

**MINUTES OF THE REGULAR MEETING
OF THE
AUDIT COMMITTEE**

March 25, 2014

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Minutes of the regular meeting of the New York Power Authority's Audit Committee held at the Authority's Offices at 123 Main Street, White Plains, New York at approximately 8:55 a.m.

The following Members of the Audit Committee were present:

Trustee Terrance P. Flynn, Chairperson
Trustee Eugene L. Nicandri
Trustee R. Wayne LeChase

Also in attendance were:

John Koelmel	Chairman, New York Power Authority
Jonathan Foster	Trustee, New York Power Authority
Joanne Mahoney	Trustee, New York Power Authority
Gil Quiniones	President and Chief Executive Officer
Edward Welz	Chief Operating Officer
Judith McCarthy	Executive Vice President and General Counsel
Donald Russak	Executive Vice President and Chief Financial Officer
William J. Nadeau	Senior Vice President and Chief Risk Officer
Karen Delince	Corporate Secretary
Brian McElroy	Treasurer
Thomas Concadoro	Vice President and Controller
Lesly Pardo	Vice President – Internal Audit
Frank Deaton	Director – Enterprise Risk Management
Brittney Frazier	Project Coordinator – Public Relations
Kenneth Deon	Engagement Partner, KPMG
Scott Heiser	Senior Manager, KPMG
Nicholas DiVirgilio	Manager, KPMG

Chairman Terrance P. Flynn presided over the meeting. Corporate Secretary Delince kept the Minutes.

Introduction

Chairman Flynn welcomed committee members Trustees Nicandri and LeChase, the Authority's Chairman and senior staff to the meeting. He said the meeting had been duly noticed as required by the Open Meetings Law and called the meeting to order pursuant to section B(4) of the Audit Committee Charter.

1. Adoption of the Proposed Meeting Agenda

Upon motion made and seconded the agenda for the meeting was adopted as amended.

2. **Motion to Conduct an Executive Session**

Mr. Chairman, I move that the Authority conduct an executive session to discuss matters leading to the appointment, employment, promotion, demotion, discipline, suspension, dismissal or removal of a particular person or corporation. Upon motion made and seconded, an executive session was held.

3. **Motion to Resume Meeting in Open Session**

Mr. Chairman, I move to resume the meeting in Open Session. Upon motion made and seconded, the meeting resumed in Open Session.

4. Consent Agenda:

Upon motion made and seconded the Consent Agenda was approved as amended.

a. Approval of the Minutes

Upon motion made and seconded, the Minutes of the Committee's Regular Meeting held on September 24, 2013 were approved.

b. Internal Audit Activity Report – December 31, 2013

The Vice President of Internal Audit submitted the following report:

"SUMMARY

The Internal Audit Activity Report covers the performance of the Internal Audit Department for the period January 1 through December 31, 2013. The report provides the status of the 2013 Audit Plan as of December 31, 2013, including a summary of completed audits, audits in progress and reports issued (Exhibit '4b-A').

BACKGROUND

The Internal Audit Department is an independent, objective and consulting function designed to add value by improving the Authority's internal control structure and operations. It helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate, test and improve the effectiveness of internal controls, risk management and governance processes.

The Audit Committee Charter states that the Committee shall provide oversight of the Office of Internal Audit ('OIA') and the OIA's resources and activities to facilitate the OIA's improvement of internal controls. In addition, the Committee shall meet at least three times a year with the head of the OIA for the purpose of reviewing audit activities, audit findings, management's responses, remedial action plans, and providing the OIA with an opportunity to discuss items and topics of relevance to the Audit Committee.

The purpose of this report is to provide the Audit Committee the status of the 2013 Internal Audit Plan, which was approved by the Committee at its meeting on March 21, 2013."

Discussion Agenda:

5. Year-End 2013 Financial Report

“The Vice President and Controller submitted the following report:

Pursuant to Section 2800 of the Public Authorities Law, as amended by the Public Authorities Accountability Act of 2005 (‘PAAA’), the Authority is required to file its financial report for the year ended December 31, 2013 and submit this report to the Governor, legislative leaders, the State Comptroller and the Authorities Budget Office. The PAAA reflects the State’s commitment to maintaining public confidence in public authorities by ensuring that the essential governance principles of accountability, transparency and integrity are followed at all times.

This year-end 2013 financial report includes financial statements that present the financial position and results of operations of the Authority as of December 31, 2013 under generally accepted accounting principles. The report is prepared by staff and the financial statements are audited by independent accountants from KPMG LLP. As required by the PAAA, the financial reports have been certified by the Authority’s chief executive officer and chief financial officer. After the Audit Committee’s review, the 2013 financial report is scheduled to be presented for approval by the Authority’s Trustees at their meeting later today. Changes of particular significance have been highlighted in the attached draft (Exhibit ‘5-A’) to facilitate the Audit Committee’s review.

REQUESTED ACTION

It is requested that the Audit Committee recommend that the Authority’s Trustees approve the financial statements for the year ended December 31, 2013.”

Mr. Thomas Concadoro referred to the financial statements for the year 2013 provided to the Audit Committee members with items of note and significant changes from prior years highlighted. He indicated that the financials had been audited by KPMG and certified by the Chief Financial Officer and asked if the Committee members had any questions.

The following resolution, as submitted by the Vice President and Controller, was unanimously approved by the Audit Committee.

WHEREAS, the Executive Vice President and Chief Financial Officer and Vice President and Controller have prepared, reviewed and submitted for consideration of the Audit Committee the attached financial statements for the year ending 2013; and

WHEREAS, the Audit Committee has itself reviewed the attached financial statements;

NOW THEREFORE BE IT RESOLVED, That the Audit Committee recommends that the Authority’s Trustees approve the financial statements for the year ended December 31, 2013.

6. Summary of 2013 Annual Audit of Financial Statements

Mr. Kenneth Deon, KPMG's Audit Engagement Partner, presented an overview of the Authority's 2013 Annual Audit of Financial Statements (Exhibit "6-A"). He introduced Mr. Scott Heiser, the Senior Manager on the Audit and Mr. Nicholas DiVirgilio, Manager. He said they would be presenting the results of the audit, risks and issues they considered and the audit procedures.

Mr. Deon said KPMG would be issuing an unmodified opinion on the Authority's financial statements for the year 2013. He said that the terminology used in the profession had changed since the prior year due to a new auditing standard and that this was the new term for a positive audit report. Mr. Deon also reported that in performing the audit, KPMG did not identify any material weaknesses or significant deficiencies in the Authority's internal controls.

Mr. Heiser provided an overview of the items KPMG reviewed as outlined in the audit plan provided to the Committee in September. He said the items tested included revenues and derivatives; also recoverability of deferred assets and regulatory assets. In addition, they completed testing of investments, and this was outlined in the Compliance Report KPMG will issue to the Authority.

Mr. DiVirgilio provided highlights of the procedures used to address audit risks and issues to the Committee. For example, they performed detailed testing on Revenues and Accounts Receivables to ensure that they are appropriately recorded. The firm's Valuation specialists were used to test the fair value of Derivatives. Regulatory Assets and Deferred Charges were tested and reviewed to ensure they are recoverable over time. Analytical procedures were used; inquiries were made with Authority management and staff who have financial reporting roles. He said KPMG did not identify any deficiencies in the internal control procedures.

With regard to other required communication, Mr. DiVirgilio said no issues came up during the audit that KPMG needed to communicate to the Audit Committee.

Mr. DiVirgilio said KPMG will be issuing the Audit Opinion on the Authority's Financial Statements, the Investment Compliance, and the Internal Controls Reports, as well as the SAS 114 Letter. He ended by saying that KPMG would not be issuing a Management Letter this year.

In response to a question from Authority Chairman Koelmel, Mr. Deon said the fact that a Management Letter is not being issued is a complement to the Authority since it is an indication of a very strong internal control system over financial reporting on the part of the Authority.

Responding to a question from Trustee Nicandri, Mr. Deon said the new audit standard was issued by the AICPA last year. The “unmodified” opinion is the equivalent of the “unqualified” opinion issued in prior years. The new auditing standard clarifies the responsibilities of the Audit Committee, Authority management and the Auditors with respect to the financial statements.

7. **Risk Management Update** – TABLED

8. **2014 Internal Audit Plan** – TABLED

9. **Next Meeting**

Chairman Flynn said that the next regular meeting of the Audit Committee will be held on **Tuesday, July 29, 2014**, at the Clarence D. Rappleyea Building in White Plains, New York.

Closing

On motion made and seconded, the meeting was adjourned by the Chairman at approximately 10:30 a.m.

A handwritten signature in black ink, appearing to read "Karen Delince". The signature is fluid and cursive, with the first name "Karen" and last name "Delince" clearly distinguishable.

Karen Delince
Corporate Secretary

March 25, 2014

EXHIBITS

For

March 25, 2014

Meeting Minutes

Audit Committee

Internal Audit Activity Report
December 31, 2013

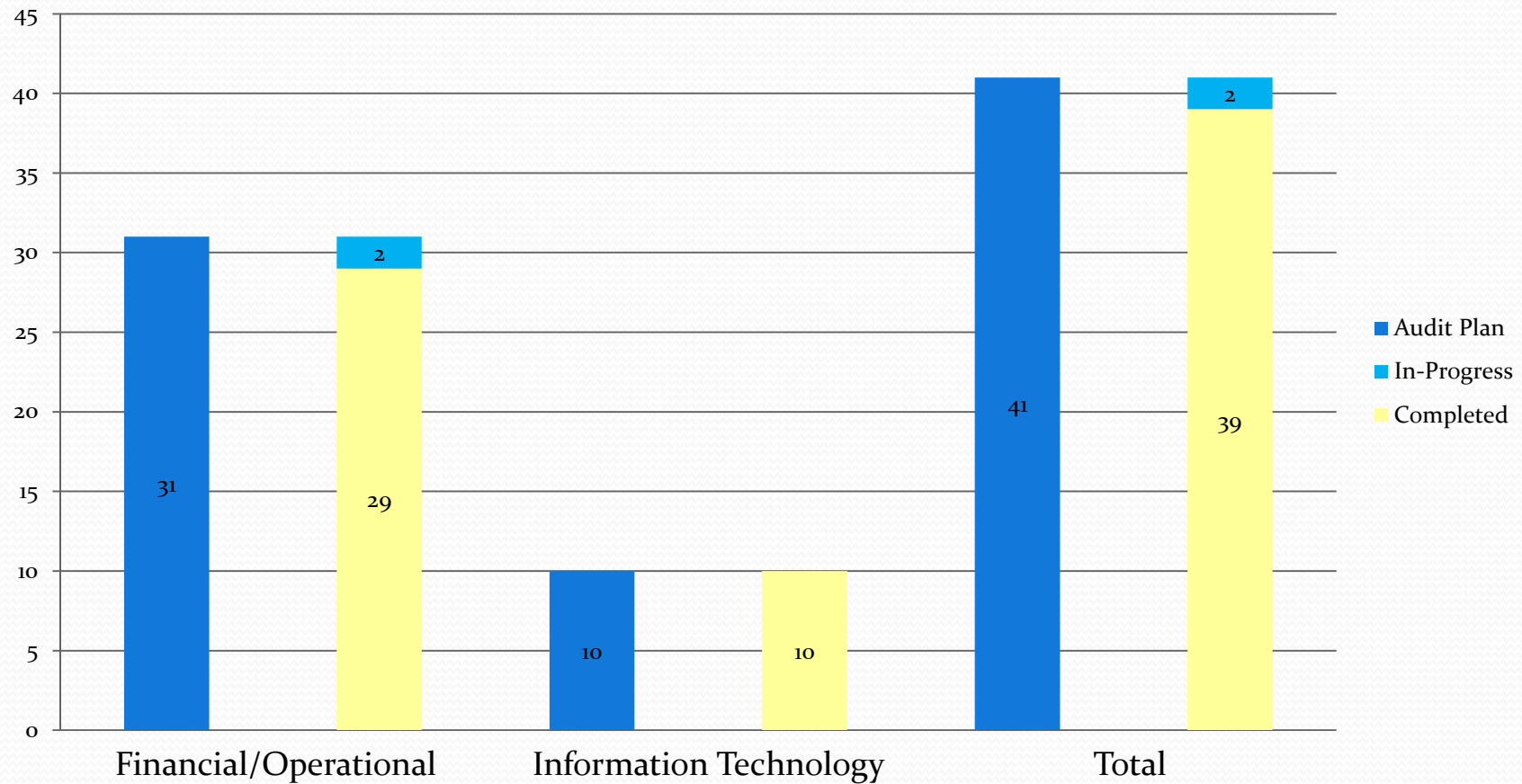
2013 INTERNAL AUDIT PLAN
ACTIVITY REPORT
12/31/13
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2013 INTERNAL AUDIT PLAN ACTIVITY REPORT 12/31/13 SUMMARY

- Completed 39 audits and projects including 29 financial/operational and 10 information technology audits.
- Two (2) audits in progress as of 12/31/13.
- Ninety-five (95) percent of the Plan was completed exceeding our performance target of 90%.
- Issued 37 audit reports containing 114 recommendations to improve internal controls/operational efficiency.
- All issues and recommendations are being appropriately addressed by management and have either been implemented or are scheduled for implementation.
- As required by professional auditing standards, an independent Quality Assessment Review on NYPA's Internal Audit activities was conducted by the Institute of Internal Auditors.
- Internal Audit is organizationally independent and no restrictions have been placed on Internal Audit work.

2013 INTERNAL AUDIT PLAN
ACTIVITY REPORT
12/31/13
AUDIT PLAN STATUS



2013 INTERNAL AUDIT PLAN ACTIVITY REPORT 12/31/13 AUDIT PLAN UPDATE

FINANCIAL

- Energy Efficiency – Statewide Program (C)
- ReCharge NY Customer Revenues (IP)
- Energy Hedging Transactions (C)
- NYISO Energy Settlements – LSE (C)
- Flynn/Sound Cable Revenues (C)
- Headquarters Procurement (Consulting Contracts) (C)
- SENY Revenues (C)
- Energy Efficiency Contractors (SENY) (C)
- Facility Management (C)
- Energy Efficiency Contractors (Statewide) (C)
- NYISO Ancillary Services/Transmission Charges (C)
- (2)• Headquarters Accounts Payable
 - Headquarters Travel & Living Expenses (C)
 - Purchasing/Warehousing – SENY (C)
 - SENY Finance & Administration/HR (C)
 - CEC Finance & Administration/HR (C)
 - St. Lawrence Finance & Administration/HR (C)
 - Headquarters Business Expenses (Consulting) (C)
- (1)• Navigant Consulting Contracts (C)
- (1)• Headquarters Payroll (C)

INFORMATION TECHNOLOGY

- NERC – CIP Compliance (C)
- IT Disaster Recovery – Niagara (C)
- IT Disaster Recovery – Energy Control Center (C)
- SAP Materials Management (C)

- (1) Audit Added
- (2) Audit Postponed
- (3) Combined with NERC-CIP Audit

INFORMATION TECHNOLOGY (Continued)

- (2)• SAP Accounts Payable
 - Electronic Record Management System (Livelink) (C)
 - Time Warner Wide Area Network (C)
 - Internet/Intranet Security (C)
- (1)• Procurement E-Sourcing Pre-Implementation Review (C)
- (3)• Intrusion Prevention and Monitoring
- (2)• SAP Project Systems
- (1)• Health Insurance Portability and Accountability Act (HIPAA) Security (C)
- (1)• SAP Human Resources (C)

OPERATIONAL/COMPLIANCE

- ReCharge NY Program Management (C)
- Emergency Management (C)
- Lewiston Pump Generation Plant LEM (C)
- Safety Program (C)
- Transmission LEM (IP)
- Western Region O&M (C)
- Fuel Operations (C)
- 500 MW O&M (C)
- Budgetary Control – O&M and Capital (C)
- Transmission O&M Follow-up (C)
- Physical Security Program (C)

OTHERS

- Vendor Contract Audits (C)
- Assistance to KPMG (C)
- RNY Job Commitment Audits (C)

C = Completed
IP = In-Progress

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
Energy Hedging	Evaluate the adequacy and effectiveness of internal controls over risk management activities related to energy hedging transactions and verify compliance with established policies, procedures and guidelines.	<p>Controls are operating effectively, except in the following areas:</p> <ul style="list-style-type: none"> • The Procedure for Energy Commodity & Credit Risk Management is not updated to reflect the current processes. • Energy Commodity & Credit Risk Management does not have established minimum guidelines documenting the requirements for the validation of new hedging strategies. • The validation of hedge transactions for conformity against the strategy is not documented. • For some of NYPA's hedge transaction counterparties, NYPA does not have International Swaps and Derivatives Association conforming agreements with associated Credit Support Annexes (CSAs).

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/Recommendations
Health & Safety	Review processes, procedures and controls over the Health and Safety Program. Review Health & Safety performance metrics. Verify compliance with NYPA policies and procedures. Confirm the resolutions of prior audit issues.	<p>The following key issues were raised:</p> <ul style="list-style-type: none"> • There is no support for determining whether a reported incident should be included or excluded on the Health & Safety recordable incident log. • Documentation supporting Level 2 performance metrics was not readily available for some sites. • There are inaccuracies in the reported quantity of Near Misses and Safety Walk-Downs. • There are no written procedures for providing Safety training to contractors working at NYPA sites. • The Safety Training Policy has not been updated since 1996.
SAP Materials Management	Evaluate the adequacy and effectiveness of internal controls over SAP Materials Management activities and ensure compliance with established policies, procedures and guidelines.	<p>The following key issues were raised:</p> <ul style="list-style-type: none"> • More than 500 SAP users have access to confidential and Personally Identifiable Information (e.g. social security number, vendor bank account number) which was inadvertently disclosed in the SAP Materials Management module. • Vendor master additions and changes are not being reviewed.

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
Western Region O&M	Evaluate the effectiveness of processes, procedures and controls over plant maintenance and operations, and to ensure compliance with established policies, procedures and regulatory guidelines.	<p>The following key issues were raised:</p> <ul style="list-style-type: none"> • The Monthly Operational Summary Report should include the performance targets and the reasons for significant variances. • The monthly review of outstanding Priority 2 work orders should include an aging analysis and the status of high priority preventative maintenance work orders. • There is no documented review of canceled work orders.
NERC – CIP Compliance	Evaluate NYPA’s North American Electric Reliability Corporation (NERC) Critical Infrastructure Protection (CIP) Compliance Program to determine its adequacy and effectiveness and for compliance with the Authority’s policies and procedures and applicable laws and regulations.	<ul style="list-style-type: none"> • The following key issues were raised to improve internal controls: • No action is being taken at the respective facilities to remediate issues and/or recommendations identified during the periodic internal assessments. • The Technical Compliance Group is responsible for ownership and monitoring on some of the NERC-CIP control processes resulting in a segregation of duties issue. • The Cyber Security Incident Response Plan should be updated in a timely manner and Incident Test Response Plan should occur annually and evidence should be maintained. • There is currently no inventory of information documents that are classified as “controlled”.

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
Emergency Management	Evaluate NYPA's Emergency Management Plan to determine its adequacy and effectiveness and for compliance with NYPA's policies and procedures.	<ul style="list-style-type: none"> • The Comprehensive Emergency Management Plan does not have stated goals and objectives, nor does it contain clear lines of responsibilities. • At the St. Lawrence and Niagara Plants, there is an inability to notify all occupants during an emergency event in a timely manner. • Training has not been provided to the sites by Headquarters personnel, as it pertains to Emergency Management. In addition, exercises and drills at the facilities are infrequent, with little evaluation and follow-up. • The current roles and responsibilities of Headquarters Emergency Management are unclear in its oversight responsibilities of Emergency Management activities. • A comprehensive hazard/vulnerability analysis is not in place.

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
Transmission O&M	Evaluate the adequacy and effectiveness of internal controls over Transmission O&M processes and procedures, including Right-of-Way Vegetation Management Program, Transmission Performance Procedures and Transmission Line Maintenance Procedures. Verify compliance with NYPA policies and procedures.	<ul style="list-style-type: none"> • Actual performance data for the Transmission performance metrics should be reviewed by supervisory personnel. • Time and Material invoices should be approved by the respective Regional Foresters. • The Geographical Information System should be updated monthly for adequate management review and monitoring of results.
Energy Efficiency SENY Implementation Contractors	Determine that vendor charges were supported, approved and in agreement with contract terms and conditions and the related Customer Installment Commitment.	Vendor billings to the Authority were supported, approved and in compliance with the terms of the contracts and related Customer Installment Commitments.
SAP – Human Resources	Evaluate the adequacy and effectiveness of internal controls over SAP Human Resources. Review user access/security controls, configuration controls, Employee Master Record Changes, Data Interface Validation and Personal Identifying Information Privacy.	<ul style="list-style-type: none"> • There were 15 employee records that show different retirement tiers when comparing Human Resources and Payroll Files. • Controls over the activities reviewed are operating effectively.

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
ReCharge New York Program	Evaluate the adequacy and effectiveness of controls designed to administer the ReCharge NY Program, ensure ongoing compliance with legislative mandates and ensure the program is being administered in accordance with NYPA's governance documents.	Internal controls over the ReCharge NY Program are operating effectively. There were no significant issues raised.
Statewide Implementation Contractors	Determine that vendor charges were supported and in agreement with contract terms and conditions and the related Customer Installment Commitment.	Vendor billings to the Authority were supported, approved and in compliance with the terms of the contracts and related Customer Installment Commitments.
St. Lawrence/FDR Project Finance & Administration and Human Resources	Review procedures, processes and controls over budget monitoring, accounts payable, payroll, travel and living expenses and human resources. Verify compliance with established NYPA policies and procedures.	Internal controls are operating effectively. The following recommendations were made: <ul style="list-style-type: none"> • The process for verifying existence of Plant Assets should be formalized. • Petty Cash funds should not be used to pay non-Petty Cash items.
Clark Energy Center Finance & Administration and Human Resources	Review procedures, processes and controls over budget monitoring, accounts payable, payroll, travel and living expenses and human resources. Verify compliance with established NYPA policies and procedures.	Internal controls were found to be adequate and effective. The following recommendations were made: <ul style="list-style-type: none"> • The facility should maintain a list of personnel who are authorized to approve overtime. • The Petty Cash Policy should be complied with and non-Petty Cash items should not be paid from the Petty Cash funds.

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
Operation Technology Disaster Recovery Plan - Niagara	Evaluate the IT Disaster Recovery Plan to determine if it is adequate to ensure the recovery of critical systems, applications, data and operations in the Niagara Power Project. Determine that the plan has been adequately tested and updated based on test results.	The Disaster Recovery Plan can be improved by considering a recovery strategy that addresses the risk of catastrophic events that would render the Control Room and SCADA server room inoperable/inaccessible.
Headquarters Payroll	Evaluate the adequacy and effectiveness of internal controls over Headquarters Payroll and ensure compliance with established policies, procedures and regulatory guidelines. The scope of the audit included: <ul style="list-style-type: none"> •Payroll Processing •Processing of Salary Changes, New Hires and Terminations •Payroll Benefits Deductions •Processing of Third Party Payments 	Controls were found to be effective except for controls over the review of payroll changes. Key issues raised: <ul style="list-style-type: none"> •Procedures over key payroll processes should be documented. •A detailed review of payroll changes (new hires, salary changes, terminations) processed by the Payroll department should be performed by the Human Resources Information Systems group. •Documentation of the annual reconciliation process between Ceridian and Benefits should be formalized.

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
500 MW Power Plant	<p>Evaluate the effectiveness of processes, procedures and controls over:</p> <ul style="list-style-type: none"> •Plant Maintenance Procedures •Plant Performance Management •Maintenance Contract Management and Cost Control •General Information Technology Controls 	<p>The following key issues were raised:</p> <ul style="list-style-type: none"> •Supervisory review of certain high priority corrective maintenance work orders are not consistently documented in the Maintenance System (Maximo). •An independent review of Plant Performance Reporting data is not being performed. •Periodic training covering the review of key plant operations and maintenance procedures is needed. •A formal Disaster Recovery Plan that covers the recovery of critical operational applications in the event of a disaster does not exist.
Customer Billing – ReCharge NY	<p>Evaluate the adequacy and effectiveness of controls over billings to ReCharge NY customers and verify compliance with policies and procedures. The audit covered the following:</p> <ul style="list-style-type: none"> •Customer Billing including Verification of Billing Rates •Energy Charge Adjustment •Recording of Billing Transactions in SAP General Ledger •Follow-up on Prior Audit Recommendations 	<p>Internal controls are operating effectively. There were no issues requiring corrective action identified in this audit.</p>

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
Energy Efficiency	<p>Evaluate the adequacy and effectiveness of internal controls over Energy Services Programs and ensure compliance with established policies, procedures and regulatory guidelines. Review the following areas:</p> <ul style="list-style-type: none"> •Performance Management and Reporting •Project Assignment •Program/Project Authorization •Project Management/Cost Control •Credit Risk and Write Off •Project Risk Management 	<p>Internal controls over certain activities reviewed need improvement:</p> <ul style="list-style-type: none"> •Document requirements in Energy Efficiency System (Primavera) should be enhanced to include evidence of review and concurrence by the Project Manager. •Meeting minutes of the Implementation Contractor (IC) Assignment Committee should be formalized to include the agenda, discussion topics and documentation to support the Committee approval of the IC recommendation. •A second level review of the MMBTU saved calculation results in the Primavera System should be performed. •Monitoring reports identifying exceptions and resolution should be maintained on file to ensure transparency and awareness of non-compliance. •Projects that have been closed without a Final Customer Installation Commitment should be reviewed for trends and potential higher level issues.

2013 INTERNAL AUDIT PLAN

ACTIVITY REPORT

12/31/13

REPORT RECAP

Report Name	High-Level Audit Objectives	Observations/Findings/ Recommendations
NYISO Energy & Ancillary Service Settlements – Load Serving Transactions	<p>Evaluate the adequacy and effectiveness of controls over the following areas:</p> <ul style="list-style-type: none"> •Energy Scheduling •Energy Settlement •Ancillary Service Settlements •Allocation of NYISO Ancillary Charges to ReCharge NY Customers •Recording of Energy and Ancillary Service Settlements 	<p>Internal controls need improvements in the following areas:</p> <ul style="list-style-type: none"> •The procedures for reviewing potential NYISO billing anomalies should be updated and the billing anomaly program tested. •Review procedures to ensure forecast data of RNY customers were accurately and completely submitted to the NYISO should be documented. •Limitation on the current functionality of the nMarket System leads to inefficiencies in performing variance analysis procedures. •An anomaly check should be developed to verify NYISO Ancillary MWh used to bill NYPA for Ancillary service charges.

Exhibit A

NEW YORK POWER AUTHORITY

Financial Statements

December 31, 2013 and 2012

NEW YORK POWER AUTHORITY

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Management Report

Management is responsible for the preparation, integrity and objectivity of the financial statements of the Power Authority of the State of New York (the Authority), as well as all other information contained in the Annual Report. The financial statements have been prepared in conformity with U.S. generally accepted accounting principles and, in some cases, reflect amounts based on the best estimates and judgments of management, giving due consideration to materiality. Financial information contained in the Annual Report is consistent with the financial statements.

The Authority maintains a system of internal controls to provide reasonable assurance that transactions are executed in accordance with management's authorization, that financial statements are prepared in accordance with U.S. generally accepted accounting principles and that the assets of the Authority are properly safeguarded. The system of internal controls is documented, evaluated and tested on a continuing basis. No internal control system can provide absolute assurance that errors and irregularities will not occur due to the inherent limitations of the effectiveness of internal controls; however, management strives to maintain a balance, recognizing that the cost of such system should not exceed the benefits derived.

The Authority maintains an internal auditing program to independently assess the effectiveness of internal controls and to report findings and recommend possible improvements to management. This program includes a comprehensive assessment of internal controls as well as testing of all key controls to ensure that the system is functioning as intended. Additionally, as part of its audit of the Authority's financial statements, KPMG LLP, the Authority's independent auditors, considers internal controls over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for purpose of expressing an opinion on the effectiveness of the Authority's internal controls over financial reporting. Management has considered the recommendations of its internal auditors, the Office of the State Comptroller (OSC), and the independent auditors concerning the system of internal controls and has taken actions that it believed to be cost-effective in the circumstances to respond appropriately to these recommendations. Based on its structure and related processes, management believes that, as of December 31, 2013, the Authority's system of internal controls provides reasonable assurance as to the integrity and reliability of the financial statements, the protection of assets from unauthorized use or disposition and the prevention and detection of fraudulent financial reporting.

The members of the Authority's Board of Trustees, appointed by the Governor, by and with the advice and consent of the Senate, are not employees of the Authority. The Trustees' Audit Committee meets with the Authority's management, its Vice President of Internal Audit and its independent auditors periodically, throughout the year, to discuss internal controls and accounting matters, the Authority's financial statements, the scope and results of the audit by the independent auditors and the periodic audits by the OSC, and the audit programs of the Authority's internal auditing department. The independent auditors, the Vice President of Internal Audit and the Vice President & Chief Ethics and Compliance Officer have direct access to the Audit Committee.



Donald A. Russak
Executive Vice President and Chief Financial Officer

March 25, 2014



KPMG LLP
515 Broadway
Albany, NY 12207

Independent Auditors' Report

The Board of Trustees
Power Authority of the State of New York:

Report on the Financial Statements

We have audited the accompanying financial statements of the Power Authority of the State of New York (the Authority), which comprise the statements of net position as of December 31, 2013, and 2012, and the related statements of revenues, expenses and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of December 31, 2013 and 2012, and the changes in net position, and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis and Required Supplementary Information sections be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March [X,] 2014 on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

KPMG LLP

Albany, New York
March [X,] 2014

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Overview of the Financial Statements

This report consists of three parts: management's discussion and analysis, the basic financial statements, and the notes to the financial statements.

The financial statements provide summary information about the New York Power Authority's (the Authority) overall financial condition. The notes provide explanation and more details about the contents of the financial statements.

The Authority is considered a special-purpose government entity engaged in business-type activities and follows financial reporting for enterprise funds. The Authority's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB). Under the criteria set forth in GASB Statement No. 14, *The Financial Reporting Entity*, as amended by Governmental Accounting Standard (GAS) No. 39, *Determining Whether Certain Organizations Are Component Units* and GAS No. 61, *The Financial Reporting Entity: Omnibus--an amendment of GASB Statements No. 14 and No. 34*, the Authority considers its relationship to the State to be that of a related organization.

Forward Looking Statements

The statements in this management's discussion and analysis (MD&A) that are not purely historical facts are forward-looking statements based on current expectations of future events. Such forward-looking statements are necessarily based on various assumptions and estimates and are inherently subject to various risks and uncertainties, including, but not limited to, risks and uncertainties relating to the possible invalidity of the underlying assumptions and estimates and possible changes to or development in various important factors. Accordingly, actual results may vary from those we presently expect and such variations may be material. We therefore caution against placing undue reliance on the forward-looking statements contained in this MD&A. All forward-looking statements included in this MD&A are made only as of the date of this MD&A and we assume no obligation to update any such forward-looking statements as a result of new information, future events or other factors.

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Summary of Revenues, Expenses and Changes in Net Position

The following is a summary of the Authority's financial information for 2013, 2012, and 2011:

	2013	2012	2011	2013 vs. 2012 favorable (unfavorable)	2012 vs. 2011 favorable (unfavorable)
	(In millions, except percentages)				
Operating revenues	\$ 3,030	\$ 2,673	\$ 2,655	13%	1%
Operating expenses:					
Purchased power	934	744	854	(26)	13
Fuel	324	228	258	(42)	12
Wheeling	603	598	548	(1)	(9)
Operations and maintenance	566	558	519	(1)	(8)
Depreciation	228	226	194	(1)	(16)
Total operating expenses	2,655	2,354	2,373	(13)	1
Operating income	375	319	282	18	13
Nonoperating revenues	90	120	145	(25)	(17)
Nonoperating expenses	237	264	192	10	(38)
Net income	228	175	235	30	(26)
Contributed capital	21	—	59		
Change in net position	249	175	294		
Net position – beginning	3,470	3,295	3,001		
Net position – ending	\$ 3,719	\$ 3,470	\$ 3,295		

The following summarizes the Authority's financial performance for the years 2013 and 2012:

The Authority had net income of \$228 million for the year ended December 31, 2013 compared to \$175 million in 2012. The current year increase of \$53 million included higher operating income of \$56 million and lower nonoperating expenses of \$27 million; partially offset by lower nonoperating revenue of \$30 million. Operating income was higher primarily due to higher prices on market-based sales of capacity into the NYISO market. Capacity prices were higher primarily due to the retirement and mothballing of power plants owned by other generators in N.Y. State. Large increases in purchased power and fuel expenses from year to year were substantially offset by the recovery of such costs through operating revenues. Nonoperating expenses were lower in 2013 due to lower voluntary contributions to New York State (\$20 million) combined with lower interest expenses. Nonoperating revenue was lower primarily due to a higher unrealized loss on fixed income securities in the Authority's investment portfolio due to higher market interest rates in 2013.

The Authority had net income of \$175 million for the year ended December 31, 2012 compared to \$235 million in 2011. The decrease in 2012 net income of \$60 million was due to lower nonoperating revenues of \$25 million and higher nonoperating expenses of \$72 million partially offset by higher operating income of \$37 million. Nonoperating revenues were lower primarily due to reduced income on the investment portfolio attributable to the aging of fixed income securities combined with lower market interest rates. In addition, nonoperating revenues for 2011 included a nonrecurring gain of \$11 million, which resulted from a claim settlement against the U.S. Department of Energy, relating to spent fuel disposal at the previously owned nuclear plants. Nonoperating expenses were higher in 2012 primarily due to a \$20 million higher voluntary contribution to New York State and the recognition of higher interest expense (\$52 million) mostly related to interest expense on the capital lease of the Astoria Energy II (AEII) generating station, which began operations in July 2011. The interest expense related to AEII is recovered through customer rates along with the operating expenses for this facility.

Net position increased by \$249 million in 2013 due to positive net income \$228 million and \$21 million of contributed capital related to wind farm assets (see note 5 of the notes to the financial statements).

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Operating Revenues

Operating revenues of \$3,030 million in 2013 were \$357 million or 13% higher than the \$2,673 million in 2012, primarily due to higher prices on market-based sales of energy and capacity. Higher customer revenues resulted from higher sales volumes than 2012 and from the recovery of higher purchased power and fuel costs.

Purchased Power and Fuel

Purchased power costs increased by 26% in 2013 to \$934 million from \$744 million in 2012, primarily due to higher prices for purchased capacity, higher transmission congestion costs and additional transmission capacity purchased under agreement with Hudson Transmission Partners, LLC (HTP) (which went into effect in June 2013 - see note 11(b) "Governmental Customers in the New York City Metropolitan Area" of notes to the financial statements). Fuel costs were \$96 million (42%) higher during 2013, primarily due to higher natural gas prices. The average natural gas price incurred by NYPA increased 34% from \$3.56/MMBtu in 2012 to \$4.78/MMBtu in 2013. The year-to-year price increase principally reflected the extremely low prices in 2012 due to an abnormally warm winter. Prices increased in 2013 primarily due to colder winter temperatures and high withdrawals from storage.

Operations and Maintenance (O&M)

O&M expenses increased by \$8 million, or 1%, in 2013 to \$566 million, primarily due to higher expenses related to non-recurring projects at the Authority's hydro facilities.

Nonoperating Revenues

For 2013, nonoperating revenues decreased by \$30 million, or 25%, primarily due to a mark-to-market loss (\$22 million) on fixed income securities in the Authority's investment portfolio due to higher market interest rates in 2013, and lower income from Entergy (the final payment related to Entergy's purchase of IP2 was made in 2012). Nonoperating revenues for 2013 and 2012 include income recognition of \$72 million and \$71.7 million, respectively, resulting from a value-sharing agreement relating to the nuclear power plants sold by the Authority to subsidiaries of Entergy Corporation in 2000. See note 10(a) "Nuclear Plant Divestiture," of notes to the financial statements, for additional information.

Nonoperating Expenses

For 2013, nonoperating expenses decreased by \$27 million, or 38%, primarily due to a decrease of \$20 million in the Authority's voluntary contribution to New York State (from \$85 million to \$65 million) and slightly lower interest expenses.

Cash Flows

During 2012, the Authority generated cash flows of \$513 million from operations compared to \$391 million in 2012. Cash flows from operating activities for 2013 were higher than 2012 primarily due to higher market-based sales due primarily to higher prices on energy and capacity sales, partially offset by higher purchased power and fuel costs primarily due to higher prices.

Net Generation

Net generation for 2013 was 27.9 million megawatt-hours (MWh) essentially unchanged from the level generated in 2012. Net generation from the Niagara plant in 2013 (13.0 million MWh) was 3% lower than 2012 (13.4 million MWh) due to lower water flows. Net generation from the St. Lawrence plant in 2013 (6.7 million MWh) was unchanged from 2012 (6.7 million MWh). During 2013, net hydro generation was approximately 97% of long-term average and below 2012, which was 99% of long-term average. Combined net generation of the fossil fuel plants for 2013 was 8.26 million MWh, or 3% higher than 2012 (7.99 million MWh), with a 0.3 million MWh increase attributable to the 500MW plant.

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Summary of Statements of Net Position

The following is a summary of the Authority's statements of net position for 2013, 2012, and 2011:

	2013	2012	2011	2013 vs. 2012	2012 vs. 2011
	(In millions, except percentages)				
Current assets	\$ 1,824	\$ 1,875	\$ 1,692	(3) %	11 %
Capital assets	4,771	4,819	4,910	(1)	(2)
Other noncurrent assets	2,694	2,320	2,224	16	4
Deferred outflows	42	107	209	(61)	(49)
Total assets & deferred outflows	<u>\$ 9,331</u>	<u>\$ 9,121</u>	<u>\$ 9,035</u>	2	1
Current liabilities	\$ 1,058	\$ 1,030	\$ 982	3	5
Noncurrent liabilities	4,554	4,621	4,758	(1)	(3)
Total liabilities	<u>5,612</u>	<u>5,651</u>	<u>5,740</u>	(1)	(2)
Net position	<u>3,719</u>	<u>3,470</u>	<u>3,295</u>	7	5
Total liabilities and net position	<u>\$ 9,331</u>	<u>\$ 9,121</u>	<u>\$ 9,035</u>	2	1

The following summarizes the Authority's statements of net position variances for the years 2013 and 2012:

In 2013, current assets decreased by \$51 million (3%) to \$1,824 million primarily due to a decreases in cash resulting from the timing of payments and receipts. Capital assets decreased by \$48 million (1%) to \$4,771 million, primarily due to the excess of depreciation over additions to plant and construction in progress. Other noncurrent assets increased by \$374 million (16%) primarily due to an increase in the nuclear decommissioning fund, transmission line interconnection costs associated with HTP and energy efficiency program work in progress. Deferred outflows decreased by \$65 million (61%) primarily due to changes in fair value and settlements of derivative instruments. Current liabilities increased by \$28 million (3%), to \$1,058 million, primarily due to increases in short-term debt (\$20 million) utilized to finance energy efficiency projects. Noncurrent liabilities decreased by \$80 million (1%) to \$4,554 million primarily due to the decreases in long-term debt (\$96 million), risk management activities – derivatives (\$63 million) and Niagara relicensing (\$26 million), partially offset by increases in the nuclear plant decommissioning obligation (\$114 million). The decrease in long-term debt was due to scheduled maturities. The increase in the nuclear plant decommissioning obligation reflects the increase in investment earnings of the decommissioning fund (i.e., the Authority's obligation is limited to no more than the amount in the decommissioning fund and therefore the liability increases or decreases to reflect the fair value of the decommissioning fund). The changes in net position for 2013 and 2012 are discussed in the summary of revenues, expenses and changes in net position in this Management's Discussion and Analysis.

In 2012, current assets increased by \$183 million (11%) to \$1,875 million primarily due to increases in cash and investments reflecting the investment of cash generated by operations. Capital assets decreased by \$91 million (2%) to \$4,819 million, primarily due to a full year of depreciation related to AEII capital lease, offset by additions to construction in progress. Other noncurrent assets increased \$96 million (4%) primarily due to an increase in the Decommissioning Trust Fund investment portfolio and energy efficiency program work in progress, partially offset by a decrease in the capital fund investment portfolio and other deferred charges. Deferred outflows decreased by \$102 million (49%) primarily due to the expiration of a medium-term forward energy swap in December 2012. Current liabilities increased by \$48 million (5%), to \$1,030 million, primarily due to increases in liabilities related to short-term debt (\$57 million), reclassifications related to the Niagara relicensing (\$12 million), long-term debt and capital lease obligations due within one year (\$12 million) and other various accruals (\$23 million) partially offset by decreases in fair market values related to the Authority's energy commodity hedging transactions (\$59 million). Noncurrent liabilities decreased by \$137 million (3%) to \$4,621 million primarily due to the decreases in long-term debt resulting from reclassifications to long-term debt due within one year and scheduled repayments of debt (\$132 million), risk management activities – derivatives (\$45 million), Niagara relicensing (\$26 million), and various other deferred credits (\$46 million) partially offset by increases in the nuclear plant decommissioning obligation (\$96 million) and the issuance of \$25 million Subordinated Notes, Series 2012. The increase in the nuclear plant decommissioning obligation reflects the increase in investment earnings of the decommissioning fund (i.e., the Authority's obligation is limited to no more than the amount in the decommissioning fund and therefore the liability increases or decreases to reflect the fair value of the decommissioning fund). The changes in net position for

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2012 and 2011 are discussed in the summary of revenues, expenses and changes in net position in this Management's Discussion and Analysis.

Capital Asset and Long-Term Debt Activity

The Authority currently estimates that it will expend approximately \$1,226 million for various capital improvements over the five-year period 2014-2018. The Authority anticipates that these expenditures will be funded using existing construction funds, internally generated funds and additional borrowings. Such additional borrowings are expected to be accomplished through the issuance of commercial paper notes and/or the issuance of long-term fixed rate debt. Projected capital requirements during this period include (in millions):

Plant Modernization Program (Lewiston Pump Generation Plant)	\$	269
Switchyard Modernization Program (Niagara, St. Lawrence, Blenheim-Gilboa, Clark Energy Center)		156
Breaker and Relay Replacement Program (Niagara, St. Lawrence, Blenheim-Gilboa)		102
Marcy South Series Compensation		68
Information Technology Infrastructure & Initiatives		58
MA1 & MA2 Line - 230 kV Transmission Line		45
Relicensing And Compliance (Niagara, St. Lawrence, Blenheim-Gilboa)		34
St. Lawrence Generator Step-Up (GSU) Transformer Replacement		25
Substation Upgrades (Adirondak, Plattsburgh, Saranac, Willis, Alcoa)		37
St. Lawrence Headgate Automation		21
Pv-20 Line Assessment/Replacement/Submerged Portion Only		20
Massena 765/230 Kv Mult-Unit Autotransformer Replacement		19
Niagara Stator Rewind And Restack Project - Phase III		19
Small Hydro Facilities-Units Upgrades		15
Convertible Static Compensator Control System Upgrade		11
St. Lawrence Station Service Upgrade		10
Niagara 115Kv OCB Upgrade		10
Rotor Modification For Stress Redistribution		10
Blenheim-Gilboa Facility Improvement Project		10
Niagara Governor And Controls Upgrade		10
Shunt Reactor (Coopers Corners)		9
Mark VI - Controls Replacement		9
Other (projects less than \$9 million)		259
	\$	<u><u>1,226</u></u>

In addition, the Authority's capital plan includes the provision of \$1,185 million in financing for Energy Services and Technology projects to be undertaken by the Authority's governmental customers and other public entities in the State. It should also be noted that due to projects currently under review as well as energy initiatives announced in the Governor's State of the State address, there is a potential for significant increases in the capital expenditures indicated in the table above. Such additional capital expenditures would be subject to evaluation and Trustee approval.

In December 2012, the Authority's Trustees approved a \$726 million Transmission Life Extension and Modernization ("LEM") Program on the Authority's Transmission system through 2025. The Transmission LEM Program encompasses transmission assets in the Central, Northern and Western regions of New York and will include work to be done such as upgrades, refurbishments and replacements associated with switchyards and substations, transmission line structures or towers and associated hardware and replacement of the submarine cable on the PV-20 line. Reinvestment in this strategic component of the Authority's overall mission supports the repair, upgrade and/or expansion of the transmission infrastructure. The Authority intends to finance this LEM Program with internal funds and proceeds from debt obligations to be issued by the Authority.

In 2010, the Authority's Trustees approved a \$460 million Life Extension and Modernization ("LEM") Program at the Niagara project's Lewiston Pump-Generating Plant, of which \$253 million of expenditures have been authorized and \$92 million spent as of December 31, 2013. The work to be done includes a major overhaul of the plant's 12 pump turbine generator units. This LEM Program will increase pump and turbine efficiency, operating efficiency, and the peaking capacity of the overall Niagara project. The Authority filed an application with the Federal Energy Regulatory Commission (FERC) for a non-capacity license amendment in connection with the

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program on December 15, 2011 and supplemented it on February 15, 2012. The amendment was approved with a FERC order issued on April 25, 2012. The unit work began in late 2012, with the final unit to be completed in 2020.

By order issued March 15, 2007, FERC issued the Authority a new 50-year license for the Niagara Project effective September 1, 2007. In doing so, FERC approved six relicensing settlement agreements entered into by the Authority with various public and private entities. In 2007, the Authority estimated that the capital cost associated with the relicensing of the Niagara project would be approximately \$495 million. This estimate does not include the value of the power allocations and operation and maintenance expenses associated with several habitat and recreational elements of the settlement agreements. As of December 31, 2013, the balance in the liability associated with the relicensing on the statement of net position is \$277 million (\$31 million in current and \$246 million in noncurrent liabilities).

More detailed information about the Authority's capital assets is presented in notes 2 and 5 of the notes to the financial statements.

Capital Structure

	2013	2012	2011
		(In millions)	
Long-term debt, net of current maturities:			
Senior:			
Revenue bonds	\$ 958	\$ 1,012	\$ 1,064
Adjustable rate tender notes	96	106	115
Subordinated:			
Subordinated Notes, Series 2012	24	24	—
Commercial paper	70	102	173
Total long-term debt, net of current maturities	1,148	1,244	1,352
Net position	3,719	3,470	3,295
Total capitalization	\$ 4,867	\$ 4,714	\$ 4,647

In November 2012, the Authority's Trustees authorized the issuance of Subordinated Notes, Series 2012 (Subordinated Notes), in a principal amount not to exceed \$30 million for the purpose of accelerating the funding for the State Parks Greenway Fund, which was established pursuant to the Niagara Relicensing Settlement entered into by the Authority and the New York State Office of Parks, Recreation & Historic Preservation in connection with the Niagara project's relicensing. The Authority issued the Subordinated Notes on December 18, 2012 in the amount of \$25 million. These Subordinated Notes are subordinate to the Series 2003 A Revenue Bonds, the Series 2006 A Revenue Bonds, the Series 2007 A, B, and C Revenue Bonds, the Series 2011 A Revenue Bonds and the Adjustable Rate Tender Notes.

During 2013, long-term debt, net of current maturities, decreased by \$113 million, primarily due to scheduled maturities and cash funding of capital expenditures.

During 2012, considering the issuance of the 2012 Subordinate Notes, long-term debt, net of current maturities, decreased by \$108 million, primarily due to scheduled maturities, early extinguishments of debt and cash funding of capital expenditures.

Total debt to equity ratio as of December 31, 2013, decreased to .46-to-1 from .51-to-1 as of December 31, 2012 and from 1.45-to-1 in 2003. Total debt as of December 31, 2013 is at its lowest level since December 31, 1975.

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Debt Ratings

	<u>Moody's</u>	<u>Standard & Poor's</u>	<u>Fitch</u>
NYPA's underlying credit ratings:			
Senior debt:			
Long-term debt (a)	Aa2	AA-	AA
Adjustable rate tender notes	Aa2/VMIG1	AA-/A-1+	N/A
Subordinate debt:			
Subordinate Note, Series 2012	N/A	N/A	AA
Commercial paper	P-1	A-1	F1+

- (a) Long term debt includes certain bonds - Series 2007 A, B and C Revenue Bonds, Series 2006 A Revenue Bonds and Series 2003 A Revenue Bonds - which are covered by Municipal bond insurance. In November 2011, S&P downgraded Assured Guaranty Municipal Corp's AA+ rating (formerly Financial Security Assurance Inc.) to AA-. All other bond insurers' ratings are no longer above the Authority's underlying rating and/or are no longer rated. Consequently, the insured bonds carry the Authority's underlying rating set forth in the table above. The impact of the bond insurers' credit downgrades on the market value of the Authority's insured bonds was not discernible because of the Authority's strong underlying ratings.

The Authority has a revolving credit agreement (Agreement) with The Bank of Nova Scotia, which terminates on September 1, 2015, to provide a supporting line of credit for the purpose of repaying, redeeming or purchasing the Adjustable Rate Tender Notes. Under the Agreement, the Authority may borrow up to the outstanding principle of the ART Notes, which at December 31, 2013 was \$106 million. The Agreement provides for interest on outstanding borrowings at either (i) the Federal Funds Rate plus a percentage, or (ii) a rate based on the London Interbank Offered Rate (LIBOR) plus a percentage. The Authority expects that it will be able to renew or replace this Agreement as necessary. In addition, the Authority also has a \$550 million line of credit with a syndicate of banks supporting the Series1-3 Commercial Paper Notes, as amended, which line expires January 20, 2015. As of December 31, 2013 and 2012, there were no outstanding borrowings under either the Agreement supporting the ART Notes or line of credit supporting the Series1-3 Commercial Paper Notes. More detailed information about the Authority's debt is presented in note 6 of notes to the financial statements.

In December 2012, Fitch Ratings affirmed the Authority's senior and subordinate debt ratings. In December 2013, Standard & Poor's Rating Service affirmed the Authority's senior and subordinate debt ratings and also assigned a positive outlook. Moody's Investor Service, Inc. affirmed the Authority's senior and subordinate debt ratings in December 2013.

Economic Conditions

Competitive Environment

The Authority's mission is to provide clean, low-cost, and reliable energy consistent with its commitment to the environment and safety, while promoting economic development and job development, energy efficiency, renewables and innovation, for the benefit of its customers and all New Yorkers. The Authority's financial performance goal is to have the resources necessary to achieve its mission, to maximize opportunities to serve its customers better and to preserve its strong credit rating.

According to the National Bureau of Economic Research, a recession in the United States began in December 2007 and ended in June 2009. However, the economy continues to grow slowly and unemployment remains high. Forecasted recovery time for these economic conditions ranges from a few to many years. In this environment, the Authority has continued to utilize its financial flexibility to support its mission and its customers.

To maintain its position as a low cost provider of power in a changing environment, the Authority has undertaken and continues to carry out a multifaceted program, including: (a) the upgrade and relicensing of the Niagara and St. Lawrence-FDR projects; (b) long-term supplemental electricity supply agreements with its governmental customers located mainly within the City of New York (NYC Governmental Customers); (c) construction of a 500-megawatt (MW) combined-cycle electric generating plant at the Authority's Poletti plant site (500-MW plant); (d) a long-term electricity supply contract with Astoria Generating LLC for the purchase of the output of a new 550-MW power plant in Astoria, Queens, which entered into service on July 1, 2011; (e) contracting a new 660 MW, seven mile, underground and underwater transmission line connecting into the PJM ISO, which went operational in June 2013; (f) a significant reduction of outstanding debt; and (g) implementation of an enterprise-wide and energy/fuel risk management program. The Authority operates in a competitive and sometimes volatile market environment. Volatility in the energy market has impacted the Authority in its

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role as a buyer and until recent years had resulted in higher costs of purchased power and fuel in its NYC Governmental Customer and other market areas. The NYC Governmental Customer market cost situation is mitigated by the cost-recovery provisions in the long-term supplemental electricity supply agreements and generation from the Authority's 500-MW plant. The Authority also has implemented a restructuring program for its long-term debt through open-market purchases, early retirements and refundings, which has resulted in cost savings and increased financial flexibility. The Authority can give no assurance that even with these measures it will not lose customers in the future as a result of the restructuring of the State's electric utility industry and the emergence of new competitors or increased competition from existing participants.

Through its participation in the NYISO and other commodity markets, the Authority is subject to electric energy price, fuel price and electric capacity price risks that impact the revenue and purchased power streams of its facilities and customer market areas. Such volatility can potentially have adverse effects on the Authority's financial condition. To mitigate downside effects, many of the Authority's customer contracts provide for the complete or partial pass-through of these costs and to moderate cost impacts to its customers, the Authority hedges market risks through the use of financial instruments and physical contracts. Hedges are transacted by the Authority to mitigate volatility in the cost of energy or related products needed to meet customer needs; to mitigate risk related to the price of energy and related products sold by the Authority; to mitigate risk related to margins (electric sales versus fuel use) where the Authority owns generation or other capacity; and mitigation of geographic cost differentials of energy procured or sold for transmission or transportation to an ultimate location. Commodities to be hedged include, but are not limited to, natural gas, natural gas basis, electric energy, electric capacity and congestion costs associated with the transmission of electricity. Any such actions are taken pursuant to policies and procedures approved by the Authority's Trustees and under the oversight of an Executive Risk Management Committee headed by the Chief Financial Officer.

Rate Actions

Power and energy from the St. Lawrence-FDR and Niagara hydroelectric facilities are sold to municipal electric systems, rural electric cooperatives, industrial and other business customers, certain public bodies, investor-owned utilities, and out-of-state customers, as provided for under the state and federal laws. The charges for firm and/or firm peaking power and associated energy sold by the Authority, as applicable, to the fifty-one municipal electric systems and rural electric cooperatives in New York State, two public transportation agencies, three investor-owned utilities for the benefit of rural and domestic customers, and seven out-of-state public customers have been established on the basis of the cost to serve these loads. These charges are among the lowest found throughout the United States. In November 2011, the Authority's Trustees approved a 41-month rate plan providing for certain phased-in increases to these rates which result in effective hydro rate increases of 5.5% on December 1, 2011 and annual increases of approximately 5.5% from May 1, 2012 to May 1, 2014.

Niagara's expansion and replacement power industrial customers and St. Lawrence-FDR's industrial customers are allocated over 40% of the firm contract demand of the plants. Their rates are subject to annual adjustment based on the average of three contractually agreed-upon economic indices reflecting changes in industrial energy prices.

In an order issued January 27, 1999, the Federal Energy Regulatory Commission ("FERC") approved the use of a \$165.4 million transmission system revenue requirement in developing rates for use of NYPA's transmission facilities in the NYISO market. FERC also approved, among other things, the imposition of a NYPA Transmission Adjustment Charge ("NTAC") and the NYPA Transmission Service Charges ("TSC") which are the tariff elements established to effect full recovery of the Authority's annual transmission revenue requirement. In July 2012, the Authority filed for its first requested increase in the revenue requirement with FERC since the implementation of the NYISO. A number of NYISO market participants challenged the level of the increase and settlement talks began with a FERC order dated September 25, 2012. In March 2013 NYPA and intervening parties reached a settlement-in-principle and on May 10, 2013 filed an unconditional settlement for a new revenue requirement of \$175.5 million. FERC accepted the settlement via an order dated October 4, 2013.

Recharge New York Power Program

Chapter 60 (Part CC) of the Laws of 2011 (Chapter 60) established the "Recharge New York Power Program" (RNYPP). The RNYPP is a new power program, administered by the Authority, which has as its central benefit up to 910 MW of low cost power comprised of up to 455 MW of hydropower from the Niagara and St. Lawrence-FDR Projects and up to 455 MW of other power procured by the Authority from other sources. The 910 MW of power is available for allocation as provided by Chapter 60 to eligible new and existing businesses and not-for-profit corporations under contracts of up to seven years. RNYPP was effective beginning July 1, 2012.

The RNYPP replaced two other programs, the Power for Jobs (PFJ) and Energy Cost Savings Benefit (ECSB) Programs, which had extended benefits of low-cost power to certain businesses, small businesses and not-for-profit organizations. Those PFJ and ECSB

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Program customers who are in substantial compliance with contractual commitments under the PFJ and ECSB Programs and who apply but do not receive RNYPP allocations are eligible to apply for transitional electricity discounts, as provided for in Chapter 60. This transitional electricity discounts program provides for declining levels of discounts through June 30, 2016 when the program terminates, if payment of such discounts is deemed feasible and advisable by the Authority's Trustees. In June 2012, the Authority's Trustees authorized transitional electricity discount payments of up to \$9 million for the year July 1, 2012 – June 30, 2013. As of December 31, 2013, approximately \$1.2 million of such discounts have been paid.

The hydropower used for the RNYPP was power formerly used to provide low-cost electricity to domestic and rural customers of the three private utilities that serve upstate New York. To mitigate the impacts from the redeployment of this hydropower for the RNYPP, Chapter 60 created a "Residential Consumer Discount Program" (RCDP). The RCDP authorizes the Authority, as deemed feasible and advisable by its Trustees, to provide annual funding of \$100 million for the first three years following withdrawal of the hydropower from the residential and farm customers, \$70 million for the fourth year, \$50 million for the fifth year, and \$30 million each year thereafter, for the purpose of funding a residential consumer discount program for those customers that had formerly received the hydropower that is utilized in the RNYPP. Chapter 60 further authorizes the Authority, as deemed feasible and advisable by the Trustees, to use revenues from the sales of hydroelectric power, and such other funds of the Authority, as deemed feasible and advisable by the Trustees, to fund the RCDP. The Authority's Trustees have authorized the release of a total \$337.5 million through January 2014 in support of the RCDP. The Authority supplemented the market revenues through the use of internal funds, from the August 2011 start of the program through December 31, 2013, totaling cumulatively \$77 million. Operations and maintenance expenses included \$100 million of residential consumer discounts in each of the years ended December 31, 2013 and 2012.

New York State Legislation

The Authority is requested, from time to time, to make financial contributions or transfers of funds to the State. Any such contribution or transfer of funds must (i) be authorized by law (typically, legislation enacted in connection with the State budget), and (ii) satisfy the requirements of the Bond Resolution. The Bond Resolution requirements to withdraw moneys "free and clear of the lien and pledge created by the (Bond) Resolution" are as follows: (1) such withdrawal must be for a "lawful corporate purpose as determined by the Authority," and (2) the Authority must determine "taking into account, among other considerations, anticipated future receipt of Revenues or other moneys constituting part of the Trust Estate, that the funds to be so withdrawn are not needed" for (a) payment of reasonable and necessary operating expenses, (b) an Operating Fund reserve for working capital, emergency repairs or replacements, major renewals, or for retirement from service, decommissioning or disposal of facilities, (c) payment of, or accumulation of a reserve for payment of, interest and principal on senior debt, or (d) payment of interest and principal on subordinate debt.

In May 2011, the Authority's Trustees adopted a policy statement (Policy Statement) which relates to, among other things, voluntary contributions, transfers, or other payments to the State by the Authority after that date. The Policy Statement provides, among other things, that in deciding whether to make such contributions, transfers, or payments, the Authority shall use as a reference point the maintenance of a debt service coverage ratio of at least 2.0, in addition to making the other determinations required by the Bond Resolution. The Policy Statement may at any time be modified or eliminated at the discretion of the Authority's Trustees.

Legislation enacted into law, as part of the 2000-2001 State budget, as amended up to the present time, has authorized the Authority as deemed feasible and advisable by the trustees, to make a series of voluntary contributions into the State treasury in connection with the PFJ Program and for other purposes as well. The PFJ Program, which had been extended to June 30, 2012, has ended and was replaced by the RNYPP, as discussed above in note 11(a) "Recharge New York Power Program" of the notes to the financial statements. Cumulatively through December 31, 2012, the Authority has made voluntary contributions to the State totaling \$475 million in connection with the ended PFJ Program.

In 2013 and 2012, the Authority made \$65 million and \$85 million, respectively, in contributions to the State that are not related to the PFJ Program and which were recorded as nonoperating expenses in the year ended December 31, 2013 and 2012 statements of revenues, expenses and changes in net position. These contributions were consistent with the related State fiscal year budgets and were authorized by the Authority's Trustees. The 2013 contributions of \$65 million include \$45 million that was paid to Empire State Development to support the New York State Open for Business economic development initiative in lieu of the voluntary contributions to the State's General Fund for the State fiscal year 2013-2014. Of the \$85 million contributed in 2012, \$10 million was paid to support the Open for Business initiative. An additional \$50 million was paid to support this initiative in January 2014 pursuant to Trustee approval and this amount will be recognized as a nonoperating expense in the Authority's 2014 fiscal year. Cumulatively, between January 2008 and December 31, 2013, the Authority has made voluntary contributions to the State totaling \$492 million unrelated to the PFJ program.

The Governor's Executive Budget for State Fiscal Year 2014-2015, released in January 2014, and subsequently amended, contains language authorizing the Authority, as deemed feasible and advisable by its Trustees, to (i) make a contribution to the State treasury to the

NEW YORK POWER AUTHORITY

Management's Discussion and Analysis

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credit of the General Fund, or as otherwise directed in writing by the Director of the Budget, in an amount of up to \$90 million for the State fiscal year commencing April 1, 2014, the proceeds of which will be utilized for to support energy-related initiatives of the State or for economic development purposes, and (ii) transfer up to \$25 million of any such contribution by June 30, 2014 and the remainder of any such contribution by March 31, 2015.

Temporary Asset Transfers

In addition to the authorization for voluntary contributions, as a result of budget legislation enacted in February 2009, the Authority was requested to provide temporary asset transfers to the State of funds held in reserves. Pursuant to the terms of a Memorandum of Understanding dated February 2009 (MOU) between the State, acting by and through the State's Director of Budget, and the Authority, the Authority agreed to transfer approximately \$215 million associated with its Spent Nuclear Fuel Reserves (Asset B) by March 27, 2009. The Spent Nuclear Fuel Reserves are funds that had been set aside for payment to the federal government sometime in the future when the federal government accepts the spent nuclear fuel for permanent storage. The MOU provides for the return of these funds to the Authority, subject to appropriation by the State Legislature and the other conditions described below, at the earlier of the Authority's payment obligation related to the transfer and disposal of the spent nuclear fuel or September 30, 2017. Further, the MOU provides for the Authority to transfer within 180 days of the enactment of the 2009-2010 State budget \$103 million of funds set aside for future construction projects (Asset A), which amounts would be returned to the Authority, subject to appropriation by the State Legislature and the other conditions described below, at the earlier of when required for operating, capital or debt service obligations of the Authority or September 30, 2014. In February 2009, the Authority's Trustees authorized the execution of the MOU relating to the temporary transfers of Asset B (\$215 million) and Asset A (\$103 million) and such transfers were made in March 2009 and September 2009, respectively, following Trustee approval.

The MOU provides that the obligation of the State to return all or a portion of an amount equal to the moneys transferred by the Authority to the State is subject to annual appropriation by the State Legislature. Further, the MOU provides that as a condition to any such appropriation for the return of the moneys earlier than September 30, 2017 for the Spent Nuclear Fuel Reserves and earlier than September 30, 2014 for the construction projects, the Authority must certify that the monies available to the Authority are not sufficient to satisfy the purposes for which the reserves, which are the source of the funds for the transfer, were established.

The Governor's Executive Budget for State Fiscal Year 2014-2015, released in January 2014, and subsequently amended, contains language that would make the \$103 million appropriation available to the Authority either: (i) pursuant to a repayment agreement submitted by the Authority and approved by the Director of the Budget, or (ii) upon certification of the Director of the Budget, at the request of the Authority when and to the extent that the Authority certifies to the Director that the monies available to the Authority are not sufficient to meet the Authority's obligations with respect to its debt service or operating or capital programs.

The Authority has classified the transfers of Assets A and B (\$318 million) as a long-term loan receivable. In lieu of interest payments, the State has waived certain future payments from the Authority to the State. The waived payments include the Authority's obligation to pay until September 30, 2017 the amounts to which the State is entitled under a governmental cost recovery process for the costs of central governmental services. These payments would have been approximately \$5 million per year based on current estimates but the waiver is limited to a maximum of \$45 million in the aggregate during the period. Further, the obligation to make payments in support of certain State park properties and for the upkeep of State lands adjacent to the Niagara and St. Lawrence power plants is waived from April 1, 2011 to March 31, 2017. These payments would have been approximately \$8 million per year but the waiver would be limited to a maximum of \$43 million for the period. The present value of the waivers approximates the present value of the lost interest income.

New York Energy Highway

In his January 2012 State of the State address, Governor Andrew M. Cuomo announced the New York Energy Highway initiative, which is envisioned as a public-private partnership to upgrade and modernize the State's electric power system. The Governor formed a task force comprised of various State officials to oversee implementation of the initiative (Task Force) which is co-chaired by the Authority's President and Chief Executive Officer, Gil C. Quiniones. In April 2012, the Task Force issued a request for information seeking ideas and proposals in furtherance of the initiative. Approximately 85 organizations responded to the Task Force's request for *information* and the responses included a large number of different generation and transmission project proposals. Based on the response of all these organizations, the Energy Highway Task Force issued an action plan in October 2012. The resulting Energy Highway Blueprint, calling for public and private investments in the State's energy system of about \$5.7 billion over the next five to 10 years, proposed 13 specific actions, divided among four major categories: Expand and Strengthen the System, Accelerate Construction and Repair, Support Clean Energy and Technology Innovation.

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In November 2012, the New York Public Service Commission (NYPSC) announced new proceedings addressing various actions described in the Blueprint including (i) the initiation of electric transmission upgrades to move excess power from upstate to downstate ("AC Transmission"), (ii) the creation of contingency plans to prepare for large generator retirements ("Generation Retirement Contingency Plans") and (iii) the expansion of natural gas delivery to homeowners and businesses in New York State.

In response to the request for information and the Generation Retirement Contingency Plans and AC Transmission proceedings, the New York Transmission Owners (NYTOs), comprised of the State's largest private utilities, the Long Island Power Authority, and the Authority, indicated that they were exploring the creation of a new Statewide transmission entity (NY Transco) to pursue development, construction, operation, and ownership of new transmission projects. The NYTOs proposed to the Task Force and to NYPSC several transmission projects that could be undertaken by a NY Transco entity.

In its November 4, 2013 Generation Retirement Contingency Plan Order, the NYPSC selected three transmission projects to be built by Consolidated Edison, New York State Gas and Electric and the Authority. The NYPSC also requested that the NYTOs seek Federal Energy Regulatory Commission (FERC) approval for these three projects.

Continued participation of the Authority in the NY Transco is contingent on the enactment of legislation by the State that enables the Authority to participate.

Other recommended actions, some of which will include the Authority, are investments to improve the reliability, safety and storm resilience in the areas of electric generation and transmission and natural gas distribution, facilitation of clean and renewable energy development, and funding of "Smart-Grid" technologies to improve the transmission system performance.

Build Smart NY Initiative

On December 28, 2012, Governor Andrew M. Cuomo issued Executive Order No. 88 (EO 88) directing state agencies collectively to reduce energy consumption in state-owned and managed buildings by 20 percent within seven years – an initiative designed to produce significant savings for New York taxpayers, generate jobs, and significantly reduce greenhouse gas emissions. To meet this initiative, the Governor launched Build Smart NY, a plan to strategically implement EO 88 by accelerating priority improvements in energy performance. The Authority has offered to provide \$450 million in low-cost financing for this initiative for state owned buildings and an additional \$350 million for towns and municipalities. Such low-cost financing would be funded by proceeds of the Authority's commercial paper or another form of debt. The Authority's costs of financing would be recovered from the energy efficiency customers in this program. In addition, as provided for in EO 88, the Authority has established a central management and implementation team to carry out the Build Smart NY plan. In 2013, the Authority provided approximately \$75 million in financing for energy efficiency projects at State agencies and authorities covered by EO 88.

Contacting the Authority

This financial report is designed to provide our customers and other interest parties with a general overview of the Authority's finances. If you have any questions about this report or need additional financial information, contact the New York Power Authority, 123 Main Street, White Plains, New York 10601-3107.

NEW YORK POWER AUTHORITY

Statements of Net Position

(In millions)

	December 31,	
	2013	2012
Assets and Deferred Outflows		
Current Assets:		
Cash and cash equivalents	\$ 8	\$ 77
Investment in securities	1,287	1,269
Receivables - customers	238	223
Materials and supplies, at average cost:		
Plant and general	88	83
Fuel	22	18
Miscellaneous receivables and other	181	205
Total current assets	<u>1,824</u>	<u>1,875</u>
Noncurrent Assets:		
Restricted funds:		
Cash and cash equivalents	18	21
Investment in securities	1,365	1,245
Total restricted assets	<u>1,383</u>	<u>1,266</u>
Capital funds:		
Cash and cash equivalents	7	—
Investment in securities	43	58
Total capital funds	<u>50</u>	<u>58</u>
Capital Assets:		
Capital assets not being depreciated	379	334
Capital assets, net of accumulated depreciation	4,392	4,485
Total capital assets	<u>4,771</u>	<u>4,819</u>
Other Noncurrent Assets:		
Receivable - New York State	318	318
Notes receivable - nuclear plant sale	19	37
Other long-term assets	924	641
Total other noncurrent assets	<u>1,261</u>	<u>996</u>
Total noncurrent assets	<u>7,465</u>	<u>7,139</u>
Total assets	<u>9,289</u>	<u>9,014</u>
Deferred outflows:		
Accumulated decrease in fair value of hedging derivatives	42	107
Total assets and deferred outflows	<u>\$ 9,331</u>	<u>\$ 9,121</u>

(Continued)

NEW YORK POWER AUTHORITY

Statements of Net Position

(In millions)

	December 31,	
	2013	2012
Liabilities and Net Position		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 456	\$ 442
Short-term debt	452	431
Long-term debt due within one year	93	91
Capital lease obligation due within one year	12	8
Risk management activities - derivatives	45	58
Total current liabilities	1,058	1,030
Noncurrent liabilities:		
Long-term debt:		
Senior:		
Revenue bonds	958	1,012
Adjustable rate tender notes	96	106
Subordinated:		
Subordinated Notes, Series 2012	24	24
Commercial paper	70	102
Total long-term debt	1,148	1,244
Other noncurrent liabilities:		
Capital lease obligation	1,205	1,217
Liability to decommission divested nuclear facilities	1,300	1,186
Disposal of spent nuclear fuel	216	216
Relicensing	277	303
Risk management activities - derivatives	24	81
Other long-term liabilities	384	374
Total other noncurrent liabilities	3,406	3,377
Total noncurrent liabilities	4,554	4,621
Total liabilities	5,612	5,651
Net position:		
Net investment in capital assets	1,949	1,893
Restricted	24	27
Unrestricted	1,746	1,550
Total net position	3,719	3,470
Total liabilities and net position	\$ 9,331	\$ 9,121

See accompanying notes to the financial statements.

NEW YORK POWER AUTHORITY

Statements of Revenues, Expenses and Changes in Net Position

(In millions)

	Year Ended December 31,	
	2013	2012
Operating revenues:		
Power sales	\$ 2,264	\$ 1,925
Transmission charges	163	150
Wheeling charges	603	598
Total operating revenues	3,030	2,673
Operating Expenses:		
Purchased power	934	744
Fuel oil and gas	324	228
Wheeling	603	598
Operations	451	454
Maintenance	115	104
Depreciation	228	226
Total operating expenses	2,655	2,354
Operating income	375	319
Nonoperating revenues and expenses:		
Nonoperating revenues:		
Investment income	5	27
Other	85	93
Total nonoperating revenues	90	120
Nonoperating expenses		
Contribution to New York State	65	85
Interest on long-term debt	63	67
Interest - other	119	120
Interest capitalized	(7)	(5)
Amortization of debt premium	(3)	(3)
Total nonoperating expenses	237	264
Net income before contributed capital	228	175
Contributed capital – Wind farm transmission assets	21	—
Change in net position	249	175
Net position, January 1	3,470	3,295
Net position, December 31	\$ 3,719	\$ 3,470

See accompanying notes to the financial statements.

NEW YORK POWER AUTHORITY

Statements of Cash Flows

(In millions)

	Year Ended December 31,	
	2013	2012
Cash flows from operating activities:		
Received from customers for the sale of power, transmission and wheeling	\$ 2,972	\$ 2,577
Disbursements for:		
Purchased power	(950)	(748)
Fuel, oil and gas	(325)	(218)
Wheeling of power by other utilities	(605)	(600)
Operations and maintenance	(579)	(620)
Net cash provided by operating activities	513	391
Cash flows from capital and related financing activities:		
Gross additions to capital assets	(165)	(145)
Issuance of Subordinated Notes, Series 2012	—	25
Repayment of notes	(10)	(8)
Repayment of bonds	(49)	(43)
Repayment of commercial paper	(33)	(46)
Earnings received on construction fund investments	1	2
Interest paid, net	(63)	(67)
Net cash used in capital and related financing activities	(319)	(282)
Cash flow from noncapital-related financing activities:		
Energy conservation program payments received from participants	119	178
Energy conservation program costs	(208)	(239)
Issuance of commercial paper	143	218
Repayment of commercial paper	(122)	(185)
Interest paid on commercial paper	(4)	(4)
Transmission line interconnection costs	(173)	—
Contributions to OPEB trust fund	(22)	(22)
Contributions to New York State	(65)	(91)
Payments received from value sharing agreement	72	72
Payments received from notes receivable	20	30
Net cash used in noncapital-related financing activities	(240)	(43)
Cash flow from investing activities:		
Earnings received on investments	23	26
Purchase of investment securities	(5,802)	(5,278)
Sale of investment securities	5,760	5,194
Net cash used in investing activities	(19)	(58)
Net (decrease) increase in cash	(65)	8
Cash and cash equivalents, January 1	98	90
Cash and cash equivalents, December 31	\$ 33	\$ 98
Reconciliation to net cash provided by operating activities:		
Operating income	\$ 375	\$ 319
Adjustments to reconcile operating income to net cash provided by operating activities:		
Change in assets, deferred outflows, liabilities and deferred inflows:		
Provision for depreciation	228	226
Net (increase) decrease in prepayments and other	(1)	30
Net increase in receivables and inventory	(78)	(88)
Net decrease in accounts payable and accrued liabilities	(11)	(96)
Net cash provided by operating activities	\$ 513	\$ 391

See accompanying notes to the financial statements.

NEW YORK POWER AUTHORITY

Notes to the Financial Statements

December 31, 2013 and 2012

(1) General

The Power Authority of the State of New York (the Authority), doing business as The New York Power Authority, is a corporate municipal instrumentality and political subdivision of the State of New York (State) created in 1931 by Title 1 of Article 5 of the Public Authorities Law, Chapter 43-A of the Consolidated Laws of the State, as amended (Power Authority Act or Act).

The Authority's mission is to provide clean, low-cost and reliable energy consistent with its commitment to the environment and safety, while promoting economic development and job development, energy efficiency, renewables and innovation, for the benefit of its customers and all New Yorkers. The Authority's financial performance goal is to have the resources necessary to achieve its mission, to maximize opportunities to serve its customers better, and to preserve its strong credit rating.

The Authority is authorized by the Power Authority Act to help provide a continuous and adequate supply of dependable electricity to the people of the State. The Authority generates, transmits and sells electricity principally at wholesale. The Authority's primary customers are municipal and investor-owned utilities, rural electric cooperatives, high load factor industries and other businesses located throughout New York State, various public corporations located in Southeastern New York within the metropolitan area of New York City ("SENY governmental customers"), and certain out-of-state customers.

To provide electric service, the Authority owns and operates five major generating facilities, eleven small gas-fired electric generating facilities, and four small hydroelectric facilities in addition to a number of transmission lines, including major 765-kV and 345-kV transmission facilities. The Authority's five major generating facilities consist of two large hydroelectric facilities ("Niagara" and "St. Lawrence-FDR"), a large pumped-storage hydroelectric facility ("Blenheim-Gilboa"), the combined cycle electric generating plant located in Queens, New York (the "500-MW plant") and the Richard M. Flynn combined cycle plant located on Long Island ("Flynn"). To provide additional electric generation capacity to the Authority's NYC Governmental Customers, the Authority entered into a long-term electricity supply agreement with Astoria Energy II LLC in 2008 for the purchase of the output of an Astoria, Queens based natural-gas fueled 550-MW generating plant, which entered service in the summer of 2011.

The Authority acts through a Board of Trustees. The Authority's Trustees are appointed by the Governor of the State of New York, with the advice and consent of the State Senate. The Authority is a fiscally independent public corporation that does not receive State funds or tax revenues or credits. It generally finances construction of new projects through projects through a combination of internally generated funds and sales of bonds and notes to investors and pays related debt service with revenues from the generation and transmission of electricity. Accordingly, the financial condition of the Authority is not controlled by or dependent on the State or any political subdivision of the State. Under the criteria set forth in Governmental Accounting Standards Board (GASB) the Authority considers its relationship to the State to be that of a related organization.

Income of the Authority and properties acquired by it for its projects are exempt from taxation. However, the Authority is authorized by the Act to enter into agreements to make payments in lieu of taxes with respect to property acquired for any project where such payments are based solely on the value of the real property without regard to any improvement thereon by the Authority and where no bonds to pay any costs of such project were issued prior to January 1, 1972.

The "Public Authorities Accountability Act of 2005" ("PAAA") was signed into law in January 2006 and its various provisions address public authority reporting, governance, budgeting, oversight, and auditing matters, among other things. Additional public authority reforms were made by Chapter 506 of the Laws of 2009 ("Chapter 506") which took effect on March 1, 2010. For example, Chapter 506 provided for (i) the creation of an "Authorities Budget Office" to provide oversight and other functions regarding public authorities, including the Authority; (ii) enhanced reporting requirements for public authorities, including the Authority; (iii) additional governance responsibilities for the boards of public authorities, including the Authority; (iv) New York State Comptroller review and approval of certain contracts of public authorities, including the Authority; (v) restrictions on property disposal by public authorities, including the Authority; and (vi) State Senate approval of certain authorities' chief executive officers, including the Authority.

(2) Summary of Significant Accounting Policies

The Authority's significant accounting policies include the following:

(a) Basis of Reporting

The Authority complies with all applicable pronouncements of the GASB. In accordance with GAS No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, the Authority applies all authoritative pronouncements applicable to nongovernmental entities (i.e., Accounting Standards

NEW YORK POWER AUTHORITY

Notes to the Financial Statements

December 31, 2013 and 2012

Codification (ASC) of the Financial Accounting Standards Board) that do not conflict with GASB pronouncements. The operations of the Authority are presented as an enterprise fund following the accrual basis of accounting in order to recognize the flow of economic resources. Accordingly, revenues are recognized in the period in which they are earned and expenses are recognized in the period in which they are incurred.

(b) **Regulatory Accounting**

The Authority's Board of Trustees has broad rate setting authority for its power sales agreements with customers. The sale of transmission service over the Authority's facilities is provided pursuant to New York Independent System Operator (NYISO) tariffs and under contracts that pre-dated existence of the NYISO. The Authority files its transmission system revenue requirement with the Federal Energy Regulatory Commission (FERC) for inclusion in the NYISO's open access tariff.

The Authority accounts for the financial effects of the rate regulated portion of its operations in accordance with the provisions of ASC Topic 980, *Regulated Operations*. These provisions recognize the economic ability of regulators, through the ratemaking process, to create future economic benefits and obligations affecting rate-regulated entities. Accordingly, the Authority records these future economic benefits and obligations as regulatory assets and regulatory liabilities, respectively. Regulatory assets represent probable future revenues associated with previously incurred costs that are expected to be recovered from customers. Regulatory liabilities represent amounts that are collected from customers through the ratemaking process associated with costs to be incurred in future periods. Based on the action of the Board of Trustees, the Authority believes the future collection of the costs held over through regulatory assets is probable. For regulatory assets and liabilities see note 2(l) "Other Long-Term Assets" and 2(m) "Other Long-Term Liabilities" of the notes to the financial statements.

(c) **Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(d) **Capital Assets**

Capital assets are recorded at original cost and consist of amounts expended for labor, materials, services and indirect costs to license, construct, acquire, complete and place in operation the projects of the Authority. Interest on amounts borrowed to finance construction of the Authority's projects is charged to the project prior to completion. Borrowed funds for a specific construction project are deposited in a capital fund account. Earnings on fund investments are held in this fund to be used for construction. Earnings on unexpended funds are credited to the cost of the related project (construction work in progress) until completion of that project. Construction work in progress costs are reduced by revenues received for power produced (net of expenditures incurred in operating the projects) prior to the date of completion. The costs of current repairs are charged to operating expense, and renewals and betterments are capitalized. The cost of capital assets retired less salvage is charged to accumulated depreciation. Depreciation of capital assets is generally provided on a straight-line basis over the estimated lives of the various classes of capital assets.

The related depreciation provisions at December 31, 2013 and 2012 expressed as a percentage of average depreciable capital assets on an annual basis are:

	Average depreciation rate	
	2013	2012
Type of plant:		
Production:		
Hydro	2.0%	2.0%
Gas turbine/combined cycle	3.2	3.2
Transmission	2.5	2.5
General	3.6	3.6
	2.8%	2.8%

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Notes to the Financial Statements

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(e) **Asset Retirement Obligation**

The Authority applies the applicable provisions of ASC Topic 410, *Asset Retirement and Environmental Obligations*, which requires an entity to record a liability at fair value to recognize legal obligations for asset retirements in the period incurred and to capitalize the cost by increasing the carrying amount of the related long-lived asset. The Authority determined that it had legal liabilities for the retirement of certain Small Clean Power Plants (SCPPs) in New York City and, accordingly, has recorded a liability for the retirement of this asset. In connection with these legal obligations, the Authority has also recognized a liability for the remediation of certain contaminated soils discovered during the construction process.

ASC Topic 410 does not apply to asset retirement obligations involving pollution remediation obligations that are within the scope of GAS No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. The Authority applies GAS No. 49 which, upon the occurrence of any one of five specified obligating events, requires an entity to estimate the components of expected pollution remediation outlays and determine whether outlays for those components should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired. The Authority had no liabilities recorded related to GAS No. 49 at December 31, 2013 or 2012.

In addition to asset retirement obligations, the Authority has other cost of removal obligations that are being collected from customers and accounted for under the provisions of ASC Topic 980. See note 2(m) "Other Long-Term Liabilities" of notes to the financial statements.

Asset retirement obligations (ARO) and cost of removal obligation amounts included in other noncurrent liabilities are as follows:

	ARO amounts	Cost of removal obligation
	(In millions)	
Balance – December 31, 2012	\$ 22	241
Depreciation expense	—	6
Balance – December 31, 2013	\$ 22	247

(f) **Long Lived Assets**

The Authority applies GAS No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which states that asset impairments are generally recognized only when the service utility of an asset is reduced or physically impaired.

GAS No. 42 states that asset impairment is a significant, unexpected decline in the service utility of a capital asset. The service utility of a capital asset is the usable capacity that at acquisition was expected to be used to provide service, as distinguished from the level of utilization which is the portion of the usable capacity currently being used. Decreases in utilization and existence of or increases in surplus capacity that are not associated with a decline in service utility are not considered to be impairments.

(g) **Cash, Cash Equivalents and Investments**

Cash includes cash and cash equivalents and short-term investments with maturities, when purchased, of three months or less. The Authority accounts for investments at their fair value. Fair value is determined using quoted market prices. Investment income includes changes in the fair value of these investments. Realized and unrealized gains and losses on investments are recognized as investment income in accordance with GAS No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*.

(h) **Derivative Instruments**

The Authority uses financial derivative instruments to manage the impact of interest rate, energy and capacity price and fuel cost changes on its earnings and cash flows. The Authority recognizes the fair value of all financial derivative instruments as either an asset or liability on its statements of net position with the offsetting gains or losses recognized in earnings or deferred charges. The Authority applies GAS No. 53, *Accounting and Financial Reporting for Derivative Instruments*,

NEW YORK POWER AUTHORITY

Notes to the Financial Statements

December 31, 2013 and 2012

which establishes accounting and reporting requirements for derivative instruments (see note 8 “Risk and Hedging Activities” of the notes to the financial statements).

(i) **Accounts Receivable**

Accounts receivable are classified as current assets and are reported net of an allowance for uncollectible amounts.

(j) **Materials and Supply Inventory**

Material and supplies are valued at weighted average cost and are charged to expense during the period in which the material or supplies are used.

(k) **Debt Refinancing Charges**

Debt refinancing charges, representing the difference between the reacquisition price and the net carrying value of the debt refinanced, are amortized using the interest method over the life of the new debt or the old debt, whichever is shorter, in accordance with GAS No. 23, *Accounting and Financial Reporting for Refundings of Debt Reported by Proprietary Activities*.

(l) **Other Long-Term Assets**

Other long-term assets at December 31, 2013 and 2012 consist of the following:

	December 31,	
	2013	2012
Other long-term assets:		
Regulatory assets (a):		
Recoverable electricity supply market costs	\$ 132	\$ 78
Risk management activities	27	32
Other regulatory assets	26	30
Total regulatory assets	185	140
Energy efficiency program costs (b)	253	203
Other long-term receivables	223	225
Transmission line interconnection costs	190	—
Other	73	73
Total other long-term assets	\$ 924	\$ 641

(a) Regulatory assets reflect previously incurred costs that are expected to be recovered from customers through the ratemaking process.

(b) Energy efficiency program costs will be recovered from certain customers through the terms of contracts.

(m) **Other Long-Term Liabilities**

Other long-term liabilities at December 31, 2013 and 2012 consist of the following:

	December 31,	
	2013	2012
Other long-term liabilities:		
Regulatory liabilities (a):		
Cost of removal	\$ 247	\$ 241
Other regulatory liabilities	7	6
Total regulatory liabilities	254	247
Other	130	127
	\$ 384	\$ 374

(a) See note 2(e) “Asset Retirement Obligation” of the notes to the financial statements.

NEW YORK POWER AUTHORITY

Notes to the Financial Statements

December 31, 2013 and 2012

(n) Compensated Absences

The Authority accrues the cost of unused sick leave which is payable upon the retirement of its employees. The Authority has accrued \$30 million at December 31, 2013 and 2012 in other non-current liabilities on the statements of net position. The current year's cost is accounted for as a current operating expense in the statements of revenues, expenses, and changes in net position.

(o) Net Position

In 2012, the Authority retroactively adopted GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. This Statement provides reporting guidance for deferred outflows of resources and deferred inflows of resources to be reported in the statement of financial position in a separate section following assets and liabilities, respectively. This Statement also amends the net asset requirements of Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets.

Net Position represents the difference between assets plus deferred outflows and liabilities plus deferred inflows and is classified into three components:

- a. Net investment in capital assets – This consists of capital assets, net of depreciation reduced by related outstanding debt and accounts. This indicates that these assets are not accessible for other purposes.
- b. Restricted – This represents restricted assets reduced by related liabilities and deferred inflows of resources that are not accessible for general use because their use is subject to restrictions enforceable by third parties.
- c. Unrestricted – This represents the net amount of assets, deferred outflows of resources, liabilities and deferred inflows of resources that are not included in the components noted above and that are available for general use.

(p) New York Independent System Operator (NYISO)

The Authority is a member and a customer of the New York Independent System Operator (NYISO). The NYISO schedules the use of the bulk transmission system in the State, which normally includes all the Authority's transmission facilities, and collects ancillary services, losses and congestion fees from customers. In addition, the Authority dispatches power from its generating facilities in conjunction with the NYISO. The NYISO coordinates the reliable dispatch of power and operates a market for the sale of electricity and ancillary services within the State.

Based upon the Authority's scheduled customer power needs and available electricity generated by the Authority's operating assets, the Authority buys and sells energy in an electricity market operated by the NYISO. A significant amount of the Authority's energy and capacity revenues result from sales of the Authority's generation into the NYISO market. A significant amount of the Authority's operating expenses consist of various NYISO purchased power charges in combination with generation related fuel expenses.

(q) Operating Revenues

The customers served by the Authority and the rates paid by such customers vary with the NYPA facilities designated to serve such loads. These customers are served under contracts and tariffs approved by the Trustees.

The principal operating revenues are generated from the sale, transmission, and wheeling of power. Revenues are recorded when power is delivered or service is provided. Customers' meters are read, and bills are rendered, monthly. Wheeling charges are for costs the Authority incurred for the transmission and/or delivery of power and energy to customers over transmission lines owned by other utilities. Sales to the Authority's five (5) largest customers operating in the State accounted for approximately 47% and 54% of the Authority's operating revenues in 2013 and 2012, respectively.

In addition to contractual sales to customers, the Authority also sells power into an electricity market operated by the NYISO. These sales are affected at market prices and are not subject to rate regulation by the Authority's Board of Trustees or other regulatory bodies. Accordingly, the Authority does not apply the provisions of ASC Topic 980 to these transactions.

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Notes to the Financial Statements

December 31, 2013 and 2012

(r) **Operating Expenses**

The Authority's operating expenses include fuel, operations and maintenance, depreciation, purchased power costs, and other expenses related to the sale of power. Energy costs are charged to expense as incurred.

Purchased power costs include capacity, energy and ancillary service purchases made in the wholesale market on behalf of its customers (except for those made through previously approved purchased power agreements). Wheeling expenses are based on contractual and/or tariff rates of the service provider and are recovered through pass-through provisions in customer contracts.

(s) **New Accounting Pronouncements**

In 2013, the Authority adopted GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* (Statement No. 65), which establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities, such as refunding of debt, and recognizes as outflows of resources (expenses or expenditures) and inflows of resources (revenues), certain items that were previously reported as assets and liabilities, such as debt issuance costs. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. The adoption of GASB Statement No. 65 did not have a significant impact on the Authority's financial statements.

(t) **Reclassifications**

Certain prior year amounts have been reclassified to conform to the current year's presentation including the reclassification of debt issuance costs as a regulatory asset. These reclassifications had no effect on net income and changes in net position or cash flows.

(3) **Bond Resolution**

On February 24, 1998, the Authority adopted its "General Resolution Authorizing Revenue Obligations" (as amended and supplemented up to the present time, the Bond Resolution). The Bond Resolution covers all of the Authority's projects, which it defines as any project, facility, system, equipment or material related to or necessary or desirable in connection with the generation, production, transportation, transmission, distribution, delivery, storage, conservation, purchase or use of energy or fuel, whether owned jointly or singly by the Authority, including any output in which the Authority has an interest authorized by the Act or by other applicable State statutory provisions, provided, however, that the term "Project" shall not include any Separately Financed Project as that term is defined in the Bond Resolution. The Authority has covenanted with bondholders under the Bond Resolution that at all times the Authority shall maintain rates, fees or charges, and any contracts entered into by the Authority for the sale, transmission, or distribution of power shall contain rates, fees or charges sufficient together with other monies available therefor (including the anticipated receipt of proceeds of sale of Obligations, as defined in the Bond Resolution, issued under the Bond Resolution or other bonds, notes or other obligations or evidences of indebtedness of the Authority that will be used to pay the principal of Obligations issued under the Bond Resolution in anticipation of such receipt, but not including any anticipated or actual proceeds from the sale of any Project), to meet the financial requirements of the Bond Resolution. Revenues of the Authority (after deductions for operating expenses and reserves, including reserves for working capital, operating expenses or compliance purposes) are applied first to the payment of, or accumulation as a reserve for payment of, interest on and the principal or redemption price of Obligations issued under the Bond Resolution and the payment of Parity Debt issued under the Bond Resolution.

The Bond Resolution also provides for withdrawal for any lawful corporate purpose as determined by the Authority, including but not limited to the retirement of Obligations issued under the Bond Resolution, from amounts in the Operating Fund in excess of the operating expenses, debt service on Obligations and Parity Debt issued under the Bond Resolution, and subordinated debt service requirements. The Authority has periodically reacquired revenue bonds when available at favorable prices.

(4) **Cash and Investments**

Investment of the Authority's funds is administered in accordance with the applicable provisions of the Bond Resolution and with the Authority's investment guidelines. These guidelines comply with the New York State Comptroller's investment guidelines for public authorities and were adopted pursuant to Section 2925 of the New York Public Authorities Law.

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Notes to the Financial Statements

December 31, 2013 and 2012

(a) Credit Risk

The Authority's investments are restricted to (a) collateralized certificates of deposit, (b) direct obligations of or obligations guaranteed by the United States of America or the State of New York, (c) obligations issued or guaranteed by certain specified federal agencies and any agency controlled by or supervised by and acting as an instrumentality of the United States government, and (d) obligations of any state or any political subdivision thereof or any agency, instrumentality or local government unit of any such state or political subdivision which is rated in any of the three highest long-term rating categories, or the highest short-term rating category, by nationally recognized rating agencies. The Authority's investments in the debt securities of Federal National Mortgage Association (FNMA), Federal Home Loan Bank (FHLB), Federal Farm Credit Bank (FFCB) and Federal Home Loan Mortgage Corp. (FHLMC) were rated Aaa by Moody's Investors Services (Moody's), AAA by Fitch Ratings (Fitch) and AA+ by Standard & Poor's (S&P).

(b) Interest Rate Risk

Securities that are the subject of repurchase agreements must have a market value at least equal to the cost of the investment. The agreements are limited to a maximum fixed term of five business days and may not exceed the greater of 5% of the investment portfolio or \$100 million. The Authority has no other policies limiting investment maturities.

(c) Concentration of Credit Risk

There is no limit on the amount that the Authority may invest in any one issuer; however, investments in authorized certificates of deposit shall not exceed 25% of the Authority's invested funds. At December 31, 2013, the Authority's total investment portfolio of \$2,728 million included investments of \$553 million (20%), \$322 million (12%), \$260 million (10%) and \$86 million (3%) and \$135 million (5%) in securities of FNMA, FHLMC, FHLB and FFCB and other various municipal debt securities, respectively.

At December 31, 2012, the Authority's total investment portfolio of \$2,670 million included investments of \$513 million (19%), \$407 million (15%), \$276 million (10%) and \$49 million (2%) and \$105 million (4%) in securities of FNMA, FHLMC, FHLB and FFCB and other various municipal debt securities, respectively.

(d) Decommissioning Fund

The Decommissioning Trust Fund is managed by external investment portfolio managers. Under the Decommissioning Agreements (see note 10(c) "Nuclear Plant Decommissioning" of notes to the financial statements), the Authority will make no further contributions to the Decommissioning Funds. The Authority's decommissioning responsibility will not exceed the amounts in each of the Decommissioning Funds. Therefore, the Authority's obligation is not affected by various risks which include credit risk, interest rate risk, and concentration of credit risk. In addition, the Decommissioning Trust Fund is not held within the Trust Estate of the Bond Resolution and therefore is administered under separate investment guidelines from those of the Authority or New York State.

(e) Other

All investments are held by designated custodians in the name of the Authority. At December 31, 2013, the Authority had no investments in repurchase agreements and \$50 million of such investments at December 31, 2012. The bank balances at December 31, 2013 and 2012 were \$43 million and \$60 million, respectively, of which \$42 million and \$59 million, respectively, were uninsured, but were collateralized by assets held by the bank in the name of the Authority.

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Notes to the Financial Statements

December 31, 2013 and 2012

Cash and Investments of the Authority at December 31, 2013 and 2012 are as follows:

December 31, 2013	Total	Total restricted	Decommissioning Trust Fund	Restricted	ART note debt reserve	Capital fund	Unrestricted
				POCR and CAS projects and other (In millions)			
Cash and investments:							
Cash and cash equivalents	\$ 33	18	—	18	—	7	8
U.S. government:							
Treasury Bills	28	20	—	20	—	8	—
GNMA	11	—	—	—	—	—	11
	39	20	—	20	—	8	11
Other debt securities:							
FNMA	553	36	—	25	11	—	517
FHLMC	322	1	—	—	1	6	315
FHLB	260	4	—	—	4	22	234
FFCB	86	—	—	—	—	—	86
All other	135	4	—	—	4	7	124
	1,356	45	—	25	20	35	1,276
Portfolio Manager	1,300	1,300	1,300	—	—	—	—
Total investments	2,695	1,365	1,300	45	20	43	1,287
Total cash and investments	\$ 2,728	1,383	1,300	63	20	50	1,295
Summary of maturities (years):							
0 – 1	\$ 333	67	—	63	4	43	223
1 – 5	1,026	16	—	—	16	3	1,007
5 – 10	12	—	—	—	—	—	12
10+	57	—	—	—	—	4	53
Portfolio manager	1,300	1,300	1,300	—	—	—	—
	\$ 2,728	1,383	1,300	63	20	50	1,295

Petroleum Overcharge Restitution (POCR) Funds and Clean Air for Schools (CAS) Projects Funds – Legislation enacted into State law from 1995 to 2002, 2007 and 2008 authorized the Authority to utilize petroleum overcharge restitution (POCR) funds and other State funds (Other State Funds), to be made available to the Authority by the State pursuant to the legislation, for a variety of energy-related purposes, with certain funding limitations. The legislation also states that the Authority “shall transfer” equivalent amounts of money to the State prior to dates specified in the legislation. The use of POCR funds is subject to comprehensive Federal regulations and judicial orders, including restrictions on the type of projects that can be financed with POCR funds, the use of funds recovered from such projects and the use of interest and income generated by such funds and projects. Pursuant to the legislation, the Authority is utilizing POCR funds and the Other State Funds to implement various energy services programs that have received all necessary approvals.

The disbursements of the POCR funds and the Other State Funds to the Authority, and the Authority’s transfers to the State totaling \$60.9 million, took place from 1996 to 2009. The POCR funds are included in restricted funds in the statements of net position. The funds are held in a separate escrow account until they are utilized.

The New York State Clean Water/Clean Air Bond Act of 1996 made available \$125 million for Clean Air for Schools Projects (CAS Projects) for elementary, middle and secondary schools, with the Authority authorized to undertake implementation of the CAS Projects program. The CAS Projects are designed to improve air quality for schools and include, but are not limited to, projects that replace coal-fired furnaces and heating systems with furnaces and systems fueled with oil or gas. As of December 31, 2013, the conversions to the schools are substantially complete and the Authority is in its closeout process regarding the CAS projects.

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Notes to the Financial Statements

December 31, 2013 and 2012

As of December 31, 2013, restricted funds include the POCR fund (\$11 million), the CAS Projects fund (\$2 million), the Lower Manhattan Energy Independence Initiative fund (\$7 million) and the Fish & Wildlife Habitat Enhancement fund related to the Niagara relicensing costs (\$14 million), the Western New York Economic Development Fund (\$25 million) – see note 11(a) “Recharge New York Power Program” – and other (\$3 million).

December 31, 2012	Total	Total restricted	Decommiss- ioning Trust Fund	Restricted		Capital fund	Unrestricted
				POCR and CAS projects and other	ART note debt reserve		
				(In millions)			
Cash and investments:							
Cash and cash equivalents	\$ 98	21	—	21	—	—	77
U.S. government:							
Treasury Bills	18	3	—	3	—	15	—
GNMA	18	—	—	—	—	—	18
	36	3	—	3	—	15	18
Other debt securities:							
FNMA	513	—	—	—	—	6	507
FHLMC	407	21	—	21	—	4	382
FHLB	276	24	—	15	9	4	248
FFCB	49	—	—	—	—	12	37
All other	105	11	—	—	11	17	77
	1,350	56	—	36	20	43	1,251
Portfolio Manager	1,186	1,186	1,186	—	—	—	—
Total investments	2,572	1,245	1,186	39	20	58	1,269
Total cash and investments	\$ 2,670	1,266	1,186	60	20	58	1,346
Summary of maturities (years):							
0 – 1	\$ 421	71	—	60	11	47	303
1 – 5	1,022	9	—	—	9	5	1,008
5 – 10	1	—	—	—	—	—	1
10+	40	—	—	—	—	6	34
Portfolio manager	1,186	1,186	1,186	—	—	—	—
	\$ 2,670	1,266	1,186	60	20	58	1,346

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Notes to the Financial Statements

December 31, 2013 and 2012

(5) Capital Assets

The following schedule summarizes the capital assets activity of the Authority for the year ended December 31, 2013:

	Beginning balance	Additions	Retirements/ Transfers	Ending balance
	(Amounts in millions)			
Capital assets, not being depreciated:				
Land	\$ 156	4	—	160
Construction in progress	178	148	(107)	219
Total capital assets not being depreciated	334	152	(107)	379
Capital assets, being depreciated:				
Production – Steam (a)	437	—	(437)	—
Production – Hydro	1,830	72	(4)	1,898
Production – Gas turbine/combined cycle	2,418	1	—	2,419
Transmission	1,928	35	(1)	1,962
General	1,134	23	(1)	1,156
Total capital assets being depreciated	7,747	131	(443)	7,435
Less accumulated depreciation for:				
Production – Steam	436	1	(437)	—
Production – Hydro	684	30	(4)	710
Production – Gas turbine/combined cycle	675	103	—	778
Transmission	1,040	49	—	1,089
General	427	39	—	466
Total accumulated depreciation	3,262	222	(441)	3,043
Net value of capital assets, being depreciated	4,485	(91)	(2)	4,392
Net value of all capital assets	\$ 4,819	61	(109)	4,771

(a) Reflects the removal of the fully depreciated Polletti power plant from the balance sheet in 2013.

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Notes to the Financial Statements

December 31, 2013 and 2012

The following schedule summarizes the capital assets activity of the Authority for the year ended December 31, 2012:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Retirements/ Transfers</u>	<u>Ending balance</u>
	(Amounts in millions)			
Capital assets, not being depreciated:				
Land	\$ 154	2	—	156
Construction in progress	<u>134</u>	<u>126</u>	<u>(82)</u>	<u>178</u>
Total capital assets not being depreciated	<u>288</u>	<u>128</u>	<u>(82)</u>	<u>334</u>
Capital assets, being depreciated:				
Production – Steam	437	—	—	437
Production – Hydro	1,796	37	(3)	1,830
Production – Gas turbine/combined cycle	2,414	4	—	2,418
Transmission	1,909	20	(1)	1,928
General	<u>1,113</u>	<u>23</u>	<u>(2)</u>	<u>1,134</u>
Total capital assets being depreciated	<u>7,669</u>	<u>84</u>	<u>(6)</u>	<u>7,747</u>
Less accumulated depreciation for:				
Production – Steam	436	—	—	436
Production – Hydro	657	30	(3)	684
Production – Gas turbine/combined cycle	571	104	—	675
Transmission	993	48	(1)	1,040
General	<u>390</u>	<u>38</u>	<u>(1)</u>	<u>427</u>
Total accumulated depreciation	<u>3,047</u>	<u>220</u>	<u>(5)</u>	<u>3,262</u>
Net value of capital assets, being depreciated	<u>4,622</u>	<u>(136)</u>	<u>(1)</u>	<u>4,485</u>
Net value of all capital assets	<u>\$ 4,910</u>	<u>(8)</u>	<u>(83)</u>	<u>4,819</u>

Wind Farm Transmission Assets

The Authority is allowing three Wind Farm power facilities to interconnect to its bulk transmission system between the Willis and Plattsburgh 230 kV substations. In 2013, Marble River LLC, the wind farm developers, transferred title to one substation (valued at \$21 million) to the Authority in order for the Authority to maintain reliability standards and control of its bulk transmission system. The transfer was accounted for as a capital contribution.

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Notes to the Financial Statements

December 31, 2013 and 2012

(6) Long-Term Debt

(a) Components

	Amount		Interest rate	Maturity	Earliest redemption date prior to maturity
	2013	2012			
	(In millions)				
Senior debt:					
Revenue Bonds (Tax-Exempt):					
Series 2002 A Revenue Bonds:					
Serial Bonds	\$ —	\$ 27	N/A	N/A	N/A
Series 2006 A Revenue Bonds:					
Serial Bonds	100	111	3.75% to 5.0%	11/15/2014 to 2020	11/15/2015
Series 2007 A Revenue Bonds:					
Term Bonds	82	82	4.5% to 5.0%	11/15/2047	11/15/2017
Series 2007 C Revenue Bonds:					
Serial Bonds	264	264	4.0% to 5.0%	11/15/2014 to 2021	11/15/2017
Series 2011 A Revenue Bonds:					
Serial Bonds	68	69	3.0% to 5.0%	11/15/2014 to 2031 *	11/15/2021
Term Bonds	39	39	4.0% to 5.0%	11/15/2032 to 2038	11/15/2021
Revenue Bonds (Taxable):					
Series 2003 A Revenue Bonds:					
Serial Bonds	—	5	N/A	N/A	N/A
Term Bonds	186	186	5.230% to 5.749%	11/15/2018 to 2033	Any date
Series 2007 B Revenue Bonds:					
Serial Bonds	14	18	5.373% to 5.603%	11/15/2014 to 2017	Any date
Term Bonds	239	239	5.905% to 5.985%	11/15/2037 and 2043	Any date
	992	1,040			
Plus unamortized premium and discount	26	29			
Less deferred refinancing costs	9	9			
	1,009	1,060			
Less due in one year	51	48			
	\$ 958	\$ 1,012			

* \$26.4 million due 2022 is non-callable.

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December 31, 2013 and 2012

	<u>Amount</u>		<u>Interest rate</u>	<u>Maturity</u>	<u>Earliest redemption date prior to maturity</u>
	<u>2013</u>	<u>2012</u>			
	(In millions)				
Adjustable Rate Tender Notes:					
2016 Notes	\$ 31	\$ 40	0.15%	3/1/2016	Any adjustment date
2020 Notes	75	75	0.15%	3/1/2020	Same as above
	106	115			
Less due in one year	10	9			
	96	106			
Subordinate debt:					
Subordinated Notes, Series 2012	24	25	0.64% to 4.05%	2014 to 2037	N/A
Commercial Paper:					
EMCP (Series 1)	62	70	0.13%	2014 to 2023	
CP (Series 2)	40	65	0.08%	2014 to 2015	
	126	160			
Less due within one year	32	34			
	94	126			
Total Long-term debt	1,241	1,335			
Less due within one year	93	91			
Long-term debt, net of due in one year	\$ 1,148	\$ 1,244			

Interest on Series 2003 A and 2007 B Revenue Bonds and Subordinated Notes, Series 2012 is not excluded from gross income for bondholders' Federal income tax purposes.

Senior Debt

As indicated in note 3 of notes to the financial statements, "Bond Resolution," the Authority has pledged future revenues to service the Obligations and Parity Debt (Senior Debt) issued under the Bond Resolution. Annual principal and interest payments on the Senior Debt are expected to require less than 35% of operating income plus depreciation. The total principal and interest remaining to be paid on the Senior Debt is \$1.804 billion as of December 31, 2013. Principal and interest paid for 2013 and operating income plus depreciation were \$112 million and \$603 million, respectively. Principal and interest paid for 2012 and operating income plus depreciation were \$108 million and \$545 million, respectively.

Senior revenue bonds are subject to redemption prior to maturity in whole or in part as provided in the supplemental resolutions authorizing the issuance of each series of bonds, beginning for each series on the date indicated in the table above, at principal amount or at various redemption prices according to the date of redemption, together with accrued interest to the redemption date.

In prior years, the Authority defeased certain revenue bonds and general purpose bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Authority's financial statements. As of December 31, 2013 and 2012, there were no bonds outstanding that were considered defeased.

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Notes to the Financial Statements

December 31, 2013 and 2012

The Adjustable Rate Tender Notes may be tendered to the Authority by the holders on any adjustment date. The rate adjustment dates are March 1 and September 1. The Authority has a revolving credit agreement (Agreement) with The Bank of Nova Scotia, which terminates on September 1, 2015, to provide a supporting line of credit for the purpose of repaying, redeeming or purchasing the Adjustable Rate Tender Notes. Under the Agreement, the Authority may borrow up to the outstanding principle of the ART Notes, which at December 31, 2013 was \$106 million. The Agreement provides for interest on outstanding borrowings at either (i) the Federal Funds Rate plus a percentage, or (ii) a rate based on the London Interbank Offered Rate (LIBOR) plus a percentage. As of December 31, 2013 and 2012, there were no outstanding borrowings under this Agreement. The Authority expects that it will be able to renew or replace this Agreement as necessary. In accordance with the Adjustable Rate Tender Note Resolution, a Note Debt Service Reserve account has been established in the amount of \$20 million. See note 8 of notes to the financial statements for the Authority's risk management program relating to interest rates.

At December 31, 2013 and 2012, the current market value of the senior debt was approximately \$1.175 billion and \$1.329 billion, respectively. Market values were obtained from a third party that utilized a matrix-pricing model.

Subordinate Debt:

Subordinate Notes – In November 2012, the Authority's Trustees authorized the issuance of Subordinated Notes, Series 2012 (Subordinated Notes), in a principal amount not to exceed \$30 million for the purpose of accelerating the funding for the State Parks Greenway Fund, which was established pursuant to the Niagara Relicensing Settlement entered into by the Authority and the New York State Office of Parks, Recreation & Historic Preservation. The Authority issued the Subordinated Notes on December 18, 2012 in the amount of \$25 million. These Subordinated Notes are subordinate to the Series 2003 A Revenue Bonds, the Series 2006 A Revenue Bonds, the Series 2007 A, B, and C Revenue Bonds, the Series 2011 A Revenue Bonds and the Adjustable Rate Tender Notes.

Commercial Paper – Under the Extendible Municipal Commercial Paper (EMCP) Note Resolution, adopted December 17, 2002, and as subsequently amended and restated, the Authority may issue a series of notes, designated EMCP Notes, Series 1, maturing not more than 270 days from the date of issue, up to a maximum amount outstanding at any time of \$200 million (EMCP Notes). It is the Authority's intent to remarket the EMCP Notes as they mature with their ultimate retirement to range from 2014 to 2023. The Authority has the option to extend the maturity of the EMCP Notes and would exercise such right in the event there is a failed remarketing. This option serves as a substitute for a liquidity facility for the EMCP Notes.

Under the Commercial Paper Note Resolution adopted June 28, 1994, as subsequently amended and restated, the Authority may issue from time to time a separate series of notes maturing not more than 270 days from the date of issue, up to a maximum amount outstanding at any time of \$400 million (Series 1 CP Notes), \$450 million (Series 2 CP Notes), \$350 million (Series 3 CP Notes) and \$220 million (Series 4 CP Notes). See note 7 of the notes to the financial statements for Series 1, and certain Series 2 and Series 3 CP Notes designated as short-term debt. There were no Series 4 CP Notes outstanding at December 31, 2013.

The proceeds of certain Series 2 and 3 Commercial Paper Notes (CP Notes) were used to refund General Purpose Bonds and the proceeds of the EMCP Notes were used to refund Series 2 and 3 CP Notes. CP Notes and EMCP Notes have been used, and may in the future be used, for other corporate purposes. It is the Authority's intention to renew the Series 2 and 3 CP Notes and the EMCP Notes as they mature so that their ultimate maturity dates will range from 2014 to 2023, as indicated in the table above.

The Authority has a line of credit under a 2011 revolving credit agreement, as amended, (the 2011 RCA) with a syndicate of banks, to provide liquidity support for the Series 1-3 CP Notes, under which the Authority may borrow up to \$550 million in aggregate principal amount outstanding at any time for certain purposes, including the repayment of the Series 1-3 CP Notes. This revolving line of credit expires January 20, 2015. There are no outstanding borrowings under the 2011 RCA.

CP Notes and EMCP Notes are subordinate to the Series 2003 A Revenue Bonds, the Series 2006 A Revenue Bonds, the Series 2007 A, B, and C Revenue Bonds, the Series 2011 A Revenue Bonds and the Adjustable Rate Tender Notes.

Interest on the CP (Series 3) is taxable to holders for Federal income tax purposes.

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Notes to the Financial Statements

December 31, 2013 and 2012

Maturities and Interest Expense:	Long-Term Debt				Capitalized Lease Obligations		
	(In millions)				(In millions)		
	Hedging Derivative Instruments, Net						
	Principal	Interest		Total	Principal	Interest	Total
Year:							
2014	\$ 93	53	4	150	\$ 12	97	109
2015	90	51	3	144	16	95	111
2016	77	48	3	128	20	95	115
2017	85	45	—	130	25	93	118
2018	85	42	—	127	31	91	122
2019 – 2023	307	164	—	471	254	402	656
2024 – 2028	97	124	—	221	489	257	746
2029 – 2033	143	92	—	235	370	40	410
2034 – 2038	90	57	—	147	—	—	—
2039 – 2043	78	33	—	111	—	—	—
2044 – 2048	79	10	—	89	—	—	—
	1,224	719	10	1,953	1,217	1,170	2,387
Plus unamortized bond premium	26	—	—	26	—	—	—
Less deferred refinancing cost	9	—	—	9	—	—	—
	<u>\$ 1,241</u>	<u>719</u>	<u>10</u>	<u>1,970</u>	<u>\$ 1,217</u>	<u>1,170</u>	<u>2,387</u>

The interest rate used to calculate future interest expense on variable rate debt is the interest rate at December 31, 2013.

(b) Terms by Which Interest Rates Change for Variable Rate Debt

Adjustable Rate Tender Notes

In accordance with the Adjustable Rate Tender Note Resolution adopted April 30, 1985, as amended up to the present time (Note Resolution), the Authority may designate a rate period of different duration, effective on any rate adjustment date. The Authority and the remarketing agent appointed under the Note Resolution determine the rate for each rate period which, in the agent's opinion, is the minimum rate necessary to remarket the notes at par.

CP Notes and EMCP Notes (Long-Term Portion)

The Authority determines the rate for each rate period which is the minimum rate necessary to remarket the notes at par in the Dealer's opinion. If the Authority exercises its option to extend the maturity of the EMCP Notes, the reset rate will be the higher of (SIFMA + E) or F, where SIFMA is the Securities Industry and Financial Markets Association Municipal Swap Index, which is calculated weekly, and where "E" and "F" are fixed percentage rates expressed in basis points (each basis point being 1/100 of one percent) and yields, respectively, that are determined based on the Authority's debt ratings subject to a cap rate of 12%. As of December 31, 2013, the reset rate would have been 7.33%.

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(c) *Changes in Noncurrent Liabilities*

Changes in the Authority's noncurrent liabilities for the year ended December 31, 2013 are comprised of the following:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Maturities/ refundings and other</u> (In millions)	<u>Ending balance</u>	<u>Due within one year</u>
Senior debt:					
Revenue bonds	\$ 1,040	—	48	992	51
Adjustable rate tender bonds	115	—	9	106	10
Subtotal	<u>1,155</u>	<u>—</u>	<u>57</u>	<u>1,098</u>	<u>61</u>
Subordinate debt:					
Subordinated Notes, Series 2012	25	—	1	24	1
Commercial paper	135	—	33	102	31
Subtotal	<u>160</u>	<u>—</u>	<u>34</u>	<u>126</u>	<u>32</u>
Net unamortized discounts/ premiums and deferred losses	<u>20</u>	<u>—</u>	<u>3</u>	<u>17</u>	<u>—</u>
Total debt, net of unamortized discounts/ premiums/ deferred losses	<u>\$ 1,335</u>	<u>—</u>	<u>94</u>	<u>1,241</u>	<u>93</u>
Other noncurrent liabilities:					
Capitalized lease obligation	\$ 1,217	—	12	1,205	12
Nuclear decommissioning	1,186	114	—	1,300	—
Disposal of nuclear fuel	216	—	—	216	—
Relicensing	303	18	44	277	—
Other	455	31	78	408	—
Total other noncurrent liabilities	<u>\$ 3,377</u>	<u>163</u>	<u>134</u>	<u>3,406</u>	<u>12</u>

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Changes in the Authority's long-term liabilities for the year ended December 31, 2012 are comprised of the following:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Maturities/ refundings and other</u> (In millions)	<u>Ending balance</u>	<u>Due within one year</u>
Senior debt:					
Revenue bonds	\$ 1,083	—	43	1,040	48
Adjustable rate tender bonds	123	—	8	115	9
Subtotal	<u>1,206</u>	<u>—</u>	<u>51</u>	<u>1,155</u>	<u>57</u>
Subordinate debt:					
Subordinated Notes, Series 201	—	25	—	25	1
Commercial paper	204	—	69	135	33
Subtotal	<u>204</u>	<u>25</u>	<u>69</u>	<u>160</u>	<u>34</u>
Net unamortized discounts/ premiums and deferred losses	<u>24</u>	<u>—</u>	<u>4</u>	<u>20</u>	<u>—</u>
Total debt, net of unamortized discounts/ premiums/ deferred losses	<u>\$ 1,434</u>	<u>25</u>	<u>124</u>	<u>1,335</u>	<u>91</u>
Other long-term liabilities:					
Capitalized lease obligation	\$ 1,230	—	13	1,217	8
Nuclear decommissioning	1,090	96	—	1,186	—
Disposal of nuclear fuel	216	—	—	216	—
Relicensing	329	20	46	303	—
Other	<u>546</u>	<u>16</u>	<u>107</u>	<u>455</u>	<u>—</u>
Total other noncurrent liabilities	<u>\$ 3,411</u>	<u>132</u>	<u>166</u>	<u>3,377</u>	<u>8</u>

(7) Short-Term Debt

CP Notes (short-term portion) outstanding was as follows:

	<u>2013</u>		<u>2012</u>	
	<u>Availability</u>	<u>Outstanding</u>	<u>Availability</u>	<u>Outstanding</u>
	(In millions)			
CP Notes (Series 1)	\$ 53	\$ 347	\$ 70	\$ 330
CP Notes (Series 2) (a)	332	78	305	80
CP Notes (Series 3)	323	27	329	21

(a) Availability includes long-term CP Notes (Series 2) of \$40 million and \$65 million outstanding at December 31, 2013 and 2012, respectively (see note 6 of notes to the financial statements).

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Under the Commercial Paper Note Resolution adopted June 28, 1994, as subsequently amended and restated, the Authority may issue from time to time a separate series of notes maturing not more than 270 days from the date of issue, up to a maximum amount outstanding at any time of \$400 million (Series 1 CP Notes), \$450 million (Series 2 CP Notes), \$350 million (Series 3 CP Notes) and \$220 million (Series 4 CP Notes). See note 6 “Long-term Debt – Subordinated Debt–Commercial Paper” of notes to the financial statements for Series 2 CP Notes designated as long-term debt. It had been and shall be the intent of the Authority to use the proceeds of the Series 1 CP Notes and certain Series 2 and Series 3 CP Notes to finance the Authority’s current and future energy efficiency programs and for other corporate purposes.

The changes in short-term debt are as follows:

	<u>Beginning balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending balance</u>
		(\$ in millions)		
Year:				
2013	\$ 431	143	122	452
2012	\$ 374	242	185	431

(8) Risk Management and Hedging Activities

Overview

The Authority purchases insurance coverage for its operations, and in certain instances, is self-insured. Property insurance purchase protects the various real and personal property owned by the Authority and the property of others while in the care, custody and control of the Authority for which the Authority may be held liable. Liability insurance purchase protects the Authority from third-party liability related to its operations, including general liability, automobile, aircraft, marine and various bonds. Insured losses by the Authority did not exceed coverage for any of the four preceding fiscal years. The Authority self-insures a certain amount of its general liability coverage and the physical damage claims for its owned and leased vehicles. The Authority is also self-insured for portions of its medical, dental and workers’ compensation insurance programs. The Authority pursues subrogation claims as appropriate against any entities that cause damage to its property.

Another aspect of the Authority’s risk management program is to manage risk and related volatility on its earnings and cash flows associated with electric energy prices, fuel prices, electric capacity prices and interest rates.

Through its participation in the NYISO and other commodity markets, the Authority is subject to electric energy price, fuel price and electric capacity price risks that impact the revenue and purchased power streams of its facilities and customer market areas. Such volatility can potentially have adverse effects on the Authority’s financial condition. To mitigate downside effects, many of the Authority’s customer contracts provide for the complete or partial pass-through of these costs and to moderate cost impacts to its customers, the Authority hedges market risks through the use of financial instruments and physical contracts. Hedges are transacted by the Authority to mitigate volatility in the cost of energy or related products needed to meet customer needs; to mitigate risk related to the price of energy and related products sold by the Authority; to mitigate risk related to margins (electric sales versus fuel use) where the Authority owns generation or other capacity; and mitigation of geographic cost differentials of energy procured or sold for transmission or transportation to an ultimate location. Commodities to be hedged include, but are not limited to, natural gas, natural gas basis, electric energy, electric capacity and congestion costs associated with the transmission of electricity.

To achieve the Authority’s risk management program objectives, the Authority’s Trustees have authorized the use of various interest rate, energy, and fuel derivative instruments for hedging purposes that are considered derivatives under GAS No. 53, *Accounting and Financial Reporting for Derivative Instruments* (GAS No. 53).

The fair values of all Authority derivative instruments, as defined by GAS No. 53, are reported in current and noncurrent assets or liabilities on the statements of net position as risk management activities. For designated hedging derivative instruments, changes in the fair values are deferred and classified as deferred outflows or deferred inflows on the statements of net position. For designated interest rate and commodity option hedging derivative instruments the change in fair value is applied to interest expense and related commodity revenue or expense. For renewable energy derivative instruments, designated as investment derivative instruments, changes in fair value are deferred as regulatory assets or liabilities, as they are recoverable from customers by contractual agreements. The fair value of interest rate swap agreements take into consideration the prevailing interest rate environment and the specific terms and conditions of each agreement. The fair values were estimated using the zero-coupon

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discounting method. The fair value of interest rate options were measured using an option pricing model that considers certain variables such as volatilities, time and underlying prices. The fair value for over-the-counter and exchange-traded energy, renewable energy natural gas, natural gas transportation and capacity derivative instruments are determined by the monthly market prices over the lifetime of each outstanding derivative instrument using the latest end-of-trading-month forward prices published by Platts or derived from pricing models for option and/or option-based derivative instruments using the underlying price, time and observed volatilities based upon Platts published prices and other variables.

Derivative Instruments

The following table shows the fair value of outstanding derivatives instruments for 2013 and 2012:

Derivative instrument description	Fair value balance December 31, 2012	Net change in fair value	Fair value balance December 31, 2013	Type of hedge or transaction	Financial statement classification for changes in fair value	Notional amount December 31, 2013	Volume
(\$ in millions)							
Interest rate swaps	\$ (15)	\$ 6	\$ (9)	Cash Flow	Deferred outflow	146.1	USD
Energy :							
Swaps	(92)	55	(37)	Cash Flow	Deferred outflow	1,902,680	MWh
Call option	—	2	2	Cash Flow	Deferred inflow	107,520	MWh
Renewable energy swaps	(32)	5	(27)	Investment	Regulatory Asset	727,525	MWh
Energy capacity swaps/futures	—	—	—	Cash Flow	Deferred outflow	(300,000)	MWh
Fuel swaps	—	2	2	Cash Flow	Deferred inflow	3,010,000	MMBtu
Totals	\$ (139)	\$ 70	\$ (69)				

Interest rate swaps – The Authority has outstanding forward interest rate swaps to fix rates on long-term obligations initially issued to refinance revenue bonds that were required to be tendered in the year 2002 (the 2002 Swaps). Based upon the terms of these forward interest rate swaps, the Authority would pay interest calculated at a fixed rate of 5.123% to the counterparties through February 15, 2015. In return, the counterparties would pay interest to the Authority based upon the Securities Industry and Financial Markets Association municipal swap index (SIFMA Index) on the established reset dates. The 2002 swaps are scheduled to terminate on February 15, 2015. Net settlement payments were \$2.2 and \$3.4 million in 2013 and 2012, respectively.

In addition, the Authority has outstanding a forward interest rate swap to fixing the interest rates on the Authority's Adjustable Rate Tender Notes (ART Notes) for the period September 1, 2006 to September 1, 2016. Based upon the terms of the forward interest rate swap, the Authority pays interest calculated at a fixed rate of 3.7585% on the outstanding notional amount. In return, the counterparty pays interest to the Authority based upon 67% of the six-month LIBOR established on the reset dates that coincide with the ART Notes interest rate reset dates. Net settlement payments were \$3.7 and \$3.8 million in 2013 and 2012, respectively.

Energy swaps – The Authority has outstanding a medium-term forward energy swap to fix its exposure for the cost of energy purchases in the NYISO electric market in meeting certain governmental customer load requirements for 2014. Net settlement payments were \$35.7 million and \$49.6 million in 2013 and 2012, respectively. In 2013, the Authority entered into short-term forward energy swaps and options to manage the cost of forecasted purchased power requirements and transmission congestion for certain business customers in 2013 and 2014. Net settlement receipts were \$0.3 million in 2013.

Renewable energy swaps – The Authority has outstanding long-term forward energy swaps and purchase agreements based upon a portion of the generation of the counterparties' wind-farm-power-generating facilities through 2017. The fixed price ranges from \$74 to \$75 per MWh and includes the purchase of the related environmental attributes. The intent of the swaps and purchase agreements is to assist certain customers in acquiring and investing in wind power and related environmental attributes to satisfy certain New York State mandates to support renewable energy. Net settlement payments were \$6.7 million and \$7.1 million in 2013 and 2012, respectively. The Authority anticipates the recovery or distribution of any net settlements through specific contractual agreements with customers.

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Energy Capacity Swaps/Futures – In 2013, the Authority sold and purchased forward installed capacity swaps and futures to mitigate the volatility of market prices for sales into the NYISO markets in 2013 and 2014. Net settlement payments were \$0.5 million in 2013.

Fuel Swaps and Futures – In 2013, the Authority purchased forward natural gas swaps and natural gas futures to mitigate the volatility of market prices for fuel to operate certain natural gas facilities in 2013 and 2014 for the benefit of certain of the Authority's customers. Net settlement receipts were \$1.0 million in 2013. In 2013, in connection with the purchase of fuel swaps and futures and for the benefit of the Authority's customers, the Authority purchased natural gas transportation basis swaps to mitigate the volatility of market prices for gas line usage/transportation to New York City in 2013 and 2014. There were no settlements in 2013.

Other – The Authority from time to time enters into certain derivative instruments that may become ineffective as hedging instruments due to changes in the hedged item. The change in fair value of such derivative instruments is recognized as other nonoperating charges or credits in the statements of revenues, expenses and changes in net position. The fair value of these derivative instruments was insignificant to the Authority's 2013 financial statements.

Counterparty Credit Risk

The Authority's policy regarding the creditworthiness of counterparties for interest rate derivative instruments is defined in the Bond Resolution. The policy requires that such counterparties be rated in at least the third highest rating category for each appropriate rating agency maintaining a rating for qualified swap providers at the time the derivative instrument is executed or have a guarantee from another appropriate entity or an opinion from the rating agencies that the underlying bonds or notes will not be downgraded on the derivative instrument alone. The Authority's Board of Trustees has adopted a Policy for the Use of Interest Rate Exchange Agreements which provides the overall framework for delegation of authority; allowable interest rate hedging instruments; counterparty qualifications and diversification as well as reporting standards.

The Authority also imposes thresholds, based on agency-published credit ratings, for unsecured credit that can be extended to counterparties to the Authority's commodity derivative transactions. The thresholds are established in bilateral credit support agreements with counterparties and require collateralization of mark-to-market values in excess of the thresholds. In addition, the Authority regularly monitors each counterparty's market-implied credit ratings and financial ratios and the Authority can restrict transactions with counterparties on the basis of that monitoring, even if the applicable unsecured credit threshold is not exceeded.

Based upon the fair values as of December 31, 2013, the Authority's individual or aggregate exposure to derivative instrument counterparty credit risk is not significant.

Other Considerations

The Authority from time to time may be exposed to any of the following risks:

Basis risk – The Authority is exposed to basis risk on its pay-fixed interest rate swaps since it receives variable-rate payments on these hedging derivative instruments based on indexes which differ from the actual interest rates the Authority pays on its variable-rate debt. The Authority remarkets its Notes at rates that approximate SIFMA and LIBOR after considering other factors such as the Authority's creditworthiness.

The Authority is exposed to other basis risk in a portion of its electrical commodity-based swaps where the electrical commodity swap payments received are based upon a reference price in a NYISO Market Zone that differs from the Zone in which the hedged electric energy load is forecasted. If the correlation between these Zones' prices should fall, the Authority may incur costs as a result of the hedging derivative instrument's inability to offset the delivery price of the related energy.

Tax risk – The Authority is at risk that a change in Federal tax rates will alter the relationship between the interest rates incurred on its ART Notes and LIBOR Index used in the pay-fixed receive-variable interest rate swap transaction.

Rollover risk – The Authority is exposed to rollover risk on hedging derivative instruments that terminate prior to the maturity of the Authority's ART Notes, which these derivative instruments hedge. When the derivative instruments terminate the Authority will be re-exposed to the variable interest rate risk being hedged by the derivative instruments. The termination of the interest rate swaps on September 1, 2016 exposes the Authority to rollover risk since the hedged debt matures on March 1, 2020.

Certain electrical commodity-based derivative instruments are based upon projected future customer loads or facility operations. Beyond the terms of these derivative instruments (varying from one month to 48 months) the Authority is subject to the corresponding market volatilities.

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Termination risk – The Authority or its counterparties may terminate a derivative instrument agreement if the either party fails to perform under the terms of the agreement. The risk that such termination may occur at a time which may be disadvantageous to the Authority has been mitigated by including certain terms in these agreements by which the counterparty has the right to terminate only as a result of certain events, which includes a payment default by the Authority; other Authority defaults which remain uncured within a defined time-frame after notice; bankruptcy or insolvency of the Authority (or similar events); or a downgrade of the Authority's credit rating below investment grade. If at the time of termination the Authority has a liability position, related to its hedging derivative instruments, the Authority would be liable to the counterparty for a payment equal to the liability, subject to netting arrangements.

Market access risk – The Authority remarkets its CP Notes on a continuous basis and its ART Notes every March 1 and September 1. Should the market experience a disruption or dislocation, the Authority may be unable to remarket its Notes for a period of time. To mitigate this risk, the Authority has entered into liquidity facilities with highly rated banks to provide loans to support both the CP Note and ART Note programs. See note 6 of the notes to the financial statements.

Dodd Frank Act

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act ("DF Act") which addresses, among other things, interest rate and energy related commodity swap transactions of the type in which the Authority engages ("Swaps"). The requirements and processes are set forth in regulations promulgated by the Commodities Futures Trading Commission ("CFTC"). Pursuant to CFTC rules thus far, the Authority, as a public entity and electric utility which uses swaps solely to manage its risk, will be exempted from posting collateral beyond that of any existing credit support annexes in support of its open over-the-counter ("OTC") hedge positions. These CFTC rules are not anticipated to have significant impact on the Authority's liquidity and/or future risk mitigation activities. CFTC DF Act rules are still being promulgated, and Authority will continue to monitor their potential impact on the Authority's liquidity and/or future risk mitigation activities.

(9) Pension Plans, Other Postemployment Benefits, Deferred Compensation and Savings

(a) Pension Plans

The Authority and substantially all of the Authority's employees participate in the New York State and Local Employees' Retirement System (ERS) and the Public Employees' Group Life Insurance Plan (the Plan). These are cost-sharing, multiple-employer defined benefit retirement plans. The ERS and the Plan provide retirement benefits as well as death and disability benefits. Obligations of employers and employees to contribute and benefits to employees are governed by the New York State Retirement and Social Security Law (NYSRSSL). As set forth in the NYSSRSSL, the Comptroller of the State of New York (Comptroller) serves as sole trustee and administrative head of the ERS and the Plan. The Comptroller adopts and may amend rules and regulations for the administration and transaction of the business of the ERS and the Plan, and for the custody and control of their funds. The ERS and the Plan issue a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the New York State and Local Employees' Retirement System, 110 State Street, Albany, NY 12236.

The ERS is contributory except for employees who joined the ERS on or prior to July 27, 1976. Employees, who joined between July 28, 1976 and December 31, 2009 and have less than ten years of service, contribute 3% of their salary. Employees who joined the ERS on or after January 1, 2010 contribute 3% of their salary during their entire length of service. Employees who joined the ERS on or after April 1, 2012 contribute 3% of their salary through March 31, 2013 and up to 6% thereafter, based on their annual salary, during their entire length of service. Under the authority of the NYSSRSSL, the Comptroller shall certify annually the rates expressed as proportions of payroll of members, which shall be used in computing the contributions required to be made by employers.

The Authority is required to contribute at an actuarially determined rate. The required contributions for 2013, 2012 and 2011 were \$29 million, \$27 million and \$21 million, respectively. The Authority's contributions to the ERS were equal to 100% of the required contributions for each year.

A decline in financial markets could adversely impact state pension investment market values, including those of the ERS. If ERS's investment market values are adversely impacted, increases in the annual contributions to ERS in subsequent years may occur. The average contribution rate relative to payroll for the fiscal years ended March 31, 2013 was 18%. The average contribution rates relative to payroll for the fiscal years ended March 31, 2014 and 2015 have been set at approximately 19% for each year.

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(b) Other Postemployment Benefits (OPEB)

The Authority provides certain health care and life insurance benefits for eligible retired employees and their dependents under a single employer noncontributory (except for certain optional life insurance coverage) health care plan. Employees and/or their dependents become eligible for these benefits when the employee has at least 10 years of service and retires or dies while working at the Authority. Approximately 4,300 participants, including 1,600 current employees and 2,700 retired employees and/or spouses and dependents of retired employees, were eligible to receive these benefits at December 31, 2013. The Authority's post-retirement health care trust does not issue a stand-alone financial report.

Through 2006, other postemployment benefits (OPEB) provisions were financed on a pay-as-you-go basis and the plan was unfunded. In December 2006, the Authority's Trustees authorized staff to initiate the creation of a trust for OPEB obligations (OPEB Trust), with the trust fund to be held by an independent custodian. Prior to 2009, the Authority funded the OPEB Trust with contributions totaling \$225 million. Plan members are not required to contribute to the OPEB Trust. The Authority did not make any contributions to the OPEB Trust in 2010. During 2011, the Authority's Trustees approved ongoing annual funding of the Trust in order to strengthen the Authority's financial position. Contributions of \$22 million were made to the OPEB Trust in both 2013 and 2012.

The following table shows the components of the Authority's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the Authority's net OPEB obligation.

	<u>2013</u>	<u>2012</u>	<u>2011</u>
		(\$ in millions)	
Annual OPEB cost:			
Annual required contribution (ARC):			
Normal cost	\$ 11	\$ 10	\$ 9
Amortization payment	<u>31</u>	<u>27</u>	<u>22</u>
Total	42	37	31
ARC adjustment	4	9	7
Interest on net OPEB obligation	<u>(5)</u>	<u>(5)</u>	<u>(3)</u>
Annual OPEB cost	<u>\$ 41</u>	<u>\$ 41</u>	<u>\$ 35</u>
Net OPEB obligation:			
Net OPEB (asset) obligation at beginning of fiscal year	\$ (71)	\$ (71)	\$ (46)
Annual OPEB cost	41	41	35
Employer contribution:			
Benefit payments for retirees during the year	(20)	(19)	(20)
Trust fund contributions	<u>(22)</u>	<u>(22)</u>	<u>(40)</u>
Total employer contribution	<u>(42)</u>	<u>(41)</u>	<u>(60)</u>
Net OPEB (asset) obligation at end of fiscal year	<u>\$ (72)</u>	<u>\$ (71)</u>	<u>\$ (71)</u>

The net OPEB asset of \$72 million, which consists of \$21 million current assets and \$51 million noncurrent assets, is reported in miscellaneous receivables and other long-term assets, respectively, in the statements of net position at December 31, 2013.

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The Authority's annual OPEB cost for 2013 was \$41 million, which is reflected as an expense in the statements of revenues, expenses, and changes in net position. The Authority's annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GAS No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. As indicated herein, the Authority uses a 20-year amortization period.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits. The Authority's most recent actuarial valuation was performed as of January 1, 2012 and resulted in an actuarial accrued liability of \$517 million which was funded with assets totaling \$283 million indicating that the Authority's retiree health plan was 55% funded as of the valuation date. As of December 31, 2013 and 2012, the balance in the OPEB Trust was \$422 million and \$341 million, respectively, and the actuarial accrued liability was \$573 million and \$544 million, respectively, resulting in the retirees' health plan being 74% funded.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. In the 2012 actuarial valuation, the projected unit credit actuarial cost method was used with benefits attributed on a level basis. The actuarial assumptions included a 7% investment rate of return (net of administrative expenses) and an annual healthcare cost trend rate of approximately 9% (net of administrative expenses), including inflation, declining approximately 1/2% each year to an ultimate trend rate of approximately 5%. Both the cost trend rate and the ultimate trend rate include a 3% inflation assumption. The Authority amortizes gains and losses over an open 20-year period while continuing to amortize its initial unfunded accrued liability over a closed 20-year period.

(c) Deferred Compensation and Savings Plans

The Authority offers union employees and salaried employees a deferred compensation plan created in accordance with Internal Revenue Code, Section 457. This plan permits participants to defer a portion of their salaries until future years. Amounts deferred under the plan are not available to employees or beneficiaries until termination, retirement, death or unforeseeable emergency.

The Authority also offers salaried employees a savings plan created in accordance with Internal Revenue Code, Section 401(k). This plan also permits participants to defer a portion of their salaries. The Authority matches contributions of employees up to limits specified in the plan. Such matching annual contributions were approximately \$2.5 million and \$2.4 million for 2013 and 2012, respectively.

Both the deferred compensation plan and the savings plan have a loan feature.

Independent trustees are responsible for the administration of the 457 and 401(k) plan assets under the direction of a committee of union representatives and nonunion employees and a committee of nonunion employees, respectively. Various investment options are offered to employees in each plan. Employees are responsible for making the investment decisions relating to their savings plans.

(10) Nuclear Plant Divestiture and Related Matters

(a) Nuclear Plant Divestiture

On November 21, 2000 (Closing Date), the Authority sold its nuclear plants—Indian Point 3 (IP3) and James A. FitzPatrick (JAF) to two subsidiaries of Entergy Corporation (collectively Entergy or the Entergy Subsidiaries) for cash and noninterest-bearing notes totaling \$967 million (subsequently reduced by closing adjustments to \$956 million) maturing over a 15-year

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period. The present value of these payments recorded on the Closing Date, utilizing a discount rate of 7.5%, was \$680 million.

As of December 31, 2013 and 2012, the present value of the notes receivable were:

	<u>2013</u>		<u>2012</u>
		(In millions)	
Notes receivable – nuclear plant sale	\$ 37	\$	53
Less due within one year	<u>18</u>		<u>16</u>
	<u>\$ 19</u>	\$	<u>37</u>

The long-term portion of this notes receivable is reported in other noncurrent assets in the statements of net position at December 31, 2013 and 2012.

On September 6, 2001, a subsidiary of Entergy Corporation completed the purchase of Indian Point 1 and 2 (IP1 and IP2) nuclear power plants from Consolidated Edison Company of New York Inc. Under an agreement between the Authority and Entergy, which was entered into in connection with the sale of the Authority's nuclear plants to Entergy, the acquisition of the IP2 nuclear plant by a subsidiary of Entergy resulted in the Entergy subsidiary which now owns IP3 being obligated to pay the Authority \$10 million per year for 10 years beginning September 6, 2003, subject to certain termination and payment reduction provisions upon the occurrence of certain events, including the sale of IP3 or IP2 to another entity and the permanent retirement of IP2 or IP3. The Authority received its final \$10 million payment on September 6, 2012. The 2012 payment received was included in other nonoperating income.

As part of the Authority's sale of its nuclear projects to Entergy Subsidiaries in November 2000, the Authority entered into two Value Sharing Agreements (VSAs) with them. These VSAs, as amended, provide for the Entergy Subsidiaries to pay the Authority a set price (\$6.59 per MWh for IP3 and \$3.91 per MWh for JAF) for all MWhs metered from each plant between 2007 and 2014, with the Authority being entitled to receive annual payments up to a maximum of \$72 million. Nonoperating income, in the statements of revenues, expenses, and changes in net position, for the years ended December 31, 2013 and 2012 included \$72 million and \$71.7 million, respectively, relating to these agreements. The payments are subject to continued ownership of the facilities by the Entergy Subsidiaries or its affiliates.

If the license for IP3 or JAF is extended, an amount equal to \$2.5 million (per plant) per year for a maximum of 20 years, would be paid to the Authority by the relevant Entergy Subsidiary for each year of life extension during which the plant operates. The original licenses for JAF and IP3 expire in 2014 and 2015, respectively. In April 2007, the NRC received a license renewal application (for an additional 20 years) for IP3. On September 9, 2008, the NRC renewed the operating license of JAF for 20 years to October 17, 2034.

As a result of competitive bidding, and not related to the sale of the nuclear plants, the Authority's agreement to purchase energy from Entergy's IP3 and IP2 nuclear power plants in the total amount of 200 MW expired in 2013.

(b) Nuclear Fuel Disposal

In accordance with the Nuclear Waste Policy Act of 1982, in June 1983, the Authority entered into a contract with the U.S. Department of Energy (DOE) under which DOE, commencing not later than January 31, 1998, would accept and dispose of spent nuclear fuel. In conjunction with the sale of the nuclear plants, the Authority's contract with the DOE was assigned to Entergy. The Authority remains liable to Entergy for the pre-1983 spent fuel obligation (see note 11(e)) "New York State Budget and Other Matters" relating to a temporary transfer of such funds to the State). As of December 31, 2013 and 2012, the liability to Entergy totaled \$216 million.

(c) Nuclear Plant Decommissioning

In connection with the Authority's sale of the nuclear plants, the Authority entered into a Decommissioning Agreement with each of the Entergy Subsidiaries relating to the responsibility for decommissioning the nuclear plants acquired. The Decommissioning Agreements deal with the decommissioning funds (the Decommissioning Funds) currently maintained by the Authority under a master decommissioning trust agreement (the Trust Agreement). Under the Decommissioning Agreements, the Authority will make no further contributions to the Decommissioning Funds.

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The Authority retains contractual decommissioning liability for IP3 and JAF until license expiration, a change in the tax status of the fund, or any early dismantlement of the plant, at which time the Authority will have the option of terminating its decommissioning responsibility and transferring the plant's fund to the Entergy Subsidiary owning the plant. At that time, the Authority will be entitled to be paid an amount equal to the excess of the amount in the Fund over the Inflation Adjusted Cost Amount, if any. The Inflation Adjusted Cost Amount for a plant means a fixed estimated decommissioning cost amount adjusted in accordance with the effect of increases and decreases in the U.S. Nuclear Regulatory Commission (NRC) minimum cost estimate amounts applicable to the plant. The Authority's decommissioning responsibility is limited to the lesser of the Inflation Adjusted Cost Amount or the amount of the plant's Fund.

Certain provisions of the Decommissioning Agreements provide that if the relevant Entergy Subsidiary purchases, or operates, with the right to decommission, another plant at the IP3 site, then the Inflation Adjusted Cost Amount would decrease by \$50 million. In September 2001, a subsidiary of Entergy purchased the Indian Point 1 and Indian Point 2 plants adjacent to IP3.

If the Authority is required to decommission IP3 or JAF pursuant to the relevant Decommissioning Agreement, an affiliate of the Entergy Subsidiaries, Entergy Nuclear, Inc. would be obligated to enter into a fixed price contract with the Authority to decommission the plant, the price being equal to the lower of the Inflation Adjusted Cost Amount or the plant's Fund amount.

Decommissioning Funds of \$1,300 million and \$1,186 million are included in restricted funds and other noncurrent liabilities in the statements of net position at December 31, 2013 and 2012, respectively.

(11) Commitments and Contingencies

(a) *Power Programs*

Recharge New York Power Program

Chapter 60 (Part CC) of the Laws of 2011 (Chapter 60) established the "Recharge New York Power Program" (RNYPP), administered by the Authority, which has as its central benefit up to 910 MW of low cost power comprised of up to 455 MW of hydropower from the Niagara and St. Lawrence-FDR Projects and up to 455 MW of other power procured by the Authority from other sources. The 910 MW of power is available for allocation as provided by Chapter 60 to eligible new and existing businesses and not-for-profit corporations under contracts of up to seven years. RNYPP was effective beginning July 1, 2012.

The RNYPP replaced two other programs, the Power for Jobs (PFJ) and Energy Cost Savings Benefit (ECSB) Programs, which had extended benefits of low-cost power to certain businesses, small businesses and not-for-profit organizations. Those PFJ and ECSB Program customers who were in substantial compliance with contractual commitments under the PFJ and ECSB Programs and who applied but did not receive RNYPP allocations are eligible to apply for transitional electricity discounts, as provided for in Chapter 60. This transitional electricity discounts program provides for declining levels of discounts through June 30, 2016 when the program terminates, if payment of such discounts is deemed feasible and advisable by the Authority's Trustees. In June 2012, the Authority's Trustees authorized transitional electricity discount payments of up to \$9 million for the year July 1, 2012 – June 30, 2013. As of December 31, 2013, approximately \$1.2 million of such discounts have been paid.

The hydropower used for the RNYPP was power formerly used to provide low-cost electricity to domestic and rural customers of the three private utilities that serve upstate New York. To mitigate the impacts from the redeployment of this hydropower for the RNYPP, Chapter 60 created a "Residential Consumer Discount Program" (RCDP). The RCDP authorizes the Authority, as deemed feasible and advisable by its Trustees, to provide annual funding of \$100 million for the first three years following withdrawal of the hydropower from the residential and farm customers, \$70 million for the fourth year, \$50 million for the fifth year, and \$30 million each year thereafter, for the purpose of funding a residential consumer discount program for those customers that had formerly received the hydropower that is utilized in the RNYPP. Chapter 60 further authorizes the Authority, as deemed feasible and advisable by the Trustees, to use revenues from the sales of hydroelectric power, and such other funds of the Authority, as deemed feasible and advisable by the Trustees, to fund the RCDP. The Authority's Trustees have authorized the release of a total \$337.5 million through January 2014 in support of the RCDP. The Authority supplemented the market revenues through the use of internal funds, from the August 2011 start of the program through December 31, 2013, totaling cumulatively \$77 million. Operations and maintenance expenses included \$100 million of residential consumer discounts in each of the years ended December 31, 2013 and 2012.

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Western New York Power Proceeds Allocation Act

Effective March 30, 2012, Chapter 58 (Part GG) of the Laws of 2012 (Chapter 58) created the Western New York Power Proceeds Act (WNYPPA). The WNYPPA authorizes the Authority, as deemed feasible and advisable by the Trustees, to deposit net earnings from the sale of unallocated Expansion Power and Replacement Power from the Authority's Niagara project into an account administered by the Authority known as the Western New York Economic Development Fund (Fund). Net earnings are defined as any excess revenues earned from such power sold into the wholesale market over the revenues that would have been received had the power been sold at the Expansion Power and Replacement Power rates. Proceeds from the Fund may be used to support eligible projects undertaken within a 30-mile radius of the Niagara power project that satisfy applicable criteria. Chapter 58 also establishes a five-member Western New York Power Allocations Board, which is appointed by the Governor. Chapter 58 also repealed Chapter 436 of the Laws of 2010 which had created a similar program that could not be effectively implemented.

The Authority's Trustees have approved the release of up to \$35 million in net earnings, calculated for the period August 30, 2010 through December 31, 2013 as provided in the legislation, for deposit into the Fund. As of December 31, 2013, \$26 million has been deposited into the Fund. As of December 31, 2013, the Authority has approved awards of Fund money totaling approximately \$12.8 million to businesses that have proposed eligible projects and has made payments totaling \$1 million to such businesses. Payment of these awards is contingent upon the execution of acceptable contracts between the Authority and individual awardees.

(b) Governmental Customers in the New York City Metropolitan Area

In 2005, the Authority and its eleven NYC Governmental Customers, including the Metropolitan Transportation Authority, the City of New York, the Port Authority of New York and New Jersey (Port Authority), the New York City Housing Authority, and the New York State Office of General Services, entered into long-term supplemental electricity supply agreements (Agreements). Under the Agreements, the NYC Governmental Customers agreed to purchase their electricity from the Authority through December 31, 2017, with the NYC Governmental Customers having the right to terminate service from the Authority at any time on three years' notice and, under certain limited conditions, on one year's notice, provided that they compensate the Authority for any above-market costs associated with certain of the resources used to supply the NYC Governmental Customers.

Under the Agreements, the Authority will modify rates annually through a formal rate case where there is a change in fixed costs to serve the NYC Governmental Customers. Except for the minimum volatility price option, changes in variable costs, which include fuel and purchased power, will be captured through contractual pricing adjustment mechanisms. Under these mechanisms, actual and projected variable costs are reconciled and all or a portion of the variance is either charged or credited to the NYC Governmental Customers. The Authority provides the customers with indicative electricity prices for the following year reflecting market-risk hedging options designated by the NYC Governmental Customers. Such market-risk hedging options include a full cost energy charge adjustment ("ECA") pass-through arrangement relating to fuel, purchased power, and NYISO-related costs (including such an arrangement with some cost hedging) and a sharing option where the customers and the Authority will share in actual cost variations as specified in the Agreements. For 2012 and 2013, the NYC Governmental Customers chose a market-risk hedging price option designated an "ECA with hedging" pricing option whereby actual cost variations in variable costs are passed through to the customers as specified above. Under the Agreements, the Authority committed to finance up to \$100 million annually over the term of the Agreements for energy efficiency projects and initiatives at such governmental customers' facilities. Amounts financed may exceed \$100 million if mutually agreed to by the customers and the Authority. The costs of such projects are recovered from such customers.

As a result of a Request for Proposals for Long-Term Supply issued in 2005 and the Trustees' 2011 authorization, Authority staff entered into negotiations with Hudson Transmission Partners, LLC (HTP) for an agreement to serve the long-term requirements of the Authority's NYC Governmental Customers and to improve the transmission infrastructure serving New York City through the transmission rights associated with HTP's proposed transmission line (the Line) extending from Bergen County, New Jersey, to Consolidated Edison's West 49th Street substation. In 2011, the Authority executed a Firm Transmission Capacity Purchase Agreement (FTCPA) with HTP which would provide the Authority with 75% of the Line's 660 MW capacity, or 495 MW, for 20 years. The Authority's capacity payment obligations under the FTCPA began upon the Line's commencement of commercial operation, which occurred on June 3, 2013. Also upon commercial operation, the FTCPA obligates the Authority to reimburse HTP for the cost of interconnection and transmission upgrades in New York and New Jersey associated with the Line and to pay for all remaining upgrade costs as they are incurred. Accordingly,

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through December 2013, the Authority paid approximately \$173 million to HTP for completed upgrades. The total cost of the upgrades is estimated to be approximately \$250 million.

The Authority is currently in negotiations with certain of its NYC Governmental Customers and other third parties regarding partial recovery of the costs of the Line. It is estimated that the revenues derived from the Authority's rights under the FTCPA will not be sufficient to fully cover the Authority's costs under the FTCPA during the initial 20-year term of the FTCPA. Depending on a number of variables, it is estimated that the Authority's under-recovery of costs under the FTCPA could be in the range of approximately \$50 million to \$70 million per year during the first five years of commercial operation. In April 2013, the Authority entered into a three-year contract with Con Edison Energy, Inc. (CEE), an affiliate of Consolidated Edison Company of New York, Inc. to manage the Authority's transmission capacity on the Line and make economical energy transactions.

In anticipation of the closure of the Authority's Poletti plant in 2010, the Authority, in 2007, issued a nonbinding request for proposals for up to 500 MW of in-city unforced capacity and optional energy to serve the needs of its NYC Governmental Customers. This process, which included approval of the NYC Governmental Customers, resulted in a long-term electricity supply contract in 2008 between the Authority and Astoria Energy II LLC for the purchase of the output of Astoria Energy II, a new 550-MW plant, which was constructed and entered into commercial operation on July 1, 2011 in Astoria, Queens. The costs associated with the contract will be borne by these customers for the life of the Astoria Energy II contract. The Authority is accounting for and reporting this lease transaction as a capital lease in the amount of \$1.217 billion as of December 31, 2013, which reflects the present value of the monthly portion of lease payments allocated to real and personal property. The balance of the monthly lease payments represents the portion of the monthly lease payment allocated to operations and maintenance costs which are recorded monthly. Fuel for the plant is provided by the Authority and the costs thereof are being recovered from the NYC Governmental Customers.

The Authority's other Southeastern New York (SENY) Governmental Customers are Westchester County and numerous municipalities, school districts, and other public agencies located in Westchester County (collectively, the "Westchester Governmental Customers"). By early 2008, the Authority had entered into a new supplemental electricity supply agreement with all 103 Westchester Governmental Customers. Among other things, under the agreement, an energy charge adjustment mechanism is applicable, and customers are allowed to partially terminate service from the Authority on at least two months' notice prior to the start of the NYISO capability periods. Full termination is allowed on at least one year's notice, effective no sooner than January 1 following the one year notice.

(c) *Small, Clean Power Plants and 500-MW Plant*

To meet capacity deficiencies and ongoing load requirements in the New York City metropolitan area that could also adversely affect the statewide electric pool, the Authority placed in operation, in 2001, the Small, Clean Power Plants (SCPPs), consisting of eleven natural-gas-fueled combustion-turbine electric units, each having a nameplate rating of 47 MW at six sites in New York City and one site in the service region of LIPA.

As a result of the settlement of litigation relating to certain of the SCPPs, the Authority has agreed under the settlement agreement to cease operations at one of the SCPP sites, which houses two units, under certain conditions and if the Mayor of New York City directs such cessation. No such cessation has occurred.

(d) *Legal and Related Matters*

St. Regis Litigation

In 1982 and again in 1989, several groups of Mohawk Indians, including a Canadian Mohawk tribe, filed lawsuits against the State, the Governor of the State, St. Lawrence and Franklin counties, the St. Lawrence Seaway Development Corporation, the Authority and others, claiming ownership to certain lands in St. Lawrence and Franklin counties and to Barnhart, Long Sault and Croil islands (St. Regis litigation). These islands are within the boundary of the Authority's St. Lawrence-FDR Project and Barnhart Island is the location of significant Project facilities. Settlement discussions were held periodically between 1992 and 1998. In 1998, the Federal government intervened on behalf of all Mohawk plaintiffs.

The parties agreed to a land claim settlement, dated February 1, 2005, which if implemented would include, among other things, the payment by the Authority of \$2 million a year for 35 years to the tribal plaintiffs, the provision of up to 9 MW of low cost Authority power for use on the reservation, the transfer of two Authority-owned islands; Long Sault and Croil, and a 215 acre parcel on Massena Point to the tribal plaintiffs, and the tribal plaintiffs withdrawing any judicial challenges to the Authority's new license, as well as any claims to annual fees from the St. Lawrence FDR project.

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The legislation required to effectuate the settlement was never enacted and the litigation was reactivated. In November 2006, all defendants moved to dismiss the three Mohawk complaints as well as the United States' complaint based on the lengthy delay in asserting the land claims (i.e., the laches defense).

On September 28, 2012, the U.S. Magistrate recommended dismissal of all land claims brought against the Authority by three St. Regis tribal factions as well as the Federal government. The Magistrate upheld the Authority's laches defense and also recommended dismissal on the same grounds of all claims by the same plaintiffs against the other defendants relating to all but one of the other challenged mainland parcels.

In orders dated July 2013, the Judge assigned to the case accepted the Magistrate's recommendation and granted the Authority judgment on the pleadings. The Judge accepted all but one of the Magistrate's other recommendations, which results in dismissal of all land claims against the other defendants except those relating to two mainland parcels. Barring an appeal by the plaintiffs, all claims against the Authority have been dismissed and the lawsuit against the Authority is concluded.

In the interim, the State and the St. Regis plaintiffs have been discussing a settlement of the land claims, as well as other issues between the State and the tribes. The discussions are ongoing. Federal and State legislation would be required for any settlement, including one that would involve payments or concessions to be made by the Authority, to become effective.

The Authority had accrued an estimated liability based upon the provisions of the February 1, 2005 settlement related to this litigation. However, while the Authority is unable to predict the outcome of the matters described above, the Authority believes that it has meritorious defenses and positions with respect thereto and as result of current court rulings has reversed its previously accrued estimated liability. The reversal of this liability did not have any effect on the Authority's net income for 2012.

Tropical Storm Irene

In late November 2011, approximately 14 notices of claim were received by the Authority involving the heavy rains and widespread flooding resulting from Tropical Storm Irene's passage through the Northeast in late August 2011. The notices of claim essentially claim that property and other damages allegedly incurred by certain landowners were the result of the Authority's negligence in its operations at its Blenheim-Gilboa Pumped Storage Power Project located on the Schoharie Creek in Schoharie County, New York. In addition, in mid-January 2012, the County of Schoharie, eight towns and villages therein, and one school district ("Municipalities") filed a motion in Schoharie County Supreme Court requesting leave to serve late notices of claim on the Authority. In August 2012, the Municipalities initiated a lawsuit in Schoharie County Supreme Court against the Authority involving the heavy rains and widespread flooding resulting from Tropical Storm Irene's passage through the Northeast in August 2011. The Municipalities essentially allege that they sustained property damage and lost tax revenues resulting from lowered assessed valuation of taxable real property due to the Authority's negligence in its operations at the Blenheim-Gilboa pumped-storage hydroelectric facility located on the Schoharie Creek in Schoharie County, New York. The Municipalities complaint seeks judgment "in an amount to be determined at trial with respect to each of the ten plaintiffs in the sum of at least \$5,000,000, plus punitive damages in the sum of at least \$5,000,000" as well as attorney fees. In February 2012, a private landowner filed a similar motion and lawsuit in such court on behalf of a park campground and makes nearly the same allegations with the plaintiff seeking at least \$5 million in damages, at least \$5 million in punitive damages, as well as attorney's fees. In November 2012, the Authority formally responded to the two lawsuits.

In December 2012, the Authority was served with a third lawsuit by five plaintiffs arising out of Tropical Storm Irene and the Authority's operation of its Blenheim-Gilboa Pumped Storage Project. Plaintiffs previously filed timely notices of claim. The five plaintiffs include three individual landowners and two corporations. The three individual landowners own properties located in Schoharie, NY and Central Bridge, NY and are claiming damages in the aggregate amount of \$1.55 million. The two corporations also own properties in Schoharie, NY and are claiming damages in the aggregate amount of \$1.05 million.

While the Authority is unable to predict whether and to what extent any lawsuits will be initiated based on notices of claim or similar claims that may be filed in the future, or the outcome of any litigation, the Authority believes that it has meritorious defenses and positions with respect thereto. Conversely, adverse decisions of a certain type in the matters discussed above could adversely affect Authority operations and revenues.

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Other Actions or Claims

In addition to the matters described above, other actions or claims against the Authority are pending for the taking of property in connection with its projects, for negligence, for personal injury (including asbestos-related injuries), in contract, and for environmental, employment and other matters. All of such other actions or claims will, in the opinion of the Authority, be disposed of within the amounts of the Authority's insurance coverage, where applicable, or the amount which the Authority has available therefore and without any material adverse effect on the business of the Authority.

(e) *New York State Budget and Other Matters*

Section 1011 of the Power Authority Act (Act) constitutes a pledge of the State to holders of Authority obligations not to limit or alter the rights vested in the Authority by the Act until such obligations together with the interest thereon are fully met and discharged or unless adequate provision is made by law for the protection of the holders thereof. Bills are periodically introduced into the State Legislature, which propose to limit or restrict the powers, rights and exemption from regulation that the Authority currently possesses under the Act and other applicable law or otherwise would affect the Authority's financial condition or its ability to conduct its business, activities, or operations, in the manner presently conducted or contemplated by the Authority. It is not possible to predict whether any such bills or other bills of a similar type which may be introduced in the future will be enacted.

In addition, from time to time, legislation is enacted into New York law that purports to impose financial and other obligations on the Authority, either individually or along with other public authorities or governmental entities. The applicability of such provisions to the Authority would depend upon, among other things, the nature of the obligations imposed and the applicability of the pledge of the State set forth in Section 1011 of the Act to such provisions. There can be no assurance that in the case of each such provision, the Authority will be immune from the financial obligations imposed by such provision. Examples of such legislation affecting only the Authority include legislation, discussed below and elsewhere herein, relating to the Authority's voluntary contributions to the State, the Authority's temporary transfer of funds to the State, and contributions and transfers to fund temporary and permanent programs administered by the Authority and other State entities.

Budget

The Authority is requested, from time to time, to make financial contributions or transfers of funds to the State. Any such contribution or transfer of funds must (i) be authorized by law (typically, legislation enacted in connection with the State budget), and (ii) satisfy the requirements of the Bond Resolution. The Bond Resolution requirements to withdraw moneys "free and clear of the lien and pledge created by the (Bond) Resolution" are as follows: (1) such withdrawal must be for a "lawful corporate purpose as determined by the Authority," and (2) the Authority must determine "taking into account, among other considerations, anticipated future receipt of Revenues or other moneys constituting part of the Trust Estate, that the funds to be so withdrawn are not needed" for (a) payment of reasonable and necessary operating expenses, (b) an Operating Fund reserve for working capital, emergency repairs or replacements, major renewals, or for retirement from service, decommissioning or disposal of facilities, (c) payment of, or accumulation of a reserve for payment of, interest and principal on senior debt, or (d) payment of interest and principal on subordinate debt.

In May 2011, the Authority's Trustees adopted a policy statement (Policy Statement) which relates to, among other things, voluntary contributions, transfers, or other payments to the State by the Authority after that date. The Policy Statement provides, among other things, that in deciding whether to make such contributions, transfers, or payments, the Authority shall use as a reference point the maintenance of a debt service coverage ratio of at least 2.0, in addition to making the other determinations required by the Bond Resolution. The Policy Statement may at any time be modified or eliminated at the discretion of the Authority's Trustees.

Legislation enacted into law, as part of the 2000-2001 State budget, as amended up to the present time, has authorized the Authority as deemed feasible and advisable by the trustees, to make a series of voluntary contributions into the State treasury in connection with the PFJ Program and for other purposes as well. The PFJ Program, which had been extended to June 30, 2012, has ended and was replaced by the RNYPP, as discussed above in note 11(a) "Recharge New York Power Program" of the notes to the financial statements. Cumulatively through December 31, 2012, the Authority has made voluntary contributions to the State totaling \$475 million in connection with the ended PFJ Program.

In 2013 and 2012, the Authority made \$65 million and \$85 million, respectively, in contributions to the State that are not related to the PFJ Program and which were recorded as nonoperating expenses in the year ended December 31, 2013 and

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2012 statements of revenues, expenses and changes in net position. These contributions were consistent with the related State fiscal year budgets and were authorized by the Authority's Trustees. The 2013 contributions of \$65 million include \$45 million that was paid to Empire State Development to support the New York State Open for Business economic development initiative in lieu of the voluntary contributions to the State's General Fund for the State fiscal year 2013-2014. Of the \$85 million contributed in 2012, \$10 million was paid to support the Open for Business initiative. An additional \$50 million was paid to support this initiative in January 2014 pursuant to Trustee approval and this amount will be recognized as a nonoperating expense in the Authority's 2014 fiscal year. Cumulatively, between January 2008 and December 31, 2013, the Authority has made voluntary contributions to the State totaling \$492 million unrelated to the PFJ program.

The Governor's Executive Budget for State Fiscal Year 2014-2015, released in January 2014, and subsequently amended, contains language authorizing the Authority, as deemed feasible and advisable by its Trustees, to (i) make a contribution to the State treasury to the credit of the General Fund, or as otherwise directed in writing by the Director of the Budget, in an amount of up to \$90 million for the State fiscal year commencing April 1, 2014, the proceeds of which will be utilized for to support energy-related initiatives of the State or for economic development purposes, and (ii) transfer up to \$25 million of any such contribution by June 30, 2014 and the remainder of any such contribution by March 31, 2015.

Temporary Asset Transfers

In addition to the authorization for voluntary contributions, as a result of budget legislation enacted in February 2009, the Authority was requested to provide temporary asset transfers to the State of funds held in reserves. Pursuant to the terms of a Memorandum of Understanding dated February 2009 (MOU) between the State, acting by and through the State's Director of Budget, and the Authority, the Authority agreed to transfer approximately \$215 million associated with its Spent Nuclear Fuel Reserves (Asset B) by March 27, 2009. The Spent Nuclear Fuel Reserves are funds that had been set aside for payment to the federal government sometime in the future when the federal government accepts the spent nuclear fuel for permanent storage (see note 10(b) "Nuclear Fuel Disposal"). The MOU provides for the return of these funds to the Authority, subject to appropriation by the State Legislature and the other conditions described below, at the earlier of the Authority's payment obligation related to the transfer and disposal of the spent nuclear fuel or September 30, 2017. Further, the MOU provides for the Authority to transfer within 180 days of the enactment of the 2009-2010 State budget \$103 million of funds set aside for future construction projects (Asset A), which amounts would be returned to the Authority, subject to appropriation by the State Legislature and the other conditions described below, at the earlier of when required for operating, capital or debt service obligations of the Authority or September 30, 2014. In February 2009, the Authority's Trustees authorized the execution of the MOU relating to the temporary transfers of Asset B (\$215 million) and Asset A (\$103 million) and such transfers were made in March 2009 and September 2009, respectively, following Trustee approval.

The MOU provides that the obligation of the State to return all or a portion of an amount equal to the moneys transferred by the Authority to the State is subject to annual appropriation by the State Legislature. Further, the MOU provides that as a condition to any such appropriation for the return of the moneys earlier than September 30, 2017 for the Spent Nuclear Fuel Reserves and earlier than September 30, 2014 for the construction projects, the Authority must certify that the monies available to the Authority are not sufficient to satisfy the purposes for which the reserves, which are the source of the funds for the transfer, were established.

The Governor's Executive Budget for State Fiscal Year 2014-2015, released in January 2014, and subsequently amended, contains language that would make the \$103 million appropriation available to the Authority either: (i) pursuant to a repayment agreement submitted by the Authority and approved by the Director of the Budget, or (ii) upon certification of the Director of the Budget, at the request of the Authority when and to the extent that the Authority certifies to the Director that the monies available to the Authority are not sufficient to meet the Authority's obligations with respect to its debt service or operating or capital programs.

The Authority has classified the transfers of Assets A and B (\$318 million) as a long-term loan receivable. In lieu of interest payments, the State has waived certain future payments from the Authority to the State. The waived payments include the Authority's obligation to pay until September 30, 2017 the amounts to which the State is entitled under a governmental cost recovery process for the costs of central governmental services. These payments would have been approximately \$5 million per year based on current estimates but the waiver is limited to a maximum of \$45 million in the aggregate during the period. Further, the obligation to make payments in support of certain State park properties and for the upkeep of State lands adjacent to the Niagara and St. Lawrence power plants is waived from April 1, 2011 to March 31, 2017. These payments would have been approximately \$8 million per year but the waiver would be limited to a maximum of \$43 million for the period. The present value of the waivers approximates the present value of the forgone interest income.

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(f) Relicensing of Niagara

By order issued March 15, 2007, FERC issued the Authority a new 50-year license for the Niagara project effective September 1, 2007. In doing so, FERC approved six relicensing settlement agreements entered into by the Authority with various public and private entities. By decision dated March 13, 2009, the U.S. Court of Appeals for the District of Columbia Circuit denied a petition for review of FERC's order filed by certain entities, thereby concluding all litigation involving FERC's issuance of the new license. In 2007, the Authority estimated that the capital cost associated with the relicensing of the Niagara project would be approximately \$495 million. This estimate does not include the value of the power allocations and operation and maintenance expenses associated with several habitat and recreational elements of the settlement agreements. As of December 31, 2013, the balance in the liability associated with the relicensing on the statement of net position is \$277 million (\$31 million in current and \$246 million in other noncurrent liabilities)

In addition to internally generated funds, the Authority issued additional debt obligations in October 2007 to fund, among other things, Niagara relicensing costs. The costs associated with the relicensing of the Niagara project, including the debt issued therefore, were incorporated into the cost-based rates of the project beginning in 2007.

(g) Regional Greenhouse Gas Initiative and Air Pollution Rule

The Regional Greenhouse Gas Initiative (RGGI) is a cooperative effort by Northeastern and Mid-Atlantic states, including New York, to hold carbon dioxide emission levels steady from 2009 to 2014 and then reduce such levels by 2.5% annually in the years 2015 to 2018 for a total 10% reduction. Central to this initiative is the implementation of a multi-state cap-and-trade program with a market-based emissions trading system. The program requires electricity generators to hold carbon dioxide allowances in a compliance account in a quantity that matches their total emissions of carbon dioxide for the compliance period. The Authority's Flynn plant, SCPPs, and 500-MW Plant are subject to the RGGI requirements as is AEII. The Authority has participated in program auctions commencing in September 2008 and expects to recover RGGI costs through its power sales revenues. The Authority is monitoring federal legislation and proposed programs that would impact RGGI. For 2014, the number of allowances offered in the auction by RGGI cap and trade program has been reduced (from allowances covering 165 million tons of carbon dioxide emissions in 2013 to 91 million tons in 2014), and will continue to decline by 2.5% each year from 2015 through 2020. This reduction may well likely increase the price for carbon dioxide allowances, which NYPA acquires to cover operation of its fossil-fuelled power plants and the Astoria Energy II plant. The Authority continues to monitor federal legislation and proposed programs that would impact RGGI.

During 2011, the Environmental Protection Agency ("EPA") issued a series of rulings to establish the Cross-State Air Pollution Rule ("CSAPR"). The CSAPR establishes emission allowance budgets for sulfur dioxide and nitrogen oxides for eastern states, including New York, and requires power plants in those states to hold allowances to cover their emissions. Certain trading of allowances is authorized under the CSAPR. In December 2011, the U.S. Court of Appeals for the D.C. Circuit (the "Court") granted a stay of the CSAPR pending the Court's resolution of numerous petitions for review and in the interim, the Court indicated that the EPA should continue to enforce its Clean Air Interstate Rule ("CAIR") which the CSAPR was designed to replace. By decision issued August 21, 2012, the Court vacated the CSAPR; directed the EPA to develop a replacement rule; and directed that the CAIR continue to be enforced pending the development of the replacement rule. On October 5, 2012, the EPA filed a petition seeking en banc rehearing of the Court's decision, which the Court denied on January 24, 2013. In 2013, the U.S. Supreme Court granted the EPA's request to review the D.C. Circuit's decision to invalidate EPA's CSAPR. Pending the U.S. Supreme Court decision, CAIR remains in effect. The Authority continues to operate its fossil-fuelled power plants and the Astoria Energy II plant within the allocated allowances under the CAIR. In the event the CSAPR, as promulgated by the EPA, is ultimately implemented, the Authority anticipates that operation of its fossil-fuelled power plants and the Astoria Energy II plant would not be impacted.

In 2013, President Obama sent a memorandum to EPA on "Power Sector Carbon Pollution Standards" (the "Presidential Memorandum") as part of the President's Climate Action Plan. The Presidential Memorandum requires the EPA to propose carbon pollution standards for power plants. In 2013, the EPA met the first milestone in the Presidential Memorandum by proposing stringent new carbon pollution standards affecting new large and small gas-fired and coal-fired generating units. Next, the EPA will issue proposed standards for existing power plants by June 1, 2014.

(h) Wind and Solar Initiatives

The Long-Island-New York City Offshore Wind Collaborative (Collaborative), which consists of the Authority, Con Edison, the Long Island Power Authority (LIPA), the City of New York and other New York City and New York State governmental entities, is evaluating the potential development of between 350 MW up to 700 MW of offshore wind. The Collaborative is currently planning the next steps in project evaluation. In January 2013, the Bureau of Ocean Energy

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Management (BOEM) issued a request to determine whether there is competitive interest in wind power development in federal waters off the coast of the Rockaway Peninsula and Long Island. When BOEM's review is completed, the agency will determine whether competitive interest in the lease area exists. If there is such interest, BOEM will use an auction(s) to award lease(s) under its competitive lease process.

In March 2012, the Authority's Trustees authorized up to \$30 million in funding over five years for a solar market acceleration program involving solar research, training, and demonstration projects.

(i) **Construction Contracts and Net Operating Leases**

Estimated costs to be incurred on outstanding contracts in connection with the Authority's construction programs aggregated approximately \$579 million at December 31, 2013.

Noncancelable operating leases primarily include leases on real property (office and warehousing facilities and land) utilized in the Authority's operations. Rental expense for years ended December 31, 2013 and 2012 was \$2 million in each year. Commitments under noncancelable operating leases are as follows:

	<u>Total</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Thereafter</u>
	(In millions)						
Operating leases	\$ <u>1.9</u>	<u>0.7</u>	<u>0.4</u>	<u>0.3</u>	<u>0.2</u>	<u>0.1</u>	<u>0.2</u>

(j) **Other Developments**

New York Energy Highway

In his January 2012 State of the State address, Governor Andrew M. Cuomo announced the New York Energy Highway initiative, which is envisioned as a public-private partnership to upgrade and modernize the State's electric power system. The Governor formed a task force comprised of various State officials to oversee implementation of the initiative (Task Force) which is co-chaired by the Authority's President and Chief Executive Officer, Gil C. Quinones. In April 2012, the Task Force issued a request for information seeking ideas and proposals in furtherance of the initiative. Approximately 85 organizations responded to the Task Force's request for information and the responses included a large number of different generation and transmission project proposals. Based on the response of all these organizations, the Energy Highway Task Force issued an action plan in October 2012. The resulting Energy Highway Blueprint, calling for public and private investments in the State's energy system of about \$5.7 billion over the next five to 10 years, proposed 13 specific actions, divided among four major categories: Expand and Strengthen the System, Accelerate Construction and Repair, Support Clean Energy and Technology Innovation.

In November 2012, the New York Public Service Commission (NYPSC) announced new proceedings addressing various actions described in the Blueprint including (i) the initiation of electric transmission upgrades to move excess power from upstate to downstate ("AC Transmission"), (ii) the creation of contingency plans to prepare for large generator retirements ("Generation Retirement Contingency Plans") and (iii) the expansion of natural gas delivery to homeowners and businesses in New York State.

In response to the request for information and the Generation Retirement Contingency Plans and AC Transmission proceedings, the New York Transmission Owners (NYTOs), comprised of the State's largest private utilities, the Long Island Power Authority, and the Authority, indicated that they were exploring the creation of a new Statewide transmission entity (NY Transco) to pursue development, construction, operation, and ownership of new transmission projects. The NYTOs proposed to the Task Force and to the NYPSC several transmission projects that could be undertaken by a NY Transco entity.

In its November 4, 2013 Generation Retirement Contingency Plan Order, the NYPSC selected three transmission projects to be built by Consolidated Edison, New York State Gas and Electric and the Authority. The NYPSC also requested that the NYTOs seek Federal Energy Regulatory Commission (FERC) approval for these three projects.

Continued participation of the Authority in the NY Transco is contingent on the enactment of legislation by the State that enables the Authority to participate.

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Notes to the Financial Statements

December 31, 2013 and 2012

Build Smart NY Initiative

On December 28, 2012, Governor Andrew M. Cuomo issued Executive Order No. 88 (EO 88) directing state agencies collectively to reduce energy consumption in state-owned and managed buildings by 20 percent within seven years – an initiative designed to produce significant savings for New York taxpayers, generate jobs, and significantly reduce greenhouse gas emissions. To meet this initiative, the Governor launched Build Smart NY, a plan to strategically implement EO 88 by accelerating priority improvements in energy performance. The Authority has offered to provide \$450 million in low-cost financing for this initiative for state owned buildings and an additional \$350 million for towns and municipalities. Such low-cost financing would be funded by proceeds of the Authority's commercial paper or another form of debt. The Authority's costs of financing would be recovered from the energy efficiency customers in this program. In addition, as provided for in EO 88, the Authority has established a central management and implementation team to carry out the Build Smart NY plan. In 2013, the Authority provided approximately \$75 million in financing for energy efficiency projects at State agencies and authorities covered by EO 88.

Energy Efficiency Market Acceleration Program

In June 2012, the Authority's Trustees authorized up to \$30 million in funding over five years for an energy efficiency market acceleration program involving energy efficiency research, demonstration projects, and market development. As of December 31, 2013, the Authority's Trustees have approved the award of contracts with a cumulative value of up to approximately \$22 million.

**REQUIRED SUPPLEMENTARY INFORMATION
(UNAUDITED)**

New York Power Authority

Required Supplementary Information

(Unaudited)

Schedule of Funding Progress for the Retiree Health Plan

(In millions)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)--- Projected Unit Credit Method (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
January 1, 2012	\$ 283	\$ 517	\$ 234	55%	\$ 143	163%
January 1, 2010	218	400	182	55	141	129
January 1, 2008*	100	337	237	30	133	178
January 1, 2006	—	301	301	—	130	232

* During 2007, a trust for the Authority's OPEB obligations was funded with an initial amount of \$100 million. This amount is reflected in the table above as of the 1/1/08 Actuarial Valuation Date.



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New York Power Authority Audit Committee Meeting March 25, 2014 2013 Audit Results

**Ken Deon, Partner
Scott Heiser, Senior Manager
Nick DiVirgilio, Manager**

This presentation to the Audit Committee is intended solely for the information and use of the Audit Committee and management and is not intended to be and should not be used by anyone other than these specified parties. This presentation is not intended for general use, circulation or publication and should not be published, circulated, reproduced or used for any purpose without our prior written permission in each specific instance.

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Audit results

Results of the audit

- Scope and audit testing consistent with that discussed on September 24, 2013
- Scope focused on the following:
 - Revenue and accounts receivable (NYISO, SENY and Wholesale)
 - Derivatives (purchased power and financial)
 - Long-term debt obligations including compliance with covenants
 - Accuracy and recoverability of regulatory assets and deferred charges
 - Capital assets additions
 - Investments and compliance with the New York State Comptroller's investment regulations
- No material misstatements identified
- No corrected or uncorrected adjustments identified
- No significant deficiencies or material weaknesses identified within internal controls
- KPMG will issue an unqualified opinion on the Authority's financial statements
- KPMG will issue an unqualified opinion on the Authority's compliance with its investment guidelines with no exceptions noted in compliance or internal control

Significant accounting policies

- Significant accounting policies are disclosed in the financial statements
- We have reviewed the accounting policies used by management in preparation of the financial statements and found such policies to be appropriate

Significant accounting policies	Financial statement accounts affected
■ Accounting for Rate Regulation	<ul style="list-style-type: none"> ■ Deferred charges ■ Regulatory assets/liabilities
■ Revenue Recognition	<ul style="list-style-type: none"> ■ Receivables ■ Revenue
■ Derivatives – Energy and Interest Rate	<ul style="list-style-type: none"> ■ Purchased power costs ■ Interest/financing cost ■ Deferred inflows/outflows
■ Cash and Investments	<ul style="list-style-type: none"> ■ Cash and investments ■ Investment income ■ Decommissioning trust fund
■ Capital Assets	■ Capital assets, depreciation
<ul style="list-style-type: none"> ■ Asset Retirement Obligations ■ Removal Costs 	<ul style="list-style-type: none"> ■ Other assets ■ Other liabilities

Significant judgments and estimates

- We have reviewed the accounting estimates used by management in preparation of the financial statements. We evaluated the key factors and assumptions used by management and found such factors and assumptions to be reasonable.

Accounting area	Financial statement accounts affected
<ul style="list-style-type: none"> ■ Self-Insurance Accruals <ul style="list-style-type: none"> – Claims and Damages 	<ul style="list-style-type: none"> ■ Deferred credits and other ■ Operating expense
<ul style="list-style-type: none"> ■ Asset Retirement Obligations 	<ul style="list-style-type: none"> ■ Deferred charges, long-term receivables and other ■ Deferred credits and other
<ul style="list-style-type: none"> ■ Energy Derivatives ■ Interest Rate Derivatives 	<ul style="list-style-type: none"> ■ Deferred outflows ■ Risk management obligations
<ul style="list-style-type: none"> ■ Other Post-employment Benefits (OPEB) 	<ul style="list-style-type: none"> ■ Miscellaneous receivables and other ■ Deferred charges, long-term receivables and other
<ul style="list-style-type: none"> ■ Accounting for Rate Regulation 	<ul style="list-style-type: none"> ■ Regulatory assets – risk management activities ■ Deferred charges, long-term receivables and other

Audit risks and issues

Key audit risks/account balances and primary procedures to address the risk:

- Revenue
 - Appropriate revenue recorded as power is delivered
 - Confirmation of Receivables and detailed testing of SENY/Wholesale revenue
 - Agree SENY/Wholesale billed rates to the approved tariffs
 - Confirmation and detail testing of Revenue/Receivables with NYISO
 - Detail testing of wheeling charges
- Derivatives
 - Valuation of derivatives associated with energy price and interest rate fluctuations
 - Testing management's determination of the fair value of derivatives utilizing firm valuation specialists
 - Confirm open derivative contracts and key terms with counterparties
 - Testing management's determination of hedging effectiveness utilizing firm specialists
 - Detail testing derivative settlements throughout the year
- Long Term Debt
 - Appropriate classification of debt and assessment of compliance with covenants
 - Confirm outstanding long term debt, including commercial paper with third parties
 - Recalculate interest expense throughout the year
 - Review debt covenants and ensure the Authority was compliant as of December 31, 2013

Audit risks and issues (continued)

- Regulatory Assets/Liabilities and Deferred Charges
 - Appropriate assessment of the recoverability and accuracy of amounts deferred
 - Detail tested additions to deferred charges/regulatory assets throughout the year
 - Assessed the recoverability of the charges to ensure they are appropriately deferred
- Capital Assets
 - Appropriate capitalization and depreciation of assets
 - Test additions and disposals from capital assets to ensure amounts are appropriately capitalized
 - Test depreciation expense recorded for the year
 - Review the impairment policy to ensure there were no trigger events
- Investments (including Nuclear Decommissioning Trust Fund)
 - Appropriate accounting for investments in accordance with approved guidelines
 - Fair market value testing of all investments
 - Review of sample of investments for compliance with Board approved policies
 - Reporting and receipt of information and accounting for decommissioning trust and liabilities
 - Review of financial statements for completeness and accuracy of trust assets and obligations
- Management Judgments and accounting estimates
 - Appropriate methodologies and assumptions in assessing exposures/liabilities
 - Reviewed methodology, assumptions (and third party reports/data) for reasonableness of amounts set up as reserves/liabilities
- Manual Journals and non recurring transactions
 - Appropriate accounting for existence and accuracy of unusual nonrecurring transactions
 - Selection and review of manual journal entries based on the timing of the entries, recording to certain accounts and recorded by specific members of management

Consideration of fraud risks

Summary of Fraud-Related Audit Procedures

In accordance with Statement on Auditing Standards (SAS) No. 99, Consideration of Fraud in a Financial Statement Audit, we have a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud.

Principal Audit Procedures

In executing our fraud-related audit procedures under SAS No. 99, we:

- Performed fraud risk assessment, which included the following:
 - Reviewed analytical procedures performed in planning the audit
 - Completed client/engagement continuance procedures
 - Reviewed interim financial statements
 - Held a meeting among engagement team personnel regarding fraud risk factors
- Evaluated client programs and controls to prevent, detect, and deter fraud
- Made inquiries of certain members of management and others within the entity about the risks of fraud and their knowledge of any fraud
- Reviewed postclosing journal entries and significant accounting estimates
- Reviewed significant accounting estimates and nonroutine transactions

KPMG reports

- Audit Opinion on the Authority's Financial Statements as of and for the year ended December 31, 2013
- Accountant's Report on Investment Compliance with New York State Guidelines
- Auditor's Report on Internal Control over Financial Reporting and on Compliance on Other Matters
- Required Communications to the Audit Committee (SAS 114 letter)
- Management Letter – Not applicable this year

Other matters

Related-party transactions	No issues were noted
Litigations, claims, and assessments	No issues were noted
Illegal acts or fraud	No instances of fraud or suspected fraud involving management or employees who have significant roles where fraud may result in a material misstatement of the financial statements were noted.
Noncompliance with laws and regulations	No matters involving actual or suspected non-compliance with laws and regulations came to our attention during the course of the audit.
Significant difficulties encountered during the audit	No matters to report
Disagreements with management	No matters to report
Management's consultation with other accountants	No matters to report
Significant issues discussed, or subject to correspondence, with management	No matters to report
Scope limitation	No matters to report
Other findings or issues relevant regarding oversight of the financial reporting process	No matters to report
External confirmations (If relevant)	No matters to report

Material written communications between KPMG and management

- Engagement letter
- Management representation letters
 - Financial statement report
 - Investment compliance report
- SAS 114 letter

Independence

- We are in compliance with the Public Authority Accountability Act in regards to non-audit services
- In our professional judgment, we are independent with respect to the Authority, as that term is defined by the professional standards (AICPA).
- Contact the KPMG Ethics and Compliance Hotline with questions or concerns
 - Phone: 1-877-576-4033
 - Online: www.kpmgethics.com

KPMG's Audit Committee Institute (ACI)

Communicating with Audit Committees Since 1999

Upcoming Events

- 11th Annual Audit Committee Issues Conference

- February 2 – 3, 2015

This conference brings together Audit Committee members from around the country to discuss challenges, practices, and priorities shaping Audit Committees and board agendas.

- Audit Committee Quarterly Webcast Series

- March 27, 2014 11:00am EST

- A quarterly Webcast providing updates and insights into issues affecting Audit Committee/board oversight – from key accounting and regulatory changes to developments in risk oversight.

Resources

- *Audit Committee Insights – U.S. and International editions (biweekly electronic publications):* www.kpmginsights.com
- ACI Web site: www.auditcommitteeinstitute.com
- ACI mailbox: auditcommittee@kpmg.com
- ACI hotline: [1-877-KPMG-ACI](tel:1-877-KPMG-ACI)



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