

Electricity Not a Good for Administrative Priority Claims

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Is electricity a good for purposes of establishing an administrative priority claim under Section 503(b)(9) of the U.S. Bankruptcy Code? That is the question that U.S. Bankruptcy Judge Christopher Sontchi of the District of Delaware answers in *In re NE Opco*, Case No. 13-11483 (CSS) (Bankr. D. Del. Nov. 1, 2013). Faced with a split in authority from other jurisdictions and no written opinions on the subject in the U.S. Court of Appeals for the Third Circuit, Sontchi, in a fascinating opinion, holds that electricity is not a good for purposes of Section 503(b)(9).

The *NE Opco* case involved a utility provider's claim for administrative priority status for electricity and natural gas it delivered to the debtors in the weeks before they filed for bankruptcy. Section 503(b)(9) provides for the allowance of an administrative priority claim if the claimant establishes: (1) the claimant sold goods to the debtor; (2) the goods were received by the debtor within 20 days prior to filing; and (3) the goods were sold to the debtor in the ordinary course of business. There was no dispute that the utility delivered electricity to the debtors in the ordinary course of business within the 20-day period. The parties' disagreement concerned whether electricity is a good for purposes of Section 503(b)(9).

The Bankruptcy Code does not define the term "goods," but the courts have previously adopted the definition of "goods" set forth in Article 2 of the Uniform Commercial Code for this purpose. UCC Section 2-105 states that goods are "all things (including specially manufactured goods) that are movable at the time of identification to the contract for sale." The bankruptcy court found that there is a split in authority among the courts regarding whether electricity is a good under Section 2-105 of the UCC and Section 503(b)(9) of the Bankruptcy Code. A leading case that held electricity is a good is *In re Erving Industries*, 432 B.R. 354 (Bankr. D. Mass. 2010). The court there found that electricity is a "thing" because it is tangible and possesses physical properties; it is not simply an "idea" like intellectual property. It can be felt, measured and stored. The *Erving* court also found that electricity is moveable as it travels through transmission lines from its origin to the ultimate user, and "identifiable" as it is measured on a meter

when it is delivered to the customer. The critical question, however, was whether electricity is moveable at the time it is identified to the contract—when it passes through the meter to the customer. The *Erving* court said that it was, because the electricity does not pass through the meter and then cease to exist. "Logic dictates" that some period of time, however short, must elapse between the measurement of the electricity at the meter and its ultimate consumption by the customer, the court said. Since electricity is moveable and identifiable prior to its consumption, it meets the UCC definition of a good.

Sontchi expressly rejects this argument in *NE Opco*. He observes that the *Erving* court based its conclusion on the fact that electricity is not identified on the meter and consumed by the customer simultaneously: Some "infinitesimal period of time" elapses between identification and use and it is that period of time that makes electricity a good. While Sontchi agrees that there must be a period of time between when electricity is identified and consumed for it to be a good within the meaning of the UCC, he said that this period must be "meaningful," which is not the case with electricity. At this point, Sontchi journeys deep into the physics of electricity. Electricity, he notes, travels at the speed of light in a vacuum and at two-thirds the speed of light through coaxial cable. This is one kilometer in 4.978 microseconds. Thus, the time that elapses between identification and consumption is so infinitesimal as to be meaningless. "Under the plain meaning of Section 503(b)(9) of the Bankruptcy Code, electricity is not movable at identification and, thus, is not a good because there is not a meaningful delay between identification and consumption," the opinion said. For that reason alone, he concludes, electricity is not a good for purposes of establishing an administrative priority claim under Section 503(b)(9).

Sontchi proceeds to consider other arguments that courts have advanced in determining whether electricity is a good. Some courts argue that electricity is comparable to other things that are goods under the UCC, such as water and natural gas. But water and natural gas, unlike electricity, fall within the plain meaning of the definition of goods in the UCC. Moreover, water and natural gas can be identified well before consumption; both can be stored for an indefinite period of time. The same is not true of electricity. Water and natural gas stored in a tank remain as water and natural gas, while electricity stored in a battery is not electricity: It is transformed into potential energy that is stored in materials or chemicals that will generate electricity when they react with each other.

Sontchi also considers whether other provisions in the Bankruptcy Code are relevant in determining whether electricity is a good. Other courts considered whether goods under Section 503(b)(9) are limited to those that can be stockpiled and reclaimed under Section 546(c) of the Bankruptcy Code, or whether Section 366 of the Bankruptcy Code governing "utility services" controls whether electricity is a good or a service. Sontchi concludes that both sections are irrelevant for purposes of determining whether electricity is a good under Section 503(b)(9). These other provisions have distinct purposes not related to Section 503(b)(9). For example, while certain goods are subject to reclamation under Section 546(c), other non-reclaimable goods are also entitled to administrative expense priority. Similarly, the fact that Section 366 uses the terms "service" and "utility service" does not control whether something is a service or a good under the UCC and, by extension, under Section 503(b)(9). Sontchi also concludes that the nature of the parties' relationship—whether the claimant is acting as a "public utility" or not—is problematic and irrelevant in determining whether electricity is a good. Finally, Sontchi rejects the argument that the result should be affected by strict construction of Section 503(b)(9) because it provides

an otherwise unsecured creditor with an administrative claim. The court, he said, should simply apply the law as written and not put a judicially created obstacle in the path of an administrative expense claimant.

The decision in the *NE Opco* case is important for those who represent utility companies seeking to assert an administrative expense claim in a bankruptcy proceeding for electricity provided in the weeks before the bankruptcy and for those who represent the debtors in those proceedings. The issue is likely to recur, since it is hard to imagine a case where the debtor did not purchase electricity in the 20-day period prior to the bankruptcy petition. But just as Sontchi concludes that whether electricity is a good rises or falls on the nature of electricity "in and of itself," the decision in *NE Opco*, and the court's analysis of the issue in the face of a split in authority, the absence of binding precedent, and the presence of complex scientific and technical facts, is interesting "in and of itself."

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