

LONG ISLAND POWER AUTHORITY

Legislative Oversight Committee

Verbatim Minutes

A regular meeting of the LIPA Oversight Committee of the Suffolk County Legislature was held in the Rose Y. Caracappa Legislative Auditorium of the William H. Rogers Legislature Building, 725 Veterans Memorial Highway, Smithtown, NY 11788, on April 11, 2011 at 1:00 P.M.

Members Present:

Matthew C. Cordaro - Co-Chair/Electric Utility Expert
Sheldon R. Sackstein - Co-Chair/Energy Expert
Peter G. Schlussler - Electric Utility Expert/Secretary
Irving Like, Esq. - Energy Expert
Joseph Schroeder - Energy Expert/Suffolk County Legislature
Fred Gorman - Nesconset Sachem Civil Organization

Also in Attendance:

Scott Hempling, Esq. - Executive Director/National Regulatory Research Institute

Verbatim Minutes Taken By:

Lucia Braaten, Court Stenographer

Verbatim Minutes Transcribed By:

Kim Castiglione, Legislative Secretary

(THE MEETING WAS CALLED TO ORDER AT 1:09 P.M.)

MR. CORDARO:

Let's get started. We don't know if we're going to have anybody else showing up, but we've got the essential participants here. The primary purpose of this meeting today is to hear from Scott Hempling, who's an attorney. He's Executive Director of the National Regulatory Research Institute. There has been some correspondence between Scott and Joe Schroeder and Irving Like relative to the kind of information that he could provide this committee, and the light he can shed on a few major issues. Scott's been kind enough to at least put together an agenda here to sort of guide his presentation and discussion. We're going to allow him to begin, and at different points in his discussion that cover major topics, we can chime in with questions and perhaps ask for some expansion of some of the things that Scott talks about. So with that, why don't we just give the floor to Scott and let him -- let him begin, and we'll see what direction that takes us in.

MR. HEMPLING:

Good afternoon, gentlemen. Thanks for giving me this chance to share my thoughts with you. I was last here 13 years ago during the last effort to bring accountability to electric production and delivery in Long Island. So I'm glad to be here, but sorry that you still need help. I am an expert, I suppose, on the practice of regulation. The National Regulatory Research Institute is funded by the 50 state regulatory commissions to help them do the best possible job you in utility regulation. So in the course of that experience over the last five years and in my prior 16 or so years advising and representing the regulatory commissions, I've probably been inside or before as a litigant, an advisor or an opinion writer, probably 20 or so different state commissions and am pretty familiar with what works and what doesn't in terms of different forms of accountability. So my purpose today is to help you think through forms of governance, standard setting, and regulation so that you can make the best possible decisions for your Island.

I'm pretty ignorant of the specifics of Long Island and LIPA. I last perhaps had a high water mark familiarity 13 years ago when I was here representing the County Legislature in litigation over LIPA, but I've not been involved in your detail since then. So asking me questions about the specifics is unlikely to get productive answers, but I hope I can help you structure your own thinking about these topics.

So what I plan to do is discuss three separate areas. And as I've said on this first page, if our purpose is performance, then you need three things. You need regulation, you need standards, and you need governance, and I'd like to talk briefly about each of these, pause after each section and there can be commentary and discussion, and then we'll move on to the next piece. I figure two hours is probably your anatomical limit for something like this. If it goes on longer that's fine; shorter, it's also fine. My purpose is not to lobby you on anything, but to provoke your own creative thinking and give you the benefit of my experience and do some back and forth in that regard. So thanks, again, for the opportunity to do this.

It says on the first page that regulation, its purpose is to establish standards and then assign consequences. The real purpose, the underlying purpose of regulation is to align the utility's behavior with the public interest. If that's the purpose of regulation, aligning behavior with public interest, then self-regulation is logically impossible. You can't expect a single entity to regulate itself. It has to be done by an outside entity, something independent of the utility.

Now, the second part of this tripod is standards. Standards need to be proposed, imposed, absorbed and then exceeded. Proposed by independent experts, imposed by the regulator, absorbed into the utility's culture and then exceeded by the utility's leaders and its employees.

Governance is the third part. It means governance of and by the utility and that governance needs to be designed to satisfy the standards that are established by regulation.

So those are the three things, regulation, standards and governance that you have to have in place to produce performance. So what I'd like to do now is delve into a moderate level of detail on each of these and pause for discussion after each one and see what you all think.

Let me start with successful regulation on the next page. I've divided this into two categories. One is infrastructure of regulation and the other is the practices of regulation. But I want to reemphasize for a second thinking about governance without regulation for me doesn't work. You can't govern without standards that are set by somebody outside.

So here's what you need for successful regulation and I've seen plenty of unsuccessful regulation, only rarely have I seen successful regulation. I've listed the seven things that I think are most important skill sets. That means the diverse skill sets reflecting each performance area. So in your own thinking you're asking yourself where do I expect this utility to perform, whether it's outages, whether it's innovation, whether it's adaptation of new technologies, whether it's pollution control, whether it's communications with the public, whether it's finding the most cost effective way to do things. Each of those requires different skill sets and those skill sets have to be matched within the regulatory infrastructure.

Pay. Sufficient pay scale to attract to regulation the equals of the utility managers. I may be swimming upstream on this one because everybody wants to cut budgets, cut public employees, cut pay scales, but I can tell you from being on the inside of so many regulatory commissions that the inferiority complex that accompanies inferior pay is so deeply embedded that there's no hope. And if you were a utility executive, and some of you have been, you don't want to be judged by somebody who's not your equal. You don't want to be judged by somebody with a Bachelor's Degree in economics if you're the guy who is responsible for operating a nuclear plant. You want your equal judging you if you want to be treated fairly, and that doesn't go on in regulation and pay is a big reason.

Quantity matters, too. You need a base staff that's large enough to be both proactive and reactive. You really need twice the staff that most people think. The typical regulatory staff is usually reactive to what's been proposed because they have a statutory obligation to process the cases that are presented by the utility. You use your whole staff to react, you have nobody thinking independently, nobody asking when they wake up in the morning what's my vision for the regulatory results here. They're only reacting to somebody else's self-interested proposals. So the quantity of staff matters.

Leadership. Without talking in a way that's going to get me fired from my current job, because I'm paid by commissioners, they write the checks. The commissioners should be expert in regulation, they should be undistracted by other career goals, they should be politically secure enough to assign consequences, and they should exemplify the key attributes of effectiveness which for me are purposefulness, education, decisiveness and independence. That's the leadership of these commissions. I've often seen combinations of weak staff and strong commissioners; doesn't work. Weak commissioners and strong staff; doesn't work. Weak commissioners and weak staff; really doesn't work. You need strong commissioners, strong staff. You need them both and I see them only rarely.

Now, the fifth item is a little obscure. It says consistently among multiple boundaries. What I mean here is that the boundaries of the regulator's authority have to match the boundaries of the utility's activities and any effects of those activities. One of the options we'll talk about later is a Long Island only regulatory authority. The logic of that option depends on whether the effects of

Long Island decision making stay within Long Island, because if they don't, you're going to be in the business of exporting your harm to some other county or some other part of the state, and that's not going to fly politically. So before we get overly excited about a Long Island only solution we have to ask whether there are Long Island activities that could affect people outside the County, outside the Island.

Sixth part of the infrastructure is accountability. Regulation has to be accountable. That means accountable to whom, to anybody who's behavior you're dependent on for your own success. So you have to be accountable to the Legislature, to the consumers, to the utility, to the financial community, and ultimately to the courts. With the risk of stepping on toes here, it seemed to me the problem I had is your outside counsel, 13 years ago, was that when I tried to take LIPA to court for its poor performance and poor decision making processes, the ability of the courts to review LIPA's decisions was almost zero because the statute made them virtually unaccountable to the court system. I can understand the impetus for that type of legislation, but the outcome was that there was no way to turnaround a poor performance through a court review. So regulation, beside setting standards, itself has to be accountable to the various sectors that make for success.

Why did I list the financial community? Because you're not the ones or the regulators aren't the ones that supply the billions that are necessary to keep a company running. We're still in a capitalist system, and so regulation has a reputation with the financial community and that reputation has to be a good one. That means that when things cost, regulators have to impose those costs on the consumers in a responsible way whether they like it or not if they want financing for the things that they need. So accountability is to a variety of sectors.

The seventh -- this is perhaps regulations biggest weakness today. Alternatives to the incumbent. Alternatives are essential to avoid the moral dilemma of too big to fail. I can't tell you the number of times I've had regulators tell me, "Well, Scott, you're right, the consequences that we ought to be imposing on this utility are quite severe and they're deserved, but if we do that we're not going to have a utility. The utility is going to weaken or the financial community is going to say we're quote inhospitable closed quote to capital and so we just can't impose the type of accountability that you think we should." And so it's as my old colleague Peter Bradford used to say, the regulator ends up saying if you do that again we'll clobber you, but they go ahead and do it again in some different form and nobody gets clobbered. There's just way too many examples of this.

I'll give you another one. Back in the '80's, Consumers Power in Michigan tried to convert a nuclear plant into a gas plant. You're probably familiar with this, Dr. Cordaro. It was a double catastrophe. So the commission found about three billion dollars of cost were imprudent, and the way the law works is you don't put imprudent costs in rates. That's what shareholders are there for. Well, the commission found that if it had disallowed that three billion dollars the company would just sink, so they invented what regulators are good at inventing, which is a euphemism, it was financial stabilization rates, and they included all the imprudent costs.

Now, I ran into this 20 years ago. I ran into the utility's director, his chief staff, the Michigan Commissioner, said, "But John", his name was John {Abramson}, "how could you possibly put imprudent costs in rates?" And he said, "Scott, sometimes you've got to put your principals aside and do what's right." And that's the situation you find yourself in when you have no alternatives, that's regulations weak spot.

A few thoughts on regulatory practices and then we'll take a pause for your comments and questions. Those are my seven thoughts on infrastructure.

Practices. Nothing profound here. The first is transparency. All decisions need public, written explanation in an evidentiary basis that includes a comparison to all feasible alternatives. Decision

making ought to be agonizing until you make your decision, and it means you examine alternatives, you explain yourself. Not all regulators do that and not all utilities do that without inducement by the regulators.

Second, performance reviews. I know some of you have talked about management audits. I prefer the word performance review because, it is a minor thing, the word audit tends to connote a green eye shades just matching dollars to invoices. A performance review is deeper. It's emersion in the company's practices, it compares those practices to best practices. The purpose is not only cost accounting, but finding the best practices in all lines of work.

And the last practice for regulation is cost accountability. And I've discussed here two types. One is expenditure accountability, where the focus is cost effectiveness over the long run, and the other is what I'm calling generational accountability or pay-as-you-go, always matching costs to benefits within the same generation of ratepayers. You can't borrow to cover fuel costs when the fuel's being consumed today. That's just shoving costs on to a future generation. We're great at that in politics; we shouldn't be doing it in regulation, but it happens. You can have exceptions from time to time, minor, temporary and short-term, but what I mean by this concept of cost accountability in the generational sense is if you're going to make a costly decision, be sure you have the political wherewithal to support it with your current electorate, because otherwise you are being dishonest.

So I'll pause, we can have a discussion of whatever type you'd like on this first area, successful regulation. The premise here is that you'll come to a decision, as we'll discuss later, where you don't only have governance, but you have regulation overseeing that. And, Dr. Cordaro, back to you for any questions or comments.

MR. CORDARO:

Well, I'm going to yield to the committee initially. I have a number of reactions. I think just in general, an immediate response, we're faced here with a situation of no regulation as far as LIPA's concerned. You know, it's a vacuum relative to regulation, and that's the starting point. There have been efforts by the New York State Legislature to involve the New York State Public Service Commission in overseeing LIPA. The most recent version of that is a bill, which was passed by the New York State Senate, which calls for LIPA to have any rate increase above 2 1/2 percent to be approved by the Public Service Commission. There's a companion bill in the Assembly, which is quite similar.

Interestingly enough, at a hearing that was held last week by the New York State Senate Energy and Telecommunications Committee, the New York State version of the bill was discussed and, in fact, the Chairman of the Public Service Commission appeared at that hearing to address the PSC's role. And the interesting thing that I came away, and Shelly was at the same meeting and was able to observe the same things. The interesting thing that I came away with was that the Public Service Commission was, at least in its current state of affairs with the limited resources, very reluctant to jump into the fray as far as regulating LIPA. First of all, claiming it didn't have the authority to do that because of the LIPA statute, and also that it didn't have the resources to do that.

Now, interestingly enough, and I was amazed to find this out last week, first of all, private utilities pay for regulation through an assessment that they funnel through -- in rates. They collect in rates and then pass on to the government to pay for the PSC's operation. The interesting thing that came out of this hearing was that a similar assessment has been made for LIPA since its inception and never funneled to the Public Service Commission for the purpose of regulation, because the Public Service Commission didn't have the authority and it wasn't performing at a regulatory function. But that that assessment, which continues to be collected today, finds its way into the General Fund at the State level. So it just -- it was interesting to find out that LIPA customers had been paying for regulation in effect, but not receiving regulation on the part of the State.

But one thing became clear at the hearing from the remarks of the head of the Public Service Commission, was that the Public Service Commission needs to be vested with the authority to, in fact, regulate LIPA, and also has to obtain resources to do that. The reaction of the State Senators present there was a little bit of -- in surprise, because they thought that what they were doing by passing a law, which called for regulatory review of LIPA rate increases for 2.5 percent, was an adequate step to take to bring LIPA into a situation where it would have oversight in that its rates would be regulated. The PSC claimed at the hearing, however, without the authority and the resources they couldn't perform that function, they just merely couldn't be handed a LIPA rate request, which exceeded 2.5 percent, and be expected to do the work necessary to determine the validity or merit of such a request.

The thing that was encouraging for me was that the reaction from the State Senators was that they were inclined to maybe go back and look at the legislation again, to possibly broaden it, so that it would provide the PSC the authority to do what we're asking, what we're all seeking them to do, or in the broader sense to achieve regulatory oversight of the Public Service Commission. But that's the latest news, I mean, as far as -- I think the hearing was held last Thursday, but that's the latest news on that front. I just wanted to bring everyone up to date on that. Maybe Shelly has his own personal observations he wants to make about it.

But I agree with everything you say in what successful regulation is. I think, just looking at the Long Island situation, probably the only feasible way for it to happen, because of all the requirements, would be for the Public Service Commission, and this is my personal view, to have -- be given the authority to, and the resources, to regulate LIPA. I think to start from scratch, and we may talk about that a little bit more later, with a Long Island entity, although desirable, would be a very monumental challenge from the standpoint of obtaining the resources to do that, and putting the organization in place to actually accomplish it.

So on a short-term basis I think the only practical way to maybe achieve a lot of the objectives that you have set forth here in the regulatory area is to be able to call on a professional entity, commission, as it's set up in New York State, to step in and perform the same regulatory function for LIPA as a public utility, a state authority, as it does for the private utilities. Unfortunately, LIPA really doesn't have transparency, as you call for here, as far as practices. As I said earlier, there is no regulation to begin with, but then beyond that, there is very little transparency at LIPA. There has been no performance review or management audit, even in view of all the -- of the snafus which have taken place recently with hundreds of millions of dollars in overcharges, borrowing money to actually pay for fuel costs, high fuel costs, rather than build it into rates. There has been no performance review or no way of having LIPA justify its actions in those regards. So that is sorely missing and needed.

But I've talked a little bit too much. Let me just throw it open to anyone else on the committee who wants to talk about this phase of your presentation.

MR. GORMAN:

I'd like to ask you a question, Scott. What do you think about a Long Island regulatory authority? Do you think it's possible, do you think it can be done? There's a lot of smart people here on Long Island. There's a lot of people that have, you know, worked in this utility. And certainly I'm sure that we could find the right kind of people to get it done. It's whether or not we can find the funding. Do you think it's cost effective? Do you think it's something worth pursuing? Because Long Islanders, if anything, really want to have some sort of control about what's happening here.

MR. HEMPLING:

Thanks for the question. There are pros and cons to having an Island specific regulatory authority. I don't have my mind made up about it obviously because I just got here, so I can just give you a

list of what I think the pros and cons would be. To some extent I was going to cover that in phase -- the last phase of this conversation, why don't we take it up now.

There is something unique about you on Long Island relative to all the other utilities in the State. You know that uniqueness better than I do. You've got this double debt you've got to carry for current plant and for the plant, that never operated plant. You've got a long history of lack of accountability here, which isn't matched by any of the other utility regions in the State. You've got your own separate economic issues relative to the defense industry and your geographic location. You've got, let's see, as far as I can tell, no plan for the future in respect to fuel mix, customer accountability for monitoring their own consumption practices, rate design, none of the innovative practices that progressive utilities around the country are getting implemented here. So one could argue that the, pardon me, sad state of affairs that you find yourself in warrants a unique regulatory solution, which is your own regulatory authority. Those are on the positive side.

On the negative side, I would agree with Dr. Cordaro that starting from scratch is never as easy as working off a model that works. That's assuming your evaluation is that the PSC model that you have does work, and I'm not going to venture into a discussion here about what I think of the PSC, you know, they are what they are. But to the extent there isn't trust in Long Island of PSC decisions then that's a negative associated with relying on the PSC. A positive is that they're there. As Dr. Cordaro pointed out, they have an economics area, and an engineer area, and they have lawyers and they have procedures and they have commissioners, and it's all there. The problem is if you don't agree that their culture is proactive enough and creative enough and hard driving enough to make the significant changes and accountability that are necessary, then a PSC approach is not a good approach.

What I would do at this stage is keep thinking about those two options and keep lining up all of the pros and cons. The funding actually, sir, doesn't concern me as much. People need to pay for regulation or they're going to pay more for the absence of regulation, so whether you use the tax method or the assessment through rates method, everybody pays for regulation. So I guess I would say one advantage, one advantage of starting your own regulatory authority here, just to move back to the other side of the ledger, is new State Law. You can invent your own pay scale, you're not tied to the current Civil Service approach, which I think pushes down salaries rather than raises them to where they belong. You start a new culture and you come up with an assessment method that's making your own ratepayers pay for regulation. So that's a benefit on the Long Island only side. But I wouldn't know how those factors all would balance out until we continue to pursue them. Neither one is going to be a perfect solution. I hope that answers your question.

MR. GORMAN:

Actually, it does and you were extremely helpful. You know, my opinion, looking at the list that you did, because I took the time to write it down, it seems to me much stronger on the side of doing your own. That's my own reading of what was said. Very interesting, very helpful.

MR. HEMPLING:

I think what you want to do is keep studying it. I wouldn't want you to infer a particular solution from this short conversation. I will tell you that it is very unusual, although not unprecedented, to have a regulatory authority for a particular area within a state that's distinct from the statewide regulatory authority. It's not unprecedented, but it would make news. That doesn't mean it's good or bad.

In Louisiana the New Orleans City Council is the local regulator for the investor owned utility company that serves New Orleans. And then there is any number of situations with respect to municipal systems where there would be a municipal regulatory board that is distinct from the municipal company, but those are still in a minority. So you'd be breaking some barriers.

MR. GORMAN:

I think what you have to say is wonderful and very, very helpful.

MR. HEMPLING:

Thank you, sir.

MR. GORMAN:

I understand what you're saying. Nobody's going to make a decision based on just bullet points.

MR. LIKE:

I have a follow-up to Dr. Cordaro's comments. On the issue of regulation, I wasn't at the meeting that he described, however, according to the newspaper reports, LIPA's representative, Hervey, stated that PSC regulation would result in millions of dollars of extra charges to be paid by the Long Island Power Authority ratepayers. Question to you is, is that a credible statement, that the cost of regulation by the PSC exercising oversight would result in the perverse consequence of the ratepayers having to pay more than absent such regulation.

MR. SACKSTEIN:

Let me just step in for one moment, Irv. I think what Hervey was saying was that it would disrupt the bond community and would cast some doubt on the ability of LIPA to make decisions, and that would drive the cost of borrowing up. Is that what he was basically saying, Matt?

MR. CORDARO:

Yes.

MR. SACKSTEIN:

So it wasn't that, it was that the regulatory cost was going to be a cost that was going to drive rates, because according to Matt, and I'm sure you said that also, that that cost is already built into or buried in the LIPA rate currently, and now is finding its way somehow into the General Fund of the State of New York. So what Hervey was basically saying was it was going to drive the cost of borrowing up. I would disagree with him, because it just seems to me that the bonding authority, the bond houses would look at it and say "Well, now I have a second level of confidence". So, Irv, it may not have come across that way in the newspaper.

MR. LIKE:

Thanks, Shelly. That raises the implication that the bonding people look with hostility upon an authority that is not an investor owned utility, because if that's the reason they say the rates will go up, that suggests to me that the Wall Street would prefer to have an investor owned utility than a public owned utility, and would show its displeasure by charging higher rates. I don't know whether that's a credible assertion based on your experience.

MR. HEMPLING:

It's pretty disappointing to have such a one sided statement made on such a complicated topic. I don't mean the statement by you, I mean the statement by the gentleman that you're quoting. It also reminds me of the kind of statement that says if we cut our kids education we're going to save money; I guess you will this year. The premise of regulation, if it's done right, is that it improves performance. If it's done poorly, it can raise the cost of doing business. I'm sure you all -- anybody's who's been in business, and I've been in business, you're a lawyer, any one of you have been in business, the cost of poor regulation can exceed the benefits, so it's best to be humble. In fact, the great Alfred Kahn, his famous quote from the beginning of his treatise, the Economics of Regulation, said that you need to get the best possible mix of an inevitably imperfect regulation and an inevitably imperfect competition.

In any event, there are ways to discuss the question with the bond community so that you have some empirical facts on which to base a judgment. I'm not sure this gentleman had that conversation. For example, and I point this out later on in our conversation, recognizing that holding a nonprofit company accountable requires a different set of measures than holding an investor owned company accountable, is the first thing I'd be telling the bonding community. You know, you can penalize an investor owned utility by hitting its shareholders where it hurts. A nonprofit doesn't have shareholders. You penalize the company financially, it's just the ratepayers that are going to have to pay for it and you are just going to weaken the company. So as we'll discuss, there's other forms besides financial penalties.

The conversation I would be having with the bond community would start right there. This is not -- we're not talking about a public that's going to make the company weaker. It's a public that is committed to making the company stronger, and you can write your statutes that concerning governance and regulation, such that all the signals that need to be sent to the financial community about responsibility and acknowledgment that you're in a capitalist system, all those signals get sent. That's what I would be doing. You can't say the financial community won't have an effect on bond ratings, which in turn won't have an effect on the cost of capital. Of course it will; an irresponsible regulation from irresponsible sources has that effect.

So -- but to generalize about it, it doesn't work. So I don't want to be longwinded about it. It's possible to screw up regulation and have the cost exceed the benefits; it's possible to do it right. I've had executives say to me, "Thank God for regulators, they save us from ourselves". It's like an adolescent, it's nice to have limits so that you don't keep doing things you shouldn't be doing. A lot of people are glad for the speed limits when it's their kid crossing at the streetlight.

I can't generalize about it except to say that I think the answer, sir, would be more nuance than the one that was given. That was disappointing to have somebody sort of focus on the cost side and not on the benefit side. It shows me how primitive the conversation in New York State is at this point.

MR. CORDARO:

I just want to just inject a comment here. There are many public utilities similar to LIPA throughout the United States that have some form of regulatory oversight, that actually have higher bond ratings than LIPA does. So, I mean, it's definitely possible to have that regulatory oversight and have very reasonable financial ratings so -- now, I think LIPA is getting their information from -- on a self-serving basis. LIPA has always resisted regulation and oversight. I think when the State Legislature was considering bills a year or two ago, and LIPA fought ferociously against the adoption of a bill that would call for PSC regulatory oversight. They -- they actually went out and solicited Wall Street, talked to the rating agencies. And, you know, I have had similar conversations as CEO of a public utility with rating agencies. And, sure, the rating agencies and the investment houses would love to have cart blanche of being assured that all costs would be covered without any limitation and that bondholders would face no risk whatsoever. I mean, that's the easy street. However, that's not reality in many respects. That doesn't happen.

Reasonable regulation produces a lot of benefits, as you say, and one thing that LIPA has overlooked, and I made this statement at the hearing last week, is the cost benefits of regulation. If -- you know, we recently had the situation where LIPA over collected \$231 million from its customers because it used a flawed method to estimate lost and unbilled energy, energy losses over the system. If regulatory oversight had been present and resulted in avoiding that kind of overcharge, right there and then you would have paid for any increment, assuming that there is some, any increase in cost through regulation from the savings of the regulatory process and being able to ferret out these situations where overcharges exist and are definitely possible. But LIPA has lost sight of that argument.

They're trying to take the, in my estimation, to take the easy road. It's just everyone feels that if they're their own boss they can do a better job with little interference from the outside. The unfortunate thing is, and as you may, you pointed that out in your initial remarks, it just doesn't work that way. You benefit from having someone looking over your shoulder and checking things twice. And it's almost un-American to have a situation where you have cart blanche with no boss and no oversight and no checks and balances. Even our -- even the United States system of government has its checks and balances built in. LIPA cannot exist without some form of checks and balances.

MR. HEMPLING:

Here's a more direct answer to Mr. Like's question. My observation, the financial community, and I've been in many hearings where I've communicated with them either by cross-examining them or in more informal dialogs, they like certainty more than they like uncertainty. They like consistency more than they like inconsistency. I've never heard somebody say that they're happier with no regulation versus some regulation. Every investor owned utility in this country is regulated in some way and all of the municipal systems are regulated in one way or the other. And what drives the bond ratings is the quality of the regulation, not its presence or its absence.

MR. SACKSTEIN:

Scott, are you familiar with the LIPA model in terms of how the entity is structured, how it functions? Do you have some familiarity? If not, Dr. Cordaro will bring you up to speed.

MR. HEMPLING:

I was familiar with it in '97 and '98, so I have a faint memory of how it's structured, or at least how it was supposed to be structured, yes, sir.

MR. SACKSTEIN:

How would you change that model, because it doesn't work. And, you know, by the way, I am also looking at something that I find incredible, and that is if we're collecting these charges from the ratepayers for PSC oversight or oversight, and we're not getting the oversight, then one could argue it's an additional tax on the ratepayers of New York -- of Long Island that is going into the General Fund of the State of New York, and I want my money back or I want my oversight. And, frankly, I would prefer local oversight because one of the things that the PSC Chairman had said was that they would not have a problem doing the work since the model that's followed in terms of rate structure is the same model that was utilized by the Long Island Lighting Company. Consequently, there must be any number of experts out there, albeit maybe some of them are retired, that would be able to shed some light on it.

I'd like to fix the broken model. The problem that we run into, and now I'm going to speak as a former LIPA Trustee, is this is a political playground. It is not run as a company. It is not an entity that's in there to be done -- to do the work of the people, unfortunately. I wish it was, because it started with Governor Pataki when he saddled us with the Shoreham debt and bailed out the shareholders of the Long Island Lighting Company. I've always wondered how many shares of Long Island Lighting Company stock sat in the hands of the New York State Pension Fund at the time that caused them to saddle us with that debt. But can we fix this broken model? Can we help to design something better so we can go forward? Because my biggest fear is that what's going to happen ultimately is all the money that we poured into this transmission and distribution system, which is what caused the benefit or the penalty that was put upon the ratepayers, because when we fixed the system the loss in the system decreased and they never adjusted for it, and that's really what happened. We spent over three billion dollars. Is that right, Joe, 3.6 some-odd billion dollars, roughly speaking, went into that system to make it gold plated. I don't want to lose it.

MR. SCHROEDER:

(Nodded yes)

MR. SACKSTEIN:

I was hearing rumbling in that room that says to me as a Long Islander we're going to lose not just that system, but the entity. It's going to go into some other big pot someplace else for somebody else to play around with the bond houses. It's just not a good system the way it's structured now. Can we fix it? And we meaning this body, this board, this Legislature. We've got an election coming up for a new County Executive. This is a moment of opportunity to, if we can set something in place, sit down with the candidates and see what their appetite is, because no one has ever, ever lost an election on this Island taking on the Lighting Company. And so this is a moment of opportunity. The election comes in November.

We need to get smart quickly. Can we do that? Can you help us? Can you guide us there? I mean, we can look at all these things we want to look at, but as I said to Irv earlier today, yeah, we can ask for elected board members, but elected board members of an entity that ceases to operate doesn't -- it's a hollow fight. I'd rather build a company that's really, you know, working in the best interest of the ratepayers of Long Island. My kids, their kids, and as you've said, future generations, and put something in place that makes sense, try and save -- save this thing.

MR. HEMPLING:

Concerning a model, what I'd like to do is reserve that conversation to the end when I've covered the other two areas, because the best model is going to be a combination of why is regulation effective standards and effective governance. So I think it would be better to address that final exam question after we have covered all parts of the course.

MR. CORDARO:

I was going to suggest the same thing. But before we move on to that, I think Joe has a question or two.

MR. SCHROEDER:

Scott, if you would. I just want to try to put some of this in context. How many states across the country would you say you've got regulatory experience in, you know, involved with the regulatory process.

MR. HEMPLING:

My present job involves all 50 of them, but in terms of being inside or in front of a commission, probably 20 out of the 50 I've had to practice before or practice within.

MR. SCHROEDER:

And elsewhere in the country, have you seen a model similar to the LIPA model in terms of no regulation whatsoever?

MR. HEMPLING:

Other than the Federal systems like TVA and Bonneville, the answer is no, and even those systems have some forms of accountability, although it's not necessarily a regulator on top of it. LIPA really did stand out in terms of its size, the extent of its past error and the absence of any current -- or oversight to address those errors. It really was outstanding.

MR. SCHROEDER:

Well, the LIPA arrangement includes some contractual review by the State Comptroller's Office. The Governor can activate a Public Authority's Control Board to review rate increases of greater than 2 1/2 percent or 2 1/2 percent and greater. Is there anything similar in the TVA and BPA

arrangement with whatever Federal oversight exists that even comes close to this arrangement?

MR. HEMPLING:

I'm not familiar enough with their governance situations to answer that question. We can comment or I will comment when I come to that context as to the sufficiency of this 2.5 percent rate review and a sufficiency of a contract by contract review. But the answer to your question is I don't have full information on that. There just is nothing precedented about the LIPA situation, either its history or its current set up.

MR. SCHROEDER:

So there's not a lot of working models that we could pattern after to marginally correct this regulatory deficiency without doing something more dramatic, like a complete PSC or a complete local oversight.

MR. HEMPLING:

I'm hesitant to use adjectives like radical or incremental. I'll just stick with the word substantial. I don't think there's a simple, direct, easy to design answer because you're completely absent of accountability, so something new has to be created. It doesn't mean there aren't models to choose from, and that will be the basis of my final section, is to see how you can piece together some features of different models that work. I'm starting with these criteria so that we can have a context for that.

MR. SCHROEDER:

Just one last question, if I might. The New Orleans model that you mentioned earlier, perhaps we'll get into this more as you address that subject later of local governance or local regulation, how successful is that model in your opinion, how well is it working there?

MR. HEMPLING:

It's such a unique situation, Joe, it's unique in the following ways. I don't want to drag you too much into that region, but New Orleans, the City of New Orleans is the smallest piece of a vast multistate holding company called -- now called Entergy, that includes major utilities in Texas, Louisiana, Mississippi, and Arkansas. And the small size of New Orleans relative to the huge size of that holding company makes it relatively non-influential over anything that goes on at the holding company level. That's point number one that makes it different from your situation.

Point number two is the city council on one day is going to be dealing with potholes and the next day it's dealing with the future of nuclear power, and you can draw your own conclusions as to whether that's, given what you know about local politics and then extrapolating to the city of Bourbon Street. You probably can start to ask yourself how successful it is.

What actually happens in New Orleans is they essentially contract out the regulatory function through a very expensive DC law firm, and the effectiveness of that law firm some people think is quite high in terms of taking a bite out of the Entergy system and bringing things home for ratepayers. So I can't tell you whether it's a poor or a good model, it's just that it's an expensive one and one that I wouldn't replicate that way here. I wouldn't want you to contract out your entire regulatory infrastructure, which is how they do it there. I happen to know the lawyers and they're good folks, but they are expensive.

MR. LIKE:

In point six of your infrastructure, accountability, you should be aware that the Supreme Court of Suffolk County, in a scholarly decision written by Judge Lifson, in a case brought by the Suffolk County Legislature against LIPA, held that LIPA was accountable as a fiduciary to the ratepayers and was forbidden to discriminate against any class of ratepayers. I think that goes to your comment

that accountability means accountability to the courts as well as to the Legislative Body that you mentioned. So we do have a judicial precedent. LIPA at first took an appeal and then withdrew its appeal. That became the law of the case. LIPA is accountable to the ratepayers as a fiduciary. In that case LIPA argued that they were immune from PSC review. The court brushed that aside and said, "No, you're a fiduciary". So we do have a platform for whatever we do in terms of determining the governance, future governance of LIPA.

MR. HEMPLING:

Can I ask you, this is news to me, but it's fascinating. The legal basis for the finding of fiduciary, was that it was a nonprofit corporation or what was the legal reasoning?

MR. LIKE:

I'll send you a copy of the opinion.

MR. HEMPLING:

Yeah. I would have to think personally about whether the notion of regulator as fiduciary, how that aligns with more traditional regulatory set ups, as I'll discuss later. I'm not overly excited about seeing the commission as a consumer protector as opposed to an entity that induces performance, but -- and that's one reason why fiduciary might differ from the traditional model, but it sounds like some very creative lawyering and judging went on, so I congratulate you.

MR. CORDARO:

One thing that I wanted -- because it relates to something that Joe said, is this conflict which existed -- which exists as to what possible regulatory oversight relative to rates exists at LIPA with respect to the PSC. Apparently, the LIPA statute is silent on the need for LIPA to go to the Public Service Commission to have any rate increase or rate increase of 2.5 percent approved.

MR. SACKSTEIN:

It does specify that.

MR. CORDARO:

However, the Public Authority's approval, the approval of the Public Authority's Commission, did insert that in the formation of LIPA that for any rate increase greater than 2.5 percent they had to go before the Public Service Commission. Now, apparently there is this disagreement or cloud which follows this, which has enabled LIPA to avoid this 2.5 percent hurdle in actions it's taken up to now, rate actions it's taken. I'm just reporting what I heard at the hearing last week. I haven't -- I haven't read the LIPA statute in a long time or the Public Authority's Commission approval of the LIPA organization, but this was part of a discussion last week.

MR. HEMPLING:

I was glad to hear you say -- I'm sorry. You were going to answer first, Joe?

MR. SCHROEDER:

I just wanted to maybe help clarify for you, if you're not entirely familiar with the local issues. LIPA has implemented many adjustments to its fuel and purchase power surcharge, and as you may be aware, there's an awful lot of things that go into that. It's, you know, that surcharge. Apparently, one of the things that LIPA has added to that are things that might more traditionally have entered into the rate base, such as construction of power plants, whether they be the ten fast track plants that were built to address peaking issues or the more recent addition of the Caithness Plant. They're not embedded in the base rates. And to the degree that those charges have not been embedded in the base rates, LIPA has not, either by manipulation or by happenstance, not incurred a 2 1/2 percent, or by their calculation implemented a 2 1/2 percent rate increase, and so any trigger that would have caused any outside investigation by the Public Service Commission was

never attained, and so, you know, whether or not it's part of the statute or not, they have successfully avoided that threshold.

MR. HEMPLING:

Well, you've pointed out one of several problems with this 2.5 percent business. Let me share with you some others, because my strong recommendation, if you'll permit me to give you one, is to get off of this 2.5 percent business and focus on performance. There's two problems with the 2.5 percent. One is that the focus is on rates only, and performance is not about rates only, it's about innovation, it's about customer responsiveness, it's about adopting best practices, it's about corporate culture, it's about many of the things we'll talk about when we come to the governance of the utility.

I can understand the origins of the 2.5 percent. Back in 1986 you were being walloped with major rate increases and the electorate was focused on rates, but utility management and utility performance is about more than rates. It's too narrow a platform on which to trigger regulatory review. The second concern I have with it is that if a company needs a substantial rate increase, that may be because of management problems and so it's already too late. At that point, especially with a nonprofit utility that you can't feasibly penalize financially, ain't much you can do about it. So to allow management problems to build up and then to trigger regulation only when they built up to a point that a rate increase becomes headline in magnitude, is unwise.

So that's why I was encouraged when Dr. Cordaro early in the comments said that people in the Senate were thinking about a broader approach. It's not about rates, it's about performance. There may be times when you want a rate increase. You probably should have rate increases coming up soon for reasons that the future matters. So to think about a rate increase as something bad as opposed to something that might be good is maybe a 1980's concept that we ought to replace at this point.

MR. CORDARO:

That's pretty much the description concept presented by the Chairman of the Public Service Commission last week at that Senate hearing. I mean, he made pretty much, using some different words, but pretty much the same observations you just made. And -- Senators were reacting like this is the first time they were aware of that. I'm sure a Legislator, when they consider a bill, will take the easiest path to put a bill in place that placates the public to some degree, and that's why it's maybe an easy thing to do, to put together something which limits rate increases or calls for oversight of certain rate increases. But you're absolutely right, by the time the rate increase proposal is there, it's too late to have -- to make a meaningful difference.

MR. HEMPLING:

And it invites the distortions of cost accounting that Joe pointed out. It's very easy to play with numbers. People do it when they pay their taxes, and they are going to do it when they file rate increases.

MR. CORDARO:

Apparently another thing brought up by the Chairman of the Public Service Commission, LIPA's accounting practices are different than the other utilities in New York State. And this introduces some difficulty from their perspective in regulatory oversight, just dealing with the accounting system itself. And we know from the recent news regarding overcharges and storm costs and things like that, that there are a lot of things hidden in the LIPA accounting system that are not very, very obvious that would be obvious if the accounts were carried forth in the same manner that the private utilities do their accounting.

MR. HEMPLING:

You make a strong point. For those of you who may be less familiar with this, there's something called the uniform system of accounts, and it's something that accountants within utilities and within regulation use, and uniform means uniform. We may often debate about the appropriateness of a particular cost level and fight about that, but nobody really argues a heck of a lot about where to find the numbers and how to record them. And to lose that consistency is one of the largest reasons why the absence of regulation is problematic here.

The reason for accounting is like the reason for law. It's to create predictability and accountability in people's behavior, and the word funny money comes to mind when people can record things different ways and then translate that obscurity into rates that can't be tracked. You're just heading down into a cave and people aren't going to know how to get back. Probably a good time for me to move on to -- sir.

MR. LIKE:

Before you do, if your thought is that the PSC should review as to performance, aren't you opening the door for the PSC to substitute its vision of what is in the public interest over that which LIPA had framed. And I'll give you an example historically. For years the PSC allowed the admission of construction work in progress of the Shoreham Plant into the rate base. That led to litigation. That policy was opposed by Nassau and Suffolk County to no avail because the PSC had the final say. So if in a given situation you went to the PSC and said, "What do you think of LIPA's performance?" The PSC might very well come down with a decision that would be not only contrary to LIPA, but contrary to public sentiment and opinion. How do you avoid the problem of bringing the PSC back into the picture when over the past it had a record that was not very favorable with the public opinion?

MR. HEMPLING:

Fair enough, Mr. Like. It's one reason why I wanted to leave the discussion of models to the end, so I had the full picture on the table. Again, what I've emphasized in this conversation is figuring out what the purpose of regulation is and then figuring out who the best regulator would be. I'm not here to advocate for the PSC or against it. By the way, we both won and lost cases. The key is to have a regulator independent of the entity running the utility, and a regulator, as we'll discuss, relatively independent of the public, too. That means you're going to win some and lose some.

I do think that what you're raising, though, is this. Sir, back to your point, your question. One of the advantages, I guess, of having a Long Island only regulatory authority is that you can start from scratch in terms of your precedence, rather than have your treatment swept up into whatever precedents are elsewhere in the State, because the PSC would want to have consistency among its various utilities, and if you don't like the precedent, then you'd want to create your own. So that would be an argument on the side of doing it here.

MR. GORMAN:

You can also regulate it in a way that the bondholders are going to be very appreciable of the fact that you're doing it. I just happen to know a little bit about bondholders and insurance companies and how they operate and what they look for. And as you said, stability is important. The fact that they're backed by all the assets of Long Island is equally important. When you put the State behind that, it's even more important.

You know, to get the kind of secure money that you can get from an authority like LIPA, it's not just like everything else that's out there. So you're always going to be able to get a good rate if you do it right. And, quite frankly, the quality of your bond negotiators has as much to do with it as your actual structures. The way you prepare things, the way you put them together, and the way you present them. You present an attractive package, they will come and buy it.

MR. HEMPLING:

There's no question that what Mr. Like said is correct, that there can be any number of situations, there's dozens of issues that come across the PSC's desk every year, and there can be any number of billion dollar decisions that you don't like, either because of the culture of the PSC is off or their way of balancing and investor interest where their customer interest is different from the way you would think about it, and that's a risk of getting before any regulatory entity, particularly, I guess, one that's distant from your locale. That's one of the things you have to trade-off.

I'm going to turn to my second major area. I said that there were three that I want to discuss. The first was regulation, the second and third are standards and then governance. So if you turn to page three of this short document I'll say a few things about standards. You can't regulate without standards. That's what the purpose of regulation is. It designs standards and then it holds the utility accountable to those standards. And it's my experience that regulation works best when it sets standards by finding for each performance area the best performing utility, whether it's in this nation or in this globe, and then replicating the practices here. And then performance reviews should be continuous, not once per decade or once per century in the case of your utility. Successful standards find the best performing utility, sets those standards and then monitors and reviews continuously.

Now, the second major aspect of successful standards are the consequences for failing the standards. And here's perhaps the most unsatisfying part of our discussion this afternoon. It's difficult, as I've already alluded to, to assign consequences in the nonprofit setting because you don't have shareholders to penalize. Performance pay, meaning executive pay and employee pay, is one approach, but there's really no substitute for having the right leadership and the right corporate culture.

I was just reading something over the weekend about organizations that line-up performance pay with performance, and the view is that you get people thinking about money all the time, and it's better just to have the right people who are passionate about the company and the cause, pay them above average, but forget about trying to reward them for particular outcomes, because then they'll distort to get to those outcomes. Now, Dr. Cordaro, you've been executive so you know what I'm talking about. Even my own small organization I've had to struggle with this. So I'm leaving you with some fairly unsatisfying conclusions that in this non-profit setting there have to be consequences, but I don't know what they're going to be, because it's hard to penalize the company as a whole. So those are my thoughts on standards.

They're absent now, right? There's no standards. You read through the legislation and it doesn't say anything about what you should be doing in terms of power supply planning or integrated resource planning or customer service or billing methods, or introduction of things like smart grid or relationship between gas usage and electricity usage. There's nothing in the statute, nothing in the rules that tells the public that LIPA is aiming at the highest possible performance, so you have zero right now, and better that you have something in place. And to connect it with my earlier comments, only a regulator will do that.

I guess there's some individuals among us, probably all the people in the room, who are pretty self-disciplined and set their own standards, but most corporations don't really work that way. In the competitive market the standard is set by the guy who's going to have your lunch if you don't perform, and under effective regulation the standard is set by the regulator who says do it or else, and that's what you don't have. Again, that's the reason why I'm concerned about the 2.5 percent business, because for me that's an irrelevant standard when it comes to performance. It just tells me the rates are going up; it doesn't tell me anything else.

MR. LIKE:

Not only are there no standards, but I believe in the statute LIPA is able to get Legislative immunity for its directors, and my guess is it may also have directors and officers liability that protects against liability in the event there's a lawsuit against any particular director. I'm not suggesting that that should be eliminated, but just to have the full picture.

MR. HEMPLING:

That's hardly uncommon. I have it in my own organization. I've got this little \$3,000 insurance policy I buy for, you know, the organization. I have one fellow who's, one commissioner who's independently wealthy. His great grandfather started a clothing store in Oklahoma, and he has so much money he said don't even ever talk to me about employee performance. I don't want any employees suing me. I said what about the \$3,000 insurance policy? He says the deductible is too high, because I was trying to save money on the premium. So it is not unusual.

In fact, as you may also know, Mr. Like, most utilities under State Law are themselves insulated from lawsuit for negligence, I mean, because otherwise rates would be too high. So the accountability has to occur and the standard setting occur through some other way, but I still think that is your biggest gap here, is no sense of standards, and that means the politics come in, whatever you can do to please customers in the short run is what drives the company rather than objective standards.

I'll turn to governance because I think that's perhaps the most important thing you want to talk about. And by governance here I'm talking about governance of the corporation. I've emphasized that regulation is distinct from governance. You need both, you need them both well. I don't think I've listed anything here, A through K, that's going to shock anybody here, but perhaps it will help you organize your own thinking.

A mission that succinctly states LIPA's reason for being. I'm not familiar enough with whether LIPA has a mission statement, and I know you can waste a lot of time getting the words right, but I think the question of why LIPA is here, the original purpose of a publicly owned, publicly accountable entity that's connected to the development of the economy, that's connected to the County's various needs, whether it be for schoolchildren or hospitals or economic development or pollution control, some statement of mission that binds everybody in the company together with the citizens of the Island is essential.

A vision is different. A vision describes what success looks like, what kind of populous, what kind of reputation, what kind of rate level, what kind of set of services, what kind of relationships with all of the stakeholders in these two Counties; that's what a vision is about, and I'm not familiar with one that LIPA has.

The culture and practice of self-critique that is continuous systematic and open. Perhaps you're already familiar with this book that I read several years ago when I took this job and I reread once a year. Chapter 9 is called Good Enough Never Is. State of perpetual dissatisfaction is what you want to have in a company that's going to serve the public.

Now, here's where I may be stepping on some of your toes with my own personal views. A board that contains a mix of expertise, technical, legal, managerial, community and communications. You want a board that reflects all of the perspectives and expertise that are necessary to hold the CEO accountable. E, the CEO and the chair must be separate individuals. I don't know why people still debate this. I'm the CEO of my little organization; I don't even have voting power. I'm an employee of the board, I sit on the board but I don't vote, and I'm certainly not the chair of the board. And so what we have in my organization and successful organizations is that the board is the power equal of the CEO. The CEO does run the show, not the board, but there's no CEO

controlling the board, no such thing, no such thing.

Utility employees should be staffing the board, not voting on the board. That's what I just referred to. I'm not sure how it works here. I note in many for-profit corporations half of the board is made up of internal high officials. That wouldn't be my cup of tea.

The board's purpose is to establish the mission and the vision and then hold the CEO accountable and defend the CEO's difficult decisions to the public. One of the advantages I have in my organization, all of my board members are commissioners, and I serve commissions, and when I have to make tough decisions because it's a bad economy and dues are down and I can't do study X or study Y, because I aim to have the trust of the board, I don't have to work the phones all the time, that's what the board does, to convince the rest of the community I'm making wise decisions with the resources that I have.

Now I perhaps is the most difficult part. The board needs to have a difficult combination of accountability to the public, but also insulation from the public. And I recognize that there can be different views about this, but if the board is not insulated from the public, the public is a short-term thinker. Just look at your election results. It doesn't matter which side of the, you know, which side of the party system you're on, we all know that politicians appeal to short-term interests. They talk about the long-term, but they often vote in the short-term. And we're all like that. And utilities are a long view operation. They need to think 50 years ahead, and they need to make the type of decisions that matter 50 years ahead, and those aren't always the decisions that the current electorate wants. You have to think very carefully about this difficult combination of accountability to and insulation. Insulation is probably too strong a term. It sounds like an impermeable membrane. I don't mean it that way.

Now, J is another comment that's mine personally and may differ with some of you yours. I think that the board's members should reflect perspectives and interests, like geographic, economic and social, but it should not recommend those interests, and I hope that is not too subtle a distinction. I'm on this -- our County Executive appointed a Working Group to deal with outages because our electric company, Potomac Electric, has had a lousy experience with outages during the lowest quartile. We have a County that's very computer intensive and people like their lights. We also have a lot of trees. People like their trees and they cause a lot of outages and everybody wants to blame the utility company. But I'm often concerned when one or two of my co-members say that they are there to quote represent the hotels or there to represent a particular neighborhood. They're there to serve the whole County, and when you're on the board of this LIPA, it seems to me you're there to represent and serve the whole County. You might bring a perspective, the low income perspective, the economist perspective, the defense industry's perspective, but you're there not to represent those interests and lobby for them, but to reflect them into the decision making.

And I also point out, I've learned this the hard way and I've lost some friends over this, that is in error to equate the consumer interest with the public interest. The consumer interest is one more self-interest along with the renewables and with the coal industry. Everybody wants something for themselves. You can look at consumers as oppressed and victims of monopolization and you can protect them, but that's serving the public interest and accountability. It's a fine line between protecting customers as victims and forgetting that they have a role, too, to play, which is to bear the costs as they come along prudently and to think about the future. So customers are entitled to cost effective management and transparent decision making, but they're not entitled to be happy with all of the outcomes. And that's my thought on it, and I recognize there can be different points of view about that.

And the last item I'll mention under this concept of governance is succession planning. That's just typical corporate thinking. I don't know whether LIPA practices it or not. But succession planning

starts the day you have a new leader and it ends the day you have the next leader, and then it starts all over again. It never stops. I've generally been concerned, again, I'm way on the outside, that when your -- LIPA is essentially a shell with all the real stuff being done by contractors and outside employees, that it's hard to find the joy in being a CEO of a company like that, and it must make succession planning somewhat challenging, but so be it. If that's going to be your model, you still need to be thinking ahead about who the next leader is. So those are some thoughts I wanted to share with you. I hope not too obvious on this question of governance of the entity itself. Again, governance is not a substitute for regulation. You need both. Yes, sir.

MR. LIKE:

Regarding paragraph J, where you referred to the board reflecting interests and you include geographic. Currently, the Long Island service area is Suffolk County, Nassau County, and a piece, I believe, of Far Rockaway. Geographically, would the representation be based on the doctrine of one man, one vote? When you're talking about how you choose and how you vote, that is an issue that's come up very often in regards to improvement districts and other situations other than municipalities, State and Federal. In the context that you're referring to here, is the one man, one vote doctrine applicable.

MR. HEMPLING:

That's a great question. It actually underscores why I'm not a big fan of geographic representation on your Board of Directors. What I really meant by geography is if there are geographic differences, differences in geography that make a difference in how you manage the utility and how you set priorities, that's what matters to me. But to think of a board where there's representation of various areas because they happen to be areas, seems to me distant, remote from the purpose of governance to begin with. So I'm somewhere else in this business of geographic representation.

MR. LIKE:

I envision political problems if you came out with a LIPA Board that was heavily weighted in favor of one or another county.

MR. HEMPLING:

I can imagine that would happen if there was a concentration of lawyers, economists and experts in one county. That could be difficult. I see that loud and clear, but I guess, again, being an outsider, and I apologize for being disagreeable, I think getting yourself into a notion that this is like a Senate or a House moves us too far away from the purpose of it all. Go ahead, sir.

MR. LIKE:

Well, I think there's enough motivated, qualified volunteers in all of the areas I've mentioned to come up with a pool of potential trustees or directors. But the question then becomes are you going to take into account the population in each of the ratepayer districts if you're establishing a number of districts?

MR. HEMPLING:

Yeah. Well, like I said, I wouldn't be establishing geographic districts. If it were me I would, like anybody who makes appointments, I would think with each appointment, like a Supreme Court appointment or a Public Service Commission appointment, I've got a variety of things from ethnic to race, right, to education to experience to geography and I would take them all into account, but I wouldn't emphasize one over another if that thing I was emphasizing wasn't what was most important to the management of the company.

Now, let me undercut what I'm saying. I understand, I think, the motivation behind formal geographic representativeness, and that is that people feel unlistened to, they feel underrepresented, and what they're accustomed to to solve their representational problems is

something that's geographic as a basis. I guess what I'm saying is you've had enough of the Suffolk versus Nassau stuff for as long as I've followed this whole thing, and to embed a continuation of that way of thinking into the structure of a new company I think would be -- I think -- I would hope there are better ways. I think you are absolutely right, but to end up with, you know, a bunch of people that know what they're doing, but they all come from Suffolk County, is a problem. So it means you work harder. It's like affirmative action. You work harder at finding the candidates that are going to satisfy those types of criteria.

MR. GORMAN:

There's more of a division politically, albeit elected officials but not with the people themselves. You'd be surprised. I said there's more of a division politically with people in power. Am I pronouncing my p's that loud?

MR. SCHROEDER:

Too close.

MR. HEMPLING:

I heard you so far, sir.

MR. GORMAN:

Yeah, all I'm basically saying is it's not the people, it's the government that's divisive that way, not the people. People in Nassau County, people in Suffolk County would be absolutely thrilled just to get something done. It's the governments that have to get their fingers in there that create all the problems.

MR. HEMPLING:

I figure people have in-laws, brothers, sisters across the County's and they manage to get along when the same baseball team playing the same game.

MR. GORMAN:

Absolutely. Basically, and I appreciate everything you've said. You've truly enlightened me I might add. Basically what I'm seeing here is you're making a suggestion that we seriously look at whether or not we should have a different form of regulation than we currently have now, because we don't really have regulation, and you are also suggesting that we follow a very strong governance model, and I think that's basically all that I'm taking away from this. I know that you're not trying to lead us in one direction or another, but you're giving us a lot of options and a lot of good things to consider. Have I missed anything?

MR. HEMPLING:

Sir?

MR. GORMAN:

Have I missed anything? Is there more than those two basic points?

MR. HEMPLING:

Well, you would have missed whatever I missed today, but I think you've captured what I have tried to do so far in this conversation, is to help organize the conversation along lines that will be productive.

MR. GORMAN:

Thank you. You were very, very effective.

MR. HEMPLING:

Thank you.

MR. CORDARO:

I just wanted to make a comment about your item I in your list, and part of my career I spent in the public utility business and, in fact, I was a trustee of the American Public Power Association for a number of years, traveled the country, and got a chance to observe the operations of most of the public utilities, municipal utilities, state authorities that function as public utilities. And one of the biggest problems I saw with respect to the public utilities sector was reflected in that item I, this combination of accountability to and insulation from the public. I couldn't find that anyplace, and maybe there is some idyllic location someplace that, in fact, that is the case. But one of the problems I found with public power is the difficulty in insulating it from the politics of decisions, and I always find that to be a concern.

In fact, having been in the private side of the business, too, the investor owned utility side, I was more comfortable with that model because you made decisions based on metrics, earnings, and reliability and factors meeting certain standards that would get you the rate increases necessary to provide for earnings and profitability, and in a pure sense that was easier. I mean, the objectives were very clear. In the public's side of the business, although the motivation is good, the underlying motivation and purpose to have the public have more direct control of an asset such as electric power, the difficult part of it was because of the nature of political appointments to utility boards, which is usually the case in public -- in the public utility sector, there was always the intrusion of politics and popular opinion revolving around political issues.

MR. HEMPLING:

You know, there's some -- I appreciate what you're saying. There's good politics and there's bad politics. You would never want to remove politics from regulation, because good politics is about making tough choices about what you're going to use society's resources for and who among society's members is going to pay the cost and who among society's members is going to get the benefits. That's good politics and it's why we have a democracy, it's why we have decision making processes and the transparency that goes with it. It's the bad politics that you are referring to, the short-term, the dog eat dog politics, the zero sum politics. The politics that says the only way for me to win is for you to lose. The self interest politics where somebody wants to put a power plant in his district so that he can get the employment and get the ratepayer somewhere else to pay for it. That type of politics is the bad politics.

The key, it seems to me, in trying to balance the independence from an accountability to the public is, frankly, stature. To have high stature, high credibility, trusted individuals who communicate, who spit out the bad news and explain why it's good for people, don't hide people from the consequences of where they are, and develop the type of communications and credibility that allows you to do that. You just have to think about your great leaders, whether it's Abraham Lincoln or Roosevelt or Martin Luther King, people that just told the truth. And one credibility that way, there's no substitute for that, and that's what you've been lacking, I gather, except on committees like this, right? If you could just transplant some of these great committees into the leadership of the regulatory infrastructure and the governance structure you would be great, the people are here. Something is keeping it from happening.

MR. CORDARO:

One of the most serious deficiencies, in my view, at LIPA is on your list item number three, C, the total absence of a culture and practice of self-critique that is continuous, systematic and open. I mean, if I had to label or cite one of the biggest problems with the LIPA organization, that is it.

MR. HEMPLING:

I thought what I would do, Mr. Sackstein asked about models, and what I've got on Roman four in sort of final exam manner is what your options are. This is my way of trying to escape giving you an actual answer here. So what I've done is the obvious and probably left some things out, but these are the things that we've talked about today for you to think about in terms of regulation. The possible bodies are the PSC in its current form, and again, you're going to have to deal with legislation to make sure that their scope is not confined to this 2.5 percent. That's what Chairman Garry Brown was talking about. He didn't have the authority, exactly what Dr. Cordaro said, to do anything else except look at rates, and he was concerned about that narrowness of the authority. The PSC with a new LIPA division, I just made that up on the way over here. I'm not sure I really like it. C is also what we talked about, distinct regulatory commission for LIPA only and the status quo is what you have, meaning no regulation.

Item two here, powers and duties. I've already eluded to this. Whatever regulation is established, it should not be dormant absent the 2.5 percent rate increase. Its jurisdiction should exist at all times because rate increases are not the sole reason for regulation.

Accountability, this is something you'll have to struggle with. I just don't know your court system well enough, which courts should have jurisdiction to review its decisions based on what standards. I've seen states with multiple models. You know, you've got what, three levels of courts here. You've got the Supreme Court at the trial level, you've got your Appellate Division and then you've got your Court of Appeals at the top. There's some states where the appeal of a commission decision goes right to the court's highest state. There's some where it goes to the trial court level. Yeah, I once had to appeal a Wisconsin Commission decision. We're waiting out in the hallway to do oral argument on a complicated decision about federal and state law, the judge is in there dealing with a drug misdemeanor. We walk in, and this judge was awesome. He went right from marijuana to the Public Utility Regulatory Policies Act, but I don't know that every judge at the trial level would have that type of flexibility.

If you ask my personal opinion, this is certainly premature. I like having regulatory decisions go straight to the state's highest court, it's just faster that way, and most of the time the commission is upheld anyway, so getting the certainty sooner rather than later. The downside of that is that if your highest court has discretionary review, as in California, that means a lot of cases never get to the State Supreme Court and the commission has a lot of power, which I tend to like since I am a commission advisor and don't like having the stuff that I write get reviewed, but I could see how you might see it a little differently. So, there's a question there about timeliness verses accountability.

And then governance. Boy, this is where I just found myself in a web of conflicting preferences. Who does the appointing and the confirming. You know, you've got all kinds of options. The governor -- in the country the governor is the most familiar model, is the governor appointing, the State Legislature confirming. There's a couple of states where the State Legislature elects commissioners, sometimes from districts, sometimes not, so the Governor's not involved at all. I guess you could have the PSC appointing your LIPA -- your Long Island specific regulatory commission, but that one makes no sense. I just put it there for purposes of completeness, but having the County Legislature and the County Executive and/or the County Executive be the appointing authority for a county specific PSC, again, has its pros and cons, and you could have a mix of all these things as well.

I also thought the eligibility issue was important. You find this issue addressed in multiple ways among the states. I guess you would want to argue that if it is a Long Island specific agency, the members of the -- we're talking about, excuse me now, pardon me. Excuse me while I flip my mind around this. The governance we're talking about the board, yeah, the board. I guess you could assume that you would want the board members all to be Long Island residents, but why is that

necessarily true? What if you thought if one were an executive from Westinghouse who happened to live in Maryland or Pennsylvania was an excellent choice because of the experience he or she had. You really want to rule somebody like that out? Or maybe having an outsider who isn't -- who brings in, you know, maybe ignorance of the location but they can learn that, but brings on unsurpassed expertise in a key area, especially if you are trying to transform a corporate culture. Maybe you want somebody from the outside. So I'd be very careful about the residency qualifications.

The expertise qualifications we've already alluded to. I put quotes around expertise simply to remind you that I don't mean just professional. You know, expertise in community representation, expertise in community organizing, community communications is one of the crucial things, expertise in building credibility with the public in knowing how to deliver bad news is an important expertise. Diversity really is what Mr. Like and I were discussing. You don't want to end up with all Democrats or all Republicans, or all Nassau County or all lawyers. So some thought about diversity among the members, and the length of terms.

This is something I often debate in the abstract with colleagues of mine. I sometimes feel that the length of term for a board member and for a regulator ought to be as long as ten years, because that way you start to see the consequences, both cost and benefit, of your decisions. I'm not a fan of the average term, which is about four years, for a regulator because it's just too easy to push hard stuff off into the future. On the other hand, if you get a dud and you're stuck for ten years, it's no fun.

So those are some of the questions. I didn't deal with a variety of other questions like the number of people on the board and the number of people on the commission. It's got to be a body that works. There's theories about how many people you get into a meeting before the meeting becomes unproductive or counterproductive. So, again, nothing profound here under options, just to try to give you a sense of how many things there are to consider.

MR. GORMAN:

Could you -- who would you think would appoint this board, because obviously if you're not going to do Nassau County it can't be an elected board, it has to be appointed. The logical -- obviously the preferred people would be the Suffolk and Nassau County Legislators working together or to put together some sort of concept. I mean, that's the only way I can see this unless you want to go to the Assembly. The State Legislature will never give you an answer because you're not New York City.

MR. HEMPLING:

I just have to -- I have to take a buy on this one. I just don't know enough about this to guess, and it's so personality specific. I will give you this one example that I know a little bit about. Where I come from Montgomery County, Maryland, there's a what do we call it, the Washington Suburban Sanitation Commission, the WSCC, is the company, the public company, meaning it's essentially a state agency that is the utility that provides water service in two counties, Montgomery County and Prince George's County. The Board of Directors has three people from each county. And what -- and there's some significant differences between the two counties in terms of income, in terms of race, and what happens is that each group of three meets with their own city county council, their own County Executive, comes to these meetings all ready to represent their county, and they get themselves in the divisions. The PG people want to talk about contracting from minorities all the time, the Montgomery County people want to talk about freshwater all the time, and they end up in these compromises which essentially put off a lot of the hard decisions. You have to be careful about that.

That's why, frankly, I like the idea of maybe people coming from all over the State. But I've avoided your question about appointing authority. You know, maybe some -- if we're talking about a Board of Directors maybe some were appointed by your County Executive, some by the Nassau County Executive, and maybe a majority come from outside. But don't take anything that I am saying as serious, I'm just thinking out loud with you. Sir.

MR. SCHROEDER:

If I could, I think there's some issues of jurisdictional authority associated with appointing ability also because this is a State authority. The local jurisdictions would only have authority to appoint if the State granted that authority, so at the onset you're looking at something, some action required on the part of the State to enable us to have any ability to appoint locally.

MR. GORMAN:

Exactly. That's exactly what I was alluding to, because how are you going to establish somebody to do it if you're not going to have it as part of the public vote? And I don't know how you make what you're talking about not political.

MR. LIKE:

Under the original LIPA statute, it called for a 21 member ratepayer district elected members. It was repealed when Governor Cuomo was ousted from office and replaced by Pataki, it became an appointed board. What never took place was to set up the machinery for electing the ratepayer representatives from each of the districts, and that raises a question. I don't know whether you've run into this in your experience, is if you have a ratepayer board, which is elected by the ratepayers, how do you assemble a group of candidates who present themselves as wanting to run for that position? Do we have to get into the election laws and the laws dealing with referenda in order to know what the machinery is going to be to get to the point where somebody says I'm interested in running, somebody opposes him, and then there's an election which decides the outcome. Have you run into that in any of the examples that you are familiar with?

MR. HEMPLING:

I'm afraid not. It's just electoral machinery is outside my line of work. I will say, and again with apologies for being possibly disagreeable on this, I want to remind you that I don't think ratepayer interest is the only interest that's served, either by regulation or by utility citizen interest, which is broader than ratepayer interest. We're all everything. People call themselves environmentalists or labor advocates or shareholders; we're all all of those things. A ratepayers is only one part of what I am. I also care about the environment, I also hope to retire someday on my earnings, and so to think of it as ratepayer only, in my view, narrows dangerously the governance to a particular type of accountability right at the beginning of the process, and I personally wouldn't do it that way. And people are elected to pursue a ratepayer interest and a ratepayer interest is too often a short-term, narrow financial interest. I'm not sure it's any better than having a bondholders vote or shareholders vote. Regulation and running a company is about expertise. It -- and just to, sir, I'm sorry, I forgot your name. I'm looking at my list. It's Mister --

MR. GORMAN:

Just call me Fred.

MR. HEMPLING:

Okay, Fred. It's Gorman, Mr. Gorman, yeah. On the question of appointing authority, politics will always be there. What you're looking to do is have good politics occupy its appropriate role, which means, for example, if you've drawn your criteria for selection tightly enough so that you have to have somebody who has this experience, and you have to have somebody else who has that experience, now you're starting to put boundaries on how far politics can play. Look, politicians do favors. I've been a beneficiary of those favors, and I give them out in my own political role, and

that's the way -- the grease that operates things. But when those political favors are in pursuit of a larger purpose than just politics and favor sharing, it works better. So if my job is to recommend somebody who's a very good lawyer, I don't mind doing a favor for some very good lawyer that I know by recommending them, because I know my reputation depends on making a good recommendation. So politics and favors are part of this, but you can put boundaries on it through the culture and through the Legislative specification.

MR. CORDARO:

I agree with that. I think the absolute need is for very good specifications, very tight specifications, on the characteristics and disciplines and professional capability of the people who were appointed, and that's the ultimate control as far as the models I've seen. The models I've seen also for public utilities, which have elected boards, have shown that your observation, at least from what I have seen, is correct in that it's very difficult to have an elected board, popularly elected boards, because politics dominates the situation. And you constantly have contentious and a contentious atmosphere that doesn't contribute to the solution making process and to coming up with a plan which benefits the populous as a whole. So much of the time of operation from the standpoint of an elected utility board is taken up with electioneering and politicking to be in a position to be reelected at some point in time.

In fact, an excellent example of this is out in Sacramento, the SMUD Utility, Sacramento Municipal Utility District, where they have an elected board, at least the last time I looked they did. They may have changed recently, but over the years that was the case. And it was interesting to see the set up for that. I mean, each year the board members had an office at the utility proper, they had a staff of one or two people to support them, and they pretty much devoted most of their time to positioning themselves to win the next election rather than to perform the business of the utility. I think the professional board is probably the best compromise with type specifications about the professionalism of the individual board members. The only thing you don't escape by that is the fact that they have to initially be appointed by some sort of governmental entity.

MR. GORMAN:

Which is not that hard.

MR. CORDARO:

Which is --

MR. GORMAN:

It's really easy.

MR. CORDARO:

Of course. But it depends on the motivations involved and the quality of the whole process to make it work.

MR. HEMPLING:

I'm very sympathetic to the situation, though. What you have is a company that has no transparency, no accountability, and therefore, no credibility. And you're looking for a way to restore, never mind restore, to create for the first time, trust. And I'm advising you to find some other way to do it, but there's no question that the absence of trust is what you have.

There's two other sort of variations on the theme or one other that I'd like to mention to you, yeah, because I'm -- yeah, you get the wrong governor in office or someone you don't agree with and appointments could be made for political reasons. In Indiana, the statute, if I recall, it's either the statute or the practice, you'd want it in the statute, is that the governor makes the appointments from a panel of candidates that has been screened and selected by some other body, and so there is

a body of regulatory, a changing -- personnel change on it, but this body of regulatory experts and practitioners who take all the applications in for a commissioner's position and basically find three that they think are the best. And the culture of this process is that you're looking for people who are qualified, and then those three are submitted to the governor. Now at that point the governor may make a completely political decision, but he or she is confined by a professional practice that has preceded, a professional review that's preceded his or her decision.

Another example is the ABA model, where for judges the President selects whoever the President wants to, but the ABA makes a very public review and ranking of these people based on criteria that are important to the ABA. Sometimes that's controverted, sometimes it's not. But there's any number of ways of injecting a professional component into what's otherwise a political process, and that's what you're missing right now.

MR. GORMAN:

As I said, it's easy.

MR. HEMPLING:

I would agree that it's easy, but there are ways at least to think about it in the abstract.

MR. GORMAN:

Yes, that's why I'm saying it's easy. I agree with exactly what you're saying. Maybe not the Governor, you know, the Legislature has to be involved to make a decision. After the Legislature makes a decision, you can have a panel. If they want a panel from Nassau and a panel from Suffolk County because for some reason they want them to review the people that are going to be selected for this, and those that are selected then go through a final review or peer process, be it the County Executive or the Governor or all three of them. It's simple enough to do is what I'm saying.

I think it's a good place for us to start because politically I think the time is right. Politically right now I think you would probably get more out of your New York State Legislature than ever before because of their concerns with finance and all the pressures that are on them, and this looks like another good thing that they're doing to help people out. So I'm saying between now and November, in my opinion, would be a good time to formulate something, take some of these excellent ideas, put it together, lay it out as a business plan, and present it to our Legislators, both our Senators and our Assembly people, and ask them to sponsor a bill, get it up and get it done. But we'd have to do it by June. If that's too fast, then we have to wait until next year.

MR. SCHROEDER:

Through the Chair, I'd just like to make an observation based on our discussion here today. If, in fact, LIPA has not been collecting all those costs in the near term that it should have been collecting, because it's possible they've been over collecting in many other ways other than the lost power issue. But if, in fact, costs have been deferred to give the impression or to artificially reduce rates below where they otherwise might have been, then the remedy here may not be such a public windfall from the State Legislature's perspective, because if it results in an increased unit cost for electricity, I'm sure there's going to be an awful lot of unhappy people. It may provide for the long-term health, better health of our utility and of our local economy, but in the near term there may be some pain associated with this adjustment.

MR. HEMPLING:

That's why the good Lord invented the word phase in. I mean, when you have -- when you have a deficit of political trust you can't solve it overnight, and it just may be one of those ways where you put aside your principles and do what's right and phase something like that in.

MR. GORMAN:

You're right, but it has to be done.

MR. CORDARO:

It isn't going away. If those problems are lurking in the shadows they will emerge at some point whether we do nothing or we do something. So, it's got to be dealt with somehow.

MR. SCHROEDER:

Yeah.

MR. CORDARO:

In some cases, with a complete change in the nature of the organization, people may be more willing to accept the fact that this is a legacy that's been inherited and has to be dealt with and is not the fault of the new governing body or new structure.

MR. HEMPLING:

I was taught this early in my career; build the trust first and deliver the bad news second, not the other way around.

MR. SACKSTEIN:

Mr. Hempling, in a normal business environment, if we as a Board of Directors chose to make some very significant structural changes in how a company is either perceived or operates, it would be relatively simple because we make these business decisions. We sit in the unenviable position of we don't have any power. We have to rely upon those elected officials to make non-political choices or political choices which may be unpalatable. And I want to fix a company that I think had and has a lot of potential, but I don't have the power to do it. I can persuade, I can recommend, I can suggest. How do we make it happen? I mean, the reality is everybody recognizes the shortcomings of this entity. Maybe they don't recognize some of the potential of this entity. And my biggest fear right now is with all we've invested we're going to lose this entity and it's going to be gobbled up by the State of New York. And I feel, you know, just -- so my hands are so tied, and I don't know if you can even guide us in that direction, but that's how I feel about the situation where we are now. It's a viable entity and we can't fix it.

MR. GORMAN:

You know all our State Senators, don't you, on Long Island? Do you know them, sir?

MR. SACKSTEIN:

Let me say that --

MR. GORMAN:

I would assume you know them very well, don't you?

MR. SACKSTEIN:

We know many of the elected officials. We certainly can have a dialogue with them.

MR. GORMAN:

That's where we've got to start.

MR. SACKSTEIN:

I'm prepared to do exactly that in a public forum, which I'd be delighted to do. And, Mr. Hempling, we'd be delighted if you could make yourself available in that kind of an environment, too. We'd certainly sit with you privately first and try and figure out the structure of such a dialogue, but at the end of the day, Fred, they got us into this dilemma. They allowed us to have a structure that exists

now. They allowed us to have a Shoreham debt. They allowed us to have lack of transparency. They allowed the power authority, as it is, to issue a draft resource plan with no appendices for public comment. They allowed us to be burdened by a management services agreement that was never put out to public bid. They allowed us to be in a position where that illegal management services agreement was extended. I mean, I could go on and on about the things that they allowed us or gave us or did to us or did for us, so to get them to change their behavior, you know, I'm willing to try, but I'm less than guardedly optimistic.

MR. GORMAN:

Did you ever see what happens in this room when the tea party shows up?

MR. SACKSTEIN:

No.

MR. GORMAN:

You know happens?

MR. SACKSTEIN:

I know what tea sounds like when it's boiling.

MR. GORMAN:

All right. Well, you know, you have to create political will. You have to give them a reason to do something, and it's the way that you present it and sell it. I'd like to make a motion that we consider these points very seriously, that perhaps we draw up some sort of draft as to how we feel, you know, a structure, you know, should be put together. I'm not just talking about the business points of how we would like to see, but a regulatory -- the concept of a regulatory body, and how we think it might possibly be formed. We can come up with a couple of different things, and we should come up what it should do, because every one of these points were absolutely excellent. I think they would make great press, even though we may be, you know, there may be problems down the line. But the problems down the line are the problems down the line regardless of whether we start or not. So we either sit here and do nothing, or we start.

MR. LIKE:

I think we all agree, and I think I speak for everybody here, to tell you that you've been very helpful and generous with your time. And that leads me to ask this question. Are you able to identify those additional expertise -- experts, if you will, whom we as a committee should speak to to deal with some of the issues that you modestly indicated you were not in a position to deal with today? Give us an idea of who we have to talk to, for example, if we're discussing how to define the districts, if we're proceeding with the notion of elected ratepayers, who we have to talk to to find out what we need to do in terms of the electoral process. And obviously what it would cost to meet or to retain these experts if the County were requested, as we could conceivably request them to do, to fund money to enable us to retain the additional expertise that would lead to the kind of a draft that Fred is talking about, of structural or at least the beginning of a structure for a new LIPA.

MR. HEMPLING:

Well, as I said, electoral is way outside -- I'm actually a registered Independent, I stay out of electoral politics myself, but in some of the other areas we talked about, if you send me a list of questions I can send some experts, but I'll draw a blank on electoral. Although Washington D.C. is full of people who could talk about that, but I would think that first you would want to see if that's where your priority is before you spend money on that.

One thought I have, and I really hesitate to give political advice in such an apolitical forum, but I think that I would think about involving people outside of Long Island perhaps to a larger extent

than you have up until now in the process of designing solutions. I don't know that the absence of non-Long Islanders is one of the causes of your problems. I just know that this is a great state with all kinds of people and you have a Governor who's committed to getting things done right, and it may be that the objectivity that exists, you know, in the longer view than they exist outside of the County is part of the process. That means not just dealing with your local State Legislators, but people outside.

And I would also suggest, I've known Garry Brown, your PSC Chairman, for a fairly long time and I've seen him in action and my view of him is very positive. He's a straight shooter. I'm not saying that you go to the PSC to get everything done, what I'm saying is he seems to be the type of straight shooter that talking with could give you some other ideas, and there's any number of other people like that within his commission and elsewhere in the State. It even includes the possibility of, with respect to your governing board and your regulatory board, having some membership that, as I indicated, that is from outside the County, because that sends a signal that there are values here that are bigger than Long Island county. Long Island's economic development affects more than just the people who live here and the credibility of public power, and the credibility of the utility industry is affected by what goes on here. So I think there are arguments for getting high quality people who are from outside the state, and that would lessen the notion that this is all about representativeness and not about professionalism.

MR. GORMAN:

As it respects to regulatory board I --

MR. HEMPLING:

I'm sorry, I was referring to both, sir.

MR. GORMAN:

I'm talking about the regulatory, if you want to call it commission, board, regulators. I absolutely think it's a terrific idea to get the best people from the best disciplines that we need in here. I think that we have to sit down and talk with Nassau County as well as Suffolk County. I think we have to develop the political will for something like this. I happen to think it sells well at this time, because, you know, you have a governor who's talking about consolidation. You have people complaining about things going completely out of hand. You have a board of appointed people that people are unhappy with. So right now, particularly with what's going on with all our -- all our Long Island Legislators, we currently have the majority in the Senate. That gives us a lot of clout, a lot of power. That allows -- you know, it's no longer just Sheldon Silver who makes all the decisions, it's Sheldon and Dean Skelos.

So I happen to think that we are at a time that if we are energized and if we think that this is a good idea, we prepare something quickly because this is April, they're going to close -- maybe we have to wait another year. But I happen to think politically this is a very smart move because you're not taking away the LIPA Board, but what you're asking for is an independent regulatory authority. I absolutely think it should be under the guidance of the Public Service Commission. It should have to follow their rules and regulations, work very closely hand in hand with them. It gives you the feeling of local control that at least you can do something about it. And believe me, the ratepayers really want that, they really feel that they've been -- well, everybody here knows I'm preaching to the choir. They feel that they've been led down a path and, you know, they just can't afford it anymore. Having a regulatory board to develop Long Island power over the next 10, 20, 30, 40, 50 years is something that makes all the sense in the world, because I don't think we're ever going to get control of the LIPA Board. Plus once that regulatory board is in power I'm not going to be so worried about something being sold.

MR. SACKSTEIN:

Other than the LIPA statute itself, which gives them control over all purchase, sale, lease of all of the assets within the service area. So, you know --

MR. GORMAN:

When you have a regulatory authority you have power that you don't have now.

MR. CORDARO:

Joe's been waiting to say something.

MR. HEMPLING:

I don't want to practice New York law, but the dialogue that Mr. Sackstein just raised is very important. Simply superimposing a regulatory board on the current LIPA with the current statute will fail, because their current statute gives virtually unreviewable discretion. The whole -- to the LIPA Board. The whole purpose of regulation is to channel the discretion of management, but if the statute leaves that management discretion unreviewable, merely imposing a regulatory body on top of it doesn't work. You're going to have to work at both ends of that spectrum to succeed. Sir.

MR. CORDARO:

Joe.

MR. SCHROEDER:

Scott, I want to thank you for your comments here today. Certainly very thought provoking and informative on many fronts. I really do not envision us being able to recommend anything to the Suffolk County Legislature that will not require some State action. There's got to be some -- if there's going to be any adjustments to the statute it's going to come from the State, it's not going to come from us locally.

I also think, Fred, on your motion to start to formulate something here regarding governance and regulatory structure, I think we have several public hearings that we're due to hold. I think we ought to incorporate comments from those public hearings into whatever we formulate and then make that formulation and make that recommendation to the Legislature so that they can take more official action, and maybe soliciting and encouraging some State enabling legislation.

MR. GORMAN:

I know. I just like to get things done fast.

MR. CORDARO:

That introduces, you know, a point that I want to bring up. There are two items that we need to follow up on that were brought up at our last meeting. One was to set a date for a public hearing in Riverhead, which Ed Romaine was going to look into. I haven't heard anything back about that as far as the date out at the County Center. And the second point, which becomes very important and ties directly in with what we've been discussing, was to bring in the New York State Legislators who have been sponsoring legislation, Ken LaValle in the Senate, Bob Sweeney in the Assembly.

MR. SACKSTEIN:

Fred Thiele.

MR. CORDARO:

And Fred Thiele, and even perhaps invite Chairman Brown to attend, so that we can have a dialogue to flesh out what needs to be done from the standpoint of State legislation to put us in a position to obtain regulatory oversight from -- of LIPA, and to also necessarily make whatever changes from a governance standpoint need to be made with the LIPA Board. So -- and also, I think that that is in

Ed Romaine's camp right now. He was going to contact the State Legislators and set up a time and a date for us to meet. And I think that's urgent. I think we need to do that as soon as possible, especially with the information we gathered, especially on the heels of the New York State Senate Energy Committee meeting last week and the mood and the atmosphere that exists. So I think it's very important to convene that meeting.

I would -- I think we could set the Public Hearing up for -- and we could do that at any time, and we should do that within the next couple of months, but it's probably most important to see if we can get this meeting with the State Legislators as soon as possible to lay a foundation and groundwork to accomplish what we need to -- what we want to accomplish.

MR. HEMPLING:

Well, there's a lot of different views, though, just among the five of you, on what it is you would say to the State Legislators, and you folks, I don't mean to give immediate advice, but you folks being perhaps the most up to speed and thoughtful about this might want to try to get your own sort of set of sentiments in line first, otherwise the Legislators who have thought less about this will be sponsoring something in response to your urging that might not work. I mean, there are some tough choices to make, the conversation about electoral versus appointed. The conversation about districts versus expertise. My thought would be to try to figure out where the five of you are on that before going too much further, but -- either that or your legislation is to have the Governor appoint a study commission that will come up with something which may be a good idea, but to some extent takes more time than maybe you have to solve the problem.

MR. LIKE:

What would be helpful, if in advance of a meeting with the State Legislators, if we could obtain either copies or citations to those statutes which you think are the most relevant or useful in giving us input for what would go into a LIPA statute. You mentioned various public power districts and municipalities. One or more of them may have provisions, authorizing statutes, which contain the kind of language we should be looking at in drafting our own statute or in bringing it to the attention of our own Legislators.

MR. HEMPLING:

There are certainly statutes floating around and I can work with Joe to procure those, but I hope not in disagreement with what you are saying. The conceptual options are in front of you, and I think the first step for you is to sort through the trade-offs among the options and then writing or finding language -- sometimes I find just writing it myself is faster than researching it, but if there are good models you can use them. But I think to a large extent your own thoughtfulness will cover the ground in terms of what your options are.

MR. LIKE:

Well, the ones that seem immediately useful would be those in municipalities or counties where the commissioners are elected directly by the citizens or the ratepayers of the county.

MR. HEMPLING:

I can give you some contacts on that, who would be willing to do the research, I think, on that. I should say one thing about -- it's obvious that I am not crazy about the elected idea, but, you know, that's you call versus mine. I will tell you that among the most inspiring people I have ever worked with in regulation is a gentleman named Brandon Presley, who is one-third of the Mississippi Public Service Commission. They are elected by districts down there, exactly the approach that I don't think is particularly good, but Commissioner Presley, who's only 33 years old, he was elected Mayor of his town when he was 23, he is a brilliant man and the most, I think, most committed, hardworking person, who actually -- this may be what you are thinking about, Mr. Like. He actually gets it in terms of how to combine the political complications of regulation and the political

complications of getting reelected. He's doing it right now; it's election season down there and he is one extraordinary individual.

If there was one person I would want some of you to talk to about how it might work to be elected so you're not not just getting my, you know, more negative view on it, it would be Commissioner Presley. Maybe one of you who wants to volunteer themselves I will connect you up with him. He is also on our Board of Directors.

MR. CORDARO:

The time is right, from the standpoint of taking this on a stepwise basis, to attack the regulatory oversight concept because of the Senate hearing last week and what was said by the Chairman of the PSC, as well as the State Senators there after having passed this bill which tied regulation to a specific rate increase number. The discussion was, at that hearing, was directly in line with the comments you have made as far as what is needed to enable the Public Service Commission to adequately regulate LIPA, and it went beyond reference to a particular rate increase number. And it talked about resources and authority, and all that has been placed on the table. It was obvious from the response of the State Senators at the hearing that they're receptive to move on possibly modifying their legislation and, you know, as part of that process, also influencing the Assembly legislation that's proceeding from the Assembly right now on LIPA regulation.

I think it would be very useful to convene the meeting of those principals, the State Senators sponsoring legislation as well as the Assembly and perhaps the Chairman, so that we could put on the table exactly everything that needs to be put into the State legislation to put us in an as immediate position as possible to establish regulatory oversight of the Public Service Commission of LIPA.

The time is right, the stage is set. I think there is a willingness on the part of the State Legislators to act on it and for us to be able to accomplish something significant, and to accomplish it before the session is over as Fred indicated before, to get some movement and some action. I think it's also timely because the Assembly hasn't voted on their bill yet. The Senate has voted on their bill. They're talking about amending it, but I'm sure it will be a little bit more of a task to amend it than it would be for the Assembly to modify its bill while it's being debated in the Assembly itself. But I think it's important for us to move forward as soon as possible to get that interaction between us and the State Legislators as soon as possible so that we can achieve something in a short time frame.

MR. HEMPLING:

I'm hesitant to offer this type of advice, but I guess I'm going to offer it. One of my other expertise's is drafting in legislative context, and I've worked on things far less complicated than this and they take much longer than you have between now and November. I'm just a layperson with respect to Long Island, but not with respect to the legislative process. Given the myriad of choices we've talked about, and the likely differences among the five of you, amicable, but probably big in terms of how to set this whole thing up and the large number of choices in combinations, it's hard to imagine that you are going to have a piece of legislation written, drafted, vetted and all the unintended consequences thought through, and we emphasize the unintended consequences thought through, and do that on a timeline that you are talking about.

I appreciate that you had me here and I appreciate the notion of momentum, that's how things get passed, but you want to be real careful this time. You know, part of me wants to jump on your momentum and help you get it done right away, and part of me says things just don't happen that fast and come out right, and I'd almost like to see a state level study committee with an obligation to report, say by November, so that then there's something that's on the table for the January first segment. I would rather spend the next six months, use the next six months studying, debating,

involving the community than spend the next six months trying to draft something and get it passed. But, again, that's an outsider's perspective based on my own drafting experience.

MR. SACKSTEIN:

Without getting us all the way through to the legislation and getting it passed and getting it drafted and everything, I think I feel somewhat encouraged by the fact that we now have a task that I think is achievable right in front of us, and that is putting in place. However it gets done is a different issue, whether it's elected or it's appointed, but the concept of putting in place the Long Island Public Service Commission to have direct responsibility for creating this reporting, this openness, this transparency, the standards. As far as I am concerned personally, that, as far as I am concerned, will start tomorrow to try and build up the public momentum to have it accomplished. That may put us in a position where I would like to be ultimately, which is to create a new and vibrant and viable company out of LIPA, albeit I recognize we'll never get rid of all of the politics unfortunately. I wish we could, it is what it is.

But starting tomorrow I will be on the phone and I will be speaking to Ken LaValle, I'll speak to Fred Theile, I'll speak to Bob Sweeney, and certainly I'll reach out Chuck Fuschillo, who called for those hearings last week, and we'll start immediately to have a dialogue and this won't necessarily have to bind this oversight committee. This will be done by Action Long Island through its Energy and Environmental Task Force, and we will start immediately to open up this dialogue so that we can start to put it into the public arena. Even if we don't have legislation, even if we don't have a methodology for how we're going to elect, select, appoint these people, I think the concept by itself is what we were hearing last week at the hearings, but they were pointing it away from Long Island. They were pointing it to the Public Service Commission. I would like to bring it back home where we are most familiar with the issues. I mean, the Chairman of the Energy Committee, what is his name again?

MR. CORDARO:

Maziarz.

MR. SACKSTEIN:

Maziarz didn't recognize we were the largest farming region in the State of New York, had no idea as to how many megawatts we put out, and had no idea of the population of Long Island. So while I have great respect for him, he needs to have some more familiarity with the issues here on Long Island, and I think we need to be able to have oversight of an issue that is paramount to the future of Long Island, and so for the first time I feel like we've got a shot.

MR. CORDARO:

Joe, you want to say something?

MR. SACKSTEIN:

I want to thank you for that.

MR. HEMPLING:

Thank you for having me.

MR. SCHROEDER:

I just would like to restate I, you know, I have a sense here that, you know, there's a large hole in the hull and we're taking on water and we got to patch the hole, and I understand the urgency associated with that, but we also want to be seaworthy for a long time into the future. And there may be, and I'm sure there are, unintended consequences associated with all of these options. I think that this has been a great venue for airing some of those and I appreciate the input, Scott, but I think we have more to do before we have a position as an oversight committee. I think we really

need to vet out some of these alternatives in conversation amongst ourselves, in concert with the public hearings, and create something that's a lot more viable, a lot more robust than just our opinion that this is a good thing to do. We need to substantiate that and I think we can do that as we allow the process to occur. Fred, I am not arguing against progress and progress quickly, I just agree with Scott that --

MR. GORMAN:

I am with you a hundred percent. Not even 99, I am with you one hundred percent. This has to be studied out. But we agree we're going to start studying it.

MR. SCHROEDER:

Well, I do other things on behalf of the County, and I can tell you Scott is absolutely right, things do not move quickly. The blistering glacial pace of progress is exhausting but, you know, it's what it takes.

MR. LIKE:

Joe, my experience in the early days of the evolution of the LIPA statute gave me some acquaintance with the process itself, and it began with somebody putting a draft down on a piece of paper, and the participants were bond counsel at Willkie Farr, a professor at one of the Boston law schools, and a bunch of citizens. It went through a number of iterations before it came to a form, which was introduced to Albany. And I suspect that the process of amending the statute is probably going to take the same way. We have to sit down and even without the assistance of professionals, as our own experience, start to put together at least the concepts of what should be in the statute. That could then be presented to people who are more expert than we are to review and to come up with final language.

We know that the staff assistance to Sweeney, and I'm sure the other people, will be very happy to get into the process if their bosses tell them to do so, but we have to give them the input. We have to say we want this in the statute, get it done, and we need it by a certain date.

MR. SCHROEDER:

I don't disagree with you at all. That's exactly how I envision this proceeding. I just think we need to do that amongst ourselves before we start broadcasting what our position is since we don't yet have a unified positions.

MR. SACKSTEIN:

As I said, this is going to be something that Action Long Island will take out of the station initially, and we'll see where it goes. It reminds me a little bit, Irv, of 1993 when I picked up the phone and I called Richard Kessel, and I said, "Rich, I'm a LIPA Trustee, but I'm calling you now as the Chairman of Action Long Island. Don't shoot the messenger, but Action Long Island is the push for the takeover of the Lighting Company." And Richie said to me, "Don't even think about it because this Governor will never go for it." And I said, "This Governor should", and that was Mario Cuomo at the time. And when you fast forward to October of 1994, Mario changed his mind three weeks before the election. Too little, too late.

And when I met -- and Irv was there. Irv, you were sitting there when we met with the transition team for Pataki, when Seward at the University Club, Senator Seward said, "This Governor will never take over that Lighting Company" and look what happened. Let me tell you, as it unfolded Action Long Island backed away from it because the transaction, which they artfully named it, it wasn't a takeover, it was a transaction, is -- was and now 13, 14 years later has proven to be exactly what we said, not in the best interest of the ratepayers. When they did what they did and they bifurcated the deal and they saddled us with the debt, we backed away and we said it was a idea conceptually, but a bad deal for the ratepayers. So it has to start somewhere, and sometimes it

starts out there, you know, in the mind's eye of the public and somebody has to put it out there, and that's why I say I won't bind us to it at this moment in time, but I certainly will take the train out of the station.

MR. CORDARO:

Well, you know, Action Long Island can do whatever Action Long Island wants to do. I think we still have the responsibility to do what this committee needs to do and was charged to do. I made the suggestion and I'll reiterate it. In fact, I made it at the last meeting, to have this meeting with the State Legislators and, you know, I'm going to make it again because I see the opportunity to do something in the short-term, to get a meeting of the minds. Garry Brown, at the hearing last week, laid out what he needs in legislation to be able to regulate LIPA. And the Senators seem very amenable and ready to act. I think having our interaction with the State Legislators in one of our public meetings will put all these issues on the table. Determine whether there is a study that's needed or further action on the part of the State and how to do that, or maybe determine that there's more agreement than we believe right now sitting here, and that there's a commonality of issues.

One of the things that I'm fully aware of, as far as State legislation goes, State legislation doesn't go into a lot of details. I mean, if we've got to redraft the LIPA statute and things like -- there's a lot of work and effort associated with that, but from the standpoint of a bill, and you can just look at the Senate bill that was enacted to subject LIPA to the 2.5 percent rate increase, it's not exhaustive. It's very cursory. The details are to be developed as part of the process. So to get something to happen, and to make something meaningful happen and to put everything on the table and to point out whether we need to set up a longer time frame or put other mechanisms in place to do some work and do so some study, I think this would be very, very evident by some interaction with the State Legislators, and hopefully Garry Brown. Garry Brown is probably going to be more difficult to get here just from the standpoint of the demands on his time than the State Legislators are.

MR. LIKE:

Matt, I'm move that you invite the State Legislature representatives to a meeting as early as possible, and also include Garry Brown among the list of invitees to come to such a meeting, with the understanding that the meeting will be wide open to discussing with them everything we talked about today.

MR. GORMAN:

I wanted to second it. I'm seconding it, not him.

MR. CORDARO:

All in favor? Opposition? That motion is carried. It amends what Ed Romaine was going to do from the standpoint of also bringing Garry Brown into the picture. I think we have to contact Ed Romaine and his staff to see what's been done, if anything, on setting up the meeting with the State legislative representatives and to see if it can be expanded to include Garry Brown's presence, and to hopefully be able to schedule that as soon as possible.

MR. GORMAN:

Do you think we should also mention that one of the things that we want to talk about is a Long Island regulatory board if we are going to ask them all to come here? Think we should tell them that that's part of our thinking? And maybe we should get a little -- I don't know, Scott, I don't know what you have that would flesh out more than what you've already given us, but do you have something fleshed out that's very easy for you just to e-mail us or fax us?

MR. LIKE:

I have something very beautiful, which I brought with me, I recommend that we get a copy for all of

the members of the committee, okay?

MR. HEMPLING:

But the answer to your question is, the more direct answer is no. This outline that I prepared today is about the extent of my -- everything else that I know about this is back in my brain. I think it really remains, you know, when you're an architect you are starting with a vision, and you all have the intelligence and the background and the options in front of you now to make the choices. The key is to build off ramps, to be conservative, not to be excessively optimistic about anything that you write, because there will be negatives associated with it. And it's like when two parties contract, smart lawyers think about the bad news. They don't just think about the good news and they write in their contract the protections against the bad news.

MR. CORDARO:

I think it's very possible that we can -- there's no reason why we can't discuss a Long Island Commission. I might point out, though, that one of the things that Garry Brown said last week is that if indeed the PSC had the authority to regulate LIPA, it would hire people and dedicate people to regulatory oversight of LIPA, and that's one argument he used for the additional resources that he would need, because this is the process they would pursue to initiate regulation -- regulatory oversight of LIPA.

MR. HEMPLING:

That is something you can specify in the statute. Again, I'm not here to take sides on anything. That concept make sense to me in a short run, because the LIPA situation is unique. In the long run I don't know that there would have to be a permanent or that it would be desirable to have a permanent staff. So if that's -- it's an example of the kind of thing that if you drafted you wouldn't want to fix in the concrete the necessity of a permanent LIPA division, because there can be economies of scope and scale and organization where drawing on others is helpful.

MR. CORDARO:

Well, I don't -- knowing how the PSC operates, they would hire a cadre of people who would specialize in overseeing LIPA. Whether it's organized in any official way or not, I'm not sure, but knowing how they do operate, they would shuttle people in and out of that. But there's a lot of efficiency that they gain by having staff members specialize with individual utilities because they get -- they learn to know the accounting and what all the idiosyncrasies are of the different utilities. So there's some merit to having staff specialize on particular utilities.

MR. HEMPLING:

I want to emphasize -- I'm sorry.

MR. GORMAN:

Could I just make one other suggestion for what we're going to be doing since we're going to be meeting with all the Legislators? I think we should really talk about standardized accounting. Since LIPA's accounting is completely separate than everyone else, I think it is very important that it should be standardized so whoever is looking at them understands what is going on.

MR. SACKSTEIN:

How do we know that it's not?

MR. CORDARO:

Well, Garry Brown said that last week, that it's not the same accounting that they see for the other utilities in the State. So that would be -- in fact, he implied that they would require that. If they assumed regulatory responsibility over LIPA they would demand and require LIPA to adopt the same accounting systems of the other utilities.

MR. HEMPLING:

There was one thing that came up early in the conversation that both Mr. Like and Mr. Gorman brought up, and that is the reaction of the bond community to whatever you do. This probably is too obvious to warrant repeating, but getting somebody who's a responsible, thoughtful person from the bond community in on your process early makes sense. Not somebody who's going to rain on the parade with rhetoric about how bond ratings will go down, but somebody who can advise you on what it means to make a false move in this context.

You know, you've got -- I was a community organizer in my first job out of college. I ran the research department for the Connecticut Citizen Action Group, two of my best careers years, and I know what it means to deal with the citizenry and I know what it means to have your actions misrepresented, misunderstood, exaggerated, hyperbolized. And not that we ever dealt with anything of bond rating consequences, but this time you are. So an active citizenry that can be connected to one or more of the members of this committee and the tendency for citizens to speak in loud, exaggerated terms, there's any number of ways in which the wrong impression can get created, and having somebody close to you who can help you fashion the way you think about things and the way you deliver messages is going to be real important. It was Mr. Like's comment about the fact that he had bond people in on the original discussions of the LIPA statutes that reminded of that point.

MR. CORDARO:

Well, you spent quite a bit of time with us, Scott, and we want to thank you for making the trip and taking the time out to counsel us. I'm sure all of us will agree we find your remarks very useful and incisive and we'll be -- and will turn out to be an important part of our deliberations and frame a lot of our efforts going forward. And I'm sure maybe at some point we may call on you again or interact with you again. I know we've taken advantage of your kindness in showing up uncompensated at this meeting so, you know, we'll respect that in the future, but we would hope that we could have some additional communication and ongoing dialogue as things further crystalize here.

MR. HEMPLING:

I have the career I have because I get to work with people like this. Mr. Like, for my entire career, has been a model to me of citizen activism and lawyerly professionalism, and the opportunity to be of any assistance of something that he cared about was well worth the effort to me. Thank you for having me here.

MR. SACKSTEIN:

I would echo that also, Scott, and also about Mr. Like.

MR. LIKE:

Thank you.

MR. SACKSTEIN:

Irving Like has lived his life of unfinished business.

MR. LIKE:

I can hardly hear what I have to say now.

MR. CORDARO:

I think the most prominent action items we leave here with today is a need to communicate with Ed Romaine and his staff regarding setting up this meeting with the Legislators and Garry Brown, as well as the need to establish the date and time for the Riverhead public hearing that we're going to have. So with that, I would entertain a motion to adjourn.

MR. SCHROEDER:

Motion.

MR. LIKE:

Second.

MR. CORDARO:

All in favor? Aye? Thank you very much.

(The meeting was adjourned at 3:39 P.M.)

{ } Denotes spelled phonetically