



The New Buzz! Sale of Electricity May Get Priority Status in Bankruptcy

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In a case of first impression, a bankruptcy court in Massachusetts has held that electricity sold by a supplier may be considered "goods" and that the supplier's payment claim is entitled to priority status under Section 503(b)(9) of the Bankruptcy Code. Shocking to some! *In re Erving Indus. Inc.*, 2010 Bank. LEXIS 1069 (Bank. D. Mass. Apr. 7, 2010).

The specific status given to creditor claims can lead to high stakes since those selling "goods" with a priority claim will generally be paid in full before any unsecured creditors or equity holders see any payments.

Section 503(b)(9) of the Bankruptcy Code grants creditors an administrative priority claim against the bankruptcy estate for the value of goods sold to the debtor in the ordinary course of business within 20 days prior to the commencement of the case.

In *Erving*, the court found that the sale of electricity could be considered a sale of "goods" for purposes of bankruptcy law and under section 2-105(1) of the model Uniform Commercial Code. The creditor, Constellation NewEnergy, Inc., filed a priority administrative claim under Section 503(b)(9) in the amount of approximately \$280,000 with respect to "goods" delivered to the debtor, Erving Industries, Inc., and its affiliates within the 20-day window before the bankruptcy filing. Erving objected to the priority claim status by asserting, among other things, that supplying electrical energy is a "service," not a "good." Erving invoked several references to services in the contract with Constellation and also raised the predominant factor test, which addresses the sale of mixed goods and services. Finally, Erving stated that Constellation's status as a utility automatically prohibits the priority status as a matter of law.

In response, Constellation argued that it had no role in the delivery or service of electricity and argued that "goods" should be interpreted in accordance with the definition in the UCC. Section 2-105 of the UCC defines "goods" as "things that are moveable at the time they are identified to the contract for sale."

The *Erving* court allowed Constellation's claims as a priority claim. The court found that Constellation was a "competitive supplier" that contracted with electricity generators to buy electricity and then sell them to customers under separate contract. Constellation was not a utility, rather, it purchased electricity from electricity generators under contracts and then sold such electricity under contract to end users such as Erving who agreed as part of the transaction to arrange for the utility to transport/deliver the electricity to Erving. Constellation was not merely providing a service since it was in the specific business of selling electricity that was independently generated. Electricity was found to be a good that was tangible and capable of being created, measured and stored. It was not similar to telecommunication signals (like the internet, radio or television) which the court called services since they were simply means of transmitting non-good intellectual property such as ideas, sounds, images, music, and other content.

Of significance in determining that Constellation sold (rather than serviced) electricity was the fact that it was not classified as a "utility" in Massachusetts and was not subject to regulatory restrictions. Further, its agreement with Erving consistently referred to the "purchase" and "sale" of electricity. It is however important to note that not all courts are in agreement. For example, *In re Pilgrim's Pride Corp.*, 421 B.R. 231 (Bankr. N.D. Tex. 2009) the court concluded that electricity does not come within the definition of "good" for purposes of determining whether a seller is entitled to a priority claim under § 503(b)(9), but did hold that natural gas was a "good."

The Ninth Circuit, which includes California, has not ruled on this specific issue, however, the District Court in *In re Pac. Gas & Elec. Co.*, 271 B.R. 626, 638-40 (N.D. Cal. 2002) held that electricity was a "good" in other contexts not involving the § 503(b)(9) administrative claim priority analysis. Since many suppliers/creditors, do not "bifurcate" or bill their customers separately for the sale of their goods and the service with respect to such goods, it is unclear how courts will address future claims under section 503(b)(9) of the Bankruptcy Code. However, Erving certainly provides more support for the position that electricity (like other commodities such as oil and gas) may in fact be a good for purposes of asserting a priority claim in a bankruptcy case.

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