A DISTANCE INSENSITIVE UNIFORM NATIONAL TELEPHONE RATE STRUCTURE: A SPECULATIVE EXERCISE IN FEDERALISM

Robert Carson Godbey

Program on Information Resources Policy

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PREFACE

I would like to thank Tony Oettinger and the Harvard Program on Information Resources Policy for their support and assistance not only in this project but also in my education over the past few years. Prof. Oettinger's advice and suggestions are an integral part of the discussion of the factors tending toward the postalization of telephone rates, far beyond what mere footnoting can reflect.

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Any mistakes or omissions must remain entirely the responsibility of the author.

Bob Godbey
Cambridge
16 June 1980

EXECUTIVE SUMMARY

This paper considers the establishment of a distance-insensitive uniform national telephone rate structure, referred to as the "postalization of telephone rates." Presently the telephone industry is regulated at the national and state or local levels and devising a uniform national rate structure implies centralizing regulation, presumably by the FCC. This transfer of authority raises a question of balance between national and state government. The concept of federalism, which embraces the importance of regional and local character and autonomy, will have a profound impact on any attempt to institute postalization of telephone rates.

Currently, jurisdictional separations procedures allocate costs and revenues, along with the corresponding regulatory authority, between intrastate and interstate services. Intercompany settlements procedures apportion revenues among companies cooperating to provide a single service. The present system of separations and settlements, involving a high degree of rate averaging, has lately come under attack, owing mainly to the increased competition allowed in the telephone industry. Under the system of postalization, however, it may be possible to price services to more nearly reflect their actual cost, while still allowing the cost averaging implicit in a uniform national distance-insensitive rate structure.

Several factors seem to encourage postalization of telephone rates. Economically, distance-insensitive pricing becomes desirable as the incremental increase in cost attributable to the increased distance of a call nears the incremental cost of providing facilities to record its distance and compute a distance-sensitive price.

Postalization also supports the traditional public policy goals of equal charges for equal service and universal service by utilizing cost averaging and internalizing some costs.

Decreasing long distance telephone rates reflect and encourage changing social perceptions. Consumers and businesses will in all probability be receptive to postalization because they seem to increasingly conceive of "local service" and "local markets" as beyond the limitations of the traditional local calling area.

Competition may also promote postalization by decreasing the contribution of toll services to local service costs and increasing rates for local services to correspond with lowered toll rates. However, the current regulatory commitment to competition cuts against postalization in many ways; it creates both economic and political complications.

Should Congress eventually be persuaded to enact legislation providing for the institution of postalization, it would require significant change in the regulatory structure of the industry. Both the clear wording of the Communications Act of 1934 and the long tradition of separations and settlements raise difficult barriers to postalization.

If, however, there is sufficient support in Congress, the constitutional principle of federalism constrains the potential avenues for new legislation to implement postalization. One approach could be establishment of a nationwide rate system with compulsory state enforcement of that system. Analysis of this approach, however, suggests that the courts would probably find such compulsory state enforcement of federal policy to be an unconstitutional intrusion upon state sovereignty.

Another mechanism could be the federal preemption of all telephone regulations, thus implying the elimination of state regulatory bodies. The reaction of the courts to such legislation is unclear, but the political process itself is a powerful safeguard of the constitutional role of the states. An overview of the legislative history of the Communications Act of 1934 and of testimony on bills presently under consideration by Congress suggests that the state regulatory commissions will strenuously defend their roles.

Finally, a uniform rate system could be established through the use of a minimum or voluntary federal rate structure. The FCC or a federal-state joint board would establish a uniform national rate. This might represent a minimum rate for the states, leaving each state the option of setting higher rates. If pooling and division of revenues guaranteed a fair rate of return for each telephone company, political pressure might serve to ensure that the national minimum rate was in effect the national uniform rate. Alternatively, participation in the uniform rate structure could be optional with each state. Support from the division of the national revenue pool would then be contingent upon a state's participation in the program. These approaches attempt to keep new legislation within bounds which previous court decisions have proven safe.

The major attraction of postalization, drawing the country together as a national community, is thus an interesting counterpoint to the underlying concept of federalism, the importance of the local community. Still, the uninhibited transfer of information may be a goal intrinsically worth pursuing. Freedom of communication has traditionally been a revered goal of our democratic society. Postalization of telephone rates may prove to be a valuable asset in furthering those traditional values.

I. INTRODUCTION

This paper is about the establishment of a distance-insensitive uniform national telephone rate structure for both local and toll service. Throughout the paper, this is referred to as the "postalization of telephone rates." The phrase "postalization" is used because the Post Office, for reasons becoming more common to the telephone industry, prices several of its more familiar services in that way. For example, the price of a first class letter is the same regardless of whether it is mailed from one side of the street in Boston to the other side of the street in Boston, or from one side of the continent in Boston to the other side of the continent in Los Angeles.

The price of a first class letter varies by weight, a rough measure of the amount of information transmitted; the rate for a telephone call might vary by duration of call, also a rough measure of information transmitted. Pricing might also vary with time of day, type of service, etc. Postalization means only that the price will not vary with distance.

Postalization does not mean nationalization. A major assumption of this paper is that the private corporations presently involved in providing telephone services throughout the country will continue to be involved. This paper focuses primarily on the change in the regulatory structure needed to implement postalization.

The telecommunications industry is already a highly regulated industry. But much of that regulation occurs on a state or local level, just as it has since the birth of the industry. Postalization of telephone rates would require more central control of regulation. This implies a broader role for the Federal Communications Commission and a more narrow role for the state regulatory agencies. This transfer of authority raises a question of balance between the national government and the state government, a question generally addressed under the heading of federalism. If the role of the states and their political subdivisions in our federal form of government does not include ensuring adequate provision of an essential service as traditionally and intimately local as telephone service, then what of substance is left of that role? Might not state or local regulation of power, other utilities, health, sanitation, and many other concerns also be usurped? The issue of how far the national government may go in regulating local affairs in the guise of regulating interstate commerce is a delicate one.

Postalization of telephone rates is in fundamental tension with basic notions of federalism. Federalism is based upon a conception of the importance of regional and local character and autonomy. Postalization is attractive because it tends to pull us together as a nationwide community.

This paper considers the impact of federalism upon any attempt to institute postalization of telephone rates. The paper begins by looking at this history of the telecommunications industry, and the industry as it is today. It then considers factors that may tend to influence a move toward postalization. This move toward postalization is merely hypothesized, and is not rigorously defended.

The paper then considers some potential approaches to postalization of telephone rates. The first approach considered is compelled state cooperation in implementing a uniform national rate structure. Next, federal preemption of all telephone regulation is discussed. Finally, a national uniform rate that is either a minimum rate for the states, or alternatively an optional rate for the states is considered. Analysis of these approaches will develop the basic restraints of federalism on any new legislation implementing the postalization of telephone rates.

It is not the purpose of this paper to advocate postalization of telephone rates. It would be more accurate to say that the discussion assumes an impetus toward postalization, and discusses the restraints upon such a movement that concerns for federalism create. Admittedly, the paper does attempt to explain why such a hypothesized impetus is plausible, but that should not be confused with advocacy of the position. There are significant barriers to postalization of telephone rates in today's telecommunications market, with its increasing emphasis on competition. Indeed, concern with federalism also runs counter to the trend in current thinking about the regulation of telecommunications. Yet both the concept of postalization and that of federalism merit discussion, and they intersect in an interesting fashion. Thus this paper.

II. AN OVERVIEW OF THE TELECOMMUNICATIONS INDUSTRY

The most visible corporation in the telecommunications industry is American Telephone and Telegraph (AT&T). AT&T is a holding company for what is called the Bell System. The system includes twenty-three operating companies, such as New England Bell, Southwestern Bell, etc., that provide service directly to the customers. Some of the operating companies are wholly owned subsidiaries of AT&T; others are only partially owned by AT&T. The Bell System also encompasses AT&T Long Lines, which provides interstate long distance service, Western Electric, the manufacturing arm of the Bell System, and Bell Labs, the research group for the system. The revenues of the Bell System in 1976 were over 33 billion dollars.[1]

In addition to the Bell System operating companies, there are approximately 1500 independently owned telephone companies. The majority of the larger Independents are represented by the United States Independent Telephone Association (USITA). Although the Independents serve a minority of the country's telephone customers (18% of the total telephones in the country), their service areas include the majority of the United States land area with telephone service (53% of total land area served). The revenues of Independent companies in 1976 were over 6 billion dollars.[2]

In recent years long distance service has begun to be provided by companies on a competitive basis with AT&T. These companies, such as Microwave Communications Incorporated and Southern Pacific Communications, will be referred to as Other Common Carriers (OCC's).

The Communications Act of 1934 mandates the regulation of all interstate telecommunications by the Federal Communications Commission (FCC). That act specifically reserves the regulation of intrastate telecommunications to the states.[3] The state agencies are represented by the National Association of Regulatory Utility Commissioners (NARUC).

A. Local and Toll Telephone Service

The telecommunications industry markets a plethora of services. Basic telephone service can be roughly divided into two parts, local and toll. The distinction between the two is somewhat circular. Local, or exchange, service is defined as service in an area "within which calls may be made without a toll charge," usually "consisting of a single city and environs." A toll call is, logically enough, any call "for a destination outside of the local service area of the calling station."[4]

The distinction between toll and local service used to be simple. Consider a small community served by a local exchange. All the telephones in the community are wired to one switching center where one phone is connected to another as desired. Originally an operator physically connected the wires from the phones at a switchboard; later the connection was made by an electro-mechanical switch. Technically this paradigm includes two basic elements: the subscriber loop that includes the instrument in the customer's home or business and the wires from that instrument to the central office, and the switching center in the central office that switches or connects one subscriber loop to another.

A toll or long distance call was simply a call from a subscriber in one community to a subscriber in another. Such a call introduces a third technical element: the transmission facility connecting the two local switching centers, called a toll trunk. The subscriber loop connecting the customer to the central office is dedicated to that customer (except with party lines) and is used only for that customer's calls. In contrast, the toll trunk is shared over time. When one call over the toll trunk is completed, the trunk is released and may be used for the next call between the two communities. A call from one community to another was called a long distance call, and a toll was charged for this service over and above the generally flat rate charged for providing local service.

This simple paradigm has been overcome by complexity. Almost every large urban area has more than one central office in its local calling area. Trunks connect the central offices, although no toll is charged for calling between them. Some local calling areas now far exceed traditional notions of community. That around Atlanta is larger than the states of Rhode Island and Delaware combined.[5] Some local calling areas, such as that around Houston, involve more than one operating company. Thus the conceptual line between toll and local service has blurred.[6]

Even in the simple paradigm one can anticipate problems. If the two communities are in different states, a call between them is interstate and regulated by the FCC. If they are within the same state a call between them is intrastate and regulated by the state utility commission or its equivalent. Each community may be served by a different telephone company; in that case the revenue from the toll call must be apportioned between the participating companies. Local service may be provided by two different companies and the trunk service provided by a third, with the revenue then being split between all three companies.

This division of toll revenue, which may involve not only different companies but different regulatory agencies, is a complex problem. Regulators demand that a simple equation be maintained: total revenues must equal total costs. Costs in this equation include not only the expenses associated with the provision of a service, taxes that must be paid, and depreciation on equipment used to provide the service, but also a fair rate of return on the capital investment involved, roughly the undepreciated plant. Rates are set at a level adequate to generate sufficient total revenues to cover the costs of the regulated industry.

One might expect, therefore, that the costs of providing toll service would be allocated by the regulators among jurisdictions and by the companies involved among themselves, and the revenues from the service distributed accordingly. This allocation raises the question of how the service is to be defined. Railroads have traditionally done this on a route by route basis, dividing revenues accordingly.[7] The telephone industry has traditionally defined service more broadly, and today averages the costs of all interstate toll routes in establishing the rates for interstate toll service, and subsequently divides the revenues between participating companies.[8]

In addition to the problems in defining service, in practice the allocation of some costs between toll and local service is essentially arbitrary. The costs of providing the toll trunk seem clearly associated with toll service. But some of the cost of providing the local service is shared between toll and local service. Economists refer to such a situation as one of joint or common costs. The distinction between the two is not relevant here. Toll service could not be provided without the central office and subscriber loops provided by the local operating company. Accordingly, some of the costs associated with these facilities should be allocated to the toll service, and the rates for toll service should be sufficient to provide revenues to cover those costs. The proportion of local service costs to be allocated to toll is, from the standpoint of applied economics, essentially arbitrary.[9] Appropriate allocation of costs thus becomes a political decision, albeit with significant economic consequences.[10]

B. The Present Regulatory Structure and its Evolution

Jurisdictional separations procedures allocate costs and revenue requirements, and corresponding regulatory authority, between intrastate and interstate services. Intercompany settlements procedures apportion revenues between companies cooperating to provide a single service.

Prior to 1930, the joint cost ambiguity of local plant was ignored by most regulatory agencies. The predominant separations theory was referred to as "board-to-board." The central office switchboard in our simple two-community paradigm was the point of demarcation between local and toll service. Local rates covered all local exchange costs, up to the point where the toll trunks plugged into the local switchboard. Long distance rates covered the costs of providing facilities between local exchanges.[11]

In 1930 in Smith v. Illinois Bell Tel. Co., a case which still has a profound effect upon the regulation of the telephone industry, the Supreme Court addressed the problem of the allocation of local exchange costs.[12] The Court held:

> The separation of the intrastate and interstate property, revenues and expenses of the Company is important not simply as a theoretical allocation to two branches of the business. It is essential to the appropriate recognition of the competent governmental authority in each field of regulation.[13]

Local exchange property had been attributed entirely to intrastate service. The court took notice of the fact that the local exchange, down to the individual subscriber's loop, was "used in connection with the long distance toll board [and] employed in the interstate transmission and reception of messages."[14] The Court went on to say

> While the difficulty in making an exact apportionment of the property is apparent, and extreme nicety is not required, only reasonable measures being essential, it is quite another matter to ignore altogether the actual uses to which the property is put. It is obvious that, unless an apportionment is made, the intrastate service to which the exchange property is allocated will bear an undue burden.[15]

This opinion set the stage for a new separations theory, called "station-to-station," that recognized toll rates should bear some portion of the costs of the entire system, from subscriber station to subscriber station, since all these facilities must be involved to provide toll service.

The Communications Act of 1934 emphasized the distinction between intrastate and interstate services, and the appropriate regulatory authority over each. This was an explicit recognition of the importance of jurisdictional separations.

Although the language of the Smith decision pushed regulators into relying upon a "use" theory to justify their allocation of costs between intrastate services and interstate toll services, the FCC did not immediately adopt a station-to-station approach. The state commissions could not implement such an approach without federal cooperation. There was much confusion following Smith and related decisions.[16]

To compound the confusion and discontent, AT&T Long Lines was making a substantial profit on its interstate toll service. The FCC, still adhering to a board-to-board theory, attempted to reduce Long Line's earnings by reducing interstate toll rates. This began to create an embarrassing disparity between interstate and intrastate toll rates: a call within the borders of the state might be much more expensive than a longer call across state lines.

In 1943, the station-to-station principle was finally implemented.[17] It has since evolved through a succession of plans developed by the FCC and NARUC, as well as AT&T and USITA, into an integral part of the telephone industry.

In the late 1930's the FCC began articulating a principle of nation-wide rate averaging in interstate toll ratemaking.[18] This concept was based on the idea of equal charges for equal service. Thus the rates for a toll call of 500 miles should be the same, regardless of the actual costs of providing the service. This rate system is now in effect for interstate toll calls within the continental United States.

The technological developments of this period played an essential role in allowing the successful implementation of both the station-to-station separations principle and the uniform national rate principle. Technological innovation allowed the recognition of significant economies of scale over the high density trunk routes.[19] These economies of scale were so impressive that not only could interstate rates continue to be lowered, but the high density routes provided ample revenue to support the additional costs of low density trunk routes and increasingly large portions of local exchange costs.

Successive separation plans allocated an increasing portion of what had previously been costs of local exchange service to interstate toll, as Figure 1 reflects. For example, the 1947 plan allocated 6.9% of the investment in station equipment to interstate toll costs. This increased through a succession of seven plans to an average allocation of 24% under the present "Ozark" plan. This means that 24% of the cost of the telephone instrument on an individual's desk is paid from the interstate toll revenue pool. Other costs previously associated with local services have been shifted in a similar fashion.[20]

Jurisdictional separations currently follow the Ozark plan, adopted in 1971. The Ozark plan is the result of the joint efforts of the FCC, NARUC, AT&T, and USITA. The basic rules are delineated by the FCC, and the details of implementation are developed and described by NARUC and the FCC in the Separations Manual.[21]

Figure 1.

	1973 Total Investment ($ Millions)	Interstate Allocation (% of Total Investment in category as allocated to interstate costs according to successive separations plans) 1947	Charleston 1952-57	1957	Denver 1966	FCC-16258 1967	FCC-17975 1969	Ozark 1971	1973 Interstate Plant Investment ($ Millions)	Annual Carrying Charge (Fraction of Investment)	1973 Interstate Revenue Requirements Associated with Plant ($ Million)
Station Equipment	322.7	6.91	11.66	12.11	10.41	18.79	21.50	23.96	77.3	.30	23.2
Exchange Circuit Equip.	43.3	4.40	6.89	12.35	7.05	11.25	12.61	15.15	6.6	.25	1.6
Toll Switching Equip.	3.1	6.91	6.89	37.46	37.46	37.46	37.46	37.46	1.2	.25	.3
Local Dial Switching Equip.	258.2	6.91	6.89	6.89	9.47	9.47	9.47	15.43	39.8	.25	10.0
Exchange Outside Plant	545.2	6.83	11.66	11.82	10.04	18.11	20.71	24.09	131.3	.25	32.8
Interexchange Outside Plant	33.1	42.67	42.67	42.67	42.67	42.67	42.67	42.67	14.1	.25	3.5
Interexchange Circuit Equip.	119.8	47.91	47.91	47.91	47.91	47.91	47.91	47.91	57.4	.25	14.4
	1,325.4							*24.72	327.7	*.26	85.8

* Weighted Average

Source: Response of United System Service Inc. to FCC Docket No. 20003, April 1975, Exhibit 4

Figure courtesy of Harvard Program on Information Resources Policy.

United Telecommunications -- Allocation of Local Facilities Costs to Interstate Revenue Requirements

The percentage of local plant attributed to interstate operations hence interstate revenue requirements rose sharply over successive separations plans

Source: United System Service, Inc., Response to FCC Docket No. 20003, April 1975, Exhibit 4.

The system as it has evolved utilizes nationwide rate averaging for interstate toll calls. Thus, the revenues from a low density route may cover only a portion of the costs actually associated with that route, and the revenues from a high density route may more than cover the costs actually associated with the provision of service along that route. This creates the necessity for the pooling and division of nationwide interstate toll revenues.

All revenues generated by interstate toll services are pooled and then redistributed to the participating companies on the basis of the revenue requirements associated with the portion of their investment allocated by the jurisdictional separations procedure to interstate toll service. The revenue pool first covers all out-of-pocket expenses associated with interstate service for all of the participating companies, and the remainder is then apportioned to the companies according to their investment. The revenue accorded to a company is thus not directly related to the revenue collected by that company or generated by the company.

The Ozark plan provides the rules that determine how much of a telephone company's intrastate investment and expenses will be allocated to the costs of providing interstate toll service and accordingly covered by the division of the interstate revenue pool. The formula by which this division is determined is a triumph (or cost, depending on one's perspective) of federalism. It reflects an impressive and complicated series of compromises and trade-offs among the federal regulators, the state regulators, and the regulated industry.

Consider, for example, how the Ozark Plan apportions the costs of traffic insensitive equipment. The joint cost ambiguity is particularly troublesome in attempts to allocate the cost of such equipment, because the amount of investment in such equipment is fixed and does not vary with use. The subscriber loop is an example of this type of equipment. A significant amount of the total telephone investment is in non-traffic sensitive equipment.

Smith v. Illinois Bell demanded that "the actual uses to which the property is put" be considered in apportioning the cost associated with that property between jurisdictions.[22] The Ozark plan incorporates this criterion. Cost allocation is determined in part by the ratio of minutes of use for interstate toll calls to the total number of minutes of use of the equipment.[23] The use of this ratio has been tempered and refined. From the first separations plan in 1947 until the Ozark plan in 1971 additional concerns have been reflected in the allocational calculations, moving more and more of the total investment in telephone equipment from intrastate to interstate toll service.[24]

Local rates often are distance insensitive and duration insensitive.[25] Long distance rates, however, are generally based on a charge per minute. Accordingly, the FCC argued that the allocational formula should be adjusted away from a pure usage basis to account for the "deterrent" to long distance usage which resulted from the price structure.[26]

Long distance rates are sensitive not only to duration but also to distance. "[S]ubscribers in large population centers located close to each other, but separated by State boundaries, would tend to have a high[er] calling rate between them...than subscribers located in large population centers at greater interstate distances from other population centers."[27] The FCC thus further tempered the allocation formula to account for the deterrent effect of distance upon interstate long distance.

From considerations such as these, highly dependent upon the traffic patterns and location of each state, evolved the Ozark plan for the allocation of costs to the interstate toll system, and corresponding allocation of revenues from the nationwide pool.

There is significant variation from state to state in the amount of costs allocated by the Ozark plan to interstate toll. Nevada has the high allocation of 62% of its costs to interstate service, Michigan the low at 18%. This percentage reflects the costs of equipment within a state that need not be recovered by the rates established for local and intrastate service.[28]

The state regulators are not bound by Smith v. Illinois Bell and therefore need not allocate costs between intrastate toll and local service on the basis of use. Often rates reflect purely political or marketing judgments. The only basic restraint upon the state regulator is to allow rates sufficient to raise enough revenues to cover the costs of facilities within the state not allocated by the Ozark plan to interstate toll.

State toll settlements between the Bell System and the Independents generally follow, by agreement among the carriers, the basic mechanisms of the Ozark plan. The use ratios and the deterrence factors of the Ozark plan are adjusted for intrastate use on the basis of intrastate statistics, rather than national statistics. Revenue requirements of the Independent telephone companies that are not met either by their share of the interstate revenue pool or by their portion of the state toll revenue pool must be met by their local service tariffs. Division of revenues among the Bell System operating companies proceeds in a very similar fashion.[29]

The present system of separations and settlements, involving a high degree of rate averaging, has come under increasing attack recently. In 1969 the FCC authorized competitive entry into the domestic private line field.[30] Since then, the posture of the Commission has generally been to encourage competition. Competition challenges the present system of rate averaging. The economies of scale of high density trunk routes presently support not only low density routes, but also local services. If OCC's are allowed to sell long distance service over high density routes without analogous responsibilities to the nationwide rate pool, then it seems fair that the telephone industry should be allowed to compete by pricing at the actual cost for each route. There is considerable impetus in Congress to resolve the dilemma through legislation.[31]

The momentum today seems toward introducing more competition into the telephone industry. This may imply a corresponding movement toward pricing services at their actual cost. However, the joint cost ambiguity of local plant continues to make ascertaining actual costs of long distance service difficult. Also, the industry tradition of supporting for policy reasons high cost services still has force. For example, there are pressures to include Hawaii, Alaska, Puerto Rico and the Virgin Islands in the interstate toll rate averaging scheme.[32] The next section suggests that it may be possible to price services to more nearly reflect the actual cost of each service, and yet still allow the cost averaging implicit in a uniform national distance-insensitive telephone rate structure.

III. FACTORS TENDING TOWARD THE POSTALIZATION OF TELEPHONE RATES

A. Historical Analogy to Postal Rates

There are some interesting analogies between consideration of "postalization" of telephone rates today and the original "postalization" of post rates in Britain a century and a half ago. In 1836 Britain had a postal rate system that looked remarkably like our present telephone toll rate structure. The rate for carrying a letter increased dramatically with the distance it was carried. A reformer named Rowland Hill (later knighted for his efforts) took it upon himself to restructure the postal rate system.

Sir Rowland determined:

> [F]irst, that the cost of conveying a letter between post town and post town was exceedingly small; second, that it had but little relation to distance; and thirdly, that it depended much upon the number of letters conveyed by the particular mail; and as the cost per letter would diminish with every increase in such number, and as such increase would certainly follow reduction of postage, it followed that, if a great reduction could be effected, the cost of conveyance, per letter, already so small, might be deemed absolutely insignificant.[33]

Sir Rowland published his assertions in a pamphlet, and despite resistance from the Post Office within two and a half years the change was underway. There was great public support for the idea; Sir Rowland reports that in 1839 there were some 2000 petitions to Parliament in favor of the reform.[34] In addition to Sir Rowland's economic arguments some contemporary supporters made moral arguments in favor of the reform: the morals of the entire country would be improved by increased correspondence between parents and children, friends across the country, and the like.

Today the postal rate structure is itself increasingly under attack.[35] The distance-insensitive nature of the first class rate structure seems relatively uncontroversial, however.

Much of Sir Rowland's argument seems persuasive today if applied to the telephone industry. The following discussion explores these analogies, as well as factors peculiar to the telephone industry, and their influence on a move toward a uniform national distance-insensitive telephone rate structure.

B. Factors Within the Telephone Industry

The purpose of this section is to make the postalization of telephone rates seem plausible. It is not intended to be a rigorous proof that postalization is inevitable, or even that it is probable. It will be sufficient to show that postalization is merely a possible future.

1. Economic Considerations

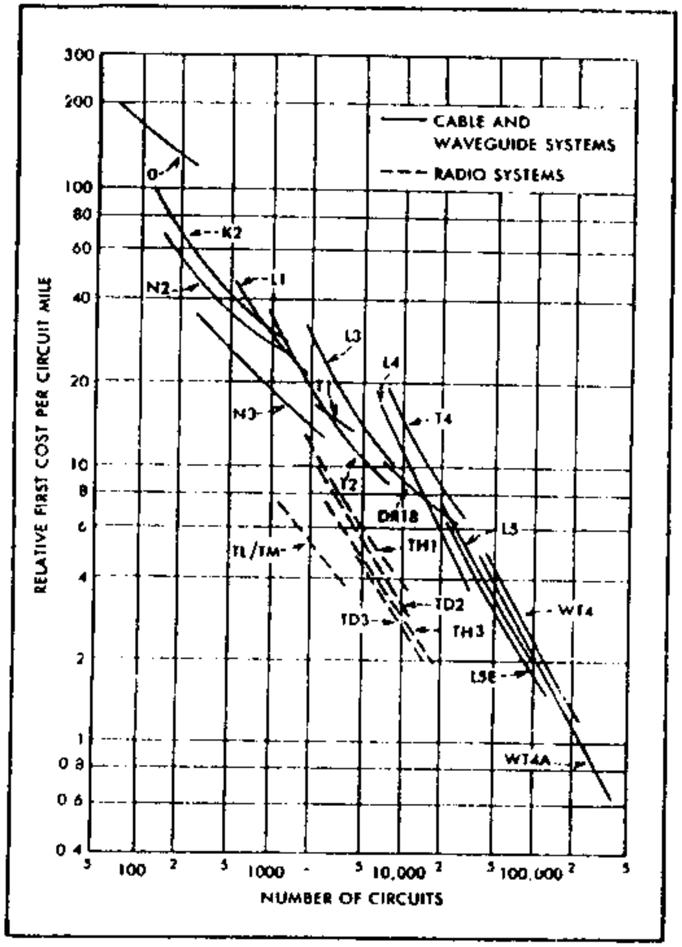
Sir Rowland's first assumption was that "the cost of conveying a letter from post town to post town was exceedingly small." The average cost of transmission of a telephone call as a portion of the total cost of the call can be estimated by comparing the investment in transmission facilities to the total investment in all telephone plant. In 1976 investment in transmission facilities accounted for only 28.8 percent of the total telephone plant. Perhaps more significant is the historical trend toward decreasing transmission investment as a proportion of total investment. Transmission facilities from 1943 to 1976 have decreased from about 45 percent of total investment to about 30 percent.[36]

Sir Rowland's second assumption was that transmission costs "had but little relation to distance." Telephone transmission technology may increasingly reflect this characteristic. The cost of long distance trunks provided by satellite, for example, is completely independent of distance.[37] The economies of scale enjoyed by high density transmission facilities have a greater impact on the average call. With present technology as the number of circuits on a transmission facility increases from roughly one to 200,000 the relative cost per circuit mile drops by a factor of approximately 200 to one.[38] Evolving technologies, such as fiber optics, seem to promise continuing cost reductions for high density routes.[39] While this does not translate directly into Sir Rowland's assumption that transmission costs bear little relation to distance, the hierarchy of long distance network routing implies it. The longer a toll call must travel, the more likely it is to be switched by the network through a high density route.[40] Thus increased distance may not imply significantly increased transmission costs, since there may be correspondingly increased access to economies of scale.

Sir Rowland's final assumption was that decreased prices of postal service would bring about increased demand that in turn would allow realization of economies of scale. The economies of scale of telephone transmission facilities have just been discussed. Estimates of price elasticity in the telephone industry vary significantly.[41]

A comprehensive analysis of the interaction of new technologies, potential economies of scale, and price elasticity of telephone service is far beyond the scope of this paper. However, at least one recent study has concluded that "a simple nationwide pricing scheme which incorporates peak load and usage-sensitive pricing and toll rates which are lower than present levels and distance-insensitive" might be advantageous.[42]

Figure 2.



LEGEND		
Bell System Code	Transmission Vehicle	Range
DR	Digital Microwave Radio	Short
K	Cabled Wires	Long
L	Coaxial Cables	Long
N	Cabled Wires	Short
O	Open Wires	Short
T1	Digital Cabled Wires	Short
T2	Digital Cabled Wires	Long
T4	Digital Coaxial Cables	Long
TD,TH	Microwave Radio	Long
WT	Waveguide	Long

Figure courtesy of Harvard Program on Information Resources Policy.

Telephone Cost and Price Trends

Cost trends for short- and long-haul transmission are down while carrying capacity is up, both by several orders of magnitude. Each of the vehicles illustrated here is capable of carrying simultaneously many conversations or other types of information. This includes the "O" system that improves on the classical open wires. The increase in the handling capacity of the several vehicles represent developments over time as well as technical improvements. Line termination, switching and personnel costs are among the additional elements that enter into the cost of complete telecommunication systems. Present cost proportions and price patterns are such that a pair of wires carrying but one conversation is still generally the vehicle for local conveyance from an individual telephone toward the nearest exchange, where many conversations heading the same way are bundled for further short or long haul.

Source: O'Neill, Eugene F., "Radio and Long-Haul Transmission", Bell Laboratories Record, January 1975, p. 55.

Postalization of telephone rates could incorporate both peak load pricing and usage-sensitive pricing. An assumption behind these pricing techniques is that the marginal cost of a telephone call is dependent upon the time of day and the duration of the call, perhaps more than upon the distance of the call.[43] If so, postalization could employ both the concept of marginal cost pricing and cost averaging.

Distance-insensitive pricing becomes more economically desirable as the incremental increase in cost attributable to the increased distance of a call nears the incremental cost of providing facilities to record the destination of a call and compute a distance-sensitive price. When the administrative cost of billing exceeds the marginal cost associated with the distance of call, it becomes economically unreasonable not to move to distance-insensitive pricing.

2. Traditional Public Policy Goals

Traditionally, the telephone rate structure has sought to support services for policy reasons that by economic standards should not be supported, while internalizing to within the industry the cost of such support.

Since the late 1930's the FCC has pursued a policy of "equal charges for equal service" in interstate toll rate making. The FCC determined that calls of equal distance reflected equal service, regardless of the costs associated with the provision of that service. This policy led to the principle of nationwide rate averaging in interstate toll rate making.[44]

Universal service has been another primary policy goal of the telephone industry and its regulators. Provision of basic telephone service in certain instances, such as remote rural areas, may be very expensive. Universal service implies financial accessibility to telephone service for all consumers. There are a number of ways financial accessibility can be ensured.

including direct subsidy from the general tax revenues. However, if some substantial portion of the cost of such policy goals is to be internalized to within the telephone industry, then this implies some degree of cost averaging.

Thus policy goals promote significant cost averaging in the telephone rate structure today. High density trunk routes support low density routes through nationwide interstate toll rate averaging. The interstate toll system supports local and intrastate toll service through the jurisdictional separations procedure.

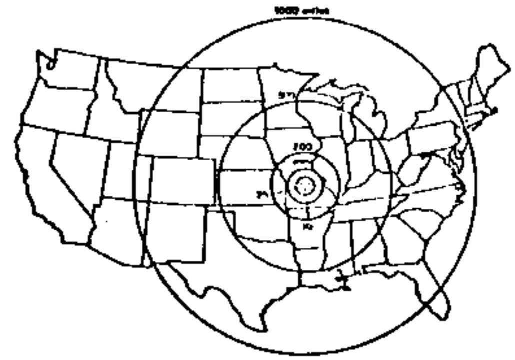
There may also be public policy reasons for extending this tradition of rate and cost averaging to the postalization of telephone rates. It might encourage and facilitate interstate commerce. Postalization might allow more industry to locate in rural areas by decreasing the telephonic distance from the rural locations to urban centers. Perhaps, as when Sir Rowland introduced the idea in England, people will just decide that they like the idea.

3. Shifting Social Perceptions

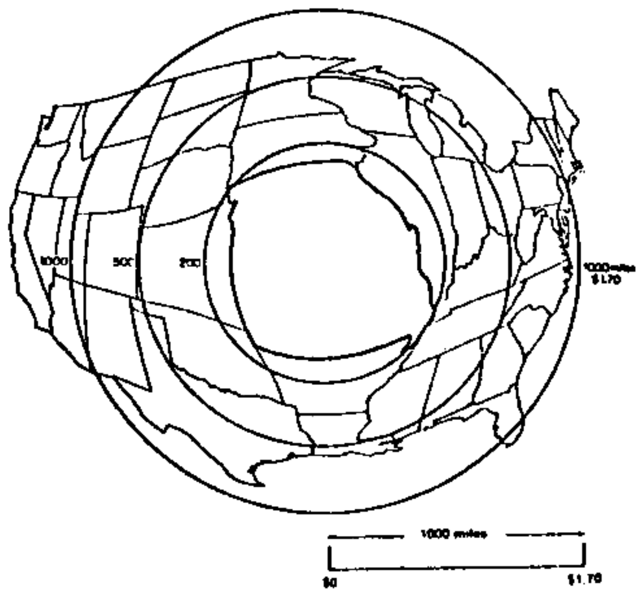
Decreasing long distance rates may reflect and encourage changing social perceptions.[45] Reduced communications costs have brought the country closer together. Figure 3 demonstrates the impact of changing toll rates on the telephonic distance from Jefferson City, Missouri to outlying points in the United States. California and New York are almost as close, in term of communication costs, as points within the state.

The momentum toward compressing telephonic distance may also been seen in the growth of Wide Area Telecommunications Service, WATS. WATS service is distance insensitive within service bands provided for a flat rate. WATS revenues as a percentage of total toll revenues have gone

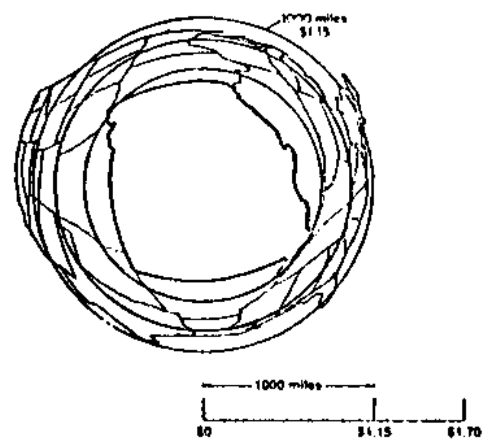
Figure 3.



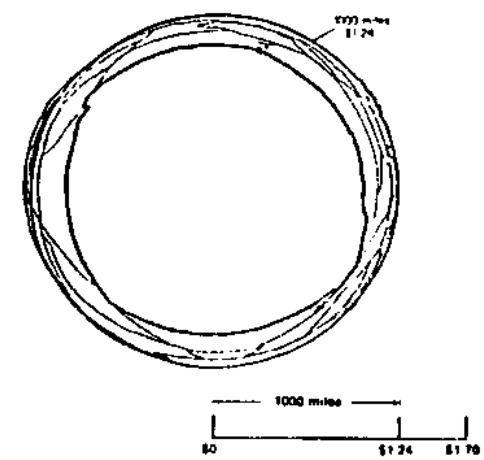
Geographic United States
(a)



1957
(b)



1971
(c)



1977
(d)

Telephonic United States

The Geographic and Telephonic United States Viewed from the Center of Missouri

All telephone calls based on 3-minute, day rates. 1977 rates are customer-dialed; 1971 interstate is customer-dialed; 1971 Missouri is station-to-station; and 1957 rates are station-to-station.

Source: AT&T, December 1978 and AT&T, Federal-State Joint Board, Request No. JB-50, April 1, 1977. National Association of Regulatory Utility Commissioners. Long Distance Message Telephone Rates, Washington, D.C., June 30, 1971, Table 25, p. 66 and Table 51, p. 79.

Figure courtesy of Harvard Program on Information Resources Policy.

from 1.8% in 1965 to 3.8% in 1973 to 6.25% in 1976.[46] This reflects a growth of approximately 350% in 11 years.

As telephonic distance shrinks, the concept of local service grows.[47] Local calling areas have become increasingly complex, may involve more than one operating company, and may even serve areas in more than one state.[48]

The growing WATS market reflects at the national level the tendency toward cost averaging and uniform rates for long distance service desired by a growing number of telephone customers. Expanding local area service reflects an increasing number of telephones accessible to some telephone customers for a uniform, flat rate. Indeed, the growing local calling areas are increasingly causing toll/local rate disparities reminiscent of the intra/interstate toll disparity of years gone by.[49] If one lives at the edge of a local calling area, it may be cheaper to call 25 miles across town than 2 miles out of town. As once before, this may create political pressure for a restructuring of rates.

The Bell System seems to have recognized some benefit in rate uniformity _per se_. With the recent introduction of a new data service Bell has applied for the same tariffs for all its operating companies nationwide, in every state jurisdiction. This is a first for the Bell System.[50] The motivation for this push toward uniformity may be a perception that the business community will find it attractive.

At least some Bell operating companies have determined from market surveys that the business community that they serve is expanding its sense of "local markets" beyond the limitations of the local calling area. New England Telephone Co., for example, is now introducing a new Regional Business-to-Business Yellow Pages covering twenty-three local exchange areas.[51]

It therefore seems that some consumers and many businesses may already be receptive to the idea of postalization. The growing local service areas suggest that consumers enjoy uninhibited access to large calling areas. The growth in WATS service and regional yellow pages suggests businesses would appreciate the marketing potential postalization would offer.

4. The Impact of Competition

Thus the economics, tradition, and social impact of the telephone industry suggest that the future postalization of telephone rates is plausible. However, Sir Roland was dealing with a simple market structure dominated entirely by a government monopoly when he proposed uniform distance insensitive postal rates in Britain. The telecommunications market in the United States is today much more complex than that. The FCC has made a positive commitment to competition wherever possible. The presence of competition makes postalization seem unlikely, at least at first glance.

Competition within the industry has both economic and political ramifications on postalization. The economic impact of Other Common Carriers (OCCs) would seem to be a pressure to deaverage telephone rates. OCCs compete with the Bell System in providing long distance service, generally over high density routes. Fairness may demand that traditional suppliers be allowed to compete by pricing at their actual cost. Thus one might expect lower priced service for high density routes, and higher rates for low density routes.

However, the introduction of competition into the telephone market and the potential deaveraging of some aspects of telephone rates may even contribute to the momentum toward postalization. If the contribution of toll services to local services is decreased, as many now advocate, one would anticipate an increase in the rates for local services and a corresponding decrease in toll rates. This would reduce the present rate disparity between toll and local calls, and would make the elimination of this increasingly artificial distinction less dramatic.[52]

The political impact of competition seems equally mixed. Consider what mandatory postalization, applicable to all carriers, including the OCCs, would imply. All OCCs would be required to conform to the uniform postalized rate. This would invite classic cream skimming: the OCCs would carry traffic over high density routes for the uniform rate, which of necessity would more than adequately compensate them for their efforts, given the averaging between high and low density routes implicit in postalization. This overcompensation can be corrected by imposing a strict regime of regulation on all common carriers, and requiring that all contribute to national rate averaging through some device for capturing excess profits.

But this runs contrary to two strong political trends in the industry. First, there is obviously a current perception that price competition is a good thing.[53] Postalization cuts directly against that ideal; postalization requires rate averaging between high and low density routes, and a uniform national rate that is the opposite of price competition.

More significant, however, may be the strong movement toward deregulation of non-dominant carriers, now most apparent in the Competitive Common Carrier proceeding.[54] More and more companies have been lured into the telecommunications industry by the vision of decreasing governmental regulation, not just in terms of deregulated rates, but also in terms of a decreased regulatory burden on doing business. In part this movement toward deregulation of non-dominant carriers may be due to an increasing recognition that the FCC cannot effectively regulate the Bell System, much less all the OCCs in a burgeoning industry. Postalization will not happen overnight. It is inevitable that significant political momentum will be established in the direction of deregulation of OCCs prior to any efforts toward postalization. Precedent has force. Thus a mandatory postalization scheme that incorporates the OCCs may well be implausible since it would require a significant increase in the regulation of non-dominant carriers.

Suppose then that one deals with this problem by postulating mandatory postalization of only the basic telecommunications network. Both the Competitive Common Carrier proceeding and Computer Inquiry II distinguish between dominant and non-dominant carriers in the type of regulation they impose; postalization might do the same. As it turns out, the basic service providers, like AT&T and the independent telephone companies, might like the idea of postalization and lobby for it. Thus the basic network could be subject to mandatory postalization, while the OCCs could remain essentially deregulated.

Suppose a uniform distance insensitive rate of 10 cents a minute. Who would pay 10 cents a minute to access an OCC system that offers "long distance" equivalent service, when the call to one's ultimate destination is also only 10 cents? That is why the dominant carriers, like AT&T, might lobby to have such a system implemented through legislation or agency action. Postalization could thus injure a significant market for the OCCs, and without the imprimatur of legislative or regulatory approval, would raise antitrust problems.

Perhaps the OCCs could provide "toll free" access to customers; basic service providers might be required to offer such services to the OCCs. Of course, to be competitive, they would have to charge less than the uniform rate of 10 cents a minute for their services. That seems odd: a "long distance" call over the OCC network would thus be less expensive than a "local" call over the basic network.

If competition in local terminations develops, that too would alter the picture. OCCs may then lead the way in offering postalized rates, if the economic and social pressures discussed earlier indicate a genuine consumer interest in postalization. Some network service providers (Graphnet, for example) already have postalized rate structures in effect.

Lest this discussion seem far-fetched, Western Union has already implemented a postalized rate structure for its TWX and telex service.[55] The basic Telex and TWX offerings provide for the transmission of typewritten and data communications between the stations of subscribers to these services. There are approximately 130,000 subscribers to the combined services.[56] Western Union argued that since distance is no longer a significant cost-causative factor, distance sensitive rate structures are not warranted. OCCs in competition with Western Union opposed the postalization of TWX and telex rates. They argued that there was indeed a distance sensitive element of the service. They also argued that postalization was anticompetitive, for the same reasons outlined in the discussion above. As of this time, the Commission has not been receptive to the OCCs' arguments.[57]

Thus both the economic and the political impact of competition upon any movement toward postalization is complex. Should Congress eventually be persuaded to enact legislation providing for the postalization of telephone rates, it would represent a significant change in the structure of the regulation of the industry. The remainder of the paper will assume a commitment to postalization, and will assume the postalization of "basic" telephone services, with network accommodation for competition to be provided through either a network access fee or some similar arrangements.

Given this assumption, whose plausibility but not likelihood is outlined in the preceding discussion, the following analysis considers the limits the constitutional principle of federalism places upon the methods available to pursue such a goal. Postalization would seem to imply nationwide pooling and averaging of all revenue. Nationwide rate setting would significantly deemphasize the role of the state regulator. Depending upon the extent of federal regulation required to make such a system work, it might mean the virtual preemption of all state regulation. This raises not only formidable political questions, but also questions of federalism and the role of the states in our constitutional form of government.

IV. APPROACHES TO POSTALIZATION OF TELEPHONE RATES

A. Under the Communications Act of 1934

A uniform national telephone rate structure could not be implemented by the Federal Communications Commission under the present language of the Communications Act. The control of intrastate rate setting is reserved to the states. A uniform national rate structure would therefore depend upon the cooperation of all the states, and that cooperation could not be ensured.

The language of the Communications Act of 1934 is a testimony to Congressional sensitivity to state sovereignty. Section 2(b) of the Act reads in part:

> [N]othing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier... .[58]

Another portion of the Act similarly restricts the Commission from jurisdiction over "wire, mobile, or point-to-point radio telephone exchange service, or any combination thereof, even though a portion of such exchange service constitutes interstate or foreign communication, in any case where such matters are subject to regulation by a State commission or by local governmental authority."[59]

North Carolina Utilities Commission v. FCC I and II[60] directly interpret these provisions reserving intrastate regulation to the states. These cases considered an FCC ruling that state regulatory commissions cannot restrict or regulate interconnection of customer equipment to the customer's individual station and line in any way that conflicts with the Commission's regulation of the same subject matter.[61] This in essence extended FCC jurisdiction to include the seemingly local concern of regulating the termination of a subscriber loop. The court said that it had "no doubt that the provisions of [the Communications Act] deprive the Commission of regulatory power over local services, facilities and disputes that in their nature and effect are separable from and do not substantially affect the conduct or development of interstate communications."[62] The court ruled, however, that "the Commission's declaratory statement of its primary authority over the interconnection of terminal equipment with the national telephone network is a proper and reasonable assertion of jurisdiction conferred by the Act."[63] Most local plant facilities are used jointly in the provision of both local and interstate toll service. Restriction of state regulatory authority to only those matters "in their nature and effect...separable from...interstate communications" would severely limit the scope of state regulation protected by the Act.

The foundations of the court's argument would not allow its extension to federal establishment of a uniform rate structure under the Act, however. First, the court argues that the restrictive provisions of the Act were primarily intended merely to reserve to the states authority to regulate local telephone rates and charges.[64] Second, the court asserts that the FCC has interpreted the Act for 30 years to allow federal control over terminal equipment; Congress must have been aware of this and would have taken action to prevent it if appropriate.[65] These arguments would cut against any federal attempt to establish a uniform rate structure. Such an attempt would run afoul of what the court found to be the primary intent of the restrictive provision of the Act, the reservation to the states of authority over local telephone rates. It would also be contrary to over 30 years of consistent regulatory practice under the Act.

The courts may be quite liberal in construing the Act to allow broad powers to the FCC over new and evolving areas of regulation. The long tradition of separations and settlements as well as the clear language of the Act and its legislative history would seem to foreclose any FCC attempt to pursue postalization, however.[56]

Thus, should there be substantial support in Congress for the concept of a uniform national distance-independent telephone rate structure that would involve the entire national system, including local rates, new legislation would be required. The states have traditionally had wide discretion in regulating their local telephone service. Postalization of all telephone rates, including local rates, implies a substantial readjustment of the traditional allocation of regulatory responsiblity. This reform would therefore raise substantial questions of the appropriate roles of the state and federal governments within our constitutional system.

The following pages discuss several potential avenues for new legislation to implement postalization. The first approach considered is federal establishment of a nationwide rate system with compulsory state enforcement of that system. Analysis of this approach suggests that the courts would probably find such compulsory state enforcement of federal policy to be an unconstitutional intrusion upon state sovereignty.

Federal preemption of all telephone regulation is discussed next. This implies the elimination of the state regulatory bodies. The reaction of the courts to such legislation is unclear. However, another powerful safeguard of the constitutional role of the states is the political process itself. An overview of the legislative history of the Communications Act of 1934 and of testimony on bills presently under consideration by Congress suggests that the state regulatory commissions will strenuously defend their roles. Thus the role of the states may here be protected from federal preemption through the political process itself.

Finally, the establishment of a uniform rate system through the use of a minimum or voluntary federal rate structure is considered. The FCC or a federal-state joint board would establish a uniform national rate. This might represent a minimum rate for the states, leaving each state the option of setting higher rates. If pooling and division of revenues guaranteed a fair rate of return for each telephone company, political pressure might serve to ensure that the national minimum rate was in effect the national uniform rate. Alternatively, participation in the uniform rate structure could be optional with each state. Support from the division of the national revenue pool would then be contingent upon a state's participation in the program.

B. Compelled State Cooperation

Congress could seek to institute the postalization of telephone rates through legislation that would compel state enforcement of federal policy. For the moment, assume that such new legislation would be an exercise of Congressional power under the Commerce Clause. This assumption will be explored subsequently in the discussion of federal preemption of telephone regulation.

Congress might direct the FCC to establish a uniform national distance-independent rate structure. Congress would then require that the states establish regulatory bodies (or use those already in existence) to enforce the local element of the nationally established rate. All national revenues could be pooled and distributed according to costs in a rough extension of the way separations and settlements work today. The following analysis will focus not on the details of how such legislation might be implemented, but rather on the narrow issue of coercing state enforcement of federally established policies and regulations.

Compelling state enforcement of federal regulations seems to infringe upon state autonomy by depriving the state of its sovereign power to determine what services it will offer its citizens and the manner in which those services will be delivered.[67] The following discussion will provide a brief historical overview of the development of Commerce Clause doctrine. It will then focus on a recent case that suggests the Supreme Court might find legislation requiring state enforcement of a federally established uniform rate structure to intrude unconstitutionally upon the sovereignty of the states.

1. Congressional Action Must be Affirmatively Authorized by the Constitution

Congress cannot establish a uniform telephone rate structure unless to do so is within its powers affirmatively authorized by the Constitution. Congressional authority must either be grounded in a specifically enumerated power in the Constitution or implied in Congress' authority to "make all laws which shall be necessary and proper for carrying into execution" an enumerated power.[68]

In 1819 The Supreme Court stated:

> This government is acknowledged by all to be one of enumerated powers. The principle, that it can exercise only the powers granted to it, [is] now universally admitted. But the question respecting the extent of the powers actually granted, is perpetually arising, and will probably continue to arise, as long as our system shall exist... [69]

Regulation of the telephone industry has traditionally been enacted under the Commerce Clause. Congressional authority under the Commerce Clause has historically been very broad. In 1976, however, the Supreme Court in National League of Cities v. Usery expressed a new willingness to protect essential attributes of state sovereignty from federal intrusion under the Commerce Clause.[70] This may affect attempts to legislate postalization of telephone rates. The difficulties in interpreting National League of Cities can be appreciated only when it is seen in context with the development of other Commerce Clause cases.

2. A Brief Historical Overview of the Development of Commerce Power Doctrine

In 1824 Chief Justice Marshall in Gibbons v. Ogden sketched an expansive view of Congressional power under the Commerce Clause:

> The subject to which the power is next applied, is to commerce "among the several States." The word "among" means intermingled with. A thing which is among others is intermingled with them. Commerce among the States, cannot stop at the external boundary line of each State, but may be introduced into the interior.[71]

The court cautioned, however, that the "completely internal commerce of a state, then, may be considered as reserved for the State itself."[72]

Congress did not begin attempting significant nationwide regulatory activity until the late nineteenth century.[73] Despite the Marshall Court's liberal interpretation of the extent of Congressional power under the

Commerce Clause, the Supreme Court from the turn of the century until the late 1930's adopted a much more restrictive view of the authority of Congress under the Commerce Power.[74]

Even in the midst of this most restrictive period in the Court's interpretation of the Commerce Power, however, the Court approved significant control over local railroad rates by the Interstate Commerce Commission. In 1914 in the Shreveport Rate Case the Court approved ICC regulation of purely intrastate rates where it was necessary to prevent discrimination against interstate commerce.[75]

In the late 1930's the Court returned to the expansive view of Congressional Commerce Clause powers heralded by Chief Justice Marshall's early decisions. Indeed, from 1936 until National League of Cities in 1976 the Supreme Court did not rule any Congressional regulatory activity unconstitutional due to its impact on state or local governmental autonomy.[76] The following sampling of cases suggests the willingness of the Court to allow Congress to regulate essentially local affairs under the guise of interstate commerce.

In 1937 the Court affirmed the validity of the National Labor Relations Act of 1935, which had broad economic impact. The Court stated:

> Although activities may be intrastate in character when separately considered, if they have such a close and substantial relation to interstate commerce that their control is essential or appropriate to protect that commerce from burdens and obstructions, Congress cannot be denied the power to exercise that control.[77]

The Court cautioned, however, that "[u]ndoubtedly the scope of the power must be considered in the light of our dual system of government and may not...effectually obliterate the distinction between what is national and what is local."[78]

A few years later, the Court upheld restrictions upon an Ohio farmer's practice of growing a small acreage of winter wheat, a seemingly very local concern. The Court held that "even if the appellee's activity be local and though it may not be regarded as commerce, it may still, whatever its nature, be reached by Congress if it exerts a substantial economic effect on interstate commerce."[79]

In 1964 in upholding Title II of the Civil Rights Act the Court approved a Congressionally mandated prohibition of racial discrimination by local hotels and small restaurants.[80] Congress based its extension of power to such a local level on a legislative finding of the interstate impact of racial discrimination. The Court accepted this. The Court stated that "the power of Congress to promote interstate commerce also includes the power to regulate the local incidents thereof, including local activities in both the States of origin and destination, which might have a substantial and harmful effect upon that commerce."[81]

The apparent willingness of the Court to defer to Congressional judgment in determining the appropriate exercise of the Commerce Clause power would seem to indicate that a federal program implementing a uniform national telephone rate structure would be well within accepted bounds. The integrated nature of the national telephone network makes it inevitable that local telephone regulation has a significant impact on the interstate aspects of the network. However, a strong counterpoint to the harmony of these earlier cases has been set by National League of Cities v. Usery.[82] It suggests that attempts to legislate a national uniform telephone rate structure by compelling state enforcement of federally established policy may impermissibly violate the sovereignty of the states.

3. National League of Cities v. Usery

In 1976 the Supreme Court in National League of Cities v. Usery (hereinafter "NLC") considered a Congressional extension of the minimum wage and maximum hour requirements of the Fair Labor Standards Act to state employees.[83] The Court asserted that it "has never doubted that there are limits upon the power of Congress to override state sovereignty, even when exercising its otherwise plenary powers to tax or to regulate commerce."[84] The Court determined that the State's power to decide the wages to be paid to those whom it hires to perform governmental functions, as well as the hours to be worked, overtime considerations, etc., is a function essential to the separate and independent existence of the State. The Court found that the Act imposed substantial costs upon the states, and displaced "state policies regarding the manner in which they will structure delivery of those governmental services which their citizens require."[85] Accordingly, for the first time in forty years the Court gave effect to its concern for federalism by holding a Congressional enactment under the Commerce Power to unconstitutionally "displace the States' freedom to structure integral operations in areas of traditional governmental functions" and therefore not to be "within the authority granted Congress by [the Commerce Clause]."[86]

The Court distinguished the unconstitutional extension of power as an "exercise of congressional authority directed not to private citizens, but to the States as States," from "the authority of Congress to enact laws regulating individual businesses necessarily subject to the dual sovereignty of the government of the Nation and of the State in which they reside."[87] The Court also limited the State's protection to areas "that the States have regarded as integral parts of their governmental activities," excluding such proprietary acts as running a railroad engaged in common carriage in interstate commerce.[88]

It is difficult to ascertain the scope of the Court's decision. The challenged enactment did not seem to seriously threaten the existence of the states as states. This implies that certain state functions are constitutionally protected, but it is hard to predict what "traditional governmental functions" are constitutionally reserved to the states in light of the previous forty years of decisions. Professors Michelman and Tribe have suggested that the line to be drawn must be based on the rights of individuals to basic government services provided by the states.[89] Thus the state's protected "sovereignty" stands for "nothing more nor less than the state's role of providing for the interests of its citizens in receiving important social services."[90] Other commentators have found the key to the Court's decision to lie in its respect for the state's right to control expenditures from its treasury, at least when those expenditures are for public services or activities which involve traditional or integral governmental functions.[91]

4. The Impact of National League of Cities on Compelled State Cooperation

There is no close precedent supporting an attempt by Congress to mandate state enforcement of a federally established national telephone rate structure.[92] Does National League of Cities forbid it? Apparently the regulation of local telephone rates must be a traditional and integral function of state government for the strictures of National League of Cities to apply.

The important traditional services identified by the Court as protected in National League of Cities all portray the state in its role as a direct provider of services. The Court includes fire prevention, police protection, sanitation, public health, and parks and recreation. The Court also implicitly includes the operation of public schools, hospitals and similar public health care institutions within the category of integral governmental functions[93] The only state activities clearly not protected are those considered business enterprises. These include running a railroad engaged in interstate commerce,[94] engaging in the production of oil and gas,[95] and operating a municipal power company.[96]

As Prof. Stewart points out, "The justifications suggested by NLC and Professors Michelman and Tribe for recognizing a special constitutional place for traditional state and local government services extends [sic] as well to at least some of the regulatory activities of the administrative state."[97] The regulatory activities of the state can be some of the most important services it provides its citizens. Even the roles specifically identified by the Court as protected may include an element of regulation. Fire prevention must include enforcement of fire code regulations. Police protection is itself merely a structure for regulating private conduct. Sanitation and public health services may include not only waste disposal but also health inspection of public restaurants.

At least one Court of Appeals seems willing to accept some regulatory activities of the state as traditional or integral governmental functions. The Ninth Circuit, while conceding that the regulation of traffic may sometimes involve federal interests, has held that "there is little question that the licensing of drivers constitutes 'an integral portion of those governmental services which the states and their political subdivisions have traditionally afforded their citizens.'"[98] The regulation and provision of local telephone service are important social functions, seen as early as 1931 to be "in point of law and fact and tradition essentially local problems."[99] Indeed, the tradition of local or state regulation of local telephone service goes back to the birth of the industry.

The telephone system intimately affects the daily lives of citizens. It is an important part of the people's everyday routine, just as are the parks, public schools, and sanitation services provided by the local governments. In an emergency, the phone system can be an indispensible link between people in trouble and the police, fire department, or hospitals. For the elderly or invalids in the community telephone service may be their only contact with the outside world. Thus the regulation of local telephone rates is arguably an essential governmental function traditionally provided by the states.

Congressional legislation requiring state enforcement of federally established telephone rates seems a regulation not merely of the industry, but also of the state public utility commissions and the ways in which they function. Requiring state funds to be expended to further federally dictated policy goals may intrude upon a state's control of its treasury at least as much as minimum wage and maximum hour provisions applied to state employees.[100] If the regulation of local telephone service is an integral and traditional function of local and state government, Congressionally mandated state cooperation in implementing postalization of telephone rates seems in danger of being invalidated by the courts.

C. Federal Preemption of All Telephone Rate Regulation

Congress could attempt to institute the postalization of telephone rates by extending the mandate of the Federal Communications Commission to include authority over local telephone regulation. This would in effect eliminate the role of the state regulatory agencies. Federal preemption of all industry regulation would be a radical change from the present regulatory structure. There may be a variety of less extreme options available to Congress. Note, however, that even limiting federal preemption of state authority to only that necessary to accomplish postalization, state regulatory authority will be eviscerated. There is really no authority that can be retained by the states in the nature of consumer protection, billing procedures, disclosure regulation, and the like that will not have an impact on the operation costs of the company. The federal authority must therefore be involved, since the nationwide system will help bear those added costs through the cost and rate averaging characteristics of the postalized rate structure. Limiting federal preemption to the regulation of rates and compelling the remaining state regulatory functions to conform to the necessary federal guidelines begins to resemble coerced state enforcement of federal policies.

The following discussion will focus on a complete federal preemption of local telephone regulation. Analysis of this extreme position will illuminate the constraints that must guide the selection of a more moderate approach.

Like compelled state cooperation, federal preemption of telephone regulation challenges a traditional role of the states. Under the mainstream of Commerce Clause decisions prior to National League of Cities, the impact of local telephone rates on the national system would justify exertion of federal authority. National League of Cities may make this less clear. If authority for Congressional action could be found in constitutional powers other than the Commerce Clause, any potential problems raised by National League of Cities could perhaps be avoided.

The courts are not the only constitutional protectors of states' rights, however. The political system itself is a powerful safeguard against intrusions upon state sovereignty. It was this mechanism which shaped the Communications Act of 1934, and it remains influential today.

1. The Impact of National League of Cities on Federal Preemption of Telephone Regulation

The imposition of a national uniform telephone rate structure would involve Congress in the regulation of what has traditionally been viewed as a local concern. This raises the central question of Commerce Clause doctrine: How far may Congress go in regulating intrastate affairs to effectuate national policy? In this case, would federal preemption of all telecommunications regulation exceed the limits which NLC indicates the Court is willing to enforce?

Prior to National League of Cities the Court was generous in approving Congressional findings of the impact on interstate commerce of local activity. The impact of local rates upon the interstate telephone system is unquestionable. Every interstate call involves the local exchange facilities in the originating and terminating states. The present intercompany settlement and jurisdictional separations procedures emphasize the financial interdependence of the system. There seems little question that under the thrust of cases prior to NLC, federal preemption of local telephone regulation would be beyond judicial reproach.[101] After NLC, a scholar could still assert: "A wealth of precedent attests to the authority of the federal courts and Congress to invalidate or preempt state regulation and taxation of private activity that affects interstate commerce."[102] Yet NLC may suggest some judicially enforceable limitations on this authority.[103]

The Court in National League of Cities distinguished those cases in which it had "upheld sweeping exercises of authority by Congress, even though those exercises preempted state regulation of the private sector," from the limitations it sought to impose upon "a similar exercise of congressional authority directed not to private citizens, but to States as States."[104] Federal preemption of state regulatory authority over local telephone rates appears within the bounds of prior cases. Thus the NLC Court would seemingly find no fault with it.

Yet the logic of NLC defies such facile dismissal. It is difficult to determine what essential attributes of the State the Court is protecting in National League of Cities. It is not merely state control over its fisc. Expenditures from the state treasury associated with proprietary acts such as running a railroad are beyond the protection of NLC.[105] The language of the case also discourages this narrow interpretation: "Quite apart from the substantial costs imposed upon the States and their political subdivisions, the Act displaces state policies regarding the manner in which they will structure delivery of those governmental services which their citizens require."[106] It seems the role of the state as a provider of governmental services is being protected. The fiscal integrity of the state is important because it is essential to the state's effective performance of its role as a provider of services.[107]

The previous discussion argued that the regulation of local telephone service is a traditional and integral governmental service, and therefore protected.[108] Preemption of a traditional governmental service may be less of an intrusion upon state sovereignty than compelled state cooperation in implementing federal policy. Preemption does not impose additional burdens upon the state, but rather relieves the state of a regulatory burden allowing it to use its resources to pursue other goals. Yet clearly the sovereignty of the states would be seriously undercut if Congress preempted a significant portion of those functions the Court has admitted to be essential to state sovereignty.

Justice Blackmun in his concurring opinion suggests that the Court "adopts a balancing approach, and does not outlaw federal power in areas...where the federal interest is demonstrably greater and where state facility compliance with imposed federal standards would be essential."[109] Yet why should the Court's balancing of federal and state interests be more satisfactory than that of Congress? Congress seems institutionally better suited for that type of political weighing of interests. Since the majority did not adopt Justice Blackmun's view, they apparently have something else in mind.

A recent Court of Appeals case asserts:

> NLC has been held to be limited to those situations where it can be shown that (1) a congressional enactment (in the exercise of commerce clause powers) operates to displace, regulate or significantly alter (2) the management, structure or operation of (3) a traditional or integral governmental function.[110]

If the regulation of a public utility is a governmental service, then federal preemption of local telephone regulation would seem to fall within the 6th Circuit's test. It is (1) a congressional enactment that displaces or significantly alters (2) the structure and operation of a (3) traditional state governmental function. However, the mere fact that a governmental service has traditionally been provided on a local level, as has local telephone regulation, should not be a constitutional bar to providing it on a federal level should that be more efficient or desirable. Nor should the fact that a new governmental service is not traditional deprive it of protection if it can be more effectively provided on a local level. To key judicial protection upon tradition is to freeze the development of state governmental innovation.[111]

A major problem in interpreting NLC as limiting Congressional authority to preempt all state telephone regulation is that such an interpretation seems inconsistent with the rich body of Commerce Clause jurisprudence prior to NLC.[112] Professor Stewart suggests that this inconsistency must lead to one of three conclusions: NLC is at odds with the traditional Commerce Clause cases and is therefore unsound, or NLC is at odds with the traditional line of cases, and the traditional cases must be revised in light of NLC, or finally that NLC is not in fact inconsistent with the prior cases. For example, in many of the prior cases supporting broad Congressional power under the Commerce Clause the state was not the party challenging the federal measures.[113]

Although the language of the Court's decision in National League of Cities suggests that federal preemption of local telephone rate regulation is acceptable to the Court, the logic of the case may be less certain. The real import of the case may be in signalling an increased willingness on the part of the Court to give effect to concerns of federalism.[114] Professor Tribe states that the "Courts' opinions have sounded such a note for several years, and the signals have recently become both louder and more frequent."[115] National League of Cities may indicate a new activism on the part of the Court with boundaries yet to be defined.

Complete resolution of the judicial response to federal preemption of state regulation of local telephone rates may be unnecessary. In drafting new legislation it may be sufficient to note potential problems and avoid them. Also, the Courts are not the only constitutional guardians of state sovereignty. The political process itself protects the principles of federalism. As subsequent discussion will show, there is a significant probability that federal preemption would not survive the political process. If that is correct, the judicial response to preemption is a moot point.

2. Alternative Sources of Congressional Authority

Before moving on to the political safeguards of federalism, it is worth pausing for a moment to consider one way around the uncertainty of National League of Cities. NLC is a Commerce Clause case. Congress might enact legislation preempting state regulation of local telephone rates under some authority other than the commerce power.[116] In fact, Congress has in the past utilized other authority for telephone regulation.

a. The Post Office and Post Roads Clause

The "postalization" of telephone rates naturally suggests that Congress might regulate the telephone industry under its Constitutional authority to "establish Post Offices and post Roads."[117]

In its Act of July 24,1866 to aid the construction of telegraph lines, Congress placed the authority for setting telegraph rates for government communications with the Postmaster General. In 1877 the Supreme Court affirmed this, saying, "The powers thus granted [by the Commerce Clause and the Post Office Clause] are not confined to the instrumentality of commerce or the post service known or in use when the Constitution was adopted, but they keep pace with the progress of the country and adapt themselves to the new developments of time and circumstance."[118] The Court also said, however, "It is not necessary now to inquire whether Congress may assume the telegraph as part of the postal service, and exclude all others from its use."[119] So the Court never clearly addressed whether Congress could indeed regulate the telegraph or telephone industry under the Post Office power. This option may now be foreclosed by the force of over a century of inertia.

b. The War Power Clause

Interestingly enough, the country has had a brief period of uniform national regulation of the telephone industry under the Postmaster General. Congress enacted this not under the authority of the Post Office clause, however, but under its War Power authority.

In the closing days of World War I the Postmaster General took over the telephone industry and established uniform rates for both interstate and intrastate calls, and asserted authority to set local rates as well. Congress in a joint resolution on July 16, 1918 authorized the takeover. On July 22, 1918, President Woodrow Wilson directed that "the supervision, possession, control, and operation of [the] telegraph and telephone system...shall be exercised by and through the Postmaster General." The act relied heavily upon analogy to the similar takeover of the railroads.[120] Although rates were not mentioned, the Postmaster General argued that the "power to operate necessarily implies the power to fix rates."[121]

Any insights to be drawn from this brief attempt to establish uniform rates are vague at best. Any similar effort today would not be taken under the War Powers, and surely would not involve a complete takeover of the industry. It is worth noting, however, that even in this extreme example of a complete industry takeover in a time of great crisis, Congress in its resolution specifically provided that "nothing in this act shall be construed to amend, repeal, impair, or affect existing laws or powers of the states in relation to taxation or the lawful police regulation of the several states."

If the federal system of telephone rate regulation were to be implemented under either the war powers or the post office and post roads powers of Congress, National League of Cities v. Usery would have no relevance.[122] The weight of history, if not of clear precedent, compels the conclusion that extension of federal regulation of the telephone industry would continue to be under the Commerce Power. Accordingly, NLC may still be important.

A major constitutional safeguard of state sovereignty is the political process itself. Although the theoretical underpinnings of this protection will be discussed with reference to Commerce Clause powers, its restraints would apply equally to attempted legislation under other powers of Congress. It may be this process that most seriously challenges federal preemption of traditional state regulation of local telephone rates.

3. The Political Safeguards of Federalism

The reluctance of the Marshall Court in Gibbons v. Ogden to judicially constrain Congressional exercise of its Commerce Power was based in part on the presumption that the restraints of federalism are political, not judicial:

> The wisdom and the discretion of Congress, their identity with the people, and the influence which their constituents possess at elections are, in this, as in many other instances, ...the sole restraints on which they have relied, to secure them from its abuse. They are the restraints on which the people must often rely solely, in all representative governments.[123]

The dissent in National League of Cities v. Usery, disturbed by the majority's "patent usurpation of the role reserved for the political process," begins by reiterating the admonition of the Marshall Court in

Gibbons v. Ogden that "the Constitution contemplates that restraints upon exercise by Congress of its plenary commerce power lie in the political process and not in the judicial process."[124] Indeed, for the four decades prior to NLC the political process and the structure of the political institutions seem to have been "the restraints on which the people must often rely solely."[125] Even after NLC, these political restraints may still be the primary safeguards of federalism.

The Tenth Amendment states: "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." This reflects a pervasive assumption throughout the Constitution of the interstitial nature of the federal government. The edifice of the national government has its foundation in the bedrock of the states; the underlying support of their laws is assumed. There are no clear or express restraints on the erosion of that bedrock, probably because its existence was so fundamental and unquestioned.

Since the protection of state sovereignty is not found in express limitations on Congress, that protection has instead been found in the political process and the institutional structure of Congress. The states have a central role in the selection and composition of Congress; both representatives and senators are chosen on a state by state basis. Even the president, the most "national" of our political officers, is selected by an electoral college which is allocated by states.[126]

The appropriateness of political, rather than judicial restraints has been advocated by several commentators, most notably Herbert Wechsler.[127] Wechsler asserts that "the Court is on weakest ground when it opposes its interpretation of the Constitution to that of Congress in the interest of the states, whose representatives control the legislative process and, by hypothesis, have broadly acquiesced in sanctioning the challenged Act of Congress."[128] The delicate balancing of interests required in making decisions about the role of state and federal government is not only a chore for which Congress is particularly well suited, it is one at which the Court is particularly inept.[129]

The Court can act, as through its rule of interpretation requiring a clear statement of intent for Congress to extend its power under the Commerce Clause to its fullest, to ensure that the political protections of federalism principles are given a fair opportunity to function.[130]

a. The Legislative History of the Communications Act of 1934

The Communications Act of 1934 is itself a fine example of the political safeguards of federalism. The Shreveport Rate Case in 1914 had extended the authority of the ICC to include setting aside intrastate railroad rates when they were found to discriminate against interstate commerce.[131] The state regulators wanted the Communications Act of 1934 to clearly reserve all regulation of local rates to the states. The restrictive provision of Section 2(b) of the Act resulted. It reads in part: "[N]othing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service... ."[132] Another part of the Act excludes from FCC regulation local telephone exchanges that include parts of more than one state.[133]

These parts of the Communications Act carefully ensconce the role of the state regulators in the scheme of telephone regulation. The pressures to which Congress was responding are clear from the provisions themselves and are amplified by the legislative history of the Act.

The state regulators, through their representative association NARUC, lobbied strongly for the inclusion of such limitations on federal authority. The Couzens Communication Commission Bill, introduced two years earlier in the Seventy-first Congress, had proposed to transfer the regulatory powers held at that time by the Interstate Commerce Commission to a newly created communications commission. This bill was unanimously opposed by state regulators of NARUC and never passed.[134] The state regulators were afraid of the authority over the intrastate rate setting process for railroads that the ICC had developed after the Shreveport Rate Case. NARUC and the state regulators wanted to ensure that the new Communications Act would not, in the vivid phrase of one of their representatives, "Shreveport us out of the telephone regulatory field. In other words,...substantially [oust] us from our jurisdiction."[135] The gist of the NARUC argument in support of the new legislation and its restrictive provisions is as follows:

> We favor this legislation because it represents, in our judgment, a legitimate exercise of national control in those matters of communications which it is appropriate for the Federal Government, and may be difficult for the states, to reach.
>
> This bill reflects the normal and proper relationship which should exist between the Federal Government and the State governments, namely, the Federal Communications Commission in its sphere of interstate commerce and the various State utility commissions in their respective realms of intrastate business.
>
> We endorse the principle of this bill, because it specifically reserves to the State governments their rightful powers over matters of purely State concern, such as so-called "exchange" or local rates of telephone companies.
>
> In railroad cases, State regulation has become practically a dead letter, due to the Shreveport doctrine which announced that intrastate rates would be set aside where they constituted a discrimination against interstate commerce.
>
> Because of the pronounced difference in the facts, the Shreveport doctrine has no application to the communications' service. Over 99 percent of telephone calls are local and never cross State lines....

> It is inconceivable that the power of the States in 99 percent of the cases should be abrogated because of theoretical discrimination against 1 percent.
>
> On the other hand, 86 percent of the tons of revenue freight carried by class I railroads in Wisconsin in 1932 were interstate traffic.[136]

In summary, NARUC's position was that "[f]ederal regulation should be attempted only insofar as it is necessary to supplement and round out State regulation."[137]

USITA representing the Independent Telephone Companies also joined in supporting the provisions of the Act ensuring continued state regulation Their president emphasized:

> As we see it, the real problem presented to this committee is that of the dividing line between Federal and State regulation of telephone companies and the setting up of a reasonable, efficient and economical system of coordinated regulation by Federal and State commissions of those matters that require coordinated action.[138]

USITA similarly emphasized that the state commissions must regulate 98 percent of the calls, and that their rules and practices must necessarily govern the remaining 2 percent of the calls, interstate calls.[139]

Some witnesses did point out the integration of interstate and intrastate facilities, and suggested that the Federal regulatory body have control over all facilities used in interstate communications. As Smith v. Illinois Bell had previously indicated, this would confer broad jurisdiction on the Federal body since all local equipment is used in providing interstate facilities as well as local.[140]

The legislative history of the Communications Act of 1934 and the resulting provisions of the Act reflect the influence of the state commissions. They vigorously protected their interest. As of early 1980, Congress was considering several potential amendments to the 1934 Act. Testimony before Congress indicated that the state regulatory agenices are still strenuously advocating their position. The battle lines had been redrawn; it appears that the line of demarcation between federal and state interests might soon be the exchange-interexchange boundary, but the fighting was still fierce.

b. Bills Before Congress--1980

A number of bills have come before Congress in the past few years as a response to the increasing pressures toward competition in the telecommunications industry.[141] These bills generally favor the introduction of competition into the industry.

Most of the proposed revisions extend the jurisdiction of the FCC. For example, Section 102 of S. 611 reads "[N]othing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to charges, practices, services, facilities, or regulations for or in connection with exchange telecommunications services which do not form part of an interexchange service." This appears to be a significant extension of FCC jurisdiction to include intrastate toll regulation.

As we have seen, the nature of the local facilities is such that almost all local facilities are used jointly for the provision of both exchange and interexchange services. Thus language similar to that of S. 611 could conceivably extend federal jurisdiction deep into the local exchange itself. In testimony before the Senate on S.611, it was argued that this should be narrowly construed, or rewritten if necessary, to guarantee that local service remain the clear domain of the states.[142] There were others who argued that FCC jurisdiction should be as broad as possible.[143]

The definition of exchange becomes very important if language similar to that of S. 611 is adopted. In Section 226(a) of S. 611 exchange area is constrained to "not extend beyond the boundaries of any standard metropolitan statistical area."[144]

Although most witnesses testifying before the Senate Committee considering S.611 and S.622 seemed to accept the new exchange-interchange boundary, both NARUC and USITA objected to it, and supported the existing scheme.[145]

NARUC argued:

> The NARUC firmly believes that the public interest is best served when decisions impacting upon the quality of citizens' lives are made by officials who are easily accessible to those citizens. It is these officials, rather than a Federal government located in Washington, who have an intimate knowledge of local situations and who are in a preeminent position to balance any competing interest that may be involved in such decisions.[146]

Given the exchange-interexchange boundary which the bills before the 96th Congress rely upon, postalization seems difficult, for much the same reason it would be difficult under the Communications Act of 1934. Local rates would still be controlled by the states. Only partial postalization could be implemented therefore. A uniform distance-independent toll rate structure could be established. Such an intermediate move may be necessary before complete postalization involving local as well as interexchange rates can be established.

The debate reflects vigorous advocacy of the state's interests. The inclusion of provisions similar to those of the 1934 Act protecting state jurisdiction over local rates reflects the potent political force of those interests. The new demarcation between state and federal jurisdiction may reflect the technological and economic absurdity of the current state jurisdictional boundary (as the present complex separations and settlement procedures also imply) rather than a weakened state influence. It is worth noting, however, that in debate upon S.611 several state commissions chose to represent themselves, rather than allow NARUC to speak for all, thus presenting a less united front than in 1934.

The legislative history of the 1934 Communications Act and the testimony before Congress on proposed bills suggest that the state regulatory agencies, either individually or through NARUC, would diligently oppose new legislation extending federal authority to preempt all telephone regulation and in effect eliminating the traditional role of the states. The primary safeguard of the state's role in this instance may thus be political.

Congress will also be sensitive to an additional political consideration, the cost of such a program. The financial cost of local telephone regulation is now borne by the states. Extension of the jurisdiction of the FCC would bring with it a shift in the cost of regulation to the federal government, and would surely necessitate an expensive expansion of FCC staff and resources. This alone might defeat federal preemption of local telephone rate making.

It would seem, therefore, that federal preemption of all telephone industry rate regulation would not be a viable approach to postalization of telephone rates. The elimination of the traditional role of the state regulators would probably be blocked in the political process, and it is unclear if it were passed by Congress whether the courts would uphold it.

D. Minimum or Optional National Rate Structures

Either compelling state cooperation in implementing the postalization of telephone rates or preempting state jurisdiction and extending the mandate of the FCC to include nationwide rate setting seems to intrude upon state sovereignty. A safe path to postalization can perhaps be surveyed by incorporating a sensitivity to the problems raised in analysis of the first two approaches with an attempt to keep new legislation within bounds which previous court decisions suggest are safe.

The following discussion will consider two approaches, variations upon each other, that could possibly survive both judicial and political scrutiny (assuming a genuine support for some form of postalization). There may well be others.

Both approaches will assume the continued existence of the state regulatory bodies functioning much as they do now. They assume a uniform national distance-independent rate will be established either by the FCC or by a federal-state joint board procedure.

In the first approach, state participation in the uniform rate structure will be optional. However, support from the national revenue pool would be contingent upon participation in the national rate structure.

The second approach involves federal establishment of a national minimum rate structure. Local political pressure would be relied upon to ensure that the minimum structure becomes a uniform structure.

1. Optional National Rate Structure

Congress could attempt to use a carrot rather than a stick to encourage state cooperation in establishing a uniform national telephone rate system.

Patriotic fervor might be sufficient to attract state cooperation, but the lure of money would probably be more reliable. Thus Congress might establish an optional uniform national distance independent rate structure, with participation in the division of the national revenue pool contingent upon a state's adherence to the uniform rate structure.

National League of Cities deliberately avoided expressing an opinion as to whether Congress can seek to affect integral operations of state governments by exercising its authority under the spending power.[147] Lower Courts have subsequently noted that "federal programs 'with strings attached' are characteristic of federal-state dealings today," and have held that inducing state cooperation in a federal program by placing qualifications on the receipt of federal funding does not violate the principles of National League of Cities or the sovereignty of the states.[148] When federal funding has "no direct, mandatory terms and conditions imposed, and...the State and its agencies can avoid completely the structuring of their relationships by declining the grants," there is no NLC violation.[149]

Smith v. Illinois Bell will place some constraints upon the allocation of joint and common costs; interexchange service will need to provide some compensation for its use of the local exchange facilities.[150] Yet Smith v. Illinois Bell has been interpreted to allow significant latitude in the allocation of costs, and new technologies may provide adequate economic freedom to satisfy the constraints of both Smith and the optional rate program.

It seems reasonable to assume as a policy goal that the costs of the telecommunication industry be borne by the consumers of the services it provides. Accordingly, the cost of any inducement offered to the states to participate in a nationwide rate system should be internalized to within the industry, just as the cost of the support of local service now is internalized through the separations and settlements procedures.[151]

Congress can give the FCC direct control over a significant portion of the national rate system. Assume, following the trend of legislative proposals, that the FCC is delegated regulatory authority over all interexchange traffic, with authority over local service reserved to the states. Presently FCC controlled interstate rates are set high enough to cover the costs of interstate toll service and also some portion of the costs of local service. Similarly under the new proposal, the FCC would want federally controlled interexchange service rates to create a surplus of funds with which to induce state participation in the nationwide uniform rate program.

The present separations and settlement procedures provide support to intrastate and local services through the allocation of joint costs. This makes it difficult to characterize such support as a federal grant, and thus any imposition of conditions upon its receipt by the states would be problematical. In an optional national rate structure this difficulty could be circumvented by taxing the interexchange services of their revenues collected in excess of their costs, and redistributing it through federal grants to participating states. While such a mechanism may initially sound cumbersome, when compared to the complexity of the present separations and settlements procedures it seems almost graceful.

In 1924 the Supreme Court upheld the constitutionality of a similar provision in the Transportation Act of 1920 that recaptured any excess profit railroads achieved because of uniform rates, and with that recaptured profit maintained a "general railroad contingent fund."[152] The Court found that Congress, through this recapture clause, "is enabled to maintain uniform rates for all shippers and yet keep the net returns of railways, whether strong or weak, to the varying percentages which are fair respectively for them."[153] No carrier had a constitutional right to more than a fair rate of return, and the "reduction of the net operating return provided by the recapture clause is, as near as may be, the same thing as if rates had all been reduced proportionately before collection."[154] The recapture clause was a failure, for reasons of little relevance to the telecommunications industry today, but its constitutionality was secure.[155]

The difficulty with an optional uniform national rate structure seems to lie not in the legality of such a proposal but in the economic constraints it must satisfy. For an optional structure to work, there must be an inducement for all states to participate. The inducement offered the states is that their local rates will be less if they participate and receive support from the national revenue pool than their rates would otherwise need to be. If a state can institute its own local rate structure that is less than the national uniform rate, and still recover all costs associated with its local services, that state will have no incentive to participate in the national program. Accordingly, for an optional uniform national rate system to function, the uniform rate must be less than that otherwise necessary to cover the local costs of the least costly state.

The fundamental aggregate rate equation still must be satisfied: total national telephone revenues must equal total national telephone costs. Postalization further implies that the rate for an interexchange call will be identical to that for a local call. Thus, since the rates associated with federally controlled interexchange service and state controlled local service will be determined by the aggregate rate equation, the revenues associated with each jurisdiction will also be determined by the aggregate rate equation. As the previous discussion has indicated, the revenues associated with local service must be less than the costs associated with that service. This means the revenues associated with interexchange service must be sufficient both to cover the costs allocated to interexchange service and to compensate for the shortfall in local revenues.

The issue then, since revenues associated with each jursidiction are already determined, is whether there will be enough flexibility in the allocation of joint and common costs between local and interexchange services to satisfy the conditions necessary for the incentive system to function. This will depend in part upon such varied factors as the impact of new technologies and the elasticity of demand for telephone service. The economic prerequisites to the successful implementation of this approach seem quite stringent, however.

2. Minimum National Rate Structure

There is a series of well established railroad cases in which the Supreme Court has approved in certain circumstances federally dictated minimum intrastate railroad rates. Congress could perhaps rely on this precedent to establish a uniform national distance-independent minimum rate structure. The state regulatory agencies would continue their traditional functions, and would be free to establish higher rates should they so chose. The uniform minimum rate would be sufficient to allow total nationwide revenues to equal total nationwide costs. Revenue pooling and redistribution of revenue according to the costs incurred by participating telephone companies would continue in a fashion roughly similar to that in effect today. However the pooling would now include all local costs and local revenues. The costs of each telephone company, including a reasonable rate of return, would thus be covered through division of the national revenue pool.[156]

While state regulatory agencies could establish a local rate that was higher than the national minimum, to do so would merely allow the local telephone company to receive an unusually high rate of return on its capital investment. All other costs (including some reasonable rate of return already allowed in the national minimum rate) would be covered by the national division of revenue. One might assume that local political pressure would therefore keep local rates to the national minimum, and thus effect a national uniform rate.

The following discussion will focus first upon the railroad cases approving federally established minimum intrastate rates, and then on their applicability to a minimum national telephone rate system.

a. The Shreveport Rate Case and its Progeny

Even in the midst of its most conservative period of interpretation of Commerce Clause doctrine, the Court was willing to grant the interrelatedness of interstate and intrastate commerce in the context of railroad rate regulation. These decisions still provide a valuable precedent for any Congressional attempt to impose a uniform national telephone rate structure.

The seminal case in this line of decisions was the 1914 Shreveport Rate Case.[157] Shreveport, Louisiana, lies just across the state line from Texas. Railroad rates for a given distance within the state of Texas were less than rates for a comparable length of haul to Shreveport. The Interstate Commerce Commission found that such rates unjustly discriminated against interstate railroad traffic. The ICC order that this be corrected was in essence an order that intrastate railroad rates be increased. The railroads argued that Congress and the ICC were powerless to control the intrastate charges of a carrier, even if necessary to prevent discrimination against interstate traffic.

The Court upheld the authority of Congress to reach intrastate rates that discriminated against interstate commerce:

> The fact that carriers are instruments of intrastate commerce, as well as of interstate commerce, does not derogate from the complete and paramount authority of Congress over the latter, or preclude the Federal power from being exerted to prevent the intrastate operation of such carriers from being made a means of injury to that which has been confided to Federal care. Wherever the interstate and intrastate transactions of carriers are so related that the government of the one involves the control of the other, it is Congress and not the state that is entitled to prescribe the final and dominant rule, for otherwise Congress would be denied the exercise of its constitutional authority, and the state, and not the nation, would be supreme within the national field.[158]

When the Transportation Act of 1920 was enacted, the ICC was given new and more expansive authority to deal with the troubled financial condition of the railroads.[159] The ICC's mandate was to ensure an adequate railway system for the country, and in furtherance of that end it was empowered to consider the aggregate effects of rate setting upon individual carriers and upon carriers as a whole. In determining fair aggregate rates the ICC could consider both interstate and intrastate earnings.[160] In 1921 the Supreme Court upheld an ICC order that required a uniform increase in Wisconsin intrastate railroad rates, although a lower maximum rate was prescribed by state law.[161] The order "includes fares between all interior points although neither may be near the border and the fares between them may not work a discrimination against interstate travelers at all."[162]

In justifying this extension of authority over intrastate as well as interstate rates the Court said, "Effective control of the one must embrace some control over the other in view of the blending of both in actual operation."[163] The Court continued:

> It is said that our conclusion gives the Commission unified control of interstate and intrastate commerce. It is only unified to the extent of maintaining efficient regulation of interstate commerce under the paramount power of Congress. It does not involve general regulation of intrastate commerce.[164]

The extent to which intrastate rates were not subject to ICC regulation was left unclear. From the logic of the argument a state could presumably prescribe a higher than minimum rate, for this would neither discriminate against interstate shipping nor place an undue burden upon the interstate rate pool.

The Court subsequently expanded upon this rationale in U.S. v. Louisiana.[165] The Court held that the ICC is empowered to raise intrastate rates so that "intrastate traffic may produce its fair share of the earnings required to meet maintenance and operating costs and to yield a fair return on the value of property devoted to the transportation service, both interstate and intrastate."[166] The Court went on to say that "forbidden discrimination against interstate commerce by intrastate rates includes those cases in which disparity of the latter rates operate to thwart the broad purposes of [the Transportation Act] to maintain an efficient transportation system by enabling the carriers to earn a fair return."[167]

The Shreveport doctrine has been embraced and extended to other areas of the law. The Supreme Court has said that "[w]ith the extension of the Shreveport influence to general application, it [is] necessary no longer to search for some sharp point or line where interstate commerce ends and intrastate commerce begins."[168] A recent Court of Appeals decision asserts that the "Shreveport doctrine has been followed consistently in the ensuing years."[169]

The Court has recognized that there are limits to ICC authority to regulate intrastate rates. "Intrastate rates are primarily the State's concern and federal power is dominant 'only so far as necessary to alter rates which injuriously affect interstate transportation.'"[170] The Court went on to say that "whenever this federal power is exerted within what would otherwise be the domain of state power, the justification for its exercise must 'clearly appear.'"[171]

b. The Shreveport Decision and Minimum Telephone Rates

Thus there are at least two concerns which the Court has recognized as sufficient to justify federal establishment of minimum intrastate rates. The federal regulatory authority, with appropriate Congressional authorization, may establish minimum intrastate rates to ensure there is no discrimination against interstate traffic. The federal regulatory authority, when entrusted with the responsibility for the financial soundness of the entire nationwide system, may set minimum rates for intrastate traffic and require it to carry its fair share of the burden of supporting the nationwide system. Congress could quite legitimately rely on both of these justifications in delegating authority to either the FCC or a joint federal-state board to establish a uniform national distance-independent minimum rate structure.

A distance-insensitive rate structure would encourage equal utilization of interstate and intrastate telephone commerce. The facilitating effect such uninhibited information transfer might have on other interstate commerce could be significant. The present disparity between local and toll rates creates a disincentive which may discourage one from looking beyond the local area for goods and services. Eliminating this disincentive would prevent discrimination against interstate telephone traffic, and would encourage equal treatment of intrastate and interstate goods and services in other areas of commerce.

Congress could also quite legitimately entrust the FCC with the responsibility for ensuring the financial soundness of the entire telephone network. The technological interrelatedness of the network is reflected in the joint cost ambiguity recognized by the Supreme Court as early as 1930 in Smith v. Illinois Bell.[172] To empower the Commission to establish minimum rates to ensure that all telephone companies contribute to the financial soundness of the nationwide network seems well within the rationale of U.S. v. Louisiana.[173]

This approach would not be subject to the stringent economic requirements to which an optional national rate structure is subject. The minimum local rate can exceed the local costs. The differential constitutes the contribution of local service to an efficient national communications system.

c. The Impact of National League of Cities

The difference between compelled state enforcement of federally established local rates and a federally established minimum rate is subtle but significant. Here the state agencies are merely prohibited from establishing rates below a certain minimum rate determined by the FCC or a joint board. The National League of Cities standard is not offended by prohibiting states from establishing rates that are so low as to discriminate against interstate traffic or to prevent intrastate traffic from carrying its fair share of the burden of supporting the nationwide system. There is no traditional state's right to establish discriminatory rates, and thus state sovereignty is not infringed by this approach.

3. Federal-State Joint Board Procedure

Either a minimum or optional national rate structure must survive the political safeguards of state sovereignty. While neither approach is as devastating to the traditional role of the state regulatory bodies as complete federal preemption of telephone regulation, they can both be expected to generate some controversy. The political difficulties could possibly be mitigated by utilizing a federal-state joint board to establish the uniform rate, rather than merely empowering the FCC to make such a determination. Such a provision would not be novel.

The present Communications Act provides for Federal-State Joint Boards in proceedings regarding the jurisdictional separation of common carrier property.[174] The joint board is composed of the Commissioners of the FCC and four State commissioners nominated by NARUC. The board has the jurisdiction and powers of a hearing examiner.

The FCC and NARUC had utilized a similar procedure in developing the Ozark Plan. The FCC and NARUC agreed to seek legislation that would write into law the procedures then being followed; the Chairman of the FCC and the President of NARUC subsequently appeared before the House Subcommittee on Communications and recommended the adoption of the Joint Board procedures. Over forty state commissions were heard from during Senate hearings on the same matter. In 1971 the present provisions of the Communications Act were adopted.[175]

Revisions of the Communications Act under consideration by the Ninety-sixth Congress also utilize joint boards.[176] In testimony on these bills, NARUC has continued to vigorously support the further utilization of joint boards.[177]

The utlilization of joint boards, coupled with the continued role of the states in interfacing between the local telephone company and the customer, might be sufficient involvement to diffuse state hostility to a a minimum or optional national rate structure.

V. CONCLUSION

The day may come when economic and social forces make complete postalization worth serious consideration. A uniform national distance independent toll rate structure may already be worth consideration. This would avoid most, if not all, of the problems associated with complete postalization.

Should there be a general impetus toward postalization, perhaps this paper will provide a starting point for discussion of some of the legal aspects of such an effort. In a day in which the powers of the national government are often perceived as virtually unlimited, it is surprising how approaches to postalization can be restricted by the principles of federalism. The safeguards of the roles of the states seem alive and functioning.

The major attraction of postalization, drawing the country together as a national community, is an interesting counterpoint to the underlying concept of federalism, the importance of the local community. Harmonizing this tension is a challenge. Preserving the flavor of local and regional tradition and color in the face of the increasingly homogenizing forces of the communications industry may become virtually impossible. Someday we may all speak with the gentle Texas accent of Dan Rather.

Still, the uninhibited transfer of information may be a goal intrinsically worth pursuing. Freedom of communication has traditionally been a revered goal of our democratic society. Postalization of telephone rates may prove to be a valuable asset in furthering those traditional values.

NOTES

1. A. Oettinger, K. Borchardt, with C. Weinhaus, Stakes in Telecommunications Costs and Prices, Harvard Program on Information Resources Policy (hereinafter "Program"), Working Paper WP-80-XX, 67-71 (1980).

2. Id.

3. 47 U.S.C. §§ 152, 221.

4. Telephone Glossary, New York Telephone (1975). Similar definitions can be found throughout Bell System literature. See A. Oettinger with C. Weinhaus, The Traditional State Side of Telecommunications Cost Allocations, Program Working Paper WP-80-1, 69 (1980) (hereinafter "State").

5. Oettinger with Weinhaus, State, supra at 91.

6. For a detailed account of telecommunications technology, see A. Collins and R. Pedersen, Telecommunications, A Time for Innovation (1973).

7. R. Godbey, Revenue and Cost Allocations: Policy Means and Ends in the Railroad and Telecommunications Industries, Program Publication P-79-2 (1979).

8. Discussed infra at 11.

9. See A. Kahn, The Economics of Regulation, Vol. 1, 83-86.

10. See P. Berman and A. Oettinger, Changing Functions and Facilities: The Politics of Information Resources, 28 Fed. Com. Bar J., 227-241 (1975).

11. See J. Sichter, Separations Procedures in the Telephone Industry: The Historical Origins of a Public Policy, Program Publication P-77-2 (1977).

12. 282 U.S. 133 (1930), an appeal from a District Court order enjoining the enforcement of an Illinois Commerce Commission rate order as confiscatory and hence in violation of the Fourteenth Amendment.

13. 282 U.S. at 148.

14. 282 U.S. at 150.

15. 282 U.S. at 150 (emphasis added, citations omitted).

16. J. Sichter, supra at 63-89.

17. January 20, 1943, FCC Docket 6468; see Sichter, supra at 111-124.

18. J. Sichter, supra at 109.

19. P. Berman and A. Oettinger, The Medium and the Telephone: The Politics of Information Resources, Program Publication P-76-5, Figure 8, pp. 20-21 (1976)

20. P. Berman and A. Oettinger, supra at 82, Fig. 27.

21. See A. Oettinger with C. Weinhaus, The Federal Side of Traditional Telecommunications Cost Allocations, Program Publication P-80-1, 42-43 (1980)(hereinafter "Federal").

22. 282 U.S. at 151.

23. This ratio is known as the Subscriber Line Usage Factor, SLU.

24. A. Oettinger with C. Weinhaus, Federal,supra at 42-43.

25. A. Oettinger with C. Weinhaus, State,supra at 63, noting that 80-90% residences and 55% business were on flat rate basic service as of 1975-77.

26. A. Oettinger with C. Weinhaus, Federal,supra at 41.

27. A. Oettinger with C. Weinhaus, Federal,supra at 45 citing 16 FCC2d 324, 327.

28. A. Oettinger with C. Weinhaus, Federal, supra provides a comprehensive examination of the differential impact of separations procedures of states.

29. See A. Oettinger with C. Weinhaus, State, supra at 113-162.

30. Microwave Communications Inc., 18 FCC2d 954 (1969).

31. E.g., H.R. 3333, S. 611, S. 622, Ninety-sixth Congress, and H.R. 6121, Ninety-sixth Congress, 2d Session, S.898, Ninety-seventh Congress.

32. A. Oettinger, K. Borchardt, with C. Weinhaus, supra at 2.

33. R. Hill, The Life of Sir Rowland Hill and the History of Penny Postage 249-250 (1880).

34. R. Hill, supra at 356.

35. E.g., R. Willig with H. Quirmbach, Aspects of the Welfare Economics of Postal Pricing, Program Working Paper W-79-5 (1979), and "The Necessity for Change," Committee Print No. 94-26, Committee on Post Office and Civil Service, 94th Cong. 2d Sess. (1976).

36. A. Oettinger, K. Borchardt, with C. Weinhaus, supra at 99.

37. <u>See</u> "Commerical U.S. Satellites," <u>IEEE Spectrum</u>, October 1979, pp. 30-35.

38. P. Berman and A. Oettinger, <u>The Medium and the Telephone</u>, <u>supra</u> at 20. The cost of multiplexing equipment tends to flatten the dramatic effect of Figure 2, however.

39. <u>See</u> "Optical Systems: A review," <u>IEEE Spectrum</u>, October 1979, p. 70.

40. P. Berman and A. Oettinger, <u>The Medium and the Telephone</u>, <u>supra</u> at 30, 31 and 79, 80.

41. A summary of elasticity studies may be found in Meyer Wilson, <u>et al.</u>, <u>The Economics of Competition in the Telecommunications Industry</u>, Appendix C (1979).

42. <u>Id</u>. at C-42.

43. Telephone plant capacity must be engineered to accommodate peak load. Thus facilities may stand idle during off peak times, with very low marginal cost associated with the utilization of such idle facilities. Telephone traffic does reflect significant variation between peak and off peak load. <u>See</u> P. Berman and A. Oettinger, <u>The Medium and the Telephone</u>, <u>supra</u> at 78.

44. J. Sichter, <u>supra</u> at 109, 110.

45. For a general discussion of the social impact of information technology, <u>see</u> Bell, <u>The Coming of Post-Industrial Society</u> (1973).

46. FCC, <u>Statistics of Communications Common Carriers</u> 30 (1976).

47. The "local" flat rate calling area around Atlanta is larger than the states of Rhode Island and Delaware combined. Discussed <u>supra</u> at 6.

48. Houston, for example, includes service provided by more than one operating company within its flat rate area. Texarkana and Washington, D.C. both involve more than one state.

49. Discussed <u>supra</u> at 10.

50. <u>IEEE Spectrum</u>, January 1980, p. 41.

51. Telephone conversation with N.E. Tel. marketing representative, 1 February 1980.

52. <u>See</u> Access Charge Inquiry, Docket No. FCC 78-72, and also Common Carrier Docket No. FCC 80-286.

53. The new administration of the FCC will apparently continue this trend. The speeches of Mark Fowler, new FCC chairman, indicate his approval of the trend to deregulation, or "unregulation," as he refers to it.

54. Common Carrier Docket No. 79-252.

55. CC Docket No. 78-97, Transmittal Nos. 7346 & 7691.

56. Memorandum Opinion and Order, CC Docket No. 78-97, FCC2d (released April 30, 1981).

57. Memorandum Opinion and Order, supra.

58. 47 U.S.C. §152(b), slightly modified by amendments in 1954, and again in 1978.

59. 47 U.S.C. §221, modified slightly in 1954. The legislative history of this portion of the Act indicates that it was intended to exclude from FCC regulation those local telephone exchange areas that include parts of more than one state, for example, Texarkana, Arkansas and Texas. S. Rep. No. 781, 73d Cong. 2d Sess., 5; H.R. Rep. No. 1850, 73d Cong. 2d Sess., 7.

60. 537 F.2d 787 (1976) and 552 F.2d 1036 (1977), respectively. See also People of State of California v. FCC 567F.2d84 (1977). There are a number of cases discussing the applicability of this section of the Act to Cable TV. FCC jurisdiction is generally upheld due to its relationship to broadcasting. See P. Hochberg, Federal Preemption of State Regulation in Cable Television, Program Publication P-78-8 (1978).

61. 537 F.2d 790.

62. 537 F.2d at 793.

63. 537 F.2d at 794.

64. 537 F.2d at 793 n. 6.

65. 537 F.2d at 795 (a rather suspect argument).

66. See also N. Carolina II, 552 F.2d 1036 (1977), where the court again emphasizes the legislation intent to "deny the kind of jurisdiction over local rates approved by the Shreveport Rate Case." 552 F.2d at 1047.

67. See No-Fault Motor Vehicle Insurance, 49 N.Y.U.L. Rev. 45 (1974).

68. U.S. Const. Art. I., Sec. 8.

69. McCulloch v. Maryland, 4 Wheat. 316, 405 (1819).

70. 426 U.S. 833 (1976).

71. 9 Wheat. 1, 194 (1824).

72. 9 Wheat. at 194.

73. Judge Friendly identifies 23 Congressional enactments extending national power in the 1930's. See Friendly, Federalism: A Foreword. 86 Yale L.J. 1019 (1977).

74. Basically from U.S. v. F.C. Knight, 156 U.S. 1 (1895), until NLRB v. Jones and Laughlin Steel, 310 U.S. 1 (1937). See G. Gunther, Constitutional Law (Ninth Edition) 134-136 (1975), and L.H. Tribe, American Constitutional Law §5-4 (1978).

75. Houston E. & W. Texas Ry. Co. v. U.S. (The Shreveport Rate Case), 234 U.S. 342 (1914), discussed infra at 56-59.

76. Tribe, American Constitutional Law, 308 (1978).

77. NLRB v. Jones and Laughlin Steel, 310 U.S. 1, 37 (1937).

78. 301 U.S. at 37.

79. Wickard v. Filburn, 317 U.S. 111, 125 (1942).

80. Heart of Atlanta Motel v. U.S., 379 U.S. 241 (1964) and Katzenbach v. McClung, 379 U.S. 294 (1964).

81. 379 U.S. at 258. See Gunther, Constitutional Law 208-228 (1975).

82. Supra.

83. 426 U.S. 833 (1976).

84. 426 U.S. at 842.

85. 426 U.S. at 847.

86. 426 U.S. at 852.

87. 426 U.S. at 845.

88. 426 U.S. at 854 n. 18.

89. See Michelman, States' Rights and States' Roles: The Permutations of 'Sovereignty' in National League of Cities v. Usery, 86 Yale L.J. 1165 (1977), and Tribe, Unraveling National League of Cities: The New Federalism and Affirmative Rights to Essential Government Services, 90 Harv. L. Rev. 1065 (1977).

90. Michelman, supra at 1172.

91. See Beard and Ellington, A Commerce Power Seesaw: Balancing NLC, 11 Ga. L. Rev. 35 (1976), relating NLC to Edelman v. Jordan, 415 U.S. 651 (1974).

92. In Testa v. Katt, 330 U.S. 386 (1947), the Supreme Court ruled that Congress can require state courts to hear lawsuits based on federal law if they hear similar cases based on state law. However, this may be distinguished from the compelled state enforcement for federal policy by virtue of the relative burdens placed on state resources. Prof. Stewart differentiates between the two situations in Stewart, Pyramids of Sacrifice? Problems of Federalism in Mandating State Implementation of National Environmental Policy, 86 Yale L.J. 1196, 1246-1247 (1977).

93. This seems implicit in the Court's overruling aspects of Maryland v. Wirtz, 392 U.S. 183 (1968). See Amersbach v. City of Cleveland, 598 F.2d 1033, 1036 (Cir. 1979). (holding the operation of a municipal airport to be protected).

94. 426 U.S. at 854 n. 18.

95. Public Service Co. v. Fed. Energy Reg., 587 F.2d 716 (1979) (applying Natural Gas Act, 15 U.S.C. §717a and 717f, to Texas commercial oil and gas production).

96. City of La Fayette v. Louisiana Power and Light Co., 98 S.Ct. 1123 (1978) (holding that the operation of a municipal power company is not an attribute of state sovereignty and therefore is not exempt from federal antitrust regulation). J. Burger in his concurring opinion states that "the running of a business enterprise is not an integral operation in the area of traditional government functions." 98 S.Ct at 1142.

97. R. Stewart, Pyramids of Sacrifice? Problems of Federalism in Mandating State Implementation of National Environmental Policy, 86 Yale L.J. 1196, 1267 (1977). See also supra at 1268 n. 244.

98. U.S. v. Best 573 F.2d 1095, 1103 (9th Cir. 1978) quoting NLC 426 U.S. at 855 (holding that a federal court, bound as Congress is bound by NLC, cannot suspend the license of a motorist found guilty of operating a motor vehicle on a federal enclave under the influence of alcohol).

99. Lienthat, Law of Utility Holding Companies, 31 Colm.L.R. 207 (1931).

100. A somewhat analogous requirement of state implementation of federal policy occurred under the Clean Air Act. The EPA issued regulations under that act requiring states to adopt adequate controls to meet federal ambient air standards, or to enforce EPA drafted controls. Failure to do so would subject the states to enforcement orders and civil or criminal penalties. Four circuits considered the EPA regulations. Two circuits construed the statute to avoid the constitutional issue and determined that the regulations were beyond

the authority delegated by Congress to the EPA in the Act. Maryland v. EPA, 530 F.2d 215 (4th Cir. 1975), vacated sub nom. EPA v. Brown 431 U.S. 99 (1977); Brown v. EPA, 521 F.2d 827 (9th Cir. 1975), vacated sub. nom. EPA v. Brown, supra. One circuit faced the constitutional issue and found Congress had exceeded its authority, District of Columbia v. Train, 521 F.2d 971 (D.C. Cir. 1975), vacated sub. nom. EPA v. Brown, supra. One circuit approved the regulation, Pennsylvania v. EPA, 500 F.2d 246 (3d Cir. 1974), but relied on Maryland v. Wirtz, 392 U.S. 183 (1968), which has subsequently been overruled by National League of Cities, supra. The Supreme Court did not address the troublesome issue in EPA v. Brown, however. By the time the case reached the Supreme Court the issues had been narrowed sufficiently to avoid the question. For a detailed analysis of these cases, see Stewart, supra at 1204-1206.

101. See supra at 29 for discussion of historical Commerce Clause development.

102. Stewart, supra at 1243.

103. Stewart also discusses these implications of NLC. Stewart, supra at 1267-1269.

104. 426 U.S. at 845.

105. 426 U.S. at 854 n. 18.

106. 426 U.S. at 847(emphasis added).

107. Professors Michelman and Tribe apparently interpret this as a responsibility to provide services. Their justification for recognizing a constitutional protection of the states' role lies in the individual's right to receive these services.

108. Discussed supra at 34.

109. 426 U.S. at 856. For a discussion of lower court treatment of the Blackmun fest, see United Transportation Union v. Long Island R. Co., 634 F.2d 19, 24 (2d Cir. 1980).

110. Amersbach v. City of Cleveland, supra at 1035-1036.

111. A traditional argument in support of federalism has been the advantages of allowing courageous states to function as experimental laboratories for innovative social policies. An example of potential state innovation in telephone regulation might be implementation at "life line" rates, a very low charge for basic connection to the telephone system. Some states might even wish to provide such rates for elderly or handicapped through subsidy from general tax revenues.

112. However, the Court has never directly approved such complete federal preemption of an entire field traditionally subject to state regulation as preemption of telephone regulation would involve. The political safeguards of federalism may have ensured that Congress never attempted such a total usurpation of a traditional state regulatory role. Perhaps the most nearly analogous area is the regulation of intrastate railroad rates, as developed in the Shreveport Rate Case 234 U.S. 342 (1914), and its progeny. Even in this line of cases, certain regulatory perogatives were carefully reserved to the states. Cf. Chicago, M., St. P., & P.R. Co. v. Illinois, 355 U.S. 300 (1957); North Carolina v. U.S., 325 U.S. 507 (19); Florida v. U.S., 282 U.S. 194 (19). See discussion infra at 56-59.

113. Stewart, supra at 1268-1269.

114. The Supreme Court has deferred to the judgment of Congress in balancing its exercise of the Commerce Power against the limitations of federalism, in large measure due to Congress' peculiar institutional competence in this area. It is not surprising, therefore, that in areas such as the jurisdiction of the federal courts, where the Court has a particularly intimate understanding of the issues, the Court has been more willing to give concrete expression to its federalism concerns.

In 1971, for example, the Supreme Court avowed:

> It should never be forgotten that this slogan, "Our Federalism," born in the early struggling days of our Union of States, occupies a highly important place in our Nation's history and its future. Younger v. Harris, 401 U.S. 37, 44-45 (1971).

The Court emphasized that the phrase "Our Federalism" embodies "the belief that the National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways." 401 U.S. at 44. With these stirring words the Court went on in this and subsequent cases to develop a doctrine limiting those remedies available for the vindication in federal court of constitutional rights when proceedings are underway in a state court. (This oversimplifies a complex line of cases.) See D.P. Currie, Federal Courts 719-756 (1975).

There are other instances in which the federal courts will abstain from hearing a case in favor of a state forum.

See Railroad Commission v. Pullman Co., 312 U.S. 486 (1941), England v. Louisiana State Board of Medical Examiners, 375 U.S. 411 (1964). See Currie, supra, discusses the abstention doctrine at 647-662; Hart and Wechsler, The Federal Courts and the Federal System 984-996. The federal courts may abstain in a case involving the particular administrative expertise of a state regulatory agency. Burford v. Sun Oil Co., 319 U.S. 315 (1943). See Currie, supra at 674-678. In 1951 the Supreme Court considered a federal injunction against the discontinuation by a state public service commission of passenger train service between two cities in the state. Alabama P.S.C. v. Southern Ry., 341 U.S. 341 (1951). The Court held that the regulation of intrastate railroad service was primarily the interest of the state, and that adequate state review was provided to consider orders of the state commission. To avoid friction with state policies, the Court set aside the injunction, even though the case really involved no specialized or unclear question of state law. Accordingly, it may be that "abstention is likely to be applied in any attempt to enjoin a state regulatory body in a federal court." Currie, supra at 675-677, quoting Note, 73 Yale L.J. 850, 851 (1964).

These cases reflect the Court's concern with federalism, and perhaps its concern with state administrative expertise. National League of Cities may accordingly be seen as a logical extension of long standing concerns on the part of the Court. However, this does not clarify the question of how far the Court is willing to go in effectuating these concerns.

115. Tribe, supra at 1068.

116. Another source of Congressional authority is the spending power, U.S. Const. Art. I, §8, cl. 1, discussed infra at 51, however it is not helpful in considering federal preemption of state authority.

117. U.S. Const. Art. I, Sec. 8.

118. Pensacola Telephone Co. v. Western Union Telephone Co., 96 U.S. 1 (1877).

119. 96 U.S. at 10.

120. This eventually led to the Transportation Act of 1920. See Godbey, supra at 10.

121. Lamar, W.H., Solicitor for the Post Office, Has the Postmaster General the Power to Fix Local Telephone Rates? 40 (1919).

122. See U.S. Postal Service v. Brennan, 574 F.2d 712, 716 (1978), holding NLC adds nothing to the consideration of issues involved in the Private Express Statute "since no threat to state sovereignty is involved." See also Peel v. Fla. Dept. of Transportation, 600 F.2d 1070, 1082-1083 (1979), and Jennings v. Illinois Office of Ed., 589 F.2d 935 (1979), asserting that the "constitutional grant of war

powers is sufficient to sustain a statute that might otherwise violate the Tenth Amendment which reserves to the state Powers not delegated to the United States by the Constitution," and run afoul of NLC. 589 F.2d at 937.

123. 9 Wheat. at 197.

124. 426 U.S. at 857.

125. 426 U.S. at 857, quoting Gibbons v. Ogden, 9 Wheat. at 197.

126. Note, however, that some institutional protections such as the selection of senators by state legislatures, that existed at the enactment of the Constitution are no longer part of the federal system. See Tribe, supra at §5-7.

127. H. Wechsler, The Political Safeguards of Federalism--The Role of the States in the Composition and Selection of the National Government, 54 Colum. L. Rev. 543 (1954). See also Tribe, supra at 5-7, and Begen, The Hunting of the Shark: An Inquiry into the Limits of Congressional Power Under the Commerce Clause, 8 Wake Forest L. Rev. 187 (1972).

128. Wechsler, supra at 559.

129. Begen, supra develops this in Part IV of his article.

130. The Court can and has adopted rules of interpretation that tend to facilitate the political restraints upon Congress. The Court will not read a Congressional enactment to go to the limits of Congressional power under the Commerce Clause unless Congress has made a clear statement of its intent to do so. Such a requirement tends to ensure that Congressional usurpation of state power will not occur without attracting the attention of those concerned and full debate through the political process. Tribe, supra at §5-8.

Narrow readings of Congressional statutes may tend to preserve the underlying strata of state law.

> Federal law is generally interstitial in its nature. It rarely occupies a legal field completely...It builds upon legal relationships established by the states, altering or supplanting them only so far as necessary for the special purpose. Congress acts, in short, against the background of the total corpus juris of the states... Hart and Wechsler, The Federal Courts and the Federal System (Second Ed.) 470-471 (1973).

131. Discussed further infra at 56.

132. 47 U.S.C. §152(b), slightly modified by amendments in 1954 and again in 1978.

133. 47 U.S.C. §221, quoted supra at 24.

134. See Communications Act of 1934, 21 Va. L. Rev. 318, 320 (1934), and Hearings on H.R. 8301 before the House Committee on Interstate and Foreign Commerce, 73d Cong., 2d Sess. 180, Statement of J.E. Benton, General Solicitor of NARUC, describing their oppostion to the defeated Couzens bill. For a sampling of the rather vituperative debate over the Couzen bill itself, see Mr. Benton's testimony before the Senate Committee, 71st Cong., 2d Sess., where he attempts to defend NARUC from the Senators' accusations that it had been bought off by the utility companies its members regulate.

135. Id. at 73, statement of K.F. Clardy, chairman of NARUC Legislative Committee.

136. Id. at 132, statement of Andrew McDonald, 1st V.P. of NARUC.

137. Id. at 71, statement of K.F. Clardy.

138. Id. at 239, statement of Mr. MacKinnon, Pres. of USITA.

139. Hearings on S.2910 before the Senate Committee on Interstate Commerce, 73d Cong., 2d. Sess. 138, statement of F.B. MacKinnon, Pres. of USITA.

140. Id. at 199, statement of E.N. Nockles, American Federation of Labor.

141. E.g., H.R. 3333, S.611 and S.622, Ninety-sixth Congress, 1st Session; and H.R. 6121, Second Session, Ninety-sixth Congress.

142. See Hearings on S.611 before the Senate Committee on Interstate Commerce, 96th Congress, 1st Session, 963, statement of Dale Hatfield, National Telecommunications and Information Administration.

143. Id. at 979, 980, statement of William G. McGowan, MCI.

144. There was testimony that this was too restrictive a measure. See Id. at 261, statement of Charles Zielinski, New York State Public Utility Commission, arguing for non-contiguous exchange areas; and Id. at 1325, statement of Edward P. Larkin, NARUC, arguing that the SMSA is too restrictive a limitation.

145. Id. at 1014, statement of Milton Stewart, Jr., USITA; and Id. at 1014, statement of E. Larkin, NARUC, arguing that "the regulation of all intrastate services and facilities is a subject that is clearly best left to state authorities."

146. Id. at 1324.

147. 426 U.S. at 852 n. 17.

148. Shell Oil Co. v. Train, 585 F.2d 408, 413 (1978) (rejecting Shell's "novel theory" that EPA had so dominated the actions of a state agency as to transform it into federal action reviewable by federal courts).

149. Walker Field, Colo., Public Airport v. Adams, 606 F.2d 290, 297 (1979), although cautioning that "[it] may be that some conditions imposed under the spending power of Congress would exceed constitutional limits..." See also County of Los Angeles, Cal. v. Adams, 574 F.2d 607 (1978) (federal government can designate procedures by which transportation improvement program funds are allocated within the state).

150. 282 U.S. 133 (1930). See discussion supra at 9.

151. Discussed infra at 12. Also assume that the inducement should be associated with telephone rates. This seems more equitable than linking, say, highway grants to participation in telephone rate programs. See Stewart, supra at 1257.

152. Dayton-Goose Creek Ry. v. U.S., 263 U.S. 456 (1924), upholding 49 U.S.C. §15a(6), which read in part:

> If, under the provisions of this section, any carrier receives for any year a net railway operating income in excess of 6 percentum of the value of the railway property held for and used by it in the service of transportation, one-half of such excess shall be placed in a reserve fund established and maintained by such carrier, and the remaining one-half thereof shall...be...paid to the commission for the purpose of establishing and maintaining a general railroad contingent fund... .

153. 263 U.S. at 480.

154. 263 U.S. at 483.

155. ICC Commissioner Eastman in testimony before the House Committee on Interstate and Foreign Commerce in 1931 argued not merely for the repeal of the Recapture Clause, but for its retroactive repeal! He calculated approximately $378,000,000 was due to the fund, of which $8,000,000 had been paid. Entering the Great Depression, all the railroads were weak, and enforcement of the Recapture Clauses provisions rather than ensuring the strength of the industry might well have killed it. Implementation of the Recapture Clause had problems with the weakness of the industry, difficulties in valuation of property, and in the diversity of rates and companies involved. Hearings on H.R. 7116 and 7117 before the Committee on Interstate and Foreign Commerce, House of Representatives, 72d Congress, 1st Session, 9. 47 U.S.C. §15b(a) subsequently annulled the Recapture Clause (June 16, 1933). The new telephone rate regulation procedure under consideration would probably affect only AT&T Long Lines, in a healthy industry, with valuation procedures already in effect.

156. Congress cannot, in the exercise of the Commerce power or of any other power, violate the rights and privileges of citizens guaranteed by other Constitutional provisions. Nor will the courts hesitate to enforce these rights.

The example most applicable when considering the establishment of a uniform distance insensitive telephone rate structure is the prohibition against confiscatory rates. In 1886, the Supreme Court in considering state regulation of railroad rates asserted: "Under the pretence of regulating fares and freights, the State cannot require a railroad corporation to carry persons or property without reward; neither can it do that which in law amounts to a taking of private property for public use without just compensation, or without due process of law." The Railroad Commission Cases, 116 U.S. 307, (1886). See Gunther, supra at 555 n. 6, where he traces further judicial control over rate making. Thus a basic restraint upon any uniform rate structure established by Congress under the Commerce Power is that it must justly compensate all telephone companies involved.

157. Houston E. & W. Texas Ry. Co. v. U.S. (The Shreveport Rate Case), 234 U.S. 342 (1914).

158. 234 U.S. at 351, 352.

159. Godbey, supra at 9-12.

160. See The Transportation Act, 1920, 6 Va. L.R. 482 (1920).

161. Railroad Commission of Wisconsin v. Chicago, B.& Q.R.R., 257 U.S. 563 (1922).

162. 257 U.S. at 580.

163. 257 U.S. at 588.

164. 257 U.S. at 590.

165. 290 U.S. 70 (1933).

166. 290 U.S. at 75.

167. 290 U.S. at 75.

168. Mandeville Island Farms v. American Crystal Sugar Co., 334 U.S. 219, 232 (1948), construing the application of the Shreveport doctrine to enable antitrust law under the Sherman Act to reach intrastate conduct affecting interstate commerce.

169. People of State of Cal. v. C.A.B., 581, F.2d 954, 958 (1978), approving application of the Shreveport doctrine to the Federal Aviation Act.

170. Chicago M., St.P. & P.R. Co. v. Illinois, 355 U.S. 300, 305 (1957), citing North Carolina v. U.S., 325 U.S. 507, 511.

171. 355 U.S. at 305, citing Florida v. U.S., 282 U.S. 194, 212.

172. 282 U.S. 133 (1930), discussed _supra_ at 9.

173. 290 U.S. 70 (1933), discussed _supra_ at 58.

174. 47 U.S.C. §410(c).

175. 1971 U.S. Code Cong. and Adm. News 1511, 1514, quoting Senate Report No. 92-362.

176. _E.g._, S. 611 §222(a).

177. _E.g._, Senate Hearings, S.611 at 1331.