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FROM THE EDITOR

New Section 366 of the Bankruptcy Code

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Effective for new bankruptcy cases filed on or after October 17, 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (Act) revises many parts of the U.S. Bankruptcy Code (Code). This article analyzes significant changes to 11 U.S.C. § 366 (Section 366) – the only section of the Code and the Act addressed solely to utilities (neither defines "utility").

In general, the Act added subsection (c) to Section 366. As amended, Section 366 states:

> *(a) Except as provided in subsections (b) and (c) of this section, a utility may not alter, refuse, or discontinue service to, or discriminate against, the trustee or the debtor solely on the basis of the commencement of a case under this title or that a debt owed by the debtor to such utility for service rendered before the order for relief was not paid when due.*
>
> *(b) Such utility may alter, refuse, or discontinue service if neither the trustee nor the debtor, within 20 days after the date of the order for relief, furnishes adequate assurance of payment, in the form of a deposit or other security, for service after such date. On request of a party in interest and after notice and a hearing, the court may order reasonable modification of the amount of the deposit or other security necessary to provide adequate assurance of payment.*
>
> *(c)(1)(A) For purposes of this subsection, the term 'assurance of payment' means (i) a cash deposit; (ii) a letter of credit; (iii) a certificate of deposit; (iv) a surety bond; (v) a prepayment of utility consumption; or (vi) another form of security that is mutually agreed on between the utility and the debtor or the trustee. (B) For the purposes of this subsection an administrative expense priority shall not constitute an assurance of payment.*
>
> *(2) Subject to paragraphs (3) and (4), with respect to a case filed under chapter 11, a utility referred to in subsection (a) may alter, refuse, or discontinue utility service, if during the 30-day period beginning on the date of the filing of the petition, the utility does not receive from the debtor or the trustee adequate assurance of payment for utility service that is satisfactory to the utility.*
>
> *(3)(A) On request of a party in interest and after notice and a hearing, the court may order modification of the amount of an assurance of payment under paragraph (2). (B) In making a determination under this paragraph whether an assurance of payment is adequate, the court may not consider (i) the absence of security before the date of the filing of the petition; (ii) the payment by the debtor of changes for utility service in a timely manner before the date of the filing of the petition; or*

Continued on Page 2

In This Issue

Recent Decisions

ANTITRUST; RESTRUCTURING *U.S. Court of Appeals for the 5th Circuit holds that filed rate doctrine prevents antitrust challenge to bid-based, wholesale market rates* 4

MISCELLANEOUS; TELECOMMUNICATIONS *U.S. Supreme Court upholds FCC's determination that cable modem service is an "information service" and not a "telecommunications service"* 5

CONSTITUTIONAL; CRIMINAL *Superior Court of New Jersey, Appellate Division holds that consumers have a reasonable expectation of privacy in electrical usage records and therefore are protected from warrantless searches* 6

TERRITORIAL; UTILITY *Supreme Court of Nebraska holds that city improperly annexed property located in utility's service territory* 7

PROPERTY; UTILITY *Court of Civil Appeals of Alabama holds that prescriptive electric easement did not authorize fiber optic cable* 8

Regulatory Watch

FEDERAL ENERGY REGULATORY COMMISSION *FERC orders cooperative to net meter* 9

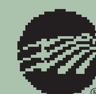
New Statutes

Ten states enact data breach notification laws 11

NEVADA 12

GEORGIA 12

MINNESOTA 12



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Bankruptcy Code *continued from page 1*

> *(iii) the availability of an administrative expense priority.*
> *(4) Notwithstanding any other provision of law, with respect to a case subject to this subsection, a utility may recover or set off against a security deposit provided to the utility by the debtor before the date of the filing of the petition without notice or order of the court.*

Overall, I predict that, in comparison with current practice under the Code, there may not be material differences in what is considered "adequate assurance of payment" for cases filed under chapters 7, 9, 12, 13, or 15 of the Act. In these cases, utilities only may receive small amounts of deposits or the like. However, for chapter 11 cases, if a utility aggressively protects its interests, then new Section 366(c)(2), and especially the language therein ("adequate assurance of payment for utility service that is satisfactory to the utility") creates hope that bankruptcy judges will be forced to award real adequate assurance to utilities.

Below, I have analyzed the "plain meaning" of amended Section 366. My analysis is based upon the directive of the U.S. Supreme Court as to how to analyze a bankruptcy statute. *In re* Henhouse Interstate, Inc., 530 U.S. 1, 6 (2000) ("Congress says in a statute what it means and means in a statute what it says there."). The legislative history behind amended Section 366, H. Rep. No. 109-31 (Part I), at 89, 109th Cong. 1st Sess. (April 8, 2005), *reprinted in* U.S.C.C.A.N. 88, 155 (June 2005), reports the key features of new Section 366(c) without elaboration into the reasons for passage thereof.

Amended Section 366 contains significant changes that appear to favor utilities. Under the Code, many bankruptcy judges have been deeming mere administrative expense priority, coupled with a directive that the debtor timely pay post-petition utility invoices, as constituting adequate assurance under Section 366(b). New Sections 366(c)(1)(B) and 366(c)(3)(B)(iii) prohibit this for all cases under the Act.

As listed above, new Section 366(c)(1)(A) defines adequate assurance of payment as meaning six alternatives, each of which is exclusive of the rest. If the options had been conjunctive through use of "and" instead of "or;" *i.e.*, the mutually agreeable requirement had been inserted into all of the other five options, then I definitely would be encouraged for utilities for all cases filed under the Act.

Except for chapter 11 cases, I predict that new Section 366(c)(1)(A) may be interpreted miserly by the bankruptcy courts. For instance, although this section defines adequate assurance as including a security deposit, it does not require bankruptcy judges to require a security deposit of substance. Thus, wherein a Chapter 7 case, a utility might request a security deposit of say $500.00, the judge may award a bare minimum, say $50.00.

My conclusion is based upon my personal experience in many contested Section 366 cases and my legal analysis of the reported Section 366 cases. While there are many cases where utilities were awarded security deposits ranging from one half (*See In re* Best Prod. Co., 203 B.R. 51 (Bankr. E.D. Va. 1996)) to two or more months of bills (*See In re* Spencer, 218 B.R. 290 (Bankr. W.D. N.Y.1998); *In re* Norsal Indus., Inc., 147 B.R. 85 (Bankr. N.D.N.Y. 1992); *In re* Smith, Richardson & Conroy, Inc., 50 B.R. 5 (Bankr. S.D. Fl. 1985); and *In re* Robmac, Inc., 8 B.R. 1 (Bankr. N.D. Ga. 1979) [this was consistent with pre-Code practice prior to 1978: *In re* Sec. Inv. Prop., Inc., 559 F.2d 1321 (5th Cir. 1977); and *In re* Chemical Lime Co., 24 F. Supp. 217 (M.D.Pa. 1938)]), or a reasonable commercial equivalent thereto (*i.e.*, an advanced payment, see *In re* Sharon Steel Co., 872 F.2d 36 (3rd Cir. 1989); *In re* Monroe Well Serv. Inc., 69 B.R. 58 (E.D. Pa. 1986); *In re* Marion Steel Co., 35 B.R. 188 (Bankr. N.D. Ohio 1983); and *In re* Hub of Mil. Circle, Inc., 19 B.R. 460 (Bankr. E.D. Va. 1982) [this was consistent with pre-Code practice: *In re* Penn Cent. Transp., 467 F.2d 100 (2nd Cir. 1972)]), the more recent large chapter 11 cases

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awarded no deposits (*See In re* Caldor, Inc., 117 F.3rd 646 (2nd Cir. 1997), *aff'g* 199 B.R. 1 (S.D. N.Y. 1996), and *In re* Adelphia Bus. Solutions, Inc., 280 B.R. 63 (Bankr. S.D. N.Y. 2002) (holding that adequate assurance can be mere administrative expense priority when coupled with meaningless, procedural relief; e.g., providing a contact person at the debtor to call about delinquent invoices), and a recent chapter 7/chapter 13 case (*In re* Steinebach, 303 B.R. 634 (Bankr. D. Az. 2004) (that was unusual; there, the judge analyzed the utility's practices in all cases pending before her)), made it impractical for the utility to assess post-petition security deposits.

New Section 366(c)(1)(B) prohibits administrative expense priority alone from being adequate assurance of payment. It is clear and leaves no wiggle room. Although new Section 366(c)(3)(B)(iii) prohibits administrative expense priority from being adequate of assurance of payment, this section applies only in a chapter 11 case. But that means nothing. In some Section 366 orders, bankruptcy judges, besides assessing no post-petition security deposits, also have not granted administrative expense priority for post-petition utility invoices.

New Section 366(c)(2) applies only to chapter 11 cases. In a chapter 11 case, the initial 20-day period in Section 366(b) banning termination of service has been expanded to 30 days. However, if by the end of the 30 days, the debtor has not furnished adequate assurance of payment that is satisfactory to the utility, or has not obtained a court order preventing the ban from lifting, then the utility may alter, refuse, or discontinue utility service to the debtor. Further, under new Section 366(c)(3)(B) (applicable only to chapter 11 cases), in deciding what is adequate assurance, a bankruptcy judge may not consider whether there was a pre-petition security deposit, the debtor timely paid its pre-petition utility invoices, or the availability of administrative expense priority. However, having experienced years of bankruptcy court orders favoring debtors and denying meaningful post-petition security deposits to utilities, I think that time will have to pass to see how bankruptcy judges interpret new Section 366(c).

Overall, I predict that, in comparison with current practice under the Code, there may not be material differences in what is considered "adequate assurance of payment" for cases filed under chapters 7, 9, 12, 13, or 15 of the Act.

Based upon past practice, a wise chapter 11 debtor may file a first day motion proposing a minor amount, e.g., a small security deposit for each utility or a small deposit for all utilities to be held in escrow. Unless a utility responds or objects timely, then the first day proposed order will take effect. Wise debtors know that, historically, many utilities have not responded to or participated in Section 366 motions.

On the other hand, use of "adequate assurance of payment for utility service that is satisfactory to the utility" in new Section 366(c)(2) cannot be ignored. That is why it will be important for a utility to participate actively in response to debtor-filed first day utility motions. For example, in a chapter 11 case, if a utility requests a security deposit equaling twice the debtor's average monthly bill, and if the utility actively participates in the case, then no bankruptcy judge reasonably could conclude that a cash deposit of significantly less will be "satisfactory to the utility." Even pro-debtor bankruptcy judges will have to award something meaningful and tangible, instead of a token deposit. But if the utility does not oppose a lower deposit, then the bankruptcy judge could say that he or she awarded the utility something other than administrative expense priority, and based upon the strength of the debtor in possession financing facility, there was no financial need to award any higher deposit.

Thus, in chapter 11 cases, if a utility participates and responds to first day utility motions under new Section 366, I envision favorable results and the assessment of meaningful post-petition deposits, surety bonds, or the like. Debtor-filed utility motions under amended Section 366 may require utilities to file objections with the bankruptcy courts, instead of permitting them to write letters requesting additional adequate assurances of payment, as is the common practice now. This will make it costlier for utilities to participate in chapter 11 cases.

Under new Section 366(c)(4), without a court order, a utility may setoff/recoup pre-petition security deposits. There is no question that this last provision will help utilities. I envision no room for a bankruptcy judge to disregard this provision and permit insertion in a first day Section 366 motion of an injunction prohibiting the setoff/recoupment of a pre-petition security deposit. This puts an end to cases like *In re* McMahon, 129 F.3d 93 (2nd Cir. 1997) (utility sued for setting off/recouping pre-petition security deposit against pre-petition debt without seeking prior bankruptcy court authorization; held, that since utility had right under applicable state regu-

Continued on page 4

Bankruptcy Code *continued from page 3*

lations to apply security deposit against unpaid charges, it could setoff/recoup without prior bankruptcy court authorization).

My prediction as to how amended Section 366 will be interpreted by bankruptcy judges is favorable, albeit limited to chapter 11 cases in which a utility actively participates before the bankruptcy courts. Other than small amounts proffered in debtor-filed utility motions, do not expect meaningful post-petition security deposits being assessed. Utilities who do not participate actively or respond to debtor-filed utility motions will receive just the superficial relief that wise debtors may propose in such motions. If you have any questions or comments, please contact me at 215-321-6909 or ghamberg@verizon.net.

Recent Decisions

ANTITRUST; RESTRUCTURING

U.S. Court of Appeals for the 5th Circuit holds that filed rate doctrine prevents antitrust challenge to bid-based, wholesale market rates

On June 17, 2005, the U.S. Court of Appeals for the 5th Circuit (Court) held that the filed rate doctrine prevented Texas Commercial Energy, a retail provider of electric energy (Retailer), from claiming that anticompetitive actions by TXU Energy, Inc., a generator of electric energy (Generator), increased the price of electric energy in a bid-based, wholesale market and violated state and federal antitrust law. **Tex. Commercial Energy v. TXU Energy, Inc., No. 04-40962, 2005 U.S. App. LEXIS 11553 (5th Cir. June 17, 2005)**.

In 1999, Texas amended its Public Utility Regulatory Act (Act) and "deregulated" its electric energy market. Retailer purchases short-term electric energy through the Balancing Energy Service, a bid-based wholesale market (Market) administered by the Electric Reliability Council of Texas (ERCOT). During "severe winter weather" in February 2003, the Market price for electric energy "soared." After paying "considerably higher sums" for electric energy, Retailer alleged that Generator used its control of 75 to 99 percent of the Market to "purposefully withhold" electric energy from the Market and increase the price.

Unsatisfied with ERCOT's attempts to address the situation, Retailer sued ERCOT and 24 Market participants, including Generator and its subsidiaries (Defendants). Among other things, Retailer alleged that Defendants violated state and federal antitrust law. The district court dismissed Retailer's antitrust claims under the filed rate doctrine, a doctrine which prevents a ratepayer from judicially challenging a rate approved by a governing regulatory agency. Retailer appealed.

Noting that the Act does not "confer immunity from state or federal antitrust laws," Retailer first argued that applying the filed rate doctrine confers immunity on Defendants and violates the Act. Disagreeing, the Court explained that the U.S. Supreme Court has held that the filed rate doctrine is "far different" from antitrust immunity. For instance, regulated entities that act anticompetitively under the filed rate doctrine remain subject to antitrust scrutiny by the government. Further, the filed rate doctrine defense is "part of current federal antitrust law" and complies with the Act's intent to "complement other state and federal antitrust provisions." In addition, the Court concluded that the filed rate doctrine "applies with equal force" to Retailer's state antitrust claims.

Observing that the Act does not require Market rates to be filed with the Public Utility Commission of Texas (Commission), and that the Commission does not set or approve these rates, Retailer next argued that the filed rate doctrine does not apply. Disagreeing, the Court noted that the Act required the Commission to ensure "safe, reliable, and reasonably priced electricity." Likewise, the Commission must ensure "that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices with terms and conditions that are not unreasonably preferential, prejudicial, discriminatory, predatory, or anticompetitive." In addition, the Commission requires certain market power information and mitigation plans. Agreeing with the approach taken by other circuits addressing rates filed with the Federal Energy Regulatory Commission, the Court held that the Commission's Market oversight was sufficient to conclude that Market rates were "filed" under the filed rate doctrine.

Asserting that the "competitor exception" to the filed rate doctrine allows a competitor, as opposed to a