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FERC Extends AES Creative Precedent to Transaction Approvals

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On October 4, 2017, the Federal Energy Regulatory Commission ("FERC") issued an order clarifying that it will not treat certain tax equity interests in public utilities or public utility holding companies as voting securities for purposes of transaction approval requirements pursuant to Section 203 of the Federal Power Act ("FPA") ("Passive Interest Order").[1] The Passive Interest Order provides guidance regarding FERC's consideration of certain "tax equity" passive interests for purposes of determining whether transactions involving such interests constitute a transfer of control over the relevant public utility operating company that could trigger FPA Section 203 prior authorization requirements.

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Subject to certain blanket approvals, FERC requires prior authorization pursuant to FPA Section 203 for transactions that constitute a transfer of control of a FERC jurisdictional public utility. Public utilities for these purposes includes the owners of FERC jurisdictional independent power production facilities ("IPPs") and wholesale power marketers. Late in 2016, an informal group of companies involved in tax equity financing for renewable energy facilities submitted a petition to FERC seeking a declaratory order confirming that the issuance or transfer of tax equity interests similar to those described in FERC's *AES Creative* decision[2] does not constitute a change in control over the relevant public utility operating companies that would require prior authorization by FERC pursuant to FPA Section 203 and that the acquisition of such interests by a public utility holding company qualifies for blanket authorization by FERC pursuant to Section 33.1(c)(2)(i) of its regulations. The Passive Interest Order grants the petition.[3]

The Passive Interest Order, and the underlying petition, stem from the industry's perceived lack of clarity in FERC's treatment of certain passive interest transactions in the FPA Section 203 transaction approval context. In the rate context pursuant to FPA Section 205, the FERC's 2009 *AES Creative* recognized the difference between ownership rights that provide investors with the authority to manage, direct, or control the activities of a company and rights that provide investors with "only those limited rights necessary to protect their ... investments."[4] In *AES Creative,* FERC concluded that interests held by tax equity investors are passive and do not constitute a voting security that would constitute control over the ultimate public utility operating company. Many in the industry have perceived the holding in *AES Creative* to be too narrow to rely on in the Section 203 context because FERC chose not to extend the interpretation to FPA Section 203 considerations explicitly even though the question of "control" was very similar.[5] Because the Passive Interest Order now expressly extends the holding in *AES Creative* to the FPA Section 203 context, FERC is likely anticipating that the number of Section 203 applications related to tax equity or "passive investments" may be reduced.

While the Passive Interest Order certainly offers long-awaited clarity and may indeed reduce the number of applications seeking authorization for tax equity investments, the scope of the holding is not without limits. Specifically, FERC reminds parties that, to the extent the securities in future tax equity transactions have characteristics that vary from those presented in *AES Creative*, "it remains the investor's responsibility to make a determination as to whether prior Commission approval for transactions involving such securities is necessary."[6] Given the fact that firms have often filed Section 203 applications out of an "abundance of caution" even when FERC approval requirements are questionable, it will be interesting to see how the Passive Interest Order affects the number of Section 203 requests. Some firms may be concerned about proceeding without seeking prior FERC Section 203 approval, even when the facts and characteristics of the transactions at

issue are substantively similar to those in *AES Creative*. If FERC continues to see applications for Section 203 authorization that it considers unnecessary in light of the Passive Interest Order, it may choose to reject those filings without prejudice as being unnecessary. However, if such uncontested applications are routinely approved by FERC Staff on delegated authority by letter orders, the scope of transactions covered by the Passive Interest Order may be limited.

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[1] *Ad Hoc Renewable Energy Financing Group*, 161 FERC ¶ 61,010 (2017).

[2] *AES Creative Resources, L.P.*, 129 FERC ¶ 61,239 (2009) ("*AES Creative*"). In *AES Creative*, FERC concluded that certain non-voting tax-equity investment interests in public utilities do not constitute "voting securities" for purposes of FERC's market-based rate regulations pursuant to FPA Section 205 because such investment interests do not entitle their holders "to vote in the direction or management of the affairs" of the public utilities. *Id.* at P 28. Accordingly, for purposes of FPA Section 205 requirements, FERC held that the investors holding such interests were not considered to be affiliates of the public utilities in which they invested. *Id.*

[3] Passive Interest Order at P 17.

[4] *AES Creative* at PP 25-28.

[5] Instead, FERC reminded investors that "the burden remains upon [them] to decide whether they need to obtain Commission authorization under section 203 to undertake a proposed transaction." *See FPA Section 203 Supplemental Policy Statement*, FERC Stats. & Regs. ¶ 31,253 at P 56 (2007).

[6] Passive Interest Order at P 17 fn30.