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FERC 'Single Entity' Ruling Increases Successor Liability Risk

By **Mark Williams, Edwin Smith and J. Daniel Skees** (August 1, 2019, 1:34 PM EDT)

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When a business entity that is regulated by the Federal Energy Regulatory Commission is closely related to another business entity, FERC takes the position that under some circumstances it may treat the two different legal entities as if they were one single entity.[1] FERC ruled recently that it "may disregard the corporate form in the interest of public convenience, fairness, or equity" and "[t]his principle of allowing agencies to disregard corporate form is flexible and practical in nature."[2]

As a result, a new power marketer could be barred by a regional transmission organization from participating in the market unless it paid off the debts to the RTO owed by another power marketer with the same business objectives and the same contacts and administrators as the bankrupt entity. This decision could make it difficult for public utilities to avoid the debts of their bankrupt affiliates, which could be attributed to the entire enterprise regardless of the final plan of bankruptcy, including the liquidation of the bankrupt entity.

When a debtor in bankruptcy is liquidated, or successfully emerges from bankruptcy, certain unsatisfied, unsecured pre-bankruptcy debts of that bankrupt debtor are discharged. The discharge functions as a defense by the debtor against the claims of the debtor's creditors.

Similarly, when a debtor in bankruptcy is affiliated (such as by common upstream ownership) with a nonbankrupt entity, the nonbankrupt affiliate is typically not presumed to be responsible for that bankrupt debtor's unsatisfied obligations, unless some statutory, contractual or security arrangement makes the nonbankrupt affiliate liable for those obligations, or one entity is viewed to be the "alter ego" of the other under applicable state law.

In a June 20, 2019, order, FERC stepped into this plain inconsistency. FERC deemed two entities to be a single entity and entirely disregarded corporate form in the process, even though a debtor's bankruptcy is particular to that debtor and ultimately will result in the discharge of certain unsatisfied obligations without recourse to the debtor's nonbankrupt affiliates under other applicable law.

This application of FERC's single entity theory allowed FERC to rule that the New York Independent System Operator Corp.'s FERC-filed tariff enables the NYISO to deem the bankrupt North Energy Power LLC to be the same legal person, for FERC purposes, as North EP's affiliate Light Power & Gas of NY LLC. Only when a theory of successor liability applies under relevant state law can the nonbankrupt entity be forced to succeed to the exposure of the bankrupt affiliate — but in LPGNY, FERC identified no theory of successor liability, and in fact explicitly refused to consider successor liability in its ruling.[3]

The Light Power Application and Complaint

In November 2018, Light Power submitted an application to the NYISO, seeking to participate in the NYISO-administered electricity market. Within New York, the NYISO is the exclusive wholesale capacity and energy market, and the NYISO functions as New York's sole transmission and wholesale market. Any NYISO refusal to accept Light Power's application would have the effect of excluding Light Power from doing business in the electric sector in New York.

In December 2018, NYISO did just that. NYISO declined to admit Light Power to the NYISO market unless and until North EP satisfied certain asserted financial obligations to the NYISO, and indicated that it would hold Light Power's application in "abeyance" until that time. North EP's sole electricity supplier had declared bankruptcy during August 2018, and North EP itself had then declared bankruptcy in September 2018 — two months before Light Power applied for admission to the NYISO's markets.

In January 2019, Light Power filed a complaint against the NYISO with FERC. Light Power asserted that:

- NYISO violated its own tariff by holding LPGNY's registration application in abeyance pending payment by North Energy of its outstanding and unpaid obligations to NYISO;
- NYISO unreasonably, unlawfully and unduly discriminated against LPGNY by refusing to process its application for registration based on an unwritten successor liability policy;
- NYISO violated the Federal Power Act by failing to include its unwritten successor liability policy in its filed OATT;
- Any determination of successor liability should be made by a court, not NYISO; and
- NYISO failed to follow relevant provisions of its own tariff relating to defaulting customers.[4]

FERC Proceedings and Order

The NYISO vigorously defended against the complaint, and was joined by several intervening parties.[5] The NYISO claimed that Light Power was a "shell company" that was only created once North EP filed for bankruptcy, and that Light Power's owners were attempting to skirt North EP's debt obligations to NYISO and reenter NYISO's markets without settling these obligations.

The NYISO claimed that the ownership, operation and control of North EP and Light Power exhibited a close factual overlap, and that FERC should disregard what amounted to a changed corporate form only, so as to cause Light Power and North EP to be treated as if they were the same, single entity.[6] Doing otherwise, the NYISO asserted, would produce "unfair, unusual, absurd or improbable results." NYISO also claimed that the concept of holding successors accountable for an obligation of their predecessors is consistent with NYISO's "overall tariff framework."[7]

Following a number of rounds of pleadings, FERC dismissed the complaint, affording no relief to Light Power. FERC explicitly refused to rule on the complaint's assertion that the NYISO had inappropriately applied a successor liability theory, and instead relied on the optical similarities between the defaulted, bankrupt North EP entity and the new Light Power entity:

> NYISO's decision to treat LPGNY as the same entity as North Energy is reasonable in light of the record, particularly the close overlap in not only those entities' relevant personnel, but also their business activities. Namely, both entities have the same contacts and administrators, similar addresses, are engaged in the same business in the same territory, and seek to serve the same customers.[8]

These similarities, FERC concluded, were sufficient to cause Light Power and North EP to be deemed a single entity.

FERC's Single Entity Theory, and What Could Come Next

FERC has described its single entity theory as follows:

The general rule applicable to our determination is that an agency may disregard the corporate form in the interest of public convenience, fairness, or equity. This principle of allowing agencies to disregard corporate forms is flexible and practical in nature. Corporations may be regarded as one entity for the purposes with which the agency is immediately concerned even though they are legitimately distinct for other purposes. Moreover, no bad intention on the part of the corporations is necessary; the inquiry is simply a question of whether the statutory purposes would be frustrated by the corporate form.[9]

LPGNY does not address a number of significant issues that arise in the specific context of bankruptcy.

For example, if FERC deems a nonbankrupt entity (such as Light Power) to be a "single entity" that is inseparable from the corporate existence of a bankrupt entity (such as North EP), it is difficult to understand how certain claims or formal actions against the solvent entity would not also be a claim against the bankrupt entity, in violation of the automatic stay in bankruptcy.

By contrast, if the bankrupt entity's bankruptcy has been terminated by a reorganization or liquidation that discharged the unsatisfied debts of the debtor in bankruptcy, then the LPGNY order effectively authorizes the NYISO to assert a discharged claim against a reorganized debtor. Or, if the bankrupt entity has been liquidated, the LPGNY order authorizes a wound-up entity to be deemed the same entity as a continuing, separate entity. Neither of these results is consistent with corporate, partnership or other applicable law that creates limited and separate liability shields under state law.

FERC's application of its single entity theory under these circumstances could affect every holding company of utilities, generators, marketers or other FERC-regulated entities. The LPGNY order would be on more familiar legal territory had FERC found that Light Power was the successor entity to North EP, or had FERC determined that Light Power and North EP were exposed to successor liability. However, FERC did not do so.

It did not find that under the Federal Power Act, Light Power was an "affiliate" of North EP; it merely found that Light Power and North EP exhibited a list of common business characteristics, but it did not expressly declare any findings with respect to actual ownership. Since no assets (such as customer contracts, or a supplier contract) were transferred from North EP to Light Power, and the only supply-

side "asset" belonging to North EP was a single power sale contract with a separate bankrupt entity that ceased to exhibit value prior to Light Power's formation,[10] it appears that some customary theory of successor liability would not apply or be available.

Holding company systems that participate in FERC-regulated organized markets should take care to consider whether the LPGNY order could impede their business planning, and could be harmful to their organization and wind-up of special-purpose subsidiaries. The parent company of an inactive or wound-up subsidiary often will place the subsidiary in bankruptcy in order to prevent the risk, surprise and disruption of some sudden claim arising after the subsidiary has ceased doing business.

The LPGNY order, if it is not appealed and if it survives intact, suggests that FERC will allow regional market entities to generally pursue the affiliates of a defaulting market participant (whether or not the defaulting participant is a debtor bankruptcy) under a single entity theory, even if tariffs do not otherwise express this claimed right, and even if principles of state law successor liability are not satisfied and would be inconsistent with FERC's single entity result.

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[1] Light Power & Gas of NY LLC v. New York Independent System Operator Inc., Order Denying Complaint, Docket No. EL19-39-000, 167 FERC ¶ 61,232 (June 20, 2019) (LPGNY).

[2] Town of Highlands v. Nantahala Power & Light Co., 37 FERC ¶ 61,149 at 61,356 (1986).

[3] LPGNY at P 40. It is doubtful, based on the record before FERC in LPGNY, whether LPGNY had been a party to a de facto merger with its affiliate, since a de facto merger typically requires a transfer of assets to the surviving entity, and no such transfer took place. See Searchay v. NTS Fort Lauderdale Office Joint Venture, 707 So.2d 958, 960 (Fla. Ct. App. 1998); see also Perimeter Realty v. GAPI Inc., 533 S.E.2d 136, 145-46 (Ga. Ct. App. 2000); Myers v. Putzmeiser Inc., 596 N.E.2d 754, 756 (Ill. Ct. App. 1992); Turner v. Bituminous Cas. Co., 244 N.W.2d 873, 891 (Mich. 1976); Howell v. Atlantic-Meeco Inc., 2002 WL 857685 at * 3 (Ohio Ct. App. 2002); CAB-TEK Inc. v. E.B.M. Inc., 571 A.2d 671, 672 (Vt. 1990). Some courts include, in a similar theory of "continuing enterprise," a requirement that the deemed continued enterprise would hold itself out as a continuation of the former entity; see Asher v. KCS Int'l Inc., 659 So. 2d 598, 599-600 (Ala. 1995) and Foster v. Cone-Blanchard Mach. Co., 597 N.W.2d 506, 510 (Mich. 1999). But the LPGNY order sets forth no information to the effect that Light Power did so.

[4] LPGNY at P 7.

[5] PJM Interconnection LLC, the New York transmission-owning utilities and the Maryland Public Service Commission.

[6] LPGNY at PP 15-18.

[7] LPGNY at P 19, 22 (internal citations omitted).

[8] LPGNY at P 41.

[9] LPGNY at P 40, citing Town of Highlands v. Nantahala Power & Light Co., 37 FERC ¶ 61,149 at 61,356 (1986) (footnotes omitted), reh'g denied, 38 FERC ¶ 61,052 (1987), aff'd sub nom. Nantahala Power & Light Co. v. FERC, 840 F.2d 11 (4th Cir. 1988); see also Transcontinental Gas Pipe Line Corp., 58 FERC ¶ 61,023, at 61,045 (1992), aff'd sub nom. Transcontinental Gas Pipe Line Corp. v. FERC, 998 F.2d 1313, 1320-1321 (5th Cir. 1993).

[10] LPGNY at P 3.