

To: FTR Credit Working Group

Date: May 15, 2008

Subject: FTRs and LTTRs – Bankruptcy Issues

The following outline has been prepared to facilitate a discussion of the bankruptcy issues concerning the trading in FTRs and LTTRs by Pool Participants.

1. The Bankruptcy Code (the “Code”) has been designed to permit futures-type contracts, whether traded on an exchange or not, to proceed unhampered by the filing of a bankruptcy by one of the parties thereto.
2. Over the years, modifications have been made to the Code to broaden the protections relating to these contracts. The intent is that any futures-type contract, and any non-debtor counterparty thereto who is in the business of dealing with such futures-type contract, be protected.
3. The key protections provided by the Code are that:
 - i. the non-debtor counterparty may terminate the contract upon a bankruptcy filing, if such termination is expressly permitted by the terms of the contract
 - ii. the automatic stay will not apply to prevent setoff or the enforcement by the non-debtor counterparty of its rights against any collateral that may be securing the debtor’s obligations under the contract
 - iii. a somewhat less important protection is that any setoffs that have occurred prior to bankruptcy will not be subject to attack as preferences
4. The applicable Code provisions require that there be a “forward contract,” and that the non-debtor counterparty be a “forward contract merchant.”
5. The term “forward contract” is very broadly defined, and, we believe, should include FTRs and LTTRs. (The definition is “a contract . . . for the purchase, sale, or transfer of a commodity . . . or any similar good, article, service, right or interest which is presently or in the future becomes the subject of dealing in the forward contract trade . . . with a maturity date more than two days after the date the contract is entered into, including but not limited to a . . . hedge transaction, deposit, loan, option, allocated transaction, unallocated transaction or any other similar agreement.”)
6. The term “forward contract merchant,” like the definition of “forward contract,” is intended to be broadly construed. It is “an entity the business of which consists in whole or in part of entering into

forward contracts as or with merchants in a commodity ... or any similar good, article, service, right, or interest which is presently or in the future becomes the subject of dealing in the forward contract trade.”

7. We believe the relevant contract is the MPSA and Tariff, and the contract parties are the purchaser of the FTR on the one hand and the Pool, or the ISO as representative for the Pool, on the other hand. The ISO functions like a clearinghouse to facilitate trades on behalf of the Pool and its participants, and therefore should be viewed as the “forward contract merchant.”

8. Clearly, the FTR and LTTR markets are not a perfect fit with the forward contracts concept. To strengthen the Pool’s argument that such agreements are forward contracts which can be terminated and liquidated, ISO-NE and the Pool should consider amending the governing documents to specify:

- (i) FTRs and LTTRs are forward contracts
- (ii) ISO-NE on behalf of the Pool is the forward contract merchant
- (iii) explicit termination and set-off provisions

9. We recommend that these revisions occur everywhere relevant, including the Financial Assurance Policy, the Billing Policy and Market Rule 1 provisions regarding FTRs and LTTRs.

10. The working group should report these recommendations back to the Budget and Finance Subcommittee and Markets Committee and ask the Committees to consider specific language for recommendation to the Participants Committee.