# MINUTES OF THE ONE HUNDRED SEVENTH MEETING OF THE AUDIT AND FINANCE COMMITTEE HELD ON JUNE 21, 2010

Pursuant to notice dated June 7, 2010, a copy of which is annexed hereto, the one hundred seventh (107<sup>th</sup>) meeting of the Audit and Finance Committee ("Committee") of the NEW YORK STATE ENERGY RESEARCH AND DEVELOPMENT AUTHORITY ("Authority") was convened at 11:00 a.m. on Monday, June 21, 2010, in the Authority's Albany office at 17 Columbia Circle, Albany, New York; and by video conference in the Authority's New York City office at 485 Seventh Avenue, 10<sup>th</sup> floor, New York, New York; and by video conference in the Authority's Buffalo office at 726 Exchange Street, Suite 821, Buffalo, New York.

The following members of the Committee were present in Albany, unless otherwise indicated:

Robert B. Catell (by video conference from New York City)
George F. Akel, Jr.
Vincent A. DeIorio, Esq., ex officio
David D. Elliman

Also in attendance was Authority Board Member Elizabeth D. Thorndike.

In addition, Francis J. Murray, Jr., President and CEO; Robert G. Callender, Vice President for Operations and Energy Services; Janet Joseph, Vice President for Technology and Strategic Planning; Jeffrey J. Pitkin, Treasurer; Hal Brodie, Esq., Secretary and General Counsel; Jacquelyn L. Jerry, Esq., Deputy Counsel and Secretary to the Audit and Finance Committee; Peter V. Mahar, Controller and Assistant Treasurer; Mark B. Mitchell, Director of Internal Audit; Donna Gonser and Sarah Hopkins from Lumsden & McCormick, LLP; and various other members of the staff of the Authority were present.

Mr. Catell called the meeting to order and noted the presence of a quorum. He stated that the meeting notice and agenda were mailed to the Committee members and press on June 7, 2010.

Mr. Catell indicated that the first item on the agenda concerned the approval of the minutes of the one hundred sixth meeting of the Committee held on April 12, 2010.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote, the minutes of the one hundred sixth meeting of the Committee held on April 12, 2010, were approved.

Mr. Catell indicated that the next item to be considered was the Authority's Investment Guidelines, Operative Policy and Instructions (June 2010) ("Investment Guidelines") and its Annual Investment Report ("Investment Report"). Mr. Pitkin explained that the Investment Guidelines set forth the policies and procedures for the investing, monitoring, and reporting of the Authority's investments. The Authority is required to review and approve its investment policies, annually, pursuant to Public Authorities Law Section 2925. No substantive changes are recommended to the Investment Guidelines.

The Investment Report, which is also required to be approved annually, summarizes the Authority's investment activities and the results of those activities. The Investment Report indicates that the Authority's overall investments increased approximately \$85 million, from \$698.7 million to \$770.9 million. The increase is principally due to funds that were received for specific programs administered by the Authority but were not expended as of March 31, 2010. Mr. Pitkin summarized the various fund balances, which included an additional \$90 million from the sale of allowances under the Regional Greenhouse Gas Initiative ("RGGI"); a payment to the irrevocable trust established for post-employment health insurance benefit costs under Governmental Accounting Standards Board Statement No. 45 ("GASB45"); and timing differences between expenditures and reimbursement billings.

The Investment Report indicates that the composition of the Authority's investments remained relatively unchanged from the prior year with 69% of total investments held in collateralized certificates of deposit, and the balance invested in Federal government obligations.

As a result of generally lower market interest rates, interest earnings for the fiscal year ended March 31, 2010, decreased by \$4.6 million to approximately \$11.4 million, and the rate of return on investments was approximately 1.6%, compared to a return of 2.7% in the prior year.

The Investment Report includes a report from the independent auditors, Lumsden & McCormick, LLP, indicating that, in their opinion, the Authority has complied with the New York State Comptroller's Investment Guidelines for Public Authorities and relevant sections of the New York State Public Authorities Law.

In response to an inquiry from Mr. Elliman, Mr. Pitkin explained that the New York State Department of Taxation and Finance ("Tax and Finance") approves the banks through which the Authority invests. The Authority's funds are combined with other Tax and Finance investment funds. Mr. Elliman asked staff to reassess whether there should be a limit on the percentage of investments held with any one institution in order to minimize Authority risk.

In response to a comment from Mr. Akel, Mr. Pitkin confirmed that Tax and Finance obtains collateral for the Authority's investments.

Mr. Pitkin said that he would reassess the potential risks and allowable percentage deposits and report to the Committee on the results of the reassessment.

Mr. Catell stated that a resolution considering approval of the Investment Report and the Investment Guidelines would be considered after the Committee members meet in executive session with the independent auditors.

Mr. Catell stated that the next discussion item concerned the Authority's Financial Statements. Peter Mahar, the Authority's Controller and Assistant Treasurer, explained that the Committee members are requested to recommend adoption of a resolution approving the Authority's annual audited Financial Statements for the fiscal year ended March 31, 2010. The independent auditors will issue an unqualified opinion on the Financial Statements.

The Authority's total revenue increased from \$494.0 million to \$582.1 million as a result of an increase in State Appropriation revenue for the construction of the Hudson Valley Community College TEC-SMART facility; an increase in funding for the New York Energy Smart<sup>sm</sup> program, which included an increase in Energy Efficiency Portfolio Standard ("EEPS") funding; an increase in Renewable Portfolio Standard ("RPS") funding; and additional RGGI auction proceeds, which were offset by a decrease in funding provided by Consolidated Edison Company of New York, Inc. ("Con Edison") pursuant to the settlement of the RGGI litigation and a decrease in investment earnings.

The Authority's total expenses increased from \$314.4 million to \$497.6 million. This included an increase in salaries and benefits of \$2.8 million primarily due to increased staffing levels. Program expenditures increased \$81.8 million primarily due to increased expenditures under the New York Energy \$mart^{SM}\$ and RPS programs and also as a result of non-recurring expenditures at the Saratoga Technology + Energy Park. Other operating costs increased by \$200,000 as a result of increased expenditures for office space rental, which were offset in part by lower travel costs.

The Authority's total assets increased from \$705.8 million to \$797.8 million. The increase in cash and investments of \$85.7 million was principally due to scheduled collections from utilities in the New York Energy \$mart<sup>SM</sup> and RPS programs, which exceeded disbursements for expenses, and proceeds received from the sale of emission allowances under RGGI. The increases were offset in part by a \$90 million transfer to the State of New York from RGGI funds as part of the State's Deficit Reduction Plan. All of these program funds are considered restricted assets.

Total liabilities increased by \$7.6 million to \$100.3 million. Short-term liabilities increased by \$16.3 million primarily due to an increase in accounts payable and accrued liabilities associated with an increase in program activity. There was also an increase of \$7.7 million due Con Edison as part of the settlement of the RGGI litigation. These increases in liabilities were offset by \$5.1 million that were not committed in the Con Edison System-Wide Demand Reduction program and were returned when the program expired. In addition, long-term liabilities decreased \$8.8 million due to the final \$1.7 million State Service Contract Revenue bond principal payment, which was made on April 1, 2009, as well as the deposit of \$7.1 million of prior years' GASB45 post-employment retiree health insurance benefit liabilities in an irrevocable trust, which was created in the last quarter of Fiscal Year ("FY") 2009-10. In accordance with GASB45, the Authority also transferred to the trust \$3.9 million for amounts accrued during FY 2009-10. In future fiscal years, the trust will be separately audited and the results provided to the Committee members.

The Authority's net assets, the difference between the Authority's assets and its liabilities, increased from \$613 million to \$697.5 million. Restricted net assets, which represent unexpended funds received for particular specified programmatic purposes such as RGGI, NY Energy \$mart<sup>SM</sup>, and RPS programs, increased from \$597.5 million to \$682.5 million.

The Authority's unrestricted net assets decreased from \$1.3 million to \$1.1 million as a result of investments made in capital assets and differences in operating revenues and expenses. These assets can be used to finance operations without constraints established by debt covenants, enabling legislation, or other legal requirements. Net assets invested in capital assets totals \$13.9 million. Staff continues to monitor the balance and to identify strategies to return to the Authority's historical reserve of \$2 million.

Mr. Mahar concluded his presentation by stating that included in the meeting packet were additional reports issued by the independent auditors under governmental auditing standards. The independent auditors disclosed no instances of noncompliance or material weaknesses, found management's estimates and financial disclosures reasonable, found no misstatements or

disagreements, and offered no management letter comments to address control weaknesses or suggestions for improvement.

In response to an inquiry from Mr. Elliman, Mr. Mahar explained that the \$90 million payment of RGGI funds to the State pursuant to deficit reduction legislation was characterized as a "Transfer to New York State" because it was not a traditional expenditure of the RGGI program. Mr. Pitkin added that the funds cannot be listed as a "reduction in revenue," because the funds were initially reported in the financial statements for prior fiscal years. Mr. Elliman suggested that the "transfer" be re-designated as a "payment," since the funds were paid to the State and resulted in a depletion of the RGGI funds.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members present, the following resolution was adopted.

#### Resolution No. 357

RESOLVED, that pursuant to Section 105 of the Public Officers Law, the Members of the Audit and Finance Committee of the New York State Energy Research and Development Authority shall convene in executive session for the purpose of reviewing the financial condition of the Authority.

The Committee members then met with only the independent auditors in executive session.

Mr. Catell reconvened the meeting in open session. Mr. Catell announced that no formal action was taken during the executive session. He said that the Committee members had a complete and thorough discussion with the independent auditors and that the independent auditors stated that Authority staff was responsive to their requests for information.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members present, the following resolution was adopted.

#### Resolution No. 358

RESOLVED, that the Audit and Finance Committee recommends that the Members of the Authority adopt a resolution in substantially the same form as the resolution submitted to the Committee (attached as Exhibit A), approving and adopting the 2009-2010 Annual Investment Report and the Investment Guidelines, Operative Policy and Instructions (June 2010), substantially in the form submitted to the Committee (attached as Exhibit B).

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members present, the following resolution was adopted.

#### Resolution No. 359

RESOLVED, that the Audit and Finance Committee recommends that the Members of the Authority adopt a resolution in substantially the same form as the resolution submitted to the Committee (attached as Exhibit C), approving the Authority's Financial Statements as of March 31, 2010 (attached as Exhibit D).

Mr. Catell then said that the next agenda item concerned the appointment of independent auditors. Mr. Pitkin explained that the Committee members are asked to approve a resolution appointing Lumsden & McCormick, LLP, as the independent auditors of the Authority for the fiscal year ending March 31, 2011. The fees and expenses for the audit would not exceed \$41,500, \$200 less than this year's fee. Lumsden & McCormick was competitively selected in 2007 under a mini-bid of firms pre-qualified by the New York State Office of General Services ("OGS") under a State contract for audit services. The Authority may renew the agreement annually for one-year extensions with annual adjustments in the fees pursuant to escalation clauses in the underlying OGS contract. The terms of the OGS contract expires in January 2011, so this reappointment will be the final year under the OGS contract. Staff will issue a competitive solicitation to select independent auditors for FY 2011-2012.

A copy of the 2010-2011 engagement letter from the independent auditors explaining the proposed services was provided to the Committee members. This engagement letter is consistent with the FY 2009-2010 engagement letter.

Staff has been satisfied with the performance of Lumsden & McCormick and recommends its reappointment for FY 2010-2011.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members present, the following resolution was adopted.

#### Resolution No. 360

RESOLVED, that the Audit and Finance Committee recommends that the Members of the Authority adopt a resolution in substantially the same form as the resolution submitted to the Committee (attached as Exhibit E), appointing Lumsden & McCormick, LLP as the Authority's independent auditors for fiscal year 2010-2011.

Mr. Catell indicated that the next agenda item was the Annual Bond Sales Report ("Bond Sales Report"), and he called upon Mr. Pitkin to discuss this item. Mr. Pitkin explained that, in accordance with Public Authorities Law Section 2800 and the Authority's Financial Services Firms Guidelines, Operative Policy and Instructions (April 2006), the Committee members are asked to adopt a resolution approving the Bond Sales Report. The Bond Sales Report indicates that the Authority participated in the interest rate conversion of two bond series during FY 2009-10 with principal amounts totaling \$42.6 million.

In addition, the last series of State Contract Revenue Bonds in the principal amount of \$1.74 million matured. Proceeds from these bonds were used to finance activities at the Western New York Nuclear Service Center.

As required, a schedule of bonds outstanding as of March 31, 2010, is included as part of the report. The Authority currently has \$3.6 billion in bonds outstanding.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members present, the following resolution was adopted.

#### Resolution No. 361

RESOLVED, that the Audit and Finance Committee recommends that the Members of the Authority adopt a resolution in substantially the same form as the resolution submitted to the Committee (attached as Exhibit F), adopting and approving for submission pursuant to Section 2800 of the Public Authorities Law, the Authority's Annual Bond Sales Report for the fiscal year April 1, 2009 through March 31, 2010 (attached as Exhibit G).

Mr. Catell indicated that the next item on the agenda was a report from Mark Mitchell, the Director of Internal Audit, on his recent activities. Mr. Mitchell reported that since the April 2010 Committee Meeting, three draft reports have been issued, work is progressing on another three reviews, and Internal Audit has begun preparations for another program audit. Mr. Mitchell indicated that this increased level of activity is the result of having an internal audit team comprised of a contract auditor and an internal auditor in addition to himself.

Mr. Mitchell stated that the first and second draft reports have been issued to program management regarding the FlexTech Program and the New York Great Appliance Swap Out Program, which is funded by the American Recovery and Reinvestment Act of 2009 ("ARRA") under a U.S. Department of Energy grant. The third draft report, which covers the payment of travel and credit card expenditures, was provided to the Authority's Controller and Assistant Treasurer. Program staff and management will be given an opportunity to comment on the reports. Mr. Mitchell will provide the Committee with the results of these three audits at the September 2010 Committee Meeting.

Next, Mr. Mitchell provided the Committee with an update on three other reviews. The contract audit of the Authority's implementation agreement with Conservation Services Group ("CSG") for the Home Performance with Energy Star® Program ("Home Performance") is approaching its final stages. Audit work has focused on determining whether CSG is invoicing the Authority appropriately for its direct labor costs, indirect rates, and travel expenses. Detailed information from CSG's books and records have been obtained and analyzed. Because of the size and complexity of the issues encountered, the audit report is just starting to be drafted. However, certain issues, which are being addressed with CSG, may need to be resolved before

the report can be completed. In the meantime, payments to CSG have been suspended. Mr. Mitchell said that he will provide the Committee with an update at the September 2010 Committee Meeting.

Mr. Mitchell reported that he is still in the process of gathering information from management and staff that will serve as input for the business risk assessment. The Officers have agreed to a timetable for completing the business risk assessment. Mr. Mitchell expects that the results will be presented to the Committee at the September 2010 Committee Meeting, along with a proposed Internal Audit Plan for FY 2010-11 ("FY 2010-11 Plan").

An information technology ("IT") risk assessment was performed independently of the business risk assessment in keeping with the latest internal auditing standards. Mr. Mitchell stated that the report has been drafted, and he is working with management to clarify the report's content. He anticipates providing the results of the IT risk assessment at the Committee's September 2010 Meeting. The results will include a proposal for a number of IT audits, which will be included in the FY 2010-11 Plan.

Internal Audit is also preparing to conduct an audit of the Main Tier of the RPS Program. Although the Officers do not have any specific concern about the RPS Program, the review has been requested because there is a significant amount of money associated with it. This will result in a "fresh set of eyes" providing additional, independent assurance that the business process controls are providing adequate assurances that the program is operating as intended.

In addition, a quality assurance review ("QAR") of Internal Audit will be conducted. Mr. Mitchell indicated that, once the previously discussed audits are completed, he will begin preparations for the QAR. As was previously explained to the Committee, it will take 6-7 weeks to prepare adequately for the QAR. Mr. Mitchell said he will allot the time needed for the preparation and the completion of the QAR in the FY 2010-11 Plan.

Mr. Mitchell concluded his report by stating that the Committee was provided with an Interim Internal Audit Plan which sets forth Internal Audit's activities until the September 2010 Committee Meeting, when Mr. Mitchell will present the FY 2010-11 Plan.

In response to an inquiry from the Chair, Mr. Mitchell indicated that the Authority does not require that its contractors provide certified payrolls, but that he would review whether the Authority should change this policy.

Mr. Murray reiterated that the Authority has taken the unusual step of holding all payments to CSG until such time as the audit is completed and there are adequate assurances of proper payments being made.

Whereafter, the Committee members indicated their concurrence with the proposed Interim Internal Audit Plan.

Mr. Catell indicated that the next item on the agenda was amendments to the Committee Charter. The Chair explained that the Public Authorities Reform Act of 2009 was amended to add the responsibility that the Committee members approve all debt issuances. Therefore, the Committee Charter would be amended to specifically state that the Committee is responsible for reviewing and making recommendations concerning proposals for the issuance of debt. This is consistent with current practice and would not require any change in existing practices.

At the April 2010 Board Meeting, the Members approved a comparable change to the By-laws and the proposed amendments incorporate the same changes.

The resolution would also recommend submission of the Committee Charter to the persons designated to receive a copy pursuant to Section 2800 of the Public Authorities Law.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members present, the following resolution was adopted.

#### Resolution No. 362

RESOLVED, that the Audit and Finance Committee recommends that the Members of the Authority adopt a resolution in substantially the same form as the resolution submitted to the Committee (attached as Exhibit H), adopting and approving the amendments to the Audit and Finance Committee Charter and approving the submission of the Audit and Finance Committee Charter pursuant to Section 2800 of the Public Authorities Law (attached as Exhibit I).

Next, Mr. Catell asked Mr. Pitkin to provide the Committee with an update on the Authority's financing program. Mr. Pitkin explained that, as approved by the Members in April 2010, the Authority participated in the conversion of 2 series of bonds on behalf of New York State Electric & Gas Corporation ("NYSEG"). The \$101 million in Bonds were converted to a 3-year, term interest rate, without liquidity, and received a rating of BBB+ from Standard and Poor's Corporation. The interest rate on both series of bonds is 3%.

Two additional conversions on behalf of Central Hudson Gas & Electric Corporation ("Central Hudson") are underway and expected to close next month. Central Hudson has requested \$81.5 million in bonds be converted to a Fixed Rate.

In response to an inquiry from Mr. Elliman, Ms. Jerry responded that NYSEG did not obtain insurance with respect to these short-term issuances, but NYSEG may pursue it in connection with other longer-term conversions. She added that NYSEG provided calculations showing that there were cost savings associated with the conversions, notwithstanding the lack of a liquidity facility. The substance of the proposed conversions was also reviewed with Department of Public Service staff.

Mr. Catell indicated that the last item on the agenda was other business and asked Mr. Pitkin to address the Committee. Mr. Pitkin explained that the New York State Comptroller has recently begun an audit of the commercial energy audit program to assess resources for the program compared to the public's demand for the services. Staff will report on the results of the audit once it is completed.

Mr. Murray added that the review appears to constitute a programmatic review, not a financial audit.

Mr. Catell asked if there were any other matters the Committee members wished to discuss. There being none, upon motion duly made and seconded, and by unanimous voice vote, the meeting was adjourned.

Respectfully submitted,

aequelyn L. Jerry

Secretary to the Committee

## NYSERDA New York State Energy Research and Development Authority

Vincent A. Delorio, Esq., Chairman

Toll Free: 1 (866) NYSERDA

www.nyserda.org • info@nyserda.org

### **NOTICE OF MEETING AND AGENDA**

June 7, 2010

#### TO THE MEMBERS OF THE AUDIT AND FINANCE COMMITTEE:

PLEASE TAKE NOTICE that the one hundred seventh (107<sup>th</sup>) meeting of the AUDIT AND FINANCE COMMITTEE of the New York State Energy Research and Development Authority will be held in the Authority's Albany Office at 17 Columbia Circle, Albany, New York, and by video conference in the Authority's New York City Office at 485 Seventh Avenue, 10<sup>th</sup> Floor, New York, New York, and by video conference in the Authority's Buffalo Office at 726 Exchange Street, Suite 821, Buffalo, New York, on Monday, June 21, 2010, commencing at 11:00 a.m., for the following purposes:

- 1. To consider the Minutes of the 106<sup>th</sup> meeting held on April 12, 2010.
- 2. To consider and act upon the Annual Investment Report of the Authority and the "Investment Guidelines, Operative Policy and Instructions (June 2010)".
- 3. To consider and act upon the Financial Statements of the Authority for FY 2009-10.
- 4. To consider and act upon a motion to enter into executive session for the purpose of reviewing the financial condition of the Authority.
- 5. To consider and act upon the appointment of the Authority's independent auditors for fiscal year 2010-11.
- 6. To consider and act upon an annual bond sale report.
- 7. To receive a report on the recent activities of the Director of Internal Audit and to consider and act upon a resolution approving an Interim Internal Audit Plan for fiscal year 2010-11.
- 8. To consider and act upon a resolution approving amendments to the Audit and Finance Committee Charter.
- 9. To receive a report on the financing program.

# 10. To transact such other business as may properly come before the meeting.

Members of the public may attend the meeting at any of the above locations. In accordance with guidance from the Office of Taxpayer Accountability, the Authority will be posting a video of its Board and Committee meetings to the web within 2 business days of the meeting. The video will be posted at http://www.nyserda.org/governancemeetings2.asp.

Secretary to the Audit and Finance Committee