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ENERGY/BANKRUPTCY ALERT

COMPETITIVE SUPPLIERS - BANKRUPTCY PRIORITY FOR ELECTRICITY

Recently, the United States District Court for the Southern District of New York issued a decision that could have far-reaching implications in bankruptcy cases for competitive suppliers.

The key issue is whether (or not) electricity is a "good" for purposes of the Bankruptcy Code. If it is a "good," competitive suppliers are entitled to administrative priority claim for electricity sold to and received by the debtor within 20 days of its bankruptcy filing.

This decision does not fully resolve the debate, but it is sure to be cited in other forums and jurisdictions. Here's what happened.

- Hudson Energy Services, LLC ("Hudson") was the energy service company ("ESCO") for The Great Atlantic and Pacific Tea Company, Inc., better known as "A&P."

- A&P filed for bankruptcy protection in December 2010.

- In April 2012, Hudson filed an administrative claim seeking payment of over $875,000 for electricity provided to A&P during the twenty days prior to its bankruptcy filing.

- A&P objected to Hudson's claim on the basis that the electricity did not qualify as "goods" under Section 503(b)(9) of the Bankruptcy Code, which confers administrative priority over general unsecured claims on claims for "the value of any goods received by the debtor within 20 days before the date of the commencement of a case under this title in which the goods have been sold to the debtor in the ordinary course of such debtor's business."

- In August 2012, the Bankruptcy Court denied Hudson's claim. In doing so, the Bankruptcy Court concluded that electricity did not "clearly fall" within the definition of "goods" under Section 503(b)(9).

- Hudson appealed, and the U.S. District Court for the Southern District of New York vacated the Bankruptcy Court's order and remanded for further fact-finding. 498 B.R. 19, 29-31 (S.D.N.Y. 2013). Simply put, that decision concluded that there was a lack of record evidence about the nature of electricity.

- On remand, the Bankruptcy Court held a hearing at which both sides presented expert testimony. In November 2014, the Bankruptcy Court again denied Hudson's claim.

    - It recognized that neither the bankruptcy court nor the district court actually held flat out that electricity was not a "good." It looked at the evidence, and concluded that under the facts presented, electricity did not qualify as a good

under Section 503(b)(9) since by the time an electricity meter registers a reading, the electricity has already been used and is therefore no longer moving.

- In the alternative, the Bankruptcy Court found that given the "metaphysical" and "ultimately unresolvable nature of this dispute," the principle that administrative priority claims should be narrowly construed dictated that Hudson's claim should be denied.

- Hudson filed an appeal. This time the U.S. District Court ruled that the Bankruptcy Court did not make an error. 2015 U.S. Dist. LEXIS 129049 (September 24, 2015).

  - The District Court did not decide the issue of whether electricity was a good, and did not take up the issue. In an non-binding opinion, the District Court agreed with the Bankruptcy Court that under the facts presented, electricity does not so qualify as a good under Section 503(b)(9).

  - However, the District Court also agreed that Hudson's claim could be denied, relying on the principle of narrow construction. The District Court concluded, that based on the record, it was not clear if electricity fell within the ambit of the Section 503(b)(9). Faced with such uncertainty, the Court narrowly construed the statute so as to exclude electricity.

- Hudson has not indicated if it will appeal the decision of the District Court.

This lengthy litigation serves as a reminder that competitive suppliers need to understand bankruptcy law and the steps needed to protect themselves in the event of a customer bankruptcy.

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