

MINUTES OF THE ONE HUNDRED FIRST MEETING OF THE
AUDIT AND FINANCE COMMITTEE
HELD ON SEPTEMBER 15, 2008

Pursuant to notice and an agenda dated September 3, 2008, a copy of which is annexed hereto, the one hundred first (101st) meeting of the Audit and Finance Committee ("Committee") of the NEW YORK STATE ENERGY RESEARCH AND DEVELOPMENT AUTHORITY ("Authority") was convened at 12:30 p.m. on Monday, September 15, 2008, in the Authority's Albany Office at 17 Columbia Circle, Albany, New York, by video conference in the Authority's New York Office at 485 Seventh Avenue, 10th floor, New York, New York, and by webcast.

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

Robert B. Catell, Chair (by video conference from New York)

Jay L. Gottlieb, Vice-Chair

Vincent A. DeIorio, Esq., *ex officio*

George F. Akel

Also present were Authority Members Roger B. Kelley, Parker D. Mathusa, and Elizabeth W. Thorndike, Ph. D.

In addition, Robert G. Callender, Vice President for Programs; Jeffrey J. Pitkin, Treasurer; Hal Brodie, Esq., General Counsel; Mark B. Mitchell, Director of Internal Audit; Jacquelyn L. Jerry, Esq., Deputy Counsel and Secretary to the Audit and Finance Committee; and various staff of the Authority were present.

Mr. Catell, Chair of the Committee, called the meeting to order. Mr. Catell noted the presence of a quorum.

Mr. Catell then stated that the first item on the agenda concerned the approval of the

minutes of the one hundredth meeting of the Committee held on June 16, 2008.

Whereafter, upon motion duly made and seconded, and by unanimous voice vote of the Committee members present, the minutes of the one hundredth meeting of the Committee, held on June 16, 2008, were approved.

Mr. Catell stated that the next agenda item concerned a report on the Authority's financing program. Jeffrey J. Pitkin, the Authority's Treasurer, reported that since June 2008, staff has worked with New York State Electric & Gas Corporation ("NYSEG") and Rochester Gas and Electric Corporation ("RG&E") to refinance various auction rate securities.

In July, three series of NYSEG bonds, totaling \$174.5 million, were converted from auction rate securities to weekly rate bonds. NYSEG estimates it will have an annual savings of approximately \$3.5 million as a result of the three conversions.

NYSEG has also started participating in its own auctions for two series of auction rate bonds. As a result of these actions, NYSEG has purchased a total of \$70.7 million of the total \$100 million outstanding. Although this is a stopgap measure, NYSEG estimates that, compared to what it was paying for failed auctions, it will save \$3.7 million annually as a result of participating in the auctions.

RG&E has also started participating in its own auctions for two series of auction rate bonds. To date, RG&E had purchased \$22.7 million of the total outstanding \$44.4 million. Although this is also a stopgap measure for RG&E, the company estimates that, compared to what it was paying for failed auctions, it will save \$1.3 million annually as a result of its participation in the auctions.

Both companies are analyzing their options for permanently restructuring their auction rate securities. Neither NYSEG nor RG&E believe that the auction rate market will be a viable market in the foreseeable future.

In addition, various investment firms have entered into settlement agreements with the State's Attorney General concerning such firms' roles in the auction rate market. These large investment firms have agreed to purchase auction rate securities from certain classes of investors, at par, thus allowing these classes to exit the auction rate market. Staff anticipates that this will result in alleviating concerns expressed by some individual bondholders that the failure of the bond auctions has prevented them from liquidating their investments.

In response to an inquiry from Mr. Catell, Mr. Pitkin indicated that the Authority does not expect any adverse effects with respect to its bonds solely due to the recent issues facing Merrill Lynch & Co., Inc. and Lehman Brothers, Inc.

Mr. Catell said that the next agenda item concerned a report from the Director of Internal Audit, Mark B. Mitchell. Mr. Mitchell reported on the status and preliminary results of the entity-wide invoice payment process review, as well as other recent internal audit activities.

In accordance with the fiscal year 2008-09 internal audit plan, Mr. Mitchell said he has been conducting a disbursements review of the Authority's invoice payments made during the last two fiscal years. The audit is substantially complete and was conducted in two phases. In the first phase, Dorfman-Robbie, CPAs, P.C. ("Dorfman-Robbie") used computer analysis techniques to analyze all of the Authority's invoice data from the prior two fiscal years, approximately 40,000 transactions, to flag certain patterns and potential anomalies. This phase generated approximately two dozen data files, which Mr. Mitchell is analyzing with the assistance of the Authority's Finance staff.

As part of phase II, a data file was analyzed to determine the validity of payments the Authority has made. For example, one file listed paid invoices in sequential order by payee. This approach, according to Mr. Mitchell, provides a way to possibly detect an inappropriate set of payments. More than forty vendors from this one file were examined and Mr. Mitchell said he did not find any invalid vendors or any invalid transactions.

A different data file containing several hundred entities that had received two or more payments for the same dollar amount was reviewed. After eliminating routine monthly payments that were to be expected, a sample of transactions were tested and Mr. Mitchell said all payments were routine payments made in the normal course of Authority business.

The Authority had never used the accounting system in this manner in the past. Thus, Mr. Mitchell said some difficulties were encountered in obtaining a complete set of data from the Authority to be analyzed. This caused an eight-week delay in Dorfman-Robbie's ability to produce the data and to provide it to Mr. Mitchell for further analysis. As a result, the final draft report is about four weeks behind the schedule established in the internal audit plan. The preliminary version of the draft report will be provided to management in the next few days. A final draft report will be issued after management has had an opportunity to consider the findings and recommendations and to provide Mr. Mitchell with any comments they may have. The report will be considered final and complete following a written response from the Vice President for Programs.

Dorfman-Robbie has assured Mr. Mitchell that the Authority's experience with this audit was not out of the ordinary for conducting this kind of an audit for the first time.

The preliminary results of the audit have been positive. After analyzing transactions for several weeks, Mr. Mitchell said he has not found any obvious errors, irregularities, or duplicate payments.

Though the results have been positive, a handful of transactions are still under review. Mr. Mitchell said that the data examined was consistent with a well run, well organized entity that has a good set of internal controls. However, the Authority relies upon contractors to implement many of its programs and to handle many of its financial transactions. Mr. Mitchell said his audit does not make any determination with respect to the operation of controls in those situations. Therefore, Mr. Mitchell plans to examine a few transactions more closely with program staff in

order to obtain a better understanding of the transactions and whether the payments made were appropriate. Mr. Mitchell said he does not expect to find anything extraordinary and will only provide an additional report on this matter to the Members if anything unusual is discovered.

Mr. Mitchell noted that although it was not directly within the scope of the audit, there were a number of recommendations that were made concerning the administrative practices associated with processing invoices. For example, one recommendation is that the Authority store all records that contain personally confidential information in a more secure manner. Also, during testing, it was noted that the invoice numbers used in the accounting system are not uniform. This occurs in cases when staff receives an invoice that does not have an invoice number, such as bills from bond counsel or an incentive payment for participation in an energy efficiency program. In these instances a random, non-sequential alpha-numeric invoice number is assigned to the transaction. Another recommendation is that the new financial reporting system ("Financial System") configuration include the issuance of uniform, numerically sequential, invoice numbers.

Mr. Mitchell said that performing the audit through electronic means allowed him to analyze a larger number of transactions, identify trends, and target transactions for further review. Additionally, he was able to gain initial insights without waiting for the cumbersome process of collecting documents by traditional means.

Mr. Mitchell said he believes the audit was a more cost-effective and more comprehensive approach than hard-copy document review. Mr. Mitchell said he also believes the review provides a higher level of assurance about the Authority's disbursements than previously available, and it also provides some lessons to the Authority that could improve the data design requirements of the new Financial System being developed.

Mr. Mitchell indicated that this will be the only report on the audit unless any significant findings are detected as the fieldwork and written report is completed.

Mr. Mitchell continued his report by stating that the internal audit of the Authority's Information Technology ("IT") controls has begun. The accounting firm of KPMG, LLP ("KPMG") was selected for the audit and a kick-off meeting was held last week. The Authority's representatives at the kick-off meeting included David Young, Manager of IT, and the Financial System implementation team.

While developing the scope of work for the IT controls audit, it was determined that it would be more efficient to combine the IT security controls review with the design review of the Financial System, splitting the work into two phases. Phase I will be a review of certain components of the Financial System design, as well as an evaluation of the IT security controls and the IT internal controls. Phase II will test the controls evaluated in phase I. KPMG plans to complete phase I by the end of October 2008. Phase II will commence in January 2009 and will be timed to coincide with the testing and implementation phase of the Financial System.

The agreement between KPMG and the Authority is still being negotiated and this current timetable is subject to KPMG's acceptance of contract terms quickly. Additionally, the timetable is subject to the cooperation and responsiveness of the Financial System implementation team during the audit fieldwork. Mr. Mitchell said that KPMG has assured him that they will be considerate when making requests for information in order to minimize the audit's impact on the Financial System implementation.

Mr. Mitchell said he will review the adequacy of the work performed by KPMG, including whether the information obtained by them is sufficient to afford a reasonable basis for the conclusions reached. Mr. Mitchell said he will also review the resolution of any significant exceptions or other unusual matters. Mr. Mitchell believes that, through this audit, KPMG will provide him with the knowledge it gains about the Financial System and the Authority's IT controls.

With respect to the status of the fiscal year 2008-09 internal audit plan, Mr. Mitchell said his work on the entity-wide payments audit was delayed by approximately four weeks by

unforeseen technical issues, but is anticipated to be completed in the next few weeks. Mr. Mitchell said the Multifamily Performance Program audit should be concluded in December 2008, just one month behind schedule.

With respect to the IT controls audit, under the current schedule, the phase I reports should be submitted to the Authority by mid-November 2008, approximately six weeks ahead of the scheduled report date. Additionally, if the Financial System implementation project adheres to its current schedule and KPMG adheres to its phase II schedule, the phase II reports should be submitted to the Authority by the third week of February 2009, approximately one month ahead of schedule.

Mr. Mitchell concluded his presentation by stating that the internal controls review of the Renewable Portfolio Standard Program is the last audit included in this year's internal audit plan. Although the audit may not begin this Fall, as originally planned, Mr. Mitchell said that he will complete it before the end of the current fiscal year, by April 2009.

Mr. Catell stated that the next agenda item was a resolution to convene in executive session for the purpose of discussing matters involving a personnel matter.

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

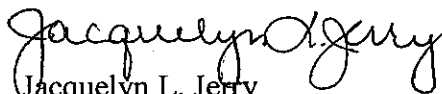
Resolution No. 339

RESOLVED, that pursuant to Section 105 of the Public Officers Law, the Members of the New York State Energy Research and Development Authority shall convene in executive session for the purpose of discussing the employment history of a particular person.

Thereafter, Mr. Catell reconvened the meeting in open session. Mr. Catell announced that no formal action was taken during the executive session.

Mr. Catell said that the last item was other business and he asked if there were any other matters the Members wished to discuss. There being none, 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 "Jacquelyn L. Jerry".

Jacquelyn L. Jerry
Secretary to the Committee

NOTICE OF MEETING AND AGENDA

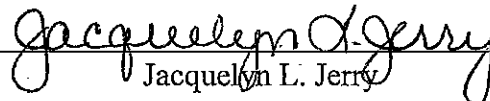
September 3, 2008

TO THE MEMBERS OF THE AUDIT AND FINANCE COMMITTEE:

PLEASE TAKE NOTICE that the one hundred first (101st) 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, 10th Floor, New York, New York, on Monday, September 15, 2008, commencing at 12:30 p.m., for the following purposes:

1. To consider the Minutes of the 100th meeting held on June 16, 2008.
2. To receive a report on the Authority's financing program.
3. To receive a report by the Director of Internal Audit.
4. To consider a motion to convene in executive session for the purpose of discussing the employment history of a particular person.
5. To transact such other business as may properly come before the meeting.

Members of the public may attend the meeting at either of the above locations. The meeting is also available through webcast at <http://www.nysERDA.org/governancemeetings.asp>.



Jacquelyn L. Jerry

Secretary to the Audit and Finance Committee

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