

LONG ISLAND POWER AUTHORITY

MINUTES OF THE FINANCE AND AUDIT COMMITTEE MEETING

HELD ON JANUARY 20, 2016

The Finance and Audit Committee of the Long Island Power Authority (the “Authority”) was convened at 8:00 a.m. at LIPA Headquarters, Uniondale, NY, pursuant to legal notice given on January 15, 2016; and electronic notice posted on the Authority’s website.

The following Trustees of the Authority were present:

**Shelly L. Cohen, Committee Chair
Mark Fischl
Matthew Cordaro**

Representing the Authority were Thomas Falcone, Chief Financial Officer; Jon Mostel, General Counsel & Secretary to the Board of Trustees; Bobbi O’Connor, Deputy General Counsel & Assistant Secretary to the Board of Trustees; Kenneth Kane, Managing Director of Finance and Budgeting; Donna Mongiardo, Controller; Corey Horowitz, Director of Power Supply Risk Management; Kathleen Mitterway, Director of Audit; Rick Shansky, Managing Director of Contract Oversight; Barbara Ann Dillon, Director of Human Resources and Administration; and Sanna Wong-Chen, Director of Finance.

Representing PSEG LI were David Lyons, Director of Corporate Integration; and Scott Payant, Senior Manager of Treasury.

Chair Cohen welcomed everyone to the Finance and Audit Committee meeting of the Long Island Power Authority Board of Trustees.

Chair Cohen stated that the first item on the agenda is the adoption of the minutes from the December 16, 2015 Committee meeting.

Chair Cohen entertained a motion to accept the minutes of the December 16, 2015 meeting, which was duly made and seconded. The minutes were approved unanimously.

Trustee Cohen stated that next item on the agenda is the Overview of Financial Results & Hedge Report.

Ms. Mongiardo presented LIPA's financial results through December 2015. Mr. Horowitz presented the Hedge Report, and Mr. Lyons and Mr. Payant of PSEG LI reported on the PSEG LI Operating Results.

Chair Cohen stated that next item on the agenda is a report on Internal Audit Activities which would be presented by Kathleen Mitterway. Ms. Mitterway gave a presentation regarding the Authority's internal audit activities and then took questions from Trustees.

Chair Cohen stated that the next item on the agenda is discussion of 2015 Accomplishments which would be presented by Mr. Falcone. Mr. Falcone gave a presentation regarding the Authority's 2015 Accomplishments and then took questions from Trustees.

Chair Cohen stated that the next item on the agenda is consideration of Recommendation to Approve Sandy Insurance Settlement and Related Accounting Adjustments which would be presented by Kenneth Kane.

Mr. Kane presented the following item:

Requested Action

The Finance and Audit Committee of the Board of Trustees (the "F&A Committee") is requested to approve a resolution recommending at the full Board authorize the Chief Financial Officer ("CFO"), or his designee, to enter into a settlement agreement related to an insurance claim for damage sustained to substations, certain underground facilities, and certain meter equipment of the Long Island Power Authority and its subsidiary, the Long

Island Lighting Company d/b/a LIPA (collectively, “LIPA” or the “Authority”) as a result of Superstorm Sandy.

Background

Superstorm Sandy struck Long Island on October 29, 2012 causing extensive damage to LIPA’s overhead transmission and distribution system, flooding 12 substations, with additional minor damage to other substations, and damaging certain underground transmission facilities and thousands of customer meters. LIPA had, and continues to hold, property insurance coverage for all the equipment within the fence of its substations, certain underground facilities including underground transmission facilities, and meter equipment. The insurance policy covering LIPA’s property at the time of the storm was obtained on LIPA’s behalf by its service provider at the time, National Grid Electric Services LLC (“National Grid”).

Due to the magnitude of the storm, the Authority’s Service Area was declared a federal disaster, making the Authority eligible for Federal Emergency Management Agency (“FEMA”) grants. In February 2014, LIPA signed a Letter of Undertaking that provides for Public Assistance grant funding under Section 428 of the Stafford Act (“428 Grant Agreement”). Funds from the 428 Grant Agreement reimburse the Authority for 90% of its eligible repair/restoration costs, net of insurance recoveries. In September 2014, the Authority signed a Community Development Block Grant agreement (“CDBG Grant”) for an amount equal to the 10% non-federal match of the 428 Grant Agreement. The Authority has received reimbursement for substantially all of its Superstorm Sandy restoration expenses through a combination of these grants.

FEMA requires grantees to pursue all other available sources of funds, including insurance, and any insurance recoveries reduce the amount of FEMA funding for storm restoration to the extent that the damaged property is considered covered under both the FEMA grant and an insurance policy. As such, the Authority expects that the insurance settlement will reduce its need for FEMA grant funds for storm restoration.

Discussion

Over the past 2 ½ years, LIPA staff, along with its advisors for disaster recovery at Ernst & Young LLP, have regularly met with the insurance carriers and their representatives regarding the Authority’s claim. LIPA arranged for the insurers to conduct numerous site visits to the flooded substations, inspect work being done at underground facilities, review volumes of supporting documentation, and participate in countless meetings with representatives of National Grid and PSEG Long Island LLC (“PSEG LI”), who were/are responsible for implementing the temporary and permanent repairs that have been completed to date and remain to be completed over the next two years at the damaged properties. As is the routine nature of any insurance claim, there remain differences in position between LIPA and the insurers as to the terms of the policy and the scope and cost of restoration and temporary/permanent repairs.

The current amount to perform all temporary and permanent repair work associated with the damages outlined above and continuing over the next two years is estimated at

approximately \$87 million (net of certain storm hardening costs and temporary restoration work expected to be recovered from the FEMA grant).

On December 10, 2015, the parties met again and negotiated a settlement of \$80 million, subject to the approval of the Board of Trustees. LIPA's claim is subject to a \$3.75 million deductible, which LIPA expects to recover from the FEMA grant. As with any settlement, this negotiated recovery must be weighed against judgements concerning the likely expense, risk, and recovery of further prolonged dispute or litigation under the policy.

Accounting Impact

The final disposition of this insurance settlement will likely result in a significant book value gain to the Authority as the depreciated book value of the substation assets damaged by the storm were approximately \$2 million while the cost recovered from the insurers to replace/repair the assets under the terms of the policy, net of certain deductions (including for temporary repair work of a non-capital nature), is estimated at approximately \$65 million.

Consistent with past actions approved by the Board for netting similar one-time book value gains against regulatory assets, Authority staff recommends that the probable book value gain of the insurance settlement be netted against certain regulatory assets previously approved by the Board. This will not impact the Authority's expenditures or the level of electric rates but does provide a less complex and more informative view of the Authority's net position and going forward financial condition to stakeholders, rating agencies, and investors. The alternative would be to realize the book value gain of the insurance settlement in net income in 2016.

Authority staff seeks permission to net the book value gain of the insurance settlement against the regulatory assets previously approved by the Board for the installation of the Outage Management System (currently \$24.3 million) and Enterprise Resource Planning System (\$38.7 million) upon the effective date of the insurance settlement. The selection of these regulatory assets is unrelated to the assets damaged by the storm or subject to the insurance settlement.

Recommendation

Based on the foregoing, Mr. Kane recommended approval of the above-requested action by adoption of a resolution in the form of the below resolution.

A motion was duly made and seconded, and the Trustees unanimously adopted the

following resolution:

RECOMMENDATION OF APPROVAL OF AUTHORIZATION TO ENTER INTO SETTLEMENT AGREEMENT FOR INSURANCE CLAIM FOR SUPERSTORM SANDY AND RELATED TREATMENT OF ACCOUNTING GAIN

WHEREAS, the Long Island Power Authority's (the "Authority")'s transmission and distribution system sustained extensive damage during Superstorm Sandy; and

WHEREAS, the Authority had property insurance coverage for all the equipment within the fence of its substations, certain underground facilities including underground transmission facilities, and meter equipment; and

WHEREAS, the Authority staff, along with its advisors for disaster recovery at Ernst & Young LLP, have regularly met with the insurance carriers and their representatives over the past 2 ½ years in order to determine the amount of the Authority's claim and negotiate an appropriate settlement; and

WHEREAS, on December 10, 2015, the negotiated a settlement of \$80 million on the Authority's insurance claim, subject to the approval of the Board of Trustees; and

WHEREAS, consistent with past actions approved by the Board, Authority staff recommends that the probable book value gain of the insurance settlement be netted against certain regulatory assets previously approved by the Board; specifically the installation of the Outage Management System (currently \$24.3 million) and Enterprise Resource Planning System (\$38.7 million) upon the effective date of the insurance settlement; and

WHEREAS, this change would not impact the Authority's expenditures or the level of electric rates but would provide a less complex and more informative view of the Authority's net position and going forward financial condition to stakeholders, rating agencies, and investors; and

WHEREAS, the Finance and Audit Committee has given due consideration to this issue and to the advice of Authority staff;

NOW, THEREFORE, BE IT RESOLVED, that the Finance and Audit Committee of the Board of Trustees hereby recommends that the full Board authorize the Authority to enter into the insurance settlement agreement for property damages sustained in Superstorm Sandy as proposed in the accompanying memorandum; and

BE IT FURTHER RESOLVED, that the Finance and Audit Committee of the Board of Trustees hereby recommends that the full Board authorize the Authority staff, in its accounting treatment of the insurance settlement, to net the probable book value gain of the settlement against certain regulatory assets as described in the accompanying memorandum.

Chair Cohen then entertained a motion to adjourn, which was duly made and seconded, after which the meeting concluded at approximately 8:55 a.m.