

# Long Island Power Authority Report to the Finance and Audit Committee

Audit plan and strategy for the year ending December 31, 2020

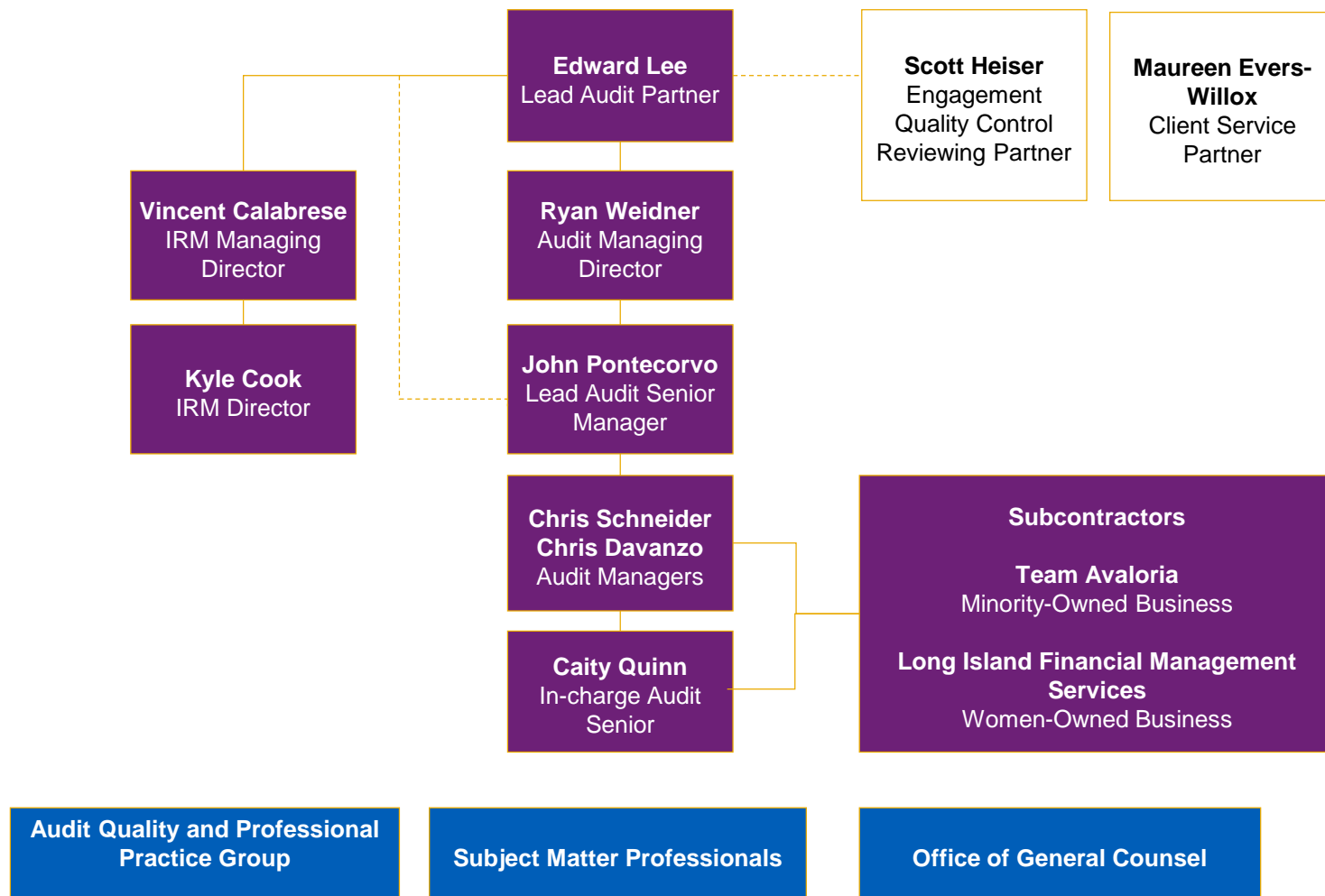
September 23, 2020





# Client service team

Team members with continuity are designated in purple.





# New team members



**Maureen Evers-Willox**

Client Service Partner

631-425-6005

[mevers@kpmg.com](mailto:mevers@kpmg.com)

Maureen is an audit and independence partner, and currently the managing partner for KPMG LLP's Long Island office. She is responsible for the strategic direction and growth for the office's audit, advisory and tax services.

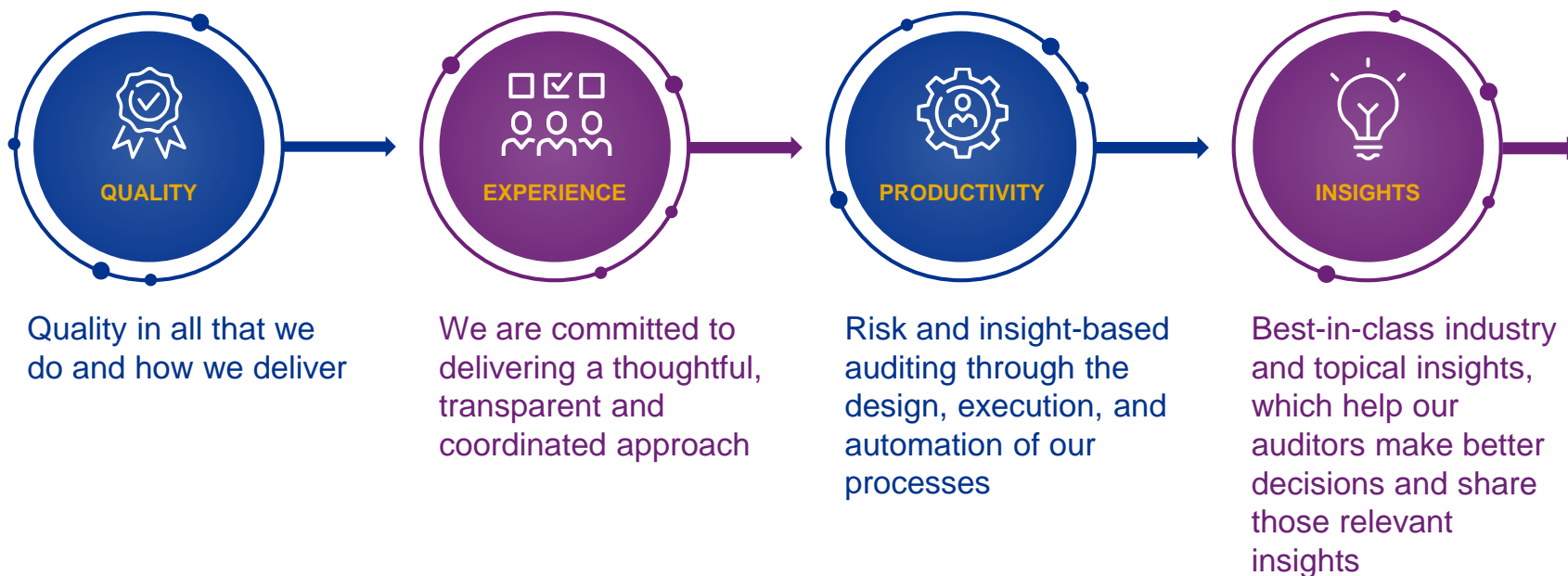
During her 26 years with the firm, Maureen has worked as an audit professional and in the firm's Independence Group. Prior to her current role, she led the firm's Personal Independence activities where she established policies on auditor independence, developed independence training, and responded to technical inquiries and regulators on independence matters.

Maureen previously worked in the firm's New York Financial Services audit practice, serving SEC audit clients in real estate, banking and asset management with SEC filings, PCAOB audits, and large global audit coordination. In addition, she spent two years on an international assignment in Germany, where she worked on a US GAAP conversion project for a large multinational bank.



# Our commitment to you

We aim to deliver an exceptional client experience by focusing on





# Executive summary

## 2020 AUDIT PLAN





# COVID-19: Resilience & Readiness

COVID-19 is truly a unique and demanding challenge with severe human consequences. We place the highest priority on the health of our people and yours, and continue to take action based on guidance from public health authorities.

## Key Insights For Your Organization

- Our team is producing insights and providing perspectives on actions we can all take to respond with resilience.
- Our [Audit Committee Institute](#) and [Board Leadership Center](#) is producing insights on oversight of companies' pandemic response.
- Our [COVID-19 resource center](#) also covers topics such as financial reporting, global economic impacts, financial management, contingency planning and business continuity, and more.



## Business Continuity Excellence

- Our business continuity plan is working effectively and we have taken steps to prepare for future, potentially longer-term, alternative work arrangements.
- We are coordinating with your teams to best work together and communicating frequently to keep each other informed.
- Our Heads Up Thinking culture vision is helping to shape the way the firm responds to challenges like this to the benefit of our clients.

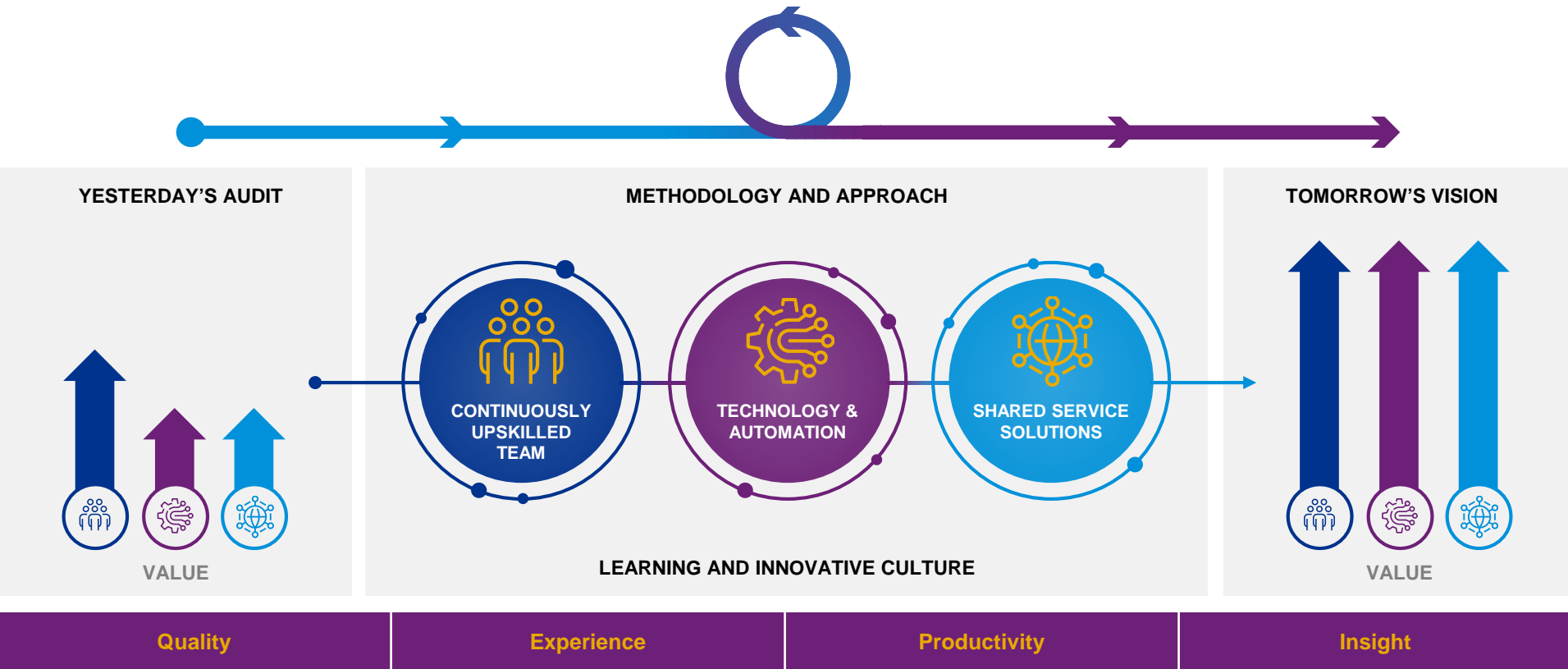


COVID-19 is a major consideration in the development of our audit plan in 2020. We are focused on understanding the impact of COVID-19 to your business, and coordinating and adjusting our audit plan as appropriate.



# Our vision for modernizing the audit

A multi-year journey aligned with yours





# Digitizing our audit platform

Our Next Generation Audit Platform, KPMG Clara, integrates our methodology to digitize and simplify our audit, improve risk assessment, and tailor our responses to risk. It is a cloud-based platform in which we will seamlessly deliver a data-and insights-rich experience to our people and your organization.

## Methodology

Audits are evolving. Our updated methodology is driving greater consistency across all of our audits and reinforcing alignment with auditing standards.

We deploy an innovative, comprehensive risk assessment that will drive the rest of the audit.

These changes:

- Simplify our approach,
- Improve our risk identification and assessment, and
- Focus our audit response on that risk.

We've also taken the next step, integrating this workflow into our digital platform.

## Aligned

We will build a tailored audit strategy that applies both of our investments in people, data and technology. KPMG Clara's agility allows us to adapt our approach to your unique business.

## Coordinated

KPMG Clara becomes a single transparent place for you to interact with us throughout the audit, monitor its status, and access audit insights.

## Digitized

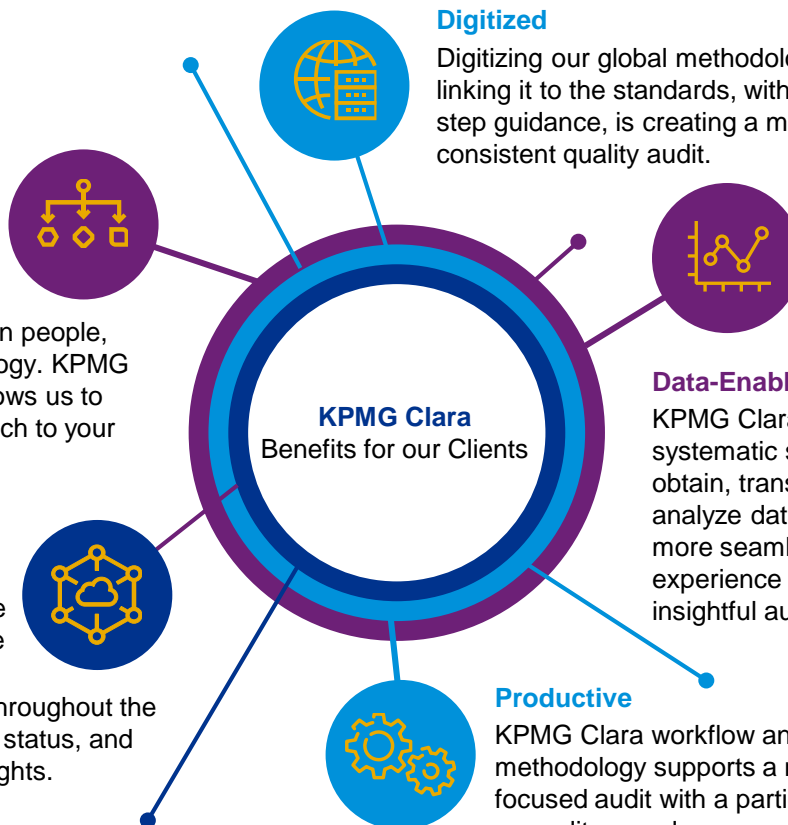
Digitizing our global methodology, directly linking it to the standards, with step-by-step guidance, is creating a more consistent quality audit.

## Data-Enabled

KPMG Clara will bring systematic solutions to obtain, transform and analyze data, creating a more seamless experience and insightful audit.

## Productive

KPMG Clara workflow and our new methodology supports a more focused audit with a particular focus on audit procedures.





# Team-led efforts to modernize the audit in 2020

## Innovation Sparks

Team-led efforts to modernize audit experience

- **CONTINUOUS IMPROVEMENT FOCUS** pertaining to a refreshed analysis at our risk assessment process, audit planning and walkthrough execution, project management, and PBC requests. The real value comes with transparency and accountability on both sides.
- **MICROSOFT POWER BI** will enable further understanding of data sets with interactive visualizations and influence the nature, timing, and extent of substantive testing downstream.
- **NEW CLIENT SERVICE PARTNER** will bring another seasoned leader to C-suite to deliver fresh insights, facilitate innovation, and communicate challenges and decisions.





# FY 2020 audit fees

## Fee Discussion

Fees for the FY 2020 audit will be billed according to the Cost Proposal dated May 15, 2019, and amended June 23, 2019.

### LIPA Financial Statements

- Independent Auditors' Report
- Report on Internal Control over Financial Reporting and Compliance on Other Matters
- Investment Guidelines Compliance Report
- Debt Compliance Report
- Agreed Upon Procedures Report related to the Rate Covenant Calculation and Amounts Held in the Rate Stabilization Fund
- Required Communications to the Finance and Audit Committee
- Management letter, if necessary

### UDSA Financial Statements

- Independent Auditors' Report
- Report on Internal Control over Financial Reporting and Compliance on Other Matters
- Investment Guidelines Compliance Report
- Agreed Upon Procedures related to the UDSA's Restructuring Property Servicing Agreements (5 reports)
- Required Communications to the Board of Trustees
- Management letter, if necessary

### 2020 Fees for above deliverables

**\$ 804,000\***

The following reports will be billed separately:

- Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance in Accordance with Uniform Guidance (formerly OMB Circular A-133)
- Series 2020 General Revenue Bond Issuance Consent Letter, as needed

\* The fees noted above do not include the additional effort that will be required in connection with the adoption of certain significant accounting pronouncements, such as GASB 87, and the additional effort which will be required in connection with LIPA's implementation of the Microsoft Dynamics enterprise resource planning system. Once management has completed its initial assessment of these items and confirmed the timeline for adoption and implementation, we will estimate the impact to our fees.



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# Required Finance and Audit Committee Communications

Presented on: September 23, 2020



# Scope of audit

**Our audit of the consolidated financial statements of LIPA, and its subsidiaries (UDSA) as of and for the year ended December 31, 2020, will be performed in accordance with auditing standards generally accepted in the United States of America.**

**Performing an audit of the consolidated financial statements includes consideration of internal control over financial reporting (ICFR) as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's ICFR.**

**Our Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance in Accordance with Uniform Guidance, will be performed in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance).**



# Materiality in the context of an audit

**We will apply materiality in the context of the preparation and fair presentation of the consolidated financial statements, considering the following factors:**

Misstatements, including omissions, are considered to be material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

Judgments about materiality are made in light of surrounding circumstances and are affected by the size or nature of a misstatement, or a combination of both.

Judgments about materiality involve both qualitative and quantitative considerations.

Judgments about matters that are material to users of the consolidated financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.

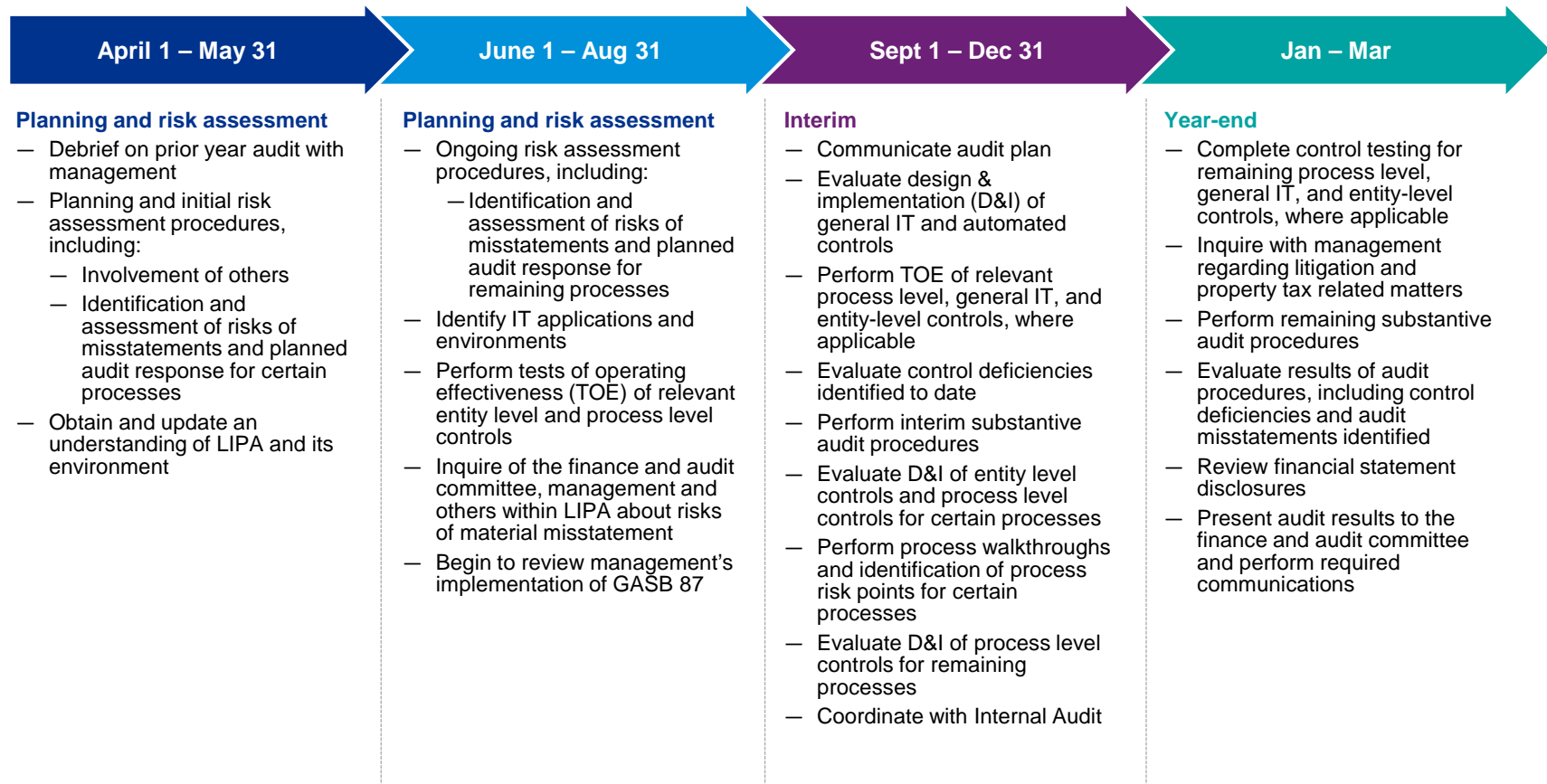
Determining materiality is a matter of professional judgment and is affected by the auditor's perception of the financial information needs of users of the consolidated financial statements.

Judgments about the size of misstatements that will be considered material provide a basis for

- a) Determining the nature and extent of risk assessment procedures;
- b) Identifying and assessing the risks of material misstatement; and
- c) Determining the nature, timing, and extent of further audit procedures.



# Our timeline



**Filing date (Before March 31, 2021): Issue audit reports on financial statements.**



# Risk assessment: Significant risks

## Significant Risks

**Management override of controls**

Management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent consolidated financial statements by overriding controls that otherwise appear to be operating effectively. Although the level of risk of management override of controls will vary from entity to entity, the risk nevertheless is present in all entities.

Susceptibility to:	
Error	Fraud
	Yes



# Risk assessment: Estimates and other significant audit areas

Audit areas	Relevant factors affecting our risk assessment
<i>Estimates – Valuation of Commodity Derivatives and Financial Derivatives</i>	<ul style="list-style-type: none"> <li>• Size and composition of the accounts</li> <li>• Nature of account and disclosure</li> <li>• Measurement uncertainty (future cash flow estimates)</li> </ul>
<i>Estimates – PSEG Pension and postretirement obligations</i>	<ul style="list-style-type: none"> <li>• Size and composition of the accounts</li> <li>• Nature of account and disclosure</li> <li>• Measurement uncertainty (assumptions utilized)</li> </ul>
<i>Estimates – Leases (in connection with adoption of GASB 87)</i>	<ul style="list-style-type: none"> <li>• Size and composition of the accounts</li> <li>• Nature of account and disclosure</li> <li>• Adoption of new accounting standard (GASB 87)</li> <li>• Measurement uncertainty (assumptions utilized)</li> </ul>



# Risk assessment: Estimates and other significant audit areas (continued)

Audit areas	Relevant factors affecting our risk assessment
<i>Significant Audit Area - Revenue recognition</i>	<ul style="list-style-type: none"> <li>• Size and composition of the account</li> <li>• Volume of activity processed through the account</li> <li>• Nature of the account and disclosure</li> </ul>
<i>Significant Audit Area - Long term debt</i>	<ul style="list-style-type: none"> <li>• Size and composition of the account</li> <li>• Issuance of Debt Compliance Report</li> </ul>
<i>Significant Audit Area - Investments</i>	<ul style="list-style-type: none"> <li>• Size and composition of the account</li> <li>• Issuance of Investment Compliance Report</li> </ul>
<i>Significant Audit Area - Utility plant and property and equipment, including depreciation</i>	<ul style="list-style-type: none"> <li>• Size and composition of the account</li> <li>• Volume of activity processed through the account</li> <li>• Nature of the account and disclosure</li> </ul>
<i>Significant Audit Area – Unbilled revenue</i>	<ul style="list-style-type: none"> <li>• Size and composition of the account</li> <li>• Nature of the account and disclosure</li> </ul>
<i>Significant Audit Area – Regulatory assets and liabilities</i>	<ul style="list-style-type: none"> <li>• Size and composition of the account</li> <li>• Nature of the account and disclosure</li> </ul>



# Involvement of others

Subject Matter Professionals	Extent of planned involvement
Internal Audit	Inquiries of Internal Audit, Collaboration on Walkthrough Process, Review Internal Audit Plan, and Review results of Internal Audits performed
KPMG Risk Analytics Valuation Specialists	Testing the valuation of Financial and Commodity Derivative Instrument selections
KPMG National Pricing Desk	Testing the valuation of Investment selections
KPMG Actuarial Specialists	Testing the valuation of the PSEG OPEB and Pension liability
KPMG Information Risk Management – IT	Understanding the IT environment, and testing the system implementation of Microsoft Dynamics
KPMG Tax	Review the entity's financial statements to determine tax-exempt status is appropriate
KPMG Forensics	Assist in brainstorming sessions related to fraud risks and fraud risk factors



# Accounting pronouncements

## **GASB Statement No. 95, *Postponement of the Effective Dates of Certain Authoritative Guidance***

The primary objective of this Statement is to provide temporary relief to governments and other stakeholders in light of the COVID-19 pandemic. That objective is accomplished by postponing the effective dates of certain provisions in Statements and Implementation Guides that first became effective or are scheduled to become effective for periods beginning after June 15, 2018, and later.

## **GASB Statement No. 87, *Leases***

This Statement addresses the recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a model for lease accounting based on the principle that leases are financings of the right to use an underlying asset.

Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities.

LIPA plans to early adopt this Statement in 2020.



# Shared responsibilities: Independence

Auditor independence is a shared responsibility and most effective when management, the finance and audit committee and audit firms work together in considering compliance with the independence rules. In order for KPMG to fulfill its professional responsibility to maintain and monitor independence, management, the finance and audit committee, and KPMG each play an important role.

## System of independence quality control

The firm maintains a system of quality control over compliance with independence rules and firm policies. Timely information regarding upcoming transactions or other business changes is necessary to effectively maintain the firm's independence in relation to:

- New affiliates (which may include subsidiaries, equity method investees/investments, sister companies, and other entities that meet the definition of an affiliate under AICPA independence rules)

## Certain relationships with KPMG

Independence rules prohibit:

- Certain employment relationships involving directors, officers, or others in an accounting or financial reporting oversight role and KPMG and KPMG covered persons.
- LIPA or its directors, officers, from having certain types of business relationships with KPMG or KPMG professionals.



# Responsibilities

## Management responsibilities



- Communicating matters of governance interest to those charged with governance.
- The audit of the consolidated financial statements does not relieve management or those charged with governance of their responsibilities.

## KPMG responsibilities – Objectives



- Communicating clearly with those charged with governance the responsibilities of the auditor regarding the financial statement audit and an overview of the planned scope and timing of the audit.
- Obtaining from those charged with governance information relevant to the audit.
- Providing those charged with governance with timely observations arising from the audit that are significant and relevant to their responsibility to oversee the financial reporting process.
- Promoting effective two-way communication between the auditor and those charged with governance.
- Communicating effectively with management and third parties.

## KPMG responsibilities – Other



- If we conclude that no reasonable justification for a change of the terms of the audit engagement exists and we are not permitted by management to continue the original audit engagement, we should:
  - Withdraw from the audit engagement when possible under applicable law or regulation,
  - Communicate the circumstances to those charged with governance, and
  - Determine whether any obligation, either legal contractual, or otherwise, exists to report the circumstances to other parties, such as owners, or regulators.
- Forming and expressing an opinion about whether the consolidated financial statements that have been prepared by management, with the oversight of those charged with governance, are prepared, in all material respects, in accordance with the applicable financial reporting framework.
- Establishing the overall audit strategy and the audit plan, including the nature, timing, and extent of procedures necessary to obtain sufficient appropriate audit evidence.
- Communicating any procedures performed relating to other information, and the results of those procedures.



# Inquiries

## The following inquiries are in accordance with AU-C 260

### Is the finance and audit committee aware of:

- Matters relevant to the audit, including, but not limited to, violations or possible violations of laws or regulations?
- Any significant communications with regulators?
- Any developments in financial reporting, laws, accounting standards, corporate governance, and other related matters, and the effect of such developments on, for example, the overall presentation, structure, and content of the consolidated financial statements, including the following:
  - The relevance, reliability, comparability, and understandability of the information presented in the consolidated financial statements?
  - Whether all required information has been included in the consolidated financial statements, and whether such information has been appropriately classified, aggregated or disaggregated, and presented?

### Does the finance and audit committee have knowledge of:

- Fraud, alleged fraud, or suspected fraud affecting LIPA, including misconduct or unethical behavior related to financial reporting or misappropriation of assets?
  - If so, have the instances been appropriately addressed and how have they been addressed?

### Additional inquiries:

- What are the finance and audit committee's views about fraud risks in LIPA?
- Who is the appropriate person (finance and audit committee chair or full committee) for communication of audit matters during the audit?
- How are responsibilities allocated between management and the finance and audit committee?
- What are LIPA's objectives and strategies and related business risks that may result in material misstatements?
- Are there any areas that warrant particular attention during the audit and additional procedures to be undertaken?
- What are the finance and audit committee's attitudes, awareness, and actions concerning (a) LIPA's internal controls and their importance in the entity, including oversight of effectiveness of internal controls, and (b) detection of or possibility of fraud?
- Have there been any actions taken based on previous communications with the auditor?
- Has LIPA entered into any significant unusual transactions?
- Whether the entity is in compliance with other laws and regulations that have a material effect on the consolidated financial statements?
- What are the other document(s) that comprise the annual report, and what is the planned manner and timing of issuance of such documents?

# Questions?

For additional information and audit committee resources, including National Audit Committee Peer Exchange series, a Quarterly webcast, and suggested publications, visit KPMG's Audit Committee Institute (ACI) at [www.kpmg.com/ACI](http://www.kpmg.com/ACI)

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