Law360

What FERC's Disclosure Demands Mean For Cos., Investors

By **Norman Bay, Vivian Chum and Jake Maguire** (April 18, 2024)

Norman Bay

Vivian Chum

Jake Maguire

Move over, salacious celebrity memoirs. Detailed relationship disclosures are the new normal at the Federal Energy Regulatory Commission, as the commission ramps up its efforts to learn who calls the shots on behalf of FERC-jurisdictional public utilities and public utility holding companies.

Two FERC orders, ECP ControlCo LLC[1] and VESI 12 LLC,[2] are just the latest cases to reflect the commission's increasingly meticulous approach to reviewing corporate structures in applications for approval of proposed dispositions, consolidations, acquisitions or changes in control, pursuant to Section 203 of the Federal Power Act and requests for market-based rate authorization.

Background

FERC must review requests for Section 203 and MBR authorization to determine whether granting such requests will be in the public interest. This requires the commission to assess, among other things, whether approving the request will have an adverse impact on competition.

One way that competition may be harmed is if seemingly passive investors are in fact exercising an inordinate amount of influence on a public utility.

Historically, FERC's assessment was relatively straightforward. The commission routinely assumed, without further scrutiny, that an investor did not exercise significant control or influence over a public utility if the investor, directly or indirectly, owned, controlled or held with power to vote less than 10% of outstanding voting securities in that public utility.[3]

This created a rebuttable presumption of lack of control, which in turn meant that the investor was not an affiliate of the public utility.

Today, demonstrating that an investor owns, controls, or holds with power to vote, less than 10% of outstanding voting securities still "creates a rebuttable presumption of lack of control."[4] However, as recent cases make clear, that presumption has become subject to greater scrutiny.

Why does it matter? FERC's hard look at corporate structures could have significant consequences for applicants for MBR or Section 203 authorization.

For example, if an investor is found to be an affiliate of a public utility, the investor may become subject to certain regulatory requirements — and, to the extent the investor itself has MBR authority, the investor may have its own obligations to make additional MBR filings related to its public utility affiliate.

Furthermore, an investor's affiliate status could also increase the burden on its public utility affiliate by triggering a number of additional filing requirements — including change-in-status filings, updates to its asset appendix and ultimate upstream affiliate information filed in FERC's relational database, and updates to its horizontal and vertical market power analyses.[5]

For example, last year in Mankato Energy Center LLC, FERC determined that J.P. Morgan Investment Inc. was an affiliate of Mankato Companies and Mankato Companies' upstream owner in the course of reviewing Mankato Companies' MBR filing.[6]

The commission thus required "Mankato Companies to file a new notice of change in status that include[d] updated asset appendix information to reflect affiliation with J.P. Morgan and its affiliates, and updated horizontal and vertical market power analysis with their affiliates' generation and transmission assets, and inputs to electric power production[.]"[7]

Recent Developments

On March 1, FERC took the unusual step of denying ECP ControlCo's request for authorization, pursuant to Section 203(a)(1) of the FPA, to dispose of jurisdictional facilities. The commission held, without prejudice, that ECP and its public utility subsidiaries had failed to show that the proposed transaction would not have an adverse effect on competition.[8]

ECP had requested authorization for Bridgepoint OP LP or its designee to acquire a 19.9% interest and certain board appointment and removal rights in ECP.[9] Bridgepoint is an asset management company organized under the laws of England and Wales.[10]

Blue Owl, a publicly traded alternative investment asset manager and Cayman Islands-exempted limited partnership, owns approximately 15% of the publicly traded ordinary voting shares of Bridgepoint.[11]

ECP sought to avoid a scenario in which Blue Owl or its affiliates would be considered upstream affiliate owners of Bridgepoint.[12] Thus, ECP represented that Blue Owl would "irrevocably waive and relinquish the right to vote those Bridgepoint shares they hold cumulatively following the close of the [transaction] in excess of 9.9 percent of all voting shares."[13]

ECP sought to keep Blue Owl's voting shares under the 10% threshold, so as to assert the rebuttable presumption of lack of control. ECP argued that FERC should find that the voting restriction would be sufficient to avoid affiliate status.[14]

ECP's argument relied heavily on Hartree Partners LP, in which the commission concluded in 2019 that Oaktree Capital Group had successfully "eliminate[d] affiliation between it and Vistra Energy Corporation" through a similar voting arrangement.[15] In that case, ECP said, Oaktree "relinquished its voting rights with respect to the voting shares held in trust" such that Oaktree would have no entitlement to vote those shares and therefore would not be voting securities:[16]

> Oaktree placed its voting shares in Vistra in a voting trust with limited consent and veto rights and the trustee exercised independent voting discretion with respect to the transferred shares of Vistra and was not affiliated with or under the control of the applicants.[17]

FERC distinguished Hartree on the grounds that the applicants in Hartree had provided substantially more detailed information about the voting arrangements. First, the commission reasoned that "Oaktree retained 'limited consent and veto rights' over its entrusted securities of Vistra and provided an extensive description of how the voting trust corresponded with the Commission's findings regarding passivity in AES Creative Resources."[18]

In AES Creative Resources, FERC explained in 2009 that it distinguished between passive and active investment interests by

> [d]istinguishing between rights that give an investor the "authority to manage, direct, or control the activities" of a company and rights that give investors "only those limited rights necessary to protect their ... investments." The former make a security a voting security; the latter make it a non-voting security and thus a passive investment interest. These passive rights have the form of consent or veto rights.[19]

By contrast, ECP made no representations about the rights, if any, that Blue Owl would retain over shares in Bridgepoint subject to the voting restriction.[20]

Second, unlike Hartree, ECP did not make any representations about what would happen to the shares held by Blue Owl subject to the voting restriction.[21]

Third, FERC held that, based on the voting restrictions, it appeared that "there will be a complete prohibition on the voting of these shares," and as a matter of basic math, this would

> reduce the number of shares in Bridgepoint that are allowed to be voted by all shareholders. As such, even if Blue Owl were to only vote 9.9 percent of the outstanding nominal voting shares, this would amount to a greater than 10 percent holding of voting rights given the reduction in total shares that could be voted.[22]

The commission made clear that it would not approve ECP's request to dispose of jurisdictional facilities pursuant to Section 203 of the FPA without more details about the voting restriction and the impact the voting restriction would have on the upstream entities' ability to exercise control over FERC-jurisdictional public utilities.

Likewise, in its Feb. 23 order approving VESI 12 LLC's request for MBR authorization, FERC clarified its requirements regarding the necessary disclosures an MBR applicant or seller must make if it or its affiliates are publicly traded. The commission instructed that MBR applicants or sellers

> may not simply state that they, or their upstream affiliate(s), are publicly traded. If a publicly traded applicant or seller, or its publicly traded upstream affiliate, has owners that hold 10 percent or more of its outstanding voting securities, or other upstream affiliate(s), then it must include that information in its narrative description of its ownership structure.[23]

Otherwise, according to FERC, an applicant or seller must state that, "to the best of its knowledge, no owner holds 10 percent or more of outstanding voting securities, or other upstream affiliate(s)."[24]

Takeaways: Less Is Not More

FERC's demand for more detailed disclosures about the corporate structures of jurisdictional public utilities has been years in the making. As public utility ownership structures have become more complex — with investments from less traditional sources of capital such as private equity, infrastructure funds and foreign entities — the commission has responded with an ever-increasing appetite for detailed descriptions of corporate structures in applications for Section 203 authorization and MBR authority.

FERC's increasingly demanding disclosure requirements may very well have spurred the precipitous jump in the number of deficiency letters issued in response to requests for MBR authorization.

During calendar years 2017 through 2020, the commission issued, on average, just seven deficiency letters per year in response to MBR authorization requests. But from 2021 through 2023, the average number of deficiency letters per year jumped to 17. In the first two and a half months of 2024 alone, FERC has already issued seven deficiency letters in response to requests for MBR authorization.

According to FERC Commissioner Mark Christie, "it simply is no longer a credible assertion that investment managers … are always or should be assumed to be merely passive investors. These investment managers … wield significant financial power by virtue of their investments."[25]

Indeed, VESI 12 and ECP ControlCo are just the latest indicators that the days of a lighter-touch review of investor relationships to public utilities are behind us.

In 2022, FERC issued decisions in TransAlta Energy Mktg. (U.S.) Inc. and Evergy Kansas Central Inc., in which it held that investors with the ability to assign nonindependent members to the board of a FERC-jurisdictional utility would be considered by the commission to be affiliates with the ability to exercise control over that utility, even if the investors did not own, hold, or control 10% or more of voting securities in the utility.[26]

On Feb. 5, MBR applicant MS Solar 5 highlighted the confusion and uncertainty that FERC's increasingly demanding disclosure requirements have wrought. After MS Solar 5 filed an MBR application, commission staff reached out to MS Solar 5 to request that it supplement its petition with information about certain board members' involvement in the energy industry,[27] and to ask that MS Solar 5 provide all energy industry board positions held by those board members.[28]

FERC staff, in discussions with MS Solar 5, "advised that the Commission has not defined 'energy industry' and that they are not able to provide any additional guidance regarding what it means to be 'involved' in the energy industry other than affiliation."[29]

Strikingly, MS Solar 5 stated that while commission staff directed it "to supplement its Petition to provide additional information, ... staff is unable, given the lack of clear Commission guidance, to explain what additional information is required."[30] MS Solar 5 further contended:

> If the Commission wants to require that every applicant for market-based rate authority disclose whether its ultimate upstream affiliates hold any positions on the board of directors of any other company in the "energy industry," then we respectfully recommend that this be done through notice and comment rulemaking.

> Putting staff in the awkward position of requiring supplemental filings to provide undefined information and thereby potentially jeopardizing project development and the production of energy is not a permissible (or much appreciated) method of changing the law.[31]

FERC subsequently granted MS Solar 5's request for MBR authority without further guidance on the information required.[32]

Notably, in December 2023, the commission issued a notice of inquiry into whether it should revise its policy on providing blanket authorizations for investment companies under Section 203(a)(2) of the FPA.[33] FERC sought comment on "what constitutes control of a public utility in evaluating holding companies, including investment companies' requests for blanket authorization and what factors it should consider when evaluating control over public utilities as part of a request for blanket authorization."[34]

But the road from notice of inquiry to meaningful change is often long and filled with detours. It remains to be seen whether the notice of inquiry will lead to any significant rulemakings or changes in policy.

In the meantime, FERC continues to provide piecemeal guidance on its evolving disclosure requirements, which has put the onus on the regulated community to stay informed about — and even anticipate — the commission's increasingly demanding disclosure requirements.

As ECP ControlCo, VESI 12, MS Solar 5, TransAlta and Evergy have demonstrated, applicants risk being caught short by FERC's evolving standards. On the other hand, taking the kitchen-sink approach and sharing too much information with the commission could be burdensome and reveal commercially sensitive information.

Norman Bay is a partner at Willkie Farr & Gallagher LLP, chairs the firm's energy regulatory and enforcement practice group, and co-chairs the energy and commodities practice group.

Vivian Chum is counsel at the firm.

Jake Maguire is an associate at the firm.

Willkie senior counsel Paul Pantano and associate Alexandra Calabro contributed to this article.

[1] ECP ControlCo LLC, 186 FERC ¶ 61,164 (2024).

[2] VESI 12 LLC, 186 FERC ¶ 61,137 (2024).

[3] Hugh E. Hilliard and Caileen Kateri Gamache, FERC, May I Now?, 44 Energy L.J. 159, at 175 & n.78 (2023) (citing FPA Section 203, Supplemental Policy Statement, FERC Stats. & Regs. ¶ 31,253 (2007), 120 FERC ¶ 61,060, at P 37 (2007), 72 Fed. Reg. 42,277, clarified, 122 FERC ¶ 61,157, at P 4 (2008)).

[4] See 18 C.F.R. 36.35(a)(9).

[5] The implications are discussed at length in Willkie's 2022 client alert, Recent FERC Decisions Have Widespread Regulatory Implications for Public Utilities and Investors, available here: https://www.willkie.com/-/media/files/publications/2022/recentfercdecisionshavewidespreadregulatoryimplica.pdf.

[6] Mankato Energy Center LLC et al., 184 FERC ¶ 61,170, at P 2 (2023).

[7] Id.

[8] ECP ControlCo, 186 FERC ¶ 61,164 at P 2.

[9] Id. P 1.

[10] Id. P 4.

[11] Id. P 5.

[12] Id. P 7.

[13] Id. P 8.

[14] Id. P 21.

[15] Id. PP 22-23 (citing Hartree Partners LP, 168 FERC ¶ 61,212 (2019)).

[16] Id. P 22 (internal citations omitted).

[17] Id.

[18] Id. P 23 (internal citations omitted).

[19] AES Creative Resources LP, 129 FERC ¶ 61,239, at P 25 (2009) (quoting Solios Power LLC, 114 FERC ¶ 61,161, at PP 9-10 (2006)).

[20] ECP ControlCo, 186 FERC ¶ 61,164 at P 23.

[21] Id. P 24.

[22] Id. P 25.

[23] VESI 12 LLC, 186 FERC ¶ 61,137, at P 16 (2024).

[24] Id.

[25] Federal Power Act Section 203 Blanket Authorizations for Investment Companies, 185 FERC ¶ 61,192 (2023) (Christie, Comm'r, concurring at P 2) ("Notice of Inquiry").

[26] Evergy Kansas Central Inc., 181 FERC ¶ 61,044 (2022), order on reh'g Evergy Kansas Central Inc., 184 FERC ¶ 61,003 (2023); TransAlta Energy Mktg. (U.S.) Inc., 181 FERC ¶ 61,055 (2022). An in-depth discussion of the TransAlta and Evergy orders can be found in our 2022 client alert, Recent FERC Decisions Have Widespread Regulatory Implications for

Public Utilities and Investors, available here: https://www.willkie.com/-/media/files/publications/2022/ recentfercdecisionshavewidespreadregulatoryimplica.pdf.

[27] MS Solar 5 LLC, Supplement to Petition, Docket No. ER24-619-000, at 2 (filed Feb. 5, 2024).

[28] Id.

[29] Id.

[30] Id.

[31] Id. at 5.

[32] MS Solar 5 LLC, Docket No. ER24-619-000 (Feb. 14, 2024) (delegated order).

[33] Notice of Inquiry, 185 FERC ¶ 61,192.

[34] Id. Comments on the notice of inquiry were due March 26; reply comments are due April 25.