

ISO New England Inc.

Financial Statements

For the Years Ended December 31, 2006 and 2005

ISO New England Inc.
Index
December 21, 2006 and 2005

	Page(s)
Independent Auditors' Report	1
Financial Statements	
Statements of Financial Position	2
Statements of Activities	3
Statements of Cash Flows	4
Notes to Financial Statements	5– 15



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Independent Auditors' Report

Board of Directors and
Members of ISO New England Inc.:

We have audited the Statements of Financial Position of ISO New England Inc. (the Company) as of December 31, 2006, and the related Statements of Activities and Cash Flows for the year then ended. 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 audit. The accompanying financial statements of the Company as of and for the year ended December 31, 2005 were audited by other auditors whose report thereon, dated March 16, 2006, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally acceptable in the United States of America. 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 includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2006 financial statement referred to above present fairly, in all material respects, the financial position of ISO New England Inc. as of December 31, 2006, and the results of its operations and cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

KPMG LLP

March 15, 2007

ISO New England Inc.
Statements of Financial Position
For Years Ended December 31, 2006 and 2005

	2006	2005
	(In thousands)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 6,705	\$ 138,927
Security deposits	194,474	144,281
Unbilled receivable, net	18,488	21,486
Prepaid expenses	895	636
Restricted cash on deposit	26,416	91,699
Noncurrent assets:		
Property and equipment in-service, net (Note 3)	76,193	33,088
Work in process (Note 3)	17,491	45,586
Deferred charges (Note 1)	151	297
Swap asset (Note 4)	-	53
Regulatory asset (Note 1)	1,309	1,956
	<hr/>	<hr/>
Total assets	\$ 342,122	\$ 478,009
	<hr/>	<hr/>
Liabilities and Net Assets		
Current liabilities:		
Accounts payable:		
Settlement, net	\$ 2,999	\$ 133,114
Administration	10,827	9,335
Deposits payable	196,177	145,134
Interest payable	1,143	1,081
Revolving credit (Note 4)	7,182	1,968
Accrued compensation	9,813	9,022
Minimum pension liability (Note 5)		1,956
Regulatory liability (Note 1)	-	53
Deferred income - current	5,305	4,547
Restricted cash on deposit payable	21,553	67,176
Term loan payable-current (Note 4)	3,988	13,833
Long-term liabilities:		
Deferred income, net of current portion	-	3,667
Term loan, net of current portion (Note 4)	83,135	87,123
	<hr/>	<hr/>
Total liabilities	342,122	478,009
Unrestricted net assets	<hr/>	<hr/>
	-	-
	<hr/>	<hr/>
Total liabilities and net assets	\$ 342,122	\$ 478,009
	<hr/>	<hr/>

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

ISO New England Inc.
Statements of Activities
For Years Ended December 31, 2006 and 2005

	2006	2005
	(In thousands)	
Changes in unrestricted net assets:		
Revenues (Note 1):		
ISO tariff revenues	\$ 112,485	\$ 122,327
Interest income	2,231	1,567
Fees and services	222	527
	<hr/>	<hr/>
Total unrestricted revenues	114,938	124,421
	<hr/>	<hr/>
Expenses:		
General and administrative:		
Salaries and benefits	54,057	50,947
Professional and consultants	14,660	17,400
Rents and leases	1,071	1,077
Computer services	4,379	4,064
Depreciation and amortization expense	24,012	38,921
Loss on impaired asset (Note 3)	3,530	-
Communication expense	1,693	1,578
Insurance expense	1,759	1,785
NPCC Dues	1,427	1,399
Interest expense	3,029	2,458
Other	5,321	4,792
	<hr/>	<hr/>
Total expenses	114,938	124,421
	<hr/>	<hr/>
Change in unrestricted net assets		
Unrestricted net assets, beginning of year	-	-
	<hr/>	<hr/>
Unrestricted net assets, end of year	\$ -	\$ -
	<hr/>	<hr/>

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

ISO New England Inc.
Statements of Cash Flows
For Years Ended December 31, 2006 and 2005

	2006	2005
	(In thousands)	
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 expense	24,012	38,917
Loss on impaired asset	3,530	-
Decrease/(increase) in accounts receivable	2,998	(339)
(Increase) in prepaid expense	(259)	(30)
Decrease/(increase) in regulatory asset	647	(452)
Decrease in swap asset	53	103
(Decrease)/increase in accounts payable:		
Settlement	(130,115)	106,963
Administration	1,000	(13)
(Decrease)/increase in minimum pension liability	(1,956)	452
(Decrease) regulatory liability	(53)	(103)
Increase in accrued compensation	791	1,240
Increase in interest payable	62	194
(Decrease) in deferred income	(2,909)	(8,138)
Net cash (used in)/provided by operating activities	<u>(102,199)</u>	<u>138,794</u>
Cash flows from investing activities:		
Capital expenditures	<u>(41,914)</u>	<u>(41,223)</u>
Net cash used in investing activities	<u>(41,914)</u>	<u>(41,223)</u>
Cash flows from financing activities:		
(Increase) in security deposits	(50,193)	(76,638)
Decrease/(increase) in restricted cash on deposit	65,283	(73,925)
(Decrease)/increase in restricted cash on deposit payable	(45,623)	49,402
Increase in deposits payable	51,043	76,885
Repayment on term loan	(13,833)	(22,398)
Proceeds from tax-exempt bond financing	-	45,500
Net borrowings on working capital line	<u>5,214</u>	<u>1,968</u>
Net cash provided by financing activities	<u>11,891</u>	<u>794</u>
Net (decrease)/increase in cash and cash equivalents	(132,222)	98,365
Cash and cash equivalents, beginning of year	<u>138,927</u>	<u>40,562</u>
Cash and cash equivalents, end of year	<u>\$ 6,705</u>	<u>\$ 138,927</u>
Supplemental data:		
Aniounts included in Accounts Payable - Administration related to work in process	<u>\$ 5,567</u>	<u>\$ 5,075</u>
Cash paid during the year for interest, net of interest capitalized	<u>\$ 3,612</u>	<u>\$ 2,731</u>

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

ISO New England Inc.

Notes to Financial Statements

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 market place opened in the ISO New England Inc. control area. During the period from July 1997 through January 31, 2005, the Company was operating under the Interim ISO Agreement and administered NEPOOL's tariff.

On February 1, 2005, the ISO became the Regional Transmission Organization ("RTO") for New England, with enhanced responsibilities as the transmission provider for New England and new governing documents (Transmission Operating Agreement, Participants Agreement, Market Participants Service Agreement, ISO New England Transmission, Markets and Services Tariff) in place of the existing governing documents (the Interim ISO Agreement, NEPOOL Tariff).

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, 2006 and 2005 were held in overnight repurchase agreements and also in direct and indirect obligations of the United States, with maturities of three months or less.

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 week and provides an invoice or remittance advice to each Participant that summarizes the amount either receivable from or payable to each Participant.

Accounts payable on the balance sheet are segregated between the amounts owed for energy transactions and transmission, for which the ISO functions as paying agent, which are included in accounts payable settlement, net and for the administrative expenses incurred by the Company in the course of operations. The reference to "settlement, net" is used due to the nature of billing and payment for the amounts owed for energy transactions and transmission markets, which represents the customer's net amount due, less any amounts which may have been owed to them.

The net unbilled receivables, which have been determined as a result of the settlement process, include those amounts that will be billed and included in the invoice or remittance advice to Participants in the next weekly invoice issued. The net payables and receivables for those energy transactions stated above are settled with the Participants in the subsequent week.

Restricted Cash on Deposit

The balance of \$26,400,000 and \$91,700,000 at December 31, 2006 and 2005, respectively, recorded as Restricted Cash on Deposit represents the Congestion Revenue Fund and Net proceeds from tax-exempt bond financing. The balance is offset by liabilities on the Statements of Financial Position. The restricted cash on deposit at December 31, 2006 and 2005 were held in overnight repurchase agreements and also in direct and indirect obligations of the United States. Additionally, the net proceeds from the tax-exempt bond financing are held at cost. The fair market value as of December 31, 2006 and 2005 was \$26,400,000 and \$91,700,000, respectively.

ISO New England Inc.

Notes to Financial Statements

Property and Equipment in Service and Work in Process

Property and equipment is stated at cost, net of accumulated depreciation.

The Company applies the provisions of Statement of Financial Accounting Standards No. 34, "Capitalization of Interest Costs" ("FAS 34") and Statement of Financial Accounting Standards No. 62, "Capitalization of Interest Costs in situations involving certain tax-exempt borrowings and certain gifts and grants" ("FAS 62"), an amendment of FASB Statement No. 34", which requires the Company to capitalize the interest and fees associated with the borrowings that the Company has entered into for the acquisition of assets related to a project that has a material effect on the Company's financial position.

In addition, the Company follows the provisions of the Statement of Position 98-1, "Accounting for the Costs of Computer Service Software Development" ("SOP 98-1") in capitalizing internal software development costs.

Depreciation

Depreciation is generally computed using straight-line methods over an estimated useful life ranging from three years to twenty-five years (computer hardware, software and accessories – 3 to 5 years, software development costs – 3 to 5 years, furniture and fixtures and machinery and equipment – 7 years, building and leasehold/building improvements – 10 years or remaining life of the lease, vehicles – 3 years; building – 25 years). Capitalized interest and fees is amortized over the same useful life of the asset that it pertains to. No depreciation is recorded for assets classified as work in process until the assets are placed into service (Note 3).

Derivative Policy

The Company follows the provisions of Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("FAS 133"), as amended by FAS 138, in establishing its derivative policy. The policy states that the Company's Management will make the determination with the approval of the Company's Audit and Finance Committee to enter into fixed interest rate swaps when the fixed interest rate offered at the time will outweigh the risk of leaving the borrowings to fluctuations in the market, taking into consideration the length of the borrowing, the state of the economy and the direction in which the Management team believes the economy is moving.

Deferred Charges and Regulatory Assets and Liabilities

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 it is probable to be collected or refunded through future customer billings. The Company incurred pension cost and the purchase of land located at Sullivan Road, which were not included in the 2003 and 2004 ISO Tariff rates, respectively. A portion of these costs, which were deferred, have been included in the current year's ISO Tariff filing and therefore amortized. The remaining cost, also deferred, will be collected in future tariff filings.

ISO New England Inc.

Notes to Financial Statements

The following table is a detail of the deferred charges, regulatory assets and regulatory liability balances as presented in the Statements of Financial Position:

Deferred Charges	2006	2005
ITS Pilot Program	\$ -	\$ 4,000
Pension costs	-	142,000
Land located on Sullivan Road	151,000	151,000
	<u>\$ 151,000</u>	<u>\$ 297,000</u>

Regulatory Assets	2006	2005
Projected 2006 over collection true-up	\$1,309,000	\$ -
Minimum pension liability	-	1,956,000
	<u>\$ 1,309,000</u>	<u>\$ 1,956,000</u>

Regulatory Liability	2006	2005
Swap asset	\$ -	\$ 53,000
	<u>\$ -</u>	<u>\$ 53,000</u>

Income Taxes

The Company is an entity organized as a non-stock corporation under the General Corporation Law, as amended, of the State of Delaware. In a letter dated November 10, 2004 (the "Determination Letter"), the Internal Revenue Service (the "IRS") determined (i) that the Company is generally exempt from Federal income tax under Internal Revenue Code ("IRC") Section 501(c)(3), and (ii) that contributions to the Company are deductible under IRC Section 170. The Company is in its advance ruling period with respect to its status as a private foundation or a public charity. The Company's advance ruling period ends on December 31, 2008. In the IRS Determination Letter, the IRS stated that during the advance ruling period, the Company will be treated as a public charity, and not as a private foundation. The Company must submit IRS Form 8734 to the IRS by March 31, 2009, so that the IRS can determine whether the Company has met the requirements of the applicable public charity support test during its advance ruling period. If the Company does not meet the public support requirements, the IRS will classify the Company as a private foundation for future tax periods.

Security Deposits

The NEPOOL Participants are required to comply with the Financial Assurance Policy under ISO's Transmission, Markets & Services Tariff. In the case of non-investment grade rated Participants that meet certain criteria, the Company's Financial Assurance Policy requires these Participants to put in place alternate forms of financial assurance. There are several options allowed under the Company's Financial Assurance Policy for compliance, one of which is to post cash as collateral. The cash collateral deposits at December 31, 2006 and 2005 were approximately \$194,474,000 and \$144,281,000, respectively, and are recorded in deposits payable.

Revenue Recognition

The Company recovers its operating and debt service costs pursuant to the ISO's Transmission, Markets & Services Tariff, which provides for recovery of expenses through three schedules. Scheduling, System Control and Dispatch Service (Schedule 1), Energy Administration Service (Schedule 2) and Reliability Administration Service (Schedule 3) recover related costs through a pre-approved rate applied to each month's activity. Schedules 1, 2, and 3 are subject to true-up through subsequent years' rates, and any over or under collection is recorded as deferred charges or deferred income and will be recovered under future Tariff filings.

ISO New England Inc.

Notes to Financial Statements

Deferred Income

Deferred income represents the amount of the ISO Tariff for Schedules 1, 2, and 3 that was over/under collected from 2004 through 2006 and offsets to the net fixed assets of the Company that were purchased and placed in service in 1997 and 1998. The over/under collection amount of the ISO Tariff will be returned to the Participants through the true-up mechanism provided for within the ISO Tariff. The pre-funded fixed asset deferred income is being amortized to income over the life of the assets at the rate depreciation is recognized. The amortization of these assets was complete at December 31, 2005.

Concentrations

The Company's top 10 participants represented approximately 52% or \$55,900,000 and 54% or \$61,800,000 in tariff revenues for the years ended 2006 and 2005, respectively.

Fair Values of Financial Instruments

The carrying amounts reported in the Statements of Financial Position for 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.

ISO New England Inc.

Notes to Financial Statements

2. Commitments and Contingencies

Capital Funding Tariff

The FERC accepted ISO's "capital funding tariff" ("CFT") filing for 2006 and 2005. These filings support the ISO's loan arrangements with various banks and note holders to fund the capital and working capital requirements of the Company.

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.

3. Property and Equipment In-Service, net and Work in Process

	December 31,	
	2006	2005
Computer hardware, software and accessories	\$ 139,342,000	\$ 108,692,000
Software development costs	30,354,000	24,938,000
Furniture and fixtures	2,002,000	888,000
Machinery and equipment	59,000	59,000
Building and leasehold/building improvements	32,218,000	4,101,000
Capitalized interest and fees	6,000,000	4,325,000
Vehicles	10,000	85,000
	<u>209,985,000</u>	<u>143,088,000</u>
Less: accumulated depreciation and amortization	<u>(133,792,000)</u>	<u>(110,000,000)</u>
Property and equipment in-service, net	<u>\$76,193,000</u>	<u>\$ 33,088,000</u>
Work in process (WIP)	<u>\$ 17,491,000</u>	<u>\$ 45,586,000</u>

Cost represented in WIP includes phase II of the building construction at the Main Control Center which began in 2005 and a number of new projects which began in 2006 such as Forward Capacity Market, Information Retrieval, Oracle 10G Upgrade, EMS Upgrade and various other market enhancement projects that have not been placed in service as of December 31, 2006. In accordance with "FAS 34" and "FAS 62", the associated interest cost, which was capitalized as work in process at December 31, 2006 and 2005 was \$178,000 and \$949,000, respectively. Of the capitalized interest included in WIP for 2006, \$13,000 has been carried over from 2005 and \$10,000 represents the net of interest income and interest expense earned or paid, on the building construction, which has been recorded in its entirety on the Statements of Financial Position.

In 2006, the Company reached a settlement agreement with FERC and the Participants in NEPOOL to abandon Locational Installed Capacity Market ("LICAP") in place of a Forward Capacity Market. The result of this settlement necessitated the Company's disposal of assets related to LICAP. This asset disposal resulted in a loss of \$3,530,000 in 2006, and is reflected in "loss of impaired asset" on the accompanying Statements of Activities.

ISO New England Inc.

Notes to Financial Statements

4. Credit Facilities

Revolving Credit Arrangement

In June 2004, the Company entered into a \$15,000,000 revolving credit arrangement, of which the outstanding balances at December 31, 2006 and 2005 were \$7,182,000 and \$1,968,000, respectively. 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 .60% spread. Interest is paid at the earlier of the selected LIBOR term or 30 days. The arrangement expires July 1, 2009 and any outstanding balance must be paid by this date. The Company is charged an annual fee of .15% on the entire line of credit. For the years ended December 31, 2006 and 2005, the weighted average interest rate is approximately 5.83% and 4.50% respectively.

In June 2004, the Company also entered into a \$4,000,000 revolving credit arrangement, which was requested as a result of the change in the billing policy under ISO's Transmission, Markets & Services Tariff to go from monthly billing to weekly billing. The outstanding balance at December 31, 2006 and 2005 was \$0 for both years. This arrangement serves as a line of credit to cover any potential payment defaults by a Participant. 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 .60% spread. Interest is paid at the earlier of the selected LIBOR term or 30 days. The arrangement expires July 1, 2009 and any unpaid balances must be paid as of this date. The Company is charged an annual fee of .15% on the entire line of credit. For the year ended December 31, 2006 the weighted average interest rate is approximately 8.25%. There were no borrowings for the year ended December 31, 2005.

Term Loan

The Company entered into a \$20,000,000 term loan in 2003. Principal is payable monthly with the final repayment due in January 2007. Interest accrues on the \$20,000,000 term loan at LIBOR of which the Company has the option of selecting the 30, 60, 90, or 180-day rate, plus a 1.375% spread. The Company entered into a \$43,000,000 term loan in 2001 and a \$24,500,000 term loan in 2003, of which both have been paid off as of December 31, 2006. For the years ended December 31, 2006 and 2005, the weighted average floating interest rate is approximately 4.44% and 3.85%, respectively.

The Company has entered into interest rate exchange agreements (Swaps) to mitigate the interest rate risks associated with its floating-rate term loans. On March 17, 2003, the Company entered into three interest rate exchange agreements, two of which were terminated in 2004, whereby the Company pays at a fixed interest rate for predetermined notional amounts as scheduled at the time of execution of the agreements. On June 1, 2006 the last interest rate Swap ended as a result of the Company paying off the related term loan.

	Swap
Notional Amount at time of execution	\$43,000,000
Notional Amount at December 31, 2006	\$0
Termination Date	June 1, 2006
Rate Paid	3.3750%
Rate Received	LIBOR plus 1.375%

The fair market value of the interest rate swap as of December 31, 2006 and 2005 was \$0 and \$53,000, respectively. The fair market values are derived from proprietary models. The offset is recorded as a liability on the Statements of Financial Position.

ISO New England Inc.

Notes to Financial Statements

Private Placement Debt Arrangement

In September 2004, the Company entered into a \$39,000,000 private placement loan, which is made up of ten year 5.60% senior notes. Payment is due in full on September 2, 2014 with no mandatory prepayments. This loan is included in term loan on the Statements of Financial Position.

Tax-Exempt Bond Financing

In February of 2005, the Company entered into tax exempt financing of \$45,500,000 in the form of Multi-Mode Variable Rate Civic Facility Revenue Bonds, which were issued by the Massachusetts Development Finance Agency. The proceeds of the Bonds were loaned to the Company, to assist in financing and refinancing a project located at the Main Control Center. Principal payments are scheduled to begin May 2007 with the final repayment due on February 1, 2032. Interest accrues on the \$45,500,000 tax exempt bonds, at a weekly variable rate based upon the Bond Market Association "BMA" Swap Index plus an average spread of 2 basis points. For the years ended December 31, 2006 and 2005, the weighted average floating interest rate is approximately 3.46% and 2.59%, respectively.

The total outstanding debt at December 31, 2006 and 2005 was \$87,100,000 and \$101,000,000, respectively. Principal payments on the term loan, private placement debt, and tax-exempt bonds are due annually as follows:

2007	\$ 3,988,000
2008	1,820,000
2009	1,820,000
2010	1,820,000
2011	1,820,000
Thereafter	<u>75,855,000</u>
	<u>\$ 87,123,000</u>

These credit agreements 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, 2006 and 2005.

Interest incurred on the revolving credit, the term loans, private placement debt, and tax-exempt bonds for the years ended December 31, 2006 and 2005 was approximately \$3,834,000 and \$3,252,000, respectively. Interest capitalized from the term loans and private placement debt for the years ended December 31, 2006 and 2005 was approximately \$805,000 and \$794,000, respectively.

ISO New England Inc.
Notes to Financial Statements

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 measurement date used to determine pension and other postretirement benefit obligations for the pension plans and the postretirement benefit plan is December 31.

The following table sets forth the plans' benefit obligations, fair value of the plans' assets, and the plans' funded status:

	Pension Benefits		Other Postretirement Benefits	
	Years Ended December 31,		Years Ended December 31,	
	2006	2005	2006	2005
Change in benefit obligation:				
Benefit obligation at beginning of year	\$47,544,000	\$40,336,000	\$3,985,000	\$3,337,000
Service cost	3,329,000	2,910,000	577,000	498,000
Interest cost	2,618,000	2,338,000	226,000	186,000
Benefits paid	(923,000)	(696,000)	(144,000)	(73,000)
Plan participants' contributions			19,000	8,000
Actuarial (gain) loss	(565,000)	2,656,000	434,000	29,000
Benefit obligation at end of year	52,003,000	47,544,000	5,097,000	3,985,000
Change in plan assets:				
Fair value of plan assets at beginning of year	35,247,000	29,847,000	4,075,000	3,359,000
Actual return on plan assets	4,675,000	2,680,000	551,000	313,000
Employer contributions	3,764,000	3,416,000	565,000	468,000
Plan participants' contributions			19,000	8,000
Benefits paid	(923,000)	(696,000)	(144,000)	(73,000)
Fair value of plan assets at end of year	42,763,000	35,247,000	5,066,000	4,075,000
Funded status	(9,241,000)	(12,297,000)	(32,000)	90,000
Unrecognized transition obligation	937,000	1,062,000	586,000	642,000
Unrecognized net actuarial (gain) loss	8,275,000	11,204,000	(638,000)	(865,000)
Unrecognized prior service cost	29,000	31,000	84,000	133,000
Prepaid (accrued) benefit cost	\$	\$	\$	\$

ISO New England Inc.
Notes to Financial Statements

Amounts recognized in the Statements of Financial Position consist of:

	Pension Benefits		Other Benefits	
	12/31/2006	12/31/2005	12/31/2006	12/31/2005
(Accrued) benefit cost	\$	\$(1,956,000)		
Regulatory Assets	-	1,956,000	-	-
Net amount recognized	-		-	-

The accumulated benefit obligation for all defined benefit pension plans was:

	December 31,	
	2006	2005
Projected benefit obligation	\$52,003,000	\$47,544,000
Accumulated benefit obligation	\$41,271,000	\$37,210,000
Fair value of plan assets	\$42,763,000	\$35,247,000

The Company was required to record an additional minimum pension liability for the year ended December 31, 2005 of \$1,956,000 since the accumulated benefit obligation exceeded the fair value of the plan assets at that date. The Company determined that the minimum pension liability was probable of recovery through the ISO Tariff and recorded a regulatory asset in that amount as of December 31, 2005.

As of December 31, 2006, since the fair value of the plan assets exceeded the accumulated benefit obligation no minimum pension liability is required. As a result, the Company recognized a reduction in both the minimum pension liability and the related regulatory asset.

The Company has not yet adopted the provision of Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans ("FASB 158"). FASB 158 requires the booking of an asset, if the plan is over funded or a liability, if the plan is under funded, rather than disclosing the funded status in a note to the financial statements. The amount recorded is the difference between the fair value of plan assets and the benefit obligation. FASB 158 is effective for the Company at the end of the fiscal year ending after June 15, 2007. The Company plans to adopt the provision for the year ended December 31, 2007.

	Pension Benefits		Other Postretirement Benefits	
	Years ended December 31,		Years ended December 31,	
	2006	2005	2006	2005
Components of net periodic benefit cost:				
Service cost	\$ 3,329,000	\$ 2,910,000	\$ 577,000	\$ 498,000
Interest cost	2,618,000	2,338,000	225,000	185,000
Expected return on plan assets	(2,756,000)	(2,347,000)	(320,000)	(265,000)
Amortization of transition obligation	125,000	125,000	56,000	56,000
Amortization of net actuarial loss	445,000	388,000	-	-
Amortization of unrecognized Prior Service Cost	2,000	2,000	51,000	51,000
Amortization of unrecognized (gain)/loss			(24,000)	(57,000)
Net periodic benefit cost	\$ 3,763,000	\$ 3,416,000	\$ 565,000	\$ 468,000

The primary economic assumptions used to value these liabilities are summarized in the following chart. These assumptions are selected as the measurement data based on prevailing economic conditions.

ISO New England Inc.

Notes to Financial Statements

Weighted-average assumptions used to determine net periodic benefit cost for the following years ended:

	Pension Benefits		Other Benefits	
	12/31/2006	12/31/2005	12/31/2006	12/31/2005
Discount rate	5.50%	5.75%	5.50%	5.75%
Expected long-term rate of return on plan assets	7.50%	7.50%	7.50%	7.50%
Rate of compensation increase	3.50%	3.50%	3.50%	3.50%
Health Care cost trend rates - initial			5.00%	7.00%
Health Care cost trend rates - ultimate			4.00%	4.00%
Ultimate year			2007	2007

Weighted-average assumptions used to determine benefit obligation for the following years ended:

	Pension Benefits		Other Benefits	
	12/31/2006	12/31/2005	12/31/2006	12/31/2005
Discount Rate	5.75%	5.50%	5.75%	5.50%
Rate of compensation increase	3.50%	3.50%	3.50%	3.50%

A one percentage point change in the assumed health care cost trend rates would increase the Accumulated Post Retirement Benefit (APBO) as of December 31, 2006 by approximately \$237,000 or decrease the APBO by approximately \$216,000. Additionally, a one percentage point change in the assumed health care cost trend rates would increase or decrease the net post retirement cost for 2006 by approximately \$47,000 and \$42,000, respectively.

ISO's pension plan and postretirement benefit plan weighted-average asset allocations and expected returns by asset category are as follows:

Pension and Postretirement Plan Assets	Target	Percentage of Plan		Weighted Average
	Allocation	Assets at December 31		
	2007	2006	2005	Rate of Return - 2007
Equity Securities	60%	60%	62%	5.20%
Debt Securities	40%	40%	38%	2.30%
Total	100%	100%	100%	7.50%

The forward-looking estimates of total return are generated through combined assessment of current valuation measures, income, economic growth and inflation forecasts, and historical risk premiums. The long-term bond forecast is derived from the expected long-term return of a portfolio of corporate, government and high yield debt instruments. The equity forecasts are based on the long-term real returns of a portfolio of US large cap, US small cap, international developed markets and emerging markets equity securities.

The Plan's investment portfolio is to be invested to provide benefits for qualified employees of ISO New England Inc. Investments are to be compatible with the liquidity requirements determined by the plan's actuary. An optimal target allocation of 60/40 between equities and fixed income investments is to be kept with an allowance of fifteen percent (15%) over/under deviation from the optimal allocation target.

The Company expects to contribute \$3,707,000 to its pension plan and \$732,000 to its postretirement benefit plan in 2007.

ISO New England Inc.

Notes to Financial Statements

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits	Other Benefits
2007	\$ 897,000	\$ 176,000
2008	1,004,000	190,000
2009	1,146,000	220,000
2010	1,329,000	305,000
2011	1,513,000	391,000
Years 2013-2016	11,767,000	3,346,000
Total	<u>\$17,656,000</u>	<u>\$4,628,000</u>

6. 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 \$1,427,000 and \$1,344,000 for 2006 and 2005, respectively.

7. Leases

The following is a schedule by year of future minimum rental payments for all noncancelable-operating leases:

2007	\$580,000
2008	<u>42,000</u>
Total minimum lease payments	<u>\$622,000</u>

The Company currently houses its back-up facilities at a separate location for a nominal annual payment.

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 ending on July 31, 2007.

For fiscal years 2006 and 2005, actual rental payments for operating leases were \$944,000 and \$958,000, respectively.