

FOR CONSIDERATION

May 19, 2021

TO: The Board of Trustees

FROM: Thomas Falcone

SUBJECT: Consideration of the Adoption of Certain Implementation Plans Relating to Affiliate Services

Requested Action

The Board of Trustees (the “Board”) of the Long Island Power Authority (“LIPA”) is requested to adopt a resolution, attached hereto as Exhibit “A”, adopting certain Project Implementation Plans for the use of affiliate services to provide Shared Services, as defined in the Amended and Restated Operations Services Agreement (“OSA”) by and between LIPA and PSEG Long Island, in accordance with recommendations that were adopted by the Board on March 29, 2021.

Background

The use of PSEG subsidiaries as “affiliates” is permitted under the terms of the OSA. LIPA has a Pass-Through Expenditure obligation pursuant to Section 5.2(A)(7) of the OSA for certain costs incurred by the Service Provider in connection with the use of other PSEG subsidiaries, commonly referred to as “affiliate” costs. Further, pursuant to Section 4.4(16), Rights and Responsibilities of LIPA, of the OSA, LIPA, in part, has the right to “make recommendations to the Service Provider, in each case as may be reasonably necessary or appropriate to perform LIPA’s oversight responsibilities and obligations with respect to the provision of Operations Services under this Agreement and as may otherwise be necessary or appropriate to comply with LIPA’s legal, contractual and fiduciary obligations. . .”

The services that PSEG Long Island typically uses affiliates to perform include: Information Technology (“IT”) system support, IT project support, Human Resources, Procurement, Treasury, and Legal Services.

However, the current procedures relating to the use of affiliates do not provide LIPA with sufficient detail to accurately determine whether the use of such affiliates is the most economic approach and in the best interest of LIPA’s customers. LIPA reimbursed PSEG Long Island a total of \$23 million for affiliate related services in 2020. Of this, \$17 million, or 75 percent of the total affiliate costs are allocated based on a formula that assigns Long Island a percentage of aggregated “pooled” costs. As a result, LIPA has little accounting detail on the majority of the affiliate costs. Lastly, affiliate costs typically come with a premium due to facility, support, and administrative overhead costs being added to direct labor costs. A “fully-loaded” affiliate cost is typically higher than the cost of PSEG Long Island in-house personnel.

Board Recommendations to PSEG Long Island

To address these issues, the Board adopted the following recommendations on March 29, 2021:

1. Enhanced Affiliate Budget Transparency

a. Cost Benefit Justification

- PSEG Long Island should prepare cost and benefit justifications for affiliate use as part of the 2022 annual budget development process. Include in the cost justification an alternative analysis comparing the cost and benefit of providing the service through an affiliate as compared to the same service using PSEG Long Island in-house employees or by a third-party vendor. The analysis should reference the assumed ServCo employee costs, contracted rates, or proposals from vendors to perform similar work.
- For affiliate services identified that would be less costly if provided by ServCo employees or a vendor, PSEG Long Island should identify the steps it will take to secure these savings for Long Island electric customers.

b. Transactional Cost Allocation

- PSEG Long Island should minimize the use of transactional cost allocation. For service areas that use a transactional cost allocation methodology, LIPA expects these areas to shift to a direct, or “Professional” cost allocation methodology as a way to provide for increased accountability and transparency. Where a direct cost allocation is not feasible, PSEG Long Island must provide a justification as to why it is necessary to continue to utilize a transactional method. Further, this should include a review of the basis of the allocation percentage to ensure that Long Island customers are not subsidizing New Jersey services. The detailed transactional cost information should delineate labor costs and hours by title and the use of contractors and their associated roles.

c. IT Services

- Over 25 percent of total affiliate charges are associated with IT Customer Support and IT Client Project Support. Therefore, the budget plan needs to document the specific projects the affiliate will be working on in the upcoming year, the estimated affiliate cost by project, as well as the affiliate role in supporting the project.

d. Activity/Billing Hourly Rates

- The budget submission must include supporting documentation reflecting the calculation of the Activity/Billing Hourly Rates. This should include itemizing titles and their average salaries that comprise the Activity/Billing Rate as well as include any data and formulas that reflects any adjustments to or weighting of average salaries in the calculation of the Activity/Billing Rate. The calculation should ensure rates are an accurate representation of labor costs incurred and are not disproportionately impacted by inclusion of high salary positions in a particular Activity/Billing Rate. Positions with salaries outside a reasonable range from the average should be moved to a separate activity type.

e. Submission Due Date

- The affiliate cost and justification must be furnished to LIPA for review no later than August 15, 2021.

2. Enhanced Affiliate Actual Cost Transparency

a. Budget Variance Report

- PSEG Long Island must provide LIPA with a quarterly affiliate report, detailing actual use of affiliates as compared to budget including variance explanations that are grounded in the budget details provided to LIPA pursuant to Recommendation 1.

b. Full-time Affiliate Positions

- As part of the quarterly Budget Variance Report, detailed support must be provided for positions utilized to support PSEG Long Island at a level equivalent to one full-time equivalent. The ServCo model anticipates a workforce dedicated to supporting PSEG Long Island at a full-time level to be a PSEG Long Island employee. An explanation should accompany this analysis that confirms the employee's transition to PSEG Long Island or a justification as to why this is not possible and why the particular PSEG employee is used to support PSEG Long Island on a full-time basis.

3. Former ServCo Employees

- a. LIPA requires PSEG Long Island immediately request approval for hiring former ServCo positions by its affiliates, pursuant to its contractual obligations. The request for approval must include the work the position will perform, why it is necessary or beneficial to LIPA for the affiliate to hire the person, and how PSEG Long Island will ensure that any affiliate charges to PSEG Long Island for the position will not exceed what LIPA would have paid had the positions remained with ServCo. The request will also include an estimate of time dedicated to PSEG Long Island as an affiliate.

On April 16, 2021, PSEG Long Island submitted to LIPA Staff three proposed Project Implementation Plans to address the recommendations listed above. LIPA subsequently engaged PSEG Long Island in a discussion on the plans. As a result, PSEG Long Island resubmitted a proposed Project Implementation Plan for Recommendation 1 on May 7, 2021. LIPA has not accepted the PSEG Long Island proposed plans for Recommendations 1 and 2, which reflect a longer implementation schedule and higher thresholds for variance reporting than originally envisioned by LIPA, among other concerns. LIPA has identified these concerns to PSEG Long Island.

LIPA Staff recommends the Board adopt the Implementation Plan for Recommendation 3 attached hereto as **Exhibit "B"**. The Implementation Plan for Recommendation 3 states that PSEG Long Island will obtain approval from LIPA for four positions hired from ServCo by a PSEG Long Island affiliate. For clarity, LIPA requests this information for all such hires from ServCo by PSEG Long Island affiliates, per the OSA, which to LIPA's knowledge is approximately thirty positions. The Implementation Plans for recommendations 1 and 2 shall be resubmitted by PSEG Long Island for LIPA Staff review no later than no later than June 1, 2021 for consideration by the Board at its June meeting.

Recommendation

Based upon the foregoing, I recommend approval of the above requested action by adoption of a resolution in the form attached hereto.

Attachments

Exhibit "A" Resolution

Exhibit A

RESOLUTION ADOPTING CERTAIN IMPLEMENTATION PLANS RELATING TO AFFILIATE SERVICES

WHEREAS, pursuant to Section 4.4(16), Rights and Responsibilities of LIPA, of the Amended and Restated Operations Services Agreement (“OSA”), LIPA, in part, has the right to “make recommendations to the Service Provider, in each case as may be reasonably necessary or appropriate to perform LIPA’s oversight responsibilities and obligations with respect to the provision of Operations Services under this Agreement and as may otherwise be necessary or appropriate to comply with LIPA’s legal, contractual and fiduciary obligations. . .”; and

WHEREAS, the use of PSE&G subsidiaries as “Affiliates” is permitted under the terms of the OSA; and

WHEREAS, the services that PSEG Long Island typically uses Affiliates to perform include IT system support, IT project support, Human Resources, Procurement, Treasury, and Legal Services. Affiliate costs are charged to PSEG Long Island, and therefore funded by LIPA; and

WHEREAS, LIPA reimbursed PSEG Long Island a total of \$23 million for all Affiliate related services in 2020, including IT system and project support, support for the processing of Tropical Storm Isaias food and medicine spoilage claim processing as well as for handling overflow customer calls and other support during Tropical Storm Isaias; and

WHEREAS, the Board adopted the Affiliate Services Recommendations on March 29, 2021; and

WHEREAS, LIPA has developed these recommendations to incorporate into the budget development process a thorough cost justification review of Affiliate work plans and costs; and

WHEREAS, on April 16, 2021 and on May 7, 2021, PSEG Long Island submitted to LIPA Staff the proposed Implementation Plans.

NOW, THEREFORE, BE IT RESOLVED, the Board hereby adopts the Implementation Plan relating to the Affiliate Services attached hereto as **Exhibit “B”** as amended to address all such hires from ServCo; and

BE IT FURTHER RESOLVED, BE IT FURTHER RESOLVED, the Board hereby directs PSEG Long Island to resubmit the remaining Implementation Plans to address the comments provided by LIPA Staff; and

BE IT FURTHER RESOLVED, that the Board directs LIPA Staff, together with PSEG Long Island, to report to the Board on the completion of the Affiliate Services Implementation Plans no less than quarterly until they are completed.

Dated: May 19, 2021

PSEG Long Island

Project Implementation Plan

for

Improved Affiliate Oversight

Recommendation No. 3

**Project Title: Former ServCo
Employees**

Table of Contents

1. Project Definition	1
1.1. Project Purpose, Objectives, and Success Criteria.....	1
2. Project Deliverables:.....	2
2.1. Assumptions, Dependencies, and Constraints	2
3. Project Structure.....	2
3.1. Internal Project Organization.....	2
3.2. Other Stakeholders.....	3
4. Project Plan	3
4.1. Project Work Plan.....	3
4.2. Risk Management Plan	3
4.3. Issue Resolution Plan.....	3
4.4. LIPA Reporting Plan.....	4
5. Technical Execution Plan.....	4
5.1. Technical Approach.....	4
5.2. Quality Assurance Plan.....	4
5.3. Documentation Plan.....	4

1. Project Definition

While the vast majority of services provided for LIPA are provided by PSEG Long Island's workforce or contractors directly, in certain circumstances, functions and/or services required under the OSA are more efficient and/or cost effective to be performed by PSEG Service Corporation. Examples include certain back-office functions, such as IT or Employee Benefits, where standing up a group directly on Long Island would not be as cost-effective as the expertise and economies of scale of leveraging those services provided to a broader organization. For context, our total O&M and Capital Budget in 2020 was \$1.4 billion, of which \$16 million or ~1% was from our affiliates. Over half that amount was for IT services and, together with HR, represented almost 80% of the total. All such charges are billed on a cost basis (i.e., no profit or mark-up). As noted in separate communications, regardless of which entity is providing the service – PSEG Long Island employees, third party contractors, or our affiliate, PSEG Long Island's President and COO has the ultimate authority for the delivery of service to LIPA and our customers. For those services provided by our affiliate, PSEG Service Corporation charges PSEG Long Island on a monthly basis. These charges are commonly known or referred to as "affiliate" costs. Affiliate costs are typically charged under two main categories:

- Hourly Charges:
 - These are actual hours charged by PSEG Service Corporation employees for time spent supporting PSEG Long Island functions and services. These hours are multiplied by Billing Rates derived by PSEG Service Corporation which include salary costs and applicable overhead support costs
- Transactional Charges:
 - Transactional affiliate charges are derived from an allocation of PSEG Services Corporation pooled costs based on a cost driver metric percentage

This project is to document the process for obtaining LIPA approval prior to the hiring of any ServCo employees.

1.1. Project Purpose, Objectives, and Success Criteria

Purpose:

This project is to document the process for obtaining LIPA approval prior to the hiring of any ServCo employees.

Scope:

This project is to document the process for obtaining LIPA approval prior to the hiring of any ServCo employees. The request for approval will include the following information:

- Work the position will perform
- Justification/Benefit for hiring of ServCo employee
- How PSEG Long Island will ensure they do not incur additional costs as a result of such hiring
- Estimate of time to be dedicated to PSEG Long Island as an affiliate

Project End State and Success Criteria:

The project end state is to have a process to obtain LIPA approval prior to the hiring of any ServCo employees.

2. Project Deliverables:

Describe applicable Project Deliverables:

Deliverable	Delivery Date	Comments
Obtain approval from LIPA for identified four active affiliate positions that were originally ServCo employees. Request for approval to include: <ul style="list-style-type: none"> • Work the position will perform • Justification/Benefit for hiring of ServCo employee • How PSEG Long Island will ensure they do not incur additional costs as a result of such hiring • Estimate of time to be dedicated to PSEG Long Island as an affiliate 	5/15/21	N/A
Obtain approval from LIPA prior to a PSEG entity hiring an employee out of PSEG Long Island ServCo. Request for approval to include: <ul style="list-style-type: none"> • Work the position will perform • Justification/Benefit for hiring of ServCo employee • How PSEG Long Island will ensure they do not incur additional costs as a result of such hiring • Estimate of time to be dedicated to PSEG Long Island as an affiliate 	Prior to any offer to any employee	N/A

2.1. Assumptions, Dependencies, and Constraints

N/A

3. Project Structure

3.1. Internal Project Organization

Internal Project Organization

Group/Individual	Role/Responsibility
PSEG Long Island HR Team	<ul style="list-style-type: none"> • Obtain approval from LIPA prior to a PSEG entity hiring an employee out of PSEG Long

	Island ServCo. Request for approval to include: <ul style="list-style-type: none"> • Work the position will perform • Justification/Benefit for hiring of ServCo employee • How PSEG Long Island will ensure they do not incur additional costs as a result of such hiring • Estimate of time to be dedicated to PSEG Long Island as an affiliate
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3.2. Other Stakeholders

- PSEG Long Island Senior Leadership
- LIPA Senior Leadership
- LIPA Board of Trustees

4. Project Plan

4.1. Project Work Plan

Task	Target Date
Obtain approval from LIPA for identified four active affiliate positions that were originally ServCo employees. Request for approval to include: <ul style="list-style-type: none"> • Work the position will perform • Justification/Benefit for hiring of ServCo employee • How PSEG Long Island will ensure they do not incur additional costs as a result of such hiring • Estimate of time to be dedicated to PSEG Long Island as an affiliate 	5/15/21
Obtain approval from LIPA prior to a PSEG entity hiring an employee out of PSEG Long Island ServCo. Request for approval to include: <ul style="list-style-type: none"> • Work the position will perform • Justification/Benefit for hiring of ServCo employee • How PSEG Long Island will ensure they do not incur additional costs as a result of such hiring • Estimate of time to be dedicated to PSEG Long Island as an affiliate 	As Needed <i>(Prior to any offer to any employee)</i>

4.2. Risk Management Plan

This section is not applicable for this implementation plan.

4.3. Issue Resolution Plan

This section is not applicable for this implementation plan.

4.4. LIPA Reporting Plan

PSEG Long Island will begin obtaining approvals for all future ServCo employee hires.

5. Technical Execution Plan

5.1. Technical Approach

There are no technical approaches required beyond the steps outlined in the above project plan.

5.2. Quality Assurance Plan

There is no quality assurance plan required for this project plan.

5.3. Documentation Plan

Throughout the project the implementation team will document and deliver the key deliverables as listed above in Section 2. The due date of each deliverable will be based off the Project Schedule as outlined in Section 4.1.

Revision History

Name	Date	Reason for Changes	Version
R. Tinelli	XX	initial draft	1.0 draft 1