RECORD NO. 07-2105

In The

United States Court of Appeals

For The Fourth Circuit

In re: NATURAL GAS DISTRIBUTORS, LLC,

Debtor,

RICHARD M. HUTSON, II,
Trustee for National Gas Distributors, LLC,

Plaintiff – Appellee,

v.

E.I. DUPONT DE NEMOURS AND COMPANY, INCORPORATED; SMITHFIELD PACKING COMPANY, INCORPORATED, f/k/a Stadler's Country Hams, Incorporated,

Defendants – Appellants,

INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC.,

Amicus Curiae.

ON APPEAL FROM THE UNITED STATES BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF NORTH CAROLINA AT WILSON

BRIEF OF AMICUS CURIAE

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No. 07-2105 Caption: Richard M. Hutson, II, Trustee for National Gas Distributors, LLC v. The Smithfield Packing Company, Incorporated

Pursuant to FRAP 26.1 and Local Rule 26.1,

International Swaps and Derivatives Association, Inc. who is amicus,

(name of party/amicus) (appellant/appellee/amicus)

makes the following disclosure:

1. Is party/amicus a publicly held corporation or other publicly held entity?
   ☐ YES ☑ NO
2. Does party/amicus have any parent corporations?
   ☐ YES ☑ NO
   If yes, identify all parent corporations, including grandparent and great-grandparent corporations:

3. Is 10% or more of the stock of a party/amicus owned by a publicly held corporation or other publicly held entity?
   ☐ YES ☑ NO
   If yes, identify all such owners:

4. Is there any other publicly held corporation or other publicly held entity that has a direct financial interest in the outcome of the litigation (Local Rule 26.1(b))?
   ☐ YES ☑ NO
   If yes, identify entity and nature of interest:

5. Is party a trade association? (amici curiae do not complete this question)
   ☐ YES ☐ NO
   If yes, identify all members of the association, their parent corporations, and any publicly held companies that own 10% or more of a member's stock:

6. Does this case arise out of a bankruptcy proceeding?
   ☑ YES ☐ NO
   If yes, identify any trustee and the members of any creditors' committee:
   Richard M. Hutson, II Trustee

(signature) 1/29/08 (date)

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Amicus Curiae the International Swaps and Derivatives Association, Inc. ("ISDA"), by and through counsel, files this Brief in support of Appellants E.I. du Pont de Nemours and Company ("du Pont") and The Smithfield Packing Company, Incorporated ("Smithfield") (collectively, the "Appellants").

STATEMENT OF INTEREST

ISDA, which represents participants in the privately negotiated derivatives industry, is the largest global financial trade association by number of member firms. ISDA was chartered in 1985, and today has over 800 member institutions from 56 countries on six continents. These members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter derivatives to manage efficiently the risks inherent in their core economic activities.

Since its inception, ISDA has pioneered efforts to identify and reduce the sources of risk in the derivatives and risk management industry. Among its most notable accomplishments are developing the ISDA Master Agreement; publishing a wide range of related documentation, materials and instruments covering a variety of transaction types; producing legal opinions on the enforceability of netting and collateral arrangements (available only to ISDA members); securing recognition of the risk-reducing effects of netting in determining capital

requirements; promoting sound risk management practices; and advancing the understanding and treatment of derivatives and risk management from public policy and regulatory capital perspectives.

Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), the Bankruptcy Code definition of "swap agreement" was amended to include, among other things, a commodity forward agreement. See Pub. L. No. 109-8 (2005), codified at 11 U.S.C. § 101(53B) (2006). The interpretation of this amended provision is a matter of first impression at the Circuit Court level. As ISDA played a significant role in the drafting of the relevant provisions of the BAPCPA,[1] ISDA respectfully submits that this Court will be aided by ISDA's views on this matter.

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[1] ISDA worked in "close collaboration" with the President's Working Group on Financial Markets and others. See Michael H. Krimminger, Federal Deposit Insurance Corporation, Adjusting the Rules: What Bankruptcy Reform Will Mean for Financial Markets Contracts, http://www.fdic.gov/bank/analytical/fyi/2005/101105fyi.html. The financial provisions of the BAPCPA were originally introduced to Congress in a separate piece of legislation that was eventually incorporated into the BAPCPA. ISDA prepared a position paper in 1996 setting forth the need for amendments to the Bankruptcy Code and parallel provisions of the Federal Deposit Insurance Act ("FDIA") and proposing language for many of the provisions eventually amended by the BAPCPA. See International Swaps and Derivatives Association, Inc. & The Public Securities Association, Financial Transactions Insolvency: Reducing Risk through Legislative Reform, 13-14 (1996), available at http://www.isda.org (proposing amendments to the definitions of "swap agreement" and "forward contract"). ISDA also participated in many of the hearings that led up to the eventual adoption of the provisions that were passed as part of the BAPCPA. ISDA

ISDA submitted an Amicus Brief in support of Smithfield's and DuPont's motion to dismiss the complaint of Richard M. Hutson, II, Trustee for National Gas Distributors, LLC, ("National Gas Distributors" or "NGD"), f/k/a/ Paul Lawing, Jr., LLC, in the adversary proceeding Richard M. Hutson, II, Trustee for National Gas Distributors, LLC, f/k/a/ Paul Lawing, Jr., LLC, vs. The Smithfield Packing Company, Incorporated (Adv. Proc. No. 06-00267-8-ATS) because of the importance of the issues presented by this proceeding to the financial markets. ISDA likewise submitted statements in support of Smithfield's motions for leave to appeal to the District Court and this Court.

PRELIMINARY STATEMENT

The derivatives markets involve a significant number of participants and an enormous amount of capital. These markets continue to grow rapidly. As of June 2007, the notional amount of all types of over-the-counter derivative contracts stood at $516 trillion, which represented 25% growth over the amount reported six months earlier; of that $516 trillion, commodity-based contracts which are forwards and swaps had a notional amount of $3.4 trillion. Bank for International

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was specifically thanked by Senator Dennis Deconcini for its role in the 1990 legislation that first created Bankruptcy Code safe harbors for swap agreements. 136 Cong. Rec. S7534-01 (June 6, 1990) (statement of Sen. Deconcini).

Settlement, Monetary and Economic Department, Amounts Outstanding of Over-the-counter (OTC) Derivatives (November 2007), http://www.bis.org/statistics/otcder/dt1920a.pdf. There are of course many types of derivatives and many markets linked by derivatives and similar instruments. It is this multiplicity of linked markets that Congress has sought to protect.

The statutory language at issue in this case was added to the Bankruptcy Code in 2005 as part of a steadily expansive series of Bankruptcy Code changes intended by Congress to protect markets deemed by it to be particularly vital and sensitive to the delay and dislocation that can attach to bankruptcy proceedings. This series of statutory changes began in 1982 with the creation of safe harbors protecting termination and set-off rights under "securities contracts," "commodities contracts" and "forward contracts." See An Act to Amend Title 11, United States Code, To Correct Technical Errors, and to Clarify and Make Substantive Changes, with Respect to Securities and Commodities, Pub. L. No. 97-222 (1982). The protections afforded these contracts included relief from many of the avoidance provisions of the Code, including those enabling a trustee to recoup so-called "fraudulent conveyances". See, e.g., 11 U.S.C. § 546(e) (2006). The reason for these changes was a desire to "minimize the potentially massive losses and chain reaction of insolvencies," H.R. Rep. 97-420, 4 (1982), reprinted in 1982 U.S.C.C.A.N. 582, 585, that might occur in the relevant markets.

In 1984, Congress added parallel protection for "repurchase agreements." See The Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353 (1984). Congress did so to protect the continued liquidity and safety of the repurchase agreement market from certain adverse consequences of the insolvency of market participants. See In re Bevill, Bresler & Schulman Asset Management Corp., 67 B.R. 557, 596 (D. N.J. 1986). In 1990, Congress added similar protection for "swap agreements," the particular type of agreement at issue in this case. See Bankruptcy: Swap Agreements and Forward Contracts, Pub. L. No. 101-311 (1990). In 1990, Congress also amended the already-existing forward contract provisions to expand the definition of contractual right used in Section 556. See id.; see also 136 Cong. Rec. S7534-01 (June 6, 1990). According to Senator Dennis Deconcini:

> [S]wap agreements and forward contracts play an important role in international commerce and this legislation will help American business compete effectively. The effect of the swap provisions will be to provide certainty for swap transactions and thereby stabilize domestic markets by allowing the terms of the swap agreement to apply notwithstanding the bankruptcy filing.

136 Cong. Rec. S7534-01 (June 6, 1990) (statement of Sen. Deconcini).

Each of the categories of protected contracts under the Bankruptcy Code was initially defined and then redefined and expanded in statutory changes in intervening years, culminating in the substantial expansion of BAPCPA in 2005 and in the 2006 Revising Act, described in part below. See Pub. L. No. 97-222

(1982); Pub. L. No. 98-353 (1984); Pub. L. No. 101-311 (1990); Pub. L. No. 101-394 (1994). In 2005, however, Congress provided a major structural change in the safe harbor provisions that underscored the fact that, in BAPCPA, Congress was attempting to cope with "systemic risk in a financial marketplace," H.R. Rep. 109-31(I), 1 (2005), reprinted in 2005 U.S.C.C.A.N. 88, 89, that extended across the seemingly separate markets that already had their own separate safe harbors. This major change was the addition of Bankruptcy Code Section 561, providing safe harbor protections for "master" agreements covering potentially the full range of individually safe-harbored transaction types. After BAPCPA, a single pair of contracting parties could put their physically-settled over-the-counter natural gas contracts, their cash-settled, on-exchange futures contracts and their cash-settled, over-the-counter interest rate swaps, for example, under a single agreement and treat them collectively to unified safe-harbor protections. Thus, Congress, after nearly thirty years of developing and expanding "product-specific" safe harbors separately, recognized that the development of interrelated markets and diversified trading entities required unified protection, so that a failure in one market did not lead to greater disaster across other markets. As a senior FDIC officer stated with respect to one of the several bills that ultimately were fulfilled in BAPCPA:

> The series of "netting" amendments to the Bankruptcy Code and the FDI Act over the past two decades were designed to further the policy goal of minimizing the systemic risks potentially arising from certain interrelated financial activities and markets. Systemic risk has been

> defined as the risk that a disruption—at a firm, in a market segment, to a settlement system, etc.—can cause widespread difficulties at other firms, in other market segments or in the financial system as a whole. . . . If participants in certain financial activities are unable to enforce their rights to terminate financial contracts with an insolvent entity in a timely manner, and to offset or net payment and other transfer obligations and entitlements arising under such contracts, the resulting uncertainty and potential lack of liquidity could increase the risk of an inter-market disruption. . . .
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> [T]he provisions of Title X are an important step toward harmonizing . . . statutory provisions which were enacted over more than a decade. In addition, Title X permits our statutes to remain abreast of innovations that have occurred in our financial markets since 1989.

Statement of Douglas H. Jones, Senior Deputy General Counsel, Federal Deposit Insurance Corporation, on Bankruptcy Reform Legislation, Committee on Banking, United States Senate, March 25, 1999, available at http://www.fdic.gov/news/news/speeches/archives/1999/sp25mar99b.html.

It is only with an understanding of this background that one can properly answer the very narrow question before the court: whether a physically-settled natural gas forward agreement is a "swap agreement" for purposes of the safe harbors under the Bankruptcy Code? The answer, of course, is yes.

ISDA believes that the Bankruptcy Court's narrowing of the scope of the Bankruptcy Code's safe harbors with respect to derivative transactions in this case will have a disruptive and deleterious effect on the financial markets and upset legislation which Congress has instituted through decades of effort to protect the integrity and efficiency of U.S. markets. The derivatives industry depends on,

among other things, a predictable and stable system of bankruptcy laws. Moreover, it is clear from the legislative history of the safe harbor provisions that Congress sought to protect the entire derivatives market and related markets, rather than merely one segment of that combined market, from systemic failure across different market segments.[2]

ARGUMENT

The issue before the Court is whether the forward agreements between National Gas Distributors and the Appellants fall within the revised Bankruptcy Code definition of a "swap agreement." The BAPCPA amended the Bankruptcy Code definition of swap agreement so that it now provides: "The term 'swap agreement' (A) means . . . (VII) a commodity index or a commodity swap, option, future or forward agreement[.]" Pub. L. No. 109-8 § 907 (2005), codified at 11 U.S.C. § 101(53B) (2006) (emphasis added). Under the safe harbor provisions of the Bankruptcy Code, transfers under a "swap agreement" are not subject to

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[2] The possibility of contagion across sub-markets can be vividly illustrated by the risk that was present in the collapse of the diversified energy trading empire that was Enron. Creditors affected by its collapse ranged from banks to end users. See International Swaps and Derivatives Association, Restoring Confidence in U.S. Energy Trading Markets 3, 9, 11, 15 (2003) (predating the BAPCPA); see also, Franklin R. Edwards & Edward R. Morrison, Derivatives and the Bankruptcy Code: Why the Special Treatment?, 22 Yale J. on Reg. 91 (2005).

fraudulent conveyance attack, such as that directed at the Appellants. The Bankruptcy Court's ruling in this case that as a matter of law the forward agreements between Appellants and National Gas Distributors cannot be "swap agreements" within the newly-expanded Bankruptcy Code definition of swap agreement, but are rather "supply agreements," is contrary to the express language of the Bankruptcy Code and Congressional intent, and inconsistent with industry understanding and practice.

Preliminary Matters of Size and Consistency

Before addressing the legal errors in the lower court decision, it is important to dispose of a concern that seemed of critical importance to the Bankruptcy Court's decision. The Bankruptcy Court's fear was that finding the contract at issue to be a swap agreement within the safe harbor would lead future interpreters of the provision to incorrectly apply it to "the smallest case of a farmer who contracts to sell his hogs at the end of the month for a fixed price." In re Nat'l Gas Distrib. LLC, 369 B.R. 884, 900 (Bankr. E.D.N.C. 2007). However, the instant case could not be more dramatically different in scale from the folksy imagery of the Bankruptcy Court. Smithfield Foods, Inc., "the world's largest pork processor and hog producer," was a party to forward grain contracts alone with a mark-to-market value on May 1, 2005 of $50,500,000 and on April 30, 2006 of $107,700,000.

Smithfield Foods, Inc., Annual Report (Form 10-K), at 31 (Jul. 11, 2005); Smithfield Foods, Inc., Annual Report (Form 10-K), at 34 (Apr. 30, 2006). "DuPont is a world leader in science and techonology in a range of disciplines, including biotechnology, electronics, materials science, safety and security and synthetic fibers." DuPont Co., Annual Report (Form 10-K), at 3 (Feb. 2, 2007). The debtor, National Gas Distributors stated that its income from business operations was $104,283,274 in 2004 in gross receipts and $150,506,572 in 2005 in estimated gross receipts, the two years prior to its petition date. Statement of Financial Affairs, Case No. 06-0016, Docket No. 88 (Bankr. E.D.N.C. 2006).[3] Thus, it appears from the record that Smithfield and DuPont, as well as NGD, were at the least significant business entities, and may qualify for the swap agreement

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[3] This Court may take judicial notice of these facts under Federal Rule of Evidence 201 which states that "[a] judicially noticed fact must be one not subject to reasonable dispute in that it is ... capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned." Fed. R. Evid. 201. Prior judicial records are such a source; as the Fourth Circuit has noted, "[t]he most frequent use of judicial notice of ascertainable facts is in noticing the content of court records." Colonial Penn. Ins. Co. v. Coil, 887 F.2d 1236, 1239 (4th Cir. 1989) (quoting Wright & Graham, Federal Practice and Procedure: Evidence § 5106 (1977)). In addition, Federal Rule of Evidence 201(f) provides that "judicial notice may be taken at any stage of the proceeding." Fed. R. Evid. 201(f). Thus, "an appellate court may take judicial notice of facts." Colonial Penn., 887 F.2d at 1239-40.

safe harbor as "financial participants" in addition to being "swap participants."[4] Although we trust that the access of a mere swap participant to the swap safe harbor would not be prejudiced by a decision in this case, we believe it is most important for this Court to take note of the actual scale of the parties to this case and their contracts, before worrying about the "smallest case" hypothesized by the court below. Hypothetical parties aside, there is little doubt Congress intended substantial market participants such as those actually before this Court to be swap participants covered by the swap safe harbor.

Additionally, as a general threshold concern, the Bankruptcy Court dwelled extensively on the decades-old early legislative history of the Bankruptcy Code's swap safe harbor, but ignored the lessons of the Financial Netting Improvements Act of 2006, Pub. L. No. 109-390 (2006) (the "2006 Revising Act"). See In re Nat'l Gas Distrib., 369 B.R. at 895 n.5. The legislative history of the 2006

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[4] Parties may have access to the swap safe harbor as either "swap participants" or "financial participants." 11 U.S.C. §§ 101(53C), 101(22A) (2006). "Financial participant," a term added to the Bankruptcy Code in the BAPCPA, refers to an entity that has entered into Bankruptcy Code safe harbored transactions of any type in the previous 15-month period with either a gross dollar value of not less than $1,000,000,000 in notional amount or a gross mark-to-market position of not less than $100,000,000. 11 U.S.C. § 101(22A)(A). The purpose of these thresholds in this addition to the Bankruptcy Code, as explained in the legislative history, is to "help prevent systemic impact upon the markets from a single failure." H.R. Rep. 109-31 Pt. 1 at 131. Unfortunately, the record below has not been developed in terms of the precise statistics needed to show "financial participant" status.

Revising Act makes clear that Congress intended it as a mere "technical" amendment to the BAPCPA. H.R. Rep. 109-648 Pt. 1 at 1 (2006). As the Supreme Court has repeatedly noted, "[w]hen several acts of Congress are passed, touching the same subject-matter, subsequent legislation may be considered to assist in the interpretation of prior legislation upon the same subject." Tiger v. W. Inv. Co., 221 U.S. 286, 309 (1911); see also Red Lion Broad. Co. v. F.C.C., 395 U.S. 367, 380-81 (1969) ("Subsequent legislation declaring the intent of an earlier statute is entitled to great weight in statutory construction."). Accordingly, we will proffer material from and relating to the 2006 Revising Act. We urge this Court to read the BAPCPA and the 2006 Revising Act as one piece of legislation.

"Forwards" Are Protected Agreements

The Bankruptcy Court said the contract at issue is a "forward contract,"[5] a type of contract defined under the Bankruptcy Code and itself eligible for separate

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[5] In addition to the lower court determining that the contract at issue is a "forward contract," the terms of the contract itself state that it is a "forward contract." See North American Energy Standards Board ("NAESB") Base Contract for Sale and Purchase of Natural Gas at ¶ 10.5, Memorandum in Support of Motion to Dismiss at Ex. A, J.A. 127. This statement is a standard part of the 2002 NAESB gas forward contract form, the very form used for the contract at issue and a form commonly used for forward natural gas "forward agreements". In response to this case, NAESB's Interpretation Committee has posted a proposed interpretation of its contract to the effect that forward agreements under a NAESB Base Contract should also be protected as swap agreements under the Bankruptcy Code. See Recommendation for C07003 (2008), available at: http://www.naesb.org/pdf3/wgq_interpretations012808a2.doc

safe harbor treatment parallel to that for swap agreements. The plain language of the statute and the legislative history of the BAPCPA make it clear that this conclusion should be dispositive for purposes of bringing the contract at issue under the swap safe harbor provisions of the Bankruptcy Code as well.

The term "forward agreement," unlike the term "forward contract," is not defined in the Bankruptcy Code. Yet, the terms "forward contract" and "forward agreement" are considered one and the same in common industry parlance.[6] In fact, the Black's Law Dictionary definition for "forward agreement" is a mere pass-through to that of "forward contracts" as the definition reads: "See Forward Contract." Black's Law Dictionary 861 (8th ed. 2004). The definition of "forward

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[6] Perhaps the most concise definition of a forward is that supplied in an October 11, 2005 "FYI" from the FDIC at the time of the implementation of BAPCPA, which defines a forward as a "sales contract between a buyer (holding the long position) and a seller (holding the short position) for an asset with delivery deferred until a future date." Krimminger, supra note 1. See also John Wood, Weather Derivatives, in Jonathan Denton, ed., Practical Derivatives: A Transactional Approach (Globe Business Publishing Ltd., London, 2006) ("[A forward] is a contract between two parties to trade an asset at a specific time in the future and at a specific predetermined price. These products are traded on the OTC market."); Bank for International Settlement, Monetary and Economic Department, OTC derivatives market activity in the first half of 2006 (2006), available at http://www.bis.org/publ/otc_hy0611.pdf ("Forward contracts represent agreements for delayed delivery of financial instruments or commodities in which the buyer agrees to purchase and the seller agrees to deliver, at a specified future date, a specified instrument or commodity at a specified price or yield. Forward contracts are generally not traded on organised exchanges and their contractual terms are not standardised.").

contract" contains the statement "Also termed forward agreement." Black's Law Dictionary 345 (8th ed. 2004). The term "agreement," furthermore, is generally viewed as broader than the term "contract," see Black's Law Dictionary 74 (8th Ed.), such that the use of the term "forward agreement" in Bankruptcy Code Sections 101(53B) and 546(g) casts a wider net than the use of the term "forward contract" in Sections 101(25) and 546(e). This distinction, although germane to the task of interpretation before this Court, is frequently lost in vernacular references by those in the markets to "forwards." See, e.g., Michael H. Krimminger, Adjusting the Rules: What Bankruptcy Reform Will Mean for Financial Markets Contracts, available at http://www.fdic.gov/bank/analytical/fyi/2005/101105fyi.html.

It is a recognized canon of statutory interpretation that undefined terms (such as "forward agreement" in the Bankruptcy Code) should be given their ordinary, common meaning. See Perrin v. United States, 444 U.S. 37, 42 (1979) ("A fundamental canon of statutory construction is that, unless otherwise defined, words will be interpreted as taking their ordinary, contemporary, common meaning.") As explained in the preceding paragraph, the forward agreement at issue here falls squarely within the plain language of the Code definition of "swap agreement." It also falls within the plain language of the Code definition of "forward contract" as "a contract for the purchase, sale, or transfer of a

commodity, as defined in section 761(8) of this title, 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, or product or byproduct thereof, with a maturity date more than two days after the date the contract is entered into . . . ."[7] 11 U.S.C. 101(25) (2006). Once the Bankruptcy Court acknowledged that the contract at issue was in fact a "forward," the Bankruptcy Code mandated the application of the safe harbors, including the swap agreement exemption from avoidance claims that is found in section 546(g) of the Bankruptcy Code.[8] Indeed, as the Bankruptcy Court for the District of Delaware recently held in connection with the application of the amended safe harbor provisions:

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[7] Section 761(8) in turn, refers to a specific provision in the Commodity Exchange Act for the definition of a "commodity" as, inter alia, "wheat, cotton, rice, corn, oats, . . . and all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in." 7 U.S.C. § 1a(4) (2006) (emphasis added). Natural gas is traded on both futures exchanges and over the counter. See, e.g., BCP Liquidating LLC v. Bridgeline Gas Mktg., LLC (In re Borden Chem. & Plastics Operating L.P.), 336 B.R. 214, 218 (Bankr. D. Del. 2006) ("This Court believes that, at this point in time, it can hardly be questioned that natural gas is a commodity under the Code."); In re Mirant Corp., 310 B.R. 548, 565 (Bankr. N.D. Tex. 2004) (finding that "natural gas is a commodity").

[8] Section 546(g) provides that, notwithstanding certain sections of the Bankruptcy Code, "the trustee may not avoid a transfer made by or to a swap participant or financial participant, under or in connection with any swap agreement and that is made before the commencement of the case. . . . " 11 U.S.C. § 546(g) (2006). Section 546(e) provides parallel protection for forward contracts. 11 U.S.C. § 546(e) (2006).

> [T]he Supreme Court has instructed repeatedly that the best way to determine congressional intent is to apply the plain meaning of the text of the statute . . . No further inquiry or consideration of other contractual provisions is required . . . .
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> Succinctly stated . . . [this court's] conclusion is compelled by the plain meaning of the statute and is consistent with the policy and legislative history underlying the relevant provisions of the Bankruptcy Code.

Calyon N.Y. Branch v. Am. Home Mortgage Corp. (In re Am. Home Mortgage Corp.), 2008 WL 60292, *8 (Bankr. D. Del. 2008). In American Home, American Home and Calyon were parties to a "repurchase agreement." When American Home filed a petition under chapter 11 of the Bankruptcy Code, it argued that the contract at issue did not fall under the protections of the safe harbor provisions of the Bankruptcy Code for repurchase agreements because it was a disguised form of secured financing and not a repurchase agreement. American Home urged the Bankruptcy Court to look beyond the explicit text of section 101(47) of the Bankruptcy Code (which contains the definition of "repurchase agreement") and "examine the substance of the [c]ontract to determine whether it is a 'true' repurchase agreement or a disguised secured financing." Id. at *6. However, in soundly rejecting the debtor's argument, the court held that the contract at issue was a repurchase agreement within the scope of the Bankruptcy Code's definition of that term, and that it was thus entitled to the full array of protections afforded such an agreement under the Bankruptcy Code. Id. at *11. In addition, the court

held that the contract at issue could fall under two definitional safe harbors in the Bankruptcy Code – "repurchase agreement" (Section 559) and "securities contract" (Section 555), id. at *11—just as the contract in issue in the case before this court could fall within the swap agreement safe harbors or the forward contract safe harbors.[9]

Our conclusions above are supported by the legislative history of the BAPCPA. Congress clearly desired to cover *at least* the contents of the defined-term "forward contracts" by use of the term "forward agreement" in the new Bankruptcy Code definition of "swap agreement": "The use of the term 'forward' [agreement] in the definition of 'swap agreement' is not intended to refer only to transactions that fall within the definition of 'forward contract.' Instead, a 'forward' transaction could be a 'swap agreement' even if not a 'forward contract.'" H.R. Rep. No. 109-31, Pt. 1, at 122 (emphasis added).

Although the Bankruptcy Code does not define "forward agreement," the plain language of the statute, the ordinary meaning of the term as captured in the

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[9] While not an issue in this appeal, it would appear that the transfers at issue in this case may also be entitled to the protections of Bankruptcy Code section 546(e), as such transfers may constitute settlement payments made to a forward contract merchant. As noted in the American Home decision, see 2008 WL 60292, *11, the application of more than one safe harbor to a particular instrument is not only possible, but, in the case of repurchase agreements and forward contracts, is consistent with the express provisions of the Bankruptcy Code and Congressional intent.

Black's definition of "forward agreement" and the legislative history compel a finding that the contract at issue is a "swap agreement."[10]

Errors in the Decisions Below

The Bankruptcy Court, through a misreading of the statutory definition of "swap agreement" and its early legislative history, holds that the contract at issue cannot be a swap. Instead, the Court concluded, without a finding of fact, that the contract was a "simple supply agreement," In re Nat'l Gas Distrib., 369 B.R. at 899, and not traded in the financial or derivatives markets. Id. The Bankruptcy Court's concern about simple supply agreements arises from the BAPCPA legislative history to the effect that "traditional commercial arrangements, such as supply agreements, or other non-financial market transactions . . . cannot be treated as 'swaps' under the . . . Bankruptcy Code simply because the parties purport to

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[10] Swaps may be characterized as chains of forwards. See, e.g., Peter H. Huang, A Normative Analysis of New Financially Engineered Derivatives, 73 S. Cal. L. Rev. 471 at 483 (2000), available at http://www-rcf.usc.edu/~usclrev/pdf/073301.pdf. The evolution in ISDA's own name reflects the multifaceted characteristics of the derivatives markets and the understanding in the financial markets (and in Congress) that markets once referred to generically as "swaps markets" actually encompass a rich array of transactions. Thus, ISDA, once the "International Swap Dealers Association, Inc.," became the International Swaps and Derivatives Association on August 9, 1993. This change reflected both the breadth of instrument previously represented by the term "swaps" alone and the expansion of ISDA membership beyond the dealer community.

document or label the transactions as 'swap agreements.'" H.R. Rep. 109-31 Pt. 1 at 122.

First, this legislative history taken at face, seems intended to prohibit opportunistic re-naming of transactions as something they are not. No such re-naming is alleged or present in this case. See discussion of "forwards" above at footnotes 5-10 and accompanying text; see also BCP Liquidating LLC v. Bridgeline Gas Marketing, LLC (In re Borden Chem. and Plastics Operating Ltd. P'ship, *et al.*), 336 B.R. 214, 221-23 (Bankr. D. Del. 2006).

Second, one might view this legislative history as parallel to that accompanying the definition of "forward contract," treated in the leading cases of Williams v. Morgan Stanley Capital Group (In re Olympic Natural Gas Co.), 294 F.3d 737 (5th Cir. 2002), and In re Borden Chem.. In these cases, both the U.S. Court of Appeals for the Fifth Circuit and the U.S. Bankruptcy Court for the District of Delaware, respectively, rejected the argument that Congress intended to distinguish between "financial" forward contracts and "ordinary purchase and sale" forward contracts, when, as the Fifth Circuit states in Olympic Natural Gas, "the statutory language makes no such distinction." In re Olympic, 294 F.3d at 742.[11] The Bankruptcy Court for the District of Delaware in Borden Chemicals expanded

[11] The Olympic court specifically noted that forward contracts often contemplate physical delivery of a commodity. In re Olympic, 294 F.3d at 741.

on this: "[The Debtor] states that 'the House Report goes on to explain that while the avoidance exemptions apply to genuine forward contracts regarding commodities that are not currently listed in the Commodity Exchange Act, the exemptions do not apply to ordinary supply-of-goods contracts, which are not essentially financial in character.' [citations omitted] . . . [I]t is clear[, however,] that Congress was concerned about protecting only [(and any)] contracts for the future delivery of goods that are the subject of trading in the forward contract market.[12] Therefore, as noted by the Fifth Circuit, there is no basis from which to distinguish among forward contracts." In re Borden Chem., 336 B.R. at 220 (footnote added). The Borden Chemicals Court found that natural gas, the subject of the contract before it, was "the subject of [appropriate] trading," see id. at 218.

Additionally, the court in Borden Chemicals looked at additional elements of a forward in order to reach its result, such as taking note of Black's definition of "hedging," which means, among other things, "to make advance arrangements to safeguard oneself from loss on an investment, speculation or bet, as when a buyer of commodities insures against unfavorable price changes by buying in advance at a fixed rate for later delivery." Black's Law Dictionary 740 (8th ed. 2004); see In

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12 Importantly, Section 546(g), unlike Section 546(e), does not even look to prior trading to test the type of commodity underlying transactions specifically listed in clause (A)(i) of the definition of swap agreement. Even if it did, natural gas certainly is appropriately traded. See supra note 7.

re Borden Chem., 336 B.R. at 220-21. "Hedging" of course is a "financial" activity.

"One of the most commonly used derivative contracts in the energy market as a physical hedge against price is a forward contract . . . . " In re Borden Chem., 336 B.R. at 222. In the present case, what Appellants were doing via their forward agreements with National Gas Distributors fits this description. The contracts at issue contain intrinsic hedging elements.[13] One would say, as the Borden Chemicals Court did with respect to the contract before it, that the NGD transactions were "risk-shifting in nature," H.R. Rep. No. 101-484 at 4 (1990), and therefore exactly what Congress was seeking to protect regardless of their mix of physical delivery and "financial" components. In re Borden Chem., 336 B.R. at 221. Given the intrinsic hedging element and the risk-shifting nature of the NGD contracts at issue – both financial characteristics – the NGD forward agreements are precisely what the BAPCPA Congress intended to protect when it drafted the new, expanded "swap agreement" definition.

This distinction between protected physically-settled commodity forwards with embedded hedging attributes and the kinds of contracts not intended to be

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[13] The contracts at issue had a periodically fixed, forward price, vividly illustrating the hedging function, See Memorandum in Support of Motion to Dismiss at Ex. A, J.A. 120.

within the Code safe harbors is supported by the recent legislative history of a Bankruptcy Code development effected by the 2006 Revising Act. In the 2006 Revising Act, Congress added "spot commodity contracts" to the list of agreements specifically safe-harbored as swap agreements. Spot commodity contracts are short-term contracts that always result in delivery of an underlying commodity, often to end-users. [14] Congress made a distinction between these spot contracts eligible for the safe harbor and "ordinary sales of goods" that are not eligible.[15] This distinction is reminiscent of that between safe-harbored swap agreements and "traditional commercial arrangements" dressed up as swap agreements, as referenced in the BAPCPA legislative history. See H.R. Rep. 109-

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14 In Wall Street Words, "spot market" is defined with a cross-reference to "cash market." "Cash market" is then defined as "[t]he market in which trades are made for the immediate sale or purchase of a particular item. Cash market is commonly used in commodities trading to differentiate transactions involving immediate or nearly immediate delivery from transactions requiring delivery at a future time." David L. Scott, Wall Street Words 55 (3rd ed. 2003).

15 We suggest that this eligibility, easily ascertained as intrinsic in forward contracts and forward agreements in their hedging characteristics, see In re Olympic, 294 F.3d at 740-41, can also be established in spot commodity contracts, for example, by reference to the size of the contract and the parties, nature of the commodity, relation of contract and parties to financial and commodities markets, and in some cases, hedging function. This Court, of course, does not need to decide in this case the relevant distinctions between, for example, a steel mill's spot purchases of coal in rail car lots and an individual's purchase of a pair of shoes. We suggest, however, that distinctions can be made in view of the overall purpose of the Bankruptcy Code safe harbors.

31 Pt. 1 at 122. This distinction also highlights Congressional differentiation of agreements to be protected, as it were, "for the sake of the markets" and those of a type to be left unprotected.

Besides the textual legislative history, the developmental legislative history of the definition of "swap agreement" offers further guidance which the Bankruptcy Court simply misreads. Although the Bankruptcy Court observes the massive expansion of types of agreements specifically enumerated as safe-harbored under clause (A)(i) of the BAPCPA definition of "swap agreement", the Bankruptcy Court (ignoring "precious metals agreements," see 11 U.S.C. § 101(53B)(A)(i)(II), and the 2006 Revising Act's addition of spot commodity contracts (described above)) declares that Congress "was focused on financial instruments that are themselves regularly the subject of trading." In re Nat'l Gas Distrib., 369 B.R. at 898-99.

To support this assertion, the Bankruptcy Court mistakenly reads the second clause of the Code definition of "swap agreement" into the first. The Bankruptcy Court does so even as it recognizes that clause (A)(ii) was intended to clarify the "other similar agreement" catch-all that existed in unelaborated form following the list of specifically safe-harbored agreements in the pre-BAPCPA definition. However, the Bankruptcy Court nonetheless mistakenly applies the clause (A)(ii) "subject to recurrent dealings in the swap market" test to the clause (A)(i) term

"forward agreement."[16] To do so destroys the meaning of the separate clauses of the Bankruptcy Code definition of "swap agreement" and allows the (A)(ii) catch-all clause to swallow the larger, specific substance of the definition. In short, the Bankruptcy Court's reading renders clause (A) nonsense and flies in the face of the Supreme Court's clear instruction to read statutes so as to avoid an absurd result. See e.g., Johnson v. U.S., 529 U.S. 694, 707 (2000) ("[N]othing is better settled, than that statutes should receive a sensible construction, such as will effectuate the legislative intention, and, if possible, so as to avoid an unjust or an absurd conclusion.") (citations omitted); State ex. rel. Stern Brothers & Co. v. Stilley, 337 S.W.2d 934, 939 (Mo. 1960) ("The basic rule of statutory construction is to first seek the legislative intention, and effectuate it if possible, and the law favors constructions which harmonize with reason, and which tend to avoid unjust, absurd, unreasonable or confiscatory results, or oppression"). [17]

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16 The Bankruptcy Court also mistakenly characterizes the clause A(ii) catch-all's recurrent dealing test as a test of whether the contract has been traded, as opposed to being one of a tradeable type. Although it would be erroneous to apply clause (A)(ii) to an (A)(i) contract, this standard document is used with great frequency in natural gas trading, as the full name of the NAESB Base Contract would imply.

17 The 2006 Act changed the catch all provision, Section 101(53B)(A)(ii), to include transactions "of [the] type that has been . . . the subject of recurrent dealings in the swap *or other derivatives markets* . . . . " 11 U.S.C. § 101(53A)(A)(ii) (emphasis added). This reference clearly extends to the forward markets.

CONCLUSION

The Bankruptcy Court spent much time in its opinions considering the early legislative history from 1990, but unfortunately less time with the legislative and developmental history accompanying the more recent development of the Bankruptcy Code safe harbors. As Congress said when considering an earlier version of the BAPCPA:

> [I]t has been more than ten years since the last legislative update to the safe-harbor provisions. The financial markets have evolved during that time in ways that leave various transactions and parties subject to legal uncertainty. As a greater variety of market participants engage in a broader range of transactions, statutory inconsistencies have surfaced that make it difficult to conclude that Congress's goal of minimizing systemic risk has been fully achieved through the existing market safe harbors. H.R. 2120 contains important technical corrections that are needed to minimize systemic risk in light of market developments.

Financial Contracts Bankruptcy Reform Act of 2003, H.R. Rep. 108-277 Part 1.[18] The BAPCPA amendments reflect Congressional awareness of the diversification of markets and the roles of market participants, and the need to avoid systemic risk stretching across those markets. Why else would the 2006 Revising Act definition of "swap agreement" now span such a diverse range of agreements, from interest rate swaps to spot commodity contracts? The Bankruptcy Court, by contrast, failed

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[18] Awareness of the importance of protecting against systemic risk also was a factor motivating the Olympic decision, In re Olympic, 294 F.3d at 742 n.5, as discussed above.

to share this Congressional awareness and illustrated how far it strayed when it flatly stated that the Bankruptcy Code definition of "swap agreement" does not include contracts between a seller and an end-user for delivery of a product that happens to be a recognized commodity. In re Nat'l Gas Distrib., 369 B.R. at 899. The addition of spot commodity contracts, however, makes it clear that this statement is not true. The addition of "spot" also makes it clear that the inclusion of a contract type in clause (A)(i) of the Bankruptcy Code definition of "swap agreement" does not require that the contract be of a type traded in any particular market or be cash-settled. Rather it has to be of a type, like the contracts in this case, that generically should be protected to prevent the systemic risk across interrelated markets that was of concern to Congress. See Michael H. Krimminger, Adjusting the Rules: What Bankruptcy Reform Will Mean for Financial Markets Contracts, available at http://www.fdic.gov/bank/analytical/fyi/2005/101105fyi.html.

ISDA respectfully submits that a decision consistent with the express language of the Bankruptcy Code and Congressional intent is needed to maintain market stability and confidence in the amended safe harbor provisions.

ISDA respectfully submits that for the foregoing reasons the Bankruptcy Court's opinion should be reversed.

Dated: New York, NY
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CERTIFICATE OF COMPLIANCE

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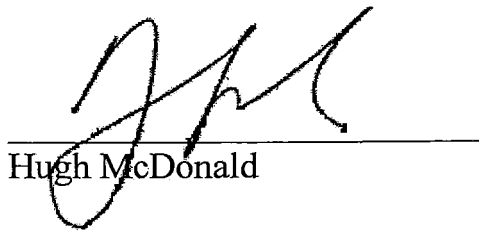

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I hereby certify that on this 30th day of January, 2008, I filed with the Clerk's Office of the United States Court of Appeals for the Fourth Circuit, via Hand Delivery, the required number of copies of this Brief of Amicus Curiae, and further certify that I served, via U.S. Mail, postage prepaid, the required number of said brief to the following:

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