

TOP BANKRUPTCY LAWYERS 2022



FERC CANNOT USURP BANKRUPTCY COURT'S POWER OVER CONTRACT REJECTION

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In *Gulfport Energy Corp. v. FERC*, No. 21-60017 (5th Cir. Jul. 19, 2022), the Fifth Circuit recently addressed a dispute regarding "how two legal regimes – the Bankruptcy Code and the Natural Gas Act – interact." Specifically, the issue involved whether the Federal Energy Regulatory Commission can override a debtor's bankruptcy-law rights and the bankruptcy court's power to reject executory contracts. The Fifth Circuit,

however, began by highlighting that it had already put this issue to rest, initially, in *Off. Comm. of Unsecured Creditors of Mirant Corp. v. Potomac Elec. Power Co.* (In re *Mirant Corp.*), 378 F.3d 511, 515 (5th Cir. 2004) and, just a mere three months earlier, in *FERC v. Ultra Res., Inc.* (In re *Ultra Petroleum Corp.*), 28 F.4th 629, 634 (5th Cir. 2022).

Subject to bankruptcy court approval, the Bankruptcy Code empowers debtors through "rejection" to breach and cease performing executory contracts. 11 U.S.C. § 365(a), (g). Accordingly, the court of appeals explained that it had twice previously ruled "that debtors may 'reject' regulated energy contracts even if ... FERC ... would not like them to." Barely hiding its exasperation with FERC for attempting to re-litigate a settled issue, the appeals court exclaimed "[n]evertheless, FERC persisted."

It is an elementary principle of bankruptcy law that, under Section 365 of the Bankruptcy Code, a debtor in possession has the power to assume or reject most executory contracts. Contracts are viewed as executory where neither party has completed performance. In *Mission Product Holdings v. Tempnology, LLC*, 203 L. Ed. 2d 876 (2019), the U.S. Supreme Court addressed rejection in bankruptcy, stating "[s]ection 365(a) enables the debtor ..., upon entering

bankruptcy, to decide whether the contract is a good deal for the estate going forward. If so, the debtor will want to assume the contract, fulfilling its obligations while benefiting from the counter-party's performance. But if not, the debtor will want to reject the contract, repudiating any further performance of its duties. The bankruptcy court will generally approve that choice, under the deferential 'business judgment' rule."

Rejection is merely a breach of the contract. It transforms the debtor's future performance obligations into the counterparty's unsecured claim for damages. 11 U.S.C. §§ 365(g), 502(g). The Fifth Circuit in *Gulfport* discussed that this might not seem helpful since rejection does not rescind the contract. The circuit court explained, however, that "here's the rub: Most debtors are broke and cannot pay in full that damages claim. ... So 'in a typical bankruptcy,' the counterparty to a rejected contract 'may receive only cents on the dollar' for its claim against the debtor, yet the debtor will retain the benefit of having ceased performance. ... In that way, 'rejection can release the debtor's estate from burdensome obligations that can impede a successful reorganization.'" Citing *Ultra*, 28 F.4th at 636.

The Natural Gas Act and the Federal Power Act regulate firms that transfer and sell natural gas in interstate

commerce and power companies, respectively. 15 U.S.C. § 717 and 16 U.S.C. § 824e. FERC has broad statutory jurisdiction over rates, terms, and conditions with regard to natural gas and power contracts, including changes to the contracts. Firms that contract to move and sell natural gas must file the rates they charge with FERC and any changes to the filed rates are conditioned on FERC's approval. Gulfport produced natural gas. Under transportation service agreements ("TSAs"), Rover Pipeline contracted to transport Gulfport's gas through its pipelines. The Fifth Circuit found that "[t]he TSAs are executory contracts. They establish the 'maximum daily quantity' of gas that Gulfport may push through Rover's pipelines, as well as the rates Rover may charge for that service."

Gulfport found itself in dire financial straits when, as the Fifth Circuit described, "[t]he COVID-19 pandemic crushed demand for energy, and with it, the price of oil and natural gas." Rover worried that Gulfport might enter bankruptcy, reject the TSAs, and that it would recover pen-

nies on the dollar. In anticipation of Gulfport's insolvency and potential bankruptcy filing, Rover sought and obtained from FERC orders purporting to require Gulfport to continue performing its gas transit contracts regardless of whether they were rejected in bankruptcy. The Fifth Circuit vacated those orders.

The Fifth Circuit discussed that approximately two decades ago, in *Mirant*, it had rejected FERC's arguments that a power company cannot "modify" or "abrogate" its rates without FERC's approval and that, accordingly, *Mirant* needed FERC's approval to reject any rate-filed contract. The appeals court stated "[w]e explained that FERC had misconstrued the effect of rejection. Rejection does not change or cancel a contract; it breaches that contract, ... giving the debtor's counterparty a damages claim for the value of the debtor's continued performance The contract itself does not change; nor does the filed rate. No change is wrought where the counterparty's claim for damages is 'calculated using the filed rate,' ..., even if the debtor

cannot pay that claim in full Thus, ... *Mirant* did not need FERC's consent to reject its filed-rate contracts, and FERC could not 'negat[e]' a rejection by requiring *Mirant* to continue performance."

Until three years ago, FERC acknowledged *Mirant*. Then, in the *PG&E* case it unsuccessfully declared that its approval was required before *PG&E* could reject its filed-rate power purchase agreements in bankruptcy. *PG&E Corp. v. FERC* (In re *PG&E Corp.*), 603 B.R. 471 (Bankr. N.D. Cal. 2019). FERC rehashed these arguments in *Gulfport*. Not pulling any punches, the appeals court held that "FERC's bizarre view of rejection" "flouts the Bankruptcy Code, Supreme Court precedent, and the caselaw of every federal circuit." The Fifth Circuit, once again, held that FERC is prohibited from usurping the bankruptcy court's power to decide rejection motions and "FERC cannot require continued performance of a filed-rate contract that is validly rejected—whether it purports to do so before, during, or after the bankruptcy proceeding."