

**FEDERALISM AND THE TELEPHONE: THE  
CASE FOR PREEMPTIVE FEDERAL  
DEREGULATION IN THE NEW WORLD OF  
INTERMODAL COMPETITION**

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## INTRODUCTION

The Commerce Clause was written into the Constitution in 1787 to address the universally recognized need to rescue “commerce among the several states” from “the embarrassing and destructive consequences, resulting from the legislation of so many different States, and to place it under the protection of a uniform law.”<sup>1</sup> Interstate commerce must be federally regulated, and the most natural subjects for exclusive federal regulation are network industries—trucking, railroads, and airlines—whose operations and markets span multiple state borders. Congress has recognized as much in each such industry by consistently following an evolutionary regulatory path of preempting inefficient state-by-state regulation when the industry’s network became largely interstate in nature, and then deregulating the industry entirely when its network had matured to the point where the forces of competition could be relied upon to operate freely. Deregulation of these interstate network industries invariably lowered prices, improved service, and spurred innovation and competition.

Major segments of the modern telecommunications industry, such as wireless telephony, broadband services, and certain types of Internet telephony, have largely been freed from state-by-state regulation, but there are some notable exceptions where telecommunications regulation has not caught up with the contemporary state of technology and the national regulatory model inherent in the Commerce Clause. Traditional wireline telephone service is the most extreme example: it is the primary vestigial remnant of state regulatory authority over telecommunications. Continuing state-by-state regulation of local wireline, notwithstanding that wireless, long distance, broadband, and Internet-based phone service have not only been taken under preemptive federal regulation, but have been significantly deregulated as well, ignores—and obscures—the fact that all of the various telecommunications media are rapidly converging. The classifications that have underpinned disparate regulatory treatment for different technologies have become irrelevant.

The current model of dual federal-state regulation of local telephone service may have been appropriate in an era when wireline telephony was the only telecommunications technology, when phone companies were local monopoly franchises, and when the distinction between “intrastate” and “interstate” calls was factually meaningful. But that world no longer exists. There is little, if anything, about today’s

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1. *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 11 (1824) (argument of counsel Daniel Webster).

wireline telephone networks that is truly “local” and that could therefore justify the inertial perpetuation of state-by-state regulation. The computer servers, databases, routers, and switches that make up modern telephone networks can serve many millions of callers and can be efficiently located thousands of miles from the customers they serve—and from the multiple state commissions that regulate them. “Local” calls to one’s neighbors or one’s voicemail service are now routinely routed through and processed by such out-of-state facilities.

State public service commissioners are concerned only with the small portion of a vast centralized telephone network that lies within their state’s borders and serves their state’s consumers. The parochial perspective of local regulators is inherently at war with the national perspective necessary to regulate an interstate network. Such a balkanized regulatory regime is particularly hard to justify when Congress and the Federal Communications Commission (“FCC” or “the Commission”) have largely deregulated other competing sectors of the telecommunications industry. Local wireline should now be understood as part of one enormous, national, multimodal telecommunications system that includes not only local and long-distance wireline, but also wireless networks, cable networks, and the Internet. These different modes of telecommunications use many of the same facilities even though they are subjected to different regulatory regimes: a “wireless” call involves wireline transmission via backhaul on a landline from a cell tower to the call’s ultimate destination, be it a wireline phone or another cell phone; “long-distance” calls travel over much of the same physical network as “local” wireline calls; a Voice over Internet Protocol (“VoIP”) call may be transported over the Internet, and VoIP customers may reach the Internet through broadband services that are delivered over the very same copper wires or fiber-optic cables that furnish those same customers’ traditional local wireline telephone service. In this telecommunications menagerie, purebred “local” telephone calls are an endangered species. Hybrids are becoming the norm: local wireline subscribers call out-of-state cell phone subscribers; cell phone subscribers call VoIP subscribers; cable telephony subscribers call local wireline subscribers and get forwarded to a cell phone, which may be traveling with the subscriber thousands of miles from home.

When the Telecommunications Act of 1996 (“1996 Act”) opened up local wireline telephony to competition but perpetuated state-by-state regulatory supervision, neither cellular telephones nor cable telephony nor VoIP constituted genuine competition for traditional local telephone service. That is no longer the case. Preemptive federal deregulation has allowed wireless and broadband to attract the investment and innovation that have fueled explosive growth. Wireline now competes directly with

other modes of telecommunications. This profound shift in the competitive structure of the telecommunications industry warrants similar federal regulatory treatment for local wireline phone companies. Indeed, both wireless telephony and multichannel video services continue to suffer from vestigial state and municipal regulation that is unwarranted in the modern world of national intermodal competition across telecommunications services.

Although these themes may seem familiar enough when considered in isolation, which is the norm, here we will consider them together. Recent telecommunications scholarship is wanting because it treats these economic and legal developments as isolated and unrelated phenomena: for example, articles on issues of federalism in telecommunications regulation ignore the impact of intermodal competition,<sup>2</sup> while articles discussing the rise of intermodal competition proceed without consideration of the defining importance of federalism.<sup>3</sup> Even those

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2. See, e.g., Thomas W. Bonnett, *Is ISP-Bound Traffic Local or Interstate?*, 53 FED. COMM. L.J. 239 (2001); Reza Dibadj, *Competitive Debacle in Local Telephony: Is the 1996 Telecommunications Act to Blame?*, 81 WASH. U. L.Q. 1, 16 n.96 (2003) (dismissing intermodal competition); Kyle D. Dixon & Philip J. Weiser, *A Digital Age Communications Act Paradigm for Federal-State Relations*, 4 J. ON TELECOMM. & HIGH TECH. L. 321 (2006); Douglas C. Sicker, *The End of Federalism in Telecommunication Regulations?*, 3 NW. J. TECH. & INTELL. PROP. 130 (2005); Paul Teske, *Digital Age Communications Law Reform: With the States? Comments on the DACA Federal-State Framework*, 4 J. ON TELECOMM. & HIGH TECH. L. 365 (2006); Philip J. Weiser, *Federal Common Law, Cooperative Federalism, and the Enforcement of the Telecom Act*, 76 N.Y.U. L. REV. 1692 (2001); Philip J. Weiser, *Towards a Constitutional Architecture for Cooperative Federalism*, 79 N.C. L. REV. 663 (2001); Philip J. Weiser, *Cooperative Federalism and its Challenges*, 2003 MICH. ST. L. REV. 727 (2003); D. Stan O'Loughlin, Note, *Preemption or Bust: Fear and Loathing in the Battle Over Broadband*, 28 CARDOZO L. REV. 479 (2006); Michelle Reed, Note, *"Arising Under" Jurisdiction in the Federalism Renaissance: Verizon Maryland Inc. v. Public Service Commission of Maryland*, 2002 B.Y.U. L. REV. 717 (2002).

3. See, e.g., Ray G. Besing, *The Telecommunications Act of 1996: A Case of Regulatory Obsolescence*, 13 COMMLAW CONSPECTUS 1 (2005); Jim Chen, *The Echoes of Forgotten Footfalls: Telecommunications Mergers at the Dawn of the Digital Millennium*, 43 HOUS. L. REV. 1311 (2007); David Cohen & Edward D. Kania, *The Future of the Communications Industry: New Products, New Services, The Need for New Regulatory Paradigms*, 13 COMMLAW CONSPECTUS 1 (2005); George S. Ford & Lawrence J. Spiwak, *Set It and Forget It? Market Power and the Consequences of Premature Deregulation in Telecommunications Markets*, 1 N.Y.U. J. L. & BUS. 675 (2005); Rob Frieden, *Adjusting the Horizontal and Vertical in Telecommunications Regulation: A Comparison of the Traditional and a New Layered Approach*, 55 FED. COMM. L.J. 207 (2003); Kenneth Katkin, *Cable Open Access and Direct Access to INTELSAT*, 53 CASE W. RES. L. REV. 77 (2002); J. Steven Rich, *Brand X and the Wireline Broadband Report and Order: The Beginning of the End of the Distinction Between Title I and II Services*, 58 FED. COMM. L.J. 221 (2006); J. Gregory Sidak, *The Failure of Good Intentions: The WorldCom Fraud and the Collapse of American Telecommunications After Deregulation*, 20 YALE J. ON REG. 207 (2003); Daniel F. Spulber & Christopher S. Yoo, *Access to Networks: Economic and Constitutional Connections*, 88 CORNELL L. REV. 885 (2003); Philip J. Weiser, *Toward a Next Generation Regulatory Strategy*, 35 LOY. U. CHI. L.J. 41 (2003); Richard S. Whitt, *A Horizontal Leap Forward: Formulating a New Communications Public Policy Framework Based on the*

commentators who do discuss federalism's role in telecom regulation often offer oversimplified, ahistorical notions of federalism.<sup>4</sup> "Federalism" cannot be facetly equated with blanket deference to state authority and autonomy. On the contrary, when it comes to the regulation of truly interstate commercial networks—be they networks of transportation (such as steamships and airlines), distribution (such as electricity and natural gas), or communication (such as wireline telephony and the Internet)—the central point of the Constitution, and in particular its Commerce Clause, was to lodge power in the national rather than the several state governments.

In the pages that follow, we present the case for immediate federal preemption of state regulation of local wireline telecommunications services, as well as the case for eliminating the unwarranted vestiges of state and municipal regulation of wireless telephony and multi-channel video services.

In Part I, we turn to the genesis of the Commerce Clause and demonstrate that its very purpose—indeed, the primary moving force behind adoption of the Constitution itself—was to permit the development of a single, national body of regulation to govern interstate

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*Network Layers Model*, 56 FED. COMM. L.J. 587 (2004); Richard E. Wiley, *Current Regulatory Realities: Overcoming the Regulatory Quandary*, 2003 MICH. ST. L. REV. 589; Orian J. Lee, Note, *Broadband Gladiators: Fostering Competition Between DSL and Cable Internet Through Mutual Deregulation*, 3 GEO. J. L. & PUB. POL'Y 663 (2005); see also Howard A. Shelanski, *Adjusting Regulation to Competition: Toward a New Model for U.S. Telecommunications Policy*, 24 YALE J. ON REG. 55 (2007) (proposing an entirely new model for national communications policy without mentioning "federalism"); James B. Speta, *Deregulating Telecommunications in Internet Time*, 61 WASH. & LEE L. REV. 1063, 1110, 1129, nn.215, 306 (2004) (examining intermodal competition and the impact of current federal regulation on facilities-based competition, but relegating federalism as such to the rare footnote); Jared S. Dinkes, Note, *Rethinking the Revolution: Competitive Telephony in a Voice over Internet Protocol Era*, 66 OHIO ST. L.J. 833, 867-70 (2005) (identifying inefficiencies arising from state-by-state regulation, but without discussing principles of federalism or their roots in the Constitution).

4. See, e.g., Barbara A. Cherry & Steven S. Wildman, *Preventing Flawed Communication Policies by Addressing Constitutional Principles*, 2000 MICH. ST. L. REV. 55, 56 (2000) (characterizing the Commerce Clause's conferral of power on the national government as an outdated "governance structure[] . . . intended to serve political objectives," despite the Framers' explicit economic objectives in embracing centralized control of interstate commerce) (the article never mentions the term "federalism"); Dibadj, *supra* note 2, at 50-51 (equating "historical" federalism with deference to state regulatory authority, despite Framers' unambiguous grant of power over truly interstate commerce to the federal government); Dixon & Weiser, *supra* note 2, at 330 (characterizing the "preempti[on] [of] state and local regulation" as subversion of the "values of regulatory federalism," despite Constitution's clear choice of national regulation of interstate networks); Jim Rossi, *Political Bargaining and Judicial Intervention in Constitutional and Antitrust Federalism*, 83 WASH. U. L.Q. 521, 572-73 (2005) (characterizing "federalism" in telecom regulation as "[b]lanket deference to state and local politics"); Sicker, *supra* note 2, at 131 (equating "a traditional style of federalism" with the balkanized regulation of interstate telecom networks by fifty different state regulatory bodies).

commerce.

Part II explains that interstate network industries are the quintessential subjects of preemptive federal regulations because they are inherently national and state-by-state regulation of such networks is simply unworkable. What is more, in network industry after network industry, a consistent historical pattern of regulatory development has evolved, moving from initial local or state regulation, to preemptive federal regulation, to federal deregulation. This regulatory pattern has invariably mirrored the historical development of the networks themselves, as they have grown from largely local facilities serving an intrastate market to vast networks serving regional or national markets.

Part III applies these lessons drawn from other national network industries to telecommunications, in particular to the cases of wireline telephony, wireless telephony, and multi-channel video services. State-by-state regulation of local wireline telephone service is an anachronism. The consistent historical pattern of preemptive federal regulation, followed by deregulation, has been accelerated for recent telecommunications technologies such as cellular telephones and Internet telephony, to the great benefit of consumers, while wireline telephone service remains mired in the regulatory morass of state-by-state regulation. Such disparate treatment of different technologies no longer makes sense because all of these networks—wireline, wireless, cable, and the Internet—now compete with one another as delivery vehicles not just for voice communications, but also for data transmission and video entertainment. In such a world of intermodal competition, state and local regulation of pieces of the telecommunications networks—as if they were separate industries that could actually be considered in isolation—is at war with the unifying imperative of the Commerce Clause.

Part IV offers three illustrations of this phenomenon of regulatory lag. The first, traditional local wireline telephone service, is the most extreme and the most in need of prompt redress. The regulatory history of wireline telephony has long since passed the point in the evolutionary process where exclusive federal regulation, as a prelude to deregulation, is necessary. “Local” telephone service has in fact become increasingly interstate and, driven by the market’s appetite for efficiency, would become far more interstate in nature but for the anachronistic regulatory overlay that arbitrarily deems many calls traveling across state lines as intrastate and thus subject to state-by-state regulation.

The second example is cellular telephones, where Congress has preemptively deregulated pricing and market entry, but left regulation of consumer protection issues to the states. The problem here is that state regulators are not happy with having been displaced so they are using the guise of consumer-protection regulation to reassert power over the terms

and rates of mobile telephone service.

The final case study is another example of local regulatory revanchism—cable television. Congress has eliminated exclusive cable TV franchises and decreed that the market for multichannel video programming distribution must be open to competition, particularly competition from telephone companies providing video entertainment over their new fiber-optic networks. But slogging through the local franchising process in each of the nation's 34,000 municipal jurisdictions is intolerably inefficient. Worse, many local franchising authorities are dragging their feet and in the most egregious cases trying to leverage their franchising power over telephone companies' video services in an attempt to reacquire something approaching the sweeping regulatory authority over local telephone service that they lost in 1996. Although the FCC announced in December 2006 that it would issue an order preempting oppressive and unreasonable local-franchising requirements, the matter will remain contentious because the Commission was narrowly divided and its order is likely to be challenged in court and perhaps in Congress. The various rationales offered for state and local regulators' resistance to preemptive national regulation of national electronic networks are unpersuasive and serve the interests of neither consumers nor the service providers as a whole.

As an FCC Commissioner recently observed, “[t]he United States is ranked number twenty-one in the International Telecommunications Union’s Digital Opportunity Index. It is difficult to take much comfort from being twenty-first in the Twenty-first century.”<sup>5</sup> Dramatic changes in network technology and intermodal competition have made state-by-state regulation an inefficiency that our national economy can no longer afford to indulge.

#### I. THE COMMERCE CLAUSE AND THE STATES’ CESSION OF CONTROL OVER INTERSTATE COMMERCE

One does not lightly displace the regulatory powers of sovereign states. The “Constitution, in all its provisions, looks to an indestructible Union, composed of indestructible States.”<sup>6</sup> The “preservation of the States, and the maintenance of their governments, are as much within

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5. Implementation of Section 621(a)(1) of the Cable Commc’ns Policy Act of 1984 as Amended by the Cable Television Consumer Prot. & Competition Act of 1992, *Report & Order & Further Notice of Proposed Rulemaking*, 22 FCC Rcd. 5101, 5192 (2006) [hereinafter *Video Franchising Order*], available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-06-180A3.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-06-180A3.pdf) (dissenting statement of Michael J. Copps, Comm’r, FCC).

6. *Texas v. White*, 74 U.S. (7 Wall.) 700, 725 (1869), *quoted in* *New York v. United States*, 505 U.S. 144, 162 (1992).

the design and care of the Constitution as the preservation of the Union and the maintenance of the National government.”<sup>7</sup> Even James Wilson, one of the most influential of the Constitution’s Framers and among the most nationalist in his thinking, insisted that the federal government, “instead of placing the state governments in jeopardy, is founded on their existence. On this principle, its organization depends; it must stand or fall, as the state governments are secured or ruined.”<sup>8</sup>

And yet the states’ act of unification more than two centuries ago—the *very fact of the Union*—necessarily focuses our attention not on some abstract inquiry as to what regulatory powers the states may have theoretically enjoyed when they were independent sovereigns, but rather on which particular powers they retain in the specific federal system that they negotiated and recorded in the Constitution. The Tenth Amendment “expressly declares the constitutional policy that Congress may not exercise power in a fashion that impairs the States’ integrity or their ability to function effectively in a federal system.”<sup>9</sup> The particular “federal system” into which the states chose to unite themselves divides sovereign power vertically between the federal government and the state governments. The central question at the time of the Constitution’s drafting and adoption was how that power should be divided, and the particular historical genesis of our federal system was the problem of “commerce among the several states.” When the colonies’ victory over Great Britain “relieved the Colonies from the pressure for solidarity that war had exerted, a drift toward anarchy and commercial warfare between states began,” with each state “legislat[ing] according to its estimate of its own interests, the importance of its own products, and the local advantages or disadvantages of its position in a political or commercial view.’ This came ‘to threaten at once the peace and safety of the Union.”<sup>10</sup> Under the Articles of Confederation, the national government was powerless to suppress such internecine economic strife; “the Framers intended the Commerce Clause as a cure for these structural ills.”<sup>11</sup>

The Constitutional Convention was held in 1787 precisely because the states had shown themselves to be, by their very nature as separate and competing sovereigns, incompetent to regulate interstate and foreign

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7. *Id.*

8. James Wilson, Summation and Final Rebuttal, *reprinted in* 1 THE DEBATE ON THE CONSTITUTION 841 (Bernard Bailyn ed., 1993) (speech to the Pennsylvania Ratifying Convention, December 11, 1787).

9. *Fry v. United States*, 421 U.S. 542, 547 n.7 (1975).

10. *H.P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 533 (1949) (quoting JOSEPH STORY, 1 COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES §§ 259, 260 (1833)).

11. *Quill Corp. v. North Dakota*, 504 U.S. 298, 312 (1992) (citing THE FEDERALIST Nos. 7, 11 (Alexander Hamilton)).



commerce. Widespread dissatisfaction with the regulation of commerce was not merely *one* cause of the Constitutional Convention—it was *the cause*. The impetus to the gathering of the states, first in Annapolis and then in Philadelphia, was the universally recognized need:

[T]o regulate commerce; to rescue it from the embarrassing and destructive consequences, resulting from the legislation of so many different States, and to place it under the protection of a uniform law. . . [T]he great topic, urged on all occasions, as showing the necessity of a new and different government, was the state of trade and commerce.<sup>12</sup>

The “sole purpose” for which the State of Virginia named commissioners and proposed the meeting among the states which ultimately produced the Constitution was its resolution “to take into consideration the trade of the United States; to examine the relative situations and trade of the said States; to consider how far a uniform system in their commercial regulations may be necessary to their common interest and their permanent harmony.”<sup>13</sup>

As Daniel Webster explained in his argument to the Supreme Court in the seminal case of *Gibbons v. Ogden*, the:

[R]esolutions of Virginia, in January, 1786, which were the immediate cause of the convention, put forth this same great object. *Indeed, it is the only object stated in those resolutions. There is not another idea in the whole document.* The entire purpose for which the delegates assembled at Annapolis, was to devise means for the uniform regulation of trade.<sup>14</sup>

However much the Revolution may have been driven by political theory, the replacement of the Articles of Confederation with the Constitution was driven by economic imperatives.

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12. *Gibbons*, 22 U.S. at 11 (argument of counsel Daniel Webster).

13. *H.P. Hood & Sons*, 336 U.S. at 533 (quoting Documents Illustrative of the Formation of the Union, H.R. DOC. NO. 69-398, at 38 (1st Sess. 1927)); see also Motion of Virginia General Assembly, Jan. 21, 1786, *reprinted in*, 1 THE FOUNDERS' CONSTITUTION 185 (Philip B. Kurland & Ralph Lerner eds., 1987) (“Resolved . . . to examine the relative situations and trade of the said States; to consider how far a uniform system in their commercial regulations may be necessary to their common interest and their permanent harmony”); Report of the Annapolis Convention, Sept. 14, 1786, *reprinted in* 1 THE FOUNDERS' CONSTITUTION 186 (“[T]he States of New York, Pennsylvania, and Virginia had, in substance, and nearly in the same terms, authorized their respective Commissioners . . . to take into consideration the trade and Commerce of the United States, to consider how far an uniform system in their commercial intercourse and regulations might be necessary to their common interest and permanent harmony.”).

14. *Gibbons*, 22 U.S. at 12 (argument of counsel Daniel Webster) (emphasis added).

Over whatever other interests of the country this government may diffuse its benefits, and its blessings, it will always be true, as matter of historical fact, that it had its immediate origin in the necessities of commerce; and, for its immediate object, the relief of those necessities, by removing their causes, and by establishing a uniform and steady system.<sup>15</sup>

In response, the Framers drafted the Commerce Clause: “The Congress shall have Power . . . To regulate Commerce . . . among the several states.”<sup>16</sup> The absolute necessity of uniform federal regulation for interstate commerce was the strongest argument in favor of ratification of the proposed Constitution.<sup>17</sup> As Alexander Hamilton declared in Federalist No. 22, “there is no object . . . that more strongly demands a Federal superintendence” than the “want of a power to regulate commerce.”<sup>18</sup> State-by-state regulation of interstate commerce, James Madison warned, “not only proved abortive, but engendered rival,

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15. *Id.*; see also *id.* at 224 (Johnson, J., concurring) (the Convention was called because the several States, “finding themselves in the unlimited possession of those powers over their own commerce, which they had so long been deprived of, and so earnestly coveted, that selfish principle which, well controlled, is so salutary, and which, unrestricted, is so unjust and tyrannical, guided by inexperience and jealousy, began to show itself in iniquitous laws and impolitic measures, from which grew up a conflict of commercial regulations, destructive to the harmony of the States”).

16. U.S. CONST. art. I, § 8, cl. 3.

17. The Framers recognized that the broad commerce power delegated to the national government created a risk that the “national government would use its power over commerce to the disadvantage of particular States.” *United States v. Ptasynski*, 462 U.S. 74, 81 (1983). When the constitutional convention’s Committee of Detail released its formulation of the Commerce Clause in the August 6, 1787 draft, delegate John Dickinson noted in the margin, next to the Commerce Clause, “no Preference or Advantage to be given to any persons or place – Laws to be equal.” THE RECORDS OF THE FEDERAL CONVENTION OF 1787 209 (Max Farrand ed., rev. ed. Supp. 1937) [hereinafter RECORDS OF THE FEDERAL CONVENTION]; see also 2 RECORDS OF THE FEDERAL CONVENTION, *supra*, at 211 (James McHenry); *id.* at 637 n.21, 639-40 (George Mason); 3 RECORDS OF THE FEDERAL CONVENTION, *supra*, at 333 (Alexander Hamilton); CHARLES WARREN, THE MAKING OF THE CONSTITUTION 575-76, 588 (1928). These widespread concerns led to the adoption of two constitutional provisions which barred the national government from discriminating against any particular State. The first was the Port Preference Clause, Art. I, § 9, cl. 6, which provides that “[n]o Preference shall be given . . . to the Ports of one State over those of another.” The second was the Uniformity Clause, Art. I, § 8, cl.1, which mandates that “Duties, Imposts and Excises shall be Uniform throughout the United States.” These limitations “were intended to allay . . . the fear that Congress might discriminate against certain of the States.” Warren, *supra*, at 588. “The clear and obvious intention of the articles mentioned was, that Congress might have no power of imposing unequal burdens; that it might not be in their power to gratify one part of the Union by oppressing another.” 3 RECORDS OF THE FEDERAL CONVENTION, *supra*, at 365-66 (Hugh Williamson); see also 2 RECORDS OF THE FEDERAL CONVENTION, *supra*, at 417-18 (James Madison); *id.* at 420 (James McHenry).

18. THE FEDERALIST No. 22, at 135-6 (Alexander Hamilton); see also THE FEDERALIST No. 42, at 283 (James Madison) (“The defect of power in the existing confederacy, to regulate the commerce between its several members, is in the number of those which have been clearly pointed out by experience.”).

conflicting and angry regulations.”<sup>19</sup>

Inherently interstate industries were fractured because each state regulated with an eye only to its own citizens and its own parochial interests, oblivious to the interests of and regulations imposed by other states. The practical impact of the Commerce Clause on the economic welfare of the new nation was illustrated by *Gibbons v. Ogden*. The immense commercial possibilities spawned by Robert Fulton’s steamboats were being strangled by conflicting state-by-state regulation from New York, New Jersey, and other states. The Supreme Court’s decision holding that the Commerce Clause made regulation of steamship traffic a federal prerogative was literally greeted with cheers from a grateful public. The first competing steamboats to arrive at the Fulton Street landing in lower Manhattan in the wake of the *Gibbons* decision were met by brass bands and cheering crowds firing cannon salutes. Fares were cut in half and, within a year, the number of steamboats operating out of New York City increased 700 percent.

In short, the regulation of interstate commerce was at once the principal concern that animated creation of the federal Union and the power that the states most unequivocally surrendered. “No other federal power was so universally assumed to be necessary, no other state power was so readily relinquished.”<sup>20</sup>

## II. THE HISTORY OF PREEMPTIVE FEDERAL DEREGULATION OF INTERSTATE-NETWORK INDUSTRIES

As the Supreme Court has observed through the years, some forms of commerce are “inherently interstate.”<sup>21</sup> This is particularly true with respect to those forms of commerce that depend upon national “networks,” where services or commodities are “constantly moving in interstate commerce.”<sup>22</sup> If the interstate network penetrates within the

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19. 3 RECORDS OF THE FEDERAL CONVENTION, *supra* note 17, at 547, *quoted in H.P. Hood & Sons*, 336 U.S. at 534.

20. *H.P. Hood & Sons*, 336 U.S. at 534.

21. *New York v. F.E.R.C.*, 535 U.S. 1, 31-32 (2002) (Thomas, J., concurring in part and dissenting in part); *see also id.* at 7 (opinion of the Court); *id.* at 16 (opinion of the Court); *Currin v. Wallace*, 306 U.S. 1, 9 (1939) (tobacco auctioned for foreign and out-of-state delivery is an “inherently interstate commodity”).

22. *F.E.R.C.*, 535 U.S. at 7; *see also id.* at 31-32 (Thomas, J., concurring in part and dissenting in part) (electricity transmission is “inherently interstate” because “[i]t takes place over a network or grid, which consists of a configuration of interconnected transmission lines that cross state lines”); *ACLU v. Johnson*, 194 F.3d 1149, 1160 (10th Cir. 1999) (“[T]he Supreme Court has long recognized that certain types of commerce are uniquely suited to national, as opposed to state, regulation.”) (discussing railroads and citing *Wabash, St. Louis & Pac. Ry. Co. v. Illinois*, 118 U.S. 557 (1886)); *id.* at 1162 (“As we observed, . . . certain types of commerce have been recognized as requiring national regulation. . . . The Internet is surely such a medium.”); *Am. Libraries Ass’n v. Pataki*, 969 F. Supp. 160, 169 (S.D.N.Y.

interior of a state, federal regulatory jurisdiction follows. “Commerce among the States, cannot stop at the external boundary line of each State, but may be introduced into the interior.”<sup>23</sup> And the federal power to regulate such commerce, likewise:

[W]as to be a[] unit; and the system by which it was to exist and be governed, must necessarily be complete, entire, and uniform. Its character was to be described in the flag which waved over it, E PLURIBUS UNUM. Now, how could individual States assert a right of concurrent legislation, in a case of this sort, without manifest encroachment and confusion?<sup>24</sup>

Nowhere has the wisdom of the Framers been more evident than in industries whose interconnected networks cut across state boundaries, such as the electric power, railroad, trucking, airline, and gas pipeline industries.<sup>25</sup> Historically, network industries have followed a consistent pattern of regulatory development, culminating in exclusive federal regulation, followed by deregulation once the forces of competition are sufficient to supplant government intervention in the marketplace. Networks are typically built one route at a time. The early regulatory issues are therefore primarily local, e.g., where to locate tracks, build roads, site airports, erect poles, and lay pipelines. Over time, as the local networks grow and connect to other local networks, they increasingly come to be used for interstate commerce. The need for unified federal regulatory authority—rather than diverse state regulation—grows with them. Absent federal preemption, jurisdictional boundaries will inevitably impose limits and burdens on the expansion and enrichment of services that naturally grow across geographic boundaries. As Justice Felix Frankfurter once wrote, “[t]he imposition upon national systems of transportation of a crazy-quilt of State laws would operate to burden commerce unreasonably.”<sup>26</sup> In general, the exercise of federal regulatory jurisdiction over network industries has typically begun with the imposition of a preemptive, uniform regulatory scheme, and ended with a uniform deregulatory mandate. This pattern has been repeated in industry after industry.

**Electricity Transmission.** Consider the case of commerce in the

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1997) (“[S]tate regulation of those aspects of commerce that by their unique nature demand cohesive national treatment is offensive to the Commerce Clause.”).

23. *Gibbons*, 22 U.S. at 194.

24. *Id.* at 14 (argument of counsel Daniel Webster).

25. *See, e.g.*, *Kassel v. Consol. Freightways Corp.*, 450 U.S. 662, 671 (1981) (“[W]here, as here, the State’s . . . regulations impair significantly the federal interest in efficient and safe interstate transportation, the state law cannot be harmonized with the Commerce Clause.”).

26. *Morgan v. Virginia*, 328 U.S. 373, 388 (1946) (Frankfurter, J., concurring).

transmission of electricity. When the Federal Power Act (“FPA”) was enacted in 1935, electricity was a local business. Utility companies were isolated systems usually limited to generating and providing power for single towns.<sup>27</sup> They were vertically integrated local companies that had constructed their own power plants, transmission lines, and local delivery systems. Interconnections among utilities were rare, and interstate connections were almost unheard of. They operated as separate, local monopolies subject to state or even local regulation.<sup>28</sup> The FPA drew a line between state and interstate power transmission and parceled out regulatory power accordingly. Although the statute reserved jurisdiction over interstate transmission of electricity to the federal government, there was virtually no commerce for it to regulate in 1935.

By the end of the century, things had changed dramatically. While interconnected networks and interstate transmissions were few and far between in 1935, today every high-voltage transmission line in the continental United States (outside Texas) is wired into one of two vast interstate grids. Thus, the electrical transmission system has become inherently interstate; the individual state regulatory territories initially defined by the FPA have been integrated into a unified federal territory.

In 1992 Congress enacted the Energy Policy Act, which expanded the authority of the Federal Energy Regulatory Commission (“FERC”), to allow independent power producers equal access to the utilities’ transmission grid.<sup>29</sup> Pursuant to that statute, in 1996 FERC issued Order No. 888, which mandated that, if a public utility “unbundles,” i.e., separates, the cost of transmission from the cost of electrical energy when billing its retail customers, the utility must also transmit competitors’ electricity over its lines on the same terms that the utility applies to its own energy transmissions.<sup>30</sup>

State public utility commissions (“PUCs”) challenged FERC’s authority to issue the order, emphasizing that most electricity used in the United States is generated in the state where it is used.<sup>31</sup> The PUCs argued that the federal commerce power could extend to electricity transmission only if FERC could show that essentially every electron used by a retail customer in each state was generated in a different state.<sup>32</sup>

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27. See J. DUNCAN GLOVER & MULUKUTLA S. SARMA, *POWER SYSTEM ANALYSIS AND DESIGN* 7 (2d ed. 1994); SYED A. NASAR, *ELECTRIC ENERGY SYSTEMS* 319 (1995); WILLIAM D. STEVENSON, *ELEMENTS OF POWER SYSTEM ANALYSIS* 2-3 (4th ed. 1982).

28. *F.E.R.C.*, 535 U.S. at 5.

29. See Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776 (1992) (codified as amended in scattered sections of 5, 15, 16, 26, 40, and 42 U.S.C.).

30. *F.E.R.C.*, 535 U.S. at 4-5 (upholding the FERC order).

31. Brief of Transmission Access Policy Study Group as Respondent at 5, *F.E.R.C.*, 535 U.S. 1 (No. 00-568).

32. *Id.* at 9 n.27.

A unanimous Supreme Court disagreed, holding that even if the power plant generating the electricity and the customer using it are located in the same state, the transmission of electricity is nevertheless interstate because the *network* that carries it is interstate. As the Court put it:

[U]nlike the local power networks of the past, electricity is now delivered over three major networks, or “grids,” in the continental United States. Two of these grids – the “Eastern Interconnect” and the “Western Interconnect” – are connected to each other. It is only in Hawaii and Alaska and on the “Texas Interconnect” – which covers most of that State – that electricity is distributed entirely within a single State. In the rest of the country, any electricity that enters the grid immediately becomes a part of a vast pool of energy that is constantly moving in interstate commerce.<sup>33</sup>

Indeed, even Justice Thomas, perhaps the Court’s most ardent defender of the constitutional prerogatives of the States, recognized that “transmissions on the interconnected national grids constitute transmissions in interstate commerce . . . because of the nature of the national grid” itself.<sup>34</sup> Electricity transmission is “inherently interstate” because “[i]t takes place over a network or grid, which consists of a configuration of interconnected transmission lines that cross state lines.”<sup>35</sup> Thus, the very nature of the commerce and the network on which it occurred took it outside the state’s borders and thereby subjected it to federal regulatory authority.

**Railroads.** When first developed early in the nineteenth century, railroads were local lines built for particular uses and sometimes even for particular users, such as the spur lines built to lakes in New England to enable ice merchants to transport their frozen wares to harbors for shipment overseas.

The basic railroad facilities of the United States were constructed under state authorization and restrictions by corporations whose powers and limitations were prescribed by state legislatures, or resulted from limitations on the states themselves. Construction in reference primarily to local or regional transportation needs created duplicating and competing facilities in some areas and provided inadequate ones in others.<sup>36</sup>

When local lines were eventually stitched together into a national network of growing importance, the railroad was still viewed as a natural

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33. *F.E.R.C.*, 535 U.S. at 7.

34. *Id.* at 16-17.

35. *Id.* at 31-32 (Thomas, J., concurring in part and dissenting in part).

36. *Schwabacher v. United States*, 334 U.S. 182, 191 (1948).

monopoly in need of comprehensive regulation.<sup>37</sup>

By the end of the nineteenth century, the public was growing increasingly dissatisfied with how the industry was being run.<sup>38</sup> In response, in 1887 Congress established the Interstate Commerce Commission (“ICC”)—the first federal regulatory commission—to regulate the services of common carriers engaged in interstate transportation.<sup>39</sup> The first job of the ICC was to manage competition and stabilize rates.<sup>40</sup> It was therefore given authority to set guidelines for how railroads could do business, to outlaw discriminatory rate-setting, to require railroads to submit annual reports, and to ban anticompetitive pools and cartels.<sup>41</sup> In 1906 and 1910, Congress extended the ICC’s authority to permit it to set what it considered “just and reasonable rates.”<sup>42</sup>

“But the stress and strain of World War I” demonstrated that “the railroads of the country did not function as a really national system of transportation. That crisis also made plain the confusions, inefficiencies, inadequacies and dangers to our national defense and economy flowing from the patchwork railroad pattern that local interests under local law had created.”<sup>43</sup> The demand for an integrated, efficient, and coordinated system of rail transport, equal to the needs of our national economy and defense, resulted in the Transportation Act of 1920.<sup>44</sup> A wave of mergers and consolidations in the public interest followed, leading to a national railway structure with regulated rates that endured for half a century.

This regulatory scheme was left in place for a long time—considerably too long, most observers now agree. By the 1970s, “nearly a third of U.S. railroads were in or close to bankruptcy,”<sup>45</sup> so Congress responded by enacting the Railroad Revitalization and Regulatory Reform Act of 1976<sup>46</sup> and the Staggers Rail Act of 1980.<sup>47</sup>

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37. See KIMBERLY VACHAL, *THE INTERSTATE COMMERCE COMMISSION: PAST AND PRESENT* 1 (1993), available at <http://www.ugpti.org/pubs/pdf/SP111.pdf>.

38. See Peter Ferrara, *Americans for Tax Reform: Policy Briefs, The Folly of Rail Regulation*, <http://www.atr.org/content/html/1999/090199pb.html> (last visited Mar. 20, 2008).

39. See Interstate Commerce Act, 24 Stat. 379 (1887).

40. See W. KIP VISCUSI ET AL., *ECONOMICS OF REGULATION AND ANTITRUST* 592 (4th ed. 2005).

41. See 24 Stat. 379; VACHAL, *supra* note 37, at 2.

42. Hepburn Act, Pub. L. No. 59-337, 34 Stat. 584 (1906); Mann-Elkins Act, Pub. L. No. 61-218, 36 Stat. 539 (1910).

43. *Schwabacher*, 334 U.S. at 191.

44. Esch-Cummings Act of 1920, Pub. L. No. 66-152, 41 Stat. 456 (repealed 1940).

45. Northeast Midwest Institute, *Rail Deregulation*, <http://www.nemw.org/raildereg.htm> (last visited Mar. 20, 2008).

46. Railroad Revitalization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, 90 Stat. 31 (codified as amended in scattered sections of 45 and 49 U.S.C.).

47. Staggers Rail Act of 1980, Pub. L. No. 96-448, 94 Stat. 1895 (codified as amended

Congress expressly found that continuing state regulation would be as harmful as continuing federal regulation,<sup>48</sup> and therefore “preempt[ed] state authority over rail rates, classifications, rules and practices.”<sup>49</sup> States were left only with the ability to petition for federal permission to regulate intrastate rail commerce in a manner consistent with federal standards.<sup>50</sup> Deregulation of the railroad industry is now credited with bringing about increased competition, more efficient routes, increased profits, better service, and an enhanced ability to attract capital investment.<sup>51</sup>

**Trucking.** Between the World Wars, the highway system grew rapidly. Cheap wages, trucks, tires, and fuel facilitated the rise of many new motor carriers.<sup>52</sup> Many viewed this competition as destructive: the new operators’ rates often were not published, many of them failed and went out of business, rates varied widely and changed frequently, and charges to different shippers using the same carrier often varied.<sup>53</sup>

Furthermore, each state public utility commission imposed its own regulatory solutions to these problems, creating further disarray that, unsurprisingly, often favored the state’s own local industry. Federal courts struck down state trucking regulations that unreasonably impaired interstate commerce,<sup>54</sup> but state commissions interpreted such decisions narrowly and tinkered endlessly with their regulations to circumvent federal preemption.<sup>55</sup> Some of this conflict was resolved by the Motor Carrier Act of 1935, which removed intrastate rate-setting authority from the States and lodged it in the ICC. The 1935 Act further gave the ICC broad power to require motor carriers to obtain certificates before providing service, to require that carriers file tariffs with their rates, to

in scattered sections of 45 and 49 U.S.C.).

48. *Ill. Commerce Comm’n v. Interstate Commerce Comm’n*, 749 F.2d 875, 877-78 (D.C. Cir. 1984) (citing H.R. REP. NO. 96-1035, at 128-30 (1980), as reprinted in 1980 U.S.C.C.A.N. 3978, 4072-74).

49. H.R. REP. NO. 96-1430, at 106 (1980) (Conf. Rep.), as reprinted in 1980 U.S.C.C.A.N. 4110, 4138 (finding preemption necessary to “ensure that the price and service flexibility and revenue adequacy goals of the [Staggers] Act are not undermined by state regulation of rates, practices, etc.”); see 49 U.S.C. § 11501(b) (1) (2000).

50. See 49 U.S.C. § 11501 (b)(3), (c).

51. See, e.g., Michael W. Babcock, *Efficiency and Adjustment: The Impact of Railroad Deregulation*, CATO POLY ANALYSIS, Jan. 31, 1984, available at <http://www.cato.org/pubs/pas/pa033.html>; John Hood, *Blessings of Liberty: John Hood on the Dividends of Deregulation*, POLY REV., July & Aug. 1997, available at <http://www.policyreview.org/jul97/thbless.html>.

52. See VACHAL, *supra* note 37, at 3.

53. ALFRED E. KAHN, *THE ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS* 178 (1988).

54. See, e.g., *Mich. Pub. Utils. Comm’n v. Duke*, 266 U.S. 570, 577 (1925).

55. See Thomas W. Hazlett, *Is Federal Preemption Efficient in Cellular Phone Regulation?*, 56 FED. COMM. L.J. 155, 187 (2003).



outline employee qualifications, to set the maximum hours they could work, and to establish uniform motor carrier equipment standards.<sup>56</sup>

This federal regulatory regime worked reasonably well for a time, but came under increasing pressure as the national highway network exploded in the 1950s and 1960s with the federal interstate highway system initiative. And all the while, state and federal regulators continued to trip over one another. The federal courts struck down state regulations that were found to burden interstate trucking by invoking the Commerce Clause,<sup>57</sup> but this *ad hoc*, case-by-case approach failed to comprehensively deal with the problem.

Finally, in 1980, in response to growing opposition to the regulatory scheme, Congress substantially reduced federal regulation of the trucking industry.<sup>58</sup> By the early 1990s, eight states followed suit and deregulated intrastate trucking.<sup>59</sup> Yet the remaining states continued to follow their own parochial approaches to trucking regulation, which cost the trucking industry and the economy between \$5 billion and \$12 billion a year.<sup>60</sup> “[T]he primary liability of state regulation was the inherent inconsistency of disparate rules dotting regional or national truck routes.”<sup>61</sup>

Finding “that ‘the regulation of intrastate transportation of property by the States’ unreasonably burdened free trade, interstate commerce, and American consumers,”<sup>62</sup> Congress moved to preempt state economic regulation of intrastate trucking entirely in 1994.<sup>63</sup> Congress attributed

56. See Motor Carrier Act of 1935, Pub. L. No. 74-255, 49 Stat. 543 (1935); see also Thomas Gale Moore, Library of Economics and Liberty, Trucking Deregulation, <http://www.econlib.org/Library/Enc/TruckingDeregulation.html> (last visited Mar. 20, 2008).

57. *E.g.*, *Kassel*, 450 U.S. 662 (invalidating an Iowa restriction on truck length); *Raymond Motor Transp., Inc. v. Rice*, 434 U.S. 429 (1978) (invalidating a Wisconsin regulation barring 65-foot double trucks); *Bibb v. Navajo Freight Lines, Inc.*, 359 U.S. 520 (1959) (invalidating an Illinois mud-guard regulation).

58. Motor Carrier Act of 1980, Pub. L. No. 96-296, 94 Stat. 793 (codified as amended in scattered sections of 49 U.S.C.); see Hazlett, *supra* note 55; Moore, *supra* note 56.

59. John C. Taylor, *Regulation of Trucking by the States*, 17 REG., Spring 1994, available at <http://www.cato.org/pubs/regulation/regv17n2/reg17n2-taylor.html>; Hazlett, *supra* note 55, at 185-86.

60. Thomas Gale Moore, *Unfinished Business in Motor Carrier Deregulation*, 14 REG., Summer 1991, at 55-57, available at <http://www.cato.org/pubs/regulation/regv14n3/reg14n3-moore.html>.

61. Hazlett, *supra* note 55, at 186.

62. *City of Columbus v. Ours Garage and Wrecker Serv., Inc.*, 536 U.S. 424, 440 (2002) (quoting Federal Aviation Administration Authorization Act of 1994, Pub. L. No. 103-305, § 601(a)(1), 108 Stat. 1605); see also H.R. REP. NO. 103-677, at 87 (1994) (Conf. Rep.) (“State economic regulation of motor carrier operations . . . is a huge problem for national and regional carriers attempting to conduct a standard way of doing business.”).

63. The Federal Aviation Administration Authorization Act of 1994, 49 U.S.C. § 40101, preempts states from regulating the rates or services of motor carriers. Safety regulation is still permissible, 49 U.S.C. § 14501(c)(2)(A), but it is also still subject to challenge under the dormant Commerce Clause – a route by which many supposed state safety regulations that disrupted interstate transportation have been invalidated. See, *e.g.*, *Kassel*, 450 U.S. 662

numerous vices to the “patchwork” of intrastate trucking regulations in 41 states, including “significant inefficiencies, increased costs, reduction of competition, inhibition of innovation and technology and curtail[ing] the expansion of markets.”<sup>64</sup> Economists now credit federal deregulation of the trucking industry with increasing the number of licensed carriers,<sup>65</sup> improving service to small communities,<sup>66</sup> decreasing the number of complaints by shippers,<sup>67</sup> and decreasing trucking rates by billions of dollars a year.<sup>68</sup>

**Airlines.** The rise and fall of federal airline regulation unfolded in much the same way. Federal regulators entered in 1926,<sup>69</sup> about twelve years after the first commercial airline service began,<sup>70</sup> in the wake of heavy losses and failures among the young air carriers.<sup>71</sup> The primary reason for enacting new regulation was to keep the airlines in business—to allow an infant industry to grow and to prosper in an orderly fashion.<sup>72</sup> The Civil Aeronautics Authority, which later became the Civil Aeronautics Board (“CAB”), was charged with regulating airlines’ entry

(invalidating an Iowa restriction on truck length); *Raymond Motor Transp., Inc.*, 434 U.S. 429 (invalidating a Wisconsin regulation barring 65-foot double trucks).

64. Hazlett, *supra* note 55, at 188.

65. Moore, *supra* note 56.

66. *Id.*

67. *Id.*

68. Studies of interstate trucking deregulation indicate that it has saved shippers and consumers as much as \$20 billion a year. A study by the staff of the Federal Trade Commission concluded that state trucking regulation raised trucking prices by as much as 20-32 percent. See Press Release, Fed. Trade Comm’n, State Trucking Regs Raise Prices Significantly, FTC Staff Study Finds (Nov. 28, 1995), available at <http://www.ftc.gov/opa/1995/11/trur.shtm>. It has been conservatively estimated that federal preemption of state regulation alone has produced efficiency gains of \$4 billion annually. See PAUL TESKE ET AL., DEREGULATING FREIGHT TRANSPORTATION: DELIVERING THE GOODS 74 (1995); see also Cassandra Chrones Moore, *Intrastate Trucking: Stronghold of the Regulators*, CATO POLY ANALYSIS, Feb. 16, 1994, available at [http://www.cato.org/pub\\_display.php?pub\\_id=1063](http://www.cato.org/pub_display.php?pub_id=1063); Taylor, *supra* note 59.

69. See Air Commerce Act of 1926, Pub. L. No. 69-254, 44 Stat. 568 (repealed 1958).

70. See Bluegrass Airlines, Bill Odell, Florida Airlines History, <http://bluegrassairlines.com/bgas/flair.htm> (last visited Mar. 20, 2008) (the first commercial airline service was between St. Petersburg and Tampa, Fla.).

71. See Hon. Richard D. Cudahy, *The Folklore of Deregulation (With Apologies to Thurman Arnold)*, 15 YALE J. ON REG. 427, 431 (1998); Hon. Richard D. Cudahy, *Full Circle in the Formerly Regulated Industries?*, 33 LOY. U. CHI. L.J. 767, 781 n.76 (2002) (“Before 1938, ‘there was not much of an airline industry. Profitable operation before regulation had been very sporadic. The thought was that regulation could manage competition so as to keep the competitors out of bankruptcy.’”) (quoting Richard D. Cudahy, *The Folklore of Deregulation (with Apologies to Thurman Arnold)*, 15 YALE J. ON REG. 427, 431 (1998)).

72. Hon. Richard D. Cudahy, *The FERC’s Policy on Electric Mergers: A Bit of Perspective*, 18 ENERGY L.J. 113, 125 (1997); see Paul Stephen Dempsey, *Transportation Deregulation - On a Collision Course?*, 13 Transp. L.J. 329, 335 (1984) (regulation of the airline industry was designed “to avoid the deleterious consequences of cutthroat and excessive competition, and thereby enhance economic stability, safety, and the sound growth and development of this young industry”).

into the industry, the routes they could fly, and the fares they could charge passengers.<sup>73</sup> By the 1970s, however, soaring fuel costs and other inflationary factors were creating enormous debt for the airline industry.<sup>74</sup> The CAB granted airlines fare increases to offset higher costs, which set off a wave of protests by consumers.<sup>75</sup> At the same time, the CAB stultified competition by refusing to permit new major carriers to enter the business and by making it extremely difficult for existing carriers to change their routes.<sup>76</sup> The CAB was widely criticized for creating large inefficiencies, including overcapitalization, and for unduly favoring incumbents.<sup>77</sup>

In response, Congress deregulated the industry in 1978, concluding that “maximum reliance on competitive market forces’ would best further ‘efficiency, innovation, and low prices’ as well as ‘variety [and] quality . . . of air transportation services.’”<sup>78</sup> In doing so, Congress expressly preempted state regulation “relating to rates, routes, or services of any air carrier having authority . . . to provide interstate air transportation.”<sup>79</sup> Economists now estimate that fares under deregulation have been 10 to 18 percent lower than they would have been under regulation, a savings to consumers of \$5 billion to \$10 billion per year.<sup>80</sup> Deregulation is also credited with increasing efficiency in the industry, increasing the number of airlines per route, and improving airline safety.<sup>81</sup>

**Gas Pipelines.** Natural gas pipelines connected the states early in the twentieth century, yet the states treated this form of commerce as a local fiefdom. For example, West Virginia enacted legislation regulating natural gas pipeline companies that was intended to keep within West

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73. See VISCUSI, *supra* note 40, at 610-11.

74. See Christine Chmura, *The Effects of Airline Regulation*, FREEMAN, Aug. 1984, available at <http://www.fee.org/publications/the-freeman/article.asp?aid=1166>.

75. *Id.*

76. See VISCUSI, *supra* note 40, at 612 (the CAB made limited entry into the industry a long and costly process and imposed a route moratorium in the early 1970s).

77. See, e.g., Frank J. Costello, Partner, Zuckert Scoult & Rasenberger, L.L.P., *The Lessons of Airline Deregulation*, <http://www.zsrlaw.com/publications/articles/fjclessons.htm> (last visited Mar. 20, 2008); John W. Barnum, Partner, McGuireWoods LLP, *What Prompted Airline Deregulation 20 Years Ago? What Were the Objectives of that Deregulation and How were They Achieved?*, Presentation to the Aeronautical Law Committee of the Business Law Section of the International Bar Association Presentation to the International Bar Association Aeronautical Law Committee (Sept. 15, 1998), available at <http://library.findlaw.com/1988/Sep/1/129304.html>.

78. *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 378 (1992) (quoting Airline Deregulation Act of 1978, 49 U.S.C. §§ 1302(a)(4), 1302(a)(9) (repealed)).

79. 49 U.S.C. § 1305(a)(1) (repealed).

80. Alfred Kahn, Library of Economics and Liberty, *Airline Deregulation*, <http://www.econlib.org/library/Enc/AirlineDeregulation.html> (last visited Mar. 20, 2008).

81. *Id.*

Virginia all natural gas produced there that might be required for local needs; other states could receive exports only after West Virginia's own needs were fully met.<sup>82</sup> Perceiving a direct threat to their own economies, the neighboring States of Ohio and Pennsylvania sued West Virginia to enjoin enforcement of its protectionist legislation. The Supreme Court noted the irony that West Virginia had encouraged the interstate growth of its local natural gas companies and had profited greatly thereby, yet now purported to wall itself off from other states in the event of a gas shortage.<sup>83</sup> The case was so contentious that it was argued before the Court three times over the course of two years. In the end, the interstate nature of the pipeline industry was unavoidable and mandated the suppression of state efforts to dictate the terms of operation of a national network industry: "If one state has [such power], all states have it; embargo may be retaliated by embargo, and commerce will be halted at state lines. And yet . . . in matters of . . . interstate commerce there are no state lines."<sup>84</sup>

Congress asserted federal control over interstate pipelines in 1938.<sup>85</sup> The National Gas Act assigned regulatory authority to the Federal Power Commission ("FPC"), which had been established nearly 20 years earlier to license hydroelectric projects.<sup>86</sup> When rapid economic growth in the 1940s and 1950s outpaced pipeline expansion and caused price volatility and shortages in some areas, the FPC held that it did not have the authority to set prices.<sup>87</sup> But, the Supreme Court concluded in 1954 that the National Gas Act not only gave the FPC the requisite authority to regulate pipeline rates, but also required that it do so.<sup>88</sup> The Court further held that the FPC was obligated to regulate the prices charged by gas producers (known as wellhead prices),<sup>89</sup> which expanded the FPC's jurisdiction from a few dozen pipelines to tens of thousands of gas wells.<sup>90</sup>

In 1978, at the peak of the energy crisis, Congress passed the National Energy Act and the Natural Gas Policy Act to reform natural

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82. See *Pennsylvania v. West Virginia*, 262 U.S. 553, 597-98 (1923).

83. See *id.* at 597; see also *H.P. Hood & Sons*, 336 U.S. at 536-37 (discussing *Pennsylvania*, 262 U.S. at 597).

84. *Pennsylvania*, 262 U.S. at 599 (citation and internal quotation marks omitted).

85. See Natural Gas Act, Pub. L. No. 75-688, 52 Stat. 821 (1938).

86. *Id.*

87. *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672, 677 (1954) (citing *In The Matter of Phillips Petroleum Co.*, 10 F.P.C. 246, 279 (1951)).

88. *Id.*

89. *Id.* at 682.

90. See Robert. J. Michaels, *The New Age of Natural Gas: How the Regulators Brought Competition*, 16 REG., Winter 1993, available at <http://www.cato.org/pubs/regulation/reg16n1e.html>.

gas pricing.<sup>91</sup> Among other things, this legislation gave FERC—which had been created a year earlier to replace the FPC—authority to deregulate wellhead gas prices.<sup>92</sup> In the mid-1980s, FERC began pipeline reform as well.<sup>93</sup> It adopted policies that enabled local gas distribution companies to switch gas suppliers<sup>94</sup> and then required pipelines to provide open access to transportation services allowing consumers to negotiate directly with producers and contract separately with the pipelines for transportation.<sup>95</sup> In 1992, FERC instituted a major restructuring of interstate pipeline operations, requiring the separation of sales from transportation services so that customers could select supply and transportation services from any competitor in any quantity or combination.<sup>96</sup>

Competition among national networks employing different technologies that are subject to different regulation is an especially compelling basis for preemptive federal regulation. For example, by the 1970s, intermodal competition—that is, competition from other modes of transportation—had increased to the point where the railroad industry, still stringently regulated, was on the verge of collapse. Congress found that while regulation had been essential to prevent the

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91. See Public Utility Regulatory Policies Act of 1978, Pub. L. No. 95-617, 92 Stat. 3117 (codified as amended in scattered sections of 5, 15, 16, 26, 30, 42, and 43 U.S.C.); Energy Tax Act of 1978, Pub. L. No. 95-618, 92 Stat. 3174 (codified as amended in scattered sections of 26 and 42 U.S.C.); National Energy Conservation Policy Act, Pub. L. No. 95-619, 92 Stat. 3206 (1978) (codified as amended in scattered sections of 12, 15, 23, 26, 31, 40 and 42 U.S.C.); Powerplant and Industrial Fuel Use Act of 1978, Pub. L. No. 95-620, 92 Stat. 3289 (codified as amended in scattered sections of 5, 15, 16, 19, 33, 42, and 49 U.S.C.); National Gas Policy Act, Pub. L. No. 95-621, 92 Stat. 3350 (1978) (codified as amended in 5, 16, 15 and 42 U.S.C.).

92. See National Gas Policy Act, Pub. L. No. 95-621, 92 Stat. 3350 (1978); see also Kenneth W. Costello & Daniel J. Duann, *Turning Up the Heat in the Natural Gas Industry*, 19 REG., Winter 1996, at 53, available at <http://www.cato.org/pubs/regulation/reg19n1c.html> (total deregulation of wellhead gas was completed by January 1, 1993).

As a policy, wellhead price control was disastrous. Basing its decisions on historic data, the FPC seriously underestimated the costs of replacing exhausted wells. In every year between 1966 and 1978 proved gas reserves in the lower forty-eight states fell. As production fell and shortages worsened, pipelines often had to curtail supplies to distributors, who in turn curtailed their captive customers.

Michaels, *supra* note 90, at 73.

93. Costello & Duann, *supra* note 92, at 53 (“Pipeline reform started in 1984 when the Federal Energy Regulatory Commission (FERC) issued Order 380.”).

94. *Id.* (citing FERC Order 380).

95. Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, 50 Fed. Reg. 42,408 (Oct. 18, 1985) (codified at 18 CFR pts. 2, 157, 250, 284, 375, and 381); Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, 52 Fed. Reg. 30,334 (Aug. 14, 1987) (codified at 18 CFR pts. 2 and 284).

96. Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation under Part 284 of the Commission’s Regulations, 59 F.E.R.C. ¶ 61,030 (Apr. 8, 1992).

abuse of monopoly power by railroads earlier in the 20<sup>th</sup> century, the competition provided by the significant increase in the use of trucks, barges, and aircraft rendered the old railway regulatory framework antiquated and inefficient.<sup>97</sup> Indeed, Congress determined that a “significant reason” for the decline of the railroad industry was the “inflexibility” of the existing regulatory regime under which it was forced to operate.<sup>98</sup> Furthermore, regulation, however well intentioned, itself adversely affected the ability of railroads to compete with substantially unregulated or deregulated modes of transportation.<sup>99</sup>

Furthermore, the rise of massive fleets of long-haul trucking operations not only provided significant intermodal competition for the railroads—it also provided the basis for the deregulation of the trucking industry. The same robust intermodal competition from trucks that justified deregulation of the railroads likewise justified deregulation of trucking itself. Although there were some state trucking regulations that seemed transparently designed to discriminate in favor of the railroads,<sup>100</sup> “the primary liability of state regulation was the inherent inconsistency of disparate rules dotting regional or national truck routes.”<sup>101</sup> Accordingly, that disruptive and erratic patchwork quilt of state-by-state regulation was finally terminated in 1994, as explained above.

Drawing parallels between different technologies or services and the regulatory models appropriate for them is both sensible and a time-honored tradition. The very first federal regulatory approach to telephony recognized the interstate capability inherent in the then-infant technology and made provisions for eventually recognizing the overriding federal regulatory interest in that technology. The Mann-Elkins Act of 1910 brought interstate telecommunications within the regulatory jurisdiction of the ICC by way of provisions that paralleled (with some omissions) the ICC’s power to regulate the railroads.<sup>102</sup> Under those provisions, the ICC enjoyed sweeping power to preempt state regulation—even when the states regulated only *intrastate* commerce. This power was confirmed by the Supreme Court in *The Shreveport Rate Case*.<sup>103</sup> The Court recognized that, in a network industry such as

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97. See Staggers Rail Act §§ 2(1)-(5).

98. See H.R. REP. NO. 96-1035, at 38 (1980), as reprinted in 1980 U.S.C.C.A.N 3978, 3983.

99. See *id.* at 115, as reprinted in 1980 U.S.C.C.A.N at 4059.

100. Hazlett, *supra* note 55, at 186 & n.99.

101. *Id.* at 186.

102. Mann-Elkins Act, Pub. L. No. 61-218, 36 Stat. 539 (1910); see also PETER W. HUBER, MICHAEL K. KELLOGG & JOHN THORNE, FEDERAL TELECOMMUNICATIONS LAW 214-15 (2d ed. 1999).

103. See *Houston, E. & W. Tex. Ry. Co. v. United States (The Shreveport Rate Case)*, 234 U.S. 342, 351 (1914).

the railroad industry, interstate and intrastate rates “are so related that the government of the one involves the control of the other.”<sup>104</sup> The same situation obtained with respect to the telephone network: the same wires and boxes used for local calls were also, after all, used for interstate calls.<sup>105</sup>

Such analogies are equally powerful with contemporary regulatory agencies. The FCC has expressly embraced analogies to deregulation on the basis of intermodal competition among motor carriers as a predicate for similar preemptive federal deregulation of telecommunications networks. In its order deregulating an Internet communications service (that will be more fully discussed below), the FCC pointed to congressional deregulation of trucking as a parallel “network’-based service example[] where, although an intrastate component of such service may exist, this intrastate component must nonetheless yield to exclusive federal jurisdiction in the area of economic or other state regulations affecting entry to advance articulated congressional or federal deregulatory objectives.”<sup>106</sup>

### III. THE GROWTH OF INTERSTATE TELECOMMUNICATIONS NETWORKS AND THE RISE OF INTERMODAL COMPETITION

#### A. *The Anachronism of State-by-State Regulation of Wireline Telephony*

State-by-state regulation of wireline telephony made sense at the start of the telephone era in the nineteenth century when local phone systems were small and localized. At the dawn of the telephonic age, telephones were connected only by wire, one to one.<sup>107</sup> There were no local telephone exchanges, let alone a network. An interstate network of telephone service was inconceivable because signal quality deteriorated so

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104. *Id.* at 351, 355.

105. *The Shreveport Rate Case*, as indicated in the text, involved railroad rather than telephone rate-setting, but the ICC’s preemptive power was the same in either instance. The regulatory import of that seminal decision is discussed at length in HUBER, KELLOGG & THORNE, *supra* note 102, at 216-18. Although the ICC never sought to exercise preemptive power over intrastate telephone rates, state regulators knew that it could and feared that it would. See, e.g., *Hearings on H.R. 8301 Before the H. Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. 135-36 (1934) (statement of John E. Benton) (“The Interstate Commerce Commission has the same power now to override State regulation in the telephone field as it has in the railroad field . . .”).

106. Petition for Declaratory Ruling That pulver.com’s Free World Dialup is Neither Telecomms. Nor a Telecomms. Serv., *Memorandum Opinion & Order*, 19 FCC Rcd. 3307, ¶ 25 n.91 (2004) [hereinafter *Pulver*] (citing 49 U.S.C. § 14501 (preempting state economic regulation of motor carriers)).

107. See HUBER, KELLOGG & THORNE, *supra* note 102, at 8.

rapidly that conversations were almost impossible over distances greater than a few miles.<sup>108</sup> By the first decade of the twentieth century, there were thousands of local, isolated telephone companies.

But there still was no telephone *network*. Most early telephone companies, whether Bell affiliate or independent, refused to connect with each other, leaving many telephone customers unable to talk to one another.<sup>109</sup> In fact, in the early years of the 20th century, one often needed *two* telephones—one to speak with those who had Bell service and the other to call those served by an independent phone company.<sup>110</sup> In such an atomized, inherently local industry, state-by-state regulation made perfect sense.<sup>111</sup> Even when this lack of interconnectivity gave the Bell System the leverage to obtain monopoly status in exchange for guaranteeing interconnection among all its affiliated companies,<sup>112</sup> state-by-state regulation still made sense because the local affiliates operated under exclusive monopoly franchises granted by those same states. In addition, as with other industries, the most important regulatory issues arose from the development of the on-the-ground infrastructure, and thus were inherently local.

In 1934, when the Federal Communications Act (“1934 Act”) became law,<sup>113</sup> barely two percent of telephone calls crossed state lines,<sup>114</sup> and some 45 of the 48 states had regulatory commissions to oversee their local telephone providers. The state regulators lobbied for limits on federal jurisdiction and, in particular, for a repudiation of the preemptive power over telephone regulation held by the ICC under *The Shreveport Rate Case*.<sup>115</sup> The result was that the 1934 Act delegated broad power over interstate communication to the new Federal Communications Commission, but also nullified *Shreveport* and explicitly denied the FCC any “jurisdiction with respect to . . . intrastate communication service.”<sup>116</sup> The 1934 Act thus embodied the tension between the fundamental

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108. *Id.* at 8-9.

109. *Id.* at 213 & n.10.

110. *Id.* at 12.

111. Hazlett, *supra* note 55, at 175 (“State regulation is typically better able to regulate when local markets are relatively idiosyncratic, . . . [and] when the rules adopted in one state are largely contained within that jurisdiction.”).

112. See HUBER, KELLOGG & THORNE, *supra* note 102, at 213-14 & nn.11-12.

113. Communications Act of 1934, Pub. L. No. 73-416, 48 Stat. 1064 (1934) (codified as amended in scattered sections of 47 U.S.C.).

114. See Eli M. Noam, *Federal and State Roles in Telecommunications: The Effects of Deregulation*, 36 VAND. L. REV. 949, 955 (1983).

115. See, e.g., K. A. Cox & W. J. Byrnes, *The Common Carrier Provisions—A Product of Evolutionary Development*, reprinted in A LEGISLATIVE HISTORY OF THE COMMUNICATIONS ACT OF 1934, at 29-30 (M. D. Paglin ed., 1989); Richard McKenna, *Preemption Under the Communications Act*, 37 FED. COMM. L. J. 1, 8-9 (1985).

116. 47 U.S.C. § 152(b) (2006).



unifying impulse of the Commerce Clause and the legacy of state-by-state regulation with which we still contend today.

Continued reliance on state-by-state regulation of wireline telephony is the inertial legacy of this *ancien regime* of dual state-federal jurisdiction that originated at a time when all telephony was wireline and the vast bulk of telephone communications were genuinely intrastate. As the next section demonstrates, that dual regulatory regime has been largely abandoned (with uniformly positive results) with respect to every other major element of the telecommunications industry: wireless phones, cable modems, data services, information services, and the Internet. Therefore, for reasons both regulatory and technological, the constitutional basis of state regulation of wireline telephony—the distinction between “intrastate” and “interstate” telephone calls—grows more illusory every day. The pervasively *interstate nature* of the supposedly “local” phone service that remains subject to state jurisdiction is worth reviewing in some detail because federal jurisdiction over commerce is predicated on its *interstate* nature. In the Commerce Clause, the Constitution has adopted what is in significant part a geographic test for defining federal jurisdiction, and therefore, the geography of the wireline telephone network matters.

To begin with, even “local” calls that are classified as intrastate, and therefore subject to state regulatory jurisdiction under 47 U.S.C. § 221(b) are, in fact, often interstate. The court decree that broke up the old Bell Telephone System created 196 Local Access and Transport Areas (“LATAs”) that geographically defined the service boundaries of the Regional Bell Operating Companies (“RBOCs”) (also known as “Baby Bells,” or Incumbent Local Exchange Carriers (“ILECs”)), into which the Bell System was divided. These LATAs are not drawn along state lines. The LATAs were primarily drawn along the lines of the Standard Metropolitan Statistical Areas delineated by the Census Bureau to identify “communities of interest” in economic terms. It turned out to be impossible to delineate the national telephone network along state lines without fragmenting natural local calling areas that reflected human habitation and economic patterns: cities and their suburbs grow across state boundaries, and many “local” telephone exchanges and “Local” Access and Transport Areas follow suit. Therefore, the LATA map departs from state boundaries in order to accommodate multi-state metropolitan areas, existing economic zones, population patterns, and similar factors. As a result, a significant portion of supposedly “local” intra-LATA calls within a given telephone exchange that are subject to *state* jurisdiction under 47 U.S.C. § 221(b) are in fact *interstate* calls by virtue of the fact that the *local exchanges and LATAs themselves cross*

*state borders.*<sup>117</sup>

Yet such calls are deemed “intrastate” under Section 221(b), which was enacted “to preserve state regulation of local exchanges that happened to overlap state lines.”<sup>118</sup> It makes little sense for a regulatory regime to maintain a fictive legal interstate-intrastate distinction when even the administrative map of the phone network itself disregards state lines and pretends that calls across those state borders are local rather than interstate calls.

Technological developments have made that fiction ever harder to maintain. The facilities that make up the national wireline telephone network are becoming more and more centralized; “local” calling facilities are no longer necessarily located in the same state as the caller and the recipient. Today, many calls that begin and end within a given state—sometimes even calls to a neighbor residing a few blocks away—are in fact interstate calls because the transmission makes use of out-of-state facilities. Such interstate transmissions necessarily constitute interstate commerce.

For example, Verizon, the successor to the Bell System that provides local phone service in the northeastern United States, serves residents of suburban Connecticut with a circuit switch that is located in New York. Therefore, every local call made by a Greenwich resident—even to his or her next-door neighbor—is routed through the New York switch and is consequently an interstate transmission in fact, even though the current regulatory regime blinks reality and deems it intrastate in law. Verizon likewise has tandem circuit switches in the District of Columbia that serve not only D.C. but also northern Virginia. “Local” calls within Virginia may therefore be routed through those switches into D.C. and then back into Virginia.<sup>119</sup>

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117. For example, LATA No. 236 encompasses the entire District of Columbia metropolitan area and therefore includes suburban Maryland and northern Virginia as well as Washington, D.C. The Cincinnati LATA (No. 922) spans three states: Ohio, Kentucky, and Indiana. Some multistate LATAs are the size of states themselves – LATA 636 sweeps in half of North Dakota and most of northern Minnesota; LATA 672 covers southwestern Washington and half of Oregon. Other examples of large, three-state LATAs are the St. Louis LATA (No. 520), which includes parts of Illinois and the eastern third of Missouri; No. 652 (southeastern Oregon, most of Idaho, and parts of Nevada) and No. 650 (northwest Wyoming, half of Montana, and parts of North Dakota). LATA No. 472 spans the borders of Tennessee, Alabama, and Georgia; LATA 960 includes the northern panhandle of Idaho and parts of Montana and Washington; and No. 240 includes parts of Maryland, Pennsylvania, and West Virginia.

118. Nat’l Ass’n of Regulatory Util. Comm’rs v. F.C.C., 746 F.2d 1492, 1500 (D.C. Cir. 1984) (citation and quotation marks omitted); see also HUBER, KELLOGG & THORNE, *supra* note 102, at 222 & n.61.

119. Local wireline service provided by Competitive Local Exchange Carriers (“CLECs”) is even more centralized and inherently interstate than ILEC service; because the CLECs began to build their networks after the 1996 Act opened up local wireline competition, the

The electronic signaling system that is part of every telephone call is even more centralized and more inherently interstate than is the voice transmission system just discussed. The wireline telephone network in fact consists of two distinct networks: a network that carries the actual voice conversation and a separate, out-of-band signaling network that carries everything else. The signaling network controls the set-up, routing, and connection of the phone call between caller and recipient, and is therefore an essential part of every call. The modern system, known as Common Channel Signaling and employing the Signaling System Seven (“SS7”) protocol, carries these processing and routing signals on a dedicated, digital, packet-switched data communications network separate from the transmission path of the caller’s voice.

New technology allows the facilities for this signaling system to be efficiently centralized rather than distributed among the states. For example, Verizon’s Gateway Access Service network consists of regional hubs that process telephone calls for huge, multistate geographic areas. The Gateway in Indiana serves seven states, including cities as far afield as Denver, Cleveland, Chicago, Detroit, and Kansas City, Missouri. The Gateway in New Hampshire provides centralized services for five states: Rhode Island, Maine, Vermont, New Hampshire, and part of Massachusetts. Given that signaling is an essential part of *every* wireline telephone call, *every* supposedly “local” phone call processed on this Gateway system that goes to or from a subscriber in any state without its own Gateway hub is necessarily an *interstate* call that makes use of out-of-state facilities, even if the separate voice path for that call is wholly intrastate.

Centralized computer systems are also an essential (if invisible) part of many popular enhanced phone services provided by local exchange carriers. Network voicemail services employ centralized servers (computers) located far from the states whose residents they serve. For example, the voicemail “mailboxes” for Verizon’s South Carolina and North Carolina customers are actually located in Florida. Every voicemail message left for every Verizon subscriber in the Carolinas—

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CLECs were largely free to place their equipment where it was most efficient to do so. Thus, CLECs such as AT&T, Teligent, PaeTec, and Conversent serve Connecticut subscribers with circuit switches located in New York, while AT&T, Allegiance Telecom, Cavalier Telephone, Focal Communications, Global Crossing, Global NAPS, Net2000, PaeTec, US LEC, Winstar, WorldCom and XO route all “local” calls to and from their Maryland subscribers through out-of-state switches located in Virginia or Washington, D.C. See TELCORDIA TECHS., INC., LOCAL EXCHANGE ROUTING GUIDE (2003). All “local” calls to and from AT&T subscribers in the State of Washington are in fact interstate because they are routed through a switch situated in Oregon. *Id.* Adelphia serves its North Carolina customers through a switch in Virginia, and other CLECs serve Delaware residents with switches located in Pennsylvania. *Id.*

even a “local” call made by the subscriber’s next-door neighbor—is routed across multiple state boundaries to Florida. Likewise, every call by a Carolina Verizon subscriber to retrieve his or her voicemail messages is an interstate call to Florida. All the voicemail for Verizon’s “local” phone service customers in Illinois, Michigan, Ohio, and Wisconsin is actually stored on a server in Indiana, and voicemail for Oregon and Idaho is stored in the hub situated in Washington.<sup>120</sup>

A host of other enhanced wireline service features is likewise provided across multiple states by centralized computers operating over this same SS7 signaling system. Telephone companies use the term Advanced Intelligent Network (“AIN”) to describe an upgraded network offering a suite of custom-calling features such as caller ID, call intercept, call blocking, Privacy Director, selective call diversion, network call forwarding, phone number portability, network-based fax applications, and many Centrex services. The broad range of telephone services provided by AIN systems is growing and is virtually infinite in potential.<sup>121</sup> The servers and databases through which these familiar services are provided are centralized and usually far removed from the telephone subscribers they serve.<sup>122</sup> Therefore, the overwhelming majority of calls that trigger network-based enhanced or custom-calling features, e.g., voicemail, caller ID, and call forwarding, are interstate transmissions that involve out-of-state facilities, even if the voice portion of the call was originally placed by one state resident to his neighbor a block away. For example, Verizon uses just seven regional Integrated Services Control Points to provide advanced network services to all of its customers in 29 noncontiguous states spread across the entire country. Thus, *all such transmissions* for Verizon’s wireline customers in states as far flung as Florida, Texas, and California are routed through and handled by a single computer system located in a town in Washington.

Operator assistance and directory assistance services are now

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120. The voicemail operations for CLECs are, unsurprisingly, even more centralized. For example, Z-Tel provides its voicemail product, “Personal Voice Assistant,” to its subscribers nationwide through a single server hub located in Florida.

121. Caller ID and related services require reference to a database that matches telephone line numbers with their subscribers, known as a Line Information Database (“LIDB”). All such databases are centralized. For example, Verizon maintains just four LIDBs, two for the west and two for the east, for all of the dozens of states it serves. A single “local” phone call to (or from) a subscriber might therefore involve multiple interstate transmissions — one or more to a regional SCP server and database in another state, and also one to a separate LIDB in yet another state.

122. The degree of centralization in such systems will very likely increase, because it is far more efficient to store programs and subscriber information in centralized servers and databases that are peripheral to the telephone network. Service upgrades and wholly new services are infinitely easier to implement when one only needs to load new programming and data onto a centralized computer rather than onto every circuit switch in the network.

centralized and are therefore typically handled outside the calling party's state, even for "local" operator-assistance and directory assistance (411) calls. In the past, traditional operator services were normally associated with the local phone company's central office in a community. However, given the enormous advances in technology, a single digital operator host switch can now support over a thousand operator positions. All "local" telephone service providers use this model for operator services. For example, Verizon's operator assistance unit, called LiveSource, has a single Call Completion Assistance team in the northeast which handles all calls from New York, New Jersey, and New England. There is also a centralized Directory Assistance office that serves traffic from ten different states. Verizon also has a centralized billing system that handles collect calls and calling card calls from nearly two dozen states as widely scattered as Texas and Florida. Given the highly centralized nature of these operations, the overwhelming majority of *supposedly intrastate*—and therefore *state-regulated*—calls for operator, directory, or billing assistance *are in fact interstate calls* routed to out-of-state operators. In addition, those operators may in turn transmit the callers' queries for information (such as directory assistance) to a centralized computer database located in yet another state.

Finally, wireline calls to cell phones and cell phone calls to wireline subscribers may cross state borders not only when the cell phone subscriber is actually in a different state, but even when both the wireline subscriber and the cellular subscriber are in the same state. Like packet-switched data transmissions, wireless routing does not respect state boundaries. When setting up wireless networks, the cellular providers did not slavishly and pointlessly duplicate the pattern of equipment placement foisted on wireline providers by decades of state-by-state regulation. Wireless providers instead placed equipment where it could most efficiently serve a particular area. Consequently, the cell antenna tower and the Mobile Telephone Service Office ("MTSO") through which a wireless call is routed may be across the border in a different state from where the cellular customer and the wireline caller are located.<sup>123</sup>

Further opportunities exist for interstate wireline calls to cell phones to masquerade as intrastate. A "local" wireline call to a cell phone is in

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123. For example, Verizon Wireless has a "supersystem" in Philadelphia that also serves cellular markets in New Jersey and Delaware, and another supersystem in Pittsburgh that serves multiple Pennsylvania, Ohio and West Virginia markets. Just as with the previously discussed case of wireline subscribers served by out-of-state circuit switches, in these cellular supersystems, even a "local" wireline call to a cell phone located in the same state would be an interstate call. These calls often make use of out-of-state facilities whenever the call is routed through a cell tower or MTSO located in one of the other states of the supersystem.

fact interstate, even if the wireline caller and the cellular recipient have the same area code, whenever the cell phone is physically out of the state. Conversely, a wireline call to a cell phone with an out-of-state area code (that is, a cell phone with its “home market” in another state) will always be interstate commerce, even if the cell phone is actually only a block away from the wireline caller throughout the time of the call, because that call will be routed by the wireline Public-Switched Telephone Network (“PSTN”) through a circuit switch in the cell phone subscriber’s home market where the call will access the subscriber’s cellular network.

Similarly, wireline calls to satellite telephones, even to those currently in the same neighborhood as the wireline caller, are necessarily interstate. Such calls do not merely leave the state—they leave the planet. A call to a satellite phone subscriber is routed out of the state—indeed, out of the atmosphere—and makes use of facilities (satellites) that cannot be said to be located in-state.

In sum, there is hardly anything “local” about local telephone wireline service anymore. Giving decisive constitutional weight to the geographic reality of a network industry is a very old and well-established Commerce Clause principle. For example, more than a century ago, the Supreme Court considered a case in which the Arkansas railroad commission asserted jurisdiction to enforce rates on train service within Arkansas between Ft. Smith and Grannis, despite the fact that the railway tracks went outside the state for some distance before returning to Arkansas for the stop at Grannis.<sup>124</sup> Arkansas claimed that the rail route was wholly intrastate, insofar as both the origin and the terminus of the service were within Arkansas. The Supreme Court unanimously rejected this emphasis on end-points as a fiction: “The transportation of these goods certainly went outside of Arkansas.”<sup>125</sup> The Court, therefore, held that this commerce was under the exclusive regulation of Congress and free from interference by the state.<sup>126</sup>

The same principles were applied a few years later to a case of interstate communication by wire—to wit, a telegram. The case involved a lawsuit brought against the telegraph company to recover damages for mental suffering caused by a mistake in delivering a telegraphic message. If federal law governed, the suit would be disallowed, and therefore the question was whether the telegram was sent in interstate or merely intrastate commerce.<sup>127</sup> “The message was from Greenville, North Carolina, to Rosemary in the same State, and was transmitted from Greenville through Richmond, Virginia, and Norfolk, to Roanoke

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124. *Hanley v. Kansas City So. Ry. Co.*, 187 U.S. 617, 618-19 (1903).

125. *Id.* at 620.

126. *Id.*

127. *Western Union Tel. Co. v. Speight*, 254 U.S. 17, 17-18 (1920).

Rapids, the delivery point for Rosemary.”<sup>128</sup> The lower court had ruled that “when as here the termini were in the same State the business was intrastate.”<sup>129</sup> In a unanimous opinion by Justice Oliver Wendell Holmes, the Supreme Court reversed: “The transmission of a message through two States is interstate commerce as a matter of fact.”<sup>130</sup> Justice Holmes noted that, although “[i]t would have been possible, physically, to send” the message by a route entirely within North Carolina, such a transmission would “have required a rearrangement of the wires and more operators. The course adopted was more convenient and less expensive for the Company. . . . As things were, the message was sent in the quickest way.”<sup>131</sup> It follows, therefore, that telephone transmissions—wireline, wireless, or otherwise—are interstate and therefore within the jurisdiction of Congress, even if the calls begin and end within a single state, if the transmissions cross state borders or otherwise make use of facilities located in more than one state. Even a typical call to one’s next-door neighbor to leave a voicemail message is likely to make use of signaling systems, databases, and computer servers located in other states hundreds or even thousands of miles away.

In short, what was once “intrastate” and therefore reasonably subject to state-by-state regulation is now inherently and undeniably interstate, and state-by-state regulation of interstate wireline networks has no basis in law, logic, or economics. As the next section demonstrates, the other inherently interstate arms of the telecommunications system, such as mobile telephones and aspects of the Internet, have already been preemptively federally regulated and then largely deregulated. Wireline telephony, which competes with wireless and Internet technologies in the provision of “local” voice transmission services, should therefore be subject to similarly uniform and exclusively federal regulation as well.

*B. Preemptive Federal Regulation (and Deregulation) of Other Telecommunication Networks and Services.*

Outside the context of local wireline telephony, the inherently interstate nature of national telecommunications networks has been recognized by Congress and reserved for regulation at the national level. Exclusive (or nearly exclusive) federal regulatory jurisdiction over such networks and services has historically been followed in relatively short order by preemptive federal *deregulation*. This regulatory treatment is now appropriate for local wireline telephony as well. The problem is not

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128. *Id.* at 18.

129. *Id.* at 19.

130. *Id.* at 18 (citing *Hanley*, 187 U.S. 617).

131. *Id.* at 19.

just inequity, but arbitrary and glaring inefficiency.

As explained in detail below, few (if any) aspects of modern telecommunications divide neatly along interstate/intrastate lines, and it is therefore specious to sort telecommunications services into intra- and inter-state baskets in an effort to rationalize continued state-by-state regulation. Those sectors of the telecommunications market that have been preemptively federally regulated—and then deregulated—are operating more efficiently and doing more for consumers, and they therefore provide the proper regulatory model for wireline telephony, which is now equally “interstate” in fact.<sup>132</sup>

**Customer Premises Equipment.** The deregulation of telecommunications began in the early 1970s, with customer premises equipment (“CPE”)—telephone handsets, Private Branch Exchanges (“PBX”), and, more recently, modems, routers, desktop computers, Local Area Networks (“LANs”), and other data equipment that is deployed on private premises rather than at a phone company facility. Until 1975, telephone equipment was leased to customers by the local phone company as part of an indivisible package of “local phone service.” The Federal Communications Commission snapped this link by declaring that the CPE markets were, or could be, competitive, and by asserting exclusive jurisdiction over even *local* telephone facilities—such as CPE leased from the local phone company.

The key jurisdictional fact was that the telephone sets used by individual customers within their own homes were physically attached to, and thus part of, an *interstate* network: “[W]hen a local transmission facility is included in an interstate transmission network, the regulation of the interstate uses of that facility lies exclusively with the F.C.C.”<sup>133</sup> While acknowledging that CPE was then used 97 percent of the time for intrastate calls, the reviewing court nevertheless affirmed the FCC’s assertion of exclusive jurisdiction not only as to “telephone companies with lines that extend interstate but also those local companies that provide interstate service solely through connection with the lines of telephone companies that are unrelated to them.”<sup>134</sup> What mattered was that even phone companies with exclusively local operations and services

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132. The leading review of this area of the law – indeed, a treatment that may well be indispensable to a working knowledge of the subject – can be found in HUBER, KELLOGG & THORNE, *supra* note 102. The authors of this article are indebted to that treatise.

133. *Telerent Leasing Corp. et al. Petition for Declaratory Rulings on Questions of Federal Preemption on Regulation of Interconnection of Subscriber-Furnished Equipment to the Nationwide Switched Public Telephone Network*, *Memorandum Opinion & Order*, 45 F.C.C.2d 204, ¶ 36 (1974) [hereinafter *Telerent*], *aff’d* *North Carolina Utils. Comm’n v. F.C.C.*, 537 F.2d 787 (4th Cir. 1976).

134. *North Carolina Utils. Comm’n*, 537 F.2d at 792.



were nonetheless “integrated into the national network.”<sup>135</sup>

The Commission established self-certification standards for equipment vendors, and preempted state regulations that either set the prices or prescribed other terms on which CPE was provided. The Commission reasoned that, without federal preemption:

[S]ubscribers can be subjected to a melange of regulations, determined by each of 50 separate jurisdictions, as to the terms and conditions upon which they shall have access to and use of the telephone network for interstate services. If each State were to be free to establish its own rules governing interconnection [of CPE] for the purposes of intrastate services, uniform nondiscriminatory interstate service throughout the country would be rendered difficult if not impossible.<sup>136</sup>

Once again, the FCC recognized “the indivisibility of the network,”<sup>137</sup> and concluded that perpetuating state-by-state regulation “would frustrate the Congressional purpose in establishing the Commission to ‘make available . . . a rapid, efficient, Nation-wide . . . communication service with adequate facilities at reasonable charges.’”<sup>138</sup> A few years later, the Commission found that the provision of all CPE was fully competitive and deregulated CPE across the board.<sup>139</sup>

**Wireless Telephone Services.** When Marconi invented radio—immediately dubbed the “wireless”—the principal use he planned for his new communications technology was as a mobile telephone for ships at sea.<sup>140</sup> Mobile phone service was severely limited until the 1980s because two-way radio voice communication requires a great deal of electromagnetic spectrum, the bandwidth available was only 25 channels, and to avoid interference with one another only half of those could be

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135. *Id.*

136. Telerent, *supra* note 133, at ¶ 37.

137. *Id.*

138. *Id.* (quoting § 1 of the 1934 Act).

139. See Amendment of Section 64.702 of the Commission’s Rules & Regulations (Second Computer Inquiry), *Final Decision*, 77 F.C.C.2d 384, ¶ 174 (1980) [hereinafter *Computer II*] (state regulation of CPE could only “thwart the competitive provision of that CPE” and was therefore “not feasible.”), *aff’d* Computer & Commc’ns Indus. Ass’n v. F.C.C., 693 F.2d 198, 214 (D.C. Cir. 1982); see also *Furnishing of Customer Premises Equip.* by the Bell Operating Tel. Cos. & the Independent Tel. Cos., *Report & Order*, 2 FCC Rcd. 143, 160-161 (1987) (preempting the ability of the states to require telephone companies to provide CPE through separate corporate subsidiaries), *on recon.*, 3 FCC Rcd. 22 (1987), *petition for review denied* by Ill. Bell Tel. Co. v. F.C.C., 883 F.2d 104 (D.C. Cir. 1989).

140. See HUBER, KELLOGG & THORNE, *supra* note 102, at 861; see also Radio-Communications Acts, Pub. L. No. 61-262, 36 Stat. 629, 629-30 (1910) (barring any ocean-going vessel licensed to carry fifty or more people from departing from any United States port unless equipped with “wireless” apparatus).

used at any given time.<sup>141</sup> For example, of the 23 channels available in the late 1970s for mobile telephone use in New York City, only twelve could be used simultaneously by the six or seven hundred users in the metropolis.<sup>142</sup> Nationwide, this narrowly restricted spectrum could support no more than about 140,000 mobile telephone subscribers, including obvious priority customers as police and fire departments.<sup>143</sup> Although Bell Laboratories had developed the concept of cellular phone communications in the late 1940s, the technology was not applied and cellular properties were not licensed until the early 1980s, whereupon cellular services exploded exponentially by the early 1990s.<sup>144</sup>

Fortuitously, due to its origins in radio technology—whose invisible wavelengths in the air were oblivious to, and certainly could not be constrained by, state political boundaries—wireless telephony was born amidst a decided governmental prejudice in favor of uniform, preemptive federal regulation. The Radio Act of 1927 nationalized the entire radio spectrum and lodged all jurisdiction over radio broadcasting and communications, as well as licensing authority for every single radio transmitter in the nation, under the authority of the Federal Radio Commission, which was then folded into the Federal Communications Commission in the 1934 Act.<sup>145</sup> Consequently, there was minimal state regulation of mobile telephone and other radio communications, even under the states' generally broad legal mandates to regulate common carriers.<sup>146</sup>

The 1993 Budget Act eliminated even that modicum of residual state regulatory power by explicitly preempting all state regulation of both mobile phone rates and entry into the cellular market.<sup>147</sup> Congress “intended generally to preempt state and local rate and entry regulation of all commercial mobile radio services to ensure that similar services are accorded similar regulatory treatment and to avoid undue regulatory burdens.”<sup>148</sup> States that wanted to continue regulating wireless rates were told to come forward and explain to the FCC why doing so was necessary to protect consumers.<sup>149</sup> A few states filed such applications,

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141. See HUBER, KELLOGG & THORNE, *supra* note 102, at 863-64.

142. *Id.* at 864.

143. *Id.*

144. *Id.* at 864-65.

145. See Radio Act of 1927, Pub. L. No. 69-632, 44 Stat. 1163; see generally National Broadcasting Co. v. United States, 319 U.S. 190, 210-13 (1943) (describing early regulatory history of radio).

146. See HUBER, KELLOGG & THORNE, *supra* note 102, at 869-70 & n.45.

147. 47 U.S.C. § 332(c)(3)(A).

148. Implementation of Sections 3(n) & 332 of the Commc'ns Act, *Second Report & Order*, 9 FCC Rcd. 1411, ¶ 250 (1994) [hereinafter Implementation of Sections 3(n) & 332], *decision quashed* by 10 FCC Rcd. 7824 (1995).

149. See 47 U.S.C. § 332(c)(3)(A).

but the Commission consistently turned them down. For example, in rejecting a petition by Connecticut, the FCC stated:

[W]hile we recognize that states have a legitimate interest in protecting the interests of telecommunications users in their jurisdiction, we also believe that competition is a strong protector of these interests and that state regulation in this context could inadvertently become as a burden to the development of this competition.<sup>150</sup>

This preemptive federal deregulation of wireless telephony was driven in part by congressional recognition that “wireless networks increasingly operate on a multistate” basis and that “calls frequently traverse state borders.”<sup>151</sup>

**Information Services.** Online “information services”—a capacious, if rather outdated, term that covers everything from online gaming to Internet search engines—were deregulated for the same reason and on the same logic as was Customer Premises Equipment: these services could be provided competitively if the market were deregulated nationwide.<sup>152</sup> The Commission would not permit state preferences for continued regulation to interfere with its “comprehensive [de]regulatory scheme.”<sup>153</sup> Any lingering state regulation “would limit the kinds of services an unregulated vendor could offer, restricting this fast-moving, competitive market.”<sup>154</sup>

The Commission has also preemptively deregulated the provision of “enhanced services”—those information services provided by common carriers that combine the transmission and processing of data, including such familiar services as voicemail, e-mail, and alarm monitoring.<sup>155</sup> The FCC released the Bell Operating Companies (“BOCs”) from a requirement that they offer enhanced services through separate

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150. *See, e.g.*, Petition of the Connecticut Dep’t Pub. Util. Control to Retain Regulatory Control of the Rates of Wholesale Cellular Serv. Providers in the State of Connecticut, *Report & Order*, 10 FCC Rcd. 7025, ¶ 4 (1995) [hereinafter Conn. Petition], *aff’d*, Conn. Dep’t of Pub. Util. Control v. F.C.C., 78 F.3d 842 (2d Cir. 1996).

151. Leonard J. Kennedy & Heather A. Purcell, *Section 332 of the Communications Act of 1934: A Federal Regulatory Framework That Is “Hog Tight, Horse High, and Bull Strong”*, 50 FED. COMM. L.J. 547, 550 (1998).

152. *See Computer II*, *supra* note 139, at ¶ 7.

153. *Id.* ¶ 129.

154. *Id.* ¶ 129; *see also* HUBER, KELLOGG & THORNE, *supra* note 102, at 1094 (discussing FCC’s treatment of a petition by enhanced services providers in the District of Columbia).

155. “Enhanced services,” as characterized for many years by the FCC (including during the period when the FCC was deregulating them), were subsequently relabeled “information services” in the 1996 Telecommunications Act such that the two categories are no longer distinct.

subsidiaries and then preempted the states from regulating or imposing tariffs on any such interstate services.<sup>156</sup> The FCC observed that even a voicemail service offered by a purely local phone company to a discrete locale within a state could nonetheless receive and store calls from out of state or be accessed by the service's customer from out of state.<sup>157</sup> Each of the enhanced services had both an intrastate and an interstate component. Although it might be technically feasible for a BOC to comply with state structural separation requirements on just the intrastate portion of these jurisdictionally mixed services, it would not be economically or operationally feasible for them to do so. Accordingly, preemption was required because "a degree of certainty and uniformity may be necessary to enable the enhanced services market to develop in the way that both state commissions and this Commission desire."<sup>158</sup>

Finally, the Internet is, of course, "inherently interstate."<sup>159</sup> There are no political borders in cyberspace. This reality will be of growing significance in the regulation not just of the Internet itself but also of *wireline* telephony because the Internet's voice application, VoIP, offers intermodal competition for wireline.<sup>160</sup> This technology, which we more

156. After an initial remand, the FCC's order was upheld on appeal. Amendment of Sections 64.702 of the Commission's Rules & Regulations (Third Computer Inquiry), *Report & Order*, 104 F.C.C.2d 958 (1986), *vacated and remanded*, California v. F.C.C., 905 F.2d 1217 (9th Cir. 1990), *proceedings on remand*, Computer III Remand Proceedings: Bell Operating Co. Safeguards, *Notice of Proposed Rulemaking & Order*, 6 FCC Rcd. 174 (1990) [hereinafter *Computer III*], *rule modification*, 6 FCC Rcd. 7571 (1991), *vacated in part and remanded*, California v. F.C.C., 39 F.3d 919 (9th Cir. 1994), *on remand*, Computer III Further Remand Proceedings: Bell Operating Co. Provision of Enhanced Servs., *Order*, 10 FCC Rcd. 5692 (1995).

157. See Petition for Emergency Relief & Declaratory Ruling Filed by the BellSouth Corp., *Memorandum Opinion & Order*, 7 FCC Rcd. 1619, ¶ 9 (1992):

We conclude, based on the record, that BellSouth's voice mail service is capable of receiving, and does receive, calls from out-of-state as well as in-state locations. These calls can be from persons calling the voice mail customer, or from the customer calling to obtain messages recorded by the voice mail service.

158. *Computer III*, *supra* note 156, at ¶ 47.

159. Implementation of the Local Competition Provisions in the Telecomms. Act of 1996, *Declaratory Ruling & Notice of Proposed Rulemaking*, 14 FCC Rcd. 3689, 3715 (1999) (Comm'r Ness, concurring) ("Switched network telephone calls to Internet service providers are inherently interstate" due to "the interstate and international nature of the Internet."), *vacated and remanded*, Bell Atl. Tel. Cos. v. F.C.C., 206 F.3d 1 (D.C. Cir. 2000), *reinstated on remand*, 16 FCC Rcd. 9151 (2001); see also Pulver, *supra* note 106, at ¶¶ 16, 21 & n.78 (all Free World Dial-Up service on Internet is deemed interstate even if both parties are in same state).

160. VoIP services are generally referred to as static or nomadic. Static providers typically use residential cable or DSL to deploy service for VoIP phones in fixed locations. Nomadic providers utilize technology that allows their subscribers to use their service wherever they have an Internet connection. See, e.g., International Engineering Consortium, *Is VoIP Without E9-1-1 Worth the Risk?: Challenges, Approaches, and Recommendations for VoIP Service Providers - Technical Challenges*, [http://www.iec.org/online/tutorials/voip\\_e911/topic03.html](http://www.iec.org/online/tutorials/voip_e911/topic03.html) (last visited Mar. 20, 2008).

fully discuss below, must be presumed to carry *all* calls in an interstate fashion. This is the case, even if the calls are from one house to the next-door neighbor, because the Internet stretches across state and national borders and uses packet switches rather than circuit switches. Packet technology slices every transmission, voice or otherwise, into small digital packets that are then dispatched individually to their destination by whichever routes are most efficient based on moment-to-moment circuit availability and congestion, whether those transmission paths to the house next door run only through local ISPs or through France and India.

Although such Internet applications themselves are no longer subject to state-by-state regulation, wireline calls to VoIP subscribers still are—or at least state regulators act as if they are. Yet even a “local” call to a VoIP subscriber down the street will almost always be interstate because VoIP providers employ centralized, high-capacity switches to serve their subscribers. For example, Cox Communications serves all of its VoIP subscribers in the eastern United States (including current customers in, e.g., Virginia) through a single switch located in Atlanta, Georgia.<sup>161</sup> Time Warner Cable, which serves customers in at least 33 states<sup>162</sup> and made VoIP available in all of its markets by 2005,<sup>163</sup> has forecast that it will need only about a dozen or so regional switches to handle its entire national telephony rollout.<sup>164</sup> Thus, the vast majority of

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161. See Unidentified Representative of Cox Commc'ns Inc. at the Citigroup Smith Barney Entm't, Media & Telecomm. Conference (Jan. 7, 2004), in FIN. DISCLOSURE WIRE, Jan. 7, 2004, at 10:30:00. The switch used to provide VoIP in Roanoke, Virginia:

[I]s sitting in Atlanta, Georgia . . . connected by our backbone. . . . [This is] how easy it is for us to leverage all of the investment that we have in telephone against other markets. Since we don't have to drop a call center into the market, we don't have to drop a big fat expensive switch into the market. We can do it this way, and that's why we think for smaller markets, the voice over IP technology is a great way to go.

*Id.*; Jim Robbins, President & CEO of Cox Commc'ns Inc. at the Citigroup Smith Barney Entm't, Media & Telecomm. Conference (Jan. 7, 2004), in FIN. DISCLOSURE WIRE, Jan. 7, 2004, at 10:30:00 (“[When] we launch in another market in the eastern part of U.S., again, the switch will be . . . served out of our switch in Atlanta.”).

162. See Time Warner Cable, Company Highlights, <http://www.timewarnercable.com/corporate/aboutus/companyhighlights.html> (last visited Mar. 20, 2008).  
<http://www.timewarnercable.com/corporate/aboutus/companyhighlights.html> (last visited Nov. 24, 2007).

163. See *The Current State of Competition in the Communications Marketplace: Hearings Before the Subcomm. on Telecomm. & the Internet of the H. Comm. on Energy & Commerce*, 108th Cong. 18 (2004) [hereinafter, *2004 Competition Hearings*] (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.), available at [http://frwebgate.access.gpo.gov/cgi-bin/useftp.cgi?IPaddress=162.140.64.183&filename=92536.pdf&directory=/diska/wais/data/108\\_house\\_hearings](http://frwebgate.access.gpo.gov/cgi-bin/useftp.cgi?IPaddress=162.140.64.183&filename=92536.pdf&directory=/diska/wais/data/108_house_hearings).

164. See Mike Farrell, *All's Quiet on the Cutting Edge*, MULTICHANNEL NEWS, Feb. 23, 2004, available at <http://www.multichannel.com/article/CA382799.html>.

wireline calls to VoIP subscribers and of VoIP calls to wireline subscribers—even “local” calls where both caller and recipient are in the same town—will necessarily make use of out-of-state facilities.

**Broadband Data Services.** In the late 1990s, the Commission’s priority was to induce the market to provide faster and better Internet access to the nation. But cable companies are selected and franchised by village, town, county, and other local regulators (or, at best, in rare instances, at the state level), and, in 1999, tenacious state and local regulators were still imposing open access rules and other requirements on cable operators.<sup>165</sup> The Commission’s staff concluded that “consumers would be poorly served by a fractured broadband landscape wherein each locality devises its own set of cable Internet access regulations.”<sup>166</sup> This concern dominated the Commission’s 2002 proceeding on whether to classify cable modems as “cable services,” “information services,” or “telecommunications services”:

If cable modems were to be defined as “cable services,” this would expose operators to regulations and taxes imposed by states and/or local franchising authorities; if deemed “telecommunications services,” operators would potentially face federal regulation; if designated “information services,” federal deregulation would preempt state or local rules.<sup>167</sup>

Once again, the Commission’s legal classification of an electronic transmission technology was dictated by the consequences for the creation of a nationwide network:

[W]e address potential areas of regulatory uncertainty at the State and local levels that could also discourage . . . investment and innovation. We would be concerned if a patchwork of State and local regulations beyond matters of purely local concern resulted in inconsistent requirements affecting cable modem service, the technical design of the cable modem service facilities, or business arrangements that discouraged cable modem service deployment across political boundaries.<sup>168</sup>

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165. See Hazlett, *supra* note 55, at 189-90.

166. DEBORAH A. LATHEN, FCC BUREAU CHIEF, BROADBAND TODAY 39 (1999), available at <http://ftp.fcc.gov/Bureaus/Cable/Reports/broadbandtoday.pdf>.

167. Hazlett, *supra* note 55, at 191; see also Barbara S. Espin & Gary S. Lutzker, *Poles, Holes and Cable Open Access: Where the Global Information Superhighway Meets the Local Right-of-Way*, 10 COMMLAW CONCEPTUS 23, 25-28 (2001).

168. Inquiry Concerning High-Speed Access to the Internet Over Cable & Other Facilities, *Declaratory Ruling & Notice of Proposed Rulemaking*, 17 FCC Rcd. 4798, ¶ 97 (2002) [hereinafter *Declaratory Broadband Ruling*], *aff'd in part, vacated in part sub nom. Brand X Internet Servs. v. F.C.C.*, 345 F.3d 1120 (9th Cir. 2003), *rev'd and remanded sub*

Accordingly, the Commission classified cable modem service—which is still an important form of broadband access to the Internet—as an “information service” in order to ensure that it would be subject exclusively to federal deregulation.<sup>169</sup>

The 1996 Telecommunications Act has also resulted in a degree of preemptive deregulation of the high-speed data services provided by local telephone companies, known as Digital Subscriber Lines (“DSL”).<sup>170</sup> After several false starts,<sup>171</sup> the FCC concluded that “broadband services should exist in a minimal regulatory environment that promotes investment and innovation in a competitive market. . . . Therefore, our policy and regulatory framework will work to foster investment and innovation in these networks by limiting regulatory uncertainty and unnecessary or unduly burdensome regulatory costs.”<sup>172</sup> Accordingly, in February 2003 the Commission largely exempted telephone-based broadband facilities from federal and state price regulation.<sup>173</sup> The Commission also ruled that states could not impose any contrary requirements.<sup>174</sup>

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*nom.* Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 545 U.S. 967, 978, 1000-02 (2005) [hereinafter *Brand X Internet Servs.*] (holding that the 9th Circuit erred in not applying the correct standard to the FCC decision). The FCC declaratory ruling was finally affirmed on remand, *Brand X Internet Servs. v. F.C.C.*, 435 F.3d 1053 (9th Cir. 2006). Even before the final declaratory ruling in that proceeding, the Commission had asserted “jurisdiction over all interstate communications services, including the high-speed services offered by such [broadband] providers.” Inquiry Concerning High-Speed Access to the Internet Over Cable & Other Facilities, *Notice of Inquiry*, 15 FCC Rcd. 19,287, 19,288 ¶ 3 (2000); see also *MediaOne Group v. County of Henrico*, 257 F.3d 356, 365 (4th Cir. 2001) (“The FCC, in its amicus brief, has diplomatically reminded us that it has jurisdiction over all interstate communications services, including high-speed broadband services.”).

169. Declaratory Broadband Ruling, *supra* note 168, at ¶ 97. The FCC’s ruling was upheld by the Supreme Court in *Brand X Internet Servs.*, 545 U.S. at 978, 1000-02.

170. See *WorldCom, Inc. v. F.C.C.*, 246 F.3d 690, 692 (D.C. Cir. 2001) (describing DSL technology).

171. See, e.g., Deployment of Wireline Servs. Offering Advanced Telecomms. Capability, *Memorandum Opinion & Order & Notice of Proposed Rulemaking*, 13 FCC Rcd. 24,012 (1998) [hereinafter *Deployment*] (subsequent negative history exists); Deployment of Wireline Servs. Offering Advanced Telecomms. Capability, *Third Report & Order*, 14 FCC Rcd. 20,912 (1999); Implementation of the Local Competition Provisions of the Telecomms. Act of 1996, *Third Report & Order & Fourth Further Notice of Proposed Rulemaking*, 15 FCC Rcd. 3696, ¶¶ 302-317 (1999), *order modified* by 15 FCC Rcd. 1760 (1999).

172. Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities, *Notice of Proposed Rulemaking*, 17 FCC Rcd. 3019, ¶ 5 (2002) [hereinafter *Appropriate Framework for Broadband Access*].

173. See Press Release, FCC, FCC Adopts New Rules for Network Unbundling Obligations of Incumbent Local Phone Carriers (Feb. 20, 2003), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-231344A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-231344A1.pdf).

174. *Id.* For a brief interval, wireline telephone companies’ broadband product, DSL, remained subject to the FCC’s common carrier requirements while the cable industry’s broadband service suffered no such burden. The Supreme Court upheld the FCC’s decision to

**Voice over Internet Protocol.** The most important new telephone technology is undoubtedly that which makes use of the Internet. The broad category of “information services” preemptively deregulated by the FCC was extended in 2004 to a service offered by pulver.com that allowed members to call one another over the Internet. Known as Free World Dialup (“FWD”), this voice application makes no use of the traditional public switched telephone network (“PSTN”). Because Pulver does not offer any transmission service of its own, members must have broadband Internet access and must acquire software that enables their personal computers to function as “soft phones.” Once these criteria are met, anyone anywhere in the world can obtain a Pulver-assigned FWD number that enables that member to establish free Voice over Internet Protocol communications with other FWD members over the Internet. Pulver neither knows nor needs to know where its members are geographically located in order for its members to use FWD, and once an FWD member obtains an FWD number, that number is completely portable to any broadband-accessible location in the world to which that member may go.<sup>175</sup>

FWD plainly has components that are, in themselves, *wholly intrastate*: the caller’s link to the location of his local ISP, which allows him to access the Internet, is typically intrastate, and the FWD service “connects consumers around the corner” as well as “across the globe.”<sup>176</sup> But the Commission noted “the existence of other ‘network’-based service examples where, although an intrastate component of such service may exist, this intrastate component must nonetheless yield to exclusive federal jurisdiction.”<sup>177</sup> The Commission found that the “nature” of

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treat DSL and cable broadband differently in *Brand X Internet Servs.*, 545 U.S. 967. The Court’s decision was predicated on the traditional rule of deference to agency interpretation of congressional delegations of power in technical regulatory fields. *Id.* at 996-97 (citing *Chevron U.S.A., Inc. v. Nat’l Resources Def. Council, Inc.*, 467 U.S. 837 (1984)). The Court acknowledged that the FCC had imposed common carrier obligations on DSL services based not on an analysis of contemporary market conditions, but on the basis of local wireline companies’ historical (and no longer extant) monopoly status, whereas the FCC order under review had analyzed current market conditions in declining to extend common carrier restrictions to cable broadband. *Id.* at 1001-02. The Court declined to address the obvious inconsistency and discrimination in the FCC’s treatment of the two competing modes of broadband access on the grounds that the FCC was already in the midst of reconsidering its regulatory treatment of all information services, and the Court would not interfere mid-stream with respect to subject matter that was so “technical, complex, and dynamic.” *Id.* Not long after the *Brand X Internet Servs.* decision, the FCC indeed reclassified broadband Internet access services offered by wireline companies as information services subject to a “lighter regulatory touch.” *Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities, Report & Order & Notice of Proposed Rulemaking*, 20 FCC Rcd. 14,853, ¶ 3 (2005) [hereinafter *Internet Over Wireline Facilities*].

175. Pulver, *supra* note 106, at ¶ 5.

176. *Id.* at 3326 (Chairman Powell, concurring).

177. Pulver, *supra* note 106, at ¶ 25 n.91.



FWD as a service:

[N]ot bound by geography may well render an attempt by a state to regulate any theoretical intrastate FWD component an impermissible extraterritorial reach. . . . Because of the way FWD is offered, one state's regulation of FWD may have the practical effect of requiring those same regulations to be applied to FWD service for all users.<sup>178</sup>

“Furthermore, if Pulver were subject to state regulation, it would have to satisfy the requirements of more than 50 state and other jurisdictions with more than 50 different certification, tariffing and other regulatory obligations.”<sup>179</sup>

The scenario that would result if FWD were characterized as “telecommunications” caused the FCC to shudder: “state-by-state regulation of a wholly Internet-based service is inconsistent with the controlling federal role over interstate commerce required by the Constitution.”<sup>180</sup> Pulver's FWD was consequently characterized as an

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178. *Id.* ¶ 23; see *Cotto Waxo Co. v. Williams*, 46 F.3d 790, 793 (8th Cir. 1995) (“Under the Commerce Clause, a state regulation is per se invalid when it has an ‘extraterritorial reach,’ that is, when the statute has the practical effect of controlling conduct beyond the boundaries of the state. The Commerce Clause precludes application of a state statute to commerce that takes place wholly outside of the state's borders.”)

179. Pulver, *supra* note 106, at ¶ 25.

180. *Id.* ¶ 16. Perhaps the most ominous example of retrograde application of state-by-state regulation to the inherently interstate Internet is the “net neutrality” fight, which concerns the offering by large Internet service providers of priority carriage for an additional fee. Advocates of broadband regulation – some consumer advocates as well as major Website operators such as Google and eBay – have recoiled from the prospect that any transaction on the Internet might be given priority (for a fee) over any other. See Kristina Rasmussen, ‘Net Neutrality’ Fight Moves to States, BUDGET & TAX NEWS, Aug. 1, 2006, available at <http://www.heartland.org/Article.cfm?artId=19415>. Free-market advocates have countered that there is little, if any, evidence of the supposed abuses that net-neutrality activists have been decrying for years. They observe that, on the contrary, the Internet has flourished in the absence of government regulation, and that proposals to regulate broadband would dampen innovation and erode incentives to investment. Congress seemed to hear and to heed that perspective in June 2006, when the House voted 269-152 against adding a net neutrality amendment to a major cable television franchise reform bill. *Id.* With national legislation at least temporarily stymied, activists have taken the campaign for net neutrality to state legislatures and the offices of state attorneys general. *Id.*; see also Mackinac Center for Public Policy, Internet Policy Strictly a Federal Prerogative: Action by Michigan Lawmakers on ‘Net Neutrality’ Would Invite Costly Lawsuit, <http://www.mackinac.org/article.aspx?ID=8103> (last visited Mar. 20, 2008); *Granholm Signs Cable TV Bill - Without Net Neutrality*, MICH. TECH. NEWS, Dec. 21, 2006, <http://mitechnews.com/articles.asp?id=6469> (upon signing Michigan's franchising reform bill, Gov. Granholm urged the Michigan Legislature to enact net neutrality legislation in its next session); Jason Lee Miller, *Net Neutrality Goes Stateside*, WEB PRO NEWS, Nov. 29, 2006, <http://www.webpronews.com/topnews/topnews/wpn-60-20061129NetNeutralityGoesStateside.html>; Jim Puzzanghera, *Congress Likely To Hang Up on '06 Telecom Reform*, L.A. TIMES, Dec. 3, 2006, (forecasting problems with efforts by telephone companies to get national legislation through Congress addressing pay-TV over phone lines in wake of Democratic Party victories in mid-term elections); Posting of Josh

unregulated “information service” subject only to federal jurisdiction. The Commission went out of its way to specify that “any state regulations that seek to treat FWD as a telecommunications service or otherwise subject it to public-utility type regulation would almost certainly pose a conflict with our policy of nonregulation.”<sup>181</sup> In short, the FCC’s *legal characterization* of FWD was driven by the imperatives of “remov[ing] any regulatory uncertainty” and ensuring that this inherently interstate service “remain insulated from unnecessary and harmful economic regulation at both the federal and state levels. This action is designed to bring a measure of regulatory stability to the marketplace and therefore remove barriers to investment and deployment of Internet applications and services.”<sup>182</sup>

The same circumstances and logic dictated the same result in the more recent battle over state-by-state regulation of a similar (but far more important) VoIP service offered by Vonage. In *In the Matter of Vonage Holdings Corporation*,<sup>183</sup> the Commission preempted an order of the Minnesota Public Utilities Commission applying its traditional “telephone company” regulations to Vonage’s “DigitalVoice” service, which provides VoIP communication that “resembles the telephone service provided by the circuit-switched network.”<sup>184</sup> Vonage’s customers may use the service anywhere in the world where they can find a broadband connection to the Internet. They “may place or receive calls over the Internet to or from anyone with a telephone number – including another Vonage customer, a customer of another VoIP provider, a customer of a commercial mobile radio service (CMRS) provider, or a user reachable only through the public switched telephone network (PSTN).”<sup>185</sup>

Stressing that “the characteristics of DigitalVoice preclude any practical identification of, and separation into, interstate and intrastate communications for purposes of effectuating a dual federal/state

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Silver to The Huffington Post Blog, *Battle for Internet Freedom Moves to States*, [http://www.huffingtonpost.com/josh-silver/battle-for-internet-freed\\_b\\_35144.html](http://www.huffingtonpost.com/josh-silver/battle-for-internet-freed_b_35144.html) (Nov. 29, 2006). Putting aside for the moment the merits of the net neutrality argument, at the very least it is obvious that such a regulatory policy choice for a national – indeed, international – network industry should be made at the national rather than the state or local level. The information superhighway cannot be regulated as if it were fifty discontinuous sets of winding country roads.

181. Pulver, *supra* note 106, at ¶ 15.

182. *Id.* ¶ 1.

183. Vonage Holdings Corp., *Memorandum & Order*, 19 FCC Rcd. 22,404 (2004) [hereinafter VoIP Order], *aff’d*, Minn. Pub. Utils. Comm’n v. F.C.C., 483 F.3d 570 (8th Cir. 2007). Jeffrey Pulver, the founder of pulver.com, was also one of the founding investors of Vonage, the leading VoIP provider.

184. *Id.* ¶ 4.

185. *Id.* ¶ 8.

regulatory scheme,<sup>186</sup> the Commission concluded that Minnesota's order regulating Vonage's service should be preempted regardless of whether it was considered a telecommunications service or an information service (an issue that the Commission left unresolved)<sup>187</sup>. Although the Commission acknowledged that Vonage's VoIP service enables (and often involves) purely intrastate communications, it found the traditional geographic "end-to-end" analysis for distinguishing between interstate and intrastate communications difficult, if not impossible, to apply, given VoIP's "total lack of dependence on *any* geographically defined location."<sup>188</sup> Nor did the Commission find it feasible to apply familiar proxy or allocation mechanisms to approximate an end-to-end result.<sup>189</sup> In short, because Minnesota's order regulating Vonage's DigitalVoice service could not, under prevailing technological and economic conditions, be "appl[ied] only to intrastate calling functionalities without also reaching the interstate aspects of Digital Voice," the FCC preempted it.<sup>190</sup>

Even when evaluated in their incomplete, partially implemented phases, the deregulatory policies for the Internet itself, for voice applications transmitted over the Internet, and for mobile phones have been extraordinarily successful. The argument in favor of these policy reforms was that eliminating state-by-state regulation would achieve greater efficiencies in the provision of regional and national networks, and that such economies would result in benefits for consumers.<sup>191</sup> There were, of course, dissenting views. For example, in the legislative and lobbying battles that preceded federal deregulation of wireless service in 1993, state regulators predicted abusive exploitation by cellular providers.<sup>192</sup> That never happened.

Instead, the advent of an unfettered market brought a flood of capital investment and a wave of innovation—and those factors drove down costs even while wireless networks were being expanded regionally and nationally. Lower costs and robust competition led to dramatic increases both in the number of wireless subscribers and in the usage of

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186. *Id.* ¶ 14.

187. *Id.* ¶ 14 & n.46.

188. *Id.* ¶ 25 (emphasis in original).

189. VoIP Order, *supra* note 183, at ¶¶ 26-29.

190. *Id.* ¶ 31; *see also* Madison River Commc'ns, LLC & Affiliated Cos., *Order*, 20 FCC Rcd 4295, ¶¶ 3-5 (2005) (company and FCC agreed upon consent decree terminating FCC's investigation into "allegations that Madison River was blocking ports used for VoIP applications, thereby affecting customers' ability to use VoIP through one or more VoIP service providers"; Madison River paid a \$15,000 fine and agreed to "not block ports used for VoIP applications or otherwise prevent customers from using VoIP applications").

191. Hazlett, *supra* note 55, at 219.

192. Robert W. Hahn et al., *Federalism & Regulation*, 26 REG., Winter 2003-2004, at 49 [hereinafter *Federalism & Regulation*].

wireless phones; prices plummeted even while new services proliferated and the quality of service rose steadily.<sup>193</sup> In 1995, there were just 34 million cell phone subscribers; a decade later there were 204 million subscribers to wireless networks covering 95 percent of the U.S. population.<sup>194</sup> Wireless phone usage (as measured in minutes) increased—exploded would be a more accurate term—more than 450 percent from 2000 through 2004, while use of wireline telephony decreased.<sup>195</sup> Consumers have responded with this surge of demand primarily because the price per minute for cell calls dropped 75 percent between 1994 and 2001.<sup>196</sup> The United States now has the lowest average wireless price among developed countries—8.1¢ effective price per minute as of 2005—and that rate continues to fall at almost 20 percent per year.<sup>197</sup>

The figures tell a similar story of success for preemptive federal deregulation of broadband data services. Broadband Internet access is now available to 99 percent of the U.S. population.<sup>198</sup> From 2000 to 2004, the number of broadband Internet access lines rose from 4.4 million to 32.5 million; by 2005 the figure was over 50 million.<sup>199</sup> Use of dial-up Internet access has shrunk dramatically in the same period, to the point that three out of four Americans who have Internet access use broadband.<sup>200</sup> Data traffic surpassed voice traffic in 1998, and now

193. Comprehensive econometric study of preemptive federal wireless regulation and deregulation confirms that it has been better both for the industry and for consumers. See, e.g., Hazlett, *supra* note 55, at 193-237. Indeed, it is touted as a rare and valuable “natural experiment” in the virtues of federal over state-by-state regulation – the perfect case study. *Id.* at 205-06.

194. See KEITH MALLINSON, YANKEE GROUP REPORT, WIRELESS SUBSTITUTION OF WIRELINE INCREASES CHOICE AND COMPETITION IN VOICE SERVICES 1 (2005) [hereinafter WIRELESS SUBSTITUTION]. The most current figures may be found in the FCC’s annual wireless report. Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, *Eleventh Report*, 21 FCC Rcd. 10,947 (2005), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-06-142A1](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-06-142A1).

195. WIRELESS SUBSTITUTION, *supra* note 194, at 1; see also *2004 Competition Hearings*, *supra* note 163, at 29-50 (statement of Ned P. Zachar, Dir. of Telecom Servs. Research, Lever House).

196. *Federalism & Regulation*, *supra* note 192, at 49; see also Hazlett, *supra* note 55, at 157 n.1.

197. WIRELESS SUBSTITUTION, *supra* note 194, at 4; *2004 Competition Hearings*, *supra* note 163, at 24 (statement of Adam Quinton, Managing Dir. & First Vice President, Merrill Lynch & Co., Inc.).

198. FCC, INDUSTRY ANALYSIS AND TECHNOLOGY DEVISION, HIGH-SPEED SERVICES FOR INTERNET ACCESS: STATUS AS OF DECEMBER 31, 2005 1 & tbl.1 (2006), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-266596A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-266596A1.pdf) (99% of U.S. population lives in the 98% of zip codes that have at least one broadband provider).

199. *Id.* at tbl.1.

200. Carol Wilson, *Nielson: Broadband Use Nears 75% in U.S.*, TELEPHONY ONLINE, June 22, 2006, [http://telephonyonline.com/broadband/news/Nielsen\\_broadband\\_Internet\\_062206/index.htm](http://telephonyonline.com/broadband/news/Nielsen_broadband_Internet_062206/index.htm)

exceeds voice traffic by an eleven-to-one margin worldwide.<sup>201</sup> Wireless and data services combined now account for well over half of the industry's revenues. In contrast, wireline local voice revenues continue to decline and to be offset by increasing growth in wireline data revenues.<sup>202</sup>

The message is clear and the confirmation of the wisdom of the Commerce Clause's Framers—and of their contemporary, Adam Smith—is undeniable: preemptive federal regulation, followed by deregulation once competition is sufficient, unleashes market forces that expand and improve interstate communications networks.

*C. All Three Major Network Technologies—Wireline, Wireless, and Cable—Now Compete to Provide Voice, Internet, and Video Services*

The most important ramification of this explosive growth in deregulated wireless and VoIP services is that both of these technologies now provide intermodal competition for traditional local wireline telephony, thus substantially strengthening the rationale for similar preemptive federal regulation (and ultimate deregulation) of wireline telephony as well. Sauce for the goose is sauce for the gander—deregulation of wireline will unleash the same market forces that have multiplied service options and driven prices down in the wireless and cable markets.

Telecommunications can no longer be divided into a neat taxonomy of distinct species—wireline, wireless, cable, VoIP—occupying separate, noncompeting niches. Wireline telephony is not an isolated, discrete business anymore. It is part of a much larger, more diverse, and more complicated telecommunications market. “[P]olicymakers, understandably, work within legacy constructs – including statutes and case law – that define wireless and other intermodal services as different from traditional telephony . . . .”<sup>203</sup> But inquiries into the proper locus of jurisdiction over, and the state of competition in, the local wireline segment of the market must take into account the “fundamental intermodal shift” created by the rise of new telephone technologies such as cell phones, cable telephony, and VoIP.<sup>204</sup> Indeed, the Commission's

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201. Paul Andrews, *A Tech Rebirth?*, U.S. NEWS & WORLD REP., Jan. 13, 2003, at 28.

202. See RAINA SMYTH ET AL., MORGAN STANLEY RESEARCH, TELECOM SERVICES: INITIATION OF COVERAGE 4 (2006). It has been estimated that data revenue now accounts for approximately 10% of average revenues per user among the national wireline carriers. *Id.*

203. *2004 Competition Hearings*, *supra* note 163, at 15 (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.).

204. *Id.* at 15; *see also id.* at 24-29 (statement of Adam Quinton, Managing Dir. & First Vice President, Merrill Lynch & Co., Inc.); *id.* at 29-50 (statement of Ned P. Zachar, Dir. of

implementation of the 1996 Act has already been reversed by the courts in at least one instance for “fail[ing] to consider adequately [the impact of] intermodal competition.”<sup>205</sup> Continued state-by-state regulation of one telecommunications medium—wireline—but not those with which it competes—wireless and VoIP—distorts consumer choice, forcing decisions to be based not on free-market competition but on regulatory classification.

Inherent mobility and bulk-minute plans that do not distinguish between local and long-distance calling have made cell phones attractive to a growing throng of consumers as a substitute for, not merely a supplement to, traditional wireline telephone service. Despite the precipitous drop in cellular service prices, wireless voice revenues surpassed wireline voice revenues in 2001,<sup>206</sup> largely because wireless subscribers now outnumber wireline switched access lines.<sup>207</sup> Furthermore, even when wireline service is retained by customers, a greater portion of their usage is being shifted to their cell phones. The availability and quality of service of cellular communications now displace 60 percent of long distance calling and 36 percent of local calling from landlines to wireless phones.<sup>208</sup> Indeed, a growing portion of telephone consumers are canceling their landlines altogether and relying entirely on their cell phones. Approximately 10 percent of the total consumer market has already gone wireless-only,<sup>209</sup> and that figure could triple within the next few years.<sup>210</sup> In metropolitan markets, 15 percent of the population is exclusively wireless, and among young adults aged 18-24 nearly a third (31 percent) have cut the landline telephone cord.<sup>211</sup> Consequently, changing demographic patterns—young, single people have more mobile lifestyles—will inevitably accelerate the substitution of cell phones for wireline service, both local and long-distance.<sup>212</sup> These

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Telecom Servs. Research, Lever House).

205. United States Telecom Ass’n v. F.C.C., 359 F.3d 554, 563 (D.C. Cir. 2004) [hereinafter *USTA II*]; United States Telecom Ass’n v. F.C.C., 290 F.3d 415, 428-29 (D.C. Cir. 2002) [hereinafter *USTA I*]. The Court of Appeals was referring specifically to intermodal competition in the broadband market.

206. T.A. JACOBS, ET AL., JP MORGAN, TELECOMMUNICATIONS SERVICES 2001 1 (2001).

207. WIRELESS SUBSTITUTION, *supra* note 194, at 4 (noting that by year-end 2004, U.S. wireless subscribers outnumbered the nation’s 178 million switched access lines).

208. *Id.* at 1.

209. *Id.*

210. 2004 Competition Hearings, *supra* note 163, at 32 (statement of Ned P. Zachar, Dir. of Telecom Servs. Research, Lever House) (“[W]ith roughly 5 million [wireline customers] having already ‘cut the cord’ it’s reasonable to believe that number could be 2-3x as high in 2008.”).

211. WIRELESS SUBSTITUTION, *supra* note 194, at 1.

212. See 2004 Competition Hearings, *supra* note 163, at 32 (statement of Ned P. Zachar, Dir. of Telecom Servs. Research, Lever House); see also *id.* at 23 (statement of Frank

figures “can be fully explained only by the reality of competitive choice”; in particular by “an acceleration in the movement toward wireless services and away from wireline telephony.”<sup>213</sup>

There has also been accelerating migration from wireline to various types of VoIP service. Just a few years ago, VoIP was described as “the thunder in the distance before the most formidable storm of intermodal competition is upon us.”<sup>214</sup> Those storm clouds have gathered and the current drizzle of competition will quickly become a monsoon. The major cable operators that currently provide the lion’s share of broadband Internet access could well prove to be the heavy-hitters in this segment of the market. To take just one example, Cablevision made VoIP service available in all of its markets in 2003<sup>215</sup> and the other major cable companies scrambled to catch up. Time Warner rolled out its VoIP service and overtook Cablevision by December of 2005, with twice the number of subscribers.<sup>216</sup> Insofar as the prerequisite for nomadic VoIP service is merely a high-speed, broadband Internet connection, VoIP competition for wireline telephony could also be presented by satellite Internet providers, ILECs offering DSL connections, wireless Web providers (known as WiFi or WISPs—Wireless Internet Service Providers), and even electric utility companies through the Broadband Over Powerline (“BPL”) technology.<sup>217</sup> Of course, there are also the companies, such as Vonage, that do not deliver the underlying broadband connectivity, but instead offer VoIP simply as another application of a customer’s existing Internet access—these are the “bring your own access” providers.<sup>218</sup>

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Louthan, Vice President, Raymond James Financial, Inc.).

213. *Id.* at 15-16 (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.); *see also id.* at 26 (statement of Adam Quinton, Managing Dir. & First Vice President, Merrill Lynch & Co., Inc.); *id.* at 32 (statement of Ned P. Zachar, Dir. of Telecom Servs. Research, Lever House).

214. *Id.* at 18 (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.).

215. *Id.* at 26 (statement of Adam Quinton, Managing Dir. & First Vice President, Merrill Lynch & Co., Inc.).

216. *See* MICHAEL PAXTON, IN-STAT REED ELEC. GROUP, CABLE TELEPHONY SERVICE: VOIP DRIVES SUBSCRIBER GROWTH 24 (2006) (in December 2005 Time Warner had more than a million VoIP subscribers to Cablevision’s 600,000). By the end of the first quarter of 2006, Time Warner had 1.4 million subscribers. *See* KATE GRIFFIN, YANKEE GROUP, THE VOIP EVOLUTION CONTINUES: FORECASTING BROADBAND VOIP AND CABLE TELEPHONY 11 (2006).

217. This technology employs the untapped transmission potential of the nation’s massive electrical power grid. The FCC has adopted changes to its rules to promote BPL broadband service. *See* Press Release, FCC, FCC Adopts Rules For Broadband Over Power Lines To Increase Competition And Promote Broadband Service To All Americans (Oct. 14, 2004), *available at* <http://www.atcb.com/publicdocs/FCC-NEWS-DOC-253125A1final-101404.pdf> (discussing Carrier Current Sys., Including Broadband Over Power Line Sys., *Report & Order*, 19 FCC Rcd. 21,265 (2004)).

218. *See* GRIFFIN, *supra* note 216, at 8. In 2005, Vonage’s subscribership grew a

The implications of VoIP for wireline telephony are profound:

[T]he introduction of VoIP services will move residential competition to a place that legislators and regulators could not have expected realistically under the copper-based telephony model. In this new intermodal competitive landscape, consumers will be able to choose from asset-based competitors whose services are differentiated from, and more convenient than, circuit-switched telephony. Further, the pricing for services will almost certainly, in my view, be more attractive than rates possible using legacy telephony, because of the underlying economics of Internet-based technologies.<sup>219</sup>

Indeed, many analysts anticipate that VoIP will quickly bypass wireline CLECs and circuit-switched cable telephony as competition for ILECs in the residential telephone market.<sup>220</sup> From December 2004 to December 2005, the number of VoIP-enabled cable telephony subscriber households in North America quadrupled.<sup>221</sup> Some analysts forecast that there will be more than 26 million residential broadband VoIP customers by 2010.<sup>222</sup>

The three major technology platforms, i.e., wireline, wireless, and cable, are now competing not just with respect to the provision of voice services, but also in broadband Internet access and video programming services. Cable companies no longer provide merely subscription television entertainment; they are now the principal providers of broadband Internet access and, as one application of that broadband service, they also provide voice service either by circuit-switched telephony or by VoIP.

Similarly, most U.S. providers of traditional voice service provide wireless services through an affiliate or subsidiary. These affiliates also provide broadband Internet access through highspeed DSL service whose signal is carried on the same ILEC copper or fiber-optic network that carries wireline phone service. And, as described more fully below, having invested billions to build the fiber-optic networks necessary to support broadband Internet access, telephone companies are now in a position to offer high-definition, digital video programming and therefore to offer genuine competition to cable systems for the first time.

Finally, wireless providers have likewise begun to compete in both

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remarkable 250%; as of March 2006, Vonage reported 1.5 million customers. *Id.* at 9.

219. *2004 Competition Hearings*, *supra* note 163, at 18-19 (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.).

220. *Id.*

221. *See* PAXTON, *supra* note 216, at 24; *see also* GRIFFIN, *supra* note 216, at 8-9 (reporting that in 2005 the U.S. residential market grew from 1.1 million to 4 million consumer broadband VoIP subscribers).

222. *See* GRIFFIN, *supra* note 216, at 8-9.



the Internet and video entertainment markets. Wireless broadband Internet access for laptop computers and hand-held Personal Data Appliances (“PDAs”) is now widely available on cellular networks, not just at the 40,000 “wi-fi hot spots” in Internet cafes, airports, hotels, and other locations.<sup>223</sup> Wireless companies have also entered the video entertainment broadcasting market. Sprint PCS got the ball rolling with its MobiTV service, which streams programs onto wireless phones via the Internet, allowing customers to watch news, sports, and other video programming.<sup>224</sup> AT&T Wireless included MobiTV as part of its mMode data service in 2004, and it is now part of Cingular’s Media Net service (after the merger of the Cingular and AT&T networks).<sup>225</sup> Verizon Wireless launched its EV-DO network to provide wireless Internet access for business customers in 2003.<sup>226</sup> In 2005 it added V CAST—the nation’s first wireless multimedia service, providing mobile subscribers with news programming, music videos, sports clips, video games, and even episodes of television programs.<sup>227</sup> Verizon took the next step in the first quarter of 2007 when it launched V CAST Mobile TV, offering television on wireless phones at 30 frames per second, which is twice the speed of prior wireless networks and comparable to broadcast TV.<sup>228</sup> The debut offering included a number of popular networks, including CBS, NBC, Fox, Comedy Central, MTV, and Nickelodeon.<sup>229</sup>

Plainly, we are no longer living in a world of one segregated technology for each separate telecommunications, information, or entertainment service. The overwhelming and undeniable trend is convergence and intermodal competition. In general, the phenomenon of service convergence described above with respect to wireline telephony replicates the experience in wireless communications that began a decade ago, when the lines between pagers, cell phones and e-mail devices began

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223. Intel estimated this figure as of July 2006. See JiWire, WiFi Finder & Hotspot Directory, <http://www.jiwire.com/search-hotspot-locations.htm> (last visited Mar. 20, 2008).

224. Walter S. Mossberg, *Watching TV on Your Cellphone*, WALL ST. J., Sept. 1, 2004, at D7.

225. Press Release, MobiTV, Inc., Cingular Goes Live With MobiTV (Jan. 25, 2005), available at [http://www.mobitv.com/press/press.php?i=press/release\\_012505](http://www.mobitv.com/press/press.php?i=press/release_012505).

226. Walter S. Mossberg, *Verizon Devices Use High-Speed Network for Voice, Web, E-Mail*, WALL ST. J., Dec. 16, 2004, at B1.

227. Press Release, FCC, FCC Issues 12<sup>th</sup> Annual Report to Congress on Video Competition (February 10, 2006) [hereinafter FCC Issues 12<sup>th</sup> Annual Report], available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-263763A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-263763A1.pdf); Press Release, Verizon Wireless, Now Playing On a Cell Phone Near You: Video Clips, Music Videos and 3D Games (Jan. 31, 2005), available at <http://news.vzw.com/news/2005/01/pr2005-01-31.html>.

228. See Ben Patterson, *Verizon Wireless Unleashes MediaFlo Mobile TV*, INFOSYNC WORLD, Jan. 7, 2007, [www.infosyncworld.com/news/n/7345.html](http://www.infosyncworld.com/news/n/7345.html).

229. Parental controls are available on this mobile phone television service. *Id.*

to disappear. At that time the FCC found that “the direction is away from a ‘balkanized view’ that sees cellular, SMRs, paging, *etc.*, competing in separate markets.”<sup>230</sup>

[G]rowth in the wireless marketplace is bringing with it an increasing degree of service convergence. Technology and consumer demand, facilitated by our general policy not to restrict the services that can be provided over any particular band, are prompting commercial service providers to follow marketing strategies that blur the differences between the various services comprising the wireless marketplace.<sup>231</sup>

The “principal force driving [that] convergence . . . was the desire of carriers to meet the demand of their customers for ‘one-stop shopping,’ the ability to buy at one place a mixture of different mobile services.”<sup>232</sup> This blurring of providers and market niches is accelerating:

The industry is offering consumers the opportunity to “bundle” services at attractive price points in a way unheard of even just a year ago. For example, all of the major ILECs will launch packages of telephony, data and video services (by working with satellite providers Echostar and DirecTV) this year [2004]. Better rates are available from cable providers if you take their “triple play.” Wireless can be bundled with wireline in some areas with the added benefit of a single bill.<sup>233</sup>

The convergence of telecommunications platforms and providers makes continued state-by-state regulation of just one of those merging modes—traditional wireline—ever harder to justify. Again, the objection is not merely inequity, but *inefficiency*: disparate regulatory treatment of competitive modes of communication distorts the choices that consumers make in the marketplace. The persistence of state regulation of local wireline cannot be justified by mere reference to a tradition of such regulation in the face of the uniform *deregulation* of the intermodal substitutes for local wireline. The Commission itself has counseled that regulators must “avoid simply extending existing rules that were crafted to govern legacy services provided over legacy networks.”<sup>234</sup> “[D]ifferent regulatory treatment of similarly situated infrastructures

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230. Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, *First Report*, 10 FCC Rcd. 8844, 8864 (1995).

231. *Id.* (citation and quotation marks omitted).

232. *Id.*

233. *2004 Competition Hearings*, *supra* note 163, at 27 (statement of Adam Quinton, Managing Dir. & First Vice President, Merrill Lynch & Co., Inc.).

234. *Appropriate Framework for Broadband Access*, *supra* note 172, at ¶ 6.

distorts the evolution of those markets.”<sup>235</sup> The nation needs federal “regulatory parity” across competing modes of telephony to “promote investment” and “prevent[] burdensome and unnecessary state regulatory practices.”<sup>236</sup> Otherwise, regulation will impede investment and innovation in those technologies that do not fit FCC categories as neatly.

With wireline telephony, as with wireless and broadband, the government can and should promote competition “[b]y establishing like regulation of substitutable services.”<sup>237</sup> The regulatory objective should not be to promote wireline CLECs as competitors for wireline ILECs, but to encourage *all modes* of telecommunications that can compete with local wireline, even if they partake of different technologies, and similarly to encourage *all modes* of competition for broadband Internet access and video-entertainment services. In telecommunications regulation, as in antitrust law, the guiding principle is “to promote and protect competition, not specific competitors.”<sup>238</sup>

#### IV. THE TENSION BETWEEN THE COMMERCE CLAUSE AND CONTINUED STATE REGULATION OF INTERSTATE WIRELINE, WIRELESS, AND CABLE NETWORKS

It is beyond cavil that the constitutional policy of the Commerce Clause has been a stunning success. “The material success that has come to inhabitants of the states which make up this federal free trade unit has been the most impressive in the history of commerce . . . .”<sup>239</sup> If the United States is to maintain (or, in some respects, regain) its preeminence as the world’s most important and most rationally integrated free-trade zone, the implications of the Framers’ deliberate choice of nationalism over parochialism must be carried to their logical conclusion in the regulation of telecommunications. We will examine three aspects of modern telecommunications and entertainment networks that now compete intermodally with one another yet are in different

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235. *Powell Stresses Need For Regulatory Restraint at FCC*, WARREN’S CABLE REG. MONITOR, Feb.12, 2001, available at 2001 WLNR 5648168 (quoting FCC Chairman Michael K. Powell).

236. Implementation of Sections 3(n) & 332, *supra* note 148, at 1421.

237. *Id.* at 1509 n.532 (citation omitted). The Commission has recognized that the goal should be to “create a rational framework for the regulation of competing services that are provided via different technologies and network architectures,” and to apply “an analytical approach that is, to the extent possible, consistent across multiple platforms.” Declaratory Broadband Ruling, *supra* note 168, at 4802; *see also* Appropriate Framework for Broadband Access, *supra* note 172, at 3023 (“[T]he Commission will strive to develop an analytical framework that is consistent, to the extent possible, across multiple platforms.”) (“a functional approach, focusing on the nature of the service provided to consumers, rather than one that focuses on the technical attributes of the underlying architecture”).

238. Implementation of Sections 3(n) & 332, *supra* note 148, at 1455.

239. *H.P. Hood & Sons*, 336 U.S. at 538.

evolutionary stages of deregulation. The principal justifications for continued state-by-state—or worse, town-by-town—regulation in these areas are in fundamental conflict with the principles that animate the Commerce Clause.

First, we will examine traditional local wireline telephony, where the federal government has terminated local monopolies but which otherwise remains subject to significant (and inefficient) state-by-state regulation. Second, we will look at certain aspects of wireless cell phone networks, where there has been federal preemptive price deregulation but which is still plagued by recalcitrant state regulation in the form of purported consumer-protection regimes that trench upon federal prerogatives and interfere with market forces. Finally, we will examine the video programming market, where Congress has outlawed cable monopoly franchises but has left the implementation of this supposedly more competitive regime to local franchising authorities (“LFAs”) that are not the most enthusiastic partners in the federal deregulatory process, and whose continued role suppresses intermodal competition to the detriment of consumers.

Both of the latter two situations are examples of the natural hydraulic pressure of state and local governments to resist federal deregulation. State regulatory power, like water, is not compressible: if the state authorities are not entirely displaced by preemptive federal deregulation, their natural tendency is to reassert their lost regulatory power over rate-setting and market entry in other ways, such as under the guise of consumer protection or through the assertion of local control over rights-of-way.

*A. The Case for Exclusive Federal Regulation (and Then Deregulation) of Local Wireline Telephony*

The Telecommunications Act of 1996 fatally undermined any remaining rationale for continued state regulation of wireline telephony by terminating the states’ exclusive jurisdiction over intrastate telephony and eliminating the monopoly franchises conferred by states on local carriers.<sup>240</sup> The 1996 Act’s division of regulatory authority constituted a shift of seismic magnitude in the balance of power between state and federal regulators. The FCC’s Chairman at the time put it bluntly, remarking that the 1996 Act threw the states’ traditional intrastate authority into “the trash can of history.”<sup>241</sup> Thus it is undeniable that

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240. See 47 U.S.C. §§ 251-252. These sections require incumbent local exchange carriers (“ILECs”)—the old local telephone monopolies—to interconnect with and to assist new competitive entrants to the market.

241. *Hundt Looks Toward ‘Radical’ Overhaul of Regulatory Regimes*, TELECOMM.

“[t]he 1996 Act move[d] beyond the distinction between interstate and intrastate matters that was established in the 1934 Act.”<sup>242</sup> In the 1996 Act, Congress not only ratified and extended federal deregulation of wireless and data services,<sup>243</sup> it also preempted state laws that had imposed exclusive local telephone franchises.<sup>244</sup> That single change made possible the rapid rise in facilities-based *wireline* competition in the market for local telephone service in the decade since.

This is confirmed by the dramatic results that accompanied preemptive federal regulation of wireline entry: Competing wireline carriers deployed local networks that quickly grew to serve more than 20 million customer lines throughout the country. Total CLEC market share had grown to 15 percent as early as June 2003.<sup>245</sup> Competing carriers deployed more than 200,000 route miles of fiber optic cable and have installed more than 3,000 switches (1,300 circuit switches and 1,700 packet switches).<sup>246</sup> Competitors operate at least 1,800 networks in more than 900 U.S. cities.<sup>247</sup> The CLEC presence in the market for business telephony became especially strong: FCC surveys as long ago as June 2003 revealed that CLECs had already captured 23 percent of U.S. business lines and more than 40 percent in denser business centers.<sup>248</sup>

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REP., July 15, 1996, available at 1996 WLNR 6141663; see also Implementation of the Local Competition Provisions in the Telecomms. Act of 1996, *First Report & Order*, 11 FCC Rcd. 15,499, 15,559-60 (1996) [hereinafter *Local Competition Order*], modified on recon., 11 FCC Rcd. 13,042 (1996), vacated in part, *Iowa Utils. Bd. v. F.C.C.*, 120 F.3d 753 (8th Cir. 1997), rev'd sub nom. *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366 (1999).

242. *Local Competition Order*, supra note 241, at ¶ 24. The FCC's sweeping new authority was confirmed in *AT&T Corp.*, 525 U.S. at 378 n.6, decision on remand, *Iowa Utils. Bd. v. F.C.C.*, 219 F.3d 744 (8th Cir. 2000), aff'd in part, rev'd in part sub nom. *Verizon Commc'ns, Inc. v. F.C.C.*, 535 U.S. 467 (2002).

243. See 47 U.S.C. § 271(b)(3), (g)(3) (permitting Bell operating companies to provide “incidental interLATA services” which includes “commercial mobile services”); § 230(a)(4), (b)(2) (the Internet and like services “have flourished, to the benefit of all Americans, with a minimum of government regulation;” vowing to uphold the competitive free-market for such services “unfettered by Federal or State regulation”); § 157 (the FCC and the state commissions are required to “encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans”); § 160 (granting forbearance to enhance competition among providers of telecommunications services).

244. See § 253. Some state regulation of entry into the wireline market remains; for example, a CLEC must still obtain a certificate from the state public utility commission before it can provide service.

245. *2004 Competition Hearings*, supra note 163, at 14 (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.).

246. NEW PARADIGM RESOURCES GROUP, CLEC REPORT 2003 Ch. 2, tbl. 6 (17th ed. 2003), available at [http://newparadigmresourcesgroup.ecnext.com/coms2/gi\\_0267-821/CLEC-Report-2003-17th-Edition.html](http://newparadigmresourcesgroup.ecnext.com/coms2/gi_0267-821/CLEC-Report-2003-17th-Edition.html); TELCORDIA TECHS., LOCAL EXCHANGE ROUTING GUIDE (2002).

247. See NEW PARADIGM RESOURCES GROUP, CLEC REPORT 2002 Ch. 6 (15th ed. 2001).

248. *2004 Competition Hearings*, supra note 163, at 11 (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.).

They had established direct connections to more than 30,000 of the largest commercial office buildings.<sup>249</sup>

None of this would have happened if total state-by-state regulation of wireline competition had continued. Congress federalized this area of the law for the same reasons it federalized regulation of the wireless industry: because it was inherently a national network industry, and because the states were imposing rate regulation that was unwise and counterproductive.

Moreover, any attempt to justify continued state-by-state wireline regulation in today's "rapidly evolving market structure"<sup>250</sup> must also consider the increasingly intense competition from other technologies such as wireless telephony and VoIP. The Commission concluded that even *impending* competition dramatically reduces the risk of abuse of market power by incumbent players.<sup>251</sup> The 1996 Act has put enormous pressure on the established incumbent companies and the interexchange companies.<sup>252</sup> Putting aside the issue of whether the unbundling requirements ushered in by the 1996 Act ever promoted genuine facilities-based wireline competition by CLECs, rather than mere regulatory arbitrage, there is a growing consensus that the 1996 Act is deterring investment by ILECs in the broadband sector that is the wave of the future.<sup>253</sup>

Although the 1996 Act commenced federal regulation of local wireline telephony by preempting state regulation of entry into the local market, it left the interpretation and implementation of that new policy to the myriad idiosyncratic, parochial judgments of the states. The market structure and technological environment on which the regulatory model of the 1996 Act was predicated is now a decade out of date. As previously noted, the number of cell phone subscribers has multiplied five-fold in the last decade, and wireless voice revenues have surpassed

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249. See Joint Comments of Allegiance Telecom, Inc. & Focal Commc'ns Corp. in Implementation of the Local Competition Provisions of the Telecomms. Act of 1996, CC Dkt. No. 96-98, at 25 (June 11, 2001), available at [http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native\\_or\\_pdf=pdf&id\\_document=6512569121](http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6512569121); Comments of WorldCom, Inc., in Implementation of the Local Competition Provisions of the Telecomms. Act of 1996, CC Dkt. No. 96-98, at 7 (June 11, 2001), available at [http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native\\_or\\_pdf=pdf&id\\_document=6512660123](http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6512660123).

250. *Conn. Dep't of Pub. Util. Control*, 78 F.3d at 850 & n.7 (citation and quotation marks omitted) (upholding FCC decision refusing to let state regulate cellular phones and ruling that FCC was correct to consider the alleged need for state regulation in the context of a "forward looking perspective" and the state of "imminent future competition" in the market).

251. Implementation of Sections 3(n) & 332, *supra* note 148, at ¶¶ 148, 174-75.

252. *2004 Competition Hearings*, *supra* note 163, at 32 (statement of Ned P. Zachar, Dir. of Telecom Servs. Research, Lever House).

253. See, e.g., *2004 Competition Hearings*, *supra* note 163, at 12-13 (statement of Michael J. Balhoff, Managing Dir., Legg Mason Inc.).

wireline voice revenues. High-speed data access was in its infancy in 1996. Today, however, broadband is available in all fifty states, the District of Columbia, and Puerto Rico, as well as in Guam, American Samoa, and other Pacific islands.<sup>254</sup> Neither wireless nor VoIP was even a prospect for intermodal competition for wireline when the 1996 Act was drafted.<sup>255</sup>

The profoundly intermodal nature of competition within the contemporary telecommunications market confirms the case for preemptive federal regulation of wireline. When the Commission preempted state regulation of Vonage's DigitalVoice service in late 2004,<sup>256</sup> it did so despite its concession that DigitalVoice, with such familiar enhancements as voicemail and three-way calling, undeniably "resembles the [wireline] telephone service provided by the circuit-switched network" that the states were still permitted to regulate.<sup>257</sup> Yet, the Commission reasoned, there remained several "fundamental differences" between traditional circuit-switched wireline service and packet-switched VoIP that justified continued state-by-state regulation of the former but preemptive federal regulation of the latter.<sup>258</sup> The first difference noted by the Commission was that VoIP telephone service "is fully portable; customers may use the service anywhere in the world where they can find a broadband connection to the Internet."<sup>259</sup> Unlike wireline service, where the phone number that one dials directs one's call exclusively to a particular geographic location from another specific and identifiable location, a VoIP subscriber can be anywhere on the planet when he makes or receives a call.<sup>260</sup>

Yet much of the same geographic indeterminacy exists with respect to wireline telephony: a wireline call made to a mobile telephone subscriber does not terminate at any predetermined location—it terminates wherever the mobile phone subscriber happens to be at that moment. Even a wireline call made to a wireline number does not terminate at a point certain, insofar as: (1) the recipient may have the incoming call set up to be forwarded to another wireline number located

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254. See FCC, WIRELINE COMPETITION BUREAU, HIGH-SPEED SERVICES FOR INTERNET ACCESS: STATUS AS OF DECEMBER 31, 2005 3 (2006), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-266596A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-266596A1.pdf).

255. WARREN'S CABLE REGULATION MONITOR, *supra* note 235 ("We increasingly are stretched by the fact that our statute and our regulatory structure are balkanized, built upon technological assumptions and the underlying technologies that form them as well as the business models that were originally generated.") (quoting FCC Chairman Powell).

256. VoIP Order, *supra* note 183.

257. *Id.* ¶ 4.

258. *Id.*

259. *Id.* ¶ 5; see also *id.* ¶ 9.

260. The FCC found the same significance in portability in its ruling preemptively deregulating FWD service in its *Pulver* decision. See *Pulver*, *supra* note 106.

anywhere in the world, or even to a cellular number then in motion somewhere; or (2) the wireline call may terminate at a call-announcement or voicemail server located far from the wireline number's assigned geographic location, and then be answered, retrieved, or returned from a different, remote, and possibly mobile location.<sup>261</sup> It appears that the Commission made its comparisons to traditional wireline telephony without focusing on the fact—unnecessary to the inquiry in which it was engaged—that “traditional” wireline has long since been augmented by a wealth of enhanced features interconnected with other modes of telecommunications.

It therefore comes as little surprise that, elsewhere in its VoIP Order, the FCC disavowed reliance on VoIP's “portability” to jurisdictionally distinguish it from wireline. The “geographical location of the end user at any particular time is only one clue to a jurisdictional finding” of whether the telephone communication in question is inter- or intrastate.<sup>262</sup> Even if Vonage could identify the geographic location of a VoIP subscriber, the suite of telecommunications services provided by Vonage “is far too multifaceted for simple identification of the user's location to indicate [federal or state] jurisdiction.”<sup>263</sup> Much the same can be said for modern wireline telephony.

Rather than focusing on VoIP's portability, the FCC squarely predicated its holding of exclusive federal regulatory jurisdiction on two characteristics of VoIP that are also exhibited by modern wireline telephony. First, the centralized nature of the VoIP network and its facilities “preclude any practical identification of, and separation into, interstate and intrastate communications for purposes of effectuating a dual federal/state regulatory scheme.”<sup>264</sup> State-by-state regulation of an

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261. Thus much of the geographic indeterminacy and fluidity that the FCC perceives in VoIP, VoIP Order, *supra* note 183, at ¶ 27, likewise exists with respect to modern wireline, especially when wireline is properly understood as merely one component of a seamless national network employing multiple modes of telecommunications and driven by intermodal competition. The FCC also distinguished VoIP from wireline by emphasizing that the former offers a “suite of integrated capabilities and features that allows the user to manage personal communications dynamically,” including such features as “voicemail, three-way calling, online account and voicemail management,” and similar “integrated features and capabilities [that] allow customers to control their communications needs by determining for themselves how, when, and where communications will be sent, received, saved, stored, forwarded and organized.” *Id.* ¶¶ 7-8. As explained above, a number of similar features are available in some form under the AIN services now offered by wireline providers.

262. *Id.* ¶ 25.

263. *Id.* ¶ 23.

264. *Id.* ¶ 14. Ultimately, the immateriality of the “portability” feature and the independent decisiveness of the inherently interstate nature of the VoIP network were confirmed by the fact that the Commission concluded that, to decide between state and federal jurisdiction for VoIP, it did not even have to determine whether VoIP was an “information service” or a “telecommunications service.” *Id.* ¶ 14 & n.46. The irrelevance of that once-vital



inherently national network would simply “thwart federal law and policy.”<sup>265</sup> The Commission accepted that the centralized VoIP:

[N]etwork design . . . permits providers to offer a single, integrated service that includes both local and long distance calling and a host of other features that can be supported from national or regional data centers and accessed by users across state lines. . . . In addition to call setup, these functions include generation of call announcements, record-keeping, CALEA, voicemail and other features such as \*67, conferencing and call waiting. . . . [T]here are no facilities at the local level of a managed voice over IP network that can perform these functions.<sup>266</sup>

As demonstrated above, the facilities used to provide modern, feature-laden wireline services are also centralized and multi-state in nature.

With respect to VoIP, the Commission ruled that the inherently interstate, centralized network could not be dissected into separate regulatory jurisdictions along state lines because it “form[ed] an integrated communications service *designed to overcome geography, not track it.*”<sup>267</sup> Indeed, even with respect to wireline telephony and its traditional “end-to-end” jurisdictional analysis, the Commission noted that its purported segregation of “jurisdictionally mixed” telephone facilities into discrete interstate and intrastate “components” and “services” was becoming more and more arbitrary—if not wholly illusory.<sup>268</sup> The mere “fact that a particular service enables communication within a state does not necessarily subject it to state economic regulation,”<sup>269</sup> “because the points among which” the cable modem traffic “travel[s] are often in different states and countries.”<sup>270</sup> Such communications are inherently interstate and therefore subject to exclusive federal jurisdiction. That reasoning applies no less to wireline than to VoIP.

The second feature of VoIP that required preemptive federal

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issue of statutory classification reflects the disintegration of the traditional taxonomy of telecommunications and the convergence of telephony with all other forms of data transmission. Voice is now but one application of data transmission, and regardless of how one classifies VoIP, the problem is that state-by-state regulation of it would conflict with the Commission’s “pro-competitive deregulatory rules and policies.” *Id.* ¶ 20 & n.69; *see also id.* ¶¶ 20-21 & n.78.

265. *Id.* ¶ 14.

266. *Id.* ¶ 32 n.113 (citation omitted).

267. VoIP Order, *supra* note 183, at ¶ 25 (emphasis added).

268. *See id.* ¶¶ 17-19 & n.65.

269. *Id.* ¶ 22.

270. *Id.* n.85 (citing Declaratory Broadband Ruling, *supra* note 168, at ¶ 59); *see also id.* ¶ 22.

regulation was the Commission's concern that "multiple state regulatory regimes would likely violate the Commerce Clause because of the unavoidable effect that regulation on an intrastate component would have on interstate use of this service . . . within other states."<sup>271</sup> A state law that "has the 'practical effect' of regulating commerce occurring wholly outside that [s]tate's borders" is a violation of the Commerce Clause.<sup>272</sup> When a telecommunications network's facilities serve multiple states—as do both Internet-based VoIP and, as explained above, modern wireline networks—a given state's regulation of facilities used moment-to-moment for both *intrastate* (to whatever extent the term retains semantic content) and *interstate* communications necessarily has extraterritorial effect. When a key wireline hub is located in Rhode Island, for example, an attempt by Massachusetts to regulate that facility's operational role in intrastate Massachusetts telephony would violate the Commerce Clause.

As the FCC noted in *Vonage*, "state regulation of those aspects of commerce that by their unique nature demand cohesive national treatment is offensive to the Commerce Clause."<sup>273</sup>

[And] while states can and should serve as laboratories for different regulatory approaches, we have here a very different situation because of the nature of the service – our federal system does not allow the strictest regulatory predilections of a single state to crowd out the policies of all others for a service that unavoidably reaches all of them.<sup>274</sup>

As explained above, this is the rationale for exclusive federal regulation of national network industries, and it is noteworthy that the Commission relied upon the highly successful, preemptive federal regulation of both trucking and railroads in support of its decision to displace state-by-state regulation of VoIP.<sup>275</sup>

The Constitution's Framers adopted the Commerce Clause precisely because they recognized the hydraulic political pressure on state regulators to promote local interests at the expense of the nation as a whole. It therefore should come as no surprise that state regulators often chafe under even the 1996 Act's limited restriction on their authority. Some state and local authorities have threatened to regulate service quality or even to require wireline carriers to obtain a local franchise in order to provide broadband service. For example, California regulators

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271. *Id.* ¶ 14.

272. *Healy v. Beer Inst.*, 491 U.S. 324, 332 (1989).

273. VoIP Order, *supra* note 183, at ¶ 38 (citations omitted).

274. *Id.* ¶ 39.

275. *Id.* ¶ 41 n.144 (discussing "network-based industries").

ruled in 2004 that the high-frequency portion of the loop must be offered to competitors by ILECs on an unbundled basis, despite the FCC's contrary determination in the *Triennial Review Order*.<sup>276</sup> Yet in 2006, the same state regulators relaxed pricing restrictions on the basis of their newfound faith in “market forces”; the pricing power of ILECs:

[I]s sufficiently checked by . . . the realistic threat of entry by carriers in any market using [unbundled loops] and the widespread competition offered by wireless, cable, and VoIP providers. These market conditions lead us to conclude that we should rely on market forces. . . .

In a fast-moving technology space like telecommunications, there is no public interest in maintaining an outmoded tariffing procedure that requires the burdensome regulatory review of cost data and delays the provision of services (particularly new or less expensive ones) to customers.<sup>277</sup>

Some state and local authorities also continue to retard the deployment of broadband transmission facilities by their imposition of onerous information collection requirements, ponderous processing routines, and unreasonable fees on ILECs seeking access to public rights-of-way to lay new wire and fiber-optic cables. The issue of local control over access to, and construction on or under, rights of way is naturally among the local authorities' favorite objections to preemptive federal regulation of wireline. Of course, states and municipalities of course have an essential role in regulating access to, and construction on and under, their own streets and sidewalks. Nobody has suggested otherwise, and nothing in the preemptive federalization of wireline regulation would impair that important local responsibility any more than federal preemption of broadband regulation by state or local authorities has given cable companies or other Internet service providers carte blanche to dig up streets as they wish. However, local control over such access cannot be allowed to become a burdensome chokehold on the deployment of the next generation of broadband networks that holds such promise for all Americans. “[T]he state may not use its admitted

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276. See Rulemaking on the Commission's Own Motion to Govern Open Access to Bottleneck Servs. & Establish a Framework for Network Architecture Dev. of Dominant Carrier Network, *Opinion Granting Motion to Vacate Stay in Decision*, Cal. PUC D. 04-05-022 (2004), available at [http://docs.cpuc.ca.gov/word\\_pdf/FINAL\\_DECISION/36390.pdf](http://docs.cpuc.ca.gov/word_pdf/FINAL_DECISION/36390.pdf).

277. Order Instituting Rulemaking on the Commission's Own Motion to Assess & Revise the Regulation of Telecomms. Utils., *Opinion on Rulemaking*, Cal. PUC D. 06-08-030, at 182-183 (2006), available at [http://docs.cpuc.ca.gov/word\\_pdf/Final\\_decision/59388.pdf](http://docs.cpuc.ca.gov/word_pdf/Final_decision/59388.pdf).

powers to protect the health and safety of its people as a basis for suppressing competition.”<sup>278</sup>

The remaining rationale for state-by-state regulation of wireline is the need to guarantee universal 9-1-1 emergency service. But that consideration cuts in favor of *federal*, not state, regulation. Universal 9-1-1 service—the assurance that dialing those three digits anywhere in the nation, by any form of telephony, will summon emergency help—is best promoted by *uniform national* regulation. The FCC is best situated—with respect both to its national jurisdiction and its superior staff resources and technical expertise—to regulate 9-1-1 service provided not only by wireless and VoIP technologies, but by wireline as well.

In short, there is simply no good reason for the nation to stumble on with the legacy of state-by-state regulation of wireline telephony. In contrast, the rationales—legal, economic, and practical—favoring preemptive federal regulation (and eventual deregulation) of wireline are compelling. State-by-state regulation imposes unnecessary costs that stifle innovation and growth.

First, lack of regulatory uniformity in a market where capital investment is intensive and costs are high “reduces product experimentation, restricts investment, and raises costs.”<sup>279</sup> When the FCC deregulated cable modem service, it found that “a patchwork of State and local regulations beyond matters of purely local concern” would “result[] in inconsistent requirements” affecting “service” and “technical design” of facilities, and in “business arrangements that discouraged” deployment of service “across political boundaries.”<sup>280</sup> Precisely the same is true with respect to local telephony.

Second, state-by-state regulation fosters uncertainty and instability. Regulated companies have not one but 50 different regulatory bodies to anticipate and work with. In preemptively deregulating other telecommunications markets, the Commission has stressed the importance of “remov[ing] regulatory uncertainty that may discourage investment and innovation,”<sup>281</sup> and of “establishing a stable, predictable regulatory environment that facilitates prudent business planning.”<sup>282</sup> In addition, these state regulatory bodies are rarely as well-funded and as

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278. *H.P. Hood & Sons*, 336 U.S. at 538.

279. Hazlett, *supra* note 55, at 192.

280. Declaratory Broadband Ruling, *supra* note 168, at ¶ 97.

281. *Id.* ¶ 97 (deregulating cable modem service); *see also id.* ¶ 99 (declaring aversion to an “unpredictable regulatory environment”).

282. Conn. Petition, *supra* note 150, at ¶ 10 (refusing state petition to regulate cellular telephones); *see also* Pulver, *supra* note 106, at ¶ 1 (preemptively deregulating Free World Dialup Internet telephony in order to “remove any regulatory uncertainty” and to “bring a measure of regulatory stability to the marketplace”).

technically knowledgeable as federal regulators.<sup>283</sup> They are, more importantly, *institutionally* incompetent to regulate a *national* communications network simply because they will never have the necessary national perspective. Indeed, in a recent decision in which the D.C. Circuit overturned an FCC decision delegating to state regulators discretion under the 1996 Act to define geographic markets for “unbundling” purposes, the court observed that state regulators could not be entrusted with implementing federal telecommunications policy because they lacked the necessary “national vision and perspective.”<sup>284</sup> Like the fabled “blind men of Indostan,” who offered conflicting descriptions of an elephant after individually feeling different parts of the animal, state regulators in touch with only those parts of the interstate telephone network that are within their reach are doomed to reach incomplete and often inconsistent conclusions based on their own parochial interests.<sup>285</sup>

State regulators answer only to local constituencies, but when they regulate national networks, their regulations affect network users and providers in other states. This is unavoidable, because modern interstate telephone networks involve “economies of scale [that] extend across states.”<sup>286</sup> As previously discussed, each of the three remaining ILECs defies state boundaries in three respects: (1) their facilities are centralized and serve multiple states; (2) none has operations confined to a single state; and (3) each has an operational “footprint” that bears no resemblance to political boundaries.

Perhaps the most fundamental problem with continued state regulation of wireline is the familiar phenomenon of externalities. Judge McConnell has noted, with respect to both political and economic theory, such “[e]xternalities present the principal countervailing consideration in favor of centralized government.”<sup>287</sup> When they impose regulatory burdens on their own local portion of a national telephone

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283. Hazlett, *supra* note 55, at 175.

284. *United States Telecomm. Ass'n*, 359 F.3d at 566 (citation and quotation marks omitted).

285. See John Godfrey Saxe, *The Blind Men and the Elephant*, in 1 THE HOME BOOK OF VERSE 1877-79 (Burton E. Stevenson ed., 9th ed. 1953). In the poem, six blind men, each examining a different part of an elephant such as its ear, trunk, flank, tusk, leg or tail, variously concluded that the elephant was like a fan, a snake, a wall, a spear, a tree, or a rope.

286. Hazlett, *supra* note 55, at 176 (when “economies of scale stretch beyond state borders . . . decentralized regulations lack effective feedback”); *id.* (“[W]hen economies of scale extend across states . . . the highly complementary nature of supplying consumers in multiple political jurisdictions produces costs and benefits which may largely go unnoticed by regulatory authorities.”).

287. Michael W. McConnell, *Federalism: Evaluating the Founders' Design*, 54 U. CHI. L. REV. 1484, 1495 (1987).

network that is a sprawling, indivisible, “single integrated system,”<sup>288</sup> state regulators are in no position even to see, much less to weigh, the competing costs and benefits that their acts generate throughout that integrated system. As the FCC’s former Chief Economist, Thomas Hazlett, has noted: “The problem is not that ripple effects occur, but that state regulators have no reason to take into account what ripples across state borders. States can overconsume regulation by dumping costs on others, or they can underconsume because benefits are too widely distributed.”<sup>289</sup> Hazlett further explains:

[B]ecause the cost of rules falls, at least in part, on consumers [i]n other states, regulators will tend to ignore some of the costs they impose. The latter effect allows regulators to free-ride; indeed, political constraints push them to do so, as electoral power is undermined by focusing on outside interests at the expense of constituents.<sup>290</sup>

In sum, state-by-state regulation is fundamentally incompatible with modern wireline telephony because wireline providers are not organized or operated state-by-state. They are national businesses employing centralized network facilities and operating on multi-state economies of scale. When a dozen or more states all impose requirements on the operation of such centralized network facilities, all the vices associated with externalities—regulatory spillovers, free-rider problems, conflicting rules, and grotesque inefficiencies—are assured. This is why the Framers of the Constitution provided a Commerce Clause and a predicate for uniform, preemptive federal regulation of

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288. *La. Pub. Serv. Comm’n v. F.C.C.*, 476 U.S. 355, 375 (1986).

289. Hazlett, *supra* note 55, at 181.

290. *Id.* at 205.

In markets where economies of scale or scope are important, it is possible for decentralized policy makers to effectively free-ride on investments undertaken by consumers in other jurisdictions. This occurs when a system is built to serve a large regional or national market, and state or local policy makers impose expensive regulations over a subset of that system. These regulations impose a tax, which may or may not be efficient for local consumers. Given that costs and/or benefits spill over to other jurisdictions, effects of local regulatory decisions will likely escape the attention of policymakers. The pressing issue in considering optimal jurisdiction is that with decentralized authority there will be important implications for consumers in other jurisdictions, and that these costs and benefits are not likely to be accounted for by policymakers. Analogous to a ‘race to the bottom,’ state regulators search for rules that will bestow benefits locally while shifting costs to network investments that enable local benefits to be subsidized by users elsewhere.

*Id.* at 180; *see also id.* at 205 (“Where large interstate networks are involved, however, spillovers occur and regulations are easier to harmonize at the federal, rather than at the state, level.”).

interstate commerce. The time is now ripe for preemptive federal regulation of wireline telephony.

*B. The Problems Created by Vestigial State-by-State Regulation of Wireless Communications*

As discussed above, mobile phone service has been primarily subject to federal regulation since its inception due to the nationalization of the radio spectrum in 1927 and the 1982 and 1993 amendments to the 1934 Act that expressly preserved exclusive federal authority over the two most important features of wireless regulation—rate-setting and market entry.<sup>291</sup> Within these two sub-divisions of the regulatory landscape, Congress has essentially occupied the field and displaced state authority.<sup>292</sup> Yet, the same 1993 amendment nevertheless failed to expressly preempt power over “other terms and conditions” of wireless phone service,<sup>293</sup> which a House Report elaborated as including “such matters as customer billing information and practices and billing disputes and other consumer protection matters; facilities siting issues (e.g., zoning); transfers of control; [and] the bundling of services and equipment.”<sup>294</sup>

Unsurprisingly, state regulators have resisted these limits on their power and have pushed back with sometimes aggressive assertions (and expansive interpretations) of their traditional police powers over consumer protection.<sup>295</sup> That is unproblematic and entirely consistent with the 1993 Act—so long as the state’s efforts, however they are labeled, do not amount to regulation of rates or of the terms of market entry. Consider the Eighth Circuit’s recent decision in *Cellco P’ship v. Hatch*.<sup>296</sup> Minnesota enacted a “Wireless Consumer Protection” statute that required cell phone companies to obtain affirmative consent from their subscribers prior to any proposed change in rates, with a 60-day notice requirement, even if the subscriber’s current contract provided for rate increases to take effect unless the subscriber, after due notice,

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291. See Communications Act of 1934 § 332 (codified as amended at 47 U.S.C. § 332(c)(3)(A)).

292. See *Cellco P’ship v. Hatch*, 431 F.3d 1077, 1081-82 (8th Cir. 2005); *Fedor v. Cingular Wireless Corp.*, 355 F.3d 1069, 1072-73 (7th Cir. 2004); *Bastien v. AT&T Wireless Servs., Inc.*, 205 F.3d 983, 987 (7th Cir. 2000).

293. See Omnibus Reconciliation Act of 1993 § 6002, Pub. L. No. 103-66, 107 Stat. 312, 394 (codified as amended at 47 U.S.C. § 332).

294. H.R. REP. NO. 103-111, at 261 (1993), as reprinted in 1993 U.S.C.C.A.N. 378, 588.

295. See, e.g., *Cellco P’ship*, 431 F.3d at 1082-83. States may also, of course, regulate wireless consumer protection issues not just by administrative action by state utility or public service commissions but also by way of state law contract, fraud, consumer protection, and deceptive trade practice claims brought in state courts. See, e.g., *Fedor*, 355 F.3d at 1072-73.

296. 431 F.3d 1077.

affirmatively objected. The Court of Appeals ruled that the statute was impermissible state regulation of mobile phone rates:

This statute effectively voids the terms of contracts currently used by providers in one industry and substitutes by statute a different contractual arrangement. The existing contracts exemplify an “opt-out” structure – that is, they permit the providers to effect rate increases upon reasonable notice to the customer, whose continued use of the service binds him to the new rate unless he affirmatively declines to accept the changes. [Whereas the new law] mandates an “opt-in” contract structure: the provider cannot increase rates unless the customer affirmatively accepts the changes.<sup>297</sup>

The notification period thus effectively froze rates for two months, and fixed rates for any customer who declined to opt-in to a provider’s proposed rate increase for the remaining term of that customer’s “existing contract, often one or two years.”<sup>298</sup>

The State of Minnesota, as might be expected, claimed that this regulatory power over the other “terms of and conditions” of cellular service contracts had been preserved by Congress with its express enumeration of continued state authority in “consumer protection matters.”<sup>299</sup> The Court of Appeals correctly recognized that this argument proved too much:

We find this argument overbroad, and we are not persuaded. Any measure that benefits consumers, including legislation that restricts rate increases, can be said in some sense to serve as a “consumer protection measure,” but a benefit to consumers, standing alone, is plainly not sufficient to place a state regulation on the permissible side of the federal/state regulatory line drawn by § 332(c)(3)(A). To avoid subsuming the regulation of rates within the governance of “terms and conditions,” the meaning of “consumer protection” in this context must exclude regulatory measures, such as [Minnesota’s], that directly impact the rates charged by providers.<sup>300</sup>

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297. *Id.* at 1083.

298. *Id.* at 1082.

299. *Id.* (quoting the House Budget Committee Report).

300. *Id.* at 1082-83 (emphasis added). In contrast, consider *Nat’l Ass’n of State Util. Consumer Advocates v. F.C.C.*, 457 F.3d 1238 (11th Cir. 2006), where the Eleventh Circuit overturned a Commission order “that preempted the states from requiring or prohibiting the use of line items in customer billing for cellular wireless services.” *Nat’l Ass’n of State Util. Consumer Advocates*, 457 F.3d at 1241. The FCC argued that “[e]fforts by individual states to regulate [wireless services providers’] rates through line item requirements . . . would be inconsistent with the federal policy of a uniform, national and deregulatory framework of the Communications Act.” *Id.* at 1253 (brackets and ellipsis by the court) (quoting the FCC order). “According to the Commission, section 332(c)(3)(A) prohibits the state regulation of



Given that state regulators can be expected to wave the “consumer protection” flag in defense of any proposal to regain jurisdiction over the cell phone industry, it is worth remembering that consumer protection is by no means an exclusively state responsibility—it becomes more properly a federal concern when the industry being regulated operates across state lines. The production and transportation of meat, milk and poultry were, once upon a time, regulated only by the states and even by local health inspection boards. However, when refrigeration and more rapid transport transformed those industries into national operations, much, if not all, of the regulatory responsibility shifted to the federal Department of Agriculture and the Food and Drug Administration. And both consumers and the industry were undeniably the better for it.

The same jurisdictional shift is even more pronounced—and even more appropriate—when the object of regulation is consumer protection within a network industry whose network has expanded across state boundaries, as discussed above. Only the federal government, not the multitude of states, could effectively and efficiently protect consumers from the predations of providers of interstate bus, rail and airline services. Telephony is likewise an interstate network phenomenon and consumer protection on a state-by-state basis may be both wholly inadequate for consumers and unduly burdensome for providers. The success of the “National Do Not Call” list (rather than 50 different state lists) to spare telephone subscribers irritation from intrusive telemarketers provides a perfect example of how national regulation often benefits both industry and consumers. The FCC is fully aware of its consumer protection responsibilities and is even now in the midst of a rulemaking process designed to generate regulations protecting cell phone subscribers from billing abuses.<sup>301</sup> Furthermore, the 1934 Act itself imposes a substantive duty on providers to charge reasonable rates and specifically

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‘rate structures’ and ‘rate levels,’” yet state regulation of billing formats “directly intrudes upon the carrier’s ability to set rates and establish rate structures.” *Id.* at 1254 (quoting the FCC order). The Court of Appeals rejected this argument out of hand: “The prohibition or requirement of a line item affects the presentation of the charge on the user’s bill, but it does not affect the amount that a user is charged for service.” *Id.*

301. See Truth-in-Billing & Billing Format, *Second Report & Order, Declaratory Ruling, and Second Further Notice of Proposed Rulemaking*, 20 FCC Rcd. 6448, 6475-76 (2005) (“[W]e tentatively conclude that the line between the Commission’s jurisdiction and states’ jurisdiction over carriers’ billing practices is properly drawn to where states only may enforce their own generally applicable contractual and consumer protection laws, albeit as they apply to carriers’ billing practices.”). The Eighth Circuit took the same approach in its decision in *Cellco P’ship*, 431 F.3d at 1080-82 & n.2. But see *Nat’l Ass’n of State Util. Consumer Advocates*, 457 F.3d at 1254 (vacating FCC order that had preempted states from requiring or prohibiting use of line items in customer billing for cellular phone service and holding that the “prohibition or requirement of a line item affects the presentation of the charge on the user’s bill, but it does not affect the amount that a user is charged for service”).

provides aggrieved customers with a right either to apply to the FCC to investigate or to bring a claim in federal court.<sup>302</sup>

States can also be expected to assert their traditional state (and even local) zoning prerogatives to control the location of wireless telephone towers and other facilities. But again, great care must be taken to scrutinize the state claim of jurisdiction carefully, both to ferret out subterfuges by state regulators annoyed by their loss of authority and trying to regulate rates or competition indirectly, and to fend off even well-intended state zoning regulations that would intrude on the federal government's exclusive authority over rates and market entry. For example, no federal preemption was found in *MetroPCS, Inc. v. San Francisco*,<sup>303</sup> because the zoning board's denial of a cell provider's application to locate cell towers in a particular area was non-discriminatory and did not effectively prohibit wireless service. And the House Report, after all, included "facilities siting issues (e.g., zoning)" on its list of "terms and conditions" that the states may continue to regulate.<sup>304</sup>

But in *Bastien v. AT&T Wireless Serv., Inc.*,<sup>305</sup> the Seventh Circuit correctly recognized that the private plaintiff's state law breach-of-contract and consumer fraud claims against AT&T, which alleged that the provider had signed up customers without first building an adequate number of towers to provide reliable service, were preempted because they would impermissibly "tread directly on the very areas reserved to the FCC: the modes and conditions under which AT&T Wireless may begin offering services in the Chicago market."<sup>306</sup> The FCC, not state courts or regulators, "is responsible for determining the number, placement and operation of cellular towers and other infrastructure [required for market entry], as well as the rates and conditions that could be offered for the new service."<sup>307</sup>

The lesson is that neither state public service commissions nor state courts should be allowed to employ either "consumer protection" or "zoning" considerations as a shield against the federal government's preemptive regulation—and, in significant part, its preemptive *deregulation*—of wireless telephony. Nor does the risk to exclusive federal regulation of mobile telephones lie only in the machinations of

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302. See Communications Act of 1934 §§ 201(b), 207 (codified as amended at 47 U.S.C. §§ 201, 207).

303. 400 F.3d 715, 735 (9th Cir. 2005).

304. H.R. REP. NO. 103-111, at 261 (1993), as reprinted in 1993 U.S.C.C.A.N. 378, 588.

305. 205 F.3d 983.

306. *Id.* at 989 (plaintiff's claims "would directly alter the federal regulation of tower construction, location and coverage, and quality of service and hence rates for service").

307. *Fedor*, 355 F.3d at 1072 (reaffirming *Bastien*).

state regulators who continue to regard with a jealous eye the powers they once held. Illegitimate state encroachment on federal jurisdictional turf need not be nefarious or even intentional. State disruption of unitary federal regulation of national networks is just as harmful when it is well-intended or even unintentional. Nor should the courts or the FCC be beguiled by the defense that a state regulation challenged on preemption grounds is only a trifling incursion on uniform federal regulation. The government officials charged with responsibility for choices must recognize that even small jurisdictional encroachments are important because the cumulative result of small incremental changes—the “tyranny of small decisions”—might well be wholly alien, and profoundly objectionable, to those who acquiesce in just one small step after another.<sup>308</sup> To avoid such nibbling away at the federal jurisdiction necessary for interstate network industries, the remnants of state regulatory authority over wireless telephony must be carefully policed by the FCC and the federal courts, and Congress should seriously consider further limits on state regulatory power.

*C. Implementation of Federal Standards for Cable Television Competition by Local Franchising Authorities Impedes Intermodal Competition and Frustrates Deployment of Next-Generation Telecommunications Networks*

Section 621(a) of the 1984 Cable Act, which generally required cable operators to obtain a franchise, was amended by Congress in the 1992 Cable Act to limit the authority of local franchising authorities (“LFAs”) by outlawing monopoly cable-TV franchises. Congress provided that “a franchising authority may not grant an exclusive franchise and may not unreasonably refuse to award an additional competitive franchise.”<sup>309</sup> At least, that was what was supposed to happen. In point of fact, the Multichannel Video Programming Distribution (“MVPD”) market is still largely in the grip of the original monopoly cable companies and the marketplace continues to suffer from grossly inadequate competition. As FCC Chairman Kevin Martin recently noted, “from 1995 to 2005, cable rates have risen 93% . . . [while] [s]ince 1996 the prices of every other communications service have declined.”<sup>310</sup> Although cable has lost some market share to Direct Broadcast Satellite (“DBS”),<sup>311</sup> the first stirrings of genuine competition

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308. See Alfred E. Kahn, *The Tyranny of Small Decisions*, in *ECONOMIC THEORIES OF INTERNATIONAL POLITICS* 537 (Bruce M. Russett ed., 1968).

309. 47 U.S.C. § 541(a)(1).

310. Video Franchising Order, *supra* note 5, at 92 (statement of Chairman Kevin J. Martin), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-06-180A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-06-180A1.pdf).

311. “[F]rom 2001 to 2005, the number of cable subscribers, as a share of total MVPD

in delivery of video programming in the form of DBS television providers have done nothing to constrain cable rates,<sup>312</sup> and the MVPD marketplace is actually becoming *more* concentrated: “[T]he top four MVPDs serve 63 percent of all MVPD subscribers, up five percent from 2004.”<sup>313</sup>

Intermodal competition is once again the answer, and the future. As Commissioner Robert McDowell has put it, “[m]ore delivery platforms mean more competition.”<sup>314</sup> This time, the new market entry is by an established player in a different field—wireline telephone companies (the ILECs). The FCC observed in a 2006 report that:

[W]e are seeing wired competitors to cable trying to enter the market. The Commission should facilitate this entry, not only because it furthers video competition, but also because it promotes the deployment of the broadband networks over which the video services are provided. The widespread deployment of these networks is critical to the United States’ international competitiveness. Further, it will improve Americans’ lives through applications such as distance learning and remote medical diagnosis.<sup>315</sup>

The new fiber-optic networks being built by ILECs will substantially or completely overlay the existing circuit-switched feeder and distribution networks. For example, AT&T is building a Fiber-to-the-Node (“FTTN”) system and Verizon is building a Fiber-to-the-

subscribers, has decreased from 77 percent to 69 percent. Commensurately, DBS subscribership has increased from 18 percent to 27 percent.” Jonathan S. Adelstein, Comm’r, FCC, Statement at FCC Open Meeting in Keller, Texas on the Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, at 1 (Feb. 10, 2006) [hereinafter Keller Hearing], available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-263763A4.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-263763A4.pdf).

312. See Implementation of Section 3 of the Cable Television Consumer Prot. & Competition Act of 1992, *Report*, 21 FCC Rcd. 15087, ¶ 2 (2006) (“DBS competition, however, does not appear to constrain cable prices – average prices are the same as or slightly higher in communities where DBS was the basis for a finding of effective competition than in noncompetitive communities.”).

313. Jonathan S. Adelstein, Comm’r, FCC, Statement, Keller Hearing, *supra* note 311, at 2; FCC Issues 12<sup>th</sup> Annual Report, *supra* note 227, at 3. Following the purchase of the Adelphia cable systems by Comcast and Time Warner in July 2006, the market share for the largest MVPDs has risen even further. See Applications for Consent to the Assignment and/or Transfer of Control of Licenses, *Memorandum Opinion & Order*, 21 FCC Rcd. 8203, ¶ 2 (2006).

314. Video Franchising Order, *supra* note 5, at 108 (statement of Comm’r Robert M. McDowell).

315. Kevin J. Martin, Chairman, FCC, Statement at Keller Hearing, *supra* note 311, at 1, available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-263763A2.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-263763A2.pdf); see also Michael J. Copps, Comm’r, FCC, Statement at Keller Hearing, *supra* note 311, at 1, available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-263763A3.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-263763A3.pdf); Jonathan S. Adelstein, Comm’r, FCC, Statement, Keller Hearing, *supra* note 311, at 1.

Premises (“FTTP”) network. The improvement in broadband speed that fiber-optic technology offers is staggering. Although the service parameters are still being worked out, ILECs have already begun rolling out this service. Verizon’s FTTP customers, for example, now enjoy Internet access and data transmission speeds that are *ten to twenty times faster than anything currently available* through DSL or cable modem service.<sup>316</sup> Such lightening speed will allow FTTP customers to use a host of new real-time applications and data-rich services, including video telephony and telecommuting, HDTV-quality video, interactive video, network-based personal video recording, remote medical monitoring, and premises surveillance.

The value and promise of preemptive federal deregulation were dramatically confirmed when the FCC announced on October 22, 2004 that it would deregulate fiber-optic networks.<sup>317</sup> Specifically, the FCC ruled that the unbundling obligations of Section 271 of the 1996 Act would not be applied to fiber-to-the-home loops, to fiber-to-the-curb loops, to the packetized functionality of hybrid copper-fiber loops, or to packet switching.<sup>318</sup> The Commission noted the “presence of robust intermodal competition from cable operators”<sup>319</sup> and the need to alleviate the stifling “investment disincentives” created by the unbundling requirements.<sup>320</sup> The Commission concluded that “forbearance from these requirements will provide an increased incentive for the [ILECs] to deploy broadband services and compete with cable providers, which will in turn increase competition and benefit consumers.”<sup>321</sup> That insight was immediately borne out: as soon as the FCC voted on the unbundling petitions—indeed, even before its decision was formally released—the phone companies announced that they were dramatically accelerating their construction of all-digital, high-speed fiber-optic networks and that

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316. See Verizon, The Technology: Fiber to the Premises (FTTP), <http://newscenter.verizon.com/kit/fiber/fttp102104.html> (last visited Mar. 20, 2008)

317. See Press Release, FCC, Federal Communications Commission Further Spurs Advanced Fiber Network Deployment (Oct. 22, 2004), available at [http://fallfoss.fcc.gov/edocs\\_public/attachmatch/DOC-253492A1.pdf](http://fallfoss.fcc.gov/edocs_public/attachmatch/DOC-253492A1.pdf); see also Anne Marie Squeo, *Regional Bells Get Broadband Win*, WALL ST. J., Oct. 15, 2004, at B8.

318. See Petition for Forbearance of the Verizon Tel. Cos. Pursuant to 47 U.S.C. §160(c), *Memorandum Opinion & Order*, 19 FCC Rcd. 21,496 (2004) [hereinafter Petition for Forbearance]. The FCC’s order was upheld on appeal. See *Earthlink, Inc. v. F.C.C.*, 462 F.3d 1, 7 (D.C. Cir. 2006):

Ultimately, the FCC concluded that any short-term effects on competition are offset by the prospect of additional intermodal competition and the benefits that forbearance will provide: incentives for both ILECs and CLECs to invest in and deploy broadband facilities, which will increase competition going forward and thereby keep rates reasonable, benefit consumers, and serve the public interest.

319. Petition for Forbearance, *supra* note 318, at ¶ 23.

320. *Id.* ¶ 25.

321. *Id.* ¶ 31.

they anticipated that the number of consumers being offered such service would increase by more than 500 percent in the next year.<sup>322</sup>

The FCC quickly followed suit in 2005 with an order deregulating the more traditional wireline broadband services.<sup>323</sup> Again, the Commission stressed the arrival of vigorous intermodal competition,<sup>324</sup> the need to eliminate regulations that deter both investment and the deployment of new technologies,<sup>325</sup> and the wisdom of imposing “a consistent regulatory framework across platforms by regulating like services in a similar functional manner.”<sup>326</sup>

The Commission’s decision to free both traditional wireline broadband and the new fiber-optic broadband services from inefficient regulatory hobbles was premised on the realities of a dynamic telecommunications market permeated by intermodal competition—realities that likewise support preemptive federal deregulation of local wireline telephony:

[W]e specifically reject the assertions of competitive carriers that forbearance should be denied because the [ILECs] either are not subject to competition with respect to their broadband offerings, or are constrained only by a duopolistic relationship with cable operators. Again, we refuse to take the static view suggested by some competitors of this dynamic broadband market, thus leveling the terms of competition, providing real competitive choice, and furthering the goal of ensuring just, reasonable and nondiscriminatory rates, terms and conditions for these services. . . . [B]roadband technologies are developing and we expect intermodal competition to become increasingly robust, including providers using platforms such as satellite, power lines and fixed and mobile wireless in addition to the cable providers and [ILECs].<sup>327</sup>

In 2006, to symbolize the importance of ILEC fiber-optic video

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322. See, e.g., Squeo, *supra* note 317, at B8 (“SBC yesterday said it would accelerate its plan to build an all-digital, high-speed network that reaches 18 million homes by 2007, two years earlier than planned. ‘This is the latest in a series of broadband rulings that demonstrate [that] this administration and the FCC understand that keeping outdated regulation off of tomorrow’s technology will boost jobs, investment and innovation,’ said SBC Chairman and Chief Executive Edward Whiteacre.”); Petition for Forbearance, *supra* note 318, at 21515 (statement of then-FCC Chairman Michael K. Powell) (“[C]ompanies are responding to the Commission’s efforts to create a stable regulatory environment for new investment. For example, just this week Verizon announced its plans to double its fiber-to-the-premises (FTTP) deployment rate next year, bringing FTTP to 2 million additional locations. This represents a 566 percent increase over the number of existing FTTP subscribers.”).

323. Internet Over Wireline Facilities, *supra* note 174.

324. *Id.* at *passim*.

325. *Id.* at *passim*.

326. *Id.* ¶ 1; see also *id.* ¶¶ 17, 39, 45, 79.

327. Petition for Forbearance, *supra* note 318, at ¶ 29.

services, the FCC convened a public hearing on its annual MVPD report in the town of Keller, Texas. Keller is the town where Verizon first rolled out its Fiber Optic Service (“FiOS”) in 2004-05 that ultimately provided both broadband Internet access and television programming. In the first three months FiOS was available, 20 percent of eligible households in Keller, Texas signed up.<sup>328</sup> Verizon is building this FTTP network in 16 states; by the end of 2006 the FTTP network passed six million premises in ten states.<sup>329</sup> Other phone companies are in the process of deploying their own competing fiber-optic products: AT&T is planning an Internet-Protocol-enabled FTTN network called Project Lightspeed<sup>330</sup> and Qwest is preparing to offer MVPD services over existing phone lines using DSL technology.<sup>331</sup> Nationally, in the few places where cable has competition from another wireline video provider, both the Commission and the Government Accountability Office (“GAO”) have found that the total price for cable TV is over 15 percent lower, and the price per channel is more than 27 percent lower.<sup>332</sup>

Unsurprisingly, the FCC has recognized that the ILECs’ investment in fiber-optic technology “could bring the most substantial new competition into the video marketplace that this country has ever seen,” and is therefore an effort “to provide a competitive alternative for video services . . . that deserves our attention and encouragement.”<sup>333</sup> Intermodal competition must become the nation’s telecommunications

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328. Keller Hearing, *supra* note 311, at 3 (testimony of Marilyn O’Connell, Sr. Vice President, Verizon Commc’ns), *available at* <http://www.fcc.gov/realaudio/presentations/2006/021006/oconnell.pdf>.

329. Verizon Commc’ns Inc., Current Report (Form 8-K) (Sept. 27, 2006), *available at* [http://forbes.brand.edgar-online.com/EFX\\_dll/EDGARpro.dll?FetchFilingHTML1?SessionID=qXMAWLubcdS-pxB&ID=4673880](http://forbes.brand.edgar-online.com/EFX_dll/EDGARpro.dll?FetchFilingHTML1?SessionID=qXMAWLubcdS-pxB&ID=4673880). By the end of 2006, FiOS TV had been deployed in California, Delaware, Florida, Massachusetts, Maryland, New Jersey, New York, Pennsylvania, Texas and Virginia. *Id.* Verizon has announced that in 2007 FiOS TV will also become available in Indiana, Oregon and Rhode Island. *Id.*

330. In 2005, SBC Communications acquired AT&T Corp. and the combined entity took the AT&T brandname. *See Earthlink*, 462 F.3d at 6 n.5.

331. FCC Issues 12<sup>th</sup> Annual Report, *supra* note 227, at 3.

332. BANK OF AMERICA EQUITY RESEARCH, BATTLE FOR THE BUNDLE: CONSUMER WIRELINE SERVICES PRICING 4 (2006); *see also Telecommunications: Subscriber Rates and Competition in the Cable Television Industry: Testimony Before the S. Comm. on Commerce, Sci. & Transp.*, 108th Cong. 6 (2004) (statement of Mark Goldstein, Dir., U.S. Gen. Accounting Office), *available at* <http://www.gao.gov/new.items/d04262t.pdf>; *Telecommunications: Issues Related to Competition and Subscriber Rates in the Cable Television Industry: Report to the Chairman, S. Comm. on Commerce, Sci. & Transp.*, 108th Cong. 3-4 (2003), *available at* <http://www.gao.gov/new.items/d048.pdf>. The name of the GAO changed from General Accounting Office to Government Accountability Office on July 7, 2004, pursuant to the GAO Human Capital Reform Act of 2004, Pub. L. 108-271, 118 Stat. 811 (2004) (codified as amended in scattered sections of 5 and 31 U.S.C.).

333. Jonathan S. Adelstein, Comm’r, FCC, Statement, Keller Hearing, *supra* note 311, at 1.

mantra so that the “erosion of old industry boundaries can give way to a more consumer-friendly future.”<sup>334</sup>

Unfortunately, growth of this vital intermodal competition for broadband video programming has been stymied by local franchising authorities. Regulation of a national network industry by fifty state regulatory bodies is bad enough; regulation by tens of thousands of city, county, and village franchising authorities is two orders of magnitude more suffocating. And the problem is not merely one of numbers—this is worse than a simple case of way too many cooks spoiling the broth. The Supreme Court has observed that, by its very nature, the “parochial favoritism” of local government authorities is even more inimical to the unifying principle of the Commerce Clause—and therefore even more suspect—than that of state regulators.<sup>335</sup> “[M]unicipalities are more apt to promote their narrow parochial interests ‘without regard to extraterritorial impact and regional efficiency.’”<sup>336</sup> James Madison warned of this danger in THE FEDERALIST PAPERS,<sup>337</sup> and the Supreme Court has recognized “the serious economic dislocation which could result if cities were free to place their own parochial interests above the Nation’s economic goals.”<sup>338</sup> Indeed, the Court has noted the particular significance of this problem in the context of local franchising of cable television services.<sup>339</sup> Accordingly, the recent adoption by a handful of states—California, Texas, Virginia, New Jersey, North Carolina, South Carolina, Kansas, Missouri, and Michigan—of state-wide video-

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334. Michael J. Copps, Comm’r, FCC, Statement at Keller Hearing, *supra* note 311, at 1 (discussing offerings of bundled voice, video and broadband Internet services by both wireline telephone companies and cable operators).

335. *White v. Mass. Council of Constr. Employers*, 460 U.S. 204, 213 (1983); *see also id.* at 215 (Blackmun, J., concurring in part and dissenting in part) (discussing “local discrimination against interstate commerce”).

336. *City of Columbia v. Omni Outdoor Adver., Inc.*, 499 U.S. 365, 389 (1991) (Stevens, J., dissenting) (quoting *City of Lafayette v. La. Power & Light Co.*, 435 U.S. 389, 404 (1978)).

337. *See* THE FEDERALIST NO. 10 (James Madison) (describing the greater tendency of smaller polities to promote oppressive and narrow interests above the common good).

338. *City of Lafayette*, 435 U.S. at 412-13 (holding that cities, unlike states, are not immune from liability under federal antitrust laws); *see also* *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 38 (1985) (city’s actions are immune from antitrust laws only if city acts pursuant to an articulated state regulatory policy).

339. *See* *Cnty. Commc’ns Co. v. City of Boulder*, 455 U.S. 40, 51 (1982) (quoting *City of Lafayette*, 435 U.S. at 412-13). The decisions in *Boulder* and *Lafayette* were superseded insofar as they exposed cities to damages under federal antitrust laws by the Local Government Antitrust Act of 1984, 15 U.S.C. §§ 34-36 (1984), which established the general rule that antitrust damages are not recoverable from local governments. *See* *Opdyke Inv. Co. v. City of Detroit*, 883 F.2d 1265, 1266 (6th Cir. 1989). However, the Act does not bar injunctive relief against cities for violations of the Sherman Antitrust Act. *See* 15 U.S.C. § 35; *Montauk-Caribbean Airways, Inc. v. Hope*, 784 F.2d 91, 95 (2d Cir. 1986).



franchising reform statutes is a very welcome development.<sup>340</sup>

Equally welcome are the FCC's new rules implementing Section 621 of the 1984 Cable Act.<sup>341</sup> The 1992 Cable Act amendments were intended to remove the barriers to entry into the MVPD market, but, as the market-concentration statistics reviewed above reveal, that legislation has yet to generate much improvement. The Act provided a list of factors that cabins the discretion of local franchising authorities in awarding a competing MVPD franchise,<sup>342</sup> and Section 621(a)(1) mandated that "[a] franchising authority may not . . . unreasonably refuse to award an additional competitive franchise."<sup>343</sup> However, in the absence of firm substantive guidance from the FCC, the courts have been relatively inactive in enforcing the 1992 Act. But the entire point of national regulation of interstate networks under the Commerce Clause is to avoid the balkanizing and parochialism of local regulation.

In issuing its Notice of Proposed Rulemaking in 2005 to explore rules to implement Section 621, the Commission observed that the Act "prohibits not only the ultimate refusal to award a competitive franchise, but also the establishment of procedures and other requirements that have the effect of unreasonably interfering with the ability of a would-be competitor to obtain a competitive franchise, either by (1) creating

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340. The statewide franchising bill passed in the California legislature on August 31, 2006, and was subsequently signed by the governor. See James K. Glassman, *Cable Guys*, WALL ST. J., Sept. 28, 2006, at A16. The states that have enacted these statewide video franchise laws are home to about one-third of the nation's population. *Id.*; see also TEX. UTIL. CODE ANN. § 66.003 (Vernon 2005); Keller Hearing, *supra* note 311, at 7 (testimony of Marilyn O'Connell, Sr. Vice President, Verizon Commc'ns) (within weeks of enactment of the Texas statewide franchise law, Verizon applied for and was granted a state franchise for an additional 21 cities beyond the four Verizon had already negotiated individually); Keller Hearing, *supra* note 311, at 2-3 (statement of Mike Moncrief, Mayor, Fort Worth), available at <http://www.fcc.gov/realaudio/presentations/2006/021006/moncrief.pdf> (discussing Texas Senate Bill 5 and describing how the new state-wide franchising law protects local interests in revenue, community programming obligations, and control over rights of way); *Granholm Signs Cable TV Bill - Without Net Neutrality*, *supra* note 180 (upon Michigan Governor's signing of the video-franchising reform legislation, AT&T announced it would invest \$620 million and add 2,000 full-time jobs).

341. See Implementation of Section 621(a)(1) of the Cable Commc'ns Policy Act of 1984 as Amended by the Cable Television Consumer Prot. & Competition Act of 1992, *Notice of Proposed Rulemaking*, 20 FCC Rcd. 18,581 (2005) [hereinafter *Cable Proposed Rulemaking*]; Video Franchising Order, *supra* note 5.

342. The first paragraph of new Section 621(a)(4) imposed an affirmative duty on local franchising authorities to give franchise applicants "a reasonable period of time to become capable of providing cable service to all households in the franchise area." 47 U.S.C. § 541(a)(4)(A). The second and third paragraphs delineated "adequate assurances" that local franchising authorities "may require" of a franchise applicant – namely, that the MVPD operator "provide adequate public, educational, and governmental access channel capacity, facilities, or financial support," *id.* § 541(a)(4)(B), and that it have "the financial, technical, or legal qualifications to provide cable service," *id.* § 541(a)(4)(C).

343. *Id.* § 541(a)(1).

unreasonable delays in the process, or (2) imposing unreasonable regulatory roadblocks.”<sup>344</sup> That analysis hews closely to the statutory text which, as Chairman Martin reminded us, provides that “[a] franchising authority . . . *may not unreasonably refuse to award an additional competitive franchise.*”<sup>345</sup> In its order, the FCC concluded that “the current operation of the franchising process constitutes an unreasonable barrier to entry that impedes the achievement of the interrelated federal goals of enhanced cable competition and accelerated broadband development.”<sup>346</sup> Specifically, the Commission found that “an LFA is unreasonably refusing to grant a competitive franchise when [1] it does not act on an application within a reasonable time period, [2] imposes taxes on non-cable services such as broadband, [3] requires a new entrant to provide unrelated services or imposes unreasonable build-out requirements.”<sup>347</sup>

These problems are very real. Federal intervention was needed because LFAs have been preventing effective competition in the provision of video programming services to consumers. The Commission’s first finding was that LFAs are unreasonably refusing to award a competitive video franchise when they drag out the franchising

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344. Cable Proposed Rulemaking, *supra* note 341, at ¶ 19.

345. Video Franchising Order, *supra* note 5, at 5189 (statement of Kevin J. Martin, Chairman, FCC) (emphasis in original) (quoting 47 U.S.C. § 541(a)(1)). One dissenting commissioner complained that this passage of the statute is too small to bear the regulatory weight of the FCC’s new franchising rules. *See id.* at 5193-94 (dissenting statement of Jonathan S. Adelstein, Comm’r, FCC). But it cannot be disputed that Section 621(a)(1)’s terms go beyond outright denial of a franchise and expressly encompass LFA actions that merely “unreasonably refuse to award” a franchise. Surely that additional language is not to be dismissed as meaningless surplusage. As Commissioner Tate noted, “[i]n amending Section 621(a)(1) to include the phrase ‘unreasonably refuse to award,’ Congress explicitly limited the authority of LFAs. . . . It is nonsensical to contend that, despite the limitations on LFA authority in the Act, LFAs remain the sole arbiters of whether their actions in the franchise approval process are reasonable.” *Id.* at 5204 (statement of Deborah Taylor Tate, Comm’r, FCC). The Commission has undoubted authority to issue rules to enforce the entirety of the Communications Act, the Cable Act included. *See AT&T Corp.*, 525 U.S. at 380; *City of Chicago v. F.C.C.*, 199 F.3d 424, 428 (7th Cir. 1999); *Nat’l Cable Television Ass’n v. F.C.C.*, 33 F.3d 66, 70 (D.C. Cir. 1994). And the enforcement of a statutory “reasonableness” requirement or “unreasonableness” standard is no novelty to the FCC. *See, e.g.*, Implementation of Section of the Cable Television Consumer Prot. & Competition Act of 1992, *Report & Order & Further Notice of Proposed Rulemaking*, 8 FCC Rcd. 5631, ¶ 1 (1993) (setting rules to ensure reasonable rates for basic cable); *Star Lambert & Satellite Broad. and Commc’ns Ass’n of Am., Petition for Declaratory Ruling*, 12 FCC Rcd. 10,455, ¶¶ 2-3 (1997) (holding that local ordinances violated FCC rules prohibiting unreasonable delays and unreasonable increases in costs for satellite providers).

346. Press Release, FCC, FCC Adopts Rules to Ensure Reasonable Franchising Process for New Video Market Entrants (Dec. 20, 2006), *available at* [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-269111A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-269111A1.pdf).

347. Video Franchising Order, *supra* note 5, at 5189 (statement of Kevin J. Martin, Chairman, FCC).

process. “The record collected by the Commission in this proceeding cited instances where LFAs sat on applications for more than a year . . . .”<sup>348</sup> For example, it routinely takes Verizon fifteen months or more to obtain a video franchise. Outside the few states that have enacted statewide franchising reform laws, 74 percent of Verizon’s applications have been pending for fifteen months or more, and 56 percent for eighteen months or more. Fully 83 percent of Verizon’s applications have been pending before LFAs for more than a year. This local foot-dragging is what prompted the Commission to act.<sup>349</sup>

The FCC’s second finding was that LFAs unreasonably deny competitive franchises when they impose taxes on non-cable services such as broadband Internet access or telephone services. This pertains to the first justification usually offered in defense of a continued primary role for local franchising: the fact that local governments have become dependent upon, and are entitled by statute, to a five percent franchise fee from all MVPD providers.<sup>350</sup> This is a red herring (indeed, the justifications for local franchising of video services constitute an entire school of red herring). The telephone companies that seek to enter the video market generally do not contest that they are subject to, as are the original cable-TV franchisees, a maximum fee (payable to the local government) of five percent of their annual gross video service revenues. The problem is that some local franchising authorities, eagerly eyeing a new source of revenue for local government, have tried to bootstrap this fee for a *video* service franchise into a demand that ILECs entering the video market also remit five percent of the revenues derived from the ILEC’s *pre-existing telephone and broadband* services provided over the same fiber network. The Commission made clear that this is unacceptable.<sup>351</sup>

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348. *Id.*

349. See Reply Comments of Verizon on Video Franchising to the *Report & Order & Further Notice of Proposed Rulemaking* in Implementation of Section 621(a)(1) of the Cable Comm’n’s Policy Act of 1984 as Amended by the Cable Television Consumer Prot. & Competition Act of 1992, MB Dkt. No. 05-311, at 34-37 (Mar. 28, 2006), available at [http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native\\_or\\_pdf=pdf&id\\_document=6518332224](http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6518332224) (reply to Video Franchising Order, *supra* note 5); see also Letter from Leora Hochstein, Executive Dir., Verizon, to Marlene Dortch, Sec’y, FCC (Dec. 13, 2006), available at [http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native\\_or\\_pdf=pdf&id\\_document=6518332192](http://fallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6518332192).

350. See 47 U.S.C. § 542(b).

351. The Commission was not plowing new ground here. Both the FCC and the courts have held that broadband Internet service is not subject to the 5 percent franchise fee for video services. See, e.g., Declaratory Broadband Ruling, *supra* note 168, at ¶ 105 (because “cable modem service [is] an information service, revenue from cable modem service would not be included in the calculation of gross revenues from which the franchise fee ceiling is determined”); *City of Minneapolis v. Time Warner Cable*, No. 05-994 ADM/AJB, 2005 U.S. Dist. LEXIS 27743, \*17-20 (D. Minn. Nov. 10, 2005); *Time Warner Cable-Rochester v. City of Rochester*, 342 F. Supp. 2d 143 (W.D.N.Y. 2004); 129 CONG. REC. 15,461 (1983)

The Commission's third finding was that some local governments have used their leverage over franchise applications to extort in-kind benefits from ILECs that likewise exceed the 5 percent statutory cap and often have nothing to do with the provision of video services to the town's consumers. Chairman Martin noted that some LFAs have "required extraordinary in kind contributions such as the building of public swimming pools and recreation centers."<sup>352</sup> One town in the northeast conditioned a franchise on an ILEC's willingness to buy the town new streetlights, give free cell phones to all town employees, and provide free parking spaces for the town at the ILEC's local facility. A town in the south demanded that the franchise applicant hook up hundreds of town traffic signals with fiber connections, furnish free cell service to a thousand city employees, and provide free fiber services to some sixty organizations with whom the city did business.

Other local franchising authorities are refreshingly candid in their extortion: they simply demand fees of hundreds of thousands of dollars for an ILEC to apply for an MVPD franchise, or insist that the ILEC pay equally outrageous sums for the town to hire attorneys to negotiate and contest the ILEC's application. The Commission was on familiar territory in rejecting such overreaching.<sup>353</sup> Even though such abuses have often been struck down by the courts, LFAs have persisted nonetheless and compelled ILECs that wish to break cable TV's virtual monopoly to jump through the same illegal hoops and contest the same abuses in court on a town-by-town, village-by-village basis. This is not the unified national marketplace that the Commerce Clause was adopted to engender.<sup>354</sup>

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(remarks of Sen. Goldwater) ("[T]he overriding purpose of the 5% fee cap was to prevent local governments from taxing private operators to death as a means of raising revenues for other concerns."); 47 U.S.C. § 541(b)(3)(B) (local franchising authorities specifically prohibited from "impos[ing] any requirement . . . that has the purpose or effect of prohibiting, limiting, restricting, or conditioning the provision of a telecommunications service by a cable operator or affiliate thereof").

352. Video Franchising Order, *supra* note 5, at 5189 (statement of Kevin J. Martin, Chairman, FCC).

353. The Cable Act authorizes local franchising authorities to seek reimbursement only for "charges incidental to the awarding or enforcing of the franchise," such as "payments for bonds, security funds, [or] insurance." 47 U.S.C. § 542(g)(2)(D). The courts have consistently held that LFAs' consultants and attorneys' fees are not recoverable "incidental charges." *See, e.g.,* Charter Commc'ns, Inc. v. County of Santa Cruz, 133 F. Supp. 2d 1184, 1212-14 (N.D. Cal. 2001), *rev'd on other grounds*, 304 F.3d 927 (9th Cir. 2002) (rejecting consulting local franchising authorities' claim for consulting fees that exceeded the 5 percent fee cap); Time Warner Entm't, Co. v. Briggs, No. 92-40177-GN, 1993 U.S. Dist. LEXIS 1196, \*16-18 (D. Mass. Jan. 14, 1993) (local franchising authorities' attempt to charge their consulting and attorney fees imposed "franchise fees" in excess of statutory cap).

354. This is a complete answer to the dissenting Commissioners' argument that rulemaking action by the FCC was not needed because the phone companies have generally been successful in *eventually* obtaining video franchises on a town-by-town basis. *See* Video

It is essential to recognize intermodal competition's unique ability to promote expansion of networks and enhancement of telecommunications services. Chairman Martin has made widespread deployment of broadband his top priority, and in the Commission's 2006 *Video Franchising Order* he accurately observed that the "ability to deploy broadband networks rapidly . . . is intrinsically linked to the ability to offer video to consumers."<sup>355</sup> In a policy paper issued in 2005, the Phoenix Center:

[F]ound that video 'is now the key driver for new fiber deployment in the residential market. . . . Quite simply, the ability to sell video services over these fiber networks may be a crucial factor in getting those fiber networks deployed.' By enhancing the ability of new entrants to provide video services then we are advancing our goal of universal affordable broadband access for Americans, as well as our goal of increased video competition.<sup>356</sup>

Therefore, the Commission's new Section 621 rules are not an isolated tweaking of the regulatory apparatus, but part of a unified national strategy to rationalize telecommunications regulation through preemptive federal regulation and, ultimately, deregulation. As Commissioner McDowell put it, "creating a deregulatory environment where competition is given the chance to flourish kicks off a virtuous cycle of hope, investment, growth and opportunity."<sup>357</sup>

The final justification trotted out by LFAs for retaining local control over video franchising is the need for towns and counties to control access to, and the digging up of, their streets and other rights of way. Considered in the abstract, that rationale is both sensible and unquestioned. The Cable Act itself requires video providers using public rights of way to ensure "that the safety, functioning and appearance of the property and the convenience and the safety of other persons not be adversely affected by the installation or construction of facilities necessary

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Franchising Order, *supra* note 5, at 5194 n.6 (dissenting statement of Jonathan S. Adelstein, Comm'r, FCC). Regulation of a *national* network is not supposed to be carved up into myriad local franchising fiefdoms. Eliminating such inefficiencies is what the Commerce Clause is all about, and the Cable Act imposed federal limits to avoid just such problems.

355. *Id.* at 5189 (statement of Kevin J. Martin, Chairman, FCC).

356. *Id.* at 5189-90 (statement of Kevin J. Martin, Chairman, FCC) (quoting the Phoenix Center report); *see also id.* at 5204 (statement of Deborah Taylor Tate, Comm'r, FCC) ("[T]he development of competition in the video marketplace . . . speeds the deployment of broadband across the country in a platform-neutral manner.").

357. *Id.* at 5205 (statement of Robert M. McDowell, Comm'r, FCC); *see also id.* at 5204 (statement of Deborah Taylor Tate, Comm'r, FCC) ("At a high level, however, I view this as a continuation down a path of deregulatory policies designed to encourage new market entry, innovation, and investment.").

for a cable system.”<sup>358</sup> However, local governments must not be permitted to leverage authority over rights of way to extort discriminatory, burdensome, and redundant concessions from new competitors wishing to enter the MVPD market.

A telephone company is already subject to local control in digging up rights of way because those operations take place to install and maintain the wireline and fiber-optic cables that carry the ILEC’s telephone services. The fact that the same network is now to be used to provide video services does not grant local franchising authorities the authority to impose additional requirements or, indeed, *any* regulation on the telephone or broadband network that is not otherwise sanctioned by federal law. This applies with particular force to Internet access which, as an “information service,” has already been preemptively deregulated by Congress and the FCC. The *content* of the electronic signal carried on fiber-optic cables buried beneath or strung above a city’s streets—whether voice communication, broadband Internet access, or television entertainment—has no impact on the safety of, or the city’s authority over, those public rights of way. Wireline telephony is already locally regulated insofar as necessary to ensure the safety and utility of public streets. Therefore, forcing a phone company to submit to another round of scrutiny when the very same cables are used to provide a different service is a prime example of irrational, transparently extortionate piling-on. Demanding that a telephone company subject the entirety of its integrated telecommunications-data-cable network to municipal jurisdiction as a condition for getting a video franchise would likewise be abusive overreaching and a violation of federal statutes.<sup>359</sup> If the nation truly wants the competitive video services market that Congress tried to

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358. 47 U.S.C. § 541(a)(2)(A).

359. Section 522(7) of Title 47 provides that a common carrier’s mixed-use network is a cable system subject to municipal jurisdiction *only* “to the extent” that it is used to transmit video programming directly to subscribers. Section 541(b)(3)(A) provides that, if “a cable operator . . . is engaged in the provision of telecommunications services,” “such cable operator . . . shall not be required to obtain a franchise . . . for the provision of telecommunications services,” and the cable provisions of the Act “shall not apply to such cable operator or affiliate for the provision of telecommunications services.” The following section, 541(b)(3)(B), states that a “franchising authority may not impose any requirement under this subchapter that has the purpose or effect of prohibiting, limiting, restricting, or conditioning the provision of a telecommunications service by a cable operator.” Section 541(b)(3)(C) provides that a local franchising authority may not order a cable operator to “discontinue the operation of a cable system, to the extent such cable system is used for the provision of a telecommunications service, by reason of the failure of such cable operator . . . to obtain a franchise or franchise renewal under this title with respect to the provision of such telecommunications service.” Finally, attempting to assert jurisdiction over a telecommunications provider’s mixed-use network impermissibly has the effect of requiring the provision of telecommunications facilities, in violation of Section 541(b)(3)(D). *See also id.* § 253(a).

create in the 1992 Cable Act, the myriad barriers to entry erected by local franchising authorities cannot be tolerated.

Nevertheless, two members dissented from the Commission's decision to enforce Section 621 and did so principally on grounds that the FCC's order policing local video regulation supposedly upends "long-standing principles of federalism,"<sup>360</sup> and "turns federalism on its head" by indulging "arrogant . . . federal power riding roughshod over local governments."<sup>361</sup> This position totally misconceives the Constitution's federal structure. The Commission did not "go[] out on a limb in asserting federal authority to preempt local governments"<sup>362</sup>—the whole point of the Commerce Clause was to authorize federal preemption of parochial, atomizing, inefficient state-by-state regulation of genuinely interstate commerce. The propriety of federal preemption of *local* regulation of interstate network industries is a logically compelled corollary.

#### CONCLUSION

If the current state of the Internet and contemporary wireline, wireless, and cable networks demonstrates nothing else, it decisively confirms that these services are inherently interstate, that they engage in ever-increasing intermodal competition to provide the full range of voice, data, and video services, and that they therefore should be subject to a single, uniform set of federal regulations. As Justice Jackson noted long ago, the Constitution itself, not just its Commerce Clause, was engendered by the Framers' recognition that "[n]o other federal power was so universally assumed to be necessary, no other state power was so readily relinquished," as the power over interstate network industries.<sup>363</sup> It follows *a fortiori* that the regulatory power of local governments must bow along with that of the States to the supervening needs of the Nation.

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360. Video Franchising Order, *supra* note 5, at 5191 (dissenting statement of Michael J. Copps, Comm'r, FCC). Ironically, Commissioner Copps simultaneously argued that "we need the certainty of a national strategy to get the job done" in fostering "ubiquitous high-speed broadband to all our citizens." *Id.* at 5192.

361. *Id.* at 5203 (dissenting statement of Jonathan S. Adelstein, Comm'r, FCC); *see also id.* at 5193-96.

362. *Id.* at 5193 (dissenting statement of Jonathan S. Adelstein, Comm'r, FCC).

363. *H.P. Hood & Sons*, 336 U.S. at 534.

