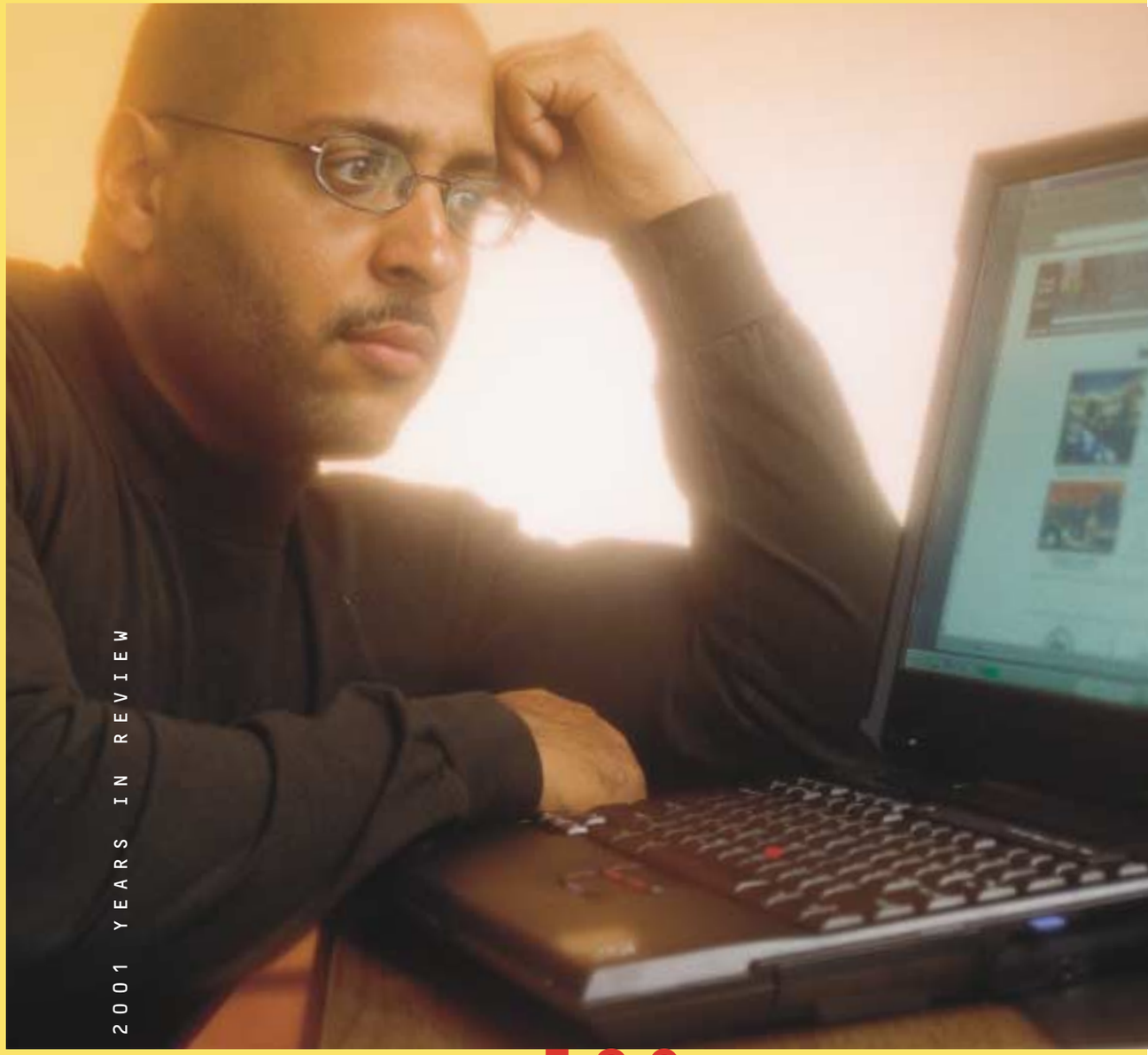
ISO NEW ENGLAND INC.

Holyoke, Massachusetts

413/535-4000 www.iso-ne.com

The people behind New England's power



2000 2001 YEARS IN REVIEW

ISO NEW ENGLAND

COVER: JACQUES ASSELIN, CUSTOMER SERVICE SPECIALIST

PAGE 10: DAVID BERTAGNOLLI, PRINCIPAL ENGINEER, NEAR TERM TRANSMISSION RELIABILITY

PAGE 16: KIM WHITNEY-YOUNG, OPERATIONS COORDINATOR

PAGE 24: LEFT TO RIGHT:

BRIAN SNOW, SYSTEM OPERATOR
JAMES "SEAMUS" MCGOVERN, SUPERVISOR, CONTROL ROOM OPERATIONS
DANIEL DILLON, OPERATIONS SHIFT SUPERVISOR
JANICE SERAFINI, TRAINING COORDINATOR

ISO New England 2000-2001 Years in Review

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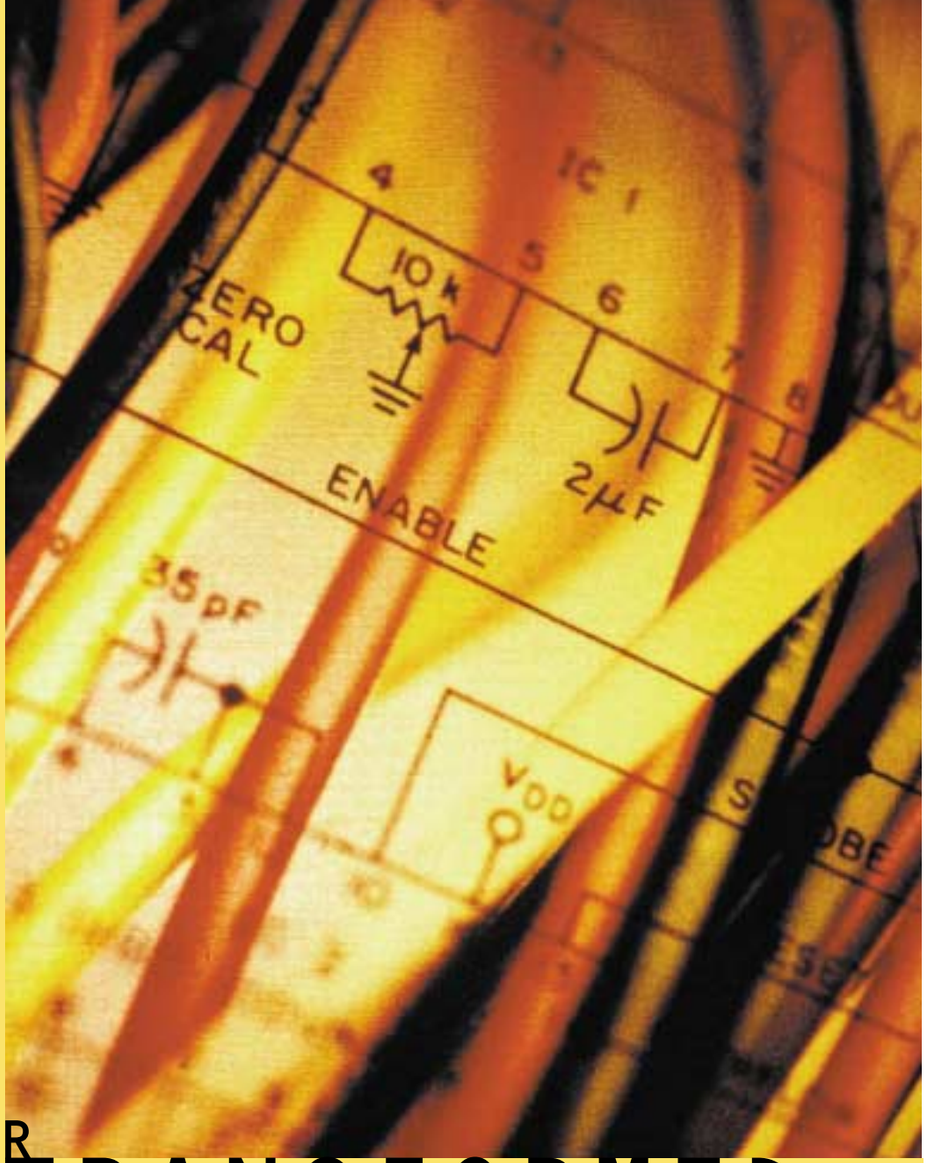


POWER TRANSFORMED

New England's electric power industry, like that of the entire nation, has changed dramatically during the past few decades. Until the 1970s, the industry was comprised of utilities that handled every aspect of providing electricity: generating it, transmitting it and then distributing it to homes and businesses. These utilities were regulated local monopolies that operated independently of each other.

The Great Northeast Blackout of 1965 marked a turning point for the region's electric power industry. Concerned about the system's reliability, the Northeast's power companies formed three "power pools" to ensure a dependable supply of electricity. The New England Power Pool (NEPOOL), formed in 1971 by the region's private and municipal utilities, was intended to foster cooperation and coordination among utilities in the six-state region.

During the next three decades, NEPOOL created a regional power grid that now includes more than 350 separate generating units, more than 8,000 miles of transmission lines and a generating capacity of more than 28,000 megawatts.

THE PURPOSE OF THE GRID WAS TO ENSURE THE RELIABLE, SAFE DELIVERY OF ELECTRICITY TO EVERY HOME AND BUSINESS IN THE REGION.

A second turning point for New England's electric power industry came in the 1990s. Electric power had been tightly regulated for a century, with federal, state and local governments each having a role in determining such factors as the price utilities could charge their customers. In the years leading up to that period, many industries, including transportation, communications and financial services, experienced sweeping deregulation as a means of creating competitive, more efficient industries.

Eventually, the federal government acted to deregulate the electric power industry. Most utilities, which previously had been responsible for all aspects of electric power were required to unbundle their generation operations from their transmission operations. A new wholesale market was created for generators to sell the electricity they produced to utilities and others who would then sell it to residential and business users.

The Federal Energy Regulatory Commission (FERC) created new institutions called independent system operators to oversee this new wholesale market. In an age of deregulation, these independent system operators would also independently operate and administer the bulk power system and ensure open and fair access to the transmission network that brings power from generators to utilities and then to homes and businesses.

The independent system operator for New England, ISO New England, began operation on July 1, 1997, with a little more than 130 former NEPOOL staff members who had previously been responsible for managing the region's power supply. These were the very first of The People Behind New England's Power.

Since ISO New England's creation, NEPOOL has continued to operate as a voluntary association, with membership expanded to incorporate all of the wholesale power market's participants, including not only utilities and municipal light companies, but also merchant generators, transmission companies, suppliers, end-user groups and others.

During 1998-99, ISO New England worked closely with NEPOOL to develop the rules and procedures for the new wholesale power market. With FERC approval, the new market opened for business on May 1, 1999.

Over the past two years, we have taken the wholesale electricity market in New England from a period of experimentation to one of standardization. We began implementing the Standard Market Design and are moving toward forming a Regional Transmission Organization. We are striving for a seamless market for the Northeast that will facilitate easier transfer of electricity among states, guarantee better bidding practices for market participants and reduce inefficiencies in the market with the promise of greater choice and greater long-term efficiency through competition.

THE OPERATION OF NEW ENGLAND'S WHOLESALE ELECTRICITY MARKET SHOWCASES THE BEST OF OUR PEOPLE, PROCESSES AND TECHNOLOGY.

LETTER FROM THE PRESIDENT AND CEO

GORDON VAN WELIE,
PRESIDENT AND CEO*

Who are The People Behind New England's Power? They are the more than 300 men and women of ISO New England who ensure that New Englanders have the electricity they need to live their daily lives. Their job is to keep the lights on every minute of every day, and they do so in two ways: by ensuring that enough bulk electricity is generated and transmitted to meet daily demand and that the exchange of wholesale power between buyers and sellers is equitable.

What makes the people of ISO New England remarkable? In short, it's their ability to maintain these day-to-day operations while monitoring and refining the wholesale electricity system so that it meets the demands of growth and change intrinsic to the industry as it undergoes unprecedented restructuring. While years 2000-2001 brought formidable challenges to the organization, ISO New England exceeded expectations, making considerable enhancements in the reliability and efficiency of the bulk power system and its marketplace that are necessary in the new era of free-market competition.

The People Behind New England's Power

Enhancing the market: Throughout 2000 and 2001, ISO New England built on progress made during the market's first year to provide a fair and efficient venue for buyers and sellers to exchange wholesale power. As the independent system operator for the region's wholesale power market, it is our job to ensure that this market operates fairly, efficiently and competitively, in accordance with rules approved both by federal regulators and by the market participants themselves. When it is determined that there are flaws in the wholesale market rules, we commit to fix them. In fact, our commitment to implement reforms to the current markets, our decision to implement the Standard Market Design, and our efforts toward forming a Regional Transmission Organization are clear evidence of this.

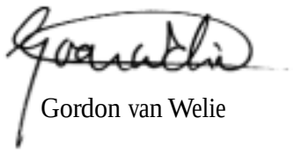
Strengthening the infrastructure: ISO New England remains at the forefront of the industry in seeking and creating market-based answers to power system needs. In summer 2001, we faced the highest demand for electricity in New England history and were able to meet the challenge with the addition of 3,000 megawatts of generation, along with the implementation of an innovative and collaborative Load Response Program designed to reduce consumption during peak periods of demand. At FERC's request, we developed a comprehensive Regional Transmission Expansion Plan to identify bottlenecks in the system that tend to decrease marketplace efficiency and hinder our ability to meet demand in constrained areas. The first of its kind in the country, the plan serves as a blueprint for investment and improvement in the power station system infrastructure.

Integrating process and technology: Throughout last year we dramatically improved our processes and performance as an organization. We expanded our market monitoring and project management capabilities so that we can systematically identify areas for reform and efficiently plan improvements to the system. And, since the events of September 11, coordinated information efforts among electricity industry participants have enabled us to better monitor the security of the energy infrastructure in New England.

While the introduction of competition has created challenges in the industry, we strive to address them with greater vision and cooperation than ever before. In sustaining a successful energy strategy, ISO New England must continue to refine measures to improve wholesale electricity markets; focus on developing the right market incentives to build and expand our electricity infrastructure; and achieve greater coordination of energy, environment and economic policy making in New England.

The People Behind New England's Power are the people who have the knowledge and the ingenuity to ensure the region's electric power system meets today's demands. I am proud of their commitment and dedication to ensuring that the lights stay on all over New England.

Sincerely,



Gordon van Welie

*On May 18, 2001, the Board of Directors chose Gordon van Welie as ISO New England's President and CEO, replacing Philip J. Pellegrino, who resigned as President and CEO on January 4, 2001.

ISO NEW ENGLAND BOARD OF DIRECTORS

THE 10-MEMBER BOARD INCLUDES GORDON VAN WELIE, PRESIDENT AND CEO, AND FROM
BACK LEFT: MARY SHARPE HAYES, ALVIN K. KLEVORICK, JOHN G. KASSAKIAN, KENNETH R. LEIBLER, DONALD L. ISAACS
FRONT LEFT: ALGER "DUKE" B. CHAPMAN, VINCENT M. O'REILLY, VICE CHAIRMAN, WILLIAM W. BERRY, CHAIRMAN, V. LOUISE MCCARREN

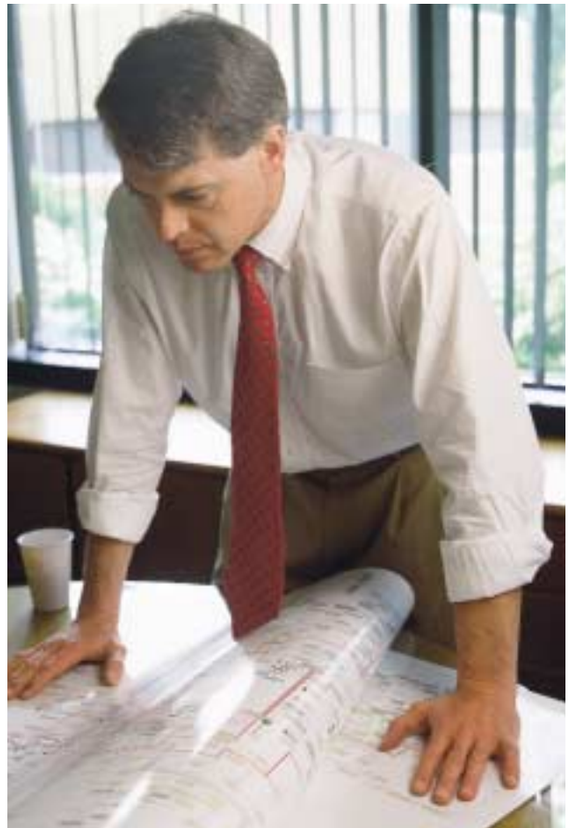
INDEPENDENTLY OPERATE AND ADMINISTER A HIGHLY RELIABLE BULK POWER SYSTEM AND A FAIR, EFFICIENT WHOLESALE ELECTRICITY MARKET.

We in New England were one of the first to implement a wholesale electricity market in the United States.

Our market system, like any market system, is by nature designed to send signals, or incentives, that result in responses by market participants–in our case, responses in bulk power generation, transmission and demand-side management.

These incentives keep the factors of production–the supply and demand–in balance, thus allowing industry participants to meet the energy needs of consumers without the "obligation to serve" that exists under a regulated system. For this balance to take place, however, the market must operate fairly, competitively and efficiently.

ISO New England acts as the market's monitor. We evaluate the system and coordinate the selection of appropriate solutions to ensure the market functions as it is intended to and to ensure that all of its participants abide by the market rules developed in concert with market participants and approved by FERC.



Inconsistencies or inefficiencies in the market that arise, in part due to the interconnected and interdependent nature of the industry, are addressed through market monitoring and mitigation, adjustment of market rules, appropriate transmission expansion and new generation by suppliers.

MARKET DEVELOPMENT *Staying on top*

2000-01 marked the first full years of operation of New England's wholesale electricity market. During that time, the marketplace evolved as market participants became familiar with a newly deregulated system. We, in turn, continued to evaluate and refine the market design with the goal of fostering a marketplace that would function well–a market that has the right incentives in place, that is fair and competitive and that ensures a reliable supply of electricity.

Throughout the last two years, we worked with market participants on a series of interim enhancements to our current single-settlement market with the longer-term goal of implementing a more robust, multi-settlement market design. These include reducing costly energy uplift, a socialized side payment, and capping the energy clearing price during times of a capacity deficiency. And, to support a robust marketplace, market rule changes are expected to allow more efficient energy pricing during periods of peak power demand.

We also made great strides toward developing a standard, seamless market for the Northeast that will increase competition and bolster reliability throughout the region. In February 2001, ISO New England and the New York Independent System Operator agreed to share power reserves, allowing lower cost operations in both regions. In November 2001, FERC authorized the sale of non-recallable electric generating capacity across the New England and New York border. It is clear that a natural marketplace exists between the regions, and the two ISOs are together doing their best to eliminate any barriers to buying and selling electricity.

STANDARD MARKET DESIGN *Optimizing the market system*

Over the past few years, ISO New England has worked with our counterparts in the Northeast, the PJM Interconnection and the New York Independent System Operator to move towards standardizing a market design that will:

- Reduce the barriers to the free flow of energy between regions;
- Supplement the overall reliability of bulk electric power systems throughout the Northeast; and
- Enhance the management and efficient operation of New England's wholesale electric power market.

In March 2001, we began a major market redesign effort to incorporate a market design based on PJM's rules that also included some of the best practices of New England's market management. Using a proven market design will speed up the implementation of new market rules by as much as a year and save upwards of $30 million in development costs, compared with developing a unique New England market design. ISO New England expects to implement Standard Market Design (SMD) during the first half of 2003. Key market features of SMD include new congestion management and multi-settlement systems (CMS and MSS) designed to reduce market inefficiencies and improve market responses.

ISO NEW ENGLAND IS MOVING TOWARDS STANDARDIZING A MARKET DESIGN

CMS helps to fairly allocate the cost of producing and transmitting electricity, which is currently socialized among wholesale market participants. The locational marginal pricing feature included within CMS will provide economic incentives needed to stimulate the location of new generating units, upgrades to transmission facilities and participation in demand-side management programs.

MSS determines how participants bid and are paid in the market. The two-part market settlement structure consists of "day-ahead" and "day-of" settlements that allow for greater financial certainty to market participants.

ISO New England's vision of standardized markets continues to evolve. During the last quarter of 2001, we began working with the New York ISO to develop a common electricity marketplace for our adjacent regions based on a common market design that incorporates SMD principles. SMD is viewed as the most advantageous and expedient approach to bringing needed wholesale market improvements to New England while progressing toward a single, seamless market for the Northeast. We are committed to the development of standardized, integrated markets, and with SMD, we will be one of the first regions to comply with FERC's efforts to standardize markets nationwide.

MARKET MONITORING *Assuring integrity and independence*

During the past two years, we strengthened our market monitoring and mitigation capabilities so that we are now better able to detect and mitigate actions intended to interfere with the competitive and efficient operation of the region's wholesale power market.

In June 2001, we hired an economics consulting firm to serve as Independent Market Adviser to ISO New England's Board of Directors and retained a strategic consulting firm to provide extended market analysis capabilities. Within the organization, we increased the size of our Market Monitoring and Market Power Mitigation department.

To underscore the independent role we play in managing the market, we commissioned third-party experts to analyze the operations and efficiency of New England's wholesale electricity market. The first study reviewed energy pricing processes to determine whether prices in peak demand periods are reflective of market rules and operational conditions, and produce the appropriate price signals. Findings of the study outlined valuable enhancements to the current NEPOOL market rules that will be implemented throughout the next year.

The second study assessed–and confirmed–the competitiveness of the New England market and found that it compares favorably with other U.S. wholesale electricity markets, with relatively low levels of "market power." Both studies support our implementation of SMD as a means of ensuring that the marketplace continues to be fair and competitive.

It is through these kinds of market monitoring efforts that we are able to pinpoint solutions and initiate enhancements to market rules and practices. Our market monitoring group will continue its ongoing evaluation of New England's electricity market so that we can facilitate the best possible market operations for the region's market participants.

REGIONAL TRANSMISSION ORGANIZATION
Creating a vision for the future

FERC strongly supports the creation of Regional Transmission Organizations, or RTOs, as the next step in the restructuring of the wholesale electric power industry. By directing ISOs to become RTOs, the federal government hopes to ensure greater coordination in planning and operating power grids, improved access to transmission lines that would enhance competition and larger pools to improve the reliability of the power system.

ISO New England supports the federal government's call for RTOs and worked throughout the last two years to develop an RTO model for New England. In January 2001, ISO New England and six companies owning transmission facilities in New England filed a plan to form the New England Regional Transmission Organization. FERC ordered mediation on the petition in July 2001, and a final order is expected in 2002.

Throughout this time, we took steps to strengthen relationships with other ISOs in the Northeast to enhance interregional coordination of the markets. On January 28, 2002, ISO New England and the New York ISO executed an agreement to jointly evaluate the feasibility of creating a Northeast Regional Transmission Organization (NERTO).

While the process for developing the NERTO is just beginning, we will continue our efforts to ensure that New England market participants and consumers reap the benefits of a larger, standardized and seamless power market. We are striving to create an RTO that will reflect regional needs and characteristics, employ best practices for its operations and take a prudent approach to creating a combined market.

Working toward convergence

THE PEOPLE BEHIND THE POWER

WORK COLLABORATIVELY AND PROACTIVELY WITH STATE AND FEDERAL REGULATORS, NEPOOL PARTICIPANTS AND OTHER STAKEHOLDERS.

ISO New England sets the standard for reliable operation and planning of the bulk power system.

A GROWING DEMAND
Generating the power New England needs

New England continues to attract investment in new generation capacity, keeping pace with the region's steadily growing demand for electric power and providing the economic and environmental benefits of the latest generating technologies.

During the past few years alone, more than a dozen power plants have come online in New England, and 16 more are under construction. That will total more than 11,000 megawatts of capacity added to the system since the market began in 1999–enough power to light up a major metropolitan area with 9.5 million homes. This added generation has already proved crucial, when in August 2001, the heat and humidity brought the four highest days of electricity use in New England's history. The extra 3,000 megawatts of power already online allowed the system to meet the record demand of 24,967 megawatts.

ISO New England forecasts peak summer demand to increase to 27,240 megawatts (under normal weather conditions) in 2010, from 23,150 megawatts in 2000–an overall increase of 17.5 percent. This new capacity will help us to stay ahead of the curve and ensure a reliable supply of electricity in the coming years.

GENERATOR UNIT AVAILABILITY *Measuring market readiness*

In June 2001, ISO New England released a study which found that generating unit availability in New England has improved since 1995. This study indicates that plant owners are responding to economic incentives to keep their plants running when demand is highest and that owners are scheduling planned maintenance during off-peak seasons.

As a result of this effort, ISO New England developed a comprehensive database that enables us to track hourly generating unit performance. Through analysis of this data and investigation of availability problems, reasons and trends for changes in unit availability are now documented as part of the quarterly Market Report.

NATURAL GAS *A generating mainstay*

New England's increasing reliance on cleaner-burning natural gas to fuel its new fleet of merchant generators will dramatically change the region's traditional fuel mix, as roughly 50 percent of New England's electricity will soon be generated using natural gas. Facing concern over the operational and reliability implications of such a change, ISO New England has recently undertaken studies to assess the adequacy of the region's interstate natural gas pipelines to serve both the seasonal demands from the traditional gas utilities and the ever-increasing demands from the electric power generation sector.

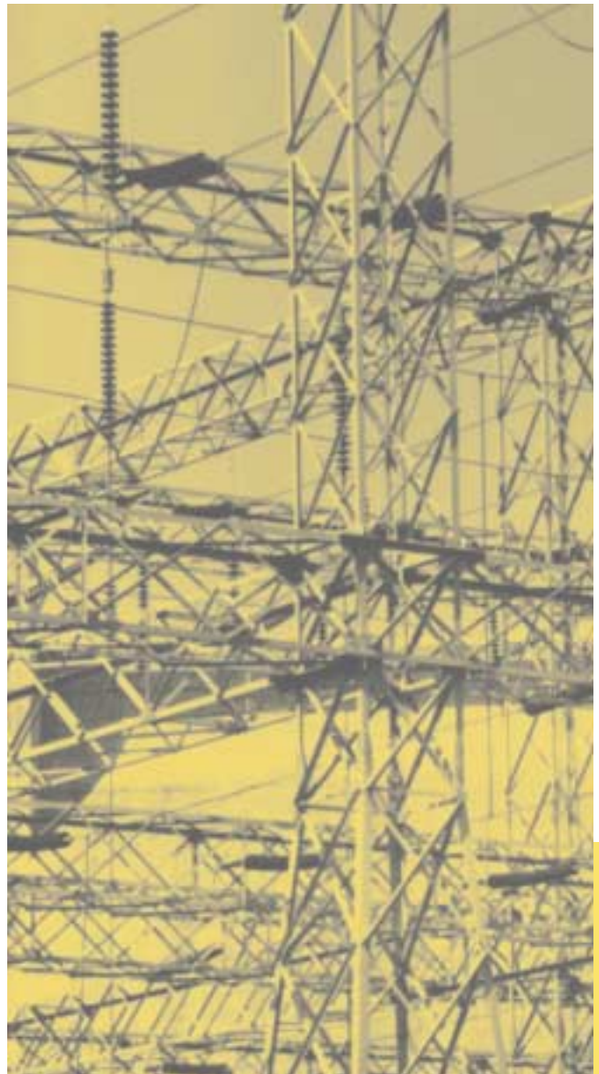
In February 2002, we released the second phase of a comprehensive technical assessment of the delivery capability of New England's interstate natural gas infrastructure. This analysis builds upon the foundations laid within a similar assessment published in Febuary 2001 and provides ISO New England with critical information to reliably dispatch the system.

REGIONAL TRANSMISSION EXPANSION PLAN

Getting the power where it needs to go

Projections show that, while we should have enough electricity for the next few years, we must address another challenge: how to get that electricity to where it needs to go. Outdated or inadequate transmission capabilities limit the transmission of power, especially into densely-populated areas of New England.

These constraints arise, in large part, because the correct economic incentives and signals designed to trigger investment in transmission and distribution system improvements have simply not been in place in most regions of the country, including New England.



Recognizing the need to address these transmission concerns, in 2001, FERC assigned ISO New England to develop a regional transmission plan. As an independent system operator, we were in a position to evaluate the necessary information in an objective manner and to develop a plan focused on the needs of the overall market.

Within a year, and with significant input from New England transmission owners and other industry stakeholders, including state regulatory agencies, ISO New England completed its evaluation of the region's transmission system, known as the 2001 Regional Transmission Expansion Plan, or RTEP01. The ISO New England Board of Directors unanimously approved the five-year assessment in October 2001. RTEP01 is currently one of the most comprehensive evaluations of a bulk electric power system in the country and should serve as a model for similar assessments in other regions.

RTEP01 combines several separate studies of the region's bulk power system reliability and cost to consumers. By identifying transmission system inefficiencies, the plan is a blueprint for investment in transmission expansion and upgrades, siting of new generation and the development of viable demand response programs. Taking these steps will help relieve "bottled generation," improve operating and market efficiency, reduce congestion costs and improve supply competition in areas that are both transmission constrained and that lack enough local generation.

While we are working on near- and long-term solutions, the bottom line remains that we need more transmission lines to transport the region's power–particularly in areas where we have identified constraints, such as southwestern Connecticut and greater Boston. The RTEP process supports ongoing solicitation of the most effective solutions to these issues through an open stakeholder process. It sets the direction for future efforts to address needed expansion of the region's transmission system.

Analyzing system needs

THE PEOPLE BEHIND THE POWER

DELIVER VALUABLE NEW PRODUCTS AND SERVICES TO MARKET PARTICIPANTS IN A TIMELY, COST-EFFECTIVE MANNER.

From grassroots efforts to high technology, ISO New England uses innovation to meet the demands of growth and new challenges.

CUSTOMER SERVICE
Quality and Responsiveness

Customer Services and Training (CST) provides the key link between market participants (our customers) and ISO New England's products and services. CST assures that customers and their employees are registered to do business, that their generation and load assets are on file, and that they can make secure digital connections to market systems.

CST also provides information needed to participate in the markets through its customer communications, call center and training programs. Each year, a score of newsletters, 600 Web-based special notices and responses to nearly 10,000 inquiries keep customers informed. For both 2000 and 2001, 1,200 customers participated in CST-sponsored training seminars and forums. During 2001, 200 customers also participated in SMD training–a number expected to swell to over 3,500 during 2002.

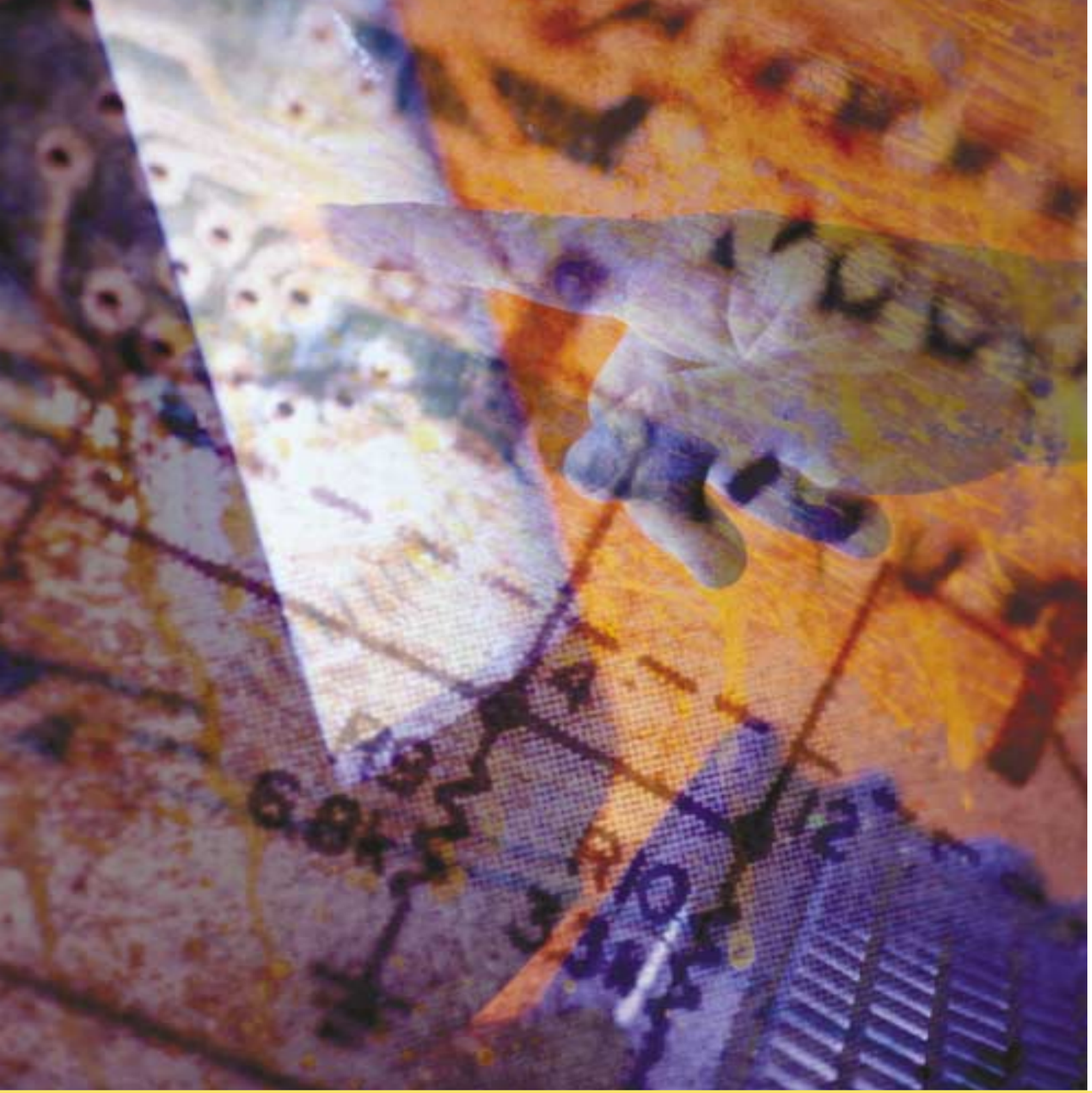
ELETRONIC DISPATCH *Going high-tech*

In response to NEPOOL concerns, ISO New England implemented an Electronic Dispatch (ED) system in 2000–a software system that automates the generation dispatch process. ED monitors conditions on the power grid so that power is dispatched as economically and efficiently as possible based on bid prices.

As is typical for any systems modification of this magnitude and complexity, post-implementation analysis, diagnostics and design changes were made to enhance the program's functional capabilities throughout 2001, including software improvements that recognize a wider array of dynamic system conditions and performance and send proper dispatch signals in accordance with market rules.

WIRELESS WEB ACCESS *Keeping in touch anytime, anywhere*

As of May 2001, ISO New England was the first independent system operator in the nation to offer wireless Web technology to its market participants. Market participants are now able to track important data, such as real-time energy prices, virtually anytime, anywhere, thus promoting marketplace efficiency and overall competitiveness.



LOAD RESPONSE PROGRAM *Involving the customers*

Well-functioning markets require price-sensitive buyers to discipline sellers, especially during times of scarcity. Currently, wholesale electricity markets in the United States do not have this feature, and as a result, markets remain more vulnerable to high prices because there is a lack of price-responsive load. So when system demand approaches maximum capacity, there is virtually no demand responsiveness to keep prices from increasing.

To stimulate these responses, ISO New England and NEPOOL joined in 2001 to initiate the Load Response Program–an energy conservation program designed to encourage reduced electricity use during peak demand periods and help moderate price fluctuations in the wholesale electricity market.

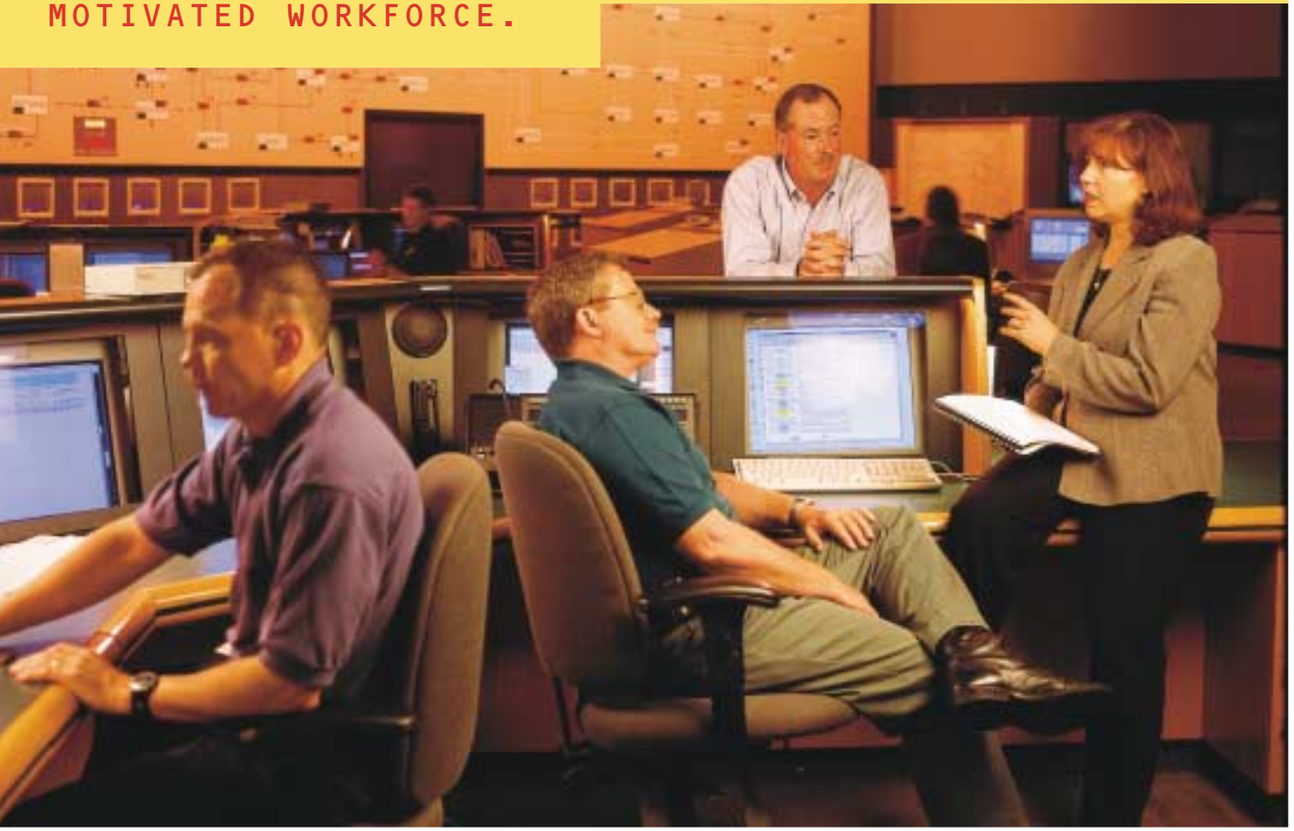
The Load Response Program has proven to be a critical element in managing the region's bulk power grid. It allows end users to have more control over their energy costs, it promotes conservation and efficiency, and it helps ensure the continued reliability of the system. Following a successful pilot program conducted in Winter 2001, load response was fully implemented last summer, helping us meet record load levels on the year's hottest days.

Our Load Response Program, in conjunction with our load response software vendor, RETX, was given the Demand Response Program award for 2001 by the Peak Load Management Alliance, a national energy industry group. More than 120 companies and organizations in New England are currently enrolled in the program.

Integrating process and technology

THE PEOPLE BEHIND THE POWER

ATTRACT, RETAIN AND DEVELOP A TALENTED, MOTIVATED WORKFORCE.



Created by the transfer of little more than 130 NEPOOL employees a few short years ago, ISO New England today has more than 300 men and women who work together to operate the region's bulk electricity grid and oversee its wholesale power markets.

ORGANIZATIONAL DEVELOPMENT *The definition of excellence*

The people of ISO New England are committed to four core values:

Independence. We always remember that we are the independent system operator, acting independently of state and local government, independently of the electric power industry and independently of special interests. We act on the belief that everyone benefits from fair, effective and efficient markets and a reliable bulk power system.

Collaboration. Although we are independent, we recognize the importance of collaborating with NEPOOL and its industry members, state and federal regulators and other stakeholders. Only by working together can we make deregulation succeed in New England.

Innovation. While the competitive electric power markets are still being defined, we continue to foster a spirit of innovation to ensure that the region's power system remains reliable and efficient and adapts to meet the demands of growth and new challenges.

Excellence. We have a highly talented workforce made up of the best and brightest from throughout the nation–and even the world. Their foresight, their ability and their willingness to do whatever it takes to get the job done is the very definition of excellence, and the single biggest factor in our growth and success.

These principles guide the work of ISO New England's employees and help us meet the challenges we face in electric power deregulation.

Committed to the challenges ahead

THE PEOPLE BEHIND THE POWER

Financial Statements for the years ended December 31, 2001 and 2000

Report of Independent Accountants

To the Board of Directors of ISO New England Inc.:

In our opinion, the accompanying statements of financial position and the related statements of activities and of cash flows present fairly, in all material respects, the financial position of ISO New England Inc., ("the Company") at December 31, 2001 and 2000, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP

March 14, 2002

STATEMENTS OF FINANCIAL POSITION

As of December 31,

	Year End (In Thousands) 2001	2000
Assets:		
Current Assets:		
Cash and cash equivalents	$19,300	$ 9,608
Cash held for Hydro-Quebec (Note 1)	-	7,582
Total cash and cash equivalents	19,300	17,190
Accounts receivable, net (Note 1)	11,238	11,637
Prepaid expenses	255	6
Noncurrent Assets:		
Property and equipment, net (Note 3)	50,628	19,591
Deferred charges (Note 1)	3,271	-
Other assets (Note 1)	38,850	4,791
Total assets	$123,542	$53,215
Liabilities and net assets:		
Current liabilities:		
Accounts payable (Note 1):		
Settlement, net	$ 164	$ 8,442
Administration	10,948	5,381
Deposits payable	39,326	5,135
Revolving credit (Note 4)	5,500	-
Interest payable	68	-
Daily billing advance collections (Note 1)	14,296	-
Accrued expenses	6,292	2,159
Working capital advances from NEPOOL Participants (Note 1)	-	10,521
Accrued pension and postretirement benefits (Note 5)	1,369	1,058
Deferred income (Note 1)	2,579	6,234
Capital expenditure funding from NEPOOL Participants	-	14,285
Long-term liabilities:		
Term loan (Note 4)	43,000	-
Total liabilities	123,542	53,215
Unrestricted net assets	-	-
Total liabilities and net assets	$123,542	$53,215

The accompanying notes are an integral part of the financial statements.

STATEMENTS OF ACTIVITIES

For the years ended December 31,

	Year End (In Thousands) 2001	2000
Changes in unrestricted net assets:		
Revenues (Note 1):		
ISO tariff revenues	$61,392	$43,362
Interest income	736	1,556
Fees and services	503	556
Total unrestricted revenues	62,631	45,474
Expenses:		
General and administrative:		
Salaries and benefits	31,176	25,231
Professional and consultants	15,089	8,222
Rents and leases	2,994	3,079
Computer services	3,361	1,959
Depreciation expense	2,833	1,423
Communication expense	1,395	1,522
Interest expense	1,037	-
Other	4,746	4,038
Total expenses	62,631	45,474
Change in unrestricted net assets	-	-
Unrestricted net assets, beginning of year	-	-
Unrestricted net assets, end of year	$ -	$ -

The accompanying notes are an integral part of the financial statements.

STATEMENTS OF CASH FLOWS

For the years ended December 31,

	Year End (In Thousands) 2001	2000
Cash flows from operating activities:		
Increase in unrestricted net assets	-	-
Adjustments to reconcile change in unrestricted net assets to Net cash provided by operating activities:		
Depreciation and amortization	$ 3,561	$ 2,152
Decrease/(Increase) in accounts receivable	399	(7,267)
Increase in deferred charges	(3,271)	-
(Increase)/Decrease in other assets	(34,059)	19,340
(Increase)/Decrease in prepaid expense	(249)	2
Increase/(Decrease) in accounts payable		
Settlement	(8,278)	8,442
Administration	5,567	1,108
Decrease in weekly billing advance collections	-	(6,433)
Increase in daily billing advance collections	14,296	-
(Increase)/Decrease in accrued pension and postretirement benefits	311	(63)
(Increase)/Decrease in accrued expenses	4,133	(1,032)
Increase in deposits payable	34,191	4,267
Decrease in disputes payable	-	(23,060)
Increase in interest payable	68	-
Decrease in deferred revenue	(3,655)	(438)
Net cash provided by (used in) operating activities	13,014	(2,982)
Cash flows from investing activities:		
Capital expenditures	(34,598)	(15,897)
Net cash used in investing activities	(34,598)	(15,897)
Cash flows from financing activities:		
Increase/(Decrease) in working capital advance from NEPOOL Participants	(10,521)	2,121
Increase/(Decrease) in capital expenditure funding from NEPOOL Participants	(14,285)	14,285
Proceeds from term loan	43,000	-
Proceeds from revolving credit, net	5,500	-
Net cash provided by financing activities	23,694	16,406
Net Increase/(Decrease) in cash and cash equivalents	2,110	(2,473)
Cash and cash equivalents, beginning of year	17,190	19,663
Cash and cash equivalents, end of year	$19,300	$ 17,190
Supplemental data:		
Cash paid during the year for interest:	$ 2,087	$ -

The accompanying notes are an integral part of the financial statements.

1. Nature of Operations & Summary of Significant Accounting Policies:

DESCRIPTION OF BUSINESS

ISO New England Inc. (the "Company" or "ISO") commenced operations on July 1, 1997 as the New England electric transmission independent system operator for the New England Power Pool ("NEPOOL") in compliance with the requirements of the Federal Energy Regulatory Commission ("FERC"). On May 1, 1999 the competitive marketplace opened in the ISO New England control area. The Company now administers NEPOOL's open-access transmission tariff, administers a power exchange, and ensures the reliable supply and transmission of electricity for the control area. The Company operates as an organization described in Section 501(c)(4) of the Internal Revenue Code and is exempt from tax pursuant to Section 501(a) of the Internal Revenue Code.

The FERC accepted ISO's "capital funding tariff" ("CFT") filing for 2001. This filing supported the ISO's loan arrangements with various banks for a line of credit to fund the capital and working capital requirements of the Company. The CFT must be refiled with FERC to increase the limits on borrowing as necessary.

CASH EQUIVALENTS

The Company considers cash on hand and short-term marketable securities with original maturities of three months or less to be cash equivalents. The cash equivalents at December 31, 2001 and 2000 were held in overnight repurchase agreements and also in direct and indirect obligations of the United States.

Restricted balances at any point in time consist of dollars held in security until settlement of Participants' accounts. At December 31, 2001 and 2000 $0 and $7,582,000, respectively, was held in security for payment to Hydro-Quebec.

ACCOUNTS RECEIVABLE AND ACCOUNTS PAYABLE

In the course of bulk power transactions administered by the Company on behalf of the NEPOOL Participants, amounts for energy purchased and sold among Participants become payable to and receivable from such Participants. The Company summarizes and prices the energy transactions each month and provides an invoice or remittance advice to each Participant that summarizes the amount either payable to or receivable from each Participant.

Included in the invoice or remittance advice is each Participant's share of Company expenses, which is netted into the payable or receivable amount for each Participant. Accounts payable on the balance sheet are segregated between the amounts owed, for which the ISO functions as paying agent, for energy transactions and for the amounts incurred by the Company in the course of operations.

The net receivables at the end of each month include those amounts which will be billed and included in the invoice or remittance advice to Participants in the subsequent month. The net payables and receivables for energy transactions are settled with the Participants in the subsequent month.

Accounts receivable and accounts payable are reflected net of NEPOOL Settlement amounts, which were $0 at December 31, 2001 and $7,582,000 at December 31, 2000. A default payment liability of $164,000 was outstanding at December 31, 2001 until it was invoiced to Participants. At December 31, 2000, a liability of $860,000 was owed to a Participant under a special billing arrangement. The December 31, 2001 default payment liability is covered by deposits held under the financial assurance policy.

CAPITAL EXPENDITURE FUNDING

Capital Expenditure Funding represents the liability due to the Participants for capital purchases of the Company plus accrued interest owed to the Participants for the year ending December 31, 2000. This balance was funded through April 2001 on a monthly basis by the NEPOOL Participants based upon their pro rata share of the ISO Tariff charges incurred by them for the previous month. Beginning January 1 of the year after the asset is placed in service, the amount of capital expenditures funded by the Participants shall be amortized in equal monthly amounts and repaid over the depreciation period as defined in accordance with generally accepted accounting principles, including interest thereon from the date of payment at a rate of 10.78%. This monthly repayment process began in January 2001 through April 2001. In June 2001, the Company received bank financing which enabled it to repay all remaining amounts due to NEPOOL participants and to fund future capital expenditures.

PROPERTY AND EQUIPMENT

The Interim Independent System Operator Agreement between the Company and NEPOOL states that any fixed assets acquired or developed by the Company shall be the property of the NEPOOL Participants. In FERC's conditional approval of the Company there was a requirement that the Company, not NEPOOL, fund all the Company's capital expenditures. The Company is presently negotiating an amendment to this agreement with NEPOOL to comply with this and other conditions or requirements promulgated by FERC. The Company has elected to capitalize additions in excess of $1,000 or whose useful life is greater than one year. Property and equipment is stated at cost, net of accumulated depreciation.

DEPRECIATION

Depreciation is generally computed using straight-line methods over an estimated useful life ranging from three years to ten years (computer hardware, software and accessories – 5 years, software development costs – 5 years, furniture and fixtures – 7 years, leasehold improvements – 10 years, vehicles – 3 years). No depreciation is recorded for assets classified in "Work in Process" (Note 3). Depreciation expense is offset by amortization of Deferred Income related to fixed assets the Company purchased and placed in service in 1997 through 1999 that were pre-funded by NEPOOL participants.

INCOME TAXES

Income taxes are not provided by the Company because it is operating as a corporation described in Section 501(c)(4) of the Internal Revenue Code, exempt under Section 501(a) of the Internal Revenue Code, and has no unrelated business tax.

WORKING CAPITAL ADVANCES

The Company billed and collected its estimated working capital needs based on a rolling three month average of the charges under the ISO Tariff, and trued up this amount on a monthly basis. In June 2001, the Company utilized proceeds from its revolving credit agreement to fund its estimated working capital needs on a monthly basis and refunded previously advanced amounts to Participants.

DEFERRED CHARGES

The Company applies the provisions of Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation" (FAS 71), which requires regulated entities, in appropriate circumstances, to establish regulatory assets or liabilities, and thereby defer the income statement impact of certain charges or revenues because they are expected to be collected or refunded through future customer billings. During 2001, the Company determined that certain Congestion Management System and Multi-Settlement System costs totaling approximately $3,300,000 that had been previously capitalized as part of work in process no longer had future value and were thus impaired. The cost of this impairment was not expensed since it will be recovered through future ISO Tariff rates and, in accordance with FAS 71, are now classified as Deferred Charges.

OTHER ASSETS

The NEPOOL Participants are required to comply with the NEPOOL Financial Assurance Policy. In the case of non-investment grade rated Participants that meet certain criteria, the NEPOOL Financial Assurance Policy requires these Participants to put in place alternate forms of financial assurance. There are several options allowed under the NEPOOL Financial Assurance Policy for compliance, one of which is to post cash as collateral. At December 31, 2001 and 2000 the balance of these deposits was approximately $38,900,000 and $4,800,000, respectively.

Certain Participants that do not meet the credit ratings criteria of the Financial Assurance Policy and have not provided an alternate form of financial assurance, can prepay an estimate of their monthly bill on a weekly basis or will be subject to default procedures to remove them from NEPOOL.

DAILY BILLING ADVANCE COLLECTIONS

During 2001, the ISO, NEPOOL, and certain Participants have entered into a Standstill Agreement. The Standstill Agreement requires the ISO to issue an invoice daily to the affected Participants, who are required to pay the invoice on a daily basis, which represents the amount of estimated charges they have incurred for each day. The amounts collected in advance are then trued-up at the end of each month through the normal settlement billing process. In addition to daily billing, certain Participants who do not meet the credit ratings criteria of the Financial Assurance Policy, and who have not provided an alternate form of financial assurance, may prepay an estimate of their monthly bill on a weekly basis.

REVENUE RECOGNITION

The Company recovers its operating costs pursuant to the Tariff for Transmission Dispatch and Power Administration Services (ISO Tariff). The tariff provides for recovery of expenses through three schedules. Scheduling, System Control and Dispatch Service (Schedule 1) and Energy Administration Service (Schedule 2) recover related operating costs through a pre-approved rate applied to each month's activity. Reliability Administration Service (Schedule 3) recovered actual operating costs through June 30, 2001 through an allocation to Participants. Beginning July 1, 2001 these costs were recovered through a pre-approved rate applied to each month's activity. Schedules 1, 2, and 3 are subject to true-up through subsequent year's rates. The tariff may be redesigned for future years.

DEFERRED INCOME

Deferred income offsets the net fixed assets of the Company that were purchased and placed in service in 1997 and 1998, and the amount of the ISO Tariff for Schedules 1, 2, and 3 that was over/under collected from 1999 through 2001. The pre-funded fixed asset deferred income is being amortized into income over the life of the assets at the rate depreciation is recognized. The over/under collection amount of the ISO Tariff will be returned to the Participants through the mechanism provided for within the ISO Tariff.

FAIR VALUES OF FINANCIAL INSTRUMENTS

The carrying amounts reported in the statement of financial position for current assets and liabilities approximate their fair values.

USE OF ESTIMATES

Generally accepted accounting principles require management to make estimates and assumptions that affect assets and liabilities, contingent assets and liabilities, and revenues and expenses. Actual results could differ from those estimates.

LIQUIDITY INFORMATION

In order to provide information about liquidity, assets have been sequenced according to their nearness to conversion to cash, and liabilities have been sequenced according to the nearness of their resulting use of cash.

2. Commitments and Contingencies:

FUNDING ARRANGEMENTS

The Company has incurred major expenses on behalf of NEPOOL relating to the development of NEPOOL's wholesale electric market for New England and the formation of the Company (implementation costs). Additional costs were incurred by NEPOOL itself. The final project costs were $50,567,000, exclusive of interest.

In accordance with the fortieth amendment to the NEPOOL Agreement, ISO New England has begun administering repayment of these costs by the current NEPOOL membership to the members that originally funded the expenses. The repayment is to be made over a five-year period to the funding Participants at an interest rate of 8% per annum until August 18, 2001 and 10.78% per annum thereafter, beginning with the Second Effective date May 1, 1999 (the start of the wholesale electric markets in New England). The source of repayment was a monthly charge to NEPOOL Participants based on their pro rata share of ISO Schedule 2 costs which expired January 1, 2001.

Beginning January 1, 2001, the source of repayment for the remaining amounts is based fifty percent on Participants' pro rata share of electrical load and generating shares and fifty percent on Participants' pro rata share of electrical load and generating share peaks as defined in the Restated NEPOOL Agreement. At December 31, 2001 the amount of these costs to be repaid by the current NEPOOL membership to the members that originally funded the expenses was approximately $25,998,000.

ISO TARIFF DESIGN

The 2000 ISO Tariff was accepted for filing by order of the FERC issued December 30, 1999 in Docket No. ER00-395-000, subject to a compliance filing. That compliance filing was made subsequently and accepted by the FERC. The FERC also rejected rehearing requests made by certain parties to that proceeding. The Company successfully completed settlement proceedings before the FERC involving the Company's recovery of its administrative costs for 2001, in Docket No. ER01-316-000. The revised tariff is in effect until December 31, 2003.

LEGAL PROCEEDINGS

The Company is party to various legal actions incident to its business; however, management believes that no material awards against the Company will result from such proceedings.

In accordance with the revised NEPOOL Billing Policy, formal billing disputes of Participants are no longer held in escrow until the dispute is resolved. However, approximately $25,400,000 and $38,700,000 remained in dispute at December 31, 2001 and 2000, respectively.

3. Property and Equipment:

Property and equipment at December 31 consists of the following:

	2001	2000
Computer hardware, software and accessories	$14,215,000	$12,257,000
Software development costs	3,234,000	2,787,000
Furniture and fixtures	540,000	603,000
Leasehold improvements	2,081,000	1,287,000
Vehicles	75,000	-
	20,145,000	16,934,000
Work in process (including $1,148,000 and $72,000 of capitalized interest)	37,438,000	6,051,000
Less: accumulated depreciation and amortization	(6,955,000)	(3,394,000)
	$50,628,000	$19,591,000

Internal software development costs capitalized in 2001 and 2000 were $1,600,000 and $860,000, respectively. These costs will be amortized over five years.

4. Credit Facilities

REVOLVING CREDIT ARRANGEMENT

On June 8, 2001, the Company entered into a $15 million revolving credit arrangement, of which $5.5 million was outstanding at December 31, 2001. Proceeds from the revolving credit arrangement were used to pay back NEPOOL participants for working capital advances and to fund future working capital requirements. Interest accrues on the revolving credit at a London Inter-bank Offering Rate ("LIBOR") of which the Company has the option of selecting the 30, 60, 90, or 180 day rate, plus a 1% spread. Interest is paid at the earlier of the selected LIBOR term or 90 days. The arrangement expires June 4, 2004 and any outstanding balance must be paid by this date. The Company is charged a fee of 0.25% on the entire line of credit. The weighted average interest rate for the year ended December 31, 2001 was 4.02%.

TERM LOAN

On June 8, 2001, the Company also entered into a $43 million term loan. Proceeds from the term loan were used to pay back NEPOOL participants for capital expenditures advanced to the Company and to fund future capital expenditures. Interest accrues on the revolving credit at a London Inter-bank Offering Rate ("LIBOR") of which the Company has the option of selecting the 30, 60, 90, or 180 day rate, plus a 1.375% spread. Interest is paid at the earlier of the selected LIBOR term or 90 days. The weighted average interest rate for the year ended December 31, 2001 was 4.98%.

Principal payments on the term loan are due annually as follows:

2002	$ -
2003	7,176,000
2004	14,333,000
2005	14,333,000
2006	7,176,000
	$ 43,000,000

These credit agreements also contain both affirmative and negative covenants, the most restrictive of which is the maintenance of a financial ratio related to revenue and expense plus debt service. The Company was in compliance with these ratios at December 31, 2001.

Interest incurred on the revolving credit and the term loan for the year ended December 31, 2001 was approximately $1,180,000. Interest capitalized from the term loan for the year ended December 31, 2001 was approximately $686,000.

In February 2002, the Company borrowed an additional $40 million to fund additional capital expenditures.

5. Pension and Other Employee Benefits:

The Company sponsors defined benefit pension and postretirement plans which cover substantially all union and nonunion employees and provide retirement income, medical, dental and life insurance benefits. The Company sponsors two defined benefit pension plans which are funded solely by Company contributions. Benefits are determined based on years of service and average compensation. The Company sponsors two defined benefit postretirement plans which provide medical, dental and life insurance benefits for union and nonunion eligible employees and their beneficiaries. The medical benefits are contributory with participants' contributions adjusted annually and participants are responsible for deductible and coinsurance amounts. Dental benefits are non-contributory but participants are responsible for deductible and coinsurance amounts. The life insurance benefits are noncontributory. The Company's future liability for medical benefits is limited to 200% of 1993 costs and as a result the impact of a one-percentage-point change in assumed health care cost trend is immaterial.

	Pension Benefits Years ended December 31,		Other Postretirement Benefits Years ended December 31,	
	2001	2000	2001	2000
Change in benefit obligation:				
Benefit obligation at beginning of year	$21,226,000	$16,386,000	$ 1,887,000	$1,520,000
Service cost	1,483,000	1,130,000	187,000	167,000
Interest cost	1,438,000	1,328,000	106,000	115,000
Plan Amendments	41,000	-	-	-
Benefits paid	(281,000)	(250,000)	(15,000)	(7,000)
Actuarial (gain) loss	(231,000)	2,632,000	(334,000)	92,000
Benefit obligation at end of year	23,676,000	21,226,000	1,831,000	1,887,000
Change in plan assets:				
Fair value of plan assets at beginning of year	16,887000	15,795,000	-	-
Actual return on plan assets	(631,000)	(103,000)	-	-
Employer contributions	1,448,000	1,445,000	15,000	7,000*
Benefits paid	(281,000)	(250,000)	(15,000)	(7,000)
Fair value of plan assets at end of year	17,423,000	16,887,000	-	-
Funded status	(6,253,000)	(4,340,000)	(1,831,000)	(1,887,000)
Unrecognized transition obligation	1,562,000	1,687,000	865,000	920,000
Unrecognized net actuarial (gain) loss	4,650,000	2,660,000	(403,000)	(91,000)
Unrecognized prior service cost	41,000	-	-	-
Prepaid (accrued) benefit cost	$ -	$ 7,000	$($1,369,000)	$($1,058,000)

**Cash contributions made by employer to providers, insurers, trusts or participants for payment of claims.*

	Pension Benefits Years ended December 31,		Other Postretirement Benefits Years ended December 31,	
	2001`	2000	2001	2000
Weighted-average assumptions:				
Discount rate	7.00%	7.25%	7.00%	7.25%
Expected return on plan assets	8.50%	9.25%	n/a	n/a
Rate of compensation increase	4.50%	4.50%	4.50%	4.50%

For measurement purposes, the assumed increase in per capita cost of dental benefits is 4.00% for 2001 and level thereafter. The medical trend rate no longer applies as the Company's commitment to cost sharing has reached caps.

	Pension Benefits Years ended December 31,		Other Postretirement Benefits Years ended December 31,	
	2001	2000	2001	2000
Components of net periodic benefit cost:				
Service cost	$1,483,000	$1,130,000	$187,000	$167,000
Interest cost	1,438,000	1,328,000	106,000	114,000
Expected return on plan assets	(1,575,000)	(1,507,000)	-	-
Amortization of transition obligation	125,000	125,000	56,000	56,000
Amortization of net actuarial loss	(16,000)	(25,000)	-	-
Amortization of unrecognized (gain)/loss	-	-	(22,000)	(5,000)
Net periodic benefit cost	$1,455,000	$1,051,000	$327,000	$332,000

6. Employee Retirement Annuity Payments:

Under a Separation Agreement entered into between Northeast Utilities Service Company ("NUSCO") and the Company, the Company agreed to honor a postretirement annuity contract entered into with a former key employee. The Company recognizes expense as payments are made which amounted to $10,000 and $30,000 in 2001 and 2000, respectively.

7. 401(k) Savings Plan:

The Company has a 401(k) Retirement and Savings Plan open to substantially all employees. This savings plan provides for employee contributions up to specified limits. The Company matches employee contributions up to 3% of eligible compensation and provides a 50% match on the next 2% of eligible compensation. The matching contributions for the Company were $746,000 and $467,000 for 2001 and 2000, respectively.

8. Leases:

The following is a schedule by year of future minimum rental payments for all non-cancelable leases with terms greater than one year:

2002	$ 2,092,000
2003	2,092,000
2004	2,092,000
2005	2,092,000
Total minimum lease payments	$ 8,368,000

The Company leases under a sublease from NEPOOL one of its buildings and various furniture and equipment with terms of up to 15 years and renewable options for additional periods. The sublease terminates on the earlier of the termination of the Interim ISO Agreement (5 years), termination of the NEPOOL Agreement, or under the terms and conditions contained in the underlying master lease. The Company is currently negotiating to extend the Interim ISO Agreement.

The Company currently houses its back-up facilities at Northeast Utilities for a minimum annual payment. The Company is negotiating for additional space at the same facility. The Company will exercise the automatic month-to-month renewal option on the current lease until the new lease is finalized.

Additionally, the Company leases office space in one other building. The additional office space is leased with an initial term of six years with an automatic month to month renewal option. The Company follows the provisions of Statement of Financial Accounting Standards No. 13, Accounting for Leases, in determining the criteria for capital leases. Leases that do not meet such criteria are classified as operating leases, and related rentals are charged to expense in the year incurred. For fiscal years 2001 and 2000, minimum rental payments for operating leases were $1,753,157 and $1,774,245, respectively.

As part of a separation agreement with NUSCO, the Company has agreed to reimburse NUSCO for all charges related to providing service to NEPOOL. This includes charges for leased equipment used at the Control Center. These leases covered approximately $5,600,000 in assets in both 2001 and 2000. The average monthly payment was approximately $99,000 and $106,000 for the years 2001 and 2000, respectively.

9. Expiration of ISO Interim Agreement

The Company currently operates under a five-year interim ISO Agreement with NEPOOL which expires June 30, 2002. The Company is currently negotiating with NEPOOL to extend this agreement beyond June 30, 2002. This extension would be subject to FERC approval.

ISO NEW ENGLAND CORPORATE OFFICERS

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President and Chief Executive Officer

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Senior Vice President and Chief Operating Officer

Kathleen A. Carrigan
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Vice President and Chief Financial Officer

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Vice President and Chief Information Officer

Kevin A. Kirby
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*Names and titles as of January 31, 2001