

Dear Stakeholder:

The Long Island Power Authority (the “Authority”) is pleased to provide this letter report highlighting the Authority’s significant projects, operational activities and accomplishments for 2014, including the following:

- Successful transition to and oversight of the Authority’s new service provider, PSEG Long Island, through whom many of the projects and operational activities were carried out;
- Reliable delivery of electric service to our 1.1 million customers in Nassau and Suffolk counties and the Rockaway peninsula in Queens at stable delivery rates;
- Strategic infrastructure investment to improve system resiliency and customer satisfaction, achieved in part by the signing of agreements for over \$1.4 billion in federal storm recovery and hardening grants;
- Refinancing of a portion of the Authority’s outstanding debt at significantly lower interest rates, made possible through diligent stewardship of the Authority’s bond ratings and continued progress on plans to securitize portions of the Authority’s debt;
- On-boarding and engagement of a new board of trustees, development of a new Authority management team with significant utility IQ, and streamlining of the Authority’s staff;
- Establishment of a constructive dialogue with the newly formed Long Island Office of the Department of Public Service (“DPS”);
- Development of a comprehensive emergency response plan, which was submitted for DPS review, and installation of a new computerized outage management system;
- Solicitation and development of additional renewable generation sources to diversify our energy portfolio;
- Implementation of the LIPA Reform Act by developing a rate plan for 2016-2018 that will enable the Authority to provide service at the lowest rates consistent with safe and reliable service;
- Development of a revenue decoupling mechanism to mitigate revenue losses resulting from proposed increased investment in demand-side management and end-use energy efficiency as well as sales-related variability from weather and other factors; and
- Active participation in NYISO and in statewide policy development including Reforming the Energy Vision and discussions with transmission owners regarding joint investments in transmission.

Over the past 15 years, the Authority’s investments in the transmission and distribution system have resulted in the Authority being among the most reliable electric utilities in New York State based on three major indices:

- System Average Interruption Duration Index (SAIDI), which measures total time the average customer experiences power outages in a year;
- System Average Interruption Frequency Index (SAIFI), which measures number of times the average customer was interrupted during the year; and,
- Customer Average Interruption Duration Index (CAIDI), which measures, on average, how long it took to restore power to customers interrupted during the year.

The Authority has achieved this level of reliability while managing its finances in a responsible and sustainable manner and heeding the call for rate stability. In 2014, the Authority achieved its goal of freezing delivery rates at existing levels for the second year in a row while nonetheless providing operating and capital spending to allow PSEG Long Island to carry out its responsibilities. In order to reduce its long-term financing costs, the Authority refinanced significant portions of its debt during 2014, making use of continued access to tax-free debt and exemption from Federal and State income taxes, which together with other advantages of our municipal status save customers over \$400 million per year.

The Authority's status as a municipal public power authority enables access to Federal grants for mitigation of the costs of storm restoration after severe weather events. During 2014, the Authority concluded negotiations for the attainment of grant funding to cover 90% of the cost of a \$730 million storm hardening program for the electric grid that will dramatically improve system resiliency. The Authority also finalized agreements for \$35 million per year in State grants for energy efficiency.

The Authority undertook significant preparations in 2014 for the filing of its three-year rate plan, which was filed in January 2015, as provided for in the LIPA Reform Act. The rate plan proposes modest increases in delivery rates of approximately 2% per year, which will result in an average delivery rate increase of only 1% per year as a percent of the overall customer bill over the period 2013-2018, which is well below the prevailing rate of inflation. At the same time, the proposed rate plan will allow for investments that improve performance in key areas like customer satisfaction, reliability and storm recovery, deployment of additional renewable resources that continue the transition to a power system based on clean, distributed resources, and greater responsiveness to public concerns.

In concert with its investments in storm hardening, the Authority, together with PSEG Long Island, developed updated emergency response implementation procedures and finalized the protocol for post flood actions to towns and villages. These procedures have been submitted to DPS for their review. The Authority also oversaw deployment by PSEG Long Island of a new computerized outage management system.

The 2014 year saw a continuation of the Authority's commitment to a comprehensive energy plan that ensures that we will be able to meet our customers' energy needs using a diverse mix of energy resources and efficiency measures that are reliably, economically, and environmentally sustainable. Adding to the recent successes of the Authority's

expanded Clean Solar feed-in tariff initiative, the Authority made continued progress with its competitive procurement of new, on-island, renewable capacity to come on line by 2018. Specifically, the Authority selected proposals submitted by 11 solar energy producers for negotiation of power purchase agreements representing a total of 122 megawatts of installed capacity. In addition, PSEG Long Island has begun plans to procure an additional 160 megawatts of renewable resources during 2015. Two developments in 2014 enhanced the nuclear energy segment in the Authority's portfolio. In April 2014, operation of the Nine Mile Point 2 nuclear plant (of which the Authority owns 18%) was transferred to Exelon Corporation with the promise of improved management and operating cost savings. Also, in December 2014, the Authority extended for another three years its long-standing purchase of energy from the Fitzpatrick nuclear plant in upstate New York. With regard to its fossil-fueled generation portfolio, the Authority deferred decisions adding or replacing such plants (including the proposed Caithness II combined-cycle plant and the proposal to repower the E.F. Barrett plant in Island Park) until these and other power supply matters can be examined comprehensively by PSEG Long Island in its 2015 Integrated Resource Plan.

The Authority also devoted substantial time and energy in 2014 to shaping policy solutions to the challenges that are expected to confront the utility industry in future years. For example, in 2014, the Authority developed a change to its tariff to introduce a revenue decoupling mechanism, which will allow for greater flexibility in the development of energy efficiency programs while preserving the Authority's ability to recover its budgeted revenues, consistent with the policy goals of the New York Public Service Commission ("PSC"). Pursuant to the State Administrative Procedures Act, a notice of proposed rulemaking regarding the tariff change was filed in December, 2014, the change was approved by the Board of Trustees in March 2015, and will become effective on April 1, 2015. In addition, the Authority is actively monitoring and participating in the PSC's Reforming the Energy Vision ("REV") proceeding, in order to make the voices of the Authority and its customers heard as the PSC seeks to effect changes in the electricity marketplace through the introduction of business and regulatory strategies that incentivize behind-the-meter innovation. In the same vein, the Authority received and continues to address implementation of the Utility 2.0 Long Range Plan prepared by PSEG Long Island, which is intended to accomplish many of the same goals as REV, including improving the transmission & distribution system's long run flexibility, service and value to customers, by, among other things, promoting cost-effective reductions in peak load through increased energy efficiency and distributed energy resources.

The Authority continues to be an active member of NYISO and the Northeast Power Coordinating Council and to work with other New York transmission owners to influence state policy regarding transmission investment and development. In 2014, this work included engaging with other transmission owners regarding the possible formation of a joint enterprise among the New York transmission owners to develop transmission projects that would provide benefits across the state ("New York Transco"). While the New York Transco was ultimately formed in 2014, it did not include the Authority or the New York Power Authority, either of whose participation requires state legislation, which was not enacted in 2014. However, the Authority continues to address related

issues, including proposals by other transmission owners to charge Long Island consumers for the cost of off-Island transmission projects; and continues to ensure that the Authority's customers are adequately represented in statewide transmission policy discussions.

On Long Island, the Authority's service provider PSEG Long Island was engaged in constructing a number of transmission projects in 2014, including:

- Installation of a new 34 kV line connecting the East Hampton and Amagansett substations. This new circuit supports reliability of service to the east end of the island.
- Installation of a new 69 kV line connecting the Great Neck and Port Washington substations. This new circuit supports reliability of service for both substations.
- Installation of the new South Manor 69 kV substation. This project installs a new 69 kV ring bus substation (South Manor) connecting the Moriches and Eastport substations. The new substation is needed to meet increased load in the area.
- Installation of a Dynamic Reactive Support System (DRSS) at the Wildwood substation. The DRSS will reduce the need for expensive local generation to maintain voltage on the system.

It is noteworthy that the significant developments impacting the system in the past year were addressed during a period of significant organizational transition. These changes included the transition to the Authority's new service provider, PSEG Long Island on December 31, 2013, and the transition of the Authority's power supply function to PSEG Long Island on December 31, 2014. In addition, the Authority seated, integrated, and fully engaged a new 9-member board and new senior management, all with substantial knowledge of the utility industry. At the same time, consistent with its mandate under the LIPA Reform Act, the Authority has reduced its staff to levels appropriate for carrying out the Authority's streamlined financial, legal, and contract oversight functions. The smooth implementation of these organizational changes without interruption to the Authority's operations was an accomplishment in and of itself, made possible by the dedication and hard work of the Authority's staff.



John McMahon
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