the Energy Management Agreement—System Power Supply Management—System Power Supply Management Fee").

"New York Power Pool" or **"NYPP"** means the member system currently comprising of Consolidated Edison Company of New York, Inc., Central Hudson Gas and Electric Company, Long Island Lighting Company, Orange and Rockland Utilities, Rochester Gas and Electric Company, New York State Electric and Gas Corporation, Niagara Mohawk Power Corporation, and the Power Authority of the State of New York, as such organization or membership may change from time to time.

"Nine Mile Point 2" or **"NMP2"** means Unit No. 2 of the Nine Mile Point Nuclear Power Generating Station located in Scriba, New York and operated pursuant to a joint operating agreement by Niagara Mohawk Power Corporation.

"NYPP/ISO" means the Independent System Operator ("ISO") into which the NYPP is proposed to be restructured to the extent approved by FERC. In the event this restructuring occurs, the principal reliability, security and dispatch functions of the NYPP will be performed by the ISO.

"NYSPSC" or **"PSC"** means the Public Service Commission of the State of New York.

"Off-System Sales" means the sale of electric capacity and/or energy to wholesale or retail customers located outside the Service Area.

"Operating Assets" means the T&D System and all of the assets of the Manager used in the operation and maintenance of the T&D System and the performance of the Manager's obligations under the MSA.

"Operation Period" means the period commencing on the Closing Date and ending on the date the MSA expires in accordance with its terms, or if earlier, on the MSA's Termination Date.

"Operation and Maintenance Services" means the services to be provided and materials to be supplied by the Manager pursuant to the MSA during the Operation Period, except Construction Work. Operation and Maintenance Services shall include, without limitation, the employment and furnishing of all labor, materials, equipment, supplies, tools, storage, transfer, transportation, insurance, delivery and other items and services necessary in order for Manager to perform its routine operation and maintenance obligations under the MSA, as well as all related administrative, accounting, record-keeping, notification and similar services relating to such obligations.

"Other Costs" means such costs as defined in MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budgets—Annual T&D Budget and Five Year Planning Budget Process—Other Costs").

"Parent" means BL Holding Corp, and its successors and assigns.

"Performance Guarantees" means the minimum reliability standard, the minimum worker safety standard and the minimum customer service standard, all as established pursuant to appendices to the MSA.

"Power and Energy" means the electrical energy and capacity available from the System Power Supply.

"Prime Rate" means the rate announced by Citibank, N.A. from time to time at its principal office as its prime lending rate for domestic commercial loans, the Prime Rate to change when and as such prime lending rate changes.

"Prudent Utility Practice" at a particular time means any of the practices, methods, and acts (including but not limited to the practices, methods and acts engaged in or approved by a significant portion of the electrical utility industry prior thereto), which, in the exercise of reasonable judgment in light of the facts and the characteristics of the T&D System, the Service Area, System Power Supply (and, insofar as the delivery of Fuel Service may require, the gas distribution and transmission system serving gas service area formerly served by Long Island Lighting Company and prevailing regulations or regulatory policies applicable to such gas distribution and transmission system), known at the time the decision was made, would have been expected to accomplish the desired result at the lowest reasonable cost consistent with reliability, safety and expedition and good customer relations. Prudent Utility Practice is not intended to be limited to the optimum practice, method or act, to the exclusion of all others, but rather to be a spectrum of possible practices, methods or acts.

"Public Works Improvements" means Major Capital Improvements performed as a result of requirements or requests of a Governmental Body.

"Public Works Improvement Costs" means the cost of any Public Works Improvement which the Manager reasonably incurs under the Agreement and proves by Cost Substantiation including, without limitation, expenditures for material, equipments, incremental labor and services supplied by architects, engineers and Subcontractors, and expenses related to managing and administering the Public Works Improvements. "Public Works Improvement Costs" shall not include amounts for an allowance for overhead, profit or contingency.

"Revenue Bonds" means any bonds, notes or other obligations issued or secured under the Bond Resolution.

"Service Area" means the counties of Suffolk and Nassau and that portion of the County of Queens constituting LILCO's electric franchise area as of the effective date of the LIPA Act. "Service Area" does not include the Villages of Freeport, Rockville Centre and Greenport.

"Service Fee" means such fee as defined in the MSA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budgets—Service Fee").

"Subcontract" means an agreement between the Manager or the Energy Manager and a Subcontractor, or between two Subcontractors, as applicable.

"Subcontractor" means every person (other than employees of the Manager or the Energy Manager) employed or engaged by the Manager or the Energy Manager or any person directly or indirectly in privity with the Manager or the Energy Manager (including every sub-subcontractor of whatever tier) for any portion of the services or the materials, supplies, or equipment to be provided by the Manager or the Energy Manager under the MSA or the EMA.

"Subsidiary Fault" means any breach, failure of compliance, or nonperformance by the Subsidiary with its obligations under an Agreement or any negligence or willful misconduct by the Subsidiary under an Agreement (whether or not attributable to any officer, trustee, member, agent, employee, representative, contractor, subcontractor of any tier, or independent contractor of the Subsidiary other than the Manager or Energy Manager and its Subcontractors) that materially and adversely affects the Manager's or Energy Manager's performance or the Manager's or Energy Manager's rights or obligations under the Agreement.

"Subsidiary Indemnified Parties", as appropriate, means such parties as defined in the EMA and the MSA (and as summarized, with respect to the EMA, in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—Indemnification," and as summarized, with respect to the MSA, in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Indemnification").

"System Policies and Procedures" means the policies and procedures adopted from time to time by the Subsidiary with respect to the T&D System and the System Power Supply in accordance with Applicable Law and Prudent Utility Practice.

"System Power Supply" means the electrical capacity and energy from all power supply sources owned by or under contract to LIPA Sub, including, but not limited to, the Existing Power Supply Agreements, the Power Supply Agreement, LIPA Sub's rights and interests with respect to the Nine Mile Point 2 power plant, LIPA Sub's interest in any future generating facilities, spot market capacity and energy purchases made by the Energy Manager on behalf of LIPA Sub, and any load control programs or energy efficiency measure adopted by LIPA Sub.

"System Power Supply Management Fee" means such fee as defined in the EMA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—System Power Supply Management—System Power Supply Management Compensation—System Power Supply Management Fee").

"System Power Supply Performance Incentive/Disincentive" means such fee as defined in the EMA (and as summarized in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—System Power Supply Management—System Power Supply Management Compensation—System Power Supply Performance Incentive/Disincentive").

"System Power Supply Services" means those services required to be furnished and done for and relating to the administration and management of System Power Supply pursuant to this Agreement subsequent to the Closing Date. A reference to "System Power Supply Services" shall mean "any part and all of the System Power Supply Services" unless the context otherwise requires.

"T&D System" means the electric transmission and distribution system located in the Service Area which provides the means for transmitting and distributing Electricity.

"T&D System Site" means the real property and interests therein upon which the components of the T&D System are and will be located, including, without limitation, those described in an appendix to the MSA.

"Term", as appropriate, means such term as defined in the EMA, the MSA or the PSA (and as summarized, with respect to the EMA, in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—Term; Events of Default—Term," and as summarized, with respect to the MSA, in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Term—Term of the Agreement," and as summarized, with respect to the PSA, in this Appendix E, under the caption "Summary of Certain Provisions of the Power Supply Agreement—Term and Termination—Term").

"Termination Date", as appropriate, means such date as defined in the EMA, the MSA or the PSA (and as summarized, with respect to the EMA, in this Appendix E, under the caption "Summary of Certain Provisions of the Energy Management Agreement—Term; Events of Default—Procedure for Termination by Cause," and as summarized, with respect to the MSA, in this Appendix E, under the caption "Summary of Certain Provisions of the Management Services Agreement—Default, Termination for Cause and Dispute Resolution—Termination for Cause," and as summarized, with respect to the PSA, in this Appendix E, under the caption "Summary of Certain Provisions of the Power Supply Agreement—Term and Termination—Procedure for Termination for Cause").

"Third Party Cost Budget" has the meaning set forth in the MSA (see "Summary of Certain Provisions of the Management Services Agreement—Annual T&D Budget and Five Year Planning Budget Process—Annual T&D Budget Preparation").

"Third Party Costs" has the meaning set forth in the MSA (see "Summary of Certain Provisions of the Management Services Agreement—Annual T&D Budget and Five Year Planning Budget Process—Annual T&D Budget Preparation").

"Total Cost" means the sum of the actual Direct Costs and the actual Third Party Costs.

"Transferee Subsidiary" means a subsidiary of BL Holding Corp acting as Manager, Energy Manager and GENCO.

"Trustee" means the trustee acting under the Bond Resolution for the benefit of the holders of LIPA's bonds.

"Uncontrollable Circumstance" means any act, event or condition, whether affecting the T&D System, the System Power Supply, LIPA Sub, the Manager, or any of LIPA Sub's subcontractors or the Manager's Subcontractors to the extent that it materially and adversely affects the ability of either party to perform any obligation under the Agreement (except for payment obligations), if such act, event or condition is beyond the reasonable control and is not also the result of the misconduct or negligent action or omission or failure to exercise reasonable diligence on the part of the party relying thereon as justification for not performing an obligation or complying with any condition required of such party under the Agreement; *provided*, however, that the contesting in good faith or the failure in good faith to contest such action or inaction shall not be construed as willful or negligent action or a lack of reasonable diligence of either party. None of the following acts or conditions shall constitute Uncontrollable Circumstances:

(a) general economic conditions, interest or inflation rates, or currency fluctuations or exchange rates,

(b) the financial condition of LIPA Sub, the Manager, the Guarantor, any of their Affiliates or any Subcontractor,

(c) the consequences of error, neglect or omissions by the Manager, the Guarantor, any Subcontractor, any of their Affiliates or any other person in the performance of any work under the Agreement;

(d) any increase for any reason in premiums charged by the Manager's insurers or the insurance markets generally for the construction work insurance or operating period insurance, each as required by the Agreement;

(e) the failure of the Manager to secure patents or licenses in connection with the technology necessary to perform its obligations under the Agreement;

(f) equipment malfunction or failure;

(g) union work rules, requirements or demands which have the effect of increasing the number of employees employed at the T&D System, reducing the operating flexibility of the Manager or otherwise increase the cost to the Manager of operating and maintaining the T&D System,

(h) any impact of prevailing wage laws on the Manager's operation and maintenance costs with respect to wages and benefits,

(i) the failure of any Subcontractor or supplier to furnish labor, materials, services or equipment for any reason;

(j) strikes, work stoppages or other labor disputes or disturbances, or

(k) any act, event or circumstance occurring outside of the United States.

"Variable Payment" has the meaning set forth in the MSA (see "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budgets—Service Fee—Variable Payment").

SUMMARY OF CERTAIN PROVISIONS OF THE MANAGEMENT SERVICES AGREEMENT

The following is a brief summary of certain provisions of the Management Services Agreement. The summary does not purport to be complete or definitive and is qualified in its entirety by reference to the Management Services Agreement, a copy of which is on file with the Trustee.

General

The Management Services Agreement was executed initially by LILCO and LIPA. In accordance with the provisions of the LIPA/LILCO Merger Agreement, and as permitted by the assignment provisions of the Management Services Agreement (see "Miscellaneous Provisions—Assignment and Transfer" below), effective upon the Closing Date the rights and obligations of LILCO and LIPA under the Management Services Agreement will be assigned to BL Holding Corp and its subsidiaries (the "Manager") and to LIPA Sub, respectively. For purposes of this summary, such assignees are treated as the parties to the Management Services Agreement.

The Management Services Agreement establishes the terms and conditions under which LIPA Sub will contract with the Manager for the purpose of providing the Operation and Maintenance Services and the Construction Work relating to the T&D System in a manner consistent with policies established by LIPA Sub in order to assure the continued delivery of electric energy to the customers of the T&D System.

Ownership of the T&D System

The Agreement provides that the Manager will not have any ownership or leasehold interest in the T&D System. LIPA Sub will engage the Manager as an independent contractor to furnish the services described in the Agreement.

The Agreement provides that the Manager will not, without LIPA Sub's prior written consent, create or permit to be created or to remain, and will promptly discharge at its expense, any Encumbrance on the T&D System, other than (1) Encumbrances existing as of the date of the Agreement, or (2) any Lien affecting the T&D System (i) resulting solely from any action or failure to act by LIPA Sub or anyone claiming by, through or under LIPA Sub; or (ii) created by Subcontractors that are promptly discharged or bonded against by the Manager. The Agreement provides that nothing in the Agreement will be deemed to create any Lien or Encumbrance in favor of the Manager on any asset of LIPA Sub as security for the obligations of LIPA Sub under the Agreement.

Operation of the T&D System

General. The Agreement provides that the Manager will not transmit or distribute Power and Energy other than Power and Energy obtained by, on behalf of, or with the approval of LIPA Sub, and will not use the T&D System for any purpose other than the purposes contemplated by the Agreement or to serve or benefit any person other than LIPA Sub and its customers in the Service Area.

Operation and Maintenance. The Agreement provides that, commencing on the Closing Date, the Manager will provide Operation and Maintenance Services and Construction Work for the T&D System on behalf of LIPA Sub in accordance with the Contract Standards. The Manager will be responsible for the safe and reliable operation and maintenance of the T&D System, management and/or

performance of construction of improvements thereto and delivery of Power and Energy to LIPA Sub's customers and will be responsible for the following tasks and services, among others: (a) day-to-day operation and maintenance of the T&D System; (b) construction activities performed by the Manager's work force; (c) supervision of routine and major capital improvements; (d) preparation of recommended and monitoring of approved annual capital and operating expenditure budgets, load and energy forecasts and long and short range system and strategic plans; (e) preparation of long and short range transmission and distribution planning analyses; (f) performance of accounting and tax and payment in lieu of tax reporting functions and preparation of monthly reports concerning the T&D System; (g) operation of the T&D System in compliance with applicable provisions of the bond resolutions, and with other requirements pertaining to qualification of the bonds for tax-exemption under the Code; (h) other actions necessary to safely and reliably operate the T&D System in accordance with Prudent Utility Practice; (i) administration and management, at the direction of LIPA Sub, of LIPA Sub's interest in Nine Mile Point 2; and (j) billing and collection, in accordance with LIPA Sub's direction, of all fees and charges in connection with the use or availability of the T&D System for wheeling services.

Maintenance and Repair of T&D System. The Agreement provides that the Manager will maintain the T&D System, the T&D System Site and the Common Facilities in good working order and repair and in a neat and orderly condition, and will conduct periodic, corrective, and preventive maintenance and repair of the T&D System consistent with the Contract Standards for the purpose of, among other things, mitigating and preventing abnormal wear, tear and usage.

The Agreement provides that all additions to the T&D System purchased in conjunction or for the use with any part of the T&D System during the Term shall be the property of LIPA Sub, except those which are leased or constitute part of the Common Facilities.

Performance Guarantees. The Agreement provides that, commencing on the Closing Date, the Manager will at all times comply with the Performance Guarantees, except to the extent excused by Uncontrollable Circumstances or Subsidiary Fault. If the Manager fails to comply with any Performance Guarantee, the Manager shall, without relief under any other Performance Guarantee under the Agreement, (1) promptly notify LIPA Sub of any such noncompliance, (2) promptly provide LIPA Sub with copies of any notices sent to or received from any Governmental Body having regulatory jurisdiction with respect to any violations of Applicable Law, (3) promptly make any applicable payments provided for in the Agreement, and (4) at its own cost and expense to the extent required under the Agreement, promptly take any action necessary in order to comply with such Performance Guarantee, continue or resume performance under the Agreement and eliminate the cause of, and avoid or prevent recurrence of noncompliance with such Performance Guarantee.

Rights and Responsibilities of LIPA Sub. The Agreement provides that LIPA Sub will retain the ultimate authority and control over the assets and operations of the T&D System and the right to direct the Manager in connection with the performance of the Manager's obligations under the Agreement. Without limiting the generality of the foregoing, LIPA Sub's specific rights and responsibilities with respect to the T&D System include: (a) the right to determine all T&D System rates and charges, line extension policies and service rules and regulations applicable to the T&D System and System Power Supply; (b) the right to determine and to change from time to time, in its sole discretion, all policies and procedures for the T&D System consistent with Applicable Law and Prudent Utility Practice; (c) the right to review, amend as appropriate and approve annual capital and operating expenditure budgets pursuant to the procedures outlined in the Agreement and approve or in its discretion, develop, all long-range strategic plans for the T&D System and System Power Supply;

and (d) to the extent the Manager acts as the representative of LIPA Sub in connection with the North American Electric Reliability Council, Northeast Power Coordinating Council, the New York Power Pool, the ISO and any other similar institutions or organizations, the right to direct the Manager's actions with respect thereto.

Customer Services, Rates and Rules of Service. The Agreement provides that the Manager shall perform normal and customary customer services in a manner designed to achieve the highest level of customer service, including, but not limited to: customer account service and maintenance; service restorations account inquiry work; customer assistance, credit and collection services; cashiering; account connection and disconnection; and conservation advice.

The Agreement provides that the Manager shall, unless otherwise directed by LIPA Sub, read the meters of electric commercial, industrial, residential heating and residential multiple rate period customers on a monthly basis and all other electric customer meters on a bi-monthly basis. The Manager shall, according to the schedule of rates, tariffs and policies (the "Schedule of Rates") then in effect, render bills to all T&D System customers in the name of LIPA Sub for electric service delivered on behalf of LIPA Sub and in the format determined by LIPA Sub. To the extent directed by LIPA Sub, such bills will also reflect electric services provided to T&D System customers by other parties. LIPA Sub may implement changes to such rates, rules of service, regulations and procedures by giving written notice to the Manager not later than sixty (60) days prior to the effective date of such change to the extent practicable given the nature of the change. The Manager will maintain customer bills and records as LIPA Sub reasonably requests.

The Manager will use best efforts to collect on a timely basis (1) all amounts due LIPA Sub for service provided to customers, and for other services, in accordance with the Schedule of Rates for the periods in which services were provided, and (2) other monies owed to LIPA Sub pursuant to the operation of the T&D System. The Manager's responsibilities will also include the institution of legal proceedings in LIPA Sub's name to collect utility billings and other monies owed LIPA Sub related to the T&D System. All monies collected by the Manager or its Subcontractors will be the property of LIPA Sub and will be deposited by the Manager daily in an account of LIPA Sub specified pursuant to the Agreement. In collecting such monies, the Manager and any Subcontractor will act solely as an agent for LIPA Sub and will have no right or claim to such moneys and, without limiting the generality of the foregoing, will have no right to assert a claim of set-off, recoupment, abatement, counterclaim or deduction for any amounts which may be owed to the Manager under the Agreement or with respect to any other matter in dispute thereunder.

It is expected that gas customers of Manager's Affiliate and the T&D System electric customers will be billed in a single statement. In the event any electric customer who is also a gas customer will pay less than the total amount due at any time under a single statement, the amounts collected will be applied pro rata between the amounts owed by such customer with respect to electric service and gas service. To the extent moneys are collected for any power supply services provided by any unrelated party, amounts collected will be allocated in accordance with the directions of LIPA Sub. The Manager may elect to bill gas customers separately, provided that the Manager will bear all incremental costs arising by reason of any such election.

Licenses, Permits and Approvals. The Manager will identify for LIPA Sub, prepare, and with LIPA Sub approval, make and prosecute all filings, applications and reports necessary to obtain and maintain all permits, licenses and approvals required to be made, obtained or maintained by each under Applicable Law in order to operate the T&D System.

Operating Period Insurance. Commencing with the Closing Date and continuing throughout the remainder of the Term of the Agreement, the Manager will obtain and maintain, the Required Operating Period Insurance as specified in accordance with the Agreement and will comply with all applicable Insurance Requirements.

Manager's Reporting Requirements

Monthly Reports. The Manager will provide LIPA Sub and the Consulting Engineer with monthly reports no later than 15 Business Days after the end of each month, which include the following data: (1) on a monthly and year-to-date basis, the actual T&D System costs versus the Annual T&D Budget and the prior year's costs at such time, (2) a description and explanation of significant variations (at least $1,000,000 and 3%) from the Annual T&D Budget or the prior year's results, (3) a description of partial or total shutdowns for maintenance and repairs during the prior month and anticipated during the current month, (4) any known or anticipated adverse conditions which may be expected to arise during the next 30 day period that may affect the ability of the Manager to transmit and distribute Power and Energy in accordance with the Performance Guarantees and the annual operating plan established for the T&D System, (5) identification of those costs which are classified as capital versus operating in sufficient detail in order to allow LIPA Sub to determine which costs qualify for bonding under the Bond Resolution and which are to be recovered through T&D System rates, and (6) any other information or statement which is requested by LIPA Sub and which may be reasonably produced from records maintained by the Manager in the normal course of business. The Manager will also provide a quarterly forecast of projected expenditures by line item through year-end.

Semi-Annual Reports. The Manager will, on a semi-annual basis within 60 days after the end of each half of the Contract Year, provide LIPA Sub and the Consulting Engineer with a report of actual Direct Costs and Third Party Costs together with identification of any material Direct Costs projects or Third Party Costs projects which were included in the Direct Cost Budget or the Third Party Cost Budget from the previous Contract Year which were deferred to the current Contract Year or proposed to be deferred to a subsequent Contract Year, or such costs in the current Contract Year which the Manager proposes deferring beyond the current Contract Year.

Other Costs Reports. The Manager will promptly notify LIPA Sub when an event occurs, or is anticipated to occur, that the Manager believes qualifies for treatment as an Other Cost.

Annual Reports. The Manager will furnish LIPA Sub and the Consulting Engineer with the Annual Settlement Statement, an annual summary of the statistical data provided in the monthly reports, certified by the Manager and the Manager's independent public accountants.

Operations Reports. The Manager will prepare appropriate reports concerning matters reasonably related to the operation of or planning for the T&D System, including, but not limited to: source of Power and Energy supply; revenues and unit sales of Power and Energy supplied to customers in the aggregate and by customer class; environmental requirements and compliance; compliance with Applicable Law; safety requirements and compliance; and reports relating to any incentive and penalty provisions set forth in the Agreement.

Fiscal Affairs, Accounting and Record Keeping. The Manager will maintain possession of operating equipment, buildings, materials and supplies, maps, plans, specifications, and customer

billing records during the Term of the Agreement in accordance with the Manager's customary practices or in such manner as LIPA Sub may reasonably require. The Manager also will maintain LIPA Sub's fixed asset books and records for those activities performed by the Manager in general conformity with municipal electric utility accounting standards or such other standards as reasonably requested by LIPA Sub.

All cash held by the Manager for the account of LIPA Sub and all cash collected by the Manager for the account of LIPA Sub after the Closing Date will be deposited on each business day in bank accounts in such bank as LIPA Sub may direct and upon such terms and conditions as may be specified by LIPA Sub.

Purchase of Equipment, Materials and Services. The Agreement provides that the Manager will arrange for the purchase or rental for the account of LIPA Sub of equipment, materials, and supplies and services which are not purchased directly by LIPA Sub or other items necessary to properly operate and maintain the T&D System and to maintain the records of LIPA Sub, and to make such additions and extensions to the T&D System, all as may be required by LIPA Sub. Subcontractors will be subject to approval by LIPA Sub in accordance with the Agreement.

Other Services. The Manager will timely pay all bills related to the T&D System which are proper, appropriate and not otherwise disputed and which it has authority to pay and will assure that, to the extent within the Manager's control, no mechanic's or similar liens are filed against any portion of the T&D System.

Major Capital Improvements

Major Capital Improvements Generally. The Major Capital Plan and Budget provided for in the Agreement is intended to provide for the implementation of major repairs and replacements not constituting routine maintenance of the T&D System. In addition, the Major Capital Plan and Budget is intended to recognize that it will be necessary or desirable from time to time during the Term of the Agreement to modify, alter or improve the T&D System from its then-current condition. All such projects which constitute Major Capital Improvements will be made in accordance with the Agreement and will be owned by LIPA Sub. The Manager will not make a Major Capital Improvement without notifying LIPA Sub and receiving written consent from LIPA Sub unless such Major Capital Improvement is included in the then current annual Major Capital Plan and Budget. LIPA Sub will have the right, when the Manager has materially exceeded the Major Capital Plan and Budget as of an interim date, to require the Manager to defer specific Major Capital Improvements planned for the remainder of the year.

Major Capital Plan and Budget. Contemporaneously with the preparation of the Annual T&D Budget, the Manager is obligated to prepare a proposed annual and five year Major Capital Plan and Budget concerning planned Major Capital Improvement projects.

The annual Major Capital Plan and Budget will be approved by LIPA Sub before or contemporaneously with the adoption of the Annual T&D Budget, provided that in the event the Major Capital Plan and Budget has not been adopted by LIPA Sub as of the beginning of a Contract Year, the Manager may undertake such Major Capital Improvements as reasonably approved by LIPA Sub on a project-by-project basis.

Cost Determination. Major Capital Improvements, except those awarded to the Manager as a result of the competitive procurement procedures established pursuant to the Agreement, will be performed at the cost of the service without any multiplier fee or mark-up.

The Manager will be entitled to incentive payments for cost savings and disincentive payments for cost overruns and delays in scheduled completion of approved Major Capital Improvements equal to 50% of all variances from the approved Major Capital Plan and Budget; provided, however, that no such incentive or disincentive will be payable for cost variances in excess of 15% of the approved Major Capital Plan and Budget. Incentives and disincentives will be trued-up upon the closing and acceptance by LIPA Sub of approved capital projects.

Public Works Improvements. The Agreement provides that the budget for each Public Works Improvement will be subject to LIPA Sub approval and the Manager will not undertake any Public Works Improvement until the budget therefor has been adopted.

Public Works Improvements will be performed at the cost of the service without any multiplier fee or mark-up; provided, however, that such costs will be reduced by all reimbursements or payments received from the applicable Governmental Body for the planning, engineering, procurement and completion of the Public Works Improvement. The Manager will be entitled to certain incentive payments for cost savings and disincentives for cost overruns and delays in scheduled completion that result in incremental costs for approved Public Works Improvement.

Major Capital Improvements for which Manager is Responsible. If the T&D System is damaged or destroyed by reason of circumstances for which the Manager is responsible described below under the heading ''Allocation of Risks of Certain Costs and Liabilities'', the Manager shall promptly proceed to make or cause to be made all Major Capital Improvements reasonably necessary to permit the Manager to perform its obligations under this Agreement. All such Major Capital Improvements for which Manager is responsible as described under the heading ''Allocation of Risks of Certain Costs and Liabilities'' shall be made at the Manager's sole cost and expense, and the Manager shall not be entitled to any compensation from LIPA Sub as a result thereof.

Compensation and Budgets

Service Fee

Formula. Commencing with the first Billing Period and for each Billing Period during the Term of the Agreement, LIPA Sub will pay the Manager a Service Fee for the services provided by the Manager under the terms of the Agreement in accordance with the following formula:

$$SF = FDF + TPC + VP + CIF \pm NCPI$$

Where

SF = Service Fee

FDF = Fixed Direct Fee

TPC = Third Party Costs

VP = Variable Payment

CIF = Cost Incentive Fee

NCPI = Non-cost Performance Incentives and Disincentives

Each component of the Service Fee will be computed in accordance with the Agreement and may be adjusted from time to time as provided in the Agreement. In addition to the Service Fee, Manager will be entitled to payment for cost overruns as and to the extent as discussed below.

Fixed Direct Fee. LIPA Sub will make a monthly payment to the Manager equal to ninety percent (90%) of the approved annual Direct Cost Budget (the "Fixed Direct Fee").

Third Party Costs. LIPA Sub will make a monthly payment to the Manager for the monthly allocation of the approved annual Third Party Cost Budget.

Variable Payment. The Manager will be entitled to a Variable Payment equal to the lesser of (a) the difference between actual Total Costs (the sum of the actual Direct Costs and the actual Third Party Costs), less the sum of the Fixed Direct Fee and the lesser of actual or budgeted Third Party Costs or (b) the difference between the approved Total Cost Budget (the sum of the Direct Cost Budget and the Third Party Cost Budget) less the sum of the Fixed Direct Fee and the lesser of the actual or budgeted Third Party Costs. Monthly allocation of such payment will be determined by the parties based on historical monthly trends to minimize working capital costs.

Management Fee, Cost Incentive Fee and Non-cost Performance Incentives and Disincentives. To the extent actual Total Costs are less than the approved Total Cost Budget for the year, the Manager will be paid the portion of its Management Fee, described within the definition of Direct Costs as discussed below under the heading "Annual T&D Budget and Five Year Planning Budget" (relating to cost savings), in an amount equal to such cost savings up to a maximum of $5 million. Beyond such $5 million level, the Manager will be paid a Cost Incentive Fee equal to 50% of such additional savings, provided that no incentive will be paid for savings in excess of 15% of the Total Cost Budget. All savings above this cap will be for the benefit of LIPA Sub.

Cost Overruns. To the extent actual Total Costs, excluding the Management Fee, are greater than the Total Cost Budget, excluding the net Management Fee, for the applicable Contract Year, the Manager will absorb the first dollars of such overruns, up to a maximum total of $15 million in each Contract Year. For cost overruns in excess of this amount, the Manager will be entitled to a payment through the Annual Settlement Statement equal to the amount of such excess overruns (the "Overrun Payment").

Limitations. The Agreement provides that the ratio of (1) the sum of the Variable Payment plus the Cost Incentive Fee plus the sum of the Non-cost Performance Incentives and Disincentives (as discussed below under the heading "Non-Cost Performance Incentives and Disincentives") plus the Overrun Payment divided by (2) the sum of (a) the amounts described in (1) above and (b) the Fixed Direct Fee, will not be greater than twenty percent (20%) in any Contract Year.

Annual T&D Budget and Five Year Planning Budget Process

General. The Agreement provides that the Annual T&D Budget and the Five-Year Planning Budget will be established in the manner described below and will provide for the determination and payment of the Manager's costs of operating and maintaining the T&D System and performing its obligations under the Agreement, inclusive of fees paid to the Manager. The Annual T&D Budget and the Five-Year Planning Budget will be comprised of two broad categories: Direct Costs and Third Party Costs. These categories of costs will exclude Incremental Internal Costs and additional Third Party Costs relating to Major Capital Improvements, Public Works Improvements, and Other Costs.

In establishing the Direct Cost Budget for the initial Annual T&D Budget under the Agreement, the Direct Cost Budget will include (1) amounts to compensate the Manager for Operation and Maintenance Services costs anticipated to be reasonably predictable and incurred by the Manager through the utilization of either its work force, or its owned assets, in carrying out its responsibilities under the Agreement and (2) the Manager's fee.

The Third Party Cost Budget will include amounts for reimbursement of, on a dollar for dollar basis, all recurring capital or operating costs incurred by the Manager in carrying out its responsibilities under the Agreement and paid to parties other than the Manager, its parent or affiliates, and any of their employees.

The Manager will be entitled to receive Cost Incentive Fees, as discussed above under the heading "Service Fee", for costs savings from the amounts included for Direct Costs and Third Party Costs in the approved Annual T&D Budget.

Annual T&D Budget Preparation. The Agreement provides that no later than six months prior to the end of each Contract Year, the Manager will prepare a recommended annual budget for the operation and maintenance, including routine capital projects not constituting Major Capital Improvements or Public Works Improvements, of the T&D System and a recommended annual budget for total revenue requirements, inclusive of LIPA Sub's own costs, with the costs that will be paid by LIPA Sub to Manager under the Agreement specifically and separately identified (together, the "Annual T&D Budget"). The recommended Annual T&D Budget will be accompanied by the Five-Year Planning Budget. LIPA will hold at least one hearing to solicit public input on the initial budgets.

LIPA Sub has established an initial Direct Cost Budget. Subsequent annual Direct Cost Budgets will be calculated based upon the initial Direct Cost Budget, subject to adjustments for the "Direct Cost Budget Indices" described in an appendix to the Agreement.

The Agreement provides that the Annual T&D Budget and Five-Year Planning Budget prepared by the Manager and submitted to LIPA Sub for review and approval will be accompanied by any Manager-recommended rate adjustments for the upcoming year at least six months before the beginning of each subsequent Contract Year. The Agreement provides that LIPA Sub will have 60 days to review the proposed Annual T&D Budget and Five-Year Planning Budget and any rate adjustments and to propose modifications as it deems appropriate, so as to have the Annual T&D Budget and the Five-Year Planning Budget adopted at least two months before the beginning of the next Contract Year. All rate proposals will be subject to public hearings prior to approval by LIPA Sub.

Other Costs. The Agreement provides that "Other Costs" are those costs which cannot reasonably be anticipated and will include those costs the Manager and LIPA Sub agree are not included in the Direct Cost Budget, Third Party Cost Budget or Major Capital Plan and Budget ("Other Costs"). Other Costs include the Incremental Internal Costs and additional Third Party Costs incurred by the Manager as a result of events (including but not limited to major storms and extreme weather) that the Manager and LIPA Sub agree have caused costs to be incurred by the Manager to respond to significant (i) damage to or adverse affects on the T&D System, (ii) changes in the level of required maintenance or operation of the T&D System, or (iii) tasks which are necessary for safety reasons.

Although Other Costs will not be budgeted, the Manager will recommend, and LIPA Sub will adopt, an annual reserve level for Other Costs for each Annual T&D Budget and Five-Year Planning Budget to enable estimation of total "System Revenue Requirements," consisting of the sum of the annual Service Fee, plus an estimate of other costs plus debt service requirements on LIPA's Revenue Bonds plus LIPA's costs as reported to the Manager pursuant to the Agreement. The Manager will be reimbursed for reasonably incurred Other Costs.

Non-Cost Performance Incentives and Disincentives. In addition to the cost saving incentives discussed above under the heading "Annual T&D Budget and Five Year Planning Budget Process," the Manager will be eligible for incentives for performance above certain threshold target levels of performance standards ("Non-cost Performance Incentives") and subject to disincentives for performance below certain other threshold minimum performance standard levels ("Non-cost Performance Disincentives"), with an intermediate band of performance in which neither incentives nor disincentives will apply, for reliability, worker safety, and customer service, all as provided in or established pursuant to the Agreement.

In any Contract Year in no event will the total of the Non-cost Performance Incentives, net of any applicable Non-cost Performance Disincentives, together with the System Power Supply Performance Incentive/Disincentive, be greater than $7.5 million, nor will the total Non-cost Performance Disincentives, net of any applicable Non-cost Performance Incentives together with the System Power Supply Performance Incentive/Disincentive be greater than $7.5 million.

LIPA Sub Non-Performance. If caused by an event the costs of which LIPA Sub is responsible for as discussed below under the heading "Allocation of Risk of Certain Costs and Liabilities," there will be an increase in the Manager's cost of Construction Work or Operation and Maintenance Services, the amount of any such incremental cost increase will be borne by LIPA Sub to the extent it is responsible therefor and will not be considered for purposes of calculating any incentive or disincentive thereunder.

If at any time the T&D System is damaged or destroyed due to an event for which LIPA Sub is responsible, LIPA Sub will pay all Major Capital Improvement Costs and adjustments as are required to be made by LIPA Sub pursuant to applicable provisions of the Agreement.

Manager Non-Performance. If due to an event for which the Manager is responsible as discussed below under the heading "Allocation of Risk of Certain Costs and Liabilities," there will be an increase in the Manager's cost of Construction Work or Operation and Maintenance Services, or in LIPA Sub's costs associated with performing obligations under the Agreement, the amount of any such incremental cost increase will be borne by the Manager to the extent it is responsible therefor.

Annual Settlement. The Agreement provides that the Manager will deliver to LIPA Sub within 60 days after the end of each Contract Year, an Annual Settlement Statement, setting forth the actual aggregate Service Fee payable with respect to such Contract Year and a reconciliation of such amount with the amounts actually paid by LIPA Sub pursuant to the billing statements. The Annual Settlement Statement will also include an accounting of any incentives or disincentives accrued during the applicable Contract Year which LIPA Sub will have an opportunity to review prior to payment.

During the first quarter of the following Contract Year, the monthly payments made to the Manager by LIPA Sub will be (i) reduced by any overpayment by LIPA Sub or (ii) increased to reflect any Non-Cost Performance Incentive earned by the Manager during the previous year and/or any Overrun Payment due.

LIPA Sub's Payment Obligations. The Agreement provides that amounts payable to the Manager under the Agreement will be paid from T&D System revenues and other funds of LIPA Sub available for such purposes in accordance with the terms of the Resolution.

The Agreement contemplates that if any billing disputes cannot be resolved within 30 days, either party may refer such dispute for resolution as discussed below under the heading "Non-Binding Mediation; Arbitration."

Allocation of Risks of Certain Costs and Liabilities. The Agreement provides that except to the extent due to Subsidiary Fault (as determined by either a final non-appealable order or judgment of a court of competent jurisdiction (including administrative tribunals) or a final non-appealable binding arbitration decision), the Manager will be responsible and liable to LIPA Sub for, and will not be entitled to reimbursement from LIPA Sub for any Loss-and-Expense incurred by the Manager or LIPA Sub,

(a) due to any gross negligence or willful misconduct by the Manager during the period commencing six months prior to the Closing Date to the extent LILCO knew or should have known of such gross negligence or willful misconduct and during the Term of the Agreement in carrying out its obligations thereunder,

(b) due to any violation of or failure of compliance with Applicable Law by the Manager (except as provided below) during the period commencing six months prior to the Closing Date to the extent LILCO knew or should have known of such violation or failure of compliance and during the Term which materially and adversely affects

(i) the condition or operations of the T&D System,

(ii) the financial condition of LIPA Sub,

(iii) the performance or ability of the Manager to perform its obligations under the Agreement, or

(iv) the cost of providing electric service to the customers of the T&D System, provided, however, that Manager will not be responsible and liable to LIPA Sub under the provisions of the Agreement described in this clause (b) with respect to any violation of, failure of compliance with, or liability under, Environmental Laws (as defined in the LIPA/LILCO Merger Agreement) for which LIPA Sub or the Manager may be strictly liable provided that Manager (or for actions prior to the Closing Date, LILCO) acted in a manner consistent with Prudent Utility Practice. Notwithstanding the foregoing, Manager will in all events be liable for any fine or penalty arising by reason of any violation of or failure of compliance with Applicable Law for acts or omissions of the Manager not consistent with Prudent Utility Practice,

(c) due to any criminal violation of Applicable Law by the Manager (or for actions prior to the Closing Date, LILCO), or

(d) due to an event which gives rise to a cost not included in the Direct Cost Budget or Third Party Cost Budget or a cost incurred with respect to Major Capital Improvements or Public Works Improvements, that is incurred by reason of actions or omissions of the Manager not consistent with Prudent Utility Practice.

Default, Termination For Cause And Dispute Resolution

Remedies for Breach. Subject to the provisions of the Agreement described below under the heading "Non-Binding Mediation; Arbitration," in the event that either party breaches any other

obligation under the Agreement or any representation made by either party under the Agreement is untrue in any material respect, the other party will have the right to take any action at law or in equity it may have to enforce the payment of any damages or the performance of such other obligation under the Agreement and such right to recover damages or to be reimbursed as provided therein will ordinarily constitute an adequate remedy for any breach of such other obligation or any material untruth in any such representation. Either party may enforce by an action for specific performance the other party's obligations under the Agreement in the event a material breach thereof has occurred and is continuing. Neither party will have the right to terminate the Agreement for cause except after an Event of Default determined in accordance with the provisions of the Agreement has occurred.

Events of Default by the Manager

(1) *Events of Default Not Requiring Cure Opportunity for Termination.* Each of the following shall constitute an Event of Default on the part of the Manager for which LIPA Sub may terminate the Agreement without any requirement of cure opportunity:

(a) *Change of Control.* Change of Control of the Manager, the Parent or the Guarantor; provided, however, that the combination effectuated under the BUG/LILCO Agreement or the LIPA/LILCO Merger Agreement shall not constitute a Change of Control of the Manager for purposes of this provision.

(b) *Worker Safety/Customer Service.* Failure for two out of three consecutive years, for reasons other than major storms or extreme weather, to achieve the "Minimum Worker Safety Standard" or "Minimum Customer Service Standard," as such standards are established in accordance with appendices to the Agreement.

(c) *Bankruptcy.* Certain voluntary or involuntary events relating to bankruptcy affecting the Manager, the Parent or the Guarantor.

(d) *Credit Enhancement.* Failure of the Manager to supply, maintain, renew, extend or replace the credit enhancement required under the Agreement (see "General—Credit Enhancement in Certain Circumstances" below).

(e) *Letter of Credit Draw.* Failure of the Manager to supplement, replace or cause to be reinstated the letter of credit as described in the Agreement (see "General—Credit Enhancement in Certain Circumstances" below) within 30 days following draws equal to, in the aggregate, 50% of the face value thereof.

(2) *Events of Default Requiring Cure Opportunity for Termination.* Each of the following shall constitute an Event of Default on the part of the Manager for which LIPA Sub may terminate the Agreement upon compliance with the notice and cure provisions set forth below:

(a) *System Reliability.* Failure to achieve, for two out of three consecutive years, the "Minimum Reliability Standard" specified in the Agreement.

(b) *Failure to Pay or Credit.* Failure of the Manager to pay or credit undisputed amounts owed to LIPA Sub under the Agreement within 90 days following the applicable due date

(c) *Failure to Comply with Agreement or Guaranty.* The failure or refusal of the Manager to perform any material obligation under the Agreement, or the failure of the Guarantor to comply with any of its material obligations under the Guaranty unless such failure or refusal is excused by an Uncontrollable Circumstance or Subsidiary Fault; except that no such failure or refusal in clause (b) or (c) will constitute an Event of Default giving LIPA Sub the right to terminate the

Agreement for cause unless LIPA Sub has given prior written notice to the Manager or the Guarantor and the Manager or the Guarantor, as applicable, has neither challenged in an appropriate forum LIPA Sub's conclusion nor corrected or diligently taken steps to correct such default within a reasonable period of time, but not more than 60 days, from receipt of the notice (but if the Manager or the Guarantor shall have diligently taken steps to correct such default within a reasonable period of time, the same shall not constitute an Event of Default for as long as the Manager or the Guarantor is continuing to take such steps to correct such default).

Events of Default by LIPA Sub. Each of the following shall constitute an Event of Default on the part of LIPA Sub for which the Manager may terminate the Agreement upon compliance with the notice and cure provisions set forth below:

(a) *Failure to Pay.* The failure of LIPA Sub to pay undisputed amounts owed to the Manager under the Agreement within 90 days following the due date for such payment.

(b) *Failure to Comply with Agreement.* The failure or refusal by LIPA Sub to perform any material obligation under the Agreement unless such failure or refusal is excused by an Uncontrollable Circumstance or Manager Fault; except that no such failure or refusal will constitute an Event of Default giving the Manager the right to terminate the Agreement for cause unless the Manager has given prior written notice to LIPA Sub and LIPA Sub has neither challenged in an appropriate forum the Manager's conclusion nor corrected or diligently taken steps to correct such default within a reasonable period of time, but not more than 60 days, from the date of the notice (but if LIPA Sub shall have diligently taken steps to correct such default within a reasonable period of time, the same shall not constitute an Event of Default for as long as LIPA Sub is continuing to take such steps to correct such default).

(c) *Change of Control of LIPA Sub.* A change of control of LIPA Sub which results in ownership control of LIPA Sub by other than a state public benefit corporation, authority, political subdivision or other instrumentality of the State or any political subdivision thereof.

Procedure for Termination for Cause. If any party has a right of termination for cause, the right may be exercised by giving a notice of termination for cause to the party in default at least two years prior to (or, in the case of a bankruptcy or insolvency default or a Change of Control, simultaneously with, or, in the case of an Event of Default as discussed above under the heading "Events of Default by LIPA Sub," six months) the date of termination specified in such notice (the "Termination Date").

Non-Binding Mediation; Arbitration

The Agreement provides that any dispute arising out of or relating to the Agreement will be resolved in accordance with the mediation and arbitration procedures for the resolution of such disputes established by the Agreement, which shall constitute the sole and exclusive procedures for the resolution of such disputes.

Either party may, without prejudice to any negotiation, mediation, or arbitration procedures, proceed in any court to obtain provisional judicial relief if, in such party's sole discretion, such action is necessary to avoid imminent irreparable harm, to provide uninterrupted electrical and other services, or to preserve the status quo pending the conclusion of the dispute procedures specified in the Agreement.

Provisional Relief

LIPA Sub Emergency Powers. The Agreement provides that if the Manager, due to Uncontrollable Circumstances or any other reason whatsoever, fails to provide any Operation and Maintenance Services and Construction Work contemplated by the Agreement and LIPA Sub or any Governmental Body finds that such failure endangers or menaces the public health, safety or welfare, then LIPA Sub will have the right, upon notice to the Manager, during the period of such emergency, to take possession of and use any or all of the Operating Assets necessary to transmit and distribute Power and Energy which the Manager would otherwise be obligated to transmit and distribute. The Manager will fully cooperate with LIPA Sub to effect such a temporary transfer of possession of the Operating Assets for LIPA Sub's use of the same.

Term

Term of Agreement. The Agreement commences on the Contract Date and will continue in effect until the eighth (8th) anniversary of the Closing Date, unless earlier terminated in accordance with its terms.

Mandatory Competitive Selection of Future Managers. LIPA Sub will conduct a competitive procurement for T&D System management services following the fifth anniversary of the Closing Date. The Manager will have the right or be ineligible to submit a bid in such procurement on the same basis as other bidders unless the Agreement is terminated due to an Event of Default of the Manager. The Manager is obligated to cooperate with LIPA Sub during such procurement process.

Miscellaneous Provisions

Affiliate. Pursuant to the Agreement, the Manager has agreed to remain an Affiliate of the Guarantor.

Credit Enhancement in Certain Circumstances. The Agreement provides that if the Guarantor's credit rating declines below investment grade, then the Manager shall provide credit enhancement of its obligations under the Agreement in the form of either (i) an unconditional guarantee of all of GENCO's obligations under the Power Supply Agreement, the Manager's obligations under the Management Services Agreement, and the Energy Manager's obligations under the Energy Management Agreement, provided by a corporation or financial institution whose long-term senior debt is or would be rated investment grade, or (ii) an irrevocable letter of credit securing GENCO's obligations under the Agreement, the Manager's obligations under the Management Services Agreement, and the Energy Manager's obligations under the Energy Management Agreement, in a face amount of $60,000,000 provided by a financial institution whose long-term senior debt is rated investment grade. The amount of such letter of credit shall be reduced by $30,000,000 if the Energy Management Agreement has theretofore been or is thereafter terminated and by $4,000,000 if the Power Supply Agreement has theretofore been or is thereafter terminated, such obligation to continue until the expiration or termination of the Agreement, the Power Supply Agreement and the Energy Management Agreement.

Uncontrollable Circumstances Generally. Except as otherwise specifically provided in the Agreement, neither LIPA Sub nor the Manager will be liable to the other for any failure or delay in performance of any obligation under the Agreement to the extent due to the occurrence of an Uncontrollable Circumstance.

Indemnification. The Agreement provides that the Manager, to the extent permitted by law, will protect, indemnify and hold harmless LIPA Sub and its respective representatives, trustees, officers, employees and subcontractors (as applicable in the circumstances), (the "Subsidiary Indemnified Parties") from and against (and pay the full amount of) any Loss-and-Expense and will defend Subsidiary Indemnified Parties in any suit, including appeals, for personal injury to, or death of, any person, or loss or damage to property arising out of any matter for which the Manager is responsible under the caption "Allocation of Risk of Certain Costs and Liabilities" in the Agreement and LIPA Sub, to the extent permitted by law, will protect, indemnify and hold harmless the Manager and its Affiliates and their respective officers, directors, Subcontractors (as applicable in the circumstances) and employees (the "Manager Indemnified Parties") from and against (and pay the full amount of) any Loss-and-Expense, and will defend the Manager Indemnified Parties in any suit, including appeals, for personal injury to, or death of, any person, or loss or damage to property arising out of any matter for which Subsidiary is responsible under the caption "Allocation of Risk of Certain Costs and Liabilities" in the Agreement. The foregoing indemnifications are subject to certain exceptions, including the negligence or other wrongful conduct of any indemnified party and any Uncontrollable Circumstance.

Assignment and Transfer. The Agreement may be assigned by either party only with the prior written consent of the other party, except that without the consent of the other party (1) LIPA Sub may make such assignments, create such security interests in its rights thereunder and pledge such monies receivable thereunder as may be required in connection with issuance of Revenue Bonds; (2) LIPA Sub may assign its rights, obligations and interests thereunder, or transfer such rights and obligations by operation of law, to any other governmental entity or to a subsidiary of LIPA Sub provided that the successor entity gives reasonable assurances to the Manager that it will be able to fulfill LIPA Sub's obligations thereunder; and (3) the Manager may assign its rights, obligations and interests thereunder to the Parent or any Affiliate thereof except that the Manager may not, without the consent of LIPA Sub, make any assignment or other transfer to any person of its rights and obligations under the Agreement unless the Guaranty is and remains in full force and effect and unless the Guarantor or a majority-owned direct or indirect subsidiary of the Guarantor will have control of and responsibility for the Operation and Maintenance Services and any Construction Work. Effective upon the Closing Date, LIPA may assign its rights, obligations and interests under the Agreement to LILCO (then a wholly-owned subsidiary of LIPA) and the Manager shall assign all of its rights, obligations and interests under the Agreement to the Parent or any Affiliate thereof.

SUMMARY OF CERTAIN PROVISIONS OF THE POWER SUPPLY AGREEMENT

The following is a brief summary of certain provisions of the Power Supply Agreement. The summary does not purport to be complete or definitive and is qualified in its entirety by reference to the Power Supply Agreement, a copy of which is on file with the Trustee.

General

The Power Supply Agreement was executed initially by LILCO and LIPA. In accordance with the provisions of the LIPA/LILCO Merger Agreement, and as permitted by the assignment provisions of the Power Supply Agreement, effective upon the Closing Date the rights and obligations of LILCO and LIPA under the Power Supply Agreement will be assigned to BL Holding Corp. and its subsidiaries (''GENCO'') and to LIPA Sub, respectively. For purposes of this summary, such assignees are treated as the parties to the Power Supply Agreement.

The Power Supply Agreement sets forth the terms and conditions for the sale and delivery of electric capacity and energy by GENCO to LIPA Sub.

Power Supply

Delivery of Power. The Agreement provides that during the term of the Agreement GENCO shall sell and deliver to LIPA Sub, and LIPA Sub shall purchase and accept delivery from GENCO of, (i) all the capacity from the GENCO Generating Facilities, and (ii) all the energy that GENCO produces from the GENCO Generating Facilities, in accordance with the Agreement, that LIPA Sub requests to meet the electricity requirements of its retail and wholesale electricity customers (regardless of whether located inside or outside the Service Area). The Agreement also provides that GENCO will provide the various Ancillary Services as required by LIPA Sub, and LIPA Sub shall pay for any associated costs not otherwise compensated by LIPA Sub.

Sale or Assignment of Generating Units. The Agreement provides that GENCO shall not sell or otherwise assign any interest in any of its generating units (as set forth in an appendix to the Agreement) except for (i) liens securing bona fide debt or other encumbrances incurred in the ordinary course of business, (ii) capital leases, or (iii) sales or assignments made with LIPA Sub's prior written consent, which consent shall be deemed to have been given in respect of certain easements specified in the Agreement.

Transmission Requirements. The Agreement provides that LIPA Sub is responsible for all transmission reinforcements required in conformance with Prudent Utility Practice for any new generation, including any new interconnections and other T&D System requirements regardless of their location, sufficient to maintain the delivery of electricity from the GENCO Generating Facilities onto the T&D System. The additional costs charged to GENCO for such transmission reinforcements will not be greater than if such costs were allocated to all of the LIPA Sub Electricity Customers and transmission service customers on an average system basis.

Purchase Price and Payment

The Agreement provides that during the Term of the Agreement LIPA Sub will pay to GENCO monthly an amount equal to the aggregate of the following components:

(i) a capacity charge to compensate GENCO for its fixed costs of generating electricity from the GENCO Generating Facilities,

(ii) a variable charge based on the variable operation and maintenance costs as established by the Agreement, multiplied by the actual MWh of operation of the GENCO Generating Facilities,

(iii) a charge for any costs incurred by GENCO in providing certain Ancillary Services to LIPA Sub, if any such services are required by LIPA Sub which are not otherwise compensated by the charges described in items (i) and (ii) above,

(iv) a charge for non-variable related expenses net of insurance proceeds, that cannot be planned for with any certainty and are outside the control of GENCO, and

(v) certain other miscellaneous charges as specified in the Agreement.

Budgets

Pursuant to the Agreement, GENCO and LIPA Sub have agreed to an initial five-year plan which provides details on the fixed and variable costs of operating the GENCO Generating Facilities. The budget establishes the monthly capacity charge and the monthly variable charge for the first year of the five-year period, which forms the basis for adjustment for subsequent years in such period in accordance with the terms of the Agreement.

The Agreement provides that prior to the commencement of each successive five-year period during the term of the Agreement, GENCO shall prepare and submit to LIPA Sub for review and approval a proposed five-year budget plan. If GENCO and LIPA Sub are unable to reach agreement concerning the budget plan, those portions that are in dispute shall be resolved in a proceeding before the FERC.

The Agreement also provides that GENCO shall annually prepare and submit to LIPA Sub a rolling Five Year Capital Improvement Budget for incremental capital expenditures and associated rate adjustments for LIPA Sub's review and approval.

Capacity Ramp Down Option

The Agreement provides that, commencing in the seventh year of the Agreement, LIPA Sub may determine to reduce the amount of capacity purchased from GENCO. In any such an event, LIPA Sub shall immediately reimburse GENCO for the capacity charges in the amount set forth in the Agreement that would have been recovered from LIPA Sub over the remaining portion of the original term of the Agreement. The Agreement provides that such reduction may not be greater than 1500 MW.

Term and Termination

Term. The Agreement commences on the Closing Date for an initial term of fifteen (15) years. The Agreement provides that it shall terminate upon the purchase of the GENCO Generating Facilities by LIPA Sub as provided for under the Generation Purchase Right Agreement attached to the Merger Agreement.

Termination for Cause by GENCO. The Agreement provides that GENCO shall have the right to terminate the Agreement for cause if one of the following events shall have occurred:

(1) *Failure to Pay.* The failure of LIPA Sub to pay undisputed amounts owed to GENCO under the Agreement within 90 days of such amounts having become due.

(2) *Failure to Comply with Agreement.* The failure or refusal by LIPA Sub substantially to perform any material obligation under the Agreement unless such failure or refusal is excused by force majeure (as defined in the Agreement), except that the Agreement further provides that

no such failure or refusal to pay or perform as referenced in these clauses (1) and (2) shall constitute an Event of Default giving GENCO the right to terminate the Agreement for cause unless GENCO has given prior written notice to LIPA Sub stating that a specified failure or refusal to perform exists and LIPA Sub has neither challenged in an appropriate forum GENCO's conclusion nor corrected or diligently taken steps to correct such default within a reasonable period of time, but not more than 60 days, from the date of the notice (but if LIPA Sub shall have diligently taken steps to correct such default within a reasonable period of time, the same shall not constitute an Event of Default for as long as LIPA Sub is continuing to take such steps to correct such default).

Termination For Cause by LIPA Sub. The Agreement provides that LIPA Sub shall have the right to terminate the Agreement for cause after one of the following Events of Default as determined in accordance with the provisions of the Agreement shall have occurred:

(1) *Events of Default Not Requiring Cure Opportunity for Termination.* Each of the following shall constitute an Event of Default on the part of GENCO for which LIPA Sub may terminate the Agreement without any requirement of cure opportunity:

(a) *Change of Control of GENCO.* Change of Control of GENCO or the Guarantor has occurred; provided, however, that the combination effectuated under the LIPA/LILCO Merger Agreement shall not constitute a Change of Control of GENCO for purposes of this provision.

(b) *Bankruptcy.* Certain voluntary or involuntary events relating to bankruptcy affecting GENCO or the Guarantor.

(c) *Credit Enhancement.* Failure of GENCO to supply, maintain, renew, extend or replace the credit enhancement required under the Agreement (see below, "Credit Enhancement in Certain Circumstances" below).

(d) *Letter of Credit Draw.* Failure of GENCO to supplement, replace or cause to be reinstated the letter of credit as described in the Agreement (see "Credit Enhancement in Certain Circumstances" below) within 30 days following draws equal to, in the aggregate, 50% of the face value thereof.

(2) *Events of Default Requiring Cure Opportunity for Termination.* Each of the following shall constitute an Event of Default on the part of GENCO for which LIPA Sub may terminate the Agreement upon compliance with the notice and cure provisions of the Agreement described below:

(a) *Failure to Comply with Agreement.* The failure or refusal by GENCO to substantially perform any material obligation under the Agreement, except that no such failure or refusal shall constitute an Event of Default giving LIPA Sub the right to terminate the Agreement for cause unless LIPA Sub has given prior written notice to GENCO or the Guarantor, as applicable, stating that a specified failure or refusal to perform exists and GENCO or the Guarantor, as applicable, has neither challenged in an appropriate forum LIPA Sub's conclusion nor corrected or diligently taken steps to correct such default within a reasonable period of time, but not more than 60 days, from receipt of the notice (but if GENCO or the Guarantor shall have diligently taken steps to correct such default within a reasonable period of time, the same shall not constitute an Event of Default for as long as GENCO or the Guarantor is continuing to take such steps to correct such default).

Procedure for Termination for Cause. If either GENCO or LIPA Sub shall have a right of termination for cause in accordance with the provisions of the Agreement outlined above, the same may be exercised by notice of termination given to the party in default at least two years prior to (or, in the case of a bankruptcy or insolvency default or a Change of Control, simultaneously with or, in the case of an event of default described in clauses (1)(c) or (1)(d) above, six months) the date of termination specified in such notice.

Non-binding Mediation; Arbitration

The Agreement provides that any dispute arising out of or relating to the Agreement shall be resolved in accordance with the mediation and arbitration procedures for the resolution of such disputes established by the Agreement which shall constitute the sole and exclusive procedures for the resolution of such disputes.

Affiliate

Pursuant to the Agreement, GENCO has agreed to remain an Affiliate of the Guarantor.

Credit Enhancement in Certain Circumstances

The Agreement provides that if the Guarantor's credit rating declines below investment grade, then GENCO shall provide credit enhancement of its obligations under the Agreement at its sole cost and expense in the form of either (i) an unconditional guarantee of all of GENCO's obligations under the Agreement, the Manager's obligations under the Management Services Agreement, and the Energy Manager's obligations under the Energy Management Agreement, provided by a corporation or financial institution whose long-term senior debt is or would be rated investment grade, or (ii) an irrevocable letter of credit securing GENCO's obligations under the Agreement, the Manager's obligations under the Management Services Agreement, and the Energy Manager's obligations under the Energy Management Agreement, in a face amount of $60,000,000 provided by a financial institution whose long-term senior debt is rated investment grade.

Allocation of Risk of Certain Costs and Liabilities

The Agreement contains provisions relating to the allocation of risks and liabilities that are substantially the same as the provisions of the Management Services Agreement described herein under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budgets—Allocation of Risks of Certain Costs and Liabilities."

SUMMARY OF CERTAIN PROVISIONS OF THE ENERGY MANAGEMENT AGREEMENT

The following is a brief summary of the Energy Management Agreement. The summary does not purport to be complete or definitive and is qualified in its entirety by reference to the Energy Management Agreement, a copy of which is on file with the Trustee.

General

The Energy Management Agreement was executed initially by LILCO and LIPA. In accordance with the provisions of the LIPA/LILCO Merger Agreement, and as permitted by the assignment provisions of the Energy Management Agreement (see "Miscellaneous Provisions—Assignment and Transfer" below), effective upon the Closing Date the rights and obligations of LILCO and LIPA under the Energy Management Agreement will be assigned to BL Holding Corp. and its subsidiaries (the "Energy Manager") and to LIPA Sub, respectively. For purposes of this summary, such assignees are treated as the parties to the Energy Management Agreement.

The Energy Management Agreement establishes the terms and conditions for the management by the Energy Manager of fuel supplies used at the GENCO Generating Facilities to produce electric energy for delivery to LIPA Sub, and for management and administration of the System Power Supply on behalf of LIPA Sub in a manner consistent with policies established by LIPA Sub.

Scope of Energy Management Services

As described in the Agreement, the Energy Manager is responsible for (a) fuel procurement, delivery, storage, and management for GENCO Generating Facilities to meet the energy generation requirements of the Electricity Customers, (b) the dispatch of all System Power Supply available to LIPA Sub to meet total capacity and energy requirements of the Electricity Customers and Off-System Sales, (c) the purchase, on behalf of LIPA Sub, of all capacity and energy to meet the needs of the Electricity Customers and (d) the sale, on behalf of LIPA Sub, of Electricity owned by, or under contract to, LIPA Sub which is not otherwise required to meet the needs of the Electricity Customers. The Agreement provides that all such responsibilities will be discharged in a manner consistent with Prudent Utility Practice, the System Policies and Procedures and New York State Public Service Commission policies and procedures pertaining to retail gas customer service. In discharging all such functions, the Energy Manager is obligated to use best efforts to obtain the least-cost fuel and least-cost capacity and energy for the benefit of the Electricity Customers.

The Energy Manager agrees to establish policies and procedures satisfactory to LIPA Sub designed to assure that the Energy Manager's responsibilities are performed without consideration of the ownership or economic return to the Energy Manager or its Affiliates, except for the incentive provisions of the Agreement (described below at "Fuel Management—Fuel Management Compensation—Fuel Purchase Performance Incentives/Disincentive Payments"), and comply with such policies and procedures.

The Agreement provides that in no event will the Energy Manager take title to Electricity being purchased or sold thereunder.

Fuel Management

Fuel Management Services. The Agreement provides that the Energy Manager will manage all aspects of the Fuel supply for the GENCO Generating Facilities, including determinations regarding

the type of Fuel used for operating the GENCO Generating Facilities and the source of such Fuel supply taking into account the purchase of alternate sources of Electricity in lieu of Electricity from the GENCO Generating Facilities when economic. LIPA Sub agrees to compensate the Energy Manager for such Fuel management services, including a Fuel Purchase Performance Incentive/ Disincentive Payment, in accordance with the terms of the Agreement (see "Fuel Management—Fuel Purchase Performance Incentives/Disincentive Payments" below). The Energy Manager will not contract for additional firm assets specifically for use in the GENCO Generating Facilities unless LIPA Sub and the Energy Manager agree to the contract.

Fuel Management Compensation. During the Term of the Agreement, LIPA Sub will make monthly payments to the Energy Manager consisting of an amount equal to the sum of: (i) the Monthly Fuel Management Fee, plus (ii) the Monthly Fuel Payment, plus or minus (iii) the Fuel Purchase Performance Incentive/Disincentive.

Fuel Management Fee. The Energy Manager will be paid an annual Fuel Management Fee in consideration for the Energy Manager's performance of the Fuel Services contemplated in the Agreement. Such Fuel Management Fee includes a fee of $750,000 and an allowance for certain costs (the "cost-related component") which, for 1998, has been established at $1,232,000. The Agreement provides that the cost-related component of the initial Fuel Management Fee, once established and approved by LIPA Sub, will be indexed in the same manner as the Direct Cost Budget under the Management Services Agreement until the termination of the Management Services Agreement and thereafter will be subject to mutually agreeable adjustments. LIPA Sub is obligated to pay the Fuel Management Fee to the Energy Manager in twelve equal monthly installments.

Monthly Fuel Payment. LIPA Sub will, in accordance with the provisions discussed below at "Fuel Management—Payment," pay the total monthly cost of all Fuel for use in the GENCO Generating Facilities that are under contract to LIPA Sub pursuant to the Power Supply Agreement, including but not limited to any current or future fuel related taxes or other fuel related fees or costs reasonably incurred by the Energy Manager. This cost will be based upon (a) the actual variable cost of gas delivered to the delivery points for such fuel plus (i) any incremental Firm Gas Supply costs which are incurred based on use of Firm Gas Supplies in the operation of the GENCO Generating Facilities, (ii) any costs the Energy Manager incurs based on non-use of gas it has otherwise contracted to purchase for use in the operation of the GENCO Generating Facilities, and (iii) the Local Transportation Charge and (b) the delivered cost of oil for use in GENCO's Generating Facilities.

Fuel Purchase Performance Incentives/Disincentive Payments. The Energy Manager will receive a Fuel Purchase Performance Incentive/Disincentive Payment, which will be calculated at the end of each month, with the results reflected in the following month's invoice. The total Fuel Purchase Performance Incentive/Disincentive Payment will not exceed $5.0 million on an annual basis.

Payment. The Energy Manager will submit monthly invoices to LIPA Sub for the Monthly Fuel Management Fee and the Fuel Purchase Performance Incentive/Disincentive Payment by the tenth (10th) Business Day following the month of service, consistent with the provisions in this description of "Fuel Management." Payment of all invoiced amounts will be due and payable by LIPA Sub within fifteen (15) Business Days of LIPA Sub receiving such invoices.

Minimization of Costs. In providing the Fuel, Energy Manager shall use best efforts to minimize Fuel costs for the GENCO Generating Facilities, such efforts being consistent with (i) all applicable insurance policies, (ii) all applicable prudent industry practices and standards, including

Prudent Utility Practice, (iii) all applicable operating and contract constraints for Fuel delivery, (iv) Energy Manager's collective bargaining agreements and (v) Applicable Law.

Off-System Sales

The Agreement provides that the Energy Manager will use best efforts to market to Off-System Sales customers, on LIPA Sub's behalf, Electricity from the System Power Supply that is not otherwise needed by the Electricity Customers in a manner which will reduce the net cost of Electricity provided to the Electricity Customers. The Energy Manager will receive 33 percent of the revenue net of incremental costs from Off-System Sales of Electricity from the System Power Supply and LIPA Sub will receive 67 percent of the revenue net of incremental costs from these Off-System Sales of Electricity from the System Power Supply. The incremental costs for such Off-System Sales will be based upon the incremental cost of energy for such Electricity sales including any other costs or charges (including applicable taxes) incurred to produce and deliver the Electricity and/or Ancillary Services for sale by the Energy Manager. The incremental costs associated with capacity sales will include the cost of replacement capacity incurred as a result of the sale, if any, and any other costs or charges related to the sale, including startup, no-load operation, transmission, and applicable taxes.

Notwithstanding any of the above, the Energy Manager will only attempt to sell excess Electricity to the extent that, in GENCO's judgment, such Electricity sales do not jeopardize any of GENCO's tax-exempt debt and to the extent that, in LIPA Sub's judgment, such Electricity sales do not jeopardize the tax-exempt status of any of LIPA Sub's debt. Each party will furnish the other an appropriately detailed description of the constraints imposed on such sales prior to the Closing Date and will update such description from time to time to reflect any applicable changes in law or regulation.

System Power Supply Management

Lowest Cost Electricity. In connection with the purchase and management of the System Power Supply, on LIPA Sub's behalf, the Energy Manager is obligated to use best efforts to provide the lowest cost Electricity to the T&D System and the Electricity Customers, given (i) the transmission and distribution limitations unique and/or external to the T&D System; (ii) the terms of the Existing Power Supply Agreements; (iii) availability of power through the New York Power Pool or its successor; (iv) regulatory and reliability council requirements, including, but not limited to system safety and reliability; and (v) System Policies and Procedures, including environmental policies contained therein.

Specific Energy Manager Responsibilities. In implementing its System Power Supply responsibilities, the Energy Manager will, subject to the transmission, contractual and reliability constraints referred to in the preceding paragraph:

(i) schedule deliveries of and Dispatch energy from the System Power Supply;

(ii) arrange for LIPA Sub's purchase of Electricity to the extent the System Power Supply is insufficient to meet the requirements of the T&D System;

(iii) continually monitor the market for LIPA Sub's sale and purchase of wholesale Electricity and purchase Electricity, on LIPA Sub's behalf, on the wholesale market to displace System Power Supply if such purchases, including the cost of transmission services to deliver such Electricity, will reduce total power supply costs;

(iv) sell Electricity on LIPA Sub's behalf from the System Power Supply that is surplus to the requirements of the T&D System whenever such sales, including consideration of any incremental cost of Transmission for delivery of such sales, are advantageous to LIPA Sub;

(v) arrange for such additional transmission services and capacity as will be necessary for the purchase or sale of Electricity by LIPA Sub; and

(vi) with the prior written consent of LIPA Sub, subcontract with power marketers or brokers, or similar entities, to assist in the acquisition of Electricity and the marketing and sale of excess Electricity.

All contracts for the purchase or sale of Electricity will be entered into by LIPA Sub or by the Energy Manager as agent for LIPA Sub. The Agreement provides that no contract for the purchase or sale of Electricity for a term in excess of three months will be entered into without the prior written consent of LIPA Sub.

System Power Supply Management Compensation. Except as otherwise provided in the Agreement, the payments LIPA Sub will make to the Energy Manager pursuant to the Agreement with respect to System Power Supply Services other than Off-System Sales will be calculated as set forth in the Agreement and as summarized below. During the Term of the Agreement, LIPA Sub will make monthly payments to the Energy Manager consisting of an amount equal to the sum of: (i) the System Power Supply Management Fee, plus or minus (ii) the System Power Supply Performance Incentive/Disincentive.

System Power Supply Management Fee. The Energy Manager will be paid an annual System Power Supply Management Fee, in consideration for the Energy Manager's performance of the System Power Supply management services contemplated in the Agreement. The amount of such System Power Supply Management Fee includes a fee of $750,000 and an allowance for certain costs which, for 1998, has been established at $868,000. Such allowance for costs will be indexed during the Term of the Agreement in the same manner as the Direct Cost Budget under the Management Services Agreement. LIPA Sub will pay the System Power Supply Management Fee to the Energy Manager in twelve equal monthly installments.

System Power Supply Performance Incentives/Disincentive. The Energy Manager will receive a System Power Supply Performance Incentive/Disincentive, calculated in accordance with the Agreement which will not exceed $2 million on an annual basis.

Payment. The Energy Manager will submit monthly invoices to LIPA Sub for the Monthly System Power Supply Management Fee and the System Power Supply Performance Incentive/Disincentive Payments and Off-System Sales compensation by the tenth (10th) Business Day following the month of service. Such invoices will show separately amounts payable with respect to Off System Sales and System Power Supply Management. Payment of all invoiced amounts will be due and payable by LIPA Sub within fifteen (15) Business Days of LIPA Sub receiving such invoices.

Records; Information

Account Records; Collection of Monies; Availability of Energy Manager

Account Records. The Energy Manager is obligated to maintain such records as LIPA Sub reasonably requests setting forth in accurate and reasonable detail the information relating to the purchase and sale of Fuel and Electricity under the Agreement requested by LIPA Sub.

Collection of Monies. The Energy Manager will use best efforts to collect on a timely basis (1) all amounts due LIPA Sub for Off-System Sales, and (2) any other monies owed to LIPA Sub in connection with System Power Supply and other matters within the purview of the Energy Manager. The Energy Manager will provide current and historical billing information concerning Fuel and System Power Supply to LIPA Sub monthly in such form as reasonably requested by LIPA Sub. All such monies collected by the Energy Manager or any Subcontractor thereto will be the property of LIPA Sub and will be deposited by the Energy Manager daily into such accounts and in the manner as LIPA Sub may from time to time designate. The Energy Manager is unconditionally and absolutely obligated to pay or deposit such moneys as directed by LIPA Sub.

Compliance with Applicable Law. The Energy Manager is obligated to perform all of its obligations under the Agreement in accordance with Applicable Law.

Information. The Agreement requires the Energy Manager to on and after the Closing Date establish and maintain an information system to provide storage and real time retrieval for LIPA Sub review and copying of operating data relating to (i) cost and quantities of Fuel Supply and Power Purchases, (ii) revenues from and quantities of Off-System Sales and (iii) the performance by the Energy Manager of its obligations under the Agreement, including, but not limited to, all information necessary to verify calculations made pursuant to the Agreement.

Books and Records. The Energy Manager will prepare and maintain proper, accurate and complete books, records and accounts regarding Fuel and System Power Supply to the extent necessary (1) to enable LIPA Sub to prepare LIPA Sub's financial statements in accordance with generally accepted accounting principles, (2) to verify data with respect to any operations or transactions in which LIPA Sub has a financial or other material interest under the Agreement, (3) to prepare periodic performance reports and statements relating to purchase of Fuel and System Power Supply, which will be submitted by the Energy Manager to LIPA Sub and (4) to enable LIPA Sub to administer any fuel adjustment clause or similar provision applicable to Electricity sales. The Energy Manager will, upon notice and demand from LIPA Sub, produce for examination and copying by representatives of LIPA Sub, any documents showing all acts and transactions relating to the Agreement, any Subcontract or any transactions in which LIPA Sub has or may have a financial or other material interest under the Agreement, and will produce such operation books and records for examination and copying in connection with the costs for which LIPA Sub may be responsible under the Agreement.

Fiscal Affairs, Accounting and Record Keeping

General. The Energy Manager will maintain possession of equipment, materials and supplies, maps, plans and specifications, and Fuel and System Power Supply billing records during the Term of the Agreement and will duly account to LIPA Sub for such items.

Bank Deposits. All cash held by the Energy Manager for the account of LIPA Sub and all cash collected by the Energy Manager for the account of LIPA Sub after the Closing Date will be deposited on each Business Day in bank accounts in such bank or banks as LIPA Sub may direct and upon such terms and conditions as may be specified by LIPA Sub.

Bill Payments. The Energy Manager will timely pay all bills related to Fuel which are proper and appropriate and which it has authority to pay and will assure that, to the extent within the Energy Manager's control, no liens are filed against any portion of the assets or revenues of LIPA Sub.

Allocation of Risk of Certain Costs and Liabilities

The Agreement contains provisions relating to the allocation of risks and liabilities that are substantially the same as the provisions of the Management Services Agreement described herein under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budgets—Allocation of Risks of Certain Costs and Liabilities."

Term; Events of Default

Term. The Term of the Agreement will commence on the Closing Date and, except as otherwise provided herein, will remain in full force and effect for an initial term of (i) fifteen (15) years from such Closing Date with respect to the Fuel Services and (ii) eight (8) years from such Closing Date with respect to System Power Supply Services.

Events of Default; Procedures for Termination

The Agreement contains provisions relating to Events of Default by the Energy Manager or LIPA Sub and the procedures for termination that are substantially the same as the provisions of the Management Services Agreement that are described herein under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budget—Events of Default by the Manager—Events of Default by LIPA Sub" and "—Procedure for Termination for Cause."

LIPA Sub Emergency Assumption of Fuel and System Power Supply Management Services. Should the Energy Manager, due to Uncontrollable Circumstances or any other reason whatsoever, fail, refuse or be unable to provide any or all Fuel and System Power Supply Services contemplated hereby and LIPA Sub or any Governmental Body finds that such failure endangers or menaces the public health, safety or welfare, then, in any of those events and to the extent of such failure, LIPA Sub will have the right, upon notice to the Energy Manager, during the period of such emergency, to perform the services which the Energy Manager would otherwise be obligated to perform under the Agreement. The Energy Manager agrees that in such event it will fully cooperate with LIPA Sub to effect such a temporary assumption. The Energy Manager agrees that, in such event, LIPA Sub may take and use any or all of the operating assets of the Energy Manager necessary for the above-mentioned purposes without paying the Energy Manager or any other person any additional charges or compensation whatsoever for such possession and use; provided, however, that if such emergency is due to Uncontrollable Circumstances, LIPA Sub will reimburse the Energy Manager for its Cost-Substantiated costs incurred due to such a transfer of the operating assets.

Energy Manager's Reporting Requirements

Monthly Reports. The Energy Manager is obligated to provide LIPA Sub and the Consulting Engineer with monthly reports no later than 20 days after the end of each month, including such data relating to the Fuel Services and System Power Supply Services as may reasonably be requested to be furnished by LIPA Sub.

Annual Reports. The Energy Manager will furnish LIPA Sub and, the Consulting Engineer, within 60 days after the end of each Contract Year, an Annual Settlement Statement together with annual summary of the statistical data provided in the monthly reports, certified by the Energy Manager, as well as such other data relating to the services provided under the Agreement as may be reasonably requested to be furnished by LIPA Sub.

Fuel Consumption Reports. Fifteen (15) Business Days following the end of each month, Energy Manager is obligated to submit to LIPA Sub a report summarizing the Fuel burned during that month and such other information as the parties may mutually agree.

Indemnification

The Agreement contains redemnification provisions that are substantially the same as the indemnification provisions of the Management Services Agreement that are described herein under the caption "Summary of Certain Provisions of the Management Services Agreement—Miscellaneous Provisions—Indemnification."

Miscellaneous Provisions

Insurance. The Agreement provides that Energy Manager shall maintain with financially responsible insurance companies insurance in such amounts and against such risks and losses as are customary for companies engaged in the business of providing services or undertaking activities similar to the Fuel Services and System Power Supply Services to be provided thereunder.

Assignment and Transfer. The Agreement contains provisions relating to assignment and transfer that are substantially the same as the assignment and transfer provisions of the Management Services Agreement that are described herein under the caption "Summary of Certain Provisions of the Management Services Agreement—Miscellaneous Provisions—Assignment and Transfer."

Non-Binding Mediation; Arbitration. The Agreement contains provisions relating to mediation and arbitration that are substantially the same as the mediation and arbitration provisions of the Management Services Agreement that are described herein under the caption "Summary of Certain Provisions of the Management Services Agreement—Compensation and Budget—Non-Binding Mediation; Arbitration."

Affiliate. Pursuant to the Agreement, the Energy Manager has agreed to remain an Affiliate of the Guarantor.

Credit Enhancement in Certain Circumstances. The Agreement contains provisions relating to credit enhancement that are substantially the same as the credit enhancement provisions of the Management Services Agreement that are described herein under the caption "Summary of Certain Provisions of the Management Services Agreement—Miscellaneous Provisions—Credit Enhancement in Certain Circumstances."

Hedging Policies. The Energy Manager agreed not engage in any hedging activities relating to the Fuel Services or System Power Supply Services without express approval from the Boards of Directors of the Energy Manager and its Parent and without notifying and consulting with LIPA Sub at least 60 days prior to implementing such activities. The Agreement provides that in the event that approval for the use of hedging activities is implemented, the incentive/disincentive program will be reexamined by the parties to determine the appropriateness of the inclusion or exclusion of the related costs, gain or losses and appropriate mutually agreeable revisions thereto will be made.

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APPENDIX F

FORM OF
CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Certificate (the "Disclosure Certificate") is executed and delivered by the Long Island Power Authority (the "Issuer") in connection with the issuance of $3,449,527,638.05 Electric System General Revenue Bonds, Series 1998A (the "Bonds"). The Bonds are being issued pursuant to the Electric System General Revenue Bond Resolution adopted by the Issuer on May 13, 1998 as amended and supplemented (the "Resolution"). The Issuer covenants and agrees as follows:

SECTION 1. *Purpose of the Disclosure Certificate.* This Disclosure Certificate is being executed and delivered by the Issuer for the benefit of the Holders and Beneficial Owners of the Bonds and in order to assist the Participating Underwriters in complying with S.E.C. Rule 15c2-12(b)(5).

SECTION 2. *Definitions.* In addition to the definitions set forth in the Resolution, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

"Annual Report" shall mean any Annual Report provided by the Issuer pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

"Beneficial Owner" shall mean any person which has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries).

"Dissemination Agent," if any, shall mean the person or firm, or any successor Dissemination Agent designated in writing by the Issuer pursuant to Section 7 of this Disclosure Certificate and which has filed with the Issuer and the Trustee a written acceptance of such designation.

"Listed Events" shall mean any of the events listed in Section 5(a) of this Disclosure Certificate.

"National Repository" shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule. The National Repositories currently approved by the Securities and Exchange Commission are set forth in Exhibit B.

"Participating Underwriter" shall mean any of the original underwriters of the Bonds required to comply with the Rule in connection with the offering of the Bonds.

"Repository" shall mean each National Repository and the State Repository.

"Rule" shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"State" shall mean the State of New York.

"State Repository" shall mean any public or private repository or entity designated by the State as the state repository for the purpose of the Rule and recognized as such by the Securities and Exchange Commission. As of the date of this Certificate, there is no State Repository.

"Trustee" shall mean United States Trust Company of New York, New York, New York and its successors and assigns.

SECTION 3. *Provision of Annual Reports.*

(a) The Issuer shall, or shall cause the Dissemination Agent to, not later than 6 months after the end of the Issuer's fiscal year (presently December 31), commencing with the report for the 1998 Fiscal Year, provide to each Repository an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Certificate with a copy to the Trustee. The Annual Report may be submitted as a single document or as separate documents comprising a package, and may cross-reference other information as provided in Section 4 of this Disclosure Certificate; provided that the audited financial statements of the Issuer may be submitted separately from the balance of the Annual Report and later than the date required above for the filing of the Annual Report if they are not available by that date. If the Issuer's fiscal year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(c).

(b) Not later than fifteen (15) Business Days prior to said date, the Issuer shall provide the Annual Report to the Dissemination Agent (if other than the Issuer). If the Issuer is unable to provide to the Repositories an Annual Report by the date required in subsection (a), the Issuer shall send a notice to each Repository or the Municipal Securities Rulemaking Board and the State Repository, if any, in substantially the form attached as Exhibit A.

(c) If a Dissemination Agent is appointed by the Issuer, the Dissemination Agent shall:

(i) determine each year prior to the date for providing the Annual Report the name and address of each National Repository and the State Repository, if any; and

(ii) file a report with the Issuer certifying that the Annual Report has been provided pursuant to this Disclosure Certificate, stating the date it was provided and listing all the Repositories to which it was provided.

SECTION 4. *Content of Annual Reports.* The Issuer's Annual Report shall contain or include by reference the following:

1. The audited consolidated financial statements of the Issuer and its subsidiaries for the prior fiscal year, prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board. If the Issuer's audited consolidated financial statements are not available by the time the Annual Report is required to be filed pursuant to Section 3(a), the Annual Report shall contain unaudited consolidated financial statements in a format similar to the financial statements contained in the final Official Statement, and the audited consolidated financial statements shall be filed in the same manner as the Annual Report when they become available.

2. Operating results for the prior fiscal year of the type set forth in the table entitled "Projected Operating Results" in Part 2 of the final Official Statement to the extent line items in the table are not included in the audited consolidated financial statements.

3. Capital expenditures for the prior fiscal year of the type set forth in the final Official Statement under the heading "The System—Capital Improvement Plan" in Part 2 of the final Official Statement.

4. Service area loads for the prior fiscal year of the type set forth in the final Official Statement under the heading "The System—Loads" in Part 2 of the final Official Statement and in Appendix A—"Independent Consultant's Report—System Loads and Resources."

5. The Issuer's own rates and charges (but not regional comparisons) for the prior fiscal year of the type set forth in the final Official Statement under the heading "Rates and Charges" in Part 2 of the final Official Statement and in Appendix A—"Independent Consultant's Report—Utility Rates and Charges."

6. Billings and collections for the prior fiscal year of the type set forth in Part 2 of the final Official Statement under the heading "Billing and Collections."

Any or all of the items listed above may be included by specific reference to other documents, including official statements of debt issues of the Issuer or related public entities, which have been submitted to each of the Repositories or the Securities and Exchange Commission. If the document included by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The Issuer shall clearly identify each such other document so included by reference.

SECTION 5. *Reporting of Significant Events.*

(a) Pursuant to the provisions of this Section 5, the Issuer shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

1. principal and interest payment delinquencies.
2. non-payment related defaults.
3. modifications to rights of Bondholders.
4. optional, contingent or unscheduled bond calls.
5. defeasances.
6. rating changes.
7. adverse tax opinions or events affecting the tax-exempt status of the Bonds.
8. unscheduled draws on the debt service reserves reflecting financial difficulties.
9. unscheduled draws on the credit enhancements reflecting financial difficulties.
10. substitution of the credit or liquidity providers or their failure to perform.
11. release, substitution or sale of property securing repayment of the Bonds.

(b) Whenever the Issuer obtains knowledge of the occurrence of a Listed Event, the Issuer shall as soon as possible determine if such event would be material under applicable federal securities laws.

(c) If the Issuer determines in its sole discretion that knowledge of the occurrence of a Listed Event would be material and would require disclosure under applicable federal securities laws, the Issuer shall promptly file a notice of such occurrence with the Repositories or the Municipal Securities Rulemaking Board and the State Repository with a copy to the Trustee. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(4) and (5) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to Holders of affected Bonds pursuant to the Resolution.

SECTION 6. *Termination of Reporting Obligation.* The Issuer's obligations under this Disclosure Certificate shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the Issuer shall give notice of such termination in the same manner as for a Listed Event under Section 5(c).

SECTION 7. *Dissemination Agent.* The Issuer may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Certificate, and may discharge any such Agent, with or without appointing a successor Dissemination Agent. The Dissemination Agent shall not be responsible in any manner for the content of any notice or report

prepared by the Issuer pursuant to this Disclosure Certificate. Initially, the Issuer will serve as its own dissemination agent.

SECTION 8. *Amendment; Waiver.* Notwithstanding any other provision of this Disclosure Certificate, the Issuer may amend this Disclosure Certificate, and any provision of this Disclosure Certificate may be waived, provided that the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Sections 3(a), 4, or 5(a), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Holders of the Bonds in the same manner as provided in the Resolution for amendments to the Resolution with the consent of Holders, or (ii) does not, in the opinion of the Trustee or nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Bonds.

In the event of any amendment or waiver of a provision of this Disclosure Certificate, the Issuer shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the Issuer. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (i) notice of such change shall be given in the same manner as for a Listed Event under Section 5(c), and (ii) the Annual Report for the year in which the change is made should present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

SECTION 9. *Additional Information.* Nothing in this Disclosure Certificate shall be deemed to prevent the Issuer from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Certificate. If the Issuer chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the Issuer shall have no obligation under this Certificate to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

SECTION 10. *Default.* In the event of a failure of the Issuer to comply with any provision of this Disclosure Certificate the Trustee may (and, at the request of any Participating Underwriter or the Holders of at least 50% aggregate principal amount of Outstanding Bonds, shall), or any Holder or Beneficial Owner of the Bonds may (unless the Issuer has so complied within 20 days after written notice from the Trustee of its failure to comply) take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the Issuer to comply with its obligations under this Disclosure Certificate. A default under this Disclosure Certificate shall not be deemed a default or an Event of Default under the Resolution, and the sole remedy under this Disclosure Certificate in the event of any failure of the Issuer to comply with this Disclosure Certificate shall be an action to compel performance.

SECTION 11. *Duties, Immunities and Liabilities of Dissemination Agent.* The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Certificate, and the Issuer agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, expense and liabilities which it may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's default or negligence or willful misconduct. The obligations of the Issuer under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds.

SECTION 12. *Beneficiaries.* This Disclosure Certificate shall inure solely to the benefit of the Issuer, the Trustee, the Dissemination Agent, the Participating Underwriters and Holders and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity.

Date: May 28, 1998

LONG ISLAND POWER AUTHORITY

By _____

EXHIBIT A

NOTICE TO REPOSITORIES OF FAILURE TO FILE ANNUAL REPORT

Name of Issuer: Long Island Power Authority

Name of Bond Issue: Long Island Power Authority Electric System General Revenue Bonds, Series 1998A

Date of Issuance: May 28, 1998

NOTICE IS HEREBY GIVEN that the Issuer has not provided an Annual Report with respect to the above-named Bonds as required by Section 3 of the Continuing Disclosure Certificate dated May 28, 1998 of the Issuer. The Issuer anticipates that the Annual Report will be filed by .

Dated: _____

LONG ISLAND POWER AUTHORITY

By _____

cc: Trustee

EXHIBIT B

NATIONAL REPOSITORIES

As of the date of this Continuing Disclosure Certificate, the following National Repositories are recognized by the Securities and Exchange Commission:

Bloomberg Municipal Repository
P.O. Box 840
Princeton, NJ 08542-0840
(609) 279-3200/(609) 279-3204 to order documents
(609) 279-5962 or (609) 279-5963 [FAX]
Internet address: MUNIS@bloomberg.com
Contact: Lena Panich

JJ Kenny Information Services
The Repository
65 Broadway, 16th Floor
New York, NY 10006
(212) 770-4568
(212) 797-7994 [FAX]
e-mail address: joan__horai@mcgrawhill.com
Contact: Ms. Joan Horai, Repository

Thomson NRMSIR
Secondary Market Disclosure
395 Hudson Street, 3rd Floor
New York, NY 10014
(212) 807-5001
(212) 989-2078 [FAX]
Contact: Carolyn Chin
e-mail address: Disclosure@muller.com

DPC Data, Inc.
One Executive Drive
Fort Lee, NJ 07024
(201) 346-0701
(201) 947-0107 [FAX]
Contact: NRMSIR
Internet address: nrmsir@dpcdata.com

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APPENDIX G

SUMMARY OF THE LIPA/LILCO MERGER AGREEMENT

The following is a brief summary of the salient terms of the Agreement and Plan of Merger. This summary does not purport to be complete or definitive and is qualified in its entirety by reference to the Agreement and Plan of Merger, a copy of which is on file with the Trustee. Certain capitalized terms used in this Appendix G may not have the same definitions as such terms have elsewhere in this Official Statement

General

As of June 26, 1997, BL Holding Corp., a corporation to be formed as a New York corporation ("BL"), LILCO, LIPA and LIPA Acquisition Corp., a corporation to be formed as a New York Corporation and wholly owned subsidiary of LIPA ("LIPA Sub") entered into the Agreement and Plan of Merger (the "Merger Agreement"). The Merger Agreement established the terms and conditions of the merger of LIPA Sub with and into LILCO (the "Merger"), with LILCO as the surviving corporation (sometimes hereinafter referred to as the "Surviving Corporation") retaining only those assets relating to its electric transmission and distribution system. Following the Merger, the Surviving Corporation, renamed the *Long Island Power Authority Inc.*, will be a wholly owned subsidiary of LIPA.

Related Transactions

General. The Merger Agreement requires that certain transactions (the "Related Transactions") take place prior to the consummation of the Merger (the "Closing"), including: (i) the formation of LIPA Sub, (ii) the formation of BL, (iii) the formation of certain subsidiaries of BL (the "Transferee Subsidiaries"), (iv) the transfer of certain assets currently held by LILCO relating to its gas, non-nuclear generation operations and common plant (the "Transferred Assets") to the Transferee Subsidiaries and (v) subject to certain conditions, the assumption by BL of certain debt of LILCO, including LILCO's outstanding 7.30% Debentures due July 15, 1999 and LILCO's outstanding 8.20% Debentures due March 15, 2023. The Merger together with the Related Transactions is sometimes hereinafter referred to as the "LIPA Transaction".

Transferred Assets. Generally, the Transferred Assets will consist of all assets currently owned and employed by LILCO in the conduct of its gas distribution business and its non-nuclear electric generation business, and all common assets used by LILCO in the operation and management of its electric transmission and distribution business and its gas distribution business and/or its non-nuclear electric generation business. LILCO will transfer the Transferred Assets to the Transferee Subsidiaries in exchange for: (x) up to $75 million face amount of newly issues preferred stock of BL ("New BL Preferred Stock"), and (y) the number of shares of the common stock of BL ("BL Common Stock") which represent the net fair market value of the Transferred Assets, less the face amount of the New BL Preferred Stock (the number of shares is referred to as the "Designated Number"). Prior to the Closing, LILCO will sell the New BL Preferred Stock for cash in a private placement to one or more purchasers which are not otherwise shareholders of LILCO or KeySpan.

Retained Assets. Generally, the assets retained by the Surviving Corporation (the "Retained Assets") will consist of all assets currently owned and employed by LILCO in the conduct of its electric transmission and distribution business.

Related Agreements. In addition to the Merger Agreement, LIPA and LILCO have entered into the following agreements (the "Related Agreements") in connection with the LIPA Transaction:

Operating Agreements. LIPA and LILCO have entered into (i) a power supply agreement, under which one or more of the Transferee Subsidiaries will provide electric capacity and energy to LIPA from the generating plants that are among the Transferred Assets, (ii) an energy management agreement, under which one or more of the Transferee Subsidiaries will provide energy management services to purchase fuel and electric capacity and energy, and manage the scheduling and sale of electric capacity and energy on behalf of LIPA and (iii) a management services agreement, under which one or more to the Transferee Subsidiaries will provide certain management services on behalf of LIPA with respect to the operation of the electric transmission and distribution system to be retained by LILCO and acquired by LIPA as part of the LIPA Transaction (collectively, the "Operating Agreements"). Prior to the Closing, (x) LILCO will assign all of its rights and obligations under the Operating Agreements to the applicable Transferee Subsidiaries, and (y) LIPA will assign all of its rights and obligations under the Operating Agreements to LIPA Sub, thereby transferring such rights and obligations to the Surviving Corporation pursuant to the Merger.

Guaranty Agreement. The Transferee Subsidiaries' obligations under the Operating Agreements will be guaranteed by BL under a guaranty agreement which will be executed by BL prior to the Closing.

Generation Purchase Right Agreement. LIPA and LILCO have entered into a generation purchase right agreement (the "Generation Purchase Right Agreement"), under which LIPA will, subject to certain conditions, have the right to purchase the Transferee Subsidiary which will hold all of LILCO's current non-nuclear generation assets. Prior to the Closing, LILCO will assign all of its rights and obligations under the Generation Purchase Right Agreement to BL.

Liabilities Undertakings. On the Closing Date, BL and each Transferee Subsidiary will execute and deliver to LIPA and the Surviving Corporation a liabilities undertaking and indemnification agreement pursuant to which BL and each Transferee Subsidiary shall jointly and severally undertake and assume certain liabilities and obligation set forth therein. On the Closing Date, LIPA and the Surviving Corporation will execute and deliver to BL and each Transferee Subsidiary a liabilities undertaking and indemnification agreement pursuant to which LIPA and the Surviving Corporation shall jointly and severally undertake and assume certain liabilities and obligation set forth therein.

The Merger

General. Pursuant to the Merger Agreement and upon the satisfaction or waiver of certain conditions set forth therein: (i) LIPA will pay an aggregate cash merger consideration of $2,497,500,000 (the "Cash Merger Consideration"), and (ii) LIPA Sub will be merged with and into LILCO, which, as the Surviving Corporation, will become a wholly owned subsidiary of LIPA.

Treatment of Shares. On the Closing Date and by virtue of the Merger, the shares of capital stock of LILCO will be treated as follows:

- *Treasury Shares.* Each share of LILCO Common Stock and LILCO Preferred Stock held in treasury (the "Canceled Shares") will be canceled and retired without payment of any consideration.
- *Common Stock.* Each issued and outstanding share of LILCO Common Stock, other than Canceled Shares and shares held by dissenting shareholders, will be canceled and converted

into the right to receive (a) an amount in cash equal to the Cash Merger Consideration divided by the number of outstanding shares of LILCO Common Stock and (b) a pro rata distribution of the BL Common Stock received by LILCO in exchange for the Transferred Assets. Each holder of shares of LILCO Common Stock will be deemed to have appointed an exchange agent as its agent (the "Exchange Agent"): (x) to receive the pro rata distribution of the BL Common Stock received by LILCO in exchange for the Transferred Assets, (y) to receive the cash otherwise due such holder and (z) to use such cash to subscribe for additional shares of BL Common Stock. The total number of shares of BL Common Stock distributable to holders of LILCO Common Stock in respect of each share of LILCO Common Stock will include the number of distributable shares of BL Common Stock received by LILCO in exchange for the Transferred Assets and distributed by LILCO to the Exchange Agent, as well as the number of shares distributable from the purchase by the Exchange Agent of additional shares of BL Common Stock with the Cash Merger Consideration and, in the aggregate, will equal:

(i) 0.880 shares of BL Common Stock for each share of LILCO Common Stock (other than the dissenting shares) if the LILCO/KeySpan Combination is consummated concurrently with the LIPA Transaction, or

(ii) one share of BL Common Stock for each share of LILCO Common Stock (other than the dissenting shares) if the LILCO/KeySpan Combination is not consummated concurrently with the LIPA Transaction.

If the LILCO/KeySpan Combination has been consummated prior to the Closing of the LIPA Transaction, then:

(i) no shares of BL Common Stock or New BL Preferred Stock will be delivered in exchange for the Transferred Assets, and BL and/or one or more of its subsidiaries, as the holders of all then outstanding LILCO Common Stock, will receive all of the Cash Merger Consideration, and

(ii) an additional 0.077 shares of BL Common Stock will be distributed to the record holders of LILCO Common Stock as of the effective time of the LILCO/KeySpan Combination (pursuant to which 0.803 shares of BL Common Stock will be distributed) in respect of each share of LILCO Common Stock.

- ***Series AA Preferred Stock.*** Each issued and outstanding share of Series AA Preferred Stock of LILCO, other than Canceled Shares and shares of such preferred stock held by any dissenting shareholder, will be canceled and converted into the right to receive one fully paid and non-assessable share of BL Preferred Stock with identical rights (including dividend rates) and designations to the LILCO Series AA Preferred Stock.

- ***Redeemable Preferred Stock.*** Each issued and outstanding share of LILCO Preferred Stock that is subject to optional redemption by LILCO at or before the Closing Date (the "Redeemable Preferred Stock"), other than Canceled Shares, will be redeemed for cash by LILCO not later than the Closing Date in accordance with the terms applicable to such shares.

- ***Non-Redeemable Preferred Stock.*** Each issued and outstanding share of LILCO Preferred Stock, other than Canceled Shares, dissenting Preferred Shares, shares of Series AA Preferred Stock and Redeemable Preferred Stock (collectively, the "Non-redeemable Preferred Stock"), will be canceled and converted into the right to receive cash in the amount of the sum of (x) the Make-Whole Amount and (y) accrued but unpaid dividends in respect of such shares through

the Closing Date. As used herein, "Make-Whole Amount" with respect to such shares of Non-Redeemable Preferred Stock means an amount equal to the present value of:

(i) the face or liquidation preference amount of such share, and

(ii) the remaining dividend payments due on such share between the Closing Date and the applicable redemption date computed using a discount rate equal to the applicable Fair Market Rate divided by 0.95.

"Fair Market Rate" is defined as the Generic General Obligation Fair Market Yield for Baa rated Low/Medium Coupon General Municipal Obligations at the time of the computation as reported on Bloomberg, with a maturity most nearly equal to the period between cancellation and final redemption of such series of Non-Redeemable Preferred Stock. The period between cancellation and redemption refers to the period between the Closing Date and: (a) August 1, 2002, with respect to the Series CC Preferred Stock; (b) March 1, 1999, with respect to the Series GG Preferred Stock; (c) May 1, 2001, with respect to the Series QQ Preferred Stock; and (d) October 16, 2018, with respect to the Series UU Preferred Stock. The amount by which the aggregate amount payable exceeds 100% of the aggregate face or liquidation preference amounts for all shares of Non-Redeemable Preferred Stock shall be paid by BL to the Surviving Corporation promptly after the Closing Date.

Cash Merger Consideration; Retained Debt. The Cash Merger Consideration is based upon the assumptions that the net book value of the Retained Assets will equal $2,500,800,000 on the Closing Date and that the total long term indebtedness of LILCO on the Closing Date will not exceed $3,576,000,000 (the "Retained Debt Amount"). The Retained Debt Amount will be adjusted base upon LILCO's net book value, as reflected on LILCO's audited consolidated balance sheet as of such date, as follows. The Retained Debt Amount will be either:

(i) increased by the amount, if any, by which the net book value of the Retained Assets exceeds $2,500,800,000; or

(ii) decreased by the amount, if any, by which the net book value of the Retained Assets is less than $2,500,800,000.

As of the Closing Date, BL will, and will cause each of the Transferee Subsidiaries to, execute and deliver promissory notes (the "Promissory Notes") on the following terms:

(i) The aggregate principal amount will be equal to the excess, if any, of the indebtedness of LILCO outstanding on such date over the Retained Debt Amount.

(ii) The rates and maturities will correspond to each portion of such excess debt on such date; provided, however, that the interest and principal payment dates will be adjusted to require payment by BL thirty (30) days prior to the corresponding payment dates on the underlying debt.

Representation and Warranties

Each of the parties to the Merger Agreement has made such representations and warranties as are customary and desirable in transactions such as the LIPA Transaction.

Covenants

Each of the parties to the Merger Agreement has agreed to take such actions prior to the Closing Date as are customary and desirable in transactions such as the LIPA Transaction.

Conditions to Closing

The LIPA Transaction is subject to certain conditions, including the following:

No Injunction. No temporary restraining order or preliminary or permanent injunction or other order by any federal or state court preventing the consummation of any of the transactions contemplated by the Merger Agreement or any of the Related Agreements shall be in effect.

Regulatory Approvals. All necessary regulatory approvals shall have been obtained.

Tax Rulings. Favorable private letter rulings shall have been received from the Internal Revenue Service with respect to the application of Sections 337(d), 103 and 115 of the Code.

Financing. LIPA shall have obtained financing in an amount sufficient to acquire the LILCO Common Stock and Non-Redeemable Preferred Stock and redeem the LILCO Redeemable Preferred Stock, and the bonds issued to obtain such financing shall have received ratings pursuant to rating applications which contemplate the issuance of up to $7.3 billion for such purposes and for the purpose of refinancing Surviving Corporation debt.

Representations and Warranties. The representations and warranties of each of BL, LILCO, LIPA and LIPA Sub set forth in the Merger Agreement and the Related Agreements shall be true and correct as of the date of such agreements and as of the Closing Date, except for failures of such representations and warranties to be true and correct, individually or in the aggregate , which would not be reasonably likely to result in a material adverse effect. Such representations and warranties do not survive the Merger.

Performance of Obligations. Each of BL, LILCO, LIPA and LIPA Sub shall have performed in all material respects its agreements and covenants contained in the Merger Agreement and the Related Agreements required to be performed by it at or prior to the Closing Date.

Third Party Consents. BL and LILCO shall have obtained all necessary third party consents to the LIPA Transaction, other than those consents the failure of which to obtain would not have a Material Adverse Effect.

Termination

The Merger Agreement may be terminated prior to the Closing Date as follows:

- by mutual written consent of the parties;
- by either LIPA or LILCO if the Closing shall not have occurred on or prior to August 31, 1998 (the "Initial Termination Date"); provided, however, that the Initial Termination Date shall be extended to April 28, 1999 if on the Initial Termination Date those conditions to the Closing relating to regulatory approvals, tax rulings or third party consents shall not have been fulfilled, but all other conditions shall either have been fulfilled or be capable of being fulfilled;
- by LILCO if its Board of Directors determines in good faith that their fiduciary obligations require that they agree to a merger, sale of a material portion of LILCO's assets or other business combination proposed by a third party;
- by LIPA if (i) LILCO has breached any of its representations, and such breach is reasonably likely to result in a Material adverse Effect, or any of its agreements under the Merger

Agreement or any of the Related Agreements in any material respect, and any such breaches have not been remedied within 20 days of receipt of notice thereof, or (ii) LILCO's Board of Directors withdraws its approval of the LIPA Transaction;

- by LILCO if (i) LIPA has breached any of its representations, and such breach is reasonably likely to result in a material adverse effect, or any of its agreements under the Merger Agreement or any of the Related Agreements in any material respect, and any such breaches have not been remedied within 20 days of receipt of notice thereof, or (ii) LIPA's Board of Trustees withdraws its approval of the LIPA Transaction;
- by either party if any of the conditions to Closing cannot be satisfied.

APPENDIX H

BOOK-ENTRY-ONLY SYSTEM

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934, as amended. DTC holds securities that its participants ("DTC Participants") deposit with DTC. DTC also facilitates the settlement among DTC Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in DTC Participants' accounts, thereby eliminating the need for physical movement of securities certificates. Direct DTC Participants include securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations ("Direct DTC Participants"). DTC is owned by a number of its Direct DTC Participants and by the New York Stock Exchange Inc., the American Stock Exchange, Inc., and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as securities brokers and dealers, banks, and trust companies that clear through or maintain a custodial relationship with a Direct DTC Participant, either directly or indirectly ("Indirect DTC Participants"). The rules applicable to DTC and its DTC Participants are on file with the Securities and Exchange Commission.

Purchases of Offered Securities under the DTC system must be made by or through Direct DTC Participants, which will receive a credit for the Offered Securities on DTC's records. The ownership interest of each actual purchaser of Offered Securities ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect DTC Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect DTC Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in Offered Securities are to be accomplished by entries made on the books of DTC Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Offered Securities, except as specifically provided in the Resolution in the event that use of the book-entry system for a series of Offered Securities is discontinued.

To facilitate subsequent transfers, all the series of Offered Securities are registered in the name of DTC's partnership nominee, Cede & Co. The deposit of a series of Offered Securities with DTC and their registration in the name of Cede & Co. effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of Offered Securities; DTC's records reflect only the identity of the Direct DTC Participants to whose accounts Offered Securities are credited, which may or may not be the Beneficial Owners. The DTC Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct DTC Participants, by Direct DTC Participants to Indirect DTC Participants, and by Direct DTC Participants and Indirect DTC Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

BENEFICIAL OWNERS SHOULD MAKE APPROPRIATE ARRANGEMENTS WITH THEIR BROKER OR DEALER TO RECEIVE NOTICES (INCLUDING NOTICES OF REDEMPTION) AND OTHER INFORMATION REGARDING OFFERED SECURITIES THAT MAY BE SO CONVEYED TO DIRECT DTC PARTICIPANTS AND INDIRECT DTC PARTICIPANTS.

Redemption notices will be sent to Cede & Co. If less than all of a maturity of Offered Securities are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct DTC Participant in such maturity to be redeemed.

Neither DTC nor Cede & Co. will consent or vote with respect to Offered Securities. Under its usual procedures, DTC mails an Omnibus Proxy to LIPA as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct DTC Participants to whose accounts Offered Securities are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Except as described below, neither DTC nor Cede & Co. will take any action to enforce covenants with respect to any security registered in the name of Cede & Co. Under its current procedures, on the written instructions of a Direct DTC Participant, DTC will cause Cede & Co. to sign a demand to exercise bondholder rights as record holder of the quantity of securities specified in the Direct DTC Participant's instructions, and not as record holder of all the securities of that issue registered in the name of Cede & Co. Also, in accordance with DTC's current procedures, all factual representations to be made by Cede & Co. to LIPA, the Trustee or any other party must be made to DTC and Cede & Co. by the Direct DTC Participant in its instructions to DTC.

For so long as Offered Securities are issued in book-entry form through the facilities of DTC, any Beneficial Owner desiring to cause LIPA or the Trustee to comply with any of its obligations with respect to Offered Securities must make arrangements with the Direct DTC Participant or Indirect DTC Participant through whom such Beneficial Owner's ownership interest in Offered Securities is recorded in order for the Direct DTC Participant in whose DTC account such ownership interest is recorded to make the instructions to DTC described above.

NEITHER LIPA NOR THE TRUSTEE NOR ANY UNDERWRITER (OTHER THAN IN ITS CAPACITY, IF ANY, AS DIRECT DTC PARTICIPANTS OR INDIRECT DTC PARTICIPANTS) WILL HAVE ANY OBLIGATION TO THE DIRECT DTC PARTICIPANTS OR THE INDIRECT DTC PARTICIPANTS OR THE PERSONS FOR WHOM THEY ACT AS NOMINEES WITH RESPECT TO DTC'S PROCEDURES OR ANY PROCEDURES OR ARRANGEMENTS BETWEEN DIRECT DTC PARTICIPANTS, INDIRECT DTC PARTICIPANTS AND THE PERSONS FOR WHOM THEY ACT RELATING TO THE MAKING OF ANY DEMAND BY CEDE & CO. AS THE REGISTERED OWNER OF OFFERED SECURITIES, THE ADHERENCE TO SUCH PROCEDURES OR ARRANGEMENTS OR THE EFFECTIVENESS OF ANY ACTION TAKEN PURSUANT TO SUCH PROCEDURES OR ARRANGEMENTS.

Principal and interest payments on Offered Securities will be made to DTC. DTC's practice is to credit Direct DTC Participants' accounts on a payment date in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on such date. Payments by DTC Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such DTC Participant and not of DTC, the Trustee, or LIPA, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to DTC is the responsibility of LIPA or the Trustee, disbursement of such payments to Direct DTC Participants shall be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners shall be the responsibility of Direct and Indirect DTC Participants.

THE ABOVE INFORMATION CONCERNING DTC AND DTC'S BOOK-ENTRY SYSTEM HAS BEEN OBTAINED FROM SOURCES THAT LIPA BELIEVES TO BE RELIABLE, BUT LIPA TAKES NO RESPONSIBILITY FOR THE ACCURACY THEREOF. NEITHER LIPA NOR THE TRUSTEE WILL HAVE ANY RESPONSIBILITY OR OBLIGATION TO DTC PARTICIPANTS, BENEFICIAL OWNERS OR OTHER NOMINEES OF SUCH BENEFICIAL OWNERS FOR (1) SENDING TRANSACTION STATEMENTS; (2) MAINTAINING, SUPERVISING OR REVIEWING, OR THE ACCURACY OF, ANY RECORDS MAINTAINED BY DTC OR ANY DTC PARTICIPANT OR OTHER NOMINEES OF SUCH BENEFICIAL OWNERS; (3) PAYMENT OR THE TIMELINESS OF PAYMENT BY DTC TO ANY DTC PARTICIPANT, OR BY ANY DTC PARTICIPANT OR OTHER NOMINEES OF BENEFICIAL OWNERS TO ANY BENEFICIAL OWNER, OF ANY AMOUNT DUE IN RESPECT OF THE PRINCIPAL OF OR REDEMPTION PREMIUM, IF ANY, OR INTEREST ON OFFERED SECURITIES; (4) DELIVERY OR TIMELY DELIVERY BY DTC TO ANY DTC PARTICIPANT, OR BY ANY DTC PARTICIPANT OR OTHER NOMINEES OF BENEFICIAL OWNERS TO ANY BENEFICIAL OWNERS, OF ANY NOTICE (INCLUDING NOTICE OF REDEMPTION) OR OTHER COMMUNICATION WHICH IS REQUIRED OR PERMITTED UNDER THE TERMS OF THE RESOLUTION TO BE GIVEN TO HOLDERS OR OWNERS OF OFFERED SECURITIES; (5) THE SELECTION OF THE BENEFICIAL OWNERS TO RECEIVE PAYMENT IN THE EVENT OF ANY PARTIAL REDEMPTION OF OFFERED SECURITIES; OR (6) ANY ACTION TAKEN BY DTC OR ITS NOMINEE AS THE REGISTERED OWNER OF OFFERED SECURITIES.

So long as Cede & Co. is the registered owner of Offered Securities, as nominee for DTC, references in this Official Statement to the Bondholders, holders or registered owners of Offered Securities (other than under the caption "Tax Matters" herein) shall mean Cede & Co., as aforesaid, and shall not mean the Beneficial Owners of Offered Securities.

When reference is made to any action which is required or permitted to be taken by the Beneficial Owners, such reference shall only relate to those permitted to act (by statute, regulation or otherwise) on behalf of such Beneficial Owners for such purposes. When notices are given, they shall be sent by LIPA or the Trustee to DTC only.

As long as the book-entry system is used for Offered Securities, the Trustee and LIPA will give any notice of redemption or any other notices required to be given to Owners of Offered Securities only to DTC. Any failure of DTC to advise any Direct DTC Participant, or of any Direct DTC Participant to notify any Indirect DTC Participant, or of any Direct DTC Participant or Indirect DTC Participant to notify any Beneficial Owner, of any such notice and its content or effect will not affect the validity of the redemption of Offered Securities called for redemption or of any other action premised on such notice. Conveyance of notices and other communications by DTC to Direct DTC Participants, by Direct DTC Participants to Indirect DTC Participants and by Direct DTC Participants and Indirect DTC Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial owners may desire to make arrangements with a Direct DTC Participant or Indirect DTC Participant so that all notices of redemption or other communications to DTC which affect such Beneficial Owners will be forwarded in writing by such Direct DTC Participant or Indirect DTC Participant.

NEITHER LIPA NOR THE TRUSTEE WILL HAVE ANY RESPONSIBILITY OR OBLIGATION TO SUCH DIRECT DTC PARTICIPANTS, OR THE PERSONS FOR WHOM THEY ACT AS NOMINEES, WITH RESPECT TO THE PAYMENTS TO OR THE PROVIDING

OF NOTICE FOR THE DIRECT DTC PARTICIPANTS, THE INDIRECT DTC PARTICIPANTS, OR THE BENEFICIAL OWNERS OF OFFERED SECURITIES.

For every transfer and exchange of a beneficial ownership interest in Offered Securities, the Beneficial Owner may be charged a sum sufficient to cover any tax, fee or other governmental charge, that may be imposed in relation thereto.

DTC may discontinue providing its services as securities depository with respect to Offered Securities at any time by giving reasonable notice to LIPA or the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, certificates for the Offered Securities are required to be printed and delivered.

LIPA may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, certificates for the Offered Securities will be printed and delivered.

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