

ORIGINAL

TRANSCRIPT OF PROCEEDINGS

IN THE SUPREME COURT OF THE UNITED STATES

ERIC J. SCHNEIDEWIND, ET AL.,)
)
 Petitioners,)
)
v.) No. 86-986
)
ANR PIPELINE COMPANY AND)
)
ANR STORAGE COMPANY)

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IN THE SUPREME COURT OF THE UNITED STATES

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ERIC J. SCHNEIDEWIND, ET AL., :

Petitioners, :

v. : No. 86-986

ANR PIPELINE COMPANY AND :

ANR STORAGE COMPANY :

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Washington, D.C.

Monday, November 2, 1987

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 10:02 a.m.

APPEARANCES:

DON L. KESKEY, ESQ., Assistant Attorney General of Michigan, Lansing, Michigan; on behalf of the Petitioners.

HOWARD J. TRIENENS, ESQ., Chicago, Illinois; on behalf of the Respondent.

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P R O C E E D I N G S

(10:02 a.m.)

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3 CHIEF JUSTICE REHNQUIST: We'll hear argument this
4 morning in Case No. 86-986, Eric Schneiderwind versus ANR
5 Pipeline Company.

6 Mr. Keskey, you may proceed whenever you're ready.

ORAL ARGUMENT OF DON L. KESKEY

ON BEHALF OF PETITIONERS

7
8
9 MR. KESKEY: Mr. Chief Justice, and may it please the
10 Court. This case involves a review of two major holdings of
11 the Court of Appeals of the Sixth Circuit. The first that
12 Michigan Act 144, which regulates the securities of utilities
13 and natural gas companies, is implicitly preempted by the
14 Natural Gas Act because Congress had the purpose to deregulate
15 securities of natural gas companies.

16 Secondly, for the opposite purpose that FERC was
17 sufficiently regulating securities under its Section 7
18 certificate powers and thirdly because of what the Court viewed
19 as an imminent possibility of conflict between Michigan Act 144
20 Securities Regulation and the Natural Gas Act.

21 In addition, the Court of Appeals found that Michigan
22 Act 144 represented an unconstitutional burden on interstate
23 commerce on all tests, the per se of discrimination test, the
24 balancing test of Pike v. Bruce Church and also on the basis of
25 a need for national uniformity with respect to Securities

1 regulation of natural gas companies.

2 In reaching these holdings, the Sixth Circuit Court
3 of Appeals failed to follow this Court's preemption test, and
4 failed to follow Congressional intent in the Natural Gas Act.
5 Congress, in the Natural Gas Act, did not occupy the whole
6 field of natural gas regulation, it did not speak to Securities
7 regulation whatsoever, it did not preempt the States from
8 regulating securities by its silence in the NGA regarding this
9 subject. This Court has held extensively in Panhandle Eastern
10 that the purpose of the NGA was to close regulatory gaps
11 brought about by the prior decisions of this Court in a
12 specific area, interstate transportation of gas and sales for
13 resales. It did not involve the area of Securities regulation
14 of natural gas companies.

15 QUESTION: Mr. Keskey, what is the purpose exactly of
16 the Michigan State statutes in this regard?

17 MR. KESKEY: The purpose of the Michigan statutes is
18 to protect the public interest, the public health safety and
19 welfare.

20 QUESTION: Be a little more specific. That doesn't
21 tell me much.

22 MR. KESKEY: One of the major purposes is to ensure
23 that the extensive pipeline facilities and storage facilities,
24 the property located within the State does not become over
25 collateralized, the company doesn't become over capitalized so

1 that the maintenance and the safety and environmental concerns
2 regarding those facilities are not harmed.

3 Secondly, that there is reliable service to the
4 public. In large part, these are still monopoly companies, or
5 at least oligopolies. The service of natural gas the captive
6 markets substantial markets in Michigan are very integral to
7 the livelihood, the existence of the people in Michigan and to
8 the economic development of the State.

9 QUESTION: Is it intended at all to make available
10 gas to Michigan consumers at reasonable rates?

11 MR. KESKEY: It can protect the rate payers by
12 ensuring that over capitalization does not result, to ensure
13 that there are not abuses in financings.

14 QUESTION: Well, is an effect on rates one of the
15 purposes of the legislation?

16 MR. KESKEY: No. It's not designed to regulate rates
17 or interstate rates.

18 QUESTION: Did your State Court ever find that one of
19 the purposes was to ensure reasonable utility rates?

20 MR. KESKEY: The State Court indicates that's one of
21 the purposes.

22 QUESTION: But you disavow that as a purpose?

23 MR. KESKEY: No, no, not whatsoever. By protecting
24 against financing abuses, and by protecting against over
25 collateralization, you can ensure that service will be

1 available at reasonable rates, that you will not get financing
2 that will eventually end up being a burden on the company and
3 would eventually harm service to Michigan at reasonable rates.
4 It's not an attempt to address rate making because we recognize
5 fully that that is a function of FERC, and we intervene in rate
6 cases at FERC, but it is to ensure that there is not an affect
7 from financing actions which results in damage to the financial
8 viability of both the natural gas assets and to the companies
9 themselves.

10 QUESTION: Actually the State does not impose this
11 what you describe as Securities regulation on any companies
12 except rate regulated companies, though, isn't that right?

13 I mean, you refer to it as Securities regulation, but
14 it's not a general Securities law that applies to all
15 companies.

16 MR. KESKEY: It applies to public utilities and to
17 natural gas companies, or interstate electric companies. Under
18 the Federal Power Act 204, Congress expressly recognized that
19 States could continue to engage in this kind of regulation with
20 respect to interstate electric companies.

21 QUESTION: So the answer to my question is?

22 MR. KESKEY: That this?

23 QUESTION: It is imposed only on rate regulated
24 public utilities, certain rate regulated public utilities?

25 MR. KESKEY: Essentially public utility type

1 companies upon which there's a heavy dependence by the public
2 on these companies or a monopoly type companies, strong nexus
3 of public interest to these companies.

4 QUESTION: So why don't we call it public utility
5 regulation instead of security regulation?

6 MR. KESKEY: It's really the same thing, or they're
7 extremely closely related.

8 QUESTION: Does the Securities and Exchange
9 Commission, for example, do anything of this sort

10 MR. KESKEY: The Securities and Exchange Commission
11 has Acts which involve registration and the filing of
12 information.

13 QUESTION: It doesn't police the dead equity ratio of
14 companies, does it?

15 MR. KESKEY: No, it does not. And it does not look
16 at the Key which Act 144 does, and that is what is the
17 relationship between the capital and the value of the assets on
18 the balance sheet and the good will of the business. Neither
19 FERC nor the SEC look at that. Are these securities being
20 issued for a lawful purpose, have they had their board
21 resolutions passed, do they have their stockholders approve
22 this, is it in accordance with the indenturers, are these
23 companies going to engage in something like buy a baseball team
24 or are they going to involve themselves in some illegal
25 securities transactions.

1 Because if they do, and they try to shift that onto
2 the company it could come back to haunt.

3 QUESTION: Well, there's constitutional doctrine,
4 isn't there, that a company is entitled, constitutionally
5 entitled to a reasonable return on its investments, and the
6 State probably has an interest in looking at what those
7 investments are.

8 MR. KESKEY: It's really pretty much dealing with the
9 problem before the fact. In other words, FERC looks at rates
10 and entirely it's an after the fact approach. The obligations
11 of the company are already issued and they're already binding.
12 But this is a peek at looking at the obligations before they're
13 issued, before they become permanently binding on the company
14 to see is this lawful, is this in the public interest, will
15 Michigan be protected. These companies have such an important
16 relationship to Michigan.

17 QUESTION: Is there any limitation on the companies
18 on which this is applied? I mean, is it to every public
19 utility that is doing business in Michigan or is there some
20 domicile requirement?

21 MR. KESKEY: It is to every public utility that
22 operates in the State of Michigan, including electric, gas,
23 telephone companies. It also applies to interstate electric
24 companies and the interstate gas companies who have more than
25 five percent of their revenues generated in the State of

1 Michigan.

2 Although in the facts of this case, this is a facial
3 attack on the Statute. We did have stipulated facts regarding
4 these particular respondents who have 40 percent of Michigan's
5 natural gas requirements are provided by these companies, 50
6 percent of their sales. The ANR storage company has all of its
7 property located in Michigan.

8 QUESTION: Mr. Keskey, when the Attleboro doctrine
9 prevailed, who regulated the issuance of securities for
10 companies like these, the State agencies, or?

11 MR. KESKEY: The State governments were involved in
12 extensive public utility regulation prior to any Federal Acts.

13 QUESTION: Specifically as to the regulation of the
14 issuance of securities?

15 MR. KESKEY: Yes. Michigan's Act was enacted in 1909
16 and it was applied to natural gas companies in 1929, which
17 predated the NGA. And numerous other States, even at the time
18 of the --

19 QUESTION: It doesn't matter as far as the regulation
20 is concerned whether the regulated company by Michigan is a
21 Michigan corporation or of some other State.

22 MR. KESKEY: One of the respondents happens to be a
23 Michigan corporation, but the important thing here is the
24 substance of their relationship to Michigan and the substantial
25 presence and importance to Michigan, not specific --

1 QUESTION: Well, if your answer to me is, it does
2 not matter whether it's a Michigan Corporation or of some other
3 State?

4 MR. KESKEY: That is an additional item that does
5 matter, but the primary thing we're looking at here besides the
6 corporation filing requirements and the regulation as a
7 Michigan Corporation is the substantial context and important
8 nexus of these companies to Michigan's public interest. And
9 just the fact that they are a Michigan corporation, and one of
10 them's a Delaware Corporation, but it has no context with
11 Delaware whatsoever. They're business is substantially in
12 Michigan and they are the life blood to Michigan, and so on
13 that basis, it's an additional basis.

14 QUESTION: Well, any interstate pipeline that goes
15 into Michigan is the life blood to Michigan, isn't it?

16 MR. KESKEY: To certain segments or portions of
17 Michigan, that's correct.

18 QUESTION: So you're asserting that that gives
19 Michigan authority to regulate, you certainly wouldn't assert
20 that gives Michigan the authority to regulate all interstate
21 pipelines just because they're essential to Michigan?

22 MR. KESKEY: We're not trying to regulate any Federal
23 area, such as rates, transportation, sales for resale. We're
24 looking at the power that Michigan had before the NGA to
25 regulate the securities based upon their presence in the State.

1 They are collateralizing Michigan's property whenever they
2 issue long term securities.

3 QUESTION: What happens, Mr. Keskey, if the State
4 does not allow a particular issuance of debt securities? It
5 says that the company would be over leveraged if this
6 particular new facility should be financed by debt, so the
7 company sells new stock on the market. When it comes around to
8 rate making by FERC, FERC decides that indeed the company has
9 too much equity and should be drawing down more of its capital
10 on the debt market which comes at a lower rate and will give
11 lower rates to consumers.

12 What does the company do?

13 And therefore FERC disallows, disallows the return on
14 the equity investment which the State required the company to
15 go into instead of debt. What happens in the event of that
16 conflict? How is the company supposed to, which of the two
17 masters does the company obey?

18 The State says you have to do it by equity, rather
19 than debt, and FERC says, well, we're sorry, you have too much
20 equity, and we're not going to allow you any rate of return on
21 this equity, you should have done this by debt.

22 MR. KESKEY: Michigan's review primarily looks at the
23 relationship of the overall capital compared to the overall
24 value of the property and the business. That's where over
25 capitalization comes in. It's not the capital ratio, which

1 you're talking about. That's very indirect.

2 QUESTION: I don't care what Michigan looks at. I'm
3 just saying, this is what happened for whatever reasons,
4 Michigan did it. Michigan says you cannot issue debt
5 securities for this, you have to do it by stock. And FERC says
6 we think you should have been in debt equities instead at a
7 lower rate of return, of course, and therefore, we're not going
8 to allow you the normal rate of return on equity securities?

9 MR. KESKEY: I would presume in that situation that
10 the Company would go to the Commission and present the rate
11 decision of FERC which you're giving me an example of FERC
12 providing a hypothetical requiring a hypothetical capital
13 structure.

14 QUESTION: Well, they always do when they make rates.

15 MR. KESKEY: Very rarely.

16 QUESTION: They only allow return on justifiable
17 equity.

18 MR. KESKEY: Hypothetical capital structures in the
19 rate regulation business is very rare. Most witnesses in rate
20 cases will testify as to what the appropriate ratios are of
21 equity to debt, and most companies, almost all companies that
22 are utilities in the United States are within those reasonable
23 ranges.

24 Now, if a company has more common equity than debt,
25 the cost of common equity is normally higher, but the business

1 risk is lower, and the economists will testify that the more
2 equity you have, the lower cost you assign to it, because of
3 this reflection of less business risk. So you're on a teeter
4 totter in a sense that if you have more and more equity,
5 usually the economists in a rate case will assign lower and
6 lower costs to that common equity so that it approaches debt.

7 Now, you've given me an example which first of all
8 hypothetical capital structure is extremely rare.

9 QUESTION: I've read a lot of rate cases where the
10 rate making agency has disallowed return on equity because the
11 agency said there shouldn't be that much equity.

12 MR. KESKEY: That's correct. It occurs.

13 QUESTION: That's not uncommon at all, is it?

14 MR. KESKEY: In terms of percentage of cases, it's
15 rare. It does occur. And in that instance, the company
16 between rate cases, which is usually an extensive period of
17 time, would either not get rate reflection for it, or would
18 make adjustments in its financial structure to accommodate
19 that.

20 QUESTION: Well, what would happen here? Is your
21 position that Michigan would have to yield as to what its
22 decision concerning the proper action of the company should be?
23 Would Michigan have to yield or would the company simply have
24 to obey Michigan and get a lower rate of return?

25 MR. KESKEY: It's extremely difficult in a

1 hypothetical and we're dealing here with a hypothetical that
2 hasn't happened in the 78 years that the Michigan Act has been
3 in effect. To imagine all of the factual possibilities of how
4 you would get to this, and those are important because there
5 could be any of number of reasons why Michigan would act the
6 way it did, and the way FERC acted the way it did.

7 QUESTION: Assume the reasons most favorable to
8 Michigan.

9 MR. KESKEY: There is a theoretical possibility that
10 Michigan -- and it's most theoretical -- that Michigan could
11 require that no more debt be issued because the company was
12 over capitalized or because it was issuing debts for an
13 unlawful purpose, and FERC would have required them indirectly
14 -- not directly, indirectly -- by not reflecting full rates for
15 common equity, let's say, that there is this situation.

16 QUESTION: I consider that pretty direct when you're
17 dealing with a company whose business is to collect rates not
18 to allow you to collect any rates on a particular issuance.
19 You consider that very indirect? I consider that a fairly
20 direct sanction on the company.

21 QUESTION: Mr. Keskey, can I ask you a little more
22 about the notion of issuing debt for an unlawful purpose, you
23 suggested buying a baseball team or something like that.

24 What would make it unlawful for one of these
25 companies to buy a baseball team?

1 MR. KESKEY: It's not necessarily that sitting here
2 in this hypothetical and the facts presented it would be
3 unlawful. But this Statute allows Michigan to obtain
4 information as to what is happening and to determine whether or
5 not it is unlawful, and those would be based upon the arguments
6 in the contested case. In other words --

7 QUESTION: This is sort of a discovery mechanism?

8 MR. KESKEY: In part. This helps Michigan obtain
9 information.

10 QUESTION: In order to get your discovery, I don't
11 suppose you'd have to be able to say, no, to a prospective
12 investment. Just get the information, and if you find they're
13 doing something unlawful, tell them not to do what's unlawful.
14 I understand --

15 MR. KESKEY: I think the best way to answer it is to
16 give you an example of how Michigan used this statute to
17 protect its local interests without affecting any interests
18 that are national or involve interstate commerce. And that is
19 not a hypothetical but an actual case.

20 In 1981, ANR, the parent company, owned Michigan
21 Consolidated Gas, which was a local utility. The Michigan
22 Public Service Commission, throughout its existence and in more
23 recent years, has promoted in Michigan the development of vast
24 natural gas storage fields which are huge caverns thousands of
25 feet below where the gas can be stored in natural sea beds. It

1 provided recognition of that in rates and encouraged it through
2 help with the local engineers and so forth, with the property
3 owners, etcetera. Many of these fields were developed and Mich
4 Con had its transmission lines to these wholly-in-State
5 facilities, and MichCon had its lines between one part of its
6 service area in Detroit and another part of its service
7 territory in northern Michigan.

8 And ANR came up with a proposal to divest MichCon
9 from its system. But it wasn't going to just divest MichCon.
10 It was going to take for itself all of these storage facilities
11 that the Michigan ratepayer had paid for and had developed. It
12 was going to take all of these transmission lines that
13 connected the company together so that MichCon would be left as
14 an orphan on the doorstep of the Michigan Public Service
15 Commission as only a distribution utility with no ability to
16 transport gas within the State to these storage facilities and
17 to the rest of its service territory. It would have to pay ANR
18 for that right. It would have to pay ANR to pay for the
19 ability to transport gas to the rest of its company on
20 facilities that it built itself, and that Michigan encouraged
21 and that Michigan rate payers paid for. And these storage
22 facilities and these lines were not necessary to ANR's
23 interstate system. And if the storage was usable for any
24 interstate purposes, MichCon was ready to lease those
25 facilities its capacity to those interstate companies. In

1 fact, does so now with ANR.

2 So we used the statute because people were walking
3 around saying, what's happening, we can't get any information.
4 What's happening is the fact that the parent company is going
5 to strip our utility of all the assets that are valuable and
6 leave everything that's not valuable on the backs of the
7 Michigan public.

8 Now, we used this statute to start a proceeding to
9 get information. That was the only way we could get
10 information. FERC had no jurisdiction whatsoever because this
11 involved no construction. This involved a situation of
12 financing transactions among ANR and MichCon that had nothing
13 to do with any of FERC's powers, nothing to do with a Section 7
14 Certificate which is the only area where even respondents
15 arguably say that Michigan and FERC both look at financing.

16 QUESTION: Did you have to use it against ANR?
17 Couldn't you have gotten the same information by using it just
18 against MichCon?

19 MR. KESKEY: No, because ANR was the one that had
20 planned the entire transaction, ANR was engaging in these
21 securities, ANR controlled MichCon.

22 QUESTION: Weren't MichCon securities involved?

23 MR. KESKEY: MichCon securities were involved, ANR
24 securities were involved, and even a third holding company that
25 --

1 QUESTION: I don't understand why you couldn't do it
2 through your regulation of MichCon.

3 MR. KESKEY: Well, that's an actual case which is not
4 here. We don't have an actual case. If we did, we would have
5 the advantage of citing to you the record. But the situation
6 was, it came down to the fact that this was the Statute that
7 permitted Michigan to get information to find out what was
8 happening to protect the dismemberment of a public utility that
9 serves millions of customers in Michigan and is integral to the
10 very economy of Michigan.

11 And we did so. We reached a settlement. Both sides
12 were accommodated. The ANR system was not harmed. There were
13 no national interests involved. There was no FERC jurisdiction
14 involved in terms of the securities, and there didn't have to
15 be. They didn't have to get approval from FERC to do this. We
16 preserved the Michigan utility as an entity, and by doing so,
17 we saved costs, we saved rates. The cost of that company to
18 the customers would be much higher today if they would have
19 been stripped.

20 QUESTION: Mr. Keskey, you also assert jurisdiction
21 to regulate the Respondent's storage company, do you not?

22 MR. KESKEY: Yes.

23 QUESTION: And that has no customers at all in
24 Michigan, is that correct?

25 MR. KESKEY: All of its other contexts are with

1 Michigan except for the fact that they have chosen to --

2 QUESTION: Well, aren't its suppliers and customers
3 all outside of Michigan?

4 MR. KESKEY: Its customers are all outside of
5 Michigan, that's correct.

6 QUESTION: And suppliers? All that's in Michigan is
7 their physical facilities, plant and equipment, is that right?

8 MR. KESKEY: That's correct. But --

9 QUESTION: And what is the interest of Michigan there
10 then do you suppose?

11 MR. KESKEY: The storage company has these vast
12 facilities in Northern Michigan which have to be adequately
13 maintained, they have to be adequately engineered, you can only
14 put a certain amount of gas in these facilities, otherwise you
15 can damage the cap rock, and have tremendously dangerous
16 blowouts. Or you could destroy the facility as a viable
17 storage facility.

18 If you become under capitalized or if you over
19 leverage those facilities, and you are not capable of
20 maintaining these facilities properly, it's very dangerous.
21 Further, the gas customers that the storage company has are
22 located --

23 QUESTION: You mean, you're talking about some
24 physical accident that might occur and injure people?

25 MR. KESKEY: Yes.

1 QUESTION: And you can't directly require safety
2 standards for employees?

3 MR. KESKEY: Well, the Michigan Commission does get
4 involved in safety by assisting FERC as the eyes and ears of
5 FERC with respect to safety requirements. But we're looking at
6 a way to prevent over capitalizations or the assets being over
7 collateralized so that they would be neglected. But there's
8 another purpose, also, and that is that in the gas business,
9 interstate transportation, when it goes from storage to
10 customers, let's say in Montana, is done by displacement. So
11 what occurs is that this gas is stored in the center of
12 Michigan, the storage company transports it to 24 miles to an
13 interstate pipeline which does the transportation.

14 Storage has no interstate transportation, it doesn't
15 sell any gas. It doesn't have any transportation tariffs to be
16 approved by FERC. Gas molecules actually are used in Michigan.
17 They are part of the reliability of supply in Michigan, but the
18 storage company delivers it to Michigan located interstate
19 transportation which sells the molecules in Michigan. And on
20 the other end of its system in Montana, it gives an accounting
21 credit to that person over there, and gives them the molecules
22 over there. So theoretically and conceptually, yes, there's
23 interstate transportation if you go right from the beginning,
24 right to Montana. But it isn't done by ANR Storage. It's
25 done by an interstate company that FERC does regulate in terms

1 of interstate rates.

2 Storage company's wholly in Michigan, the gas
3 properties are in Michigan. It does have an importance to
4 supply even in Michigan because the displacement is basically
5 an accounting type exchange. And so if there's a failure of
6 those facilities, it will affect Michigan not only in the
7 viability of the facilities, but with respect to supply
8 applications in Michigan.

9 So in conclusion, Your Honors, we have a vast area of
10 regulation over here and over here. The respondents have said
11 there's potential conflict, only a possibility of conflict in
12 this narrow area about Section 7 certificates. We see there
13 isn't. But why deregulate securities with respect to all the
14 rest of this area when there has been no actual conflict.
15 There is nothing in this record about any actual conflict in
16 the 50 years that the NGA and the Act has survived together.
17 This is a facial attack, and Congress did not occupy the field
18 of securities regulation it intended the States to continue to
19 do so. And it's not a burden on interstate commerce because we
20 are focusing totally on Michigan's interests. There is no
21 discriminatory intent or effect in this Statute. It never was
22 passed for an economic protectionist purpose.

23 QUESTION: Does any other State regulate presently
24 the securities issued by natural gas companies, Mr. Keskey?

25 MR. KESKEY: Yes. Montana does, California has a

1 statute which permits it. At the time of the 1950 hearings, 33
2 States were regulating natural gas companies' securities. We
3 don't know how many other than California and Montana are.

4 But the States are regulating the interstate electric
5 companies, and Congress provided for that in Federal Power Act
6 204.

7 QUESTION: Interstate gas companies, was your answer
8 meant to say 33 States are regulating interstate gas companies?

9 MR. KESKEY: Yes. In 1950, 33 States, and we have it
10 in a footnote about legislative history in our brief, 33 States
11 were regulating the securities in natural gas companies
12 operating interstate commerce.

13 QUESTION: Thank you.

14 CHIEF JUSTICE REHNQUIST: Thank you, Mr. Keskey.
15 We'll hear now from you, Mr. Trienens.

16 ORAL ARGUMENT OF HOWARD J. TRIENENS, ESQ.

17 ON BEHALF OF RESPONDENTS

18 MR. TRIENENS: Chief Justice, may it please the
19 Court.

20 None of those 33 States regulate interstate
21 pipelines. Those 33 States were local distribution companies
22 they were regulating, the local distribution company that also
23 had some high pressure pipeline.

24 The concern of the States at the 1950 legislative
25 amendment proposal -- might as well straighten this one out

1 the concern of the States was so broad, the FPC proposal was so
2 broad that it brought under proposed FPC preissuance security
3 regulation local distribution companies. The States came
4 screaming in and said, oh, no, we traditionally regulate the
5 local distribution. We traditionally do that. It's these
6 interstate pipelines like ANR that we don't regulate. And as
7 to what FPC does with that, that's their business, but for
8 heaven's sakes, don't touch these local distribution companies.

9 So the FPC comes along, and it says, well, we'll
10 amend our proposal, we'll amend our proposal. We'll ask for
11 this preissuance authority, this additional regulatory
12 technique only for those companies and those operations that
13 the States cannot reach. Now, just to nail that down, let me
14 give you two sentences out of that hearing where Commissioner
15 Smith made it very plain that his proposed amended legislative
16 proposal was not going to impair the State regulation of those
17 gas companies that are essentially local, meaning, do local
18 distribution.

19 But here's an example of a company that's clearly
20 beyond the reach of the States as to securities matters. The
21 Commonwealth of Massachusetts regulating the securities of a
22 pipeline operating at wholesale within the State of
23 Massachusetts but carrying gas from Texas to Massachusetts.
24 They can't do that, and the States right proponents says, if
25 that's the question, it cannot, we concede that. And of course

1 you have to concede that, because can anybody who -- take 1925,
2 when the Missouri v. Kansas Gas was decided. Can anybody
3 believe that these States could have regulated any aspect,
4 securities or anything else, of these interstate pipelines when
5 this Court held that these lines were "beyond State
6 interference" or beyond the reach of State regulations.

7 Now, the Attleboro case which was electric is a very
8 different problem. Justice Brandeis dissented in that. It was
9 a more localized problem. Even there, the Court at that time
10 said the States couldn't touch it. That case is different,
11 it's electric. Congress in regulating interstate electric
12 power provided expressly provided that States could regulate
13 it. That's a delegation of the States that Congress could have
14 made when it broke its silence, it did make in the case of the
15 interstate electric, because after all, they're very localized
16 really little grids around a few States, and they sharply
17 distinguished that. And instead of delegating to the States,
18 they created a comprehensive Federal regulatory system.

19 And as far as we know, Michigan is the only State
20 that an interstate gas pipeline of this character has any
21 problems. We serve Wisconsin almost as much as Michigan, and
22 we have no such problem with Wisconsin, although they have a
23 regulatory statute that permits a preissuance approval of
24 securities as to utilities in Wisconsin, but it doesn't apply
25 to this company.

1 Now, the premise of this argument of Michigan is that
2 somehow financing and securities are unregulated. That there's
3 some big gap that has to be filled here. And I'd like to show
4 the Court that that gap doesn't exist. And it's a combination
5 of regulatory tools, the first of which is the certification
6 power. In order to have a project you're going to finance, you
7 have to go to the FPC, FERC now, get a certificate of public
8 convenience and necessity before you can finance it.

9 For example, we want to build a pipeline extension in
10 Wisconsin, say a \$75 million one, and we have to go to FERC and
11 get a certificate. And while we're there, because Congress
12 made it very express that Congress was speaking to securities
13 regulation, in 1942, Congress expressly authorized FERC to
14 condition its approval of certificates and to modify the
15 financing as the public interest might demand.

16 So we go down to the FERC and we say, all right, its
17 going to not only cost \$75 million but we're going to raise \$25
18 million through equity and we're going to have a \$50 million
19 bond issue. That's the way, that's our financing plan, and we
20 get the certificate, and this certificate power along with the
21 rate power is described by this Court as the heart of the Act.

22 QUESTION: Did they ever in fact alter the proposed
23 manner of financing?

24 MR. TRIENENS: Yes, sir. Yes, Justice Scalia, and we
25 have three or four examples in our brief. The INGA, a trade

1 association has three or four examples where the FPC, now FERC,
2 has done just that, yes.

3 QUESTION: Will FERC condition the granting of the
4 certificate on the issuance of certain types and amounts of
5 securities?

6 MR. TRIENENS: Yes. Yes. They say your proposed
7 financing -- Congress said you're supposed to look at the
8 financial set up FERC. So they look at the financial proposal.
9 They say, we don't like it. It ought to be modified this way
10 or that way.

11 QUESTION: Would it be concerned only with the
12 construction of facilities for the transportation of gas,
13 rather than some unrelated business that the holding company
14 might be going into? I mean, FERC wouldn't get into that in
15 terms of securities?

16 MR. TRIENENS: The answer is twofold. The answer is
17 first as to the certificate power, they would only get into it
18 as to the construction of the project being certificated.

19 Secondly, as to the baseball teams, Disneyland like
20 parks, and all these other things, --

21 QUESTION: Or any other legitimate business activity
22 that the company might be engaged in.

23 MR. TRIENENS: The answer is that as to the
24 certification power, FERC would not. It would get into its
25 finances in other ways, and the practical answer to that is you

1 would never in the world buy a baseball team through a FERC
2 regulated corporation. You just would be out of your mind to
3 put a profitable baseball team in a FERC accounting and FERC
4 regulated --

5 QUESTION: Well, don't talk baseball. There may be
6 some other unrelated business, and it does seem to me the State
7 might have the only regulatory power in terms of securities
8 issuance to finance some other sort of business, other than the
9 immediate project for the gas certificate.

10 MR. TRIENENS: The only business that these two
11 entities before the Court, Pipeline and Storage are in, are the
12 transportation and storage of natural gas. They do nothing
13 else, they intend to do nothing else. And our companies have
14 done a lot of diversifying. We've bought coal mines, we've
15 bought truck companies. But we never do it at the FERC
16 regulated corporate level. We do it through the holding
17 company.

18 Bear in mind, these two entities are a long way from
19 any company that holds public stock. The public holds stock in
20 a company called Coastal, a Delaware corporation with offices
21 in Texas, Coastal has a holding company that owns ANR which is
22 a holding company, and only then do you get the ANR Pipelining
23 Corporation and ANR Storage Company.

24 QUESTION: Certainly some of the corporate
25 interrelationships in the days of Samuel Insull and so forth

1 caused concern among lots of people. It wasn't just buying a
2 baseball team, but it was the loan structure and debt structure
3 from the parent to the subsidiary.

4 I don't think that's an unreasonable concern on the
5 part of the State.

6 MR. TRIENENS: The Public Utility Holding Company
7 Act, when the company is subject to it, did deal with those
8 matters. It's true that somebody, either Congress or the
9 States, has a highly legitimate interest in worrying about over
10 leveraging, over capitalization, all the evils, all the
11 financial evils of the Insull era. And here's how it works.

12 As to the certification power, the FERC looks at the
13 initial financing proposal. As to the rate making power, the
14 debt equity ratio is a crucial part of that. Now, it is true
15 that it is only rare that the FERC exercises that power to
16 grant rates that impute a different capital structure. And the
17 reason it's rate is that FERC has made its standards so widely
18 known that you don't dare go otherwise. You're not going to
19 finance it in a way you know is going to get in trouble with
20 FERC so you always keep within a reasonable bounds because FERC
21 makes you. That takes care of over leveraging.

22 Now, over capitalization which, if you read the
23 Michigan Supreme Court decisions, you'd think is the principal
24 evil. Just what is it. And the Michigan Supreme Court
25 correctly defines over capitalization as did counsel. It's a

1 lack of correlation between the debt and equity on the
2 liability side with the amount or value of the property.
3 That's the problem, lack of correlation. Used to call it
4 watered stock, same problem.

5 That cannot happen under a FERC regulated company,
6 and the reason is, apart from certification, apart from rate
7 making, FERC regulates the accounting, and if there's anyone in
8 this world it was Charlie Smith, the head of the Bureau of
9 Accounts of the FPC, who was the most vigilant original cost
10 proponent and insisted on original cost accounting. So the
11 assets all have to be at original cost net and the liabilities
12 debt and equity has to balance and there cannot be over
13 capitalization on a FERC regulated company. It cannot happen.

14 Now, there's one other thing. They say, what if
15 there were financial ruin. Well, if there's financial ruin,
16 there's something wrong at FERC because one of their duties is
17 not only to protect rate payers but to have a financially
18 healthy entity. But if something goes wrong and there is
19 financial trouble, you have to go to FERC to get an abandonment
20 order. You can't just stop serving people in Michigan. You
21 have to go to FERC to abandon service no matter what your
22 financial situation is.

23 So in all elements, FERC regulates these securities.
24 Here's where the problem comes in. The problem comes in after
25 you get a FERC certificate. And here you are, you've told them

1 you're going to raise \$50 million in bonds to finance this FERC
2 certificated project. Now, what do you do. You go to your
3 investment banker in New York, and they advise you on timing
4 and placement.

5 As far as placement's concerned, it could be
6 domestic, it could be a Eurobond deal. Our last offering was a
7 \$50 million equivalent of Swiss francs, not registered, so
8 nobody in this country could buy it, Michigan or anybody else.
9 Nobody could buy it here. And then the other problem whether
10 it's domestic or foreign is the timing. The timing is
11 everything in financing.

12 You go to these investment bankers and they say, oh,
13 wait a minute. Hold up a month or two. We think interest
14 rates are going up, and you'll save a couple of basis points.
15 Or, get it our right away, we think interest rates are going
16 up. And the timing is everything in this, and that's exactly
17 where this Michigan statute intrudes on the Federal process.

18 Because Michigan says, you've got to come trotting in
19 with your \$50 million proposal to issue securities to finance a
20 FERC certificated project.

21 QUESTION: If you were doing it in the State, you'd
22 be subject to the State Blue Sky Laws in any case, wouldn't
23 you?

24 MR. TRIENENS: Oh, my, yes.

25 QUESTION: So your timing argument, you know, it

1 frustrates the company's best interest, but that doesn't mean
2 the State can't do it.

3 MR. TRIENENS: Or the company can go to Europe, or
4 the company can decide not to sell in Michigan, or the company
5 can get a Blue Sky which is a very automatic thing. But the
6 Michigan investors are clearly protected by the Michigan Blue
7 Sky laws. They don't need any protection to the Swiss buying
8 this issue. They're protected by that. They don't need this
9 statute to protect that interest. That's the point.

10 But no matter where the issue is, and no matter how
11 urgent the timing, the Michigan Commission is here insisting
12 that they have a right to have the securities blocked until
13 there's an affirmative order by the Commission. Now, with
14 timing being everything, sure, lots of times, they'll come in
15 and issue it in three weeks, so you know, so you've got some
16 expense. You've got expense of preparing the application,
17 you've got a filing fee. All of that is in our view
18 unconstitutional, but that isn't the real evil here.

19 The real evil is they just don't approve it. Or they
20 set it for hearing, which is the same thing as not approving
21 it. And the hearing can go on, or the hearing never gets set.
22 We had one that I'll give you in a minute that went on for a
23 year.

24 Why do they do this? What interest does Michigan
25 have? And I can speculate on a lot of local interests that

1 they could try, collateral unrelated local interests that they
2 could try to invoke and try to pressure ANR by just holding the
3 securities hostage. But let me give you an actual and it's the
4 same incident, but not quite the same story as you were told
5 about. It's the divestiture of Michigan Consolidated by ANR,
6 the parent.

7 Now, bear in mind, there's two quite separate sets of
8 securities here. One set has to do with the divestiture and at
9 record 118 and 123, the Michigan Commission wanted to
10 investigate that, and they got out orders to investigate it.
11 The orders were directed at MichCon. That's the company the
12 regulate. They were directed at MichCon. They asked ANR to
13 come along and participate, and we did.

14 But the orders were directed at MichCon and properly
15 so. Now, over here in a totally unrelated transaction, FERC
16 had issued certificates to enable Storage to expand its storage
17 facilities and pipelines, \$105 million, some such amount. In
18 order to get the underwriter's counsel to go along with it,
19 they had to either get a Court order saying this Michigan
20 Statute didn't apply, or go get an order proving these
21 securities.

22 So we go over to the Commission. We file a nice
23 routine application, and while this is going on, this wholly
24 unrelated construction approved by FERC, financing approved by
25 FERC, nothing to do with the divestiture fight that's going on

1 over here about who gets which assets. So what does the
2 Commission do? It holds hostage the storage application. And
3 you'll find --

4 QUESTION: This is a facial attack, isn't it, Mr.
5 Trienens. I mean, it isn't what might have happened in a
6 particular situation. You're saying the statute is just
7 unconstitutional however Michigan applies it?

8 MR. TRIENENS: That's correct, and I'm also saying
9 that we're not speculating about it because this club in the
10 closet -- to use a phrase in the reply brief -- has been taken
11 out of the closet and we still feel the bruises from it. So
12 this is not a hypothetical case I'm talking about, it is
13 facial. The statute is wrong on its face as applied to this
14 company.

15 I'm saying that this example they give of how
16 wonderful it was for Michigan proves the point that they use it
17 for unrelated purposes, they hold hostage these securities
18 necessary to finance a FERC authorized project, and they'll
19 hold it up until they get what they want. You'll find that the
20 record stipulates that the way we got the certificate for
21 storage was by settling the other case. And November 24, 1981,
22 happens to be the date we made our deal with the State and
23 happens to be the date that they let this security out of
24 hostage and approved it.

25 It was part of that deal and it was putting leverage

1 on us. Now, let's look on the facial part of this Statute to
2 the future. We have a stipulation in the record of what this
3 statute means to Michigan. And the stipulation at record page
4 60 says that, even without regulatory authority that they have
5 all over these other local utilities, the Michigan Commission
6 can still exert influence over pipeline and storage if it has
7 the right to regulate the security issuances. They can still
8 exert influence. That's what this is about.

9 Now, let me give you an example of what they have in
10 mind for the future. And in their brief at page 5, note 3,
11 they tell you. They tell you that what they're interested in
12 here, and why they want this statute, and bear in mind the club
13 in the closet routine, --

14 QUESTION: Mr. Trienens, any legitimate State
15 authority can be abused. I mean your companies surely have to
16 get construction permits to building buildings or to connect
17 telephone lines or whatever. They're are innumerable ways in
18 which the State can hold up your company if it wants to. But
19 that isn't an argument against the validity of those State
20 authorities.

21 MR. TRIENENS: It seems to me it's an argument when
22 they say, oh, this is facial and you're speculating and we come
23 and petition this Court because they're just speculating about
24 things to tell you not only what they did with this Statute,
25 but what they plan to do with it. And this is what they say in

1 their brief.

2 They want this Statute because it provides an
3 opportunity for the Michigan Commission to assure that ANR does
4 not violate the divestiture settlements. Now, the divestiture
5 settlements they're talking about are the same settlements --
6 and I was going to say, blackjacked out of us -- but I'll honor
7 the nomenclature they now use -- these are the same settlements
8 they clubbed out of us before, and how instead of enforcing
9 those settlements which are agreements, actual signed
10 agreements, instead of enforcing those agreements the old
11 fashioned way by going to court to sue on the contract, they
12 want this club to hit us over the head to make sure we honor
13 whatever interpretation they want to place on it.

14 That's what this case is about. It's the only use
15 they have for it. But they've got so used to using it on us,
16 they want to keep it. Now, that's not a legitimate use. And
17 I agree with everything that's said that these examples are not
18 necessary. Maybe we showed the wounds too badly but with or
19 without these examples, past and future, this is a plain flat
20 out violation of the Commerce clause.

21 Now, we cited not only the 1925 cases but the case
22 last year in Brown-Forman and there's a two-tiered test and
23 this doesn't make it past tier one. Because, as the Court
24 said, it's a violation, you can't require a company to seek
25 regulatory approval in one State before undertaking a

1 transaction in another. You can't make us go to Michigan to
2 get approval to finance securities to build something in the
3 Gulf. It's a violation of the Commerce clause.

4 And although there's only one State doing this now,
5 what's to stop Wisconsin, if this Court says this is grand for
6 Michigan, why shouldn't Wisconsin do it. They've got as much
7 interest. Milwaukee's almost as big as Detroit. They've got
8 almost as much interest. Why invite them to have a races to
9 vie with each other as to how much they can extract from ANR?
10 What's the point of that?

11 Now, it's really unnecessary in our view under the
12 Commerce Clause to get to the second balancing test, but if you
13 were to get there and the Court below is correct, what interest
14 do they have? They cite in their reply brief from the Michigan
15 Supreme Court saying that securities regulation serves the
16 interest of the rate payers in assuring continued service and
17 in receiving that service at reasonable rates. The rates are
18 just and reasonable as fixed by the FERC. They can't
19 discontinue service without going to the FERC. Storage doesn't
20 even handle gas that's burned in Michigan.

21 QUESTION: This is a Commerce Clause argument, not a
22 preemption argument?

23 MR. TRIENENS: So far. Next is. We have raised both
24 points. The Court below agreed on both points.

25 But as to the Commerce Clause, we think there's no

1 interest. As I said, the over capitalization theme which the
2 Michigan Courts and counsel stress, that cannot happen under
3 FERC regulations, and interests of investors is totally taken
4 care of.

5 So the Commerce Clause test and the so-called
6 preemption test really somewhat overlap in this area because of
7 the history. It was so clear from the Missouri v. Kansas Gas
8 and related decisions that in 1938 by the time Congress go
9 around to breaking its silence, it was so clear that the States
10 could not interfere, the power of regulation could not reach
11 these kind of companies, that Congress came in and they
12 occupied the field. This is not a preemption case like Rice v.
13 Santa Fe Elevator where the States had long been traditionally
14 regulating grain elevators since Mond v. Illinois.

15 All of a sudden Congress comes in in that case with a
16 non-comprehensive statute, Warehouse Act, and the question is
17 whether they had preempted longstanding State regulation. This
18 is not what this is about at all.

19 The purpose of this Statute, as this Court has said a
20 dozen times, is to occupy the field in which the Supreme Court
21 has held the States may not act. And that's clearly this
22 company and this field and this activity. And having occupied
23 the field, having decided to in that comprehensive regulation
24 instead of just delegating it to the States and staying silent,
25 its all occupied by the FERC authority.

1 Now, this preissuance approval, as I said, is just
2 one regulatory tool of many. And when the Statute I mentioned
3 earlier, the FPC proposal, had been narrowed down to whether
4 the FERC should be given this added power, the focusing on that
5 issue, the parties came in, the industry came in and said, who
6 needs it. They don't need it. They've got plenty. They've
7 got certification, they've got regulation of rates, they've got
8 the accounting. Who needs it. And Congress didn't act. It
9 was perfectly obvious they weren't persuaded that FERC needed
10 this additional power. But whether they thought they did or
11 not, Congress had occupied the field that this Court had said
12 the States could not enter. The Court had drawn a bright line
13 as the Court has put it. Congress occupied the field from a
14 bright line that the States couldn't occupy and Congress
15 occupied this field and therefore it's preempted.

16 Now, bear in mind while this is a facial attack on
17 this Statute, it has no affect, no affect on the application of
18 this Statute to the local distribution companies as to which
19 the States always could act. This case has nothing to do with
20 that. It only applies to this one State and applies to ANR
21 which doesn't to any end user business in Michigan and is about
22 as clear and clean and purely exclusively an interstate company
23 as you'll ever find.

24 QUESTION: Mr. Trienens, you argue both preemption
25 and the commerce clause. Which one should we approach first?

1 MR. TRIENENS: Well, that's a difficult question to
2 answer, Justice White, in this sense. When you start dealing
3 with --

4 QUESTION: Well, we're going to have to -- I suppose
5 we'll have to make up our mind as to which one to deal with
6 first?

7 MR. TRIENENS: Yeah. I think the way you do it is
8 the way you've done it in a dozen cases. Is you go into the
9 history of the Federal Power Act, the Natural Gas Act, and you
10 say here were the Constitutional decisions that led to that
11 Act, here was the line that was drawn, here's the field they
12 covered, and that's the end of it.

13 QUESTION: Is what you call a preemption argument, is
14 that it?

15 MR. TRIENENS: Yeah, when they occupied the field.

16 QUESTION: I suppose at bottom that's a
17 constitutional issue?

18 MR. TRIENENS: It's a Supremacy Clause argument.

19 QUESTION: But sometimes it's called sort of a
20 statutory?

21 MR. TRIENENS: I think the logic is you get to that
22 first, although when you get into the Commerce Clause history
23 to show --

24 QUESTION: Well, what if we agreed with you on that?
25 Should we deal with the other?

1 MR. TRIENENS: I wouldn't feel that you'd be obliged
2 to at all, no.

3 QUESTION: Well, which point would you like us to
4 agree with you on?

5 MR. TRIENENS: I'm tempted to answer that in a more
6 flip way than I ought to, but I won't.

7 QUESTION: Either one, I suppose, yeah. You want to
8 win.

9 MR. TRIENENS: That's correct. I think the logic is
10 that you deal with the history of this. You get into the fact
11 that Congress did act, and I think that's the end of it. I
12 know there's a lot of controversy about commerce clause cases,
13 and you don't have to really decide this as though Congress had
14 not acted, because Congress has acted.

15 QUESTION: So you don't think there's any real
16 inconsistency in saying, of course, this is not preempted but
17 it violates the Commerce Clause?

18 MR. TRIENENS: All I'm saying is, it violates the
19 Commerce Clause if there'd never been a Natural Gas Act.

20 QUESTION: Well, then suppose we disagree with you on
21 preemption that Congress never intended to preempt this kind of
22 thing, but nevertheless, it violates the Commerce Clause, a
23 dormant Commerce Clause?

24 MR. TRIENENS: That's surely our position.

25 QUESTION: Well, you haven't answered my question,

1 yet, I guess.

2 MR. TRIENENS: Well, if I have to take a choice, I
3 think I'd write the opinion dealing with the legislation first,
4 and that would be the end of it.

5 Thank you.

6 CHIEF JUSTICE REHNQUIST: Thank you, Mr. Trienens.
7 Mr. Keskey, you have one minute left.

8 ORAL ARGUMENT OF DON L. KESKEY, ESQ.

9 ON BEHALF OF PETITIONERS - REBUTTAL

10 MR. KESKEY: Your Honor, this is a facial attack.
11 There has been no problem with Michigan's Act. We are at a
12 disadvantage to argue from a record that doesn't exist with
13 respect to either interstate commerce or preemption. The
14 burden of proof is on Respondents. We have no record.

15 Secondly, look at Rice v. Santa Fe Elevator. That
16 takes care of Your Honor's rate question because in that we
17 have an analogous situation where this Court preserved the
18 securities regulation even though the Federal Government took
19 over all other aspects including rates. And it found the
20 purposes that the State could continue.

21 Interstate Commerce, there's no discriminatory
22 affect, no discriminatory purpose. The Congress itself has
23 recognized that uniformity's not necessary with securities
24 regulation over interstate utilities. It has done so in
25 Federal Power Act 204. How are you going to distinguish in any

1 rational sense interstate natural gas companies from interstate
2 electric companies when those two Acts grew out of the same
3 purpose, the same history. And this Court has interchangeably
4 interpreted both Acts.

5 Congress when it passed the Natural Gas Act displayed
6 a willingness to allow the States to regulate securities
7 because it provided for no preemption. You don't have
8 preemption by silence. And Congress recognized that the States
9 could regulate securities, uniformity was not required.

10 CHIEF JUSTICE REHNQUIST: Thank you, Mr. Keskey. The
11 case is submitted.

12 (Whereupon, at 10:56 a.m., the case in the above-
13 entitled matter was submitted.)

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DOCKET NUMBER: 86-986

CASE TITLE: Eric J. Schneidewind, et al vs. ANR Pipeline Co
and ANR Storage Company

HEARING DATE: November 2, 1987

LOCATION: Washington, D.C.

I hereby certify that the proceedings and evidence
are contained fully and accurately on the tapes and notes
reported by me at the hearing in the above case before the
Supreme Court of the United States
and that this is a true and accurate transcript of the case.

Date: November 10, 1987

Margaret Daly
Official Reporter

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