

NATIONAL BANKRUPTCY CONFERENCE

*A Voluntary Organization Composed of Persons Interested in the
Improvement of the Bankruptcy Code and Its Administration*

March 15, 2010

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ADMINISTRATIVE OFFICE

SHARI A. BEDKER

The Honorable John Conyers, Jr.
Committee on the Judiciary
United States House of Representatives
Washington, DC 20515

Re: Proposed Amendments to the Bankruptcy Code
Concerning Exemptions for Financial Contracts

Dear Mr. Chairman:

The National Bankruptcy Conference (the "Conference")¹ is writing to you to propose amendments to the Bankruptcy Code concerning the current exemptions in the Bankruptcy Code for financial contracts. As you may know, following amendments made to the Bankruptcy Code in 2005 and 2006, there has been a significant concern raised by bankruptcy professionals, academicians and others as to whether the current exemptions for financial contracts contained in the Bankruptcy Code are unnecessarily broad. The proposals made by the Conference in this letter would narrow the exemptions for the reasons explained below.

Some background may be helpful. By financial contracts we mean swap agreements, repurchase agreements, securities contracts, commodity contracts and futures contracts, all as defined in the Bankruptcy Code. Financial contracts are currently exempt from many of the provisions of the Bankruptcy Code that would govern ordinary commercial transactions. For example, a non-debtor would normally be barred by the automatic stay in a bankruptcy case from terminating a contract with the debtor based on the commencement of the debtor's bankruptcy case. A non-debtor party to a financial contract is not so barred. Usually a creditor in possession or control of collateral would be barred by the automatic stay in a bankruptcy case from enforcing its rights against the collateral to obtain payment of amounts owed to by it the debtor. A non-debtor party to a financial contract is not so barred. Typically also a creditor who receives a payment or collateral from the debtor on the eve of the commencement of the debtor's bankruptcy case would be vulnerable to the payment or collateral being returned to the debtor's bankruptcy estate as a preference. A non-debtor party to a financial contract is exempt from any preference risk.

¹ The Conference is a voluntary, non-profit, non-partisan, self-supporting organization of approximately sixty lawyers, law professors and bankruptcy judges who are leading scholars and practitioners in the field of bankruptcy law. For approximately 70 years, its primary purpose has been and is to advise Congress on the operation of bankruptcy and related laws and any proposed changes to those laws. A fact sheet describing the Conference and a list of its current members is enclosed.

The justification for these exemptions is based on a concern about systemic risk. Financial contracts are so much a part of the capital markets that the bankruptcy of a participant may, absent exemptions from the Bankruptcy Code, “freeze” contracts with the debtor from unwinding and produce a “daisy chain” effect of multiple defaults among market participants. The Conference does not question this justification. However, the Conference does question whether the exemptions are currently drafted so broadly that they would exempt from the Bankruptcy Code various non-financial-contract commercial transactions for which the normal rules of bankruptcy should govern, and thereby undermine the goals of the Bankruptcy Code aimed at a collective proceeding involving all creditors and equal treatment of all creditors similarly situated. Indeed, the Conference is concerned that the breadth of the current exemptions affords parties the opportunity voluntarily to structure ordinary commercial transactions, such as loans or supply agreements, as financial contracts in order to fall within the exemptions and avoid the normal rules of bankruptcy, even though the transactions pose no or little systemic risk.

The Conference in this letter is making three proposals. The first proposal is to confine collateral securing performance under financial contracts and benefiting from the exemptions to so-called “financial collateral”. The second proposal is to limit the defense relating to a settlement payment on a security so that the defense is not available to the beneficial holder of the security. The third proposal is to provide a separate scheme for forward and commodity contracts where the underlying commodity is actually used or sold in the ordinary course of the debtor’s business. Each of these proposals is discussed below.

I. Financial Collateral

The current exemptions contain no limitation on the types of collateral against which a non-debtor counterparty may exercise contractual rights with the benefit of the exemptions. Therefore, a non-debtor counterparty to a financial contract, such as a swap agreement, may exercise its secured party rights against the collateral posted for such agreement free from any bankruptcy stay, regardless of whether the collateral is cash or securities (as would be common for a swap agreement) or the debtor’s plants, equipment and other operating assets (which would be quite uncommon for a legitimate swap agreement). Indeed, the use of uncommon collateral in what is otherwise facially a protected financial contract may be a strong indicator that the transaction is, in fact, a secured loan or commercial arrangement that has been documented to appear to be a financial contract entitled to the exemptions.

The unfettered exercise of secured party rights against operating assets could end the debtor’s prospects for reorganization, and thus likely lead to the termination of its employees and the loss of going concern values to other creditors and stakeholders. Where collateral is cash, securities or other fungible financial assets, affording a non-debtor counterparty the right to realize on such collateral free from the automatic stay should not deprive the debtor of its reorganization prospects. In contrast, where the collateral is operating assets – which can often be unique or practically irreplaceable – not only does the type of collateral raise serious issues as to the bona fides of the transaction as a protected contract, but the loss of the automatic stay can be fatal to the debtor’s reorganization prospects. The Conference’s proposal limits the special protections related to the exercise of contractual rights against collateral to financial assets of types that are usual for legitimate protected financial contracts and do not present as high a level of risk to reorganization prospects.

Attached as Exhibit A is a draft of the suggested amendments to the Bankruptcy Code to confine recourse to collateral under the financial contracts exemption provisions solely to collateral that is "financial collateral" as defined in the draft. The draft is designed to exclude from the exemptions recourse to collateral consisting of a debtor's operating assets on the theory that the transactions are likely abusive ones, i.e., transactions that in economic effect are ordinary commercial transactions, but are structured as derivative transactions merely to benefit from the exemptions. In the Conference's view, these abusive transactions do not implicate systemic risk and should not benefit from the exemptions.

II. Settlement Payments

Bankruptcy Code § 546(e) was designed to protect prepetition transfers under securities contracts from avoidance as preferential transfers or fraudulent transfers. For example, a mark-to-market margin payment under a securities purchase agreement, securities loan, margin loan, clearing advance or other securities contract might be subject to avoidance as a preferential transfer absent § 546(e) protection. Similarly, § 546(e) protects intermediaries in the national securities clearance and payment process from avoidance exposure with respect to the transfers for which they act as intermediaries.

There has been disagreement among the courts as to the scope of the § 546(e) protection with respect to payments to shareholders in connection with leveraged buyouts and similar transactions. Absent § 546(e), shareholders who received payouts for their stock in connection with a leveraged buyout that rendered the target company insolvent may be vulnerable to recovery of their payouts as constructive fraudulent transfers by the target company's bankruptcy estate. The recovered amounts would be available to repay the target company's unpaid creditors. Most (but not all) courts have interpreted § 546(e) sufficiently broadly as to immunize shareholders from such recoveries if they received their payouts through the national securities clearance or payment system or even merely from a bank, even though no securities contract was implicated and they are not themselves securities or payment intermediaries. The Conference believes that this result is unfair and unnecessary to protect the securities markets.

Attached hereto as Exhibit B is a draft of the suggested amendments to §§ 546 and 550 of the Bankruptcy Code to permit recourse to the beneficial holder of a security on which a settlement payment is made if the settlement payment otherwise constitutes a constructive fraudulent transfer. The proposed amendments would not affect the exemptions under those sections currently available to banks, brokers and other intermediaries who are not the beneficial holder of the security.

III. Forward and Commodity Contracts

The current Bankruptcy Code financial contract exemptions apply to forward and commodity contracts because forward and commodity contracts are regularly traded, much in the same way as securities are traded, and pose many of the same systemic risk issues. However, the exemptions for forward and commodity contracts are so broadly drafted that they could include ordinary commodity supply contracts by which the debtor in ordinary course of its business sells a commodity to an end-user or buys a commodity from a supplier for use in the debtor's business.

The Conference is of the view that commodity supply contracts in which in the ordinary course of its business the commodity is sold by the debtor to an end-user or is used by the debtor should not pose systemic risk issues and therefore should not be exempt from the ordinary bankruptcy rules. However, the Conference has been unable to formulate a "bright line" rule that would distinguish a forward or commodity contract that is regularly traded and that poses a systemic risk concern from an ordinary supply contract that does not pose a systemic risk concern. The difficulty in devising a "bright line" rule lies in part in the fact that many debtors enter into forward and commodity contracts not only to sell or use the underlying commodity but also to hedge market volatility risk. Accordingly, a supplier or end-user will often preserve the option to trade a forward or commodity contract even though it would otherwise sell or use the underlying commodity.

Given that the efforts of the Conference to distinguish a forward or commodity contract that is regularly traded from an ordinary supply contract have not been successful, the Conference instead proposes a different scheme for forward and commodity contracts. Under this scheme, a debtor in possession would have a very short opportunity to elect that all forward and commodity contracts between the debtor and a single counterparty not have the benefit of the exemptions otherwise applicable to the contracts. If the election is made, the forward and commodity contracts with the single counterparty would be governed by a set of rules under which, if the debtor in possession wishes to preserve the value of the forward and commodity contracts for the benefit of the debtor's bankruptcy estate, the debtor in possession is required to post cash collateral in favor of the counterparty to cover postpetition volatility risk. In this way, the debtor in possession may retain the value of the forward and commodity contracts by "putting its money where its mouth is," while at the same time the non-debtor counterparty is protected by the cash collateral posted.

Attached hereto as Exhibit C is a more detailed outline as to how these provisions would work. If there is sufficient interest in exploring this proposal, we would be happy to work with you to develop statutory language.

We encourage you to consider the Conference's proposals, and look forward to discussing them with you. If you would like any further information, please contact me by telephone at (617) 951-8615 or by email at Edwin.smith@bingham.com.

Yours sincerely,

Edwin E. Smith
Chair, Committee on Capital Markets

Attachments and Enclosure

Amend section 362(b)(6), (7), (17) and (27) as follows:

(b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay –

* * *

- (6) under subsection (a) of this section, of the exercise by a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency of any contractual right (as defined in section 555 or 556) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any commodity contract, forward contract or securities contract, or of any contractual right (as defined in section 555 or 556) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such contracts, including any master agreements for such contracts;
- (7) under subsection (a) of this section, of the exercise by a repo participant or financial participant of any contractual right (as defined in section 559) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any repurchase agreement, or of any contractual right (as defined in section 559) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such agreements, including any master agreements for such agreements;

* * *

- (17) under subsection (a) of this section, of the exercise by a swap participant or financial participant of any contractual right (as defined in section 560) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any swap agreement, or of any contractual right (as defined in section 560) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such agreements, including any master agreements for such agreements;

* * *

- (27) under subsection (a) of this section, under subsection (a) of this section, of the exercise by a master netting agreement participant of any contractual

right (as defined in section 555, 556, 559, or 560) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any master netting agreement, or of any contractual right (as defined in section 555, 556, 559, or 560) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such master netting agreements to the extent that such participant is eligible to exercise such rights under paragraph (6), (7), or (17) for each individual contract covered by the master netting agreement in issue; and

* * *

Amend section 101 to insert the following after paragraph (21B):

(21C) The term "financial collateral"

(A) means, with respect to one or more contracts of the kind described in paragraphs (1) through (5) of section 561(a), --

(i) any property sold or to be sold in the performance of such contracts, cash, cash equivalent, security, instrument, certificate of deposit, mortgage loan, or interest in a contract of the kind described in paragraphs (1) through (5) of section 561(a) (except in each case any security or instrument issued or executed by the debtor or a person under common control with the debtor), in each case which also secures obligations under such contracts;

(ii) any other property not used in the operation of any business owned or conducted by the debtor or a person under common control with the debtor, in each case which secures obligations under such contracts; or

(iii) any letter of credit, guarantee, reimbursement agreement or other credit enhancement issued or provided by a person other than the debtor for the obligations under such contracts (regardless of any recourse that such person may have to the debtor), in each case which provides credit enhancement for obligations under such contracts; and

(B) notwithstanding subparagraph (A), does not include --

(i) any receivable (as defined in section 547(a)(3)) arising in the ordinary course of business of the debtor or a person under common control with the debtor relating to the sale or lease of goods, the provision of services or the licensing of information; and

(ii) any property that was not of a kind described in subparagraph (A) at the time of the filing of the petition, and the proceeds of such property.

Note: The Section 362(b) portion of the foregoing is identical to the Drafting Committee report of July 23, 2008. The Section 101(21C) portion of the foregoing contains changes from such report in clauses (A)(i) and B(ii).

Amend Section 546(e) as follows:

(e) Notwithstanding sections 544, 545, 547, 548(a)(1)(B), and 548(b) of this title, the trustee may not avoid a transfer that is a margin payment, as defined in section 101, 741, or 761 of this title, or settlement payment, as defined in section 101 or 741 of this title, made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, or that is a transfer made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, in connection with a securities contract, as defined in section 741(7), commodity contract, as defined in section 761(4), or forward contract, that is made before the commencement of the case, except

- (1) a transfer that is otherwise avoidable under section 548(a)(1)(A) of this title; or
- (2) a transfer that is otherwise avoidable under section 544, 545, 547, 548(a)(1)(B) or 548(b) of this title, but only to the extent such transfer is a redemption payment, principal payment, dividend payment, interest payment or other distribution on or in respect of a security, made for the benefit of the beneficial holder of the security, by or on behalf of the issuer of the security or another entity obligated with respect to the security.

Add a new Subsection (g) to Section 550 as follows:

(g) The trustee may not recover any transfer of a kind described in section 546(e)(2), except from the entity that is the beneficial holder of the security on or in respect of which such transfer is made.

Note: The Section 546(e) portion of the foregoing is identical to the Drafting Committee report of July 23, 2008. The Section 550(g) portion has been changed.

Excluded Commodity Contracts
Outline of Key Provisions

New definition of "excluded commodity contract".

An "excluded commodity contract" would be any "forward contract" or "commodity contract" (or similar term, such as "forward agreement") for the purchase or sale of a commodity actually used or sold by the debtor in the ordinary course of its business, including a hedging contract for actual business operations, if the debtor is not a "financial participant".

Replacement protections applicable to excluded commodity contracts.

Except as to all excluded commodity contracts with a single counterparty listed by the debtor or trustee in a statement filed with the court within 48 hours after the order for relief, the Bankruptcy Code's exemptions for financial contracts would not apply to an excluded commodity contract. The exemptions that would not apply would include exemptions from avoidance relating to the excluded commodity contract itself or any guaranty of, security interest securing, or other credit enhancement of the excluded financial contract.

Instead, the following protections would apply:

Interim post-petition performance. Pending assumption or rejection of each excluded commodity contract, the trustee would be required to perform all terms of the contract (other than provisions described in section 365(b)(2)) that are required to be performed by the debtor post-petition. During this period the trustee would not be required to pay any unpaid amounts on an excluded commodity contract that were required to have been paid by the debtor pre-petition.

No cherry picking. The trustee would not be permitted to cherry pick among excluded commodity contracts with a single counterparty. All such contracts with the counterparty would have to be either assumed or rejected.

Administrative expense claim for "in the money" claims including post-petition changes in value. If, on the date on which excluded commodity contracts with a particular counterparty are assumed or rejected, the net market value to the counterparty of the excluded commodity contracts (measured across all such contracts) is positive, then the counterparty would have an administrative expense claim for any amount by which the net market value to the counterparty on that date is greater than the net market value (by the same measure) of all those contracts on the earlier of the date of the order for relief and the post-petition date on which the net market value (by the same measure) to the counterparty is first positive.

Cash collateral to be posted to secure the administrative expense claim. The trustee would be required to post cash collateral, starting no later than X (~5) days after

the date of the order for relief, to secure payment of the administrative expense claim (determined, as to each counterparty, as if all of such excluded commodity contracts were being assumed or rejected as of the date of determination) in an amount equal to 105% of the allowable administrative expense claim, and the counterparty would be required to return any excess cash collateral. Cash collateral would be posted or returned each business day based on the closing price at the end of the prior business day. The amount of cash collateral to be posted under this provision would not be subject to modification by any agreement between the debtor and the counterparty, except a post-petition agreement approved by the court.

Period in which to assume or reject. The trustee would have up to Y (~30) days after the order for relief to move for court approval to assume or reject the contract. Cash collateral would continue to be posted or returned as required pending court approval. If the contract is not assumed within that time period, it is considered rejected.

Effect of rejection. If a counterparty's excluded commodity contracts are rejected, the counterparty's netting rights would be preserved, and the contracts would no longer be "excluded", i.e., all financial contract exemptions would apply (including with respect to collateral posted post-petition for any administrative expense claim). The counterparty would then have a period of up to 30 days following the rejection date to exercise the counterparty's right under the financial contract exemptions to terminate the contracts and exercise liquidation and netting rights without leave from the bankruptcy court. In addition, on rejection, the counterparty's damage claim under section 365(g) would be measured as of the rejection date (subject to sections 562(b) and (c)), rather than as of the petition date.

Stay relief. If the trustee fails to post cash collateral, otherwise perform the excluded commodity contract or timely assume the excluded commodity contract, then stay relief would be automatic for the counterparty, all excluded commodity contracts of that counterparty would cease to be excluded commodity contracts, and the general financial contract exemptions would be available to the counterparty.

Transition provisions

The foregoing treatment of excluded commodity contracts would apply to a contract entered into on or after the date of enactment. If a confirmation is entered into on or after the date of enactment under a master agreement entered before the date of enactment, the foregoing treatment would apply to the confirmation.

The foregoing treatment would not otherwise apply to a contract, or to a confirmation under a master agreement, entered into before the date of enactment unless the contract or confirmation were amended on or after the date of enactment to add a commodity or to increase the amount of a commodity, the price for a commodity or margin or collateral or to provide a guaranty or other credit enhancement of the debtor's performance.

Amend section 362(b)(6), (7), (17) and (27) as follows:

(b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay –

* * *

(6) under subsection (a) of this section, of the exercise by a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency of any contractual right (as defined in section 555 or 556) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any commodity contract, forward contract or securities contract, or of any contractual right (as defined in section 555 or 556) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such contracts, including any master agreements for such contracts;

(7) under subsection (a) of this section, of the exercise by a repo participant or financial participant of any contractual right (as defined in section 559) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any repurchase agreement, or of any contractual right (as defined in section 559) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such agreements, including any master agreements for such agreements;

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(17) under subsection (a) of this section, of the exercise by a swap participant or financial participant of any contractual right (as defined in section 560) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any swap agreement, or of any contractual right (as defined in section 560) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such agreements, including any master agreements for such agreements;

* * *

(27) under subsection (a) of this section, under subsection (a) of this section, of the exercise by a master netting agreement participant of any contractual

right (as defined in section 555, 556, 559, or 560) to foreclose on, dispose of, draw against, demand and receive payment under, or otherwise realize on any financial collateral under any security agreement or arrangement or other credit enhancement forming a part of or related to any master netting agreement, or of any contractual right (as defined in section 555, 556, 559, or 560) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such master netting agreements to the extent that such participant is eligible to exercise such rights under paragraph (6), (7), or (17) for each individual contract covered by the master netting agreement in issue; and

* * *

Amend section 101 to insert the following after paragraph (21B):

(21C) The term "financial collateral"

(A) means, with respect to one or more contracts of the kind described in paragraphs (1) through (5) of section 561(a), --

(i) any property sold or to be sold in the performance of such contracts, cash, cash equivalent, security, instrument, certificate of deposit, mortgage loan, or interest in a contract of the kind described in paragraphs (1) through (5) of section 561(a) (except in each case any security or instrument issued or executed by the debtor or a person under common control with the debtor), in each case which also secures obligations under such contracts;

(ii) any other property not used in the operation of any business owned or conducted by the debtor or a person under common control with the debtor, in each case which secures obligations under such contracts; or

(iii) any letter of credit, guarantee, reimbursement agreement or other credit enhancement issued or provided by a person other than the debtor for the obligations under such contracts (regardless of any recourse that such person may have to the debtor), in each case which provides credit enhancement for obligations under such contracts; and

(B) notwithstanding subparagraph (A), does not include --

(i) any receivable (as defined in section 547(a)(3)) arising in the ordinary course of business of the debtor or a person under common control with the debtor relating to the sale or lease of goods, the provision of services or the licensing of information; and

(ii) any property that was not of a kind described in subparagraph (A) at the time of the filing of the petition, and the proceeds of such property.

Note: The Section 362(b) portion of the foregoing is identical to the Drafting Committee report of July 23, 2008. The Section 101(21C) portion of the foregoing contains changes from such report in clauses (A)(i) and B(ii).

Amend Section 546(e) as follows:

(e) Notwithstanding sections 544, 545, 547, 548(a)(1)(B), and 548(b) of this title, the trustee may not avoid a transfer that is a margin payment, as defined in section 101, 741, or 761 of this title, or settlement payment, as defined in section 101 or 741 of this title, made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, or that is a transfer made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, in connection with a securities contract, as defined in section 741(7), commodity contract, as defined in section 761(4), or forward contract, that is made before the commencement of the case, except

- (1) a transfer that is otherwise avoidable under section 548(a)(1)(A) of this title; or
- (2) a transfer that is otherwise avoidable under section 544, 545, 547, 548(a)(1)(B) or 548(b) of this title, but only to the extent such transfer is a redemption payment, principal payment, dividend payment, interest payment or other distribution on or in respect of a security, made for the benefit of the beneficial holder of the security, by or on behalf of the issuer of the security or another entity obligated with respect to the security.

Add a new Subsection (g) to Section 550 as follows:

(g) The trustee may not recover any transfer of a kind described in section 546(e)(2), except from the entity that is the beneficial holder of the security on or in respect of which such transfer is made.

Note: The Section 546(e) portion of the foregoing is identical to the Drafting Committee report of July 23, 2008. The Section 550(g) portion has been changed.

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Replacement protections applicable to excluded commodity contracts.

Except as to all excluded commodity contracts with a single counterparty listed by the debtor or trustee in a statement filed with the court within 48 hours after the order for relief, the Bankruptcy Code’s exemptions for financial contracts would not apply to an excluded commodity contract. The exemptions that would not apply would include exemptions from avoidance relating to the excluded commodity contract itself or any guaranty of, security interest securing, or other credit enhancement of the excluded financial contract.

Instead, the following protections would apply:

Interim post-petition performance. Pending assumption or rejection of each excluded commodity contract, the trustee would be required to perform all terms of the contract (other than provisions described in section 365(b)(2)) that are required to be performed by the debtor post-petition. During this period the trustee would not be required to pay any unpaid amounts on an excluded commodity contract that were required to have been paid by the debtor pre-petition.

No cherry picking. The trustee would not be permitted to cherry pick among excluded commodity contracts with a single counterparty. All such contracts with the counterparty would have to be either assumed or rejected.

Administrative expense claim for “in the money” claims including post-petition changes in value. If, on the date on which excluded commodity contracts with a particular counterparty are assumed or rejected, the net market value to the counterparty of the excluded commodity contracts (measured across all such contracts) is positive, then the counterparty would have an administrative expense claim for any amount by which the net market value to the counterparty on that date is greater than the net market value (by the same measure) of all those contracts on the earlier of the date of the order for relief and the post-petition date on which the net market value (by the same measure) to the counterparty is first positive.

Cash collateral to be posted to secure the administrative expense claim. The trustee would be required to post cash collateral, starting no later than X (~5) days after

the date of the order for relief, to secure payment of the administrative expense claim (determined, as to each counterparty, as if all of such excluded commodity contracts were being assumed or rejected as of the date of determination) in an amount equal to 105% of the allowable administrative expense claim, and the counterparty would be required to return any excess cash collateral. Cash collateral would be posted or returned each business day based on the closing price at the end of the prior business day. The amount of cash collateral to be posted under this provision would not be subject to modification by any agreement between the debtor and the counterparty, except a post-petition agreement approved by the court.

Period in which to assume or reject. The trustee would have up to Y (~30) days after the order for relief to move for court approval to assume or reject the contract. Cash collateral would continue to be posted or returned as required pending court approval. If the contract is not assumed within that time period, it is considered rejected.

Effect of rejection. If a counterparty's excluded commodity contracts are rejected, the counterparty's netting rights would be preserved, and the contracts would no longer be "excluded", i.e., all financial contract exemptions would apply (including with respect to collateral posted post-petition for any administrative expense claim). The counterparty would then have a period of up to 30 days following the rejection date to exercise the counterparty's right under the financial contract exemptions to terminate the contracts and exercise liquidation and netting rights without leave from the bankruptcy court. In addition, on rejection, the counterparty's damage claim under section 365(g) would be measured as of the rejection date (subject to sections 562(b) and (c)), rather than as of the petition date.

Stay relief. If the trustee fails to post cash collateral, otherwise perform the excluded commodity contract or timely assume the excluded commodity contract, then stay relief would be automatic for the counterparty, all excluded commodity contracts of that counterparty would cease to be excluded commodity contracts, and the general financial contract exemptions would be available to the counterparty.

Transition provisions

The foregoing treatment of excluded commodity contracts would apply to a contract entered into on or after the date of enactment. If a confirmation is entered into on or after the date of enactment under a master agreement entered before the date of enactment, the foregoing treatment would apply to the confirmation.

The foregoing treatment would not otherwise apply to a contract, or to a confirmation under a master agreement, entered into before the date of enactment unless the contract or confirmation were amended on or after the date of enactment to add a commodity or to increase the amount of a commodity, the price for a commodity or margin or collateral or to provide a guaranty or other credit enhancement of the debtor's performance.