

MINUTES OF THE ONE HUNDRED TWENTY-SECOND MEETING OF THE
AUDIT AND FINANCE COMMITTEE
HELD ON JANUARY 26, 2015

Pursuant to a notice dated January 14, 2015, a copy of which is annexed hereto, the one hundred twenty-second (122nd) meeting of the Audit and Finance Committee (the “Committee”) of the NEW YORK STATE ENERGY RESEARCH AND DEVELOPMENT AUTHORITY (the “Authority”) was convened at 11:00 a.m. on Monday, January 26, 2015, in the Authority’s Albany Office located at 17 Columbia Circle, Albany, New York, in the Authority’s New York City Office located at 1359 Broadway, New York, New York, and in the Authority’s Buffalo Office located at 726 Exchange Street, Suite 821, Buffalo, New York.

The following members of the Committee were present:

Jay Koh, Chair
Richard Kauffman
Sherburne Abbott
Jigar Shah

Also present were John B. Rhodes, President and CEO; Janet Joseph, Vice President for Technology and Strategic Planning; David Margalit, Chief Operating Officer; Jeffrey J. Pitkin, Treasurer; Noah C. Shaw, Esq., General Counsel; Sara LeCain, Esq., Senior Counsel and Secretary to the Audit and Finance Committee; Mark Mitchell, Director of Internal Audit; and various other staff of the Authority.

Mr. Koh called the meeting to order and noted the presence of a quorum. Mr. Koh stated that the meeting notice and agenda were forwarded to the Committee members and the press on January 15, 2015. The first item on the agenda concerned the approval of the minutes of the one hundred twenty-first (121st) meeting of the Committee, held on September 22, 2014.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members, the minutes of the hundred twenty-first (121st) meeting of the Committee, held on September 22, 2014, were approved.

Mr. Koh indicated that the next item on the agenda concerned a proposed conversion by the New York State Electric and Gas Corporation (“NYSEG”). Mr. Koh called upon Jeff Pitkin, Treasurer, to present this item.

Mr. Pitkin stated that approval is sought for a resolution authorizing the amendment of documents related to four separate series of Pollution Control Refunding Revenue Bonds (the “Bonds”) previously issued on behalf of NYSEG in an aggregate principal amount of \$204.5 million. The resolution would authorize a waiver of the requirement that the Bonds achieve an “A” rating at the time of conversion, provided that the Bonds would achieve a rating of at least “BBB” from Standard & Poor’s, or “Baa2” from Moody’s. The amendment would authorize the waiver of these requirements through December 31, 2015 and would permit NYSEG to complete its planned remarketing of the Bonds to a term rate in excess of 13 months during this calendar year.

Mr. Pitkin reported that, historically, the Members have required that Authority bonds issued on behalf of any investor-owned utilities achieve an “A” rating both at the time of issuance and at any time they are subsequently converted to a different interest rate mode. This rating requirement was also generally required by the Public Authorities Control Board (the “PACB”), which approves the Authority’s bonds.

The purpose of these requirements was to protect the interests of the Authority by ensuring that bonds issued on a conduit basis achieved a sufficient minimum rating. As a result of this policy, those utilities not rated “A” were required to obtain credit enhancement support, such as municipal bond insurance or a letter of credit facility, from a provider with at least an “A” rating.

When these minimum rating requirements were first established, letters of credit and highly-rated insurance policies were widely available at reasonable costs, and obtaining the support facilities resulted in higher ratings, and generally lower interest rates, which in turn resulted in net cost savings to be realized by the utility's ratepayers.

NYSEG has requested authorization to convert four series of bonds previously issued on their behalf to a term rate period without the benefit of a liquidity facility or insurance. NYSEG currently has a rating of "A3" by Moody's and "BBB+" with a stable outlook by Standard & Poor's.

NYSEG advises that bond insurance and letters of credit are still not widely available at reasonable costs and that requiring a minimum "A" rating at time of conversion during calendar year 2015 would likely add 125 basis points or more to the cost of funding, with the additional cost being borne by its ratepayers. The Board has approved similar requests in the past, including a request for NYSEG in April 2010.

Mr. Pitkin stated that the Authority believes it is appropriate to grant the waiver requested by NYSEG. In the current interest rate environment, the Authority does not believe the ratepayers' interests are furthered by requiring NYSEG to incur costs for credit enhancement exceeding the benefits provided. The Authority has consulted with staff from the Department of Public Service, and they concur with this approach.

These changes and waiver, once approved by the Authority, must also be approved by the PACB before implementing amendments and modifications could be made to prior resolutions and documents approved in connection with the original issuance of the Bonds.

In response to an inquiry from Mr. Kauffman, Mr. Pitkin noted that he had spoken to Mr. Koh on how to frame this request. Specifically, this request is indicative of the current market, although since the Bonds have long maturities it was not clear that it made sense to make a permanent policy. As such, the Authority thinks it best to make this request on an *ad hoc* basis, since it only comes up periodically.

In response to an inquiry from Mr. Kauffman, Mr. Koh said that the particular request by NYSEG has implications for the cost to ratepayers, the interests of NYSEG, and the reputational interests of the Authority. In terms of the balance of interests between ratepayers, NYSEG, and the Authority, the costs of credit enhancement in the currently less liquid market outweigh the value of the actual credit enhancement. Due to the “A3” and “BBB+” with a stable outlook ratings of NYSEG, Mr. Koh stated that a slight shift in actual requirements for credit enhancement does not seem to indicate a substantial increase in potential risk to the reputation of the Authority compared to the savings that would be realized by ratepayers. The conclusion of staff has thus been to recommend the waiver, and Mr. Koh stated that the judgment in this case seems to be reasonable based on the cost-savings interest of the ratepayers within the current situation of the market.

In addition, Mr. Koh stated that the Authority ultimately did not decide to delegate this issue to a staff level both because the original setting is at the Board level and implicates the reputation of the Authority, and because there are not many of these requests for waivers. In other words, these requests for waivers are episodic and do not inhibit operations, and the Authority should wait to see how the market reacts while also analyzing the creditworthiness of the requesting utility. Mr. Koh added that, until this becomes an administrative or efficiency burden, this should be considered on a case-by-case basis.

In response to an inquiry from Mr. Shah, Mr. Koh stated that the disparity in rates is based on creditworthiness at the time.

Mr. Kauffman added that while he supports the conclusion with respect to the treatment of the current waiver as well as future waivers, he wants to make sure that the Authority continues to act on an *ad hoc* basis as long as it is not setting precedent.

Mr. Rhodes indicated that staff and the Officers concur with Mr. Koh’s view that the policy should be kept as it currently is, since the Authority does not want to delegate or loosen it. In other words, the Authority wants to go on the record of not setting precedent in this matter.

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

Resolution No. 400

RESOLVED, that the Members of the Authority authorize the amendment of the Trust Indentures by and between the Authority and The Bank of New York Mellon, successor Trustee to Deutsche Bank Trust Company Americas (collectively, the "Trust Indentures"), the Participation Agreements, by and between the Authority and New York State Electric & Gas Corporation (collectively, the "Participation Agreements"), and other documents relating to Pollution Control Refunding Revenue Bonds (New York State Electric & Gas Project) 1994 Series B; Pollution Control Refunding Revenue Bonds (New York State Electric & Gas Project) 1994 Series C; Pollution Control Revenue Bonds (New York State Electric & Gas Project) 2004 Series A; and Pollution Control Revenue Bonds (New York State Electric & Gas Project) 2005 Series A (collectively, the "Bonds"), in order to waive the minimum rating requirement of "A" with respect to the conversion of each series of the Bonds to a Term Rate or Fixed Rate (as those interest rate terms are defined by the related Trust Indentures), and to allow the remarketing of such series of Bonds at a rating of no lower than BBB/Baa2; and

BE IT RESOLVED, that the Authorized Officers of the Authority are each hereby authorized and directed to execute and deliver any such other agreements, documents, or certificates (including, but not limited to, any agreements, documents, or certificates deemed necessary or proper to evidence or establish compliance with applicable provisions of the Internal Revenue Code of 1986, as amended), to do and cause to be done any such other acts and things and to make such other changes, omissions, insertions, revisions, or amendments to the Bond documents as they may determine necessary or proper for carrying out, giving effect to, and consummating the transactions contemplated by this resolution; and

BE IT FURTHER RESOLVED that this resolution shall be in effect during the calendar year ending December 31, 2015 unless extended by the Members pursuant to resolution.

Mr. Koh then indicated that the next item on the agenda concerned the appointment of Bond Counsel to the Authority. Mr. Koh called on Mr. Shaw to discuss the item.

Mr. Shaw stated that the Members are requested to approve the appointment of Hawkins Delafield & Wood LLP ("Hawkins"), and McKenna Long and Aldridge LLP ("McKenna"), as Bond Counsel to the Authority.

Under the Authority's Financial Services Guidelines, the Authority is required to issue a Request for Proposal ("RFP") for bond counsel services every five years. In accordance with those guidelines, the Authority issued a solicitation for engaging bond counsel services in October 2014. A technical review panel comprised of staff from the Office of the General Counsel and the Finance unit met to review the eight proposals received in response to the RFP, and recommended that Hawkins and McKenna be appointed as the Authority's Bond Counsel.

Bond Counsel is responsible for advising and assisting in the implementation of the Authority's financing program. In addition, the Bond Counsel provides guidance and support with respect to general financial matters facing the Authority.

In accordance with past practice, the Authority does not pay for Bond Counsel services performed in connection with conduit issues. Instead, the utility or other entity on whose behalf the bonds are issued will be responsible for the costs of issuing the bonds. Therefore, no funds are currently budgeted for these services.

Pursuant to the terms of the RFP, prior to entering into agreements with the Authority, Hawkins and McKenna will each be required to provide the Authority with a Minority and Women-Owned Business Enterprises ("MWBE") Utilization Plan that details each firm's "good faith" efforts to actively solicit MWBE participation in connection with its services.

If approved, staff will enter into a letter agreement with both Hawkins and McKenna to serve as Bond Counsel for the period January 1, 2015 through December 31, 2019.

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

Resolution No. 401

RESOLVED, that the President and CEO is authorized to engage the firms of Hawkins Delafield & Wood, LLP and McKenna Long and Aldridge, LLP to serve, as the President and CEO may determine is required from time to time, as bond counsel for the Authority on its financings, and provide legal advice and

counsel as may be necessary or desirable on matters involving trusts and other financial related services.

Mr. Koh then indicated that the next item on the agenda concerned a report from Mark Mitchell, Director of Internal Audit, on his recent activities. Mr. Koh called upon Mr. Mitchell to report on the item.

Mr. Mitchell stated that the scope of the report was on internal audits that had been completed since his last report, as well as upcoming audit activities.

Mr. Mitchell began his report on completed audits with a discussion of the audit of the Authority's Multifamily Energy Performance Portfolio ("MEPP"). He stated that MEPP programs make cost-effective improvements to the energy efficiency of buildings with five or more residential units by providing technical and financial assistance to multifamily building owners, managers and developers.

The MEPP audit assessed the adequacy of internal controls over project management, financial reporting, and performance reporting. By performance reporting, Mr. Mitchell meant the reporting of estimated energy savings based on the nature and number of energy efficiency measures implemented during a project. The MEPP audit evaluated program activity for two of the three programs within the portfolio – the Multifamily Performance Program and the Advanced Sub-metering Program.

The MEPP audit concluded that internal controls of project management and financial reporting for both programs were effective. Forms and paperwork required to participate in the programs were provided without exception, and all the incentive payments examined by the audit were proper.

With regard to the performance reporting data, over the course of time data clean-up efforts have been made and the accuracy of the data maintained in the program's database has improved.

Mr. Mitchell reported that the MEPP audit found a few instances in which the percentage of completion of energy savings measures had not been entered or updated in the project management and performance reporting database to accurately reflect actual project results. In addition, the audit found an instance in which changes that had been made to a project's work scope were never updated in the database to reflect the measures that had been installed at the completion of the project.

Mr. Mitchell stated that these exceptions were significant at the project level and they had a noticeable impact on program reports showing the program's overall energy savings. Mr. Mitchell's conclusion is that additional internal controls that will improve the reliability and accuracy of performance data need to be identified and implemented.

In addition, once a project has been completed, certain changes or corrections to project data can affect performance reporting. Therefore, the audit recommended that program staff should maintain records that document the purpose and authorization of any changes made to projects in the performance database that have already been reported as being completed. The "Detailed Results" section of the audit report provides greater description of the observations and conclusions, and provides recommendations that would improve the data quality of energy savings acquired.

Mr. Mitchell added that management has agreed to implement all of the recommendations in the report and has already made progress to that end.

Mr. Mitchell then turned his report to a discussion of completed audit activities. Specifically, he provided a high level, non-technical overview of audit activities and the results of the audit review of the methodology that a project team, comprised of Authority staff and consultants, used to implement Phase I of the Data Warehouse project.

Mr. Mitchell stated that the purpose of the Data Warehouse project is to integrate project and energy savings data from the Authority's disparate databases and spreadsheet sources in order to create a central repository of data that may be used for more reliable performance

reporting and timely data analysis. The Data Warehouse is being designed to store current and historical data. Phase I involved integrating data from three Renewable Portfolio Standard (“RPS”) databases into the Data Warehouse.

In order to remain in compliance with Internal Auditing standards, and because Internal Audit staff do not have the skills required to conduct this type of an assessment, the Authority entered into a contract with the New York State Technology Enterprise Corporation (“NYSTEC”) to conduct the work.

Mr. Mitchell stated that the approach has been to provide a general independent review of the project team’s methodology, rather than to measure their performance against a contract or statement of work. Therefore, the recommendations were developed by evaluating the project documentation against best practices and experience, rather than providing an assessment against contractual obligations.

Mr. Mitchell reported that the timing of the agreement with NYSTEC was such that Phase I of the project had just been completed as the assessment began. Therefore, out of necessity, the review of Phase I was retrospective, mostly limited to reviewing the overall project management processes and key documents such as project requirements, design and testing project life cycle.

Mr. Mitchell stated the Committee members have been provided with an executive summary of Internal Audit’s activities and the results of the review of the project team’s methodology. A more detailed, technical report was provided to the Data Warehouse implementation team that included Information Technology (“IT”) staff and management responsible for the success of the project. The report includes the findings and recommendations provided to them and the team’s written responses to each.

Mr. Mitchell noted that, since the report was provided to the Data Warehouse team, they have diligently evaluated and worked toward resolution of each of the recommendations. While there are still a couple of areas being addressed at an enterprise level, the functional working

team took great care to ensure every probability of success for the project and was very professional and responsive to the findings.

More specifically, Mr. Mitchell reported that approximately a dozen opportunities were identified as improvements to the project management process, particularly in the area of project management and testing. One significant opportunity was the establishment of a standard project management methodology across all projects, with frequent review of all projects for compliance with the standardized methodology. This would establish a consistent approach, which would introduce a higher degree of project management effectiveness and efficiency, and would reduce reliance solely on the skills and experience of an individual project manager. Another significant opportunity is the incorporation of software testing standards and the use of templates that are consistent with those standards. Mr. Mitchell also recommended that testing staff be provided with additional training that will better familiarize them with software testing standards.

Mr. Mitchell reported that IT should be commended for recognizing the value of a robust project management process and embracing management's vision of executing strong practices in the Authority's System Development Life Cycle, with project management then executed in a way that results in effectively delivered projects at the lowest cost and risk possible.

Mr. Mitchell noted that management expressed that the insights provided by the audit have been very helpful.

In response to an inquiry from Mr. Kauffman, Mr. Mitchell stated that the project management standards referred to are used broadly in the industry and have been found to be enablers of success. Mr. Mitchell added that the proposal is to bring those learned lessons into the Authority in a way that they are scalable, and that the goal is to have a set of practices that enables success without being overly burdensome

David Margalit, Chief Operating Officer, then stated that there are standards both relative to the operation of a project and standards specific to the industry, with Mr. Mitchell's report focusing on the former, which is concerned with the Authority having a disciplined approach to

the development of a set of standards, which includes the appropriate application of that discipline to connect back to the industry.

Mr. Koh stated that management's response to the first audit is commendable and that the interaction between all the functions of the Authority is constructive. Mr. Koh also stated that there is a lot of hard work behind the scenes that does not get a lot of credit, and that he wanted to commend the work that goes into these processes.

Mr. Rhodes concurred with Mr. Koh, and acknowledged the presence of Saul Morse, the new Chief Information Officer for the Authority.

Mr. Koh thanked Mr. Rhodes, noted that the audit function is important, and also pointed out that the Authority is cognizant of potential limits on resources.

Mr. Koh then indicated that the next item on the agenda was a discussion of recent audits by the State Comptroller. Mr. Koh called upon Mr. Pitkin to report on the item.

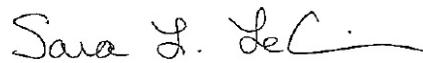
Mr. Pitkin stated that the State Comptroller issued an audit report in September 2014 on Selected Aspects of Discretionary Spending, and that the Authority's response to the audit report was provided to Governor Cuomo and legislative leaders in accordance with Section 170 of the Executive Law.

Mr. Pitkin reported that the audit encompassed a review of transactions during the period April 1, 2010 through March 31, 2012, to determine whether certain transactions complied with the Authority's prescribed procedures and that such expenses were reasonable, adequately supported, and properly approved. The audit report noted that, in certain instances, the Authority did not have policies and procedures to ensure the propriety and reasonableness of discretionary expenses, did not follow its policies, or did not require documentation of the necessity for expenses or their relationship to the Authority's core mission. The audit report provided three recommendations, all of which have been implemented.

Mr. Pitkin also stated that, in December, the State Comptroller issued another audit report regarding an audit of contract award and performance. The audit reviewed a sample of contract awards during a two year period to determine whether the Authority awarded contracts according to prescribed policies and procedures, and whether the Authority monitored vendor performance to ensure compliance with contract terms. Mr. Pitkin noted that a copy of the audit report and the Authority's response will be provided at the next scheduled Committee meeting.

Mr. Koh stated that the last agenda item concerned other business. There being no further business, upon motion duly made and seconded, and by unanimous voice vote, the meeting was adjourned.

Respectfully submitted,

A handwritten signature in cursive script that reads "Sara L. LeCain". The signature is written in black ink and is positioned above the printed name.

Sara L. LeCain
Secretary to the Committee

NOTICE OF MEETING AND AGENDA

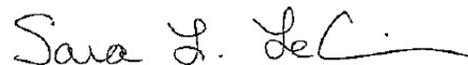
January 14, 2015

TO THE MEMBERS OF THE AUDIT AND FINANCE COMMITTEE:

PLEASE TAKE NOTICE that the one hundred twenty-second (122nd) 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 in the Authority's New York City Office at 1359 Broadway, 19th floor, New York, New York, and in the Authority's Buffalo Office at 726 Exchange Street, Suite 821, Buffalo, New York, on Monday, January 26, 2015, commencing at 11:00 a.m., for the following purposes:

1. To consider the Minutes of the 121st meeting held on September 22, 2014.
2. To consider and act upon an implementing resolution recommending authorizing the conversion of four series of bonds previously issued by the Authority, on behalf of New York State Electric & Gas Corporation, to finance pollution control, sewage and solid waste disposal, and other facilities located in New York.
3. To consider and act upon a resolution recommending approval of Hawkins Delafield & Wood, LLP and McKenna Long and Aldridge, LLP as Bond Counsel to the Authority.
4. To receive a report from the Director of Internal Audit on recent internal audit activities.
5. To receive a report on recent audits by the Office of the State Comptroller.
6. 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. Video conferencing will be used at all locations and the Authority will be posting a video of the meeting to the web within two business days of the meeting. The video will be posted at <http://www.nyserda.ny.gov/About/Board-Governance/Board-and-Committee-Meetings>.



Sara L. LeCain
Secretary to the Committee

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