LEGAL ASPECTS OF STATE AND FEDERAL REGULATORY JURISDICTION OVER THE TELEPHONE INDUSTRY: A SURVEY

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Program on Information Resources Policy

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EXECUTIVE SUMMARY

. Controversy over whether the federal government or the states should regulate specific aspects of U. S. telecommunications has existed since the beginning of government involvement in the industry. Telecommunications firms that must plan and act under the present scheme of state and federal regulation are vitally concerned with the relative jurisdictions of the regulators under this dual arrangement. The scope of these jurisdictions also influences the prices that customers pay for telecommunications services.

. As a source book for those who wish to analyze current jurisdictional issues in the telephone industry, this report focuses on the <u>legal</u> development of jurisdictional boundaries between federal and state telephone regulators.

. These boundaries evolve, in part, from the need to square the jurisdictional provisions of the Communications Act of 1934 with regulatory policies that adjust in response to technical and market changes in the telephone industry.

. The Communications Act preserves significant areas of state regulatory authority. However, the major recent court decisions on jurisdiction reflect increased federal intervention in telephone markets and industry structure. These decisions illustrate the tension which present telephone industry places on the state/federal regulatory scheme.

. Three strands of thought predominate in the court decisions:

- The telephone network is a unified whole which impacts national interests. The courts' perception of such national interests may promote federal regulatory power.

- The Communications Act protects important but limited areas of state regulatory power.

- Concepts of U. S. federalism tend to favor the supremacy of federal authority over that of the states.

. Still, the cases do not define the absolute boundaries of state and federal interaction; indeed, federal and state regulators continually adjust the scope of their jurisdictions through formal and informal agreements.

. Federal antitrust measures, particulaly the AT&T Modification of Final Judgment, add a third dimension to the problems of allocating government power over the telephone industry.

Introduction

The health of the U.S. telephone industry and the quality of the services it provides are inextricably bound to the actions of state and federal regulatory agencies. This condition remains despite major changes in the industry's structure over the years. Indeed, although recent developments have led to increased competition among private firms in certain areas of the industry, federal and state regulation continues to define the extent and freedom of such competition. Analysis of current issues in the telephone industry obviously must consider the relationship between the industry's firms and industry regulation. This relationship ultimately rests on the legal authority of the regulators as defined by their enabling statutes and the judicial decisions that apply the statutes.

This paper presents a tutorial on one facet of governmental authority over telephone: the relative scopes of federal and state regulatory jurisdiction. Controversy over whether a state or a federal agency should regulate specific activities has existed since the beginning of telephone regulation. Such disputes often arise when a regulated firm attempts to justify its actions to one agency by claiming that another agency legally authorized it to act. The relative authorities of the federal government and the states are crucial to firms in the telephone industry that must plan and defend their actions under a dual regulatory scheme.

This study focuses on a legal analysis of the historical jurisdictional relationships between federal and state telephone regulators. The goal here is not to provide a definitive jurisdictional analysis of current issues such as the access charge proposals or regulatory responsibility for customers' complaints about telephone service. Rather, the paper attempts to be a "sourcebook" for readers who wish to perform such studies. To this end, detailed legal analyses of important past jurisdictional disputes are presented. These disputes cover a wide range of factual situations and thus explore many applications of the basic constitutional and statutory limits on federal and state regulation. The Communications Act of 1934 figures prominently in the paper's discussion. The Act of course is current law. Moreover, even though proposals for new telecommunications legislation have arisen repeatedly in recent Congresses, many of the proposals have been broadly based on the Act. Precedents set in past jurisdictional decisions may have great weight when and if such new legislation is passed.

Section 1 of the paper presents an overview of the institutions involved in state and federal jurisdictional disputes. Section 2 provides background on the early history of telephone regulation as well as the underlying influences of federalism and technological change on relative jurisdictions.

Section 3 gives a brief chronology of the regulation of competition in the telephone industry and of federal antitrust actions against the dominant firms. Section 4 outlines the major jurisdictional provisions of the Communications Act of 1934. Finally, Section 5 traces the development and resolution of state and federal jurisdictional conflicts by analyzing selected state and federal court decisions dating from the beginning of the 20th century. The decisions show long-term trends in court treatment of jurisdictional conflicts. Section 6 concludes this

Section 1 - Institutional Framework

A. Overview

The federal government has been a major participant in the recent structural changes in the U.S. telephone industry. There are two principal areas of change. First, the Federal Communications Commission (the FCC) has established a pro-competitive policy for many aspects of the industry, modifying the longstanding regulated monopoly status of the telephone business.[1] Second, the American Telephone and Telegraph Company (AT&T) has divested its 22 former subsidiary operating companies and limited its control over local telephone service in the U.S. The divestiture resulted from a consent decree known as the Modification of Final Judgment (the MFJ), which settled the Justice Department's 1974 antitrust suit against AT&T.[2]

Both of these developments are governed by federal statutory and common law. The FCC's deregulatory actions take place under the Communications Act of 1934 (the "Communications Act" or the "Act").[3] Federal antitrust law governs the MFJ.[4]

These events on the federal level significantly impact state participation in regulating the telephone industry. For purposes of this paper, the "telephone industry" includes those firms that are subject to regulation as "common carriers" under the Communications Act[5]; actual and potential competitors of such firms in providing point-to-point, voice quality communication service; and manufacturers of specialized telephone equipment for such firms.

The Communications Act provides for a system of regulation over the telephone industry that is divided between state and federal jurisdictions. In general terms, the FCC is empowered to regulate "interstate and foreign commerce in communication by wire and radio."[6] The Act prohibits the FCC from regulating "intrastate telephone communication service."[7] Instead, an agency or commission of each state's government regulates aspects of the industry which affect telephone service within that state. For example, the commissions may set rates for long distance intrastate telephone calls. Usually, such commissions regulate the telephone industry as a public utility; they may regulate electrical power, water, and natural gas service within their states as well as the telephone industry. State statutes define the powers of these commissions (hereafter referred to as the "state regulators" or "regulators").[8]

Governmental regulation at both the state and federal levels focuses on the availability and efficiency of the telephone service provided by the industry. The Communications Act and state statutes provide basic expressions of these policy goals which have been construed by the FCC, the state regulators, and the courts.[9] In general, rates for telephone calls are regulated with the goal of making service available to business and residential users at a "just and reasonable" charge[10] while still permitting "reasonable compensation"[11] to the firm that provides telephone service. In addition, the FCC and state regulators are empowered to rule on industry plans to introduce telephone service to new areas or abandon service in existing areas.[12] Moreover, the FCC and the states may set uniform technical standards for the operation of telephone equipment so that equipment owned by different firms in all parts of the country operates as a single efficient network.[13]

The jurisdiction of state regulators preserved by the Communications Act is not frozen by state law but exists subject to the discretion of the federal government. Where state regulatory policies over intrastate telephone service interfere with federal regulation over interstate telephone, the FCC may "preempt" or replace state regulations with its own, as in Computer Industry Association v. FCC:

> Courts have consistently held that when state regulation of intrastate equipment or facilities would interfere with achievement of a federal regulatory goal, the [FCC's] jurisdiction is paramount, and conflicting state regulations must necessarily yield to the federal regulatory scheme.[14]

For such preemption to apply, of course, the FCC must have a valid federal regulatory goal. The FCC has broad discretion in selecting such a goal; its jurisdiction to do so must be established under the Communications Act of 1934 and the goal must be "reasonable."[15] In addition, the state regulations must in fact conflict with the FCC regulations. Because interstate and intrastate telephone communications use the same facilities, the potential for such conflict is great.

Of course, Congress ultimately defines the extent of state regulatory power over the telephone industry, under the Commerce Clause of the U.S. Constitution.[16] New federal legislation conceivably could supplant the Communications Act and expand (or contract) the extent of federal regulatory jurisdiction over telephone services. Such legislation theoretically could extend federal control over entirely intrastate telephone activities. The scope of such control depends on Congressional interpretation of what constitutes "interstate commerce." The federal courts generally have upheld broad conceptions of interstate commerce in other areas of regulation. For example, the Supreme Court has upheld legislation which regulates the rates charged for wholly intrastate railroad activities that might affect the rates for interstate service.[17] The Court has also approved federal quotas for farm products such as wheat, even though the products are grown and consumed wholly within one state.[18] Congress thus apparently has considerable constitutional scope in defining the extent of federal power over telephone service. The Supremacy Clause of the Constitution commands state conformance to valid federal legislation,[19] although state regulators would undoubtedly attempt to influence any new federal communications legislation during its consideration by Congress.

The institutional force of the FCC's preemption powers and the broad powers of Congress under the Supremacy and Commerce clauses constrain state regulatory practices that could affect interstate telephone service. Conversely, in the recent period of federal participation in structural change, state regulators primarily have reacted and adjusted to the policies established at the federal level.[20] Although state regulators continue to participate in framing the issues and contesting the results of federal telephone policy, the special interests and concerns of <u>all</u> of the state regulators surely will <u>not</u> be accommodated at the federal level as the effects of increased competition and divestiture unfold. In order to adjust to federal initiatives, the state regulators must act within their legitimate jurisdictions or else face either FCC preemption or judicial reversal. However, the restructuring has complicated the responses of state regulators by changing the scope of their jurisdiction over telephone activities.[21]

B. Basic Divisions in Federal and State Telephone Regulation

Under the dual state/federal regulatory scheme, the FCC and the states have divided regulatory control over various aspects of the telephone industry. Where a regulated activity takes place wholly within a state's borders or wholly among different states, the division of control may be relatively straightforward. For example, regulation of rates for telephone calls between points within a single state is a commonplace and standard responsibility of that state, according to North Carolina Utilities v. FCC:

> Of course, rate making typifies those activities of the telephone industry which lend themselves to practical separation of the local from the interstate in such a way that local regulation of one does not interfere with national regulation of the other.[22]

Similarly, rate regulation for calls between points in different states is a logical "interstate" duty of the FCC. In this instance, the role of states as geographical as well as political entities simplifies the assignment of regulatory control.

Where telephone activities are not so easily assigned, conflicts between the FCC and state regulators may arise over the scope of their jurisdictions. The "shared" nature of the equipment which makes up the U.S. telephone network is a source of such conflicts. Telephone users can place and receive either interstate or intrastate calls through their "terminal equipment." Terminal equipment includes dial and touch telephones, multiline telephones, answering devices, and complex terminals such as the "private branch exchanges" (PBXs) which provide telephones and a switchboard for schools, hotels, and other businesses. Terminal equipment is connected via a cable known as a "line" or "loop" to a switching machine located at a "central office" owned by the local telephone company. One central office may serve several thousand loops; numerous central offices exist in every state. The switching machine at the central office routes calls either to another loop served by that central office or to another switch that can provide connections to still other central offices and other switches that provide still further options.[23] Most of this physical network of terminal equipment, loops, switches and interconnections is "shared" or jointly used in that it can carry either intrastate or interstate messages at the user's discretion. The division of regulatory jurisdiction over jointly used telephone equipment has been a longtime source of conflict between the FCC and the states. For example, courts have repeatedly upheld the FCC's preemption of state regulations concerning technical standards for the interconnection of terminal equipment with the rest of the network.[24] In these decisions, the courts relied on the doctrine of federal primacy over telephone communications embodied in the Communications Act to hold that the FCC's preemption was within its statutory jurisdiction, even though the terminals were used predominantly for intrastate communications. The FCC and the courts relied on a policy choice, the constitutional supremacy of the federal government over the states, to resolve a jurisdictional problem caused by the shared nature of the regulated equipment.

Section 2 - Background: Influences Affecting Jurisdictional Divisions in the Telephone Industry

Jurisdictional conflicts in telephone regulation could be avoided by a regulatory system that did not divide power between the federal government and the states. Examples of such systems include the complete absence of regulation, regulation solely by the states, regulation solely by the federal government, and state or federal ownership of the telephone industry. Indeed, the dual system of federal and state regulation over the telephone industry is largely a North American phenomenon.[25] Japan and Great Britain provide alternative examples of governmental control over telephone. Japan centralized all telephone regulation in a single national agency in 1915.[26] Great Britain nationalized its telephone industry after an initial period of growth and competition among private firms. However, recent Acts of Parliament permit private firms to enter limited competitive markets for common carrier telephone service. More dramatically, on December 3, 1984, the British government further denationalized its telephone industry by selling 50.2% of British Telecommunications PLC, formerly wholly owned by the government, to the public. Even with such public ownership, the British government remains a direct participant in the operations of its telephone industry.[27]

This section does not seek to explain why the dual regulatory system is appropriate for the United States, or why another system might be preferable in light of the characteristics of the U.S. telephone industry. Instead, this section presents historical, political and technical influences on the FCC and state regulators that affect the scope of their jurisdictions and the potential for conflicts under current law. First, the origins of U.S. telephone regulation are summarized. The concept of federalism then is discussed as a basic principle in structuring U.S. regulation. Finally, the impact of innovation on telephone regulation is briefly considered.

A. Chronology: The Origins of U.S. Telephone Regulations

After the invention of the telephone in 1876, the telephone industry was essentially unregulated until the 1890s.[28] After initial patent litigation, the Bell Telephone Company effectively used its original telephone patent to bar other firms from entering the telephone industry until the patent's expiration in 1894. Bell Telephone expanded in this period by becoming a central holding company that sold area franchise rights to local "operating companies" in exchange for their stock. At this time, only short distance telephone service was possible due to technical inadequacies. As a result, the operating companies concentrated on providing local telephone service within cities, which offered concentrations of potential customers.

After the Bell patent's expiration, competition in providing local telephone service and in manufacturing telephone equipment increased. Independent non-Bell operating companies (the "independents") moved into smaller towns and rural areas to provide local service where Bell operating companies did not exist. Some independents began direct competition with Bell operating companies in a few cities. The Bell companies countered by cutting prices, merging with competitors, suing competitors for patent infringement, and developing technology for a long distance telephone network.[29] This period of competition existed until 1913, when the Justice Department threatened to bring an antitrust suit against the Bell system under the Sherman Act because of alleged anticompetitive business practices. By this time, AT&T had replaced the Bell Telephone Company as the holding company for the Bell operating companies. AT&T settled with the Justice Department in a 1913 letter agreement known as the Kingsbury Commitment, in which, among other things, AT&T promised to halt acquisitions of competing independents and to permit independents to interconnect with AT&T's long distance network. However, this intervention by the Justice Department was not the first participation by government in the U.S. telephone industry.

Active government regulation of the telephone industry began in the late 1890s at the municipal level. During that period, several city governments granted franchise charters to telephone companies that wished to provide telephone service within city limits.[30] The charters governed rates for telephone service and served as legal barriers to entry for potential competitors. In addition, North Carolina and Louisiana had established state regulatory agencies by 1899.[31] These agencies controlled telephone rates within their states. At the same time, states such as Virginia, South Carolina, and Mississippi were regulating telephone companies by statute.[32] These states limited their powers to overseeing the financial structure of operating companies and had no power to regulate rates. However, by 1919 almost all the states had created regulatory agencies with jurisdiction over telephone service and rates within their boundaries.[33]

Formal federal regulation of telephone service began in 1910, when Congress amended the Interstate Commerce Act to give the Interstate Commerce Commission (the ICC) limited jurisdiction over interstate telephone companies.[34] Like many of the the early state regulators, the ICC had no direct power to regulate interstate rates. However, it could investigate user complaints and establish accounting standards for interstate operating companies.[35] ICC jurisdiction over the telephone industry continued in this limited form until 1934, when the Communications Act[36] vested regulatory control in the FCC. The AT&T-owned Bell system, the dominant provider of local and long-distance telephone service in the U.S. throughout this period, embraced both state and federal regulation from the onset. AT&T President Theodore Vail noted in 1915 that regulation "is as necessary for the protection of corporations from each other as for protection to, or from, the public."[37] Regulation protected AT&T by limiting new entry into the industry and by shifting responsibility for industry practices to the regulatory bodies.

> By accepting regulation voluntarily, Bell reduced the risk that unfavorable regulation would be imposed. The system of competing federal and state regulation, together with the complex Bell structure, prevented real regulatory control while providing the protection and legitimacy of a regulated utility . . . The acceptance of regulation was a risk-reducing decision.[38]

However, the early independents that competed with the Bell system also welcomed the introduction of state and federal regulation as a form of protection against Bell.[39]

As this account demonstrates, dual jurisdiction over the telephone industry has existed essentially since the start of government regulation in the field. The Communications Act of 1934, with its statutory allocation of jurisdictions, provides the continuing legal basis under the Commerce Clause for this dual arrangement.

B. <u>The Doctrine of Federalism Applied to State and Federal Regulatory Jurisdictions.</u>

The concept of federalism in the U.S. embodies a governmental structure consisting of states with significant sovereign powers under a central ("federal") government having broad but not absolute powers over the states. A major underlying goal of the federalist concept is the protection of individual rights and freedoms by fragmenting power among governmental entities.[40] The Constitution's grant to Congress of power over interstate commerce limits state power to pursue economic policies which discriminate against other states, citizens of other states, or free trade among the states.[41] Conversely, the Constitution's preservation of some state sovereign power assures that states can promote local economic interests to the extent that they do not conflict with Congress's commerce powers. Identification of such conflicts lies at the heart of Commerce Clause litigation. Federalism may be seen both as a rationale for dual regulatory jurisdiction and as a source for jurisdictional difficulties, as in D. F. Pegrum's 1949 analysis:

> Thus there results a central government with control over these matters which relate to the well-being of the whole country, and a series of state governments, with the latter enjoying, within the limitations of the federation set up, sovereign powers.
>
> The federal form of government gives rise to special problems in the control of economic activity. State governments enjoy widespread powers of regulation over economic life because of their jurisdiction over what are considered purely state matters.
>
> At the same time, economic activity persistently defies political boundaries . . . . [I]t frequently becomes extremely difficult to separate interstate from intrastate commerce . . . If the federal form of government is to remain, it will be necessary to recognize that the several states must continue to enjoy extensive control over economic activity.[42]

This passage illustrates the basic difficulty in allocating regulatory jurisdiction between the states and the federal government. As noted, the formalistic distinction between "interstate" and "intrastate" commerce based on political boundaries is little help in rationally allocating power between sovereigns in a federalist political system. Federalism certainly permits the system of regulatory jurisdiction now shared by the FCC and the states. However, the concept does not dictate such sharing. National interests could be found to dominate state sovereign interests to such an extent that federal control is mandated. Conversely, some economic matters may be so intimately connected to state sovereignty that federal regulation is barred. The courts repeatedly have relied on principles of federalism both to uphold the extension of federal regulation to intrastate economic activities[43] and to preserve aspects of state regulation against federal encroachment.[44] Indeed, the Supreme Court relies on federalist concepts to justify the judicial "balancing" of national and state interests which governs its recent decisions under the Commerce Clause.[45]

However, regulatory officials often ignore the inherent flexibility of the federalist concept when defending the scope of their agencies' jurisdictions in the political arena. For example, state regulatory officials may stress the concept of state sovereignty in advocating enlarged state jurisdiction over "local" telephone issues.[46] By equating federalism with state power, such statements inject political concerns directly into the jurisdictional question without otherwise clarifying the issue of what telephone industry activities are most appropriate for state regulation.

C. Technological Innovation: Restriction of State Jurisdiction

Commentators have cited the massive and continuing process of technological innovation in the telecommunications field as a major force leading to the restructuring of the telephone industry.[47] Technological innovation provided impetus for the restructuring in two major areas. First, innovations in the development of economical alternatives to standard means of providing telephone service allowed potential rivals of the regulated telephone companies to enter the long distance telephone service market and the telephone equipment market.[48] Such innovations, coupled with political and economic pressure, contributed to the FCC's policy of permitting competition in these markets.[49]

Second, technical innovations have blurred the distinction between computers and telephone networks. Telephone companies use specialized computers to switch and route telephone calls to the correct destinations; modern telephone terminal equipment often contains small computers that provide services such as call forwarding and message recording. Conversely, the telephone network can be used to link numerous computers, permitting them to communicate with each other. As a result, a collection of computers interconnected through telephone lines may actually operate as a single computer with distributed components.

In its Computer Inquiry I[50] and Computer Inquiry II proceedings,[51] the FCC considered how its regulatory policies should affect AT&T's

participation in providing computer equipment and services in totally unregulated markets. It also considered whether the terminal equipment market would continue to be regulated as permitted but not required by the Communications Act. The FCC ordered that terminal equipment be sold in an unregulated free market, subject only to requirements for standardized technical specifications.[52] Ultimately, the FCC decided to permit AT&T to establish a separate entity to compete in the newly deregulated market for terminal equipment and an unregulated market for "enhanced services", which roughly include computer processing services.[53]

In both of these areas, technological innovation contributed to FCC decisions that extended its jurisdiction at the expense of state jurisdictions. Computer Inquiry II deregulated portions of the telephone industry, such as terminal equipment pricing, that were previously regulated by the states. The technical innovations considered in that proceeding affected all portions of the telephone network, from terminal equipment to transmission links to switches for routing messages. Thus the FCC's "interstate" jurisdiction seems clear, as courts have repeatedly decided.[54] This pervasive technological impact argued strongly for FCC decision-making in order to impose a coordinated national policy in lieu of possibly uncoordinated state actions.

An additional policy argument for FCC jurisdiction over difficult technical issues is its allegedly great technical expertise compared to that of many of the state regulators. Such expertise presumably allows the FCC to make correct technical decisions; it may also permit the FCC to make technical decisions without undue dependence on information from interest groups such as the regulated firms.[55] Technological innovation has had a restrictive effect on state regulatory jurisdiction in the telephone industry to the extent that the innovations have contributed to FCC preemption of state regulatory power.

Section 3 - Evolution and Revolution: Competition and Divestiture in the Modern Telephone Industry

The AT&T divestiture of January 1, 1984, transformed the Bell system into an unaffiliated collection of seven regional holding companies plus AT&T and its subsidiaries. The divestiture affects most groups connected with the telephone industry: telephone companies and equipment manufacturers, state and federal regulators, and telephone users. In addition, the divestiture is the most far-reaching settlement achieved by the Justice Department in enforcing U.S. antitrust policy.

The divestiture did not take place in a vacuum. Instead, a gradual but accelerating introduction of competition in key areas of the telephone industry provided the context in which divestiture occurred. The FCC has established policies supporting increased competition in the markets for interstate toll or "long distance" telephone service and telephone equipment. AT&T's management has not made public its analysis of the business and legal factors that led to its concurrence in divestiture through the MFJ. However, the opportunity for increased profits through competition without constant federal scrutiny for antitrust violations may well have been a factor.

The FCC and court decisions that established competitive markets in the telephone industry did not have the immediate tangible impact of the divestiture. Instead, their effect was to erode a longstanding industry structure and regulatory scheme. In comparison, the divestiture, set in the matrix of regulatory change and antitrust pressures, is an extreme example of a business organization adapting to changing market and legal conditions.

This section provides a general summary of regulatory changes under the FCC, and of the divestiture. Jurisdictional conflicts among the FCC and the state regulators caused by these events are discussed in Section 5. Part A outlines the AT&T divestiture mandated by the MFJ. Part B develops in more detail the history of competition in the markets for interstate toll service and telephone equipment. The roles of the MFJ and of the FCC's actions in these markets are examined.

A. Divestiture: The Modification of Final Judgment

The MFJ settled the antitrust suit started in 1974 by the U.S. Department of Justice.[56] The complaint was filed in the U.S. District Court for the District of Columbia. The defendants in the suit were AT&T and two subsidiaries: the Western Electric Company and Bell Telephone Laboratories. The complaint alleged that the defendants conspired to monopolize interstate trade and commerce in "telecommunications service" and "telecommunications equipment" in violation of Section 2 of the Sherman Act.[57] The complaint defined telecommunications service broadly, to include most types of electronic communications other than broadcasting. Similarly, telecommunications equipment included all of the electronic equipment needed to transmit a message via telecommunications service.[58]

Because of the alleged conspiracy, the complaint claimed that AT&T and its defendant subsidiaries achieved monopolies and restrained competition in the markets for telecommunications service and equipment. As a result, purchasers in these markets "have been denied the benefits of a free and competitive market."[59]

For relief, the complaint asked that AT&T divest Western Electric Company ("Western"), its manufacturing subsidiary.[60] In addition, Western was to divest a sufficient amount of its assets to "insure competition in the manufacture and sale of telecommunications equipment."[61] Also, the complaint asked that the Long Lines Department of AT&T, which managed interstate telephone service, be "separated" from the AT&T-owned Bell operating companies, which provided intrastate telephone service, "to insure competition in telecommunications service and telecommunications equipment."[62] The complaint requested the separation to occur through AT&T's "divestiture of capital stock interests or other assets,"[63] i.e., through AT&T's <u>divestiture</u> of its 21 Bell operating companies.

As Part B will show, FCC actions after the filing of the complaint acted to lessen the extent of whatever monopolies AT&T held in telecommunications service and equipment. Nevertheless, the antitrust action continued through procedural disputes and pretrial maneuvering until trial began on January 15, 1981.[64] The Justice Department and the defendants presented an initial settlement proposal to the District Court on January 8, 1982. The court considered the proposal and approved it with modifications as the MFJ on August 24, 1982.[65] A partial summary of the MFJ follows.

The MFJ required AT&T to divest its ownership interests in the 21 Bell operating companies. AT&T complied with the MFJ by creating seven regional holding companies (the "divested companies") that now own the former Bell operating companies.[66] Following the terms of the MFJ, the divested companies are financially and legally independent of each other and of AT&T. This independence dates from January 1, 1984, the date of formal divestiture.

The MFJ also divided the market for telephone service between AT&T and the divested companies. The MFJ specified that the divested companies could provide service only within restricted geographical areas that it called "exchange areas."[67] This was a confusing word choice because regulators already commonly used "exchange" to refer to the entirely different concept of pricing for local service. The "exchange areas" of the MFJ are now officially known as LATAs, for "Local Access and Transport Areas." Generally speaking, the size of each LATA depends on population density and existing operating company services, facilities, and practices.[68]

Thus, under the MFJ's division of markets, the divested companies provide intraLATA telephone service, which includes local service and some intrastate toll service. InterLATA toll service is offered by AT&T and other firms in a competitive market.[69] AT&T agreed to transfer sufficient equipment and other assets to the divested companies so that they could provide adequate intraLATA service from the time of divestiture forth.

The MFJ recognized the organizational and technical difficulties that could be expected to accompany the division of the Bell system's integrated operations. Thus, despite the organizational independence of the divested companies, the MFJ requires them to provide a single organization to serve as "a point of contact for national security and emergency preparedness [and for] those services, such as administration and engineering, which 'can most efficiently be provided on a centralized basis.'"[70]

The MFJ places various restrictions on the divested companies. The divested companies must offer equal service and connections to all interexchange companies, with no preference to AT&T.[71] The MFJ requires that the divested companies show no favoritism to AT&T in purchasing equipment, planning, or other aspects of ordinary business relations.[72] In addition, the divested companies may not manufacture telephone equipment, although they can market it.[73] However, a divested company may petition the D.C. District Court to be permitted to enter the equipment manufacturing market or the interLATA market.[74]

The MFJ does not restrict AT&T from competing in the market for interLATA telephone service.[75] AT&T is restricted from participating in the "electronic publishing industry" over its own network, for a period of seven years after divestiture. The MFJ defines electronic publishing as

> [T]he provision of any information which AT&T or its affiliates has, or has caused to be, originated, authored, compiled, collected, or edited, or in which it has a direct or indirect financial or proprietary interest, and which is disseminated to an unaffiliated person through some electronic means.[76]

Despite this restriction, AT&T can still offer electronic directory services, similar to a Yellow Pages directory, that are accessible through a computer terminal.[77] AT&T may also provide the time, weather, and sports services that it was operating as of the date of the MFJ.[78]

The D.C. District Court retains jurisdiction over the MFJ for purposes of enforcement and to hear petitions for modifying it.[79] The MFJ also contains provisions allowing the Justice Department to inspect the books and records of the divested companies.[80]

B. The Emergence of Competition

The U.S. telephone industry enjoyed a long, stable period of regulation after the competitive struggles of the early 1900s ended with the Kingsbury Commitment and the advent of comprehensive federal and state control. For a long period after the establishment of the FCC in 1934, the industry as a whole was regulated as a natural monopoly. The basic assumption behind such regulation is that telephone companies realize large economies of scale in providing telephone service. These economies are so great that if more than one company provides telephone service in a given area, the costs of service would rise significantly because no one company realizes maximum economies of scale. For example, two telephone companies competing for customers in the same area might construct expensive duplicate networks of switches and cables, even though one such network is capable of serving all the available customers. If only one company served the area, the cost of its network would be spread among all the customers in the area. If two companies competed, the cost of two such networks would have to be spread.

The theory of natural monopoly regulation thus holds that government regulation of a single company in an area is preferable to allowing wasteful duplication among competing companies in the area. Although the single company holds a legally protected monopoly, government regulation of its rates and profits theoretically prevents it from gouging its customers.

The FCC and the states historically regulated all aspects of the telephone industry under natural monopoly assumptions. However, since 1956 a series of FCC decisions that have been upheld or expanded upon by the courts has modified regulation and introduced competition in two areas of the industry: telephone equipment, and interstate toll telephone service.

1. Telephone equipment

Telephone networks are composed of terminal, switching, and transmission equipment. Switching and transmission equipment form the physical backbone of the telephone network. Switching machines route calls and transmission equipment carries them over any distance. Terminal equipment, ranging from dial telephones to PBXs, connects telephone users to the network. FCC decisions have promoted competition in the market for terminal equipment. Moreover, FCC policies now permit AT&T and other formerly regulated companies to compete in unregulated markets for computers and computer services. Such products are closely related to the switching and transmission equipment developed by the telephone industry for its own use.

(a) Computers and Computer Services

AT&T historically has been the dominant U.S. producer of telephone equipment through its manufacturing subsidiary, the Western Electric Company (now subsumed in a new corporate subsidiary, AT&T Technologies, Inc.). Indeed, Western Electric produced telephone equipment only for use by the Bell system under the terms of a 1956 consent decree (the "1956 Decree"). The 1956 Decree settled a major antitrust action brought in 1949 against AT&T and Western by the Justice Department.[81] As a result, Western Electric manufactured transmission and switching equipment solely for the needs of the Bell system.

In 1966, the FCC began investigating the regulatory issues stemming from the convergence of communications and computer (or "data processing") technologies in its Computer Inquiry I proceeding. As noted in Section 2, the switching machines now used in the telephone network are basically specially programmed computers. The telephone network itself may be viewed as one huge computer. The switches are distributed processing units that communicate with each other over the telephone network's transmission equipment.

In the 1971 Computer Inquiry I decision, the FCC adopted rules to define the role of computers in the regulated telephone industry, based on the functions that the computers performed.[82] For example, the use of a computer to switch telephone messages constituted "communication" which could be regulated under the Communications Act.[83] The decision distinguished such "communication" from other unregulated computer functions known as data processing, defined as "the processing of information as distinguished from circuit or message-switching."[84] In addition, the FCC defined a class of "hybrid" services, that combine data processing and communication functions. Whether hybrid services were regulated by the Communication Act was to be determined on a case-by-case basis by analyzing which function dominated the hybrid service.[85] Computer Inquiry I also introduced the concept that regulated companies could compete in unregulated data processing markets only through an "arms-length" affiliate.[86]

However, the communication/computer distinction set out by Computer Inquiry I quickly became obsolete for technological and administrative reasons. For example, sophisticated terminal equipment that contained microcomputers appeared in the early 1970s. Such terminals could perform data processing as well as communications functions.[87] In addition, the processing capacities of computer-based telephone switches were becoming better understood. As a result, the FCC was faced with the possibility of a multitude of decisions on whether to regulate hybrid services.

The FCC undertook the Computer Inquiry II proceeding in 1976 to restudy its Computer Inquiry I classifications and to set up a more effective regulatory system to deal with the markets for computer and communication services.[88] The Computer Inquiry II decisions of 1980 and 1981 abandoned Computer Inquiry I's functional analysis. The decisions also set out a bolder philosophy for the participation of the regulated telephone industry in the unregulated market for computers and computer services.[89]

In Computer Inquiry II, the FCC replaced its functional classifications by distinguishing between "basic transmission service" on one hand and "enhanced services" and "Customer Premises Equipment" (CPE) on the other. Roughly speaking, basic service is what ordinary residential customers think of as telephone service, "a pure transmission capability over a communications path that is virtually transparent in terms of its interaction with customer supplied information."[90] Enhanced service is any other service provided to customers. CPE is terminal equipment, which is discussed in section (b) of this part.

Enhanced services include all the uses for which computers are bought and sold, other than basic transmission services:

> [E]nhanced service combines basic service with computer processing applications that act on the format, content, code, protocol, or similar aspects of the subscribers transmitted information, or provide the subscriber additional, different, or restructured information, or involve subscriber interaction with stored information.[91]

The FCC further declared that it would continue to regulate basic transmission service under the Communications Act.[92] However, the FCC claimed jurisdiction over enhanced services and terminal equipment, and deregulated the markets for both.[93] Enhanced services thus may be sold by regulated telephone companies in competitive markets that are separate from regulated basic service. To insure this separation in the nation's dominant telephone company, Computer Inquiry II required AT&T to establish an "arms-length" subsidiary to produce and market enhanced services.[94]

Computer Inquiry II finessed the antitrust restrictions imposed on AT&T by the 1956 Decree simply by listing some of the Decree's exceptions that might permit AT&T to market enhanced services and terminal equipment.[95] Computer Inquiry II did not purport to construe the 1956 Decree, and the D.C. Circuit upheld this approach on appeal.[96]

Computer Inquiry II opened up opportunities for regulated telephone companies to market computer services and computers free of regulation. For example, the manufacturing affiliates of AT&T and the GTE Corporation potentially can adjust their outputs of switching machines to produce computers for sale in competitive markets.

The 1982 MFJ decree actually supported the FCC's holdings in Computer Inquiry II.[97] The MFJ vacated the 1956 Decree, ending its restrictions on AT&T's line of business.[98] From an antitrust standpoint, AT&T is free to enter the market for data processing and other computer-related services. Thus, Computer Inquiry II governs AT&T on this issue under the Communications Act.[99] Similarly, the MFJ refused to hold on antitrust grounds that AT&T must create a separate subsidiary for providing enhanced services.[100] However, it did not abrogate the Computer Inquiry II requirement for such a subsidiary under the Communications Act.

(b) Terminal equipment

Until 1968, telephone companies generally required customers to rent or buy terminal equipment from them. The companies received this equipment from their own manufacturing affiliates, enforcing a closed market system.[101] Indeed, telephone company tariffs forbade interconnection of unapproved terminal equipment in broad terms, e.g.,

> No equipment, apparatus, circuit or device not furnished by the telephone company shall be attached to or connected with the facilities furnished by the telephone company whether physically, by induction or otherwise.[102]

Ostensibly, this restriction protected the telephone network from physical damage caused by terminal equipment having improper technical specifications.

In 1956, the U.S. Court of Appeals for the D.C. Circuit initially limited the breadth of such restrictions by holding that a tariff prohibiting attachment of a customer-supplied device called the Hush-a-Phone was "in unwarranted interference with the telephone subscriber's right reasonably to use his telephone in ways which are privately beneficial without being publically detrimental."[103] The Hush-a-Phone was a nonelectrical, cup-shaped mouthpiece that clipped onto a telephone's regular mouthpiece. The FCC subsequently ordered that tariffs be revised so that telephone companies would permit such "harmless" attachments.[104] This revision did not significantly affect the restrictions on most terminal equipment, which was electrically powered and thus potentially dangerous.

However, in 1968, the FCC's Carterfone decision required telephone companies to interconnect with mobile telephones through a radio device that customers could purchase and provide themselves.[105] The Carterfone physically connected with the customer's telephone to provide an acoustic link between the telephone and mobile phones installed in cars and tractors. The FCC, citing Hush-a-Phone, found that there was no evidence that the Carterfone harmed the telephone network. Thus, the tariffs barring the Carterfone were unreasonable and unduly discriminatory under section 202(a) of the Communications Act.[106]

Carterfone effectively permitted telephone customers to buy terminal equipment from suppliers other than their telephone companies for their own use. In response, the telephone companies required customers who provided their own terminals to rent separate interface devices which were designed to protect the telephone network from faulty terminals. The FCC approved tariffs requiring such devices in 1968.[107] After much study, the FCC eliminated the interface program in 1975 and permitted "certified" customer-supplied terminals to be connected directly to the telephone network.[108] In effect, manufacturers of terminal equipment were required to obtain certification from the FCC that their equipment met the technical standards required by the telephone companies. This program withstood court challenges[109] and spurred competitive growth and entry into the market for terminal equipment.[110] Even so, telephone companies continued to lease or sell terminal equipment to their customers at regulated rates. Since many customers historically had dealt solely with their telephone companies for terminal equipment, the market was still not highly competitive.

However, the deregulatory trend stemming from Hush-a-Phone culminated in the FCC's 1980 Computer Inquiry II decision.[111] As with enhanced services, the decision discontinued rate regulation of terminal equipment. Terminal equipment was to be sold or leased, even by telephone companies, in a competitive, deregulated market separate from the provision of regulated basic service.[112] Indeed, Computer Inquiry II required AT&T to market terminal equipment, like enhanced services, through a separate, arms-length subsidiary. The decision's ultimate goal is to "unbundle" costs from the rate base of the regulated telephone companies after a transition period.[113]

Computer Inquiry II was the capstone of the FCC's competitive policies regarding terminal equipment. The MFJ supports the decision's separation of the terminal equipment market from regulated basic service. As with enhanced services, the MFJ does not alter Computer Inquiry II's requirement of an AT&T separate subsidiary for marketing terminal equipment.[114] Of more interest, the MFJ forbids the divested Bell operating companies from manufacturing terminal equipment, to prevent the companies from retarding competition by purchasing their own equipment. However, the MFJ does permit the divested companies to market terminal equipment. This holding is designed to promote the antitrust concerns of the MFJ by encouraging market competition between the divested companies and AT&T.[115] Because of Computer Inquiry II's deregulation, any terminal equipment marketed by a divested company is not included in its rate base.[116]

2. Toll Telephone Service

After passage of the Communications Act of 1934, the FCC regulated interstate toll ("long distance") service as a natural monopoly. AT&T, through its Long Lines Department, was the dominant interstate carrier. It thus enjoyed a protected monopoly in this market. However, the FCC gradually introduced competition into the interstate market through a series of decisions and court appeals beginning in 1956.[117] As in the case of terminal equipment, these decisions were not the fruit of an unfolding master plan. Rather, the FCC acted in a piecemeal fashion, by deciding individual cases rather than through comprehensive policy making. Indeed, from 1956 until 1974, the FCC's pro-competitive decisions only dealt with the market for interstate private-line services. In this market, telephone companies lease "dedicated" communications channels between two or more specific terminals to customers such as businesses with several locations. Depending on usage, private-line charges may be lower than charges for service through the public telephone network.

After World War II, the FCC reserved the microwave radio frequencies above 890 megahertz for AT&T. AT&T proposed to use these bands of the radio spectrum for private-line service to customers. The FCC generally permitted firms other than AT&T to use these frequencies only if AT&T did not have customers for them.

However, the FCC began reexamining its policy in 1956. In the Above 890 decision of 1959, the FCC removed its limitations on the use of these frequencies.[118] Anyone was permitted to build or use radio sets operating at frequencies greater than 890 megahertz. In this way, customers could provide for their own special communications needs. In addition, producing the radio equipment would permit manufacturers to compete with Western Electric; such competition might encourage technical innovation.[119] Like Hush-a-Phone, the Above 890 decision was a precursor of FCC decisions affecting larger markets.

Such a decision occurred in 1969, when the FCC granted a license to Microwave Communications, Inc. (MCI) to build a small microwave telephone network between St. Louis and Chicago.[120] MCI planned to offer private-line service similar to that of AT&T at lower cost. Unlike the AT&T service, MCI customers could share channels and lease channels part-time. AT&T contested the license application.

In granting the license, the FCC held that AT&T did not prove that its revenues would be harmed by MCI. More importantly, the FCC stressed that competition in this area provided consumers with more diverse and more suitable options for their communications needs. The FCC was careful, however, to limit its decision to MCI alone.

MCI's entry prompted numerous companies to apply to the FCC for permission to construct private-line microwave systems. In its 1971 Specialized Common Carrier decision, the FCC established procedures for approving such applications that favored entry of competitors in the microwave private-line market.[121] The FCC believed that free entry into the market would cause it to expand without hurting AT&T's revenues. The FCC did rule that it would permit AT&T to lower its prices for private-line service if new firms directly competed against it.[122] However, AT&T was required to give the competing carriers access to the local exchanges it controlled through its Bell system operating companies. This insured that the new competitors would not have to build local networks to serve each of their customers. Such facilities would have been a wasteful duplication of the Bell local network and would have financially burdened the new competitors. Instead, customers could access the competing private-lines through their Bell telephones.

Even before Above 890, AT&T had protected itself against new competitors in the private-line field by lowering prices for selected private-line services.[123] These efforts continued through the 1960s and intensified after the 1971 Specialized Common Carrier decision.[124] During this entire period, the FCC held numerous proceedings to determine whether the price cuts were unlawful as "discriminatory" under the Communications Act.[125] The trend of FCC decisions was to hold that most proposed AT&T price cuts were invalid as being unreasonably low. In essence, the FCC was protecting the new private-line competitors from AT&T's market power.

After Specialized Common Carrier, the FCC further solidified the position of new competitors in the private-line market with its Resale and Shared Use decision in 1976.[126] The FCC eliminated AT&T tariffs restricting the resale and sharing of its interstate private-line services. Thus, competitors could buy services from AT&T at low bulk rates and resell them as their own. This decision permits the competitors "to interconnect freely and . . . to complete portions of routes that must traverse low density, sparsely populated, and hence presumably not very profitable territory."[127] The FCC felt that this holding would lower prices by making AT&T's low bulk rates more widely available.

The 1971 Specialized Common Carrier decision permitted competition only in the relatively specialized private-line market. However, in 1974, the FCC authorized MCI to offer interstate "Foreign Exchange" (FX) service in direct competition with AT&T. FX service permits a customer in a local exchange in City 1 to call any number in a distant local exchange of City 2 without dialing an area code and without paying standard long distance charges. In its decision,[128] the FCC permitted MCI to offer FX service using Bell system local exchanges in City 1 and City 2. Thus, MCI could compete with an AT&T service using AT&T-owned facilities. More importantly, FX service is not a "pure" private-line service as the FCC previously had permitted MCI to provide. The ability to call anyone in City 2's local exchange makes FX more similar to conventional telephone service.

MCI then moved aggressively to compete in the major market for interstate toll telephone service. Unlike private-line service, a customer could use MCI facilities from any telephone, and could call any telephone in any city which the MCI network reached. MCI filed a tariff with the FCC for its toll service, known as "Execunet," in 1974. Rates for Execunet were to be lower than for comparable AT&T toll service.

After an initial complaint by AT&T, the FCC studied MCI's attempt to compete in this new market and held in 1976 that Execunet could not be offered.[129] The FCC stated that it intended the Specialized Common Carriers decision to apply only to private-line service. However, the Court of Appeals for the D.C. Circuit reversed the FCC on appeal in 1977.[130] The court held that MCI could compete with AT&T unless and until the FCC specifically found that such competition was against "public convenience and necessity" as required in the Communications Act.[131]

After the first Execunet struggle, the FCC attempted to block Execunet by holding that AT&T only had to connect MCI to its local exchanges for MCI's private-line services, not for Execunet.[132] This would require MCI to construct its own local exchanges for its Execunet customers, which could be extremely expensive for MCI. The Court of

Appeals for the D.C. Circuit reversed this decision as well, holding in 1978 that restriction of such an essential component of the Execunet service was contrary to the court's first Execunet decision.[133]

In response to the Execunet decisions, the FCC initiated a 1978 proceeding in Docket 78-72 to examine whether interstate toll telephone service should "be provided on a sole source basis (i.e., free from direct competition)."[134] After consideration, the FCC held in 1980 that events in the aftermath of Execunet required a competitive interstate toll market.[135] Indeed, the FCC generally found that competition in this market would be beneficial. Thus, the FCC officially adopted a policy of open entry into the interstate toll market.[136]

Although the D.C. Circuit's second Execunet decision required AT&T to provide MCI and other interstate toll competitors access to its local exchanges, the decision did not specify the compensation arrangements for such access. This compensation is commonly known as the "access charge." Docket 78-72 has remained open to consider proper access charges to be paid the operating companies who own the local exchanges.[137] Because of the FCC's limited jurisdiction, Docket 78-72 considers only interstate toll access charges.[138] Docket 78-72's proposals for access charges have been the subject of considerable political and technical controversy.[139]

As Docket 78-72's considerations continued, AT&T, MCI, and other interexchange competitors paid access charges according to an interim agreement known as ENFIA, meaning "Exchange Network Facilities for Interstate Access." The FCC approved ENFIA in 1979 in the wake of the Execunet decisions.[140] Although ENFIA was scheduled to expire on April 15, 1982, the FCC kept it in effect until May 25, 1984, when new interstate access charge tariffs took effect.[141] The FCC itself had described ENFIA as a "temporary 'rough justice' solution until other compensation arrangements are prescribed by this Commission or by new legislation."[142]

The emergence of a competitive interstate toll telephone market has created new tasks for the FCC, such as the definition of access charges. However, the FCC has also moved strongly to deregulate aspects of the interstate toll market, apparently trusting competition to efficiently allocate prices and services. This modification of previous regulatory practices has occurred since Execunet and the commencement of Docket 78-72.

The FCC opened Docket 79-252 in 1979 to investigate how regulation for competition should proceed.[143] In its First Report and Order, the FCC classified competitors as either dominant or non-dominant.[144] A carrier was defined as dominant if it possessed market power, i.e. power to control price. The FCC held that AT&T and the established "independent" telephone companies were dominant; new interstate toll competitors such as MCI were non-dominant. Under the First Report's scheme, dominant companies were subject to full FCC regulation. In contrast, non-dominant firms were subject only to "streamlined" requirements for the filing and approval of tariffs and for authorization to construct new facilities. The FCC based the streamlined procedures on a presumption that actions by non-dominant firms are lawful.[145] Expanding on this initial action, the FCC's Second Report and Order in Docket 79-252 reasserted that its deregulatory efforts were consistent with its duties under the Communications Act.[146]

The FCC then exempted resellers of basic services[147] from filing tariffs or applying for authorization to begin or discontinue service.[148] The FCC based its decision on the fact that such resellers own no physical networks but simply buy their services from other, regulated firms.[149]

The FCC continued modifying its regulation of the interstate toll market in Docket 79-252's *Fourth Report and Order*, released in October, 1983.[150] The *Fourth Report* basically eliminated even the streamlined tariff and facilities authorization procedures for the non-dominant firms in the interstate toll market.[151] Instead, the FCC declared a policy of "forbearance" in regulating these firms. Under forbearance, the firms need not file tariffs or facilities reports with the FCC. However, the non-dominant firms are still subject to regulatory hearings and action based on complaints to the FCC about their rates or services.[152] The *Fourth Report and Order* is not limited to deregulation of the interstate toll market; firms in other, smaller telecommunications markets were also reclassified as non-dominant rather than dominant and subjected to streamlined regulations.[153] Docket 79-252 remains open to consider further FCC deregulation.

To complement Docket 79-252, the FCC opened Docket 83-992 in October, 1983, which proposes to reduce tariff filing requirements for all remaining dominant carriers.[154] In addition, Docket 83-1147 was opened in November, 1983 to consider the deregulation of AT&T interstate toll service. The FCC does not intend to deregulate AT&T through this docket. Rather, the docket is designed merely to "begin the public policy discussion on regulatory practices regarding AT&T which will serve the public interest."[155]

The MFJ's policies on competition in toll and private-line services are related to those of the FCC. However, the MFJ impacts a broader range of telephone services than the FCC's policies do. For instance, the MFJ deals with the market for "telecommunications services," which includes but is not limited to toll and private-line services. The MFJ's broader scope applies to its geographic coverage as well. Consistent with its jurisdiction under the Communications Act, the FCC's decisions explicitly deal with interstate markets for telephone service. In contrast, the MFJ provides for competition in the entire interLATA market,[156] so that both interstate and intrastate interLATA services may possibly be offered competitively. Because the MFJ does not distinguish between interstate and intrastate interLATA services, the regulatory jurisdiction for each must be resolved under the Communications Act. The effects of this holding on state and federal regulatory jurisdiction will be discussed in Section 5. This section will refer to "interLATA toll service" when discussing the MFJ's policies regarding competition in the toll market.

The MFJ's principal tool to promote interLATA toll competition is the divestiture of the Bell operating companies from AT&T. In approving the MFJ, the District Court for the District of Columbia held that the divestiture removes "the two main barriers that previously deterred firms from entering or competing effectively in the [interLATA] market."[157]

First, because of the divestiture, AT&T cannot discriminate against competitors by providing them with technically inferior connections to the local exchanges of the Bell operating companies.[158] A major claim of the Justice Department in its suit was that the operating companies provided poor electronic connections to AT&T's competitors and very good connections to AT&T, permitting AT&T to provide higher quality service. After divestiture, AT&T no longer controls the connections to local exchanges. Indeed, the MFJ requires the divested operating companies to provide "equal access" to their local exchanges to AT&T and its interLATA competitors.[159]

Second, divestiture prevents AT&T from subsidizing the prices of its interLATA toll service with revenues from intraLATA or local service. Conversely, AT&T cannot shift costs from its competitive services to any regulated intraLATA service.[160]

Because of divestiture's broad pro-competitive effects, the MFJ does not include any specific restriction on AT&T's business practices in the interLATA toll market.[161] Indeed, the court found that although AT&T's market share was high, AT&T after divestiture will not possess "monopoly power" in the legal sense of "the power to control prices or exclude competition."[162]

In dealing with the role of the divested companies in the interLATA toll market, the MFJ places more restrictions on their business practices than on AT&T. As mentioned above, the divested companies are to provide connections "equal in type, quality and price" for AT&T and competing interLATA carriers.[163] Moreover, the divested companies must upgrade existing inferior connections to AT&T competitors. The MFJ set September 1, 1986, as the date of completion for the upgrade, with "equal access" to be enforced after that date.[164] Each divested company must file tariffs explaining its schedule for upgrading the connections. Tariffs must be filed with state regulators for intrastate connections and with the FCC for interstate connections.[165] The divested companies are required to charge the interLATA carriers rates for their connections that vary according to cost. Thus, a divested company must charge more for a high quality connection than a poor connection if the high quality connection costs more to provide.[166]

Although the goal of the equal access provisions is to eliminate unfair AT&T advantages in the competitive interLATA market, the MFJ contains minor exceptions to the equal access requirement. For example, under the MFJ, telephone users are able to place long distance calls over AT&T facilities by dialing no more than 11 digits, even though calls dialed over competitors' facilities would require 14 digits. The court accepted the explanation of AT&T and the Justice Department that this discrepancy is necessarily caused by constraints in the national area numbering plan administered by the FCC.[167] Also, the divested companies are permitted to provide billing services for only one interLATA carrier "which will presumably be AT&T."[168] Thus, one interLATA competitor will have its charges included in a divested company's bill for local service. All other competitors will have to send separate bills to their customers, an inconvenience which may be a competitve disadvantage. In approving this exception, the District Court noted that the public interest will be served by the economies of joint billing. However, the MFJ requires the divested companies to include a caption stating that AT&T and the divested company are not related.[169]

Apart from the equal access requirement, the MFJ forbids the divested operating companies from participating in the interLATA market, e.g. from competing in toll services with AT&T and MCI.[170] Such competition would undermine a basic goal of the divestiture: to separate the competitive interLATA market from the regulated intraLATA service. Participation by the divested companies in the interLATA market would give the companies incentives to violate the equal access connection requirements.[171] Moreover, the divested companies might be able to cut interLATA prices through cross-subsidies from their regulated local services.[172]

The MFJ's support of competition in the interLATA toll market contrasts with the FCC's earlier caution in approving such competition in the Execunet proceedings.[173] However, the FCC laid the groundwork for the emergence of the competitive toll market by its earlier decisions through Specialized Common Carrier.[174] The MFJ accepted the reality of the existing market and tailored its restrictions to promote competition, pursuant to basic antitrust goals.

Section 4 - The Communications Act of 1934: Statutory Bases for Federal Regulatory Jurisdiction over the Telephone Industry

A. General Provisions of the Act Regarding the Telephone Industry.

The Communications Act of 1934[175] is the key statute controlling the telephone industry. The Act created the FCC and continues to provide the basic guidelines for federal regulation of the industry. Because of the federal government's broad constitutional powers over interstate commerce, the FCC's interpretation of the Act in asserting its regulatory authority affects the ultimate scope of state regulatory authority over intrastate telephone operations. The first section of the Communications Act creates the FCC

> For the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States a rapid, efficient, nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges . . . and for the purpose of securing a more effective execution of this policy by centralizing authority heretofore granted by law to several agencies and by granting additional authority with respect to interstate and foreign commerce in wire and radio communication.[176]

Courts have consistently required the FCC to justify its actions on the basis of promoting efficient communications with adequate facilities at reasonable charges. Indeed, the FCC may not pursue a general economic or political policy without justifying that policy on the grounds of efficiency or the public interest; just as the FCC "is not free to create competition for competition's sake, it is not free to propogate monopoly for monopoly's sake. The ultimate test of industry structure . . . must be the public interest."[177]

The FCC's jurisdiction under the Act includes both telephone communication, i.e. electronic transmissions directed between two discrete points, and broadcast or area communication, i.e. radio or television transmission over a general region. The FCC oversees the telephone industry by regulating so-called "common carriers" engaged in "interstate or foreign communication by wire and radio."[178] On its face, the Act's definition of common carrier seems to be a model of circularity:

> "Common carrier" or "carrier" means any person engaged as a common carrier for hire, in interstate or foreign communication by wire or radio or in interstate or foreign radio transmission of energy, except where reference is made to common carriers not subject to this chapter; but a person engaged in radio broadcasting shall not, insofar as such person is so engaged, be deemed a common carrier.[179]

Beside excluding radio broadcasters from classification as common carriers, the definition is somewhat self-referential. However, "common carrier" is a legal term of art in the context of the law of commerce regulation. The Court of Appeals for the D.C. Circuit has applied this common law meaning in interpreting the Act's definition of common carrier. The court found that the chief characteristic of a common carrier is its "quasi-public character, which arises out of the undertaking to carry for all people indifferently. . . .[A] specialized carrier whose service is of possible use to only a fraction of the population may nonetheless be a common carrier if he holds himself out to <u>serve</u> <u>indifferently</u> <u>all</u> <u>potential</u> <u>users</u>."[180] An additional component of common carrier status necessary in the telecommunications field is that customers of the carrier "transmit intelligence of their own design and choosing."[181] Thus, companies that provide interstate telephone service for the public at large fall squarely into the Act's common carrier category for purpose of FCC jurisdiction.

The Act requires all interstate common carriers to furnish communication service without discrimination, "upon reasonable request therefor."[182] In addition, the rates and regulations for such service must be "just and reasonable."[183] Section 202 explicitly prohibits "unjust or unreasonable discrimination" in common carrier rates or practices.[184] Sections 203 through 205 of the Act lay out a hearing and review process for approving the rates and regulations (the "tariffs") of the common carriers. The FCC has authority under section 205 to prescribe just and reasonable charges and regulations if it finds proposed tariffs to be unreasonable.

In addition, the FCC may regulate the technical characteristics of equipment furnished to common carriers, even if such equipment is manufactured by firms that do not qualify as common carriers. Section 215 together with Section 151 of the Act provides the statutory basis for this authority, which judicial interpretation has established.[185] Finally, the Act requires interstate common carriers to obtain approval from the FCC in the form of a "certificate of convenience" in order to extend, acquire or discontinue telephone or telegraph lines in any area.[186] Lines are defined in section 214(a) as "any channel of communication established by the use of appropriate equipment." Courts have interpreted "lines" more broadly to signify the provision of communication service to an area.[187] Thus "lines" may include radio channels as well as wires or cables.

Under section 214, <u>all</u> carriers to which the section applies must obtain a certificate of convenience from the FCC whenever they intend to <u>discontinue</u> service. This apparently reflects concern for the telephone users who would be affected by the discontinuance. In contrast, section

214 lists some specific instances when a certificate is <u>not</u> needed for <u>extensions</u> or <u>acquisitions</u> of lines. For example, extension of "local, branch, or terminal lines not exceeding ten miles in length" does not require an FCC certificate of convenience.[188] Other exemptions from the certificate requirement of a jurisdictional nature are discussed below.

B. Jurisdictional Sections of the Act

The jurisdictional sections of the Communications Act set out the areas of telephone regulation left to the states. Section 151 defines the basic constitutional requirement for FCC jurisdiction by providing for regulation of "interstate and foreign commerce."[189]

However, section 152(b) provides more specific constraints:

> (b) Except as provided in section 224 of this title and subject to the provisions of section 301 of this title, nothing 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, or (2) any carrier engaged in interstate or foreign communication solely through physical connection with the facilities of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (3) any carrier engaged in interstate or foreign communication solely through connection by radio, or by wire and radio, with facilities, located in an adjoining State or in Canada or Mexico (where they adjoin the State in which the carrier is doing business), of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (4) any carrier to which clause (2) or clause (3) of this subsection would be applicable except for furnishing interstate mobile radio communication service or radio communication service to mobile stations on land vehicles in Canada or Mexico; except that section 201 to 205 of this title shall, except as otherwise provided therein, apply to carriers described in clauses (2), (3), and (4) of this subsection.[190]

The four subsections of section 152(b) limit FCC jurisdiction in both general and specific ways. Subsection 152(b)(1) is the fundamental jurisdictional limitation of the Communications Act. The FCC has no jurisdiction over rates or practices concerning "intrastate communication service by wire or radio of any carrier."[191] At one extreme, the Act will not apply at all to a common carrier that serves users in only one state, with no physical facilities in any other state, and with no connections to any other carrier that provides interstate service. Only state regulation will apply. At the other extreme, a carrier that only provides interstate or foreign service, e.g. connections between states or between the U.S. and other countries, is under the sole jurisdiction of the FCC. No state would have jurisdiction. However, questions of state/federal jurisdictional allocation arise when a carrier provides both intrastate and interstate service to users. In general, portions of the carrier's rates and services will be regulated by the states in which it provides intrastate service, while the FCC will regulate interstate service. However, the exact extent of intrastate versus interstate service has been extensively litigated, since the Act does not define what it means by "intrastate" service.[192] Such litigation indicates conflicts over the scope of state and federal regulatory jurisdictions. It may also reflect the efforts of private firms to pit the FCC and the states against each other in order to avoid effective regulation by either. In any event, the intrastate/interstate service distinction of subsection 152(b)(1) remains the basic jurisdictional boundary for telephone regulation.

Section 152(b)(2) withholds from the FCC jurisdiction over common carriers who only engage in interstate or foreign communication through physical connections with other, unaffiliated carriers.[193] This provision thus preserves state jurisdiction over common carriers with physical facilities located in a single state. The Act labels these carriers as "connecting carriers."[194] As the Congressional floor debates on the Act show, the connecting carriers protected by this subsection include the small independent telephone companies that provide intrastate telephone service in areas not covered by the Bell companies.[195] The subsection forbids relationships of "control" or "common control" between a connecting carrier and any interstate carriers to insure that the connecting carrier indeed does not have interstate facilities.[196] Before the AT&T divestiture, this language blocked the Bell system operating companies that were located in single states from having connecting carrier status.

Subsections 3 and 4 of section 152(b) elaborate section 152(b)(2)'s goal of limiting regulatory jurisdiction over connecting carriers to the states. The subsections were added in 1954 to address a question caused by innovations in communications technology.[197] In the period after World War II, telephone companies started to use microwave radio instead of wire lines as a means of communication. Subsections 3 and 4 specify that <u>radio</u> links to unaffiliated interstate carriers do not subject connecting carriers to FCC jurisdiction.[198] Subsection 3 parallels the structure of subsection 152(b)(2). Subsection 4, however, permits FCC jurisdiction over connecting carriers if such carriers provide <u>interstate or foreign mobile</u> radio communication service. This reflects two facts emerging at the time that subsections 3 and 4 were added. First, mobile telephone service for cars had become technologically feasible.[199] Second, the postwar increase in automobile travel opened the possibility of a significant volume of interstate communications using mobile telephone, for which the FCC would retain jurisdiction.

Despite its limitation of FCC jurisdiction over connecting carriers, section 152(b) preserves some FCC power over these carriers. If there were no federal jurisdiction, the possibility would remain that connecting carriers and state regulators would adopt discriminatory rates or practices, in order to hinder interstate telephone service.[200] To prevent such discrimination, section 152(b) states that sections 201 through 205 of the Act still apply to the connecting carriers except as those sections otherwise provide. These sections, described above, "are those providing for the regulation of rates and prohibiting unjust discrimination in interstate and foreign service."[201]

Of course, sections 201 through 205 have their own jurisdictional restrictions which apply to all common carriers including connecting carriers. For example, section 201(a) expressly places a duty on "every common carrier engaged in interstate or foreign communication by wire or radio" to furnish such service upon reasonable request.[202] This language places connecting carriers within the scope of section 201. Connecting carriers do engage in interstate or foreign communication, even if solely through connection with interstate carriers. Despite this analysis, in the 1977 case of United Telephone Company of the Carolinas v. FCC,[203] the Court of Appeals for the D.C. Circuit held that connecting carriers are only subject to the requirements of section 201(a) "tangentially because they have chosen to connect to interstate carriers."[204] The court went on to hold that connecting carriers are free to remove themselves from the FCC's jurisdiction simply by removing their connections with interstate carriers.[205] Theoretically, a connecting carrier could choose whether it is to be regulated by the FCC or by its state by changing the interconnections of its telephone network. However, the opinion does not consider the Act's controls on discontinuance of service by carriers.[206]

In contrast, section 202's ban on unjust or unreasonable discriminations or preferences applies to "any common carrier" and thus all connecting carriers. However, section 202 is not applicable to carriers that only provide intrastate service.[207]

Sections 203 and 204 prescribe the requirements for filing and revising tariffs with the FCC, for FCC modifications of the tariffs, and for FCC hearings regarding the tariffs. Section 203 explicitly excludes connecting carriers from the filing requirements and thus from the hearing requirements of section 204.[208]

However, connecting carriers are subject to section 205 of the Act, which gives the FCC the power to prescribe just and reasonable charges and regulations for "any carrier or carriers," after a full opportunity for a hearing.[209] Connecting carriers are not directly impacted by section 205 because they are not required to file tariffs with the FCC. Case law interpreting the scope of section 205's authority does not exist. Any tariffs voluntarily filed with the FCC by connecting carriers would be subject to prescription. Furthermore, connecting carriers connect with interstate carriers to provide interstate or foreign service to their users. Section 205 requires connecting carriers to agree to whatever tariffs the FCC legitimately prescribes for the interstate carriers.

Section 152 (b) does contain other exceptions to its general policy of reserving intrastate regulatory jurisdiction to the states. These exceptions deal with jurisdiction over non-common carrier matters. For example, section 152(b) does not apply to section 224, which sets out its own jurisdictional scheme for regulating cable television "pole attachments."[210] Also, section 301 of the Act, which asserts federal power over radio licensing, has its own jurisdictional requirements.[211]

As mentioned above, section 214 of the Act requires carriers to obtain certificates of convenience from the FCC for the extension or discontinuance of service.[212] Several jurisdictional limitations restrict the duty of carriers to obtain such certificates when extending telephone "lines," i.e. service. Indeed, no certificate is required for extending or acquiring "a line within a single State unless such line constitutes part of an interstate line."[215] This preserves the interstate/intrastate distinction of section 152(b)(1). It also preserves that section's key interpretational problem: when is an intrastate line "part of an interstate line?"

Consider section 214's application to connecting carriers. By the terms of sections 152(b)(2)-(4), section 214 does not apply to connecting carriers. However, such carriers could lay telephone lines or install radio relays that are physically "part of an interstate line." The extension of such lines could seriously affect interstate communications. For example, a connecting carrier could build a network of intrastate lines that converge on one switch of an interstate carrier. The volume of calls to and from the intrastate lines could overload the capacities of the interstate carrier's switch, thus degrading the quality of interstate service. Assuming that section 214 does not apply to the connecting carrier, the FCC has three options. First, it could rely on the relevant state regulators to limit the extension of lines by the connecting carrier. Second, the FCC could attempt to regulate the connecting carrier under its section 201-205 powers. The argument would be that building the lines would cause a discrimination or preference in interstate service, since users would have the quality of their interstate service degraded. Third, the FCC could ignore section 214 and invoke its residual power under section 154(i) of the Act:

> The [FCC] may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this chapter, as may be necessary in the execution of its functions.[214]

The FCC has successfully invoked this residual power in order to require a connecting carrier to file a tariff describing its interstate connections, despite the exemption of section 203(a).[215]

No court has yet ruled on section 214's applicability to connecting carriers. However, the Fifth Circuit Court of Appeals has stated in <u>dicta</u> that

> [t]he reach of Section 214 is not limited to common carriers, referring as it does simply to "carriers" and thus by necessary implication a "connecting carrier" may be subject to the certification requirements of that section if an exemption is not otherwise available.[216]

This analysis is questionable because it seems to turn on an unjustified distinction. The court bases its holding on a distinction between "common carriers" and "carriers." This distinction does not exist. The Act defines common carriers and carriers synonymously.[217] Furthermore, the Act defines a "connecting carrier" as a "carrier."[218] Logically, a "connecting carrier" is thus a "common carrier." But sections 152(b)(2)-(4) <u>still</u> facially exempt connecting carriers from section 214. The court does not address the basic issue of whether connecting carriers are subject to any sections of the Act other than sections 201 through 205.

Section 214 also does not require a certificate for the extension or acquisition of lines "acquired under section 221 or 222 of this title."[219] Section 222, governing "Competition Among Record Carriers," deals with mergers and consolidations of telegraph companies.

Section 221 regulates a number of diverse telephone issues. Subsection 221(a) provides immunity from antitrust and other conflicting federal laws for consolidation of telephone companies into a single company upon FCC approval. Subsection 221(a) is a direct descendant of the Willis-Graham Act of 1921, which authorized the ICC to grant exemptions from federal antitrust laws for telephone company mergers. The Willis-Graham Act encouraged mergers among early telephone companies that otherwise would have been forced to remain separate because of the antitrust laws. Subsection 221(a) preserves the FCC's power to exempt mergers and consolidations of companies in the modern markets for telephone services and equipment:

> (a) <u>Upon application of one or more telephone companies for authority to consolidate</u> their properties or a part thereof into a single company, or for authority for one or more such companies to acquire the whole or any part of the property of another telephone company or other telephone companies or the control thereof by the purchase of securities or by lease or in any other like manner, <u>when such consolidated company would be subject to this chapter</u>, the Commission shall give reasonable notice in writing to the governor of each of the States in which the physical property affected, or any part thereof, is situated, and to the State commission having jurisdiction over telephone companies, and to such other persons as it may deem advisable, and shall afford such parties a reasonable opportunity to submit comments on the proposal. A public hearing shall be held in all cases where a request therefor is made by a telephone company, an association of telephone companies, a State commission, or local governmental authority. If the Commission finds that the proposed consolidation, acquisition, or control will be of advantage to the persons to whom service is to be rendered and in the public interest, it shall certify to that effect; and thereupon <u>any Act or Acts of Congress making the proposed transaction unlawful shall not apply. Nothing in this</u>

> subsection shall be construed as in anywise limiting or restricting the powers of the several States to control and regulate telephone companies.[220]

The jurisdictional requirements for immunity under this subsection are straightforward. The consolidated company must be subject to the Act's common carrier provisions. Immunity thus would not be available for a merger of two entirely intrastate carriers with no interstate connections. The merger of two connecting carriers into a consolidated connecting carrier within the same state could be eligible for antitrust immunity under section 221(a) because the consolidated carrier would be subject to sections 201 through 205 of the Act. Note that the FCC does not automatically review each consolidation; telephone companies must apply for FCC review and approval.[221] The grant of immunity is a strong motivation for application. The subsection's preservation of state regulatory powers over telephone companies insures that applicable state regulations and state antitrust laws must be met by the merging companies.

Section 221(b) is a more overtly jurisdictional portion of the Act:

> (b)Subject to the provisions of section 301 of this title, nothing in this chapter shall be construed to apply, or to give the [FCC] jurisdiction, with respect to charges, classifications, practices, services, facilities, or regulations for or in connection with 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[222]

The term "telephone exchange service" is defined elsewhere in the Act to mean service within a discrete local exchange system - a relatively restricted area determined by the local telephone company which includes one or more central office switches.[223] Widespread traditional telephone practice has been to charge users a flat service charge for telephone service within this local area.

The chief issue raised by the language of section 221(b) is whether it should be read to absolutely ban any FCC jurisdiction over rates and operations for all telephone exchange service where state regulators assert their authority. This interpretation favors an expansive concept of state regulatory power relative to the FCC. The alternative viewpoint restricts the scope of the section to simply permit the states to regulate local service in areas that extend across state borders, such as New York and Washington, D.C. The first interpretation basically holds that the FCC has no jurisdiction over exchange service.

The Fourth Circuit Court of Appeals rejected this sweeping interpretation of section 221(b) in the 1976 North Carolina Utilities Commission v FCC decision (NC I).[224] That court examined the legislative history of the Act to conclude that under section 221(b), "a local carrier that serves a single multi-state exchange is assured whatever degree of freedom from federal regulation section [152(b)] provides for unistate carriers and intrastate telephone business generally."[225] Thus, section 221(b) was construed to mean that the geographical accident that a telephone exchange is located in two or more states does not enlarge the FCC's power over that exchange compared to others located in a single state. The FCC may regulate the interstate aspects of local exchanges to the same extent regardless of their locations. The First Circuit agreed with this interpretation in 1977 in Puerto Rico Telephone Company v. FCC, holding that "section 221(b) was intended not as a general grant of autonomy to state commissions, but as a special grant of freedom from federal interference for those few, essentially local, telephone exchange services which serve metropolitan areas embracing parts of several states."[226] The consequences of this interpretation in unusual fact situations have been litigated in several states.[227]

The remaining portions of section 221 do not define the FCC's jurisdiction. However, the extent of the FCC's assertions of jurisdiction directly affects how these portions are carried out. Section 221(c) permits the FCC to "classify the property of any . . .carrier used for wire telephone communication, and determine what property. . .shall be considered as used in interstate or foreign telephone toll service."[228] Such classification can take place only after hearing, with notice given to the carrier and the affected state regulators. Like "telephone exchange service," the term "telephone toll service" is defined in the Act.[229] Telephone toll service is service between different exchanges, for which there is a charge separate from the charge for exchange service. Section 221(d) states the reason for this classification. When the FCC values a carrier's property for purposes of regulating rates, depreciation, and return, section 221(d) gives the FCC discretion to value only that property classified as used for interstate or foreign telephone toll service. To the extent that the FCC legitimately classifies carrier equipment as used for interstate toll service, it extends the coverage of its rate-regulating powers and decreases the authority of the states. By limiting the property valued to that used for interstate toll service, sections 221(c) and (d) follow section 221(b)'s policy of preserving state regulatory jurisdiction over interstate local exchanges. In reality, the legal distinction between interstate and foreign toll service and exchange service may not have much effect on the classification and valuation of carrier property because so much property is used to provide both types of service.

The sections of the Act described above provide the statutory structure for FCC jurisdiction over the telephone industry. However, section 410 indicates the means by which the FCC formally interacts with state regulators.[230] Section 410(a) permits the FCC to refer regulatory matters other than formal hearings to a "joint board" composed of representatives of the affected states as well as the FCC. The joint board has the powers of an administrative law judge under the Administrative Procedure Act.[231] Section 410(b) permits less formal devices for cooperation with the states by authorizing conferences between the FCC and state regulators and by authorizing the FCC and state regulators to hold joint hearings.

In contrast to sections 410(a) and (b), section 410(c) requires the FCC to refer any proceeding regarding telephone separations to a permanent Federal-State Joint Board. "Separations" is the field of telephone regulation dealing with the allocation of common carrier property and expenses between interstate and intrastate operations.[232] The Federal-State Joint Board consists of three FCC commissioners and four state regulatory officials. It has the same general powers as the joint boards authorized in section 410(a). In addition, the Federal-State Board sits *en banc* with the FCC commissioners to hear oral argument scheduled in a proceeding in which it participates. The Federal-State Joint Board is an statutory acknowledgment of important state concerns in the separations area.

Section 5 - Case Law on Regulatory Jurisdiction

This section analyzes judicial decisions that consider the relative scopes of federal and state regulatory jurisdiction. In most cases, these decisions resolve jurisdictional questions raised by private parties who are contesting the validity of specific regulatory orders and policies. The courts almost always treat the jurisdictional issues as preliminary to any consideration on the merits. As such, the jurisdictional findings are a crucial first hurdle for the parties. Indeed, the jurisdictional findings may be dispositive in those cases where the court uses a highly deferential standard in reviewing the merits of the regulators' actions.

Many of the cases in this section base their holdings on statutory interpretations of governing federal statutes such as the Communications Act. However, variations on two underlying themes appear and reappear. First, the federal decisions show varying degrees of deference to the FCC's interpretation of the Communications Act. Such deference reinforces the FCC's jurisdictional ascendancy over the states. Second, the concept of the telephone network as a national, integrated system is a factor in many of the decisions. This conception of the national network carries with it a preference for centralized, and thus federal, jurisdiction.

A. History: The Early Telephone Industry - Conflicts Under the Commerce Clause

Before the Mann-Elkins Act and the Communications Act authorized federal telephone regulation by an independent agency, state/federal jurisdictional questions did not deal with conflicts between federal and state regulators. Instead, state or municipal ordinances were pitted against federal power under the Commerce Clause or federal statutes that directly regulated the telephone industry.

For example, the Supreme Court's 1898 decision in City of Richmond v. Southern Bell Telephone & Telegraph Company ("Southern Bell")[233] refused to apply to telephone companies an 1866 federal statute that regulated telegraph companies. The statute[234] gave telegraph companies the right to operate telegraph systems along the "military and post roads" of the United States if the companies agreed to follow a set of general operating conditions. In the Southern Bell case, the City of Richmond repealed an ordinance that granted a franchise to Southern Bell for the operation of telephone facilities within the city limits. Southern Bell argued that the federal statute applied to it. Thus Southern Bell claimed a federal right to operate in Richmond despite the City's revocation of its franchise.

The Supreme Court found that Southern Bell was not a telegraph company within the terms of the federal statute. The Court distinguished telegraph service, which transmits "only written communications," from telephone service, which electrically transmits "articulate speech."[235] The Court refused to consider any constitutional issues concerning the scope of state or municipal regulation of interstate commerce under the Commerce Clause.[236] Instead, the Court remanded Southern Bell to the lower federal courts for consideration of unresolved state law issues.[237] After further litigation, Southern Bell lost its franchise in Richmond.[238]

The Southern Bell decision left the federal government without general statutory power over the telephone industry until 1910, when the Mann-Elkins Act amended the Interstate Commerce Act to provide some federal telephone regulation.[239] Indeed, the Southern Bell opinion challenged Congress to legislate on the telephone industry "in plain words," instead of relying on judicial interpretation of a statute passed before the telephone was even invented.[240] The opinion may be seen as a plea for legislative attention to the new telephone industry.

Despite Southern Bell's limitation on federal statutory authority over telephone, federal courts continued to assert federal power in regulating telephone companies. The 1902 case of Muskogee National Telephone Company v. Hall ("Muskogee")[241] demonstrates an assertion of federal Commerce Clause power over another local franchise regulation. The action arose from the attempts of the Muskogee National Telephone Company ("Muskogee") to keep a rival company ("Hall") from entering Muskogee's area of operation in the U.S. Indian Territory (now Oklahoma). The Creek Indian Nation had granted Muskogee the exclusive franchise to provide telephone service within the Nation's tribal boundaries. On the strength of this franchise, Muskogee sought to enjoin Hall from operating in the town of Tulsa within the Creek Nation.

The Eighth Circuit upheld a denial of the injunction on constitutional and statutory grounds. The Muskogee opinion emphasized that the Creek Nation's grant of an exclusive franchise was void under the Commerce Clause:

> [T]elephone companies, like telegraph companies, are important agencies in the transaction of interstate commerce, and no state can grant to one telephone company the exclusive right to operate telephone lines within its borders; and which a state cannot do . . . the Creek Nation . . . cannot do.[242]

By the court's reasoning, the existence of a tribally-authorized telephone monopoly "would have a necessary tendency to prevent free communication between those who reside outside of, and those who reside within, the territory."[243] The court thus found that the _exclusive_ nature of the franchise obstructed interstate commerce.

Muskogee pointed out that Hall had no telephone connections outside the town of Tulsa within the Creek Nation. It thus argued that its franchise should not be held void for purposes of this intraterritorial dispute. The Eighth Circuit rejected the claim. It held that the exclusivity of the franchise was null from the time it was granted, regardless of the area covered by a rival company.

In addition, _Muskogee_ noted that a federal law enacted in 1901 authorized the Secretary of the Interior to grant rights of way for the construction and operation of telephone lines throughout the Indian Territory.[244] Regardless of the constitutional holding, this statute "necessarily prevailed over all local regulations on the subject, and operated to extinguish such exclusive rights to construct and maintain lines of telephone . . . within the territory as had here heretofore been granted."[245]

Muskogee strongly asserted the federal constitutional interest in protecting interstate telephone communications without regard to actual congressional legislation in the area. The opinion treated the 1901 federal statute as a secondary base for its decision. _Muskogee's_ Commerce Clause holding purportedly relied on the Supreme Court's 1878 decision in _Pensacola Telegraph Company v. Western Union Telegraph Company_ ("_Pensacola_").[246] However, _Muskogee's_ holding went far beyond _Pensacola's_ rationale. In _Pensacola_, the Supreme Court invalidated an exclusive telegraph franchise that Florida had granted to the Pensacola Telegraph Company. The Court noted that Florida had "attempted to regulate commercial intercourse between its citizens and those of other states."[247] However, the Pensacola Court found the franchise void because it conflicted with the 1866 federal statue at issue in the Southern Bell case, which applied only to telegraph companies.[248] In Pensacola, the Court refused to consider the validity of the franchise under the Commerce Clause absent the federal statute. Muskogee chose to go beyond both Southern Bell and Pensacola in asserting federal Commerce Clause power in the face of conflicting local reguation.

Although Southern Bell distinguished telephone service from the telegraph for purposes of interpreting a statute, three Supreme Court cases concerning telegraph service refined the federal law defining the general concept of interstate communications. In the 1920 case of Western Union Telegraph Company v. Speight,[249] Justice Holmes held that a telegram transmitted between two points in one state via another state is "interstate commerce as a matter of fact."[250] The decision reversed a North Carolina state court finding that such a message was intrastate because its originating and terminating points were within one state.[251]

Speight's broad definition of interstate telegraph extended the scope of federal telegraph regulation under the 1910 Mann-Elkins Act. The Supreme Court's 1896 decision in Western Union Telegraph Company v. James[252] considered the constitutionality of state regulation of interstate telegraph absent such federal regulation.

James upheld the validity of a Georgia statute that assessed a $100 penalty on any telegraph company operating in the state which did not transmit and deliver a message "with impartiality and good faith, and with due diligence."[253] The plaintiff in the case had sued Western Union for the tardy delivery of a message from Alabama to him in Georgia. Western Union challenged the application of the statute to

Georgia deliveries as an interference by Georgia with interstate commerce. The Supreme Court found on these facts that the statute had only an "incidental" effect on interstate commerce, even though it applied to telegraph companies offering interstate service. The Court reasoned that Georgia's statute promoted "the performance of a duty of the company that would exist in the absence of any such statute."[254] Indeed, for Georgia deliveries, the statute could be fulfilled "without in any manner affecting the conduct of the [telegraph] company with regard to the performance of its duties in other states."[255] As a result, the statute could regulate interstate messages delivered in Georgia until Congress legislated on the matter.

In accepting Georgia's regulation of incoming interstate messages, the James decision depended equally on the lack of any applicable federal regulation and on the essentially local application of the Georgia statute. The Court's description of the statute as having only an "incidental effect" on interstate commerce does not provide a clear test of constitutionality under the Commerce Clause. Instead, it seems to be shorthand for a finding that Georgia's regulation of message deliveries within the state did not substantially impede or discriminate against interstate telegraph communications in general.

After the adoption of the Mann-Elkins Act in 1910, the Supreme Court held that state statutes such as that in James were invalid as applied to interstate telegraph messages. The Court's 1920 decision in Western Union Telegraph Company v. Boegli held that the federal regulatory scheme of the Mann-Elkins Act "occupied the field" of regulating interstate telegraph sufficiently to preempt such state regulation.[256]

The Boegli holding would seem to apply to interstate telephone service as well, since the Mann-Elkins Act dealt with telephone and telegraph service equally. Of course, such state statutes are still valid as to wholly intrastate communications, as narrowly defined by Speight. Indeed, the statute at issue in James is still on the books in Georgia in a slightly revised form.

B. History: The Limited Jurisdiction of the ICC

The Mann-Elkins Act of 1910 extended the authority of the Interstate Commerce Commission to include interstate "telegraph, telephone, and cable companies (whether wire or wireless)."[257] Interstate rates were to be "just and reasonable," as were accounting classifications for telephone company assets.[258] However, the ICC engaged in relatively few formal proceedings regarding the telephone or telegraph industries.[259] In the 1917 Unrepeated Message Case,[260] the ICC held that it could not require interstate telephone and telegraph companies to file rate tariffs with it for approval. The ICC interpreted the Mann-Elkins Act to require such filing only for common carriers engaged in "the transportation of passengers or property."[261] Thus, ICC rate regulation was restricted to the hearing of complaints on specific rates brought by affected parties.

The rate dispute in the ICC's 1926 decision in Huntington Engineering Company v. Chesapeake & Potomac Telephone Company[262] involved a challenge to ICC jurisdiction that presaged common arguments under the Communications Act. Huntington Engineering Company ("Huntington") received telephone service from the Chesapeake & Potomac Telephone Company ("C & P"). C & P required Huntington to make a $40 cash deposit prior to receiving telephone service. Huntington complained to the ICC that the deposit was void as being unjust and unreasonable.

C & P acknowledged that it provided both interstate and intrastate telephone service to Huntington. It argued, however, that the ICC had no jurisdiction over the dispute because the deposit applied to the intrastate portion of the service provided to Huntington.

The ICC claimed jurisdiction. C & P's tariff, approved by the West Virginia state regulators, stated that cash deposits applied to "telephone service," not intrastate service only. Moreover, 11.8 percent of Huntington's phone bill for six months of 1924 consisted of interstate charges. Because the deposit apparently covered Huntington's interstate service, the ICC's jurisdiction applied.[263]

A striking aspect of the Huntington case was Huntington's willingness to retain counsel to contest the $40 deposit through to a final ICC decision. All in all, regulation on the basis of ad hoc complaints did not provide the uniform guidance expected from a federal agency:

> [R]eliance on "complaints" as the moving force in the regulatory process was obviously unsuited to effective telephone rate regulation. Individual monetary incentive was so largely absent in the field that no individual user of the service could fairly have been expected to bear the large costs necessarily incident to the prosecution of a telephone rate case.[264]

The ICC had a more definitive impact on the accounting and depreciation practices of the telephone industry.[265] In 1913, the ICC adopted a Uniform Classification of Accounts for Telephone Companies, which was followed by state regulators and still exists under FCC auspices as the Uniform System of Accounts. In addition, the Transportation Act of 1920[206] authorized the ICC to fix and prescribe depreciation charges for telephone companies. The ICC did not manage to prescribe such rates before the FCC superseded its telephone duties. In the 1936 decision of Northwestern Bell Telephone Company v. Nebraska State Railway Commission,[267] the Supreme Court upheld Nebraska's right to prescribe depreciation charges for telephone company property within Nebraska, in the absence of ICC-prescribed charges.

C. History and a Continuing Problem: Jurisdictional Aspects of "Separations" in Allocating Interstate and Intrastate Telephone Costs

The Supreme Court considered a fundamental jurisdictional issue in telephone regulation in the 1930 case of Smith v. Illinois Bell Telephone Company ("Smith").[268] The basic question involves the allocation of regulated telephone company costs between the federal and state regulatory jurisdictions. This allocation is known as the "separations" process. The goal of the separations process is to separate the telephone company's costs of providing interstate telephone service from its costs of providing intrastate service so that ratepayers in each jurisdiction bear a fair proportion of the total costs.[269] This process of cost allocation is entirely separate from the ratemaking process in the regulated telephone industry. Ratemaking takes place only after telephone company costs have been allocated between the state and federal regulatory jurisdictions. Rates for telephone services in each jurisdiction then are designed to permit the regulated companies to recover the costs allocated to that jurisdiction. The separations issue is crucial in examining the relative authority of state and federal regulators because of its basic economic consequences for the industry. Various separations methods have been devised that represent differing conceptual views of allocating costs among the jurisdictions.

For example, the "station-to-station" separations approach considers the costs incurred at each step of transmitting both intrastate and interstate phone calls.[270] Station-to-station separations allocates the interstate and intrastate costs of all jointly used equipment from the calling telephone (or "station") all the way through to the receiving station. The allocations are based on formulae agreed upon by state and federal regulators. These allocations do not reflect the actual costs incurred by interstate and intrastate uses for any particular piece of equipment. However, station-to-station separations explicitly recognizes the shared nature of the telephone network.

Another allocation technique known as the board-to-board method was widely used in the early days of the telephone industry. In board-to-board separations, all of the fixed costs of the equipment needed to make a local phone call were allocated to the state jurisdiction for the calculation of local rates.[271] Thus, all of the costs associated with terminal equipment, local loops, and local switches were allocated to local service. The costs of toll facilities, such as long distance links and switches, were allocated to state or federal jurisdiction depending on their use for intrastate or interstate toll calls.

Board-to-board and station-to-station separations are simply alternative views of how interstate and intrastate costs are assigned in terms of the components of the telephone network. Station-to-station separations assigns some costs associated with "local" equipment to the federal jurisdiction. Board-to-board costing assigns all costs of "local" equipment to the local (presumably state) jurisdiction. The methods reflect different costing philosophies.

From a state/federal jurisdictional viewpoint, a choice between these methods is crucial. Under the board-to-board approach, state regulators have jurisdiction over all costs associated with "local" equipment. But such equipment is often used for interstate communications as well as intrastate communications. In effect, board-to-board separations gives state regulators authority over costs of portions of the telephone network used for interstate purposes. On one hand, this seems to challenge federal regulatory authority under the Commerce Clause. On the other hand, since state regulators would be responsible for overseeing the recovery of some interstate costs, they could argue that board-to-board separations improperly burdens sovereign state regulation.

The Supreme Court addressed this jurisdictional question in Smith,[272] which pitted the Illinois Bell Telephone Company ("Illinois Bell") against the Illinois Commerce Commission ("the state") in a dispute over rates for telephone service within Chicago. Illinois Bell claimed that a set of rates specified by the state were so low as to be confiscatory under the Due Process clause of the Fourteenth Amendment.[273]

Illinois Bell had gained an injunction in a federal district court, staying the enforcement of the state's proposed rates. During the time that the injunction was effective, Illinois Bell charged rates based on costs allocated using the board-to-board method.

The state appealed to the Supreme Court to dissolve the injunction. Among other things, the state claimed that the board-to-board method was an improper way of allocating intrastate costs. Writing for the Court, Chief Justice Hughes seized on the jurisdictional implications:

> The separations of the intrastate and interstate property, revenues, and expenses of the company is important not simply as a theoretical application to two branches of the business. It is essential to the appropriate recognition of the competent government authority in each field of regulation . . . . [T]he interstate tolls are the rates applicable to interstate commerce, and neither these interstate rates nor the division of the revenue arising from interstate rates was a matter for the determination . . . of the [state].[274]

The Court did not rule that the board-to-board method was unconstitutional. It did accept the state's argument that allocation to the state of all costs associated with jointly used equipment was erroneous as a burden upon the state. The Court remanded the dispute to the district court for reconsideration of the separations procedure:

> 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 is allocated will bear an undue burden . . . .[275]

The Court thus seemed to suggest some type of station-to-station approach. On remand, the district court accepted a compromise between the board-to-board and station-to-station techniques.[276] This method assigned a portion of local fixed costs to interstate services. However, this assignment was offset by also assigning a portion of the revenues from intrastate local service to interstate service. Because these local revenues offset the allocated local costs, the total cost allocation under Lindheimer did not change from allocation under the board-to-board method. When the case reappeared before the Supreme Court as Lindheimer v. Illinois Bell Telephone Company,[277] the Court "approved" this separations method by not even discussing it. In Lindheimer, the Court accepted the modified rates put forth by the state and dissolved the injunction against their enforcement.

Although the Supreme Court tacitly approved the "Lindheimer" method of allocating intrastate revenues as well as costs to interstate services, state regulators generally opted for the station-to-station method in allocating costs. This trend is said to have indicated the state regulators' acceptance of Smith's jurisdictional holding that endorsed station-to-station separations. However, some states also allocated revenues to the federal jurisdiction as in Lindheimer.[278] The FCC finally adopted station-to-station separations in 1943.[279] The FCC and the states currently follow the station-to-station procedures specified in the Separations Manual, which describes the state/federal allocations mechanism in detail.[280]

The policy aspects of the various separations schemes help to explain the positions of the state regulators and Illinois Bell in Smith and Lindheimer. The preference of telephone companies in the early 1900s for board-to-board separations has been explained by examining the increment in cost of providing interstate toll service in addition to local service.[281] When board-to-board was first adopted, charges based on the incremental costs of interstate toll service were high compared to charges for local service. By placing all of the costs for terminal equipment, local loops, and local switches on intrastate service rates, the telephone companies avoided raising the interstate toll rates and thus promoted long distance calling. State regulators, such as those of

Illinois, may well have disliked board-to-board because of the "undue burden" of interstate costs allocated to intrastate service. The additional costs ultimately could result in relatively high intrastate rates, which might cause political pressues on the state regulators. On the other hand, the board-to-board method is simple to implement because it divides costs so neatly between "local" and "interstate" equipment.

The federal regulatory position on board-to-board separations at the time of Smith is more difficult to analyze. On one hand, the method's simplicity might be appealing to an overworked federal agency. As noted above, however, the ICC was involved in interstate rate regulation on only a sporadic basis. It did not have strong institutional stakes in the Smith controversy. Indeed, the Supreme Court's own defense of federal jurisdiction over interstate rates[282] stated the most cogent federal objection to board-to-board separations.

The station-to-station method is said to have gained acceptability in the eyes of telephone companies as the incremental costs of toll service decreased in relation to local service costs because of advances in transmission technology.[283] As long distance service became more economical, station-to-station separations permitted telephone companies to hold local intrastate rates down by allocating local costs to interstate services. Compared to board-to-board, fewer costs are allocated to state regulatory jurisdictions under station-to-station separations. However, station-to-station separations has one overriding practical difficulty: a rational and detailed separation of interstate and intrastate costs associated with shared equipment such as local loops and switching machines. In a real sense, the relative scope of the federal and state regulatory jurisdictions under station-to-station separations depends on the specific cost allocations agreed upon by the FCC and the states. Such agreement is essential to the success of a station-to-station separations regime. The necessity for such detailed allocation contrasts with the clean state/federal boundary established by the board-to-board method.

Finally, the Lindheimer method differs from both the board-to-board and station-to-station approaches. In the Lindheimer method, interstate rates reflect costs allocated to the federal jurisdiction plus some additional intrastate revenues. These additional intrastate revenues could keep the interstate rates lower than under a strict station-to-station approach in which no intrastate revenues are allocated to the federal jurisdiction.

After Lindheimer, state regulators protested against its separations method. The state regulators complained that although they approved intrastate rates based on all intrastate costs, the interstate jurisdiction received the benefits of these rates in the form of the allocated intrastate revenues.[284] In essence, the Lindheimer method extended effective FCC jurisdiction over some intrastate costs while its formal jurisdiction was restricted to a smaller set of interstate costs.[285] This disparity between effective and formal federal authority over costs was resolved when the FCC adopted the station-to-station approach.

Disputes over cost allocations between the state and federal jurisdictions did not end with the 1943 adoption of station-to-station separations. For example, in the late 1970s, New York regulators decided that some costs were being unfairly allocated to New York's jurisdiction rather than to the federal jurisdiction. The regulators acted unilaterally to change the separations procedures. These actions resulted in two judicial decisions (one in state court, one in federal court) that considered the jurisdictional implications of such unilateral actions.

In the 1980 case of New York Telephone Company v. Public Service Commission,[286] the Appellate Division of the New York Supreme Court held that the state's Public Service Commission (the "Commission") acted "unlawfully, arbitrarily and capriciously"[287] in ordering an allocation of telephone company costs to interstate toll service without FCC consent. The Commission had considered whether the state/federal allocation of costs was proper for two services, foreign exchange (FX) and common control switching arrangement (CCSA), offered by New York Telephone (NY Tel).[288] The Commission decided that New York's intrastate telephone customers were absorbing approximately $40 million per year in local switching costs that should have been paid by interstate FX and CCSA users. The Commission ordered NY Tel to file rates reflecting this disparity. NY Tel filed new rates with the Commission and not with the FCC. The new rates included a surcharge to interstate FX and CCSA customers of about $160 per month, while the surcharge for intrastate FX and CCSA customers remained at about $9 per month.

The New York court found that the Commission acted outside its authority in calling for the new rates. The court noted that the Separations Manual had "functioned satisfactorily until the Commission abruptly departed from its principles in this instance."[289] The court recognized that the Federal-State Joint Board device in Section 410(c) of the Communications Act[290] gave the Commission a means to develop a suitable allocation with FCC cooperation. Most importantly, the state court noted that a related 1980 federal court decision in New York Telephone Company v. FCC ("NY Tel")[291] found that the FCC had jurisdiction over this matter.

The NY Tel case considered another aspect of this dispute. After NY Tel filed the new interstate surcharges with the Commission, some interstate FX and CCSA customers filed a petition for relief with the FCC. NY Tel claimed that the FCC had no jurisdiction to grant relief. It argued that the new surcharges concerned only local service and rates that were considered intrastate under current separations practices, so that the Commission alone had jurisdiction.

The FCC issued a Memorandum Order and Opinion which asserted jurisdiction over local rates and service when used in connection with interstate FX and CCSA.[292] Pursuant to this jurisdiction, the FCC ordered that NY Tel's surcharges must be filed with it for approval under section 203 of the Communications Act.[293] The Commission appealed the FCC order to the U.S. Court of Appeals for the Second Circuit.

The Second Circuit upheld the FCC's claim of jurisdiction and the filing requirement it placed on NY Tel.[294] The court found that charges for the local portion of the FX and CCSA service affected interstate communication precisely because the NY Tel surcharge for interstate customers was "up to 1600 percent higher than the charge for . . . intrastate users."[295] In addition, the FCC's jurisdiction over interstate communication "does not end at the local switchboard, it continues to the transmission's ultimate destination."[296]

The court acknowledged that the FCC had held in a series of earlier decisions that the local portion of FX service was subject to state regulatory jurisdiction. However, the Second Circuit deferred to the FCC's present construction of its jurisdiction, holding that "[a]dequate explanation and reasoned analysis have been held sufficient to support departure by administrative agencies from their precedents."[297]

In addition, the court rejected NY Tel's argument that the FCC was causing a "regulatory vacuum" by preempting the state-approved rates without providing its own substitute tariff. The court held that no such vacuum existed; the FCC had simply ruled that NY Tel must file tariffs with the FCC if the tariffs discriminate against interstate FX and CCSA users.[298]

The NY Tel decision concluded that "this case is really an administrative jurisdictional dispute, with [NY Tel] and interstate FX and CCSA users to some extent caught in the middle."[299] This description seems accurate; the New York Commisssion apparently acted to force a change in separations procedures by discriminating against interstate customers. NY Tel attempted to protect the status quo by suing the Commission in state court and the FCC in federal courts. As a result, the FCC extended its jurisdiction over an area it had previously left to state regulation.

D. Jurisdictional Disputes Under the Communications Act: Jointly Used Facilities

Adoption of the Communications Act in 1934 modified the nature of state/federal jurisdictional disputes and telephone regulation. The FCC exerts its authority under the legal auspices of the Act. Indeed, the FCC's jurisdictional claims are based on its interpretation of the Act. Jurisdictional conflicts thus often turn on competing statutory interpretations.

The FCC's recent policy of introducing competition in some areas of the telephone industry has caused a number of jurisdictional challenges by state regulators as well as by the industry itself. The following cases present the controlling current judicial interpretations of the scope of FCC jurisdiction over facilities such as terminals that are used jointly for interstate and intrastate communications.

1. <u>The North Carolina Cases: Terminal Equipment</u>

In the two cases of <u>North Carolina Utilities Commission v. FCC</u> ("<u>NC I</u>" and "<u>NC II</u>"),[300] the U.S. Court of Appeals for the Fourth Circuit clarified the scope of the relative jurisdictions of the FCC and state regulators under the Communications Act. The cases arose from the FCC's introduction in the late 1960s of its policy permitting customers to connect their own terminal equipment to the telephone network.[301] Interstate common carriers filed tariffs with the FCC to permit the interconnection of customer-owned terminal equipment. Despite these tariffs, the North Carolina Utilities Commisssion and other state regulators gave public notice that <u>they</u> intended to prohibit such connection of customer-owned terminal equipment, except where the terminals were used exclusively for <u>interstate</u> communication. Independent manufacturers of terminal equipment petitioned the FCC for a declaratory ruling on the scope of its jurisdiction. The FCC held in its 1974 <u>Telerent</u> decision that its terminal equipment policies preempted those of the state regulators.[302] The state policies were held to have regulated interstate as well as intrastate communications and thus encroached on the FCC's interstate jurisdiction.

The Fourth Circuit reviewed Telerent in the 1976 case known as NC I. The state regulators' challenge to the FCC's jurisdiction relied on section 152(b)(1) of the Communications Act, which provided that

> [N]othing in this chapter shall be construed to apply or give the [FCC] jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications service by wire or radio of any carrier . . . .[303]

The state regulators argued that section 152(b)(1) cut off FCC jurisdiction over intrastate communications. A three-judge panel of the Fourth Circuit held 2 to 1 that the FCC properly asserted its authority under the Communications Act. The majority found that the legislative history of section 152(b) offered "no impressive guidance" in determining its scope.[304] Accordingly, the court deferred to the FCC's interpretation of the Act. In Telerent, the FCC had found that almost all terminal equipment is used for both interstate and intrastate communications. Therefore, state regulation of terminal equipment inevitably affects interstate communications. Thus, the court held that the FCC properly asserted its primacy, because of its general grant of jurisdiction over "interstate and foreign communications by wire or radio" under section 152(a) of the Act.[305] In addition, the Fourth Circuit noted that the FCC had repeatedly exercized jurisdiction over terminal equipment in the past. Moreover, the court focused on section 410 of the Act, which permits the FCC to refer problems of "joint Federal-State concern, to a Federal-State Joint Board," consisting of FCC commissioners and state regulators.[306] The court questioned why Congress would provide this procedural device for resolving federal and state conflicts if section 152(b) was intended to deny the FCC of jurisdiction over all "facilities that necessarily serve both interstate and intrastate communications."[307]

The Fourth Circuit did acknowledge limits on the FCC's jurisdiction over terminal equipment. It held that section 152(b) bars the FCC from jurisdiction over matters that "in their nature and effect are separable from and do not substantially affect the conduct or development of interstate communication."[308] The court mentioned intrastate ratemaking as an example of such an activity. The NC I decision thus protects the states' independent power to regulate intrastate telephone rates.[309]

Finally, the majority in NC I rejected the state regulators' claim that section 221(b) of the Act reserves exclusive jurisdiction over "telephone exchange service" to the states.[310] The court pointed out that the Act's legislative history restricted this section to assuring that the FCC does not usurp state or local regulatory authority over a local telephone company that serves an area on a state line, such as a city located in more than one state.[311]

In 1977, a different panel of the Fourth Circuit reconsidered many of the same issues in NC II.[312] In NC I, the Fourth Circuit had upheld the FCC's declaratory ruling in Telerent that FCC regulation of terminal equipment precludes conflicting state regulation if the equipment is used for interstate and intrastate communication. NC II considered the FCC's subsequent implementation of terminal equipment regulation. After its Telerent decision, the FCC issued orders detailing the standard technical requirements (known as "registration requirements") for connecting customer-owned terminal equipment to the telephone network.[313] The North Carolina Utilities Commission and other parties (the "states") appealed the FCC's orders to the Fourth Circuit on several grounds. As in NC I, the states claimed that sections 152(b)(1) and 221(b) of the Communications Act deny the FCC jurisdiction over terminal equipment used predominantly for intrastate communications.

The new three-judge panel in NC II acknowledged that NC I had rejected almost identical jurisdictional arguments one year earlier. However, the court cautiously decided to reconsider the earlier panel's holdings.[314] After stating that significant federal and state interests were at stake, the court noted that no other Court of Appeals had interpreted the disputed sections of the Act. The court further explained that the full Fourth Circuit could not review NC I *en banc* became most of the judges were disqualified. Thus, the second panel's review of the NC I decision was a substitute for *en banc* reconsideration by the entire Fourth Circuit.

The court in NC II affirmed by 2 to 1 NC I's holding that sections 221(b) and 152(b)(1) did not reserve regulation of terminal equipment to the states.[315] The court immediately adopted NC I's analysis of section 221(b).[316]

However, the court's analysis of section 152(b) extended beyond NC I's approach of deference to the FCC's statutory interpretations. The states claimed that section 152(b)(1) absolutely excludes the FCC from having any authority over intrastate equipment. The court found that this argument, even if found to be correct, begs the key question: whether terminal equipment, used jointly for interstate and intrastate purposes, is *intrastate* equipment under the statute. The court set out two reasons why such jointly used equipment must be considered *interstate* and thus under the FCC's section 152(a) jurisdiction.

First, the majority noted that in section 221(b), Congress explicitly reserves exclusive state (or local) regulatory jurisdiction over a limited class of interstate communication. Yet section 152(b)(1) does not contain a similar reservation of state jurisdiction for jointly used terminals or other facilities. The court concluded that absent such an explicit restriction, the Act must intend the FCC's jurisdiction to apply to terminals used for both interstate and intrastate services. Otherwise, "Congress created a regulatory scheme that depends on the calling habits of telephone subscribers to determine the jurisdictional competence of the FCC versus state [regulators]."[317]

Second, the majority engaged in inductive reasoning to hold that the FCC has primary authority over jointly used terminal equipment under section 152(b)(1). The court asserted that the FCC has power under the Act to remove a terminal device that actually interferes with interstate communications, even if a state regulator ordered the terminal to be installed.[318] Thus, the FCC can preempt contrary state regulation of terminal equipment "where the efficiency or safety of the national communications network is at stake."[319] Once this point is conceded, "there can be little argument" that the FCC may preempt conflicting state regulation of terminals in order to improve or expand interstate communications services. Indeed, the court noted that section 151 of the Act calls for "a rapid, efficient, nationwide . . . wire and radio communication service with adequate facilities at reasonable cost."[320] Given that the Act permits federal regulation of terminal equipment for the safety, efficiency, improvement and expansion of interstate telephone service, the court found no statutory basis for subjecting other FCC regulations of terminal equipment to the approval of state regulators.[321]

This analysis is powerful because of its underlying premises, but its reasoning is rather strained and incomplete. In this part of the opinion, the court hardly relies on the provisions of the Act or even on the Supremacy Clause in asserting the FCC's preemption power. Rather, the analysis stresses the need to maintain the "efficiency or safety of the national network." The assumption from the onset is that the national network's needs are always more important than those of the states. The court does not discuss its reasons for this assumption, although later in the discussion it cites the general language of section 151. Indeed, the analysis begins with probably the strongest intuitive argument for federal regulation of terminal equipment: to protect the "safety" of the national network. Because preemption is acceptable to guard the safety of the network, the court reasons that "other important interests of national communications policy" are similarly protected by preemption.

The opinion does not adequately describe why unspecified interests of national policy should receive the same jurisdictional protection as the safety of the national telephone system. The possibility that state policies may outweigh national interest is not considered. In light of the Supremacy Clause, the court's conclusion may or may not be correct, but it does not follow from the internal reasoning of the analysis.

Finally, the structure of this analysis is very broad. Its breadth stems from its acceptance of the primacy of the national network. Although the court specifically considers regulation of terminal equipment, similar reasoning could be used to justify federal preemption of intrastate ratemaking, a regulatory function that NC I reserved to the states.

However, the court reconsidered the limits of FCC jurisdiction under section 152(b). Agreeing with the NC I panel, the court stated that intrastate ratemaking was the exclusive province of state regulators.[322] The NC II court held that in the Communications Act, Congress intended to deny the FCC jurisdiction over setting "local" rates.[323] The court recognized this limitation of federal jurisdiction in the Act as a Congressional reaction to the Supreme Court's decision in the 1914 Shreveport Case.[324] In Shreveport, the Court held that the Interstate Commerce Commisssion had power to suspend intrastate rates for railroad freight in order to remedy a system of discriminatory rates that Texas regulators established to harm Louisiana shippers. Shreveport thus extended the reach of the Commerce Clause to control intrastate rates that create "unreasonable discriminations against interstate commerce."[325] According to the NC II panel, the Communications Act was intended to deny the FCC authority to include intrastate ratemaking as in Shreveport.

Indeed, the NC II court found no similarities between the FCC's registration program for terminal equipment and the ICC's actions upheld in Shreveport. The FCC was not regulating the intrastate uses or rates of terminal equipment in order to end state discrimination against interstate commerce. Instead, the FCC meant to regulate the use of terminal equipment "when that equipment is used directly to effectuate interstate communication."[326]

The Fourth Circuit did acknowledge that the FCC's actions might well affect intrastate rates.[327] If telephone customers are freely allowed to supply their own terminals, telephone companies will receive less revenue from providing their terminal equipment to customers. State regulators will be forced to adjust rates for telephone service in response to this revenue loss. The court stood fast in holding that for jurisdictional purposes, such adjustments by the states are not actually improper federal ratemaking under the Communications Act.[328]

Finally, the court held that the FCC's decision to preempt the states in the terminal equipment field was not "estopped" by the fact that historically, the FCC left terminal equipment regulation to the states. The Fourth Circuit noted that such a restriction would destroy the FCC's ability to use its accumulated expertise to deal with specific problems. Moreover, the court cited eight earlier FCC proceedings which regulated the use of specific types of terminal equipment without regard to applicable state regulations.[329] The court thus rejected the states' historical estoppel argument.

The NC I and NC II decisions emphasize different grounds for approving FCC preemption of jurisdiction over terminal equipment. Both opinions deal summarily with the states' claims under section 221(b) through elementary statutory construction and analysis of legislative intent. However, the courts differ in their handling of section 152(b), although their results agree.

The NC I court deferred to the FCC's findings in Telerent in order to hold federal preemption proper under section 152(b). The opinion justified its deference through the use of traditional legal devices. For example, NC I cited the FCC's previous proceedings involving terminal equipments as a basis for its jurisdiction. In addition, the NC I court looked to the Act and found support in the presence of section 410 which gives the FCC discretion to consult with the states on jurisdictional matters.

The NC II decision endorses NC I's holdings but goes beyond them by emphasizing the conflicting state and federal interests in regulating terminal equipment under section 152(b). The opinion acknowledges the jurisdictional dilemma caused by the joint use of terminals for interstate and intrastate communications. The majority resolved this dilemma through its "inductive" holding that federal interests predominate in the regulation of jointly used equipment. As noted above, the court's reasoning reveals an assumption that national interests in the interstate communications network generally outweigh those of the states.[330] Indeed, the opinion's emphasis on preserving the "national network" points to a strong basic preference for centralized regulation.

NC II further promotes the dominance of federal regulation by arguably narrowing the reservation of intrastate ratemaking powers noted in NC I. NC I held that "separable" regulatory matters which did not affect interstate communications were the exclusive jurisdiction of the states under section 152(b) of the Act. The NC I court used ratemaking as an example. Confronted with the states' subsequent argument that FCC terminal equipment regulation encroached on the states' ratemaking, the NC II panel narrowed the ratemaking reservation by discussing it in the context of the Shreveport Case. The NC I and II decisions provide a framework for later jurisdictional analysis that embraces federal preemption to serve national policy goals. The following three cases illustrate applications of the holdings of NC I and NC II.

2. FCC Jurisdiction Over Terminal Equipment: An Application

The Fourth Circuit's 1983 decision in Fort Mill Telephone Company v. FCC ("Fort Mill")[331] demonstrates the FCC's use of its regulatory primacy over terminal equipment to settle potentially troublesome jurisdictional disputes. Fort Mill involved a dispute over telephone service between the Fort Mill Telephone Company ("Fort Mill"), a small independent telephone company, and the Heritage Village Church and Missionary Fellowship, Inc. ("Heritage"), a religious and broadcasting company. Heritage owned a parcel of land straddling the border between North Carolina and South Carolina. The property contained an administrative center, television studios, guest and resident housing, and recreational facilities. The South Carolina Public Service Commission authorized Fort Mill to provide telephone service to the South Carolina part of the property. Similarly, North Carolina's regulators authorized Southern Bell Telephone and Telegraph Company ("Southern Bell") to serve an area including the North Carolina part of the property.

Heritage purchased a large PBX from an independent manufacturer for connection to the telephone network. Heritage chose to locate the PBX switch on the North Carolina part of its property for, among other things, "economic, technical, and religious reasons."[332] The PBX thus connected to the telephone network via Southern Bell.

However, the 300 individual telephones connected to the PBX switch were all located on the South Carolina part of Heritage's property. Fort Mill claimed that because the PBX telephones were used in South Carolina, Heritage must connect the PBX switch to it rather than Southern Bell. Fort Mill petitioned the South Carolina Public Service

Commission ("South Carolina") for relief. South Carolina agreed that the location of the use of telephone service controlled for jurisdictional purposes, and asserted jurisdiction over the Heritage PBX. South Carolina notified Southern Bell that it was providing unauthorized telephone service in South Carolina and ordered it to discontinue service to Heritage.

Heritage petitioned the FCC for emergency relief from the South Carolina order. The FCC granted relief, holding that Heritage had a federal right to connect its PBX to the telephone company that provided service at the point of connection, not the point of use. Fort Mill appealed to the Fourth Circuit.

The Fourth Circuit upheld the FCC's decision in Fort Mill. Heritage admittedly used the PBX for interstate communications. Under NC I and NC II, the FCC thus properly exerted its jurisdiction over terminal equipment in considering Heritage's petition. The court then adopted a deferential standard of review to approve the FCC's finding that the point of connection determines which telephone company serves the customer.

Without the clear grant of FCC jurisdiction over terminal equipment, this straightforward case would become more complicated. The dispute could well evolve into a jurisdictional struggle between South Carolina and the North Carolina regulators. Presumably, the North Carolina regulators would act against South Carolina in order to preserve both their territorial jurisdiction and Southern Bell's, revenues from the PBX. Absent a negotiated settlement, the dispute could be resolved in one of three ways. First, a state court of either North or South Carolina could hear the issue. This is most unlikely because of the parties' interests in gaining a neutral judicial forum. Second, the case could be fought through the federal courts. The Supreme Court might actually have original jurisdiction if the case was structured as a dispute between the two states.[333]

Finally, the FCC could assert jurisdiction over the dispute as involving "interstate communications" under either section 152(a)[334] or 201(a)[335] of the Act. Indeed, the connections between the 300 PBX telephones and the PBX switch could constitute interstate communications. However, the FCC would face a jurisdictional hurdle in section 221(b)[336] of the Act, which protects _state_ regulatory jurisdiction in interstate border areas. South Carolina's assertion of jurisdiction and the geographical facts of the case seem to place _Fort Mill_ within the terms of section 221(b). If the FCC had not preempted regulatory jurisdiction over terminal equipment in _NC I_, section 221(b)'s applicability would become an important initial question in any litigation on the dispute. However, the FCC's acknowledged jurisdiction over terminal equipment certainly streamlined the process of dispute resolution.

3. Application of Section 221(b) of the Communications Act

_NC I_ and _NC II_ limited the scope of section 221(b) of the Act to preclude federal regulation of local service in areas on state boundaries that had traditionally been under state regulation. In _Fort Mill_, the FCC avoided considering whether section 221(b) applied because of its jurisdiction over terminal equipment.

The Minnesota Supreme Court applied section 221(b) conventionally in a case where two states approved conflicting rates for the same local service. In the 1981 case of State By Spannaus v. Northwestern Bell Telephone Company ("Spannaus"),[337] the Attorney General of Minnesota sued Northwestern Bell for overcharging a group of its Minnesota customers. These customers received local telephone service from Northwestern Bell central offices located in North Dakota. On September 2, 1977, the North Dakota regulators approved a rate increase for local service provided by central offices in North Dakota. Northwestern Bell immediately began charging the new rates to its Minnesota customers connected to North Dakota central offices. However, Minnesota's regulators were not initially notified of the new rates, and did not approve the increases for almost nine months. In Spannaus, the state Attorney General claimed that the rate increases were illegal in Minnesota until approved by its regulators. The state asked that Northwestern Bell refund the overcharges to the affected customers.

The Minnesota Supreme Court granted the refunds by affirming a summary judgment against Northwestern Bell. The court held that the Minnesota regulators had jurisdiction over rates for local service charged to Minnesota residents, regardless of where their central offices were located. Otherwise, the affected customers would not receive the protections of Minnesota regulation guaranteed by Minnesota law. In addition, section 221(b) of the Communications Act applies in this case where local telephone service is provided through interstate facilities. Thus Minnesota, not the FCC, has authority over the rates in question. Finally, a longstanding Minnesota practice of immediately approving rates set by the North Dakota regulators does not constitute a yielding of regulatory jurisdiction by Minnesota to North Dakota.

Spannaus, unlike Fort Mill, essentially involved the interests of parties in only one state. The charges at issue in Spannaus were assessed exclusively against Minnesota residents. Only Northwestern Bell's practices in Minnesota were in question. The North Dakota regulators had no interest in the litigation; North Dakota claimed no jurisdiction over the rates charged to Minnesota residents served through North Dakota facilities.

On these facts, section 221(b) logically excludes federal jurisdiction. Spannaus reduces to a case where Northwestern Bell attempted to collect high local rates within a state without approval from its regulators. The interests of the state seem to outweigh any interests of the FCC in deciding the matter. The FCC may have a general interest in assuring that rates for interstate local service are not manipulated by the telephone company, but Minnesota's concerns in protecting its citizens and its regulatory jurisdiction appear to be more compelling. In contrast, the application of section 221(b) to the Fort Mill situation would exacerbate the dispute between North and South Carolina by precluding the FCC's intervention.

4. Jurisdictional Questions: Competition in Private-Line Telephone Service

The FCC's moves to introduce competition in the market for private-line telephone service[338] did not generate jurisdictional litigation comparable to that involved in NC I and NC II. MCI and other new competitors for these services generally attempted to enter the market for interstate service from the onset, so that all parties acknowledged the FCC's regulatory jurisdiction.

However, new entry into intrastate private-line markets raises many of the same jurisdictional issues concerning jointly used equipment as in the NC decisions. The 1977 case of People of California v. FCC ("California")[339] poses jurisdictional questions related to the regulation of intrastate telephone services with connections to interstate transmission facilities. The California case arose out of the FCC's introduction of competiton in the interstate private line market in the early 1970s. The Southern Pacific Communications Company ("Southern Pacific") entered the interstate market for FX and CCSA services in 1972. However, Southern Pacific applied to the California regulators ("California") for permission to provide intrastate service as well.

California authorized Southern Pacific to provide intrastate point-to-point private-line service, but prohibited it from providing intrastate FX or CCSA service. California restricted Southern Pacific's services in order to protect the revenues of the Bell system's Pacific Telephone & Telegraph Company ("Pactel"). Pactel's revenues from intrastate FX and CCSA subsidized low rates for its local service; competition from Southern Pacific might have eliminated the subsidy.[340]

Despite these restrictions, Southern Pacific asked Pactel to connect its private lines between Los Angeles and San Diego with Pactel's local switches in San Diego. This connection would permit Southern Pacific to provide intrastate FX service. Pactel reported the request to California. Southern Pacific countered by petitioning the FCC to assert jurisdiction over controversies relating to the interconnection of Bell system companies with competing carriers.

Southern Pacific thus sought to avoid California's restrictions on its intrastate FX service.

The FCC responded by asserting jurisdiction over all of Southern Pacific's intrastate FX services.[341] It noted that 82 percent of the calls on Southern Pacific's San Diego - Los Angeles private link originated out of state. Thus, Southern Pacific's intrastate facilities were "part of a dedicated interstate communications network."[342] By asserting jurisdiction, the FCC preempted California's authority over Southern Pacific's intrastate activites. The FCC did decline to assert jurisdiction over the local exchange portion of Southern Pacific's intrastate service.[343] California and Pactel appealed.

The FCC's claim was upheld in a 2 to 1 <u>per curiam</u> decision of the D.C. Circuit.[344] The majority rested the validity of FCC jurisdiction on <u>NC I</u>,[345] holding that the interstate and intrastate use of Southern Pacific's private link is analogous to the joint use of terminal equipment.

However, Judge Spotswood Robinson dissented, claiming that the FCC's decision did not sufficiently explain why all of Southern Pacific's intrastate links necessarily carried both interstate and intrastate calls.[346] Apparently, it was technically feasible to route <u>only</u> intrastate calls through one portion of Southern Pacific's facilities. This portion would then be subject to California jurisdiction. The dissent thus found that the FCC had dismissed the possibility of rewiring Southern Pacific's circuits to provide separate, wholly intrastate and wholly interstate facilities without adequate investigation: "The [FCC] thus far has proffered only an ambiguous finding unaccompanied by any evidentiary data whatsoever."[347] The dissent would subject the FCC to a high standard of review because it was exercising an "exceptional federal power to interfere" in intrastate matters.[348]

The California decision seems to be a natural outgrowth of NC I's holdings on the supremacy of FCC jurisdiction in regulating jointly used telephone facilities. However, the dissent raises two important points. First, it stresses that the FCC must be held accountable for its decisions. By criticizing what it sees as the FCC's lack of evidence and technical data in support of its findings, the dissent distinguishes between proper judicial deference to the FCC's expertise and blind judicial acceptance of FCC conclusions. Second, the dissent notes the possibility that the technical features of Southern Pacific's intrastate network may permit it to physically divide interstate and intrastate communications. This separation would eliminate the joint use jurisdictional problem addressed in NC I and assumed by the majority in California. Assuming that such a division could be done economically, the question arises whether the FCC or the states should require such a division for jurisdictional reasons.[349]

In a 1978 action related to the California case, the Oklahoma Supreme Court reversed a decision by its state regulators that claimed jurisdiction over Southern Pacific intrastate private services in Oklahoma.[350] Southern Pacific had claimed FCC jurisdiction from the time it entered Oklahoma's intrastate market. It filed tariffs for its intrastate FX service with the FCC only. It thus charged rates, authorized by the FCC, that were lower than those permitted by the Oklahoma regulators. Southwestern Bell Telephone Company, a competitor of Southern Pacific, complained to the state regulators. The Oklahoma court cited NC I and the California case in upholding the FCC's jurisdiction.

E. Computer Inquiry II: Jurisdictional Aspects

As discussed in Section 3, the FCC's Computer Inquiry II decisions furthered the introduction of competition in the markets for terminal equipment and enhanced services. Among other things, the decisions required the states to remove charges for terminal equipment from their intrastate tariffs after a transition period. The decisions thus moved to "unbundle" terminal equipment from regulated basic telephone service.

The U.S. Court of Appeals for the D.C. Circuit affirmed Computer Inquiry II in the 1982 decision of Computer and Communications Industry Association v. FCC.[351] In upholding Computer Inquiry II, the D.C. Circuit found that the unbundling requirement was a valid federal preemption of state regulatory power. The court held that the FCC's supremacy in regulating interstate communications permits it to remove terminal equipment charges from rates approved by state regulators. In so holding, the court's reasoning seems to permit the FCC to directly regulate intrastate rates, despite holdings to the contrary in NC I and NC II. The court also found that the FCC's so-called "deregulation" of terminal equipment was actually a valid substitution of affirmative federal regulation for state regulation.

As a preliminary matter, the D.C. Circuit followed the NC I and NC II decisions in holding that "state regulation which impedes a federal regulatory goal must yield to the federal scheme."[352] As in NC I and NC II, the appellant state regulators (the "states") argued that section 152(b) of the Act restricts FCC jurisdiction over terminal equipment.

The FCC countered by claiming that preemption was justified because state tariffing of terminal equipment would interfere with valid federal policies set out in Computer Inquiry II. The D.C. Circuit dealt with the dispute by examining the FCC's reasons for preemption as stated in Computer Inquiry II. The court limited its review to consider only whether the FCC's reasoning was arbitrary, capricious, or an abuse of discretion.[353]

The D.C. Circuit concluded that preemption of the state tariff regulations was justified. The court accepted the FCC's reasoning on the issue.[354] In deciding Computer Inquiry II, the FCC found that competition in the terminal equipment market would promote the efficiency and utilization of the interstate communications network. The FCC further noted that these benefits of competition are lost when terminal equipment charges are included in telephone company tariffs because this "bundling" of charges lowers customers' freedom of choice in the terminal market. To maximize freedom of choice, charges for terminal equipment must be separated from charges for regulated telephone service. The FCC noted that customers may use the same terminals for interstate and intrastate communications, and that most customers do purchase intrastate and interstate telephone service. Because of this pervasive sharing of terminals between interstate and intrastate service, the FCC held that any bundling of terminal charges into tariffs for telephone service would harm interstate communications and the consumer. Following NC I and NC II, the court found that "[g]iven the [FCC's] detailed and logical findings... we cannot say the... conclusion is irrational."[355]

However, the states attempted to distinguish Computer Inquiry II from the regulations approved in NC I and NC II. The states claimed broadly that the "unbundling" requirement attempts to preempt the states' ratemaking jurisdiction, which the Act protects in section 152(b). As discussed above, NC I cited intrastate ratemaking as an example of state action that "does not interfere with national regulation" and therefore is not subject to FCC jurisdiction under the Act.[356] By forcing the states to remove charges for all terminal equipment from their tariffs, the FCC arguably encroached on the states' protected ratemaking authority.

Moreover, the states capitalized on NC II's holding that Congress meant to limit FCC authority over intrastate rates in response to Shreveport.[357] The states identified section 152(b) as the section through which Congress meant to limit such authority. Interestingly, the court in NC II never made such an identification. On the contrary, that court noted that in Shreveport, the jurisdictional statute interpreted so broadly by the Supreme Court contained a proviso similar to section 152(b)(1).[358]

The D.C. Circuit rejected the states' ratemaking arguments for three reasons. Two of these reasons follow similar holdings in NC II, while the third is considerably broader. First, the Computer Inquiry II decision is unlike Shreveport in that the FCC is not concerned with the use of intrastate rates to discriminate against interstate business as Shreveport was. Second, the state tariffs preempted by the FCC do affect interstate communications. The source of the conflict, as in NC I and NC II, is the fact that terminal equipment is shared between intrastate and interstate communications. As in NC I and NC II, state regulation impedes a valid federal policy. Finally, the court looked at the language of section 152(b). It found that "the Act itself does not distinguish between authority over rates and authority over other aspects of communications.... Therefore, conflicting federal and state regulations... are no more acceptable under the Act when equipment rates are involved, as here, than when interconnection policies are involved, as in [NC II]."[359]

This interpretation of section 152(b) seems to overwhelm the court's own earlier careful distinction between Computer Inquiry II and Shreveport. Under the court's reading of section 152(b), so long as the FCC can prove a conflict between a valid federal policy and state regulation, federal regulation of intrastate rates is acceptable under the Communications Act. For example, the use of an intrastate rate to discriminate against interstate communications would conflict with the FCC's antidiscrimination mandate under section 202 of the Act.[360] As in the Shreveport Case, the FCC apparently could respond by setting intrastate rates, according to the court's interpretation of section 152(b).

The D.C. Circuit's broad reading of section 152(b) apparently conflicts with the intrastate ratemaking exception recognized by the Fourth Circuit in NC I and NC II. This reading certainly disavows the states' contentions that the FCC's unbundling requirements encroached on an area of exclusive state jurisdiction. However, the necessity of the holding in light of the court's two narrower reasons is questionable given the type of regulations involved in this case. The unbundling requirement of Computer Inquiry II affects state ratemaking more directly than did the regulations of NC II which permitted the use of customer-owned terminals. Because of unbundling, state regulators necessarily had to approve recalculated ratebases, revenue requirements, and rates for other telephone services. Still, Computer Inquiry II's regulations are fundamentally different from those permitted in Shreveport. That case held that the ICC had authority to specify intrastate rates in order to protect interstate commerce. The unbundling requirements do not purport to set any rates. At most, they cause redistribution of intrastate rates by excluding terminal equipment from rate calculations. The court's allusion to the possibility of federal jurisdiction over intrastate rates seems unnecessary for regulations so unlike those in Shreveport, and conflicts with the pro-state jurisdictional interpretations of Section 152 (b) in NC I and NC II.

The final major jurisdictional question[361] regarding Computer Inquiry II was based on the states' argument that the FCC's jurisdictional claim was improper because it did not replace state tariffs with "affirmative regulation that preempts the field."[362] The states argued that the FCC's unbundling requirement was a form of deregulation. Thus, the FCC attempted to remove functioning state regulations without replacing them with its own regulations. Therefore, the FCC's "preemption" was unlawful because it left "a vacuum of deregulation."[363]

The D.C. Circuit refused to address the philosophical question of whether "deregulation" is "regulation".[364] Instead, it held that in Computer Inquiry II, the FCC established a new form of terminal equipment regulation under the authority of a specific jurisdictional section of the Act. Under section 201 of the Act, the FCC regulates all charges and practices of common carriers.[365] Under sections 152(a) and 153(a), the FCC has so-called "ancillary jurisdiction" over "all interstate or foreign communications by wire or radio,"[366] including all "instrumentalities, facilities, [and] apparatus."[367] The D.C. Circuit held that the FCC's decision to unbundle terminal equipment was not deregulation but simply a shift from "common carrier" regulation of terminal equipment under section 201 to "a different, affirmative regulatory scheme through its ancillary jurisdiction."[368] The new scheme basically consists of the FCC policies that establish and support a free market in terminal equipment.

Moreover, the court found that Computer Inquiry II lays out "a comprehensive federal regulatory scheme . . . . 'Federal regulation need not be heavy-handed in order to preempt state regulation.'"[369]

Indeed, the D.C. Circuit's basic analysis of FCC jurisdiction is compelling, even if its distinctions between "ancillary" and "common carrier" jurisdiction seem formalistic. In opening up the terminal equipment market to competition, the FCC may be said to have stated that this market should not be subject to regulation as a natural monopoly. Rather, "efficient utilization and full exploitation of the interstate communications network"[370] is advanced by a competitive terminal equipment market. Thus, the FCC's action cannot be justified as "common carrier" regulation, since the basic premise is that terminal equipment is not a natural monopoly good like traditional common carrier service. Rather, the creation and maintenance of this competitive market must be justified under the national policy goals stated in sections 151 and 152 of the Act. The issue of whether an "affirmative" program of federal regulation must preempt state regulation is spurious in Computer Inquiry II, where the FCC used its regulatory powers to establish a competitive market in terminal equipment.

F. The MFJ: Antitrust Effects on State Regulatory Jurisdiction

Entry of the MFJ did not involve a jurisdictional struggle between the FCC and the states. Instead, the jurisdictional conflict arose over the MFJ's validity as a federal court decree in preempting state regulatory power, based on the supremacy of federal antitrust laws such as the Sherman Act. For example, the MFJ required AT&T to transfer some assets to its divested operating companies. Usually, such transfers must be approved by state regulators. Also, the MFJ prohibits interLATA telephone service by the divested companies, even though many of the divested companies were authorized to provide the equivalent of intrastate interLATA service by their state regulators.

The MFJ also displays differences in federal antitrust and regulatory approaches to controlling the telephone industry. Since 1934, the FCC had been active in regulating AT&T's rates, costs, and services under the terms of the Communications Act. Yet this continuing program of regulation did not preclude the Justice Department from separately claiming that AT&T had violated the antitrust laws. Indeed, the FCC did not protest the adoption of the MFJ as an encroachment by the Justice Department on the authority of the FCC. As discussed below, the FCC has never considered that telephone regulation under the Communications Act forecloses federal antitrust action. The assumption is that the FCC and the Justice Department's Antitrust Division oversee essentially different aspects of the telephone industry. Even so, the FCC retains the power to exempt mergers of telephone companies from the federal antitrust laws under section 221(a) of the Act.[371]

The U.S. District Court for the District of Columbia considered the terms of the MFJ in its 1982 decision in United States v. AT&T.[372] In approving the MFJ, the District Court held that the decree validly advanced federal antitrust law and preempted the authority of the state regulators.

The District Court accepted the MFJ as an implementation of the "broad sweep of the Sherman Act," which extends "beyond activities actually in interstate commerce to reach other activities that, while wholly local in nature, nevertheless substantially affect interstate commerce."[373] A valid exercize of federal power under the Sherman Act thereby preempts state law under the Supremacy Clause of the Constitution.[374] In its opinion on the MFJ's validity, the court considered and disposed of arguments by intervening state regulators (the "states") dealing with jurisdictional limitations on the scope of federal antitrust laws such as the Sherman Act.

The states' principal claim was that the MFJ is barred by the Supreme Court's 1943 holding in Parker v. Brown,[375] which exempts a limited area of state action from federal antitrust law. In Parker, the Supreme Court refused to find that the Sherman Act applied to a state regulatory program that limited competition among raisin growers by restricting production and setting prices. The Parker Court examined the legislative history of the Sherman Act and found no indication that the Sherman Act preempted such state action. As the District Court stated, "[a]t the root of the rule is the principle that federalism permits the States to impose a regime of economic regulation which is different from and inconsistent with the free competition principle mandated by the federal antitrust laws."[376]

Even acknowledging this role for the Parker exemption, the District Court found three reasons why Parker does not apply to the MFJ. First, the court questioned whether the exemption should apply to the telecommunications industry at all. The Parker exemption recognized a degree of autonomy in state economic regulation. The court emphasized that the U.S. telecommunications system is "technologically and economically, a national network with interdependent components,"[377] under significant federal regulation. The court thus expressed doubt as to whether Parker should exempt state regulation when the regulated industry is "national par excellence."[378] In doing so, the court seems to point out the limitations of the Parker exemption in promoting a federalist system when the object of regulation is of considerable interest to the national government.

Second, the District Court found that the Parker exemption does not apply because the states do not "actively supervise" much of the conduct to be controlled by the MFJ under the Sherman Act, as required by the Supreme Court's 1980 decision in California Retail Liquor Dealers Association v. Midcal Aluminum, Inc.[379] The requirement of "active supervision" by the states attempts to insure that the antitrust laws' goal of a system of free competition has been fully replaced by an adequate system of state control. However, in the telephone industry, the states have no jurisdiction over interstate telephone service, a major portion of the industry. Moreover, most state regulators ordinarily "control" intrastate rates for service and equipment only in the sense that telephone companies must file tariffs with them for approval. These limited or nonexistent controls do not qualify as "active supervision" by the states.[380] Indeed, the activities that the states do not actively supervise, such as interstate telephone service and telephone equipment marketing, are precisely those that were the targets of the antitrust suit. The District Court noted that the states <u>do</u> "actively supervise" <u>some</u> telephone company activities, such as the transfer of assets. Since these activities were not the subject of the antitrust action, the court refused to apply the exemption to the entire regulated telephone industry on that basis:

> Such a holding would place the [anti-competitive] conduct in a no-man's land -- not regulated by the states sufficiently to meet the <u>Parker-Midcal</u> test, yet immunized from effective federal antitrust jurisdiction because the antitrust remedy is barred by state regulations unrelated to this conduct.[381]

Finally, the District Court considered the practical effects of applying the <u>Parker</u> exemption when the states actively supervise only part of the regulated industry. In general,

> No effective, unconditional antitrust judgment could be entered and enforced with respect to any subject matter area in which the states had established a system of regulation. The federal antitrust court would have to await the outcome, the benevolent agreement, of the regulatory authorities before it could implement its decree. Should one or more states or their regulatory bodies object, the decree could not be enforced . . . .[382]

The court concluded that "[d]eference to state law in this type of situation would leave the Sherman Act powerless to eliminate anticompetitive activity,"[383] and refused to apply the <u>Parker</u> exemption.

In addition, the District Court rejected an argument that the MFJ unconstitutionally invades powers reserved to the states under the Tenth Amendment to the Constitution.[384] The states based their argument on the 1976 decision in <u>National League of Cities v. Usery</u>.[385] In that case, the Supreme Court held that the Tenth Amendment barred Congress from prescribing maximum hour and minimum wage standards for state and municipal employees. The Court ruled that because such controls would "directly displace the States' freedom to structure integral operations in areas of traditional governmental functions, they are not within the authority granted Congress by [the Commerce Clause]."[386] National League of Cities thus recognized an area of some state governmental immunity from congressional regulation under the Commerce Clause. This immunity is based on respect for state sovereignty. The states attempted to apply the immunity recognized in National League of Cities to state regulation of telephone service, thus removing the MFJ's legal effect from the states.

The District Court distinguished the limited range of state governmental activities protected by National Leagues of Cities from regulation of the telephone industry. The court noted that National League of Cities limited the Tenth Amendment immunity to actions of Congress that attempted to regulate "States as States."[387] Indeed, Supreme Court decisions that followed National League of Cities distinguished federal regulation of states as states from federal regulation of "private persons and businesses 'necessarily subject to the dual sovereignty of the government of the Nation and of the State in which they reside.'"[388] No Tenth Amendment immunity applies to the second type of federal regulation, since the regulation does not directly encroach on state sovereignty.

The District Court thus reasoned that the MFJ is indeed a form of federal regulation directed at the private telephone industry. As an implementation of federal Commerce Clause power, it regulates an industry which is manifestly subject to that power. Although the MFJ conflicts with some state regulation of the telephone industry, this conflict is not a federal regulation of state activities basic to state sovereignty, so the National League of Cities immunity does not apply.

Finally, the District Court dealt summarily with a claim by the states that the Communications Act of 1934 establishes a regulatory scheme which immunizes the field of telecommunications from the antitrust laws. The states' argument had alternative branches. First, the Communications Act was said to prohibit federal preemption of the state telephone regulation permitted in the Act. Second, the scheme of state and federal regulation established by the Act was said to be so pervasive that federal antitrust laws do not apply.

In rejecting the first branch of the argument, the court simply stated that it found no indication of Congressional intent for the Act to prevent federal antitrust preemption of state regulation. Moreover, the MFJ affects interstate markets which are not even within the scope of the state regulation permitted by the Act.

Regarding the second branch of the states' Communications Act argument, the court held that "regulation under the Communications Act is neither sufficiently explicit or sufficiently pervasive to allow it to stand in the way of the antitrust laws."[389] The court referred to its earlier procedural opinion in this litigation which considered the same argument.[390] There, the court found that telephone regulation was not sufficiently pervasive because a) the Communications Act did not regulate AT&T subsidiaries such as Bell Laboratories and Western Electric that were defendants in the antitrust complaint; b) the Act's basic tariff provisions actually provide very weak regulation because of the inability of the FCC to cope with the volume of tariffs filed; and c) the FCC itself has never considered telephone regulation to preempt antitrust actions.[391] Thus, the District Court found that the MFJ was a proper preemption of state regulation under both the Sherman Act and the Communications Act.

By holding that federal and state telephone regulation is not pervasive enough to foreclose a federal antitrust remedy, the District Court may be viewed as accepting two points concerning the relationship between antitrust enforcement and agency regulation.

The first point is that FCC and state regulation under the Act do not address the federal antitrust goals pursued in the Justice Department's lawsuit. The District Court's decision supports this point by noting that Bell Laboratories and Western Electric are not regulated under the Act, and that the FCC accepts a role for separate antitrust actions in the telephone industry. The decision thus sets forth the notion that antitrust and traditional regulation may coexist in the telephone industry because they pursue different policy goals.

Second, the finding of a lack of pervasive regulation may imply that an antitrust remedy and the existing state/federal regulatory scheme will not seriously interfere with each other. Indeed, the holding that the FCC's regulatory tools were weak seems to indicate that even if the FCC was attempting to pursue antitrust goals, the weakness of its efforts permitted separate federal antitrust activities. In any event, the assumption seems to be that an antitrust remedy such as the MFJ will not conflict with or hinder the regulatory goals of the FCC and the states under the Communications Act.

However, such conflicts may arise, particularly because the MFJ's divestiture remedy is such a radical restructuring of the industry. For example, the separation of AT&T and the divested companies conceivably could degrade telephone service quality enough that the FCC would take regulatory actions to maintain a "rapid, efficient, nation-wide" communications system as mandated by the Communications Act. Yet some possible FCC actions, such as the approval of telephone company mergers under section 221(a) of the Act, could directly conflict with the antitrust policies embodied in the MFJ.

In challenging the MFJ, the states explored a wide range of arguments for denying its preemptive power. The Parker v. Brown argument rests on the concept of antitrust immunity through pervasive state regulation and control of the industry. The Communications Act argument complements the Parker approach by claiming that a pervasive scheme of federal regulation under the Act immunizes the industry. Finally, the National League of Cities approach concentrates on constitutional protection of state sovereignty. This approach most clearly lays out the subject of the jurisdictional contest between the District Court and the states over the MFJ: the allocation of sovereign power between the federal government and the states. Note, however, that the states could not make an argument complementary to National League of Cities based on limitations of national sovereignty. Instead, the states admitted that the broad general powers of the Commerce Clause and the Sherman Act do permit the regulation of local aspects of commerce.[392]

Indeed, the common thread linking the District Court's rejections of the states' arguments is its fundamental realization that the telephone industry is an integrated, national concern in which the federal government has national interests beyond the jurisdiction of the states. Use of this concept is particularly important in the most involved aspect of the court's jurisdictional holdings, the rejection of the *Parker* exemption. For example, the court held that the regulators do not "actively supervise" those aspects of the telephone industry of direct concern to the MFJ. As importantly, the court condemns the inevitable interference with national policies if the states had to approve the MFJ under the *Parker* exemption. The court varies this theme in discarding the Communications Act and *National League of Cities* arguments. However, the clear precedents interpreting these claims simplified the court's findings. Indeed, the court had addressed many of the states' arguments earlier in upholding its jurisdiction to hear the antitrust case on the merits.[393]

Section 6 - Conclusion

The jurisdictional conflicts discussed in this paper illustrate the inherent difficulties of imposing a coherent program of regulation on a national industry when regulatory powers and duties are shared between state and federal governments. The difficulties in part stem from the need to square the jurisdictional provisions of the Communications Act of 1934 with regulatory policies that evolve in response to technological and market changes in the telephone industry. The major judicial decisions of the 1970s and early 1980s, such as NC I, NC II, the Computer Inquiry II appeal, and the approval of the MFJ, all provided new jurisdictional interpretations under the Act. The fact that jurisdictional questions consistently reached the courts on appeals of FCC decisions demonstrates the jurisdictional "play" permitted by the provisions of the Act when applied to new regulatory policies.

The jurisdictional decisions of Section 5 are specific reflections of the historical trend outlined in Section 3: increased federal intervention in telephone regulation in order to establish and protect competitive markets in some portions of the industry. Indeed, the judicial decisions discussed in this paper contain three strands of thought that support federal regulatory dominance over the states.

A. The Unified Telephone Network

First, the decisions acknowledge the essentially unified and interdependent nature of the telephone network. Recognition of this unity appears at two levels. One level recognizes that much telephone equipment is jointly used for both interstate and intrastate calls. For example, Smith v. Illinois Bell Telephone Company[390] addressed such joint use in considering the separations question. NC I[395] dealt extensively with this level in the terminal equipment setting. People of California v. FCC[396] applied the joint use concept to intrastate private-line services. In all of these cases, the courts upheld federal regulatory authority over that of the states. Of course, this follows from the constitutional imperatives of the Commerce and Supremacy Clauses. But practically as well, the most straightforward way of assuring a consistent, fair, and easily reviewable system of regulation over such shared equipment apparently is thought to be through FCC control.

In considering the unified nature of telephone service, the decisions also stress that the telephone network is national and thus affects national interests. This level stems from the universal availability of domestic telephone service and the interconnected facilities of the U.S. network. For example, the court in People of California v. FCC found that Southern Pacific's San Diego - Los Angeles private line was an integral link in a dedicated interstate network. And in NC II,[397] the Fourth Circuit relied on the concept of the safety and efficiency of the national network to uphold FCC preemption of terminal equipment regulation. This intense awareness of national interests certainly promotes the expansion of FCC jurisdiction over the telephone industry.

Moveover, the District Court which approved the MFJ in United States v. AT&T[398] justified the application of the federal antitrust laws over state and federal telephone regulation by referring to the national character of the telephone network in general and the Bell system in particular. The court found that this national network was a proper subject of the nationwide interests in antitrust enforcement despite the FCC's existing national regulation. These interests overrode the state action and sovereignty exemptions claimed by the state regulators. The apparent irony of the situation must be noted. In its decision, the District Court acknowledged the essential unity of AT&T's national network. Yet the court used this finding to divide control and ownership of the unified network among eight independent business organizations. One can only speculate that although the court considered the unity of the network to be sufficiently important to preempt state regulation, such unity did not outweigh the antitrust policies served by divestiture under the MFJ.

B. Legal Supremacy of Federal Jurisdiction

The constitutional and statutory supremacy of federal regulation is the fundamental legal basis for determining the scope of state and federal jurisdictions. Indeed, Muskogee National Telephone Company v. Hall[399] stressed the supremacy of federal law despite the fact that the franchise dispute at issue was wholly intraterritorial and did not directly impact interstate commerce. Western Union Telegraph Company v. Speight[400] extended the scope of federal jurisdiction over telegraph communications by finding that interstate messages include all those that are "interstate in fact" even though they originate and terminate in a single state. These early Commerce Clause decisions set the tone for later jurisdictional holdings.

Because the Communications Act is now the overarching framework for telephone regulation, the courts consistently analyze competing federal and state regulatory interests with the "burden of proof" on the states to overcome a presumption of federal dominance under the Act. This presumption often takes the form of deference to the FCC's findings; it can also occur in a court's independent construction of the Act. For example, in NC I, the Fourth Circuit's deference to the FCC's reading of the Communications Act was the fundamental ground for upholding federal preemption of terminal equipment regulation. In New York Telephone Company v. FCC,[401] the Second Circuit deferred to the FCC's current jurisdictional reading of the Act even though that reading differed from a prior line of consistent FCC holdings. Dissents, such as that of Judge Robinson in People of California v. FCC, criticize such deference when the FCC's decisions are poorly reasoned or documented.

However, direct judicial interpretation of the statute has also expanded the scope of federal jurisdiction. The D.C. Circuit did so in its review of Computer Inquiry II.[402] In holding that the FCC may regulate intrastate rates whenever conflicting federal and state policies are involved, the court seems to permit wider federal rate regulation than that contemplated under the deferential approach of NC I or NC II. The holding could serve as a ground for applying the Shreveport doctrine to intrastate telephone rates.

C. Limited State Regulatory Authority

The final strand running through the decisions on regulatory jurisdiction is the assumption of limited state regulatory jurisdiction over the telephone industry. The assumption is legally mandated by the Constitution and the Communications Act. However, it is reinforced by the perception of the telephone industry as national with overriding national concerns. As a result, state regulatory authority occupies a precarious position whenever a conflict with federal regulation arises. One paradox of Smith v. Illinois Bell Telephone Company is that the Illinois regulators defeated Illinois Bell's constitutional attack on their rates as confiscatory by sacrificing to the federal jurisdiction some of their power over costs under the board-to-board separations method. The subsequent Lindheimer separations method extended actual federal jurisdiction over telephone costs farther than its nominal limits.[403] In a more recent action, the New York regulators rather boldly extended their jurisdiction over separations for interstate FX and CCSA service in the New York Telephone Company cases.[404] Both New York and federal courts condemned this action. Indeed, the Second Circuit explicitly upheld the FCC's preemption of New York's extended jurisdiction. Thus, New York's attempt at regulatory aggrandizement resulted in the FCC's takover of the precise area at issue.

Some areas of regulation are reserved to the states. The Supreme Court's holding in Western Union Telegraph Company v. James[405] seems to provide constitutional protection for "localized" state regulation of interstate communications in the absence of applicable federal law. This protection may become increasingly important as new types of telecommunications services enter into widespread use, since such services conceivably could fall outside the scope of existing federal regulatory statutes.

In addition, judicial decisions that interpret the Communications Act may also protect specific areas of state regulation. The holdings of NC I and NC II which preserve state regulation over border areas under section 221(b) of the Communications Act provide such protection.

State by Spannaus v. Northwestern Bell Telephone Company[406] displays an application of this 221(b) reservation.

D. An Example: What is the Proper Scope of State and Federal Regulatory Jurisdictions?

Throughout the 1970s and early 1980s, bills have been unsuccessfully introduced in Congress to reform telecommunications regulation, often by amending the Communications Act. Before the MFJ, several bills would have modified the present state/federal jurisdictional scheme by granting the FCC exclusive jurisdiction over intrastate toll service.[407] State regulation would have been restricted to local telephone service.

Proponents of extending the FCC's jurisdiction over intrastate toll rates and services mount an impressive array of functional arguments.[408] The arguments are of three general types. First, the state/federal jurisdictional boundaries should be drawn along inherent, logical distinctions in types of telephone service. The technical and economic differences between toll and local service are more pronounced than the arbitrary intrastate/interstate boundaries now used. Thus the federal jurisdiction should include toll service and the state should govern only local service. Second, the toll/local regulatory distinction is arguably more equitable to telephone service customers. Charges for interstate toll calls often differ from intrastate toll charges for calls of the same distance, duration, and time of day, and such intrastate charges vary from state to state. Redefinition of jurisdictional boundaries to conform to the toll/local distinction would eliminate this disparity. Finally, state regulators who oppose the FCC's policy favoring the introduction of competition in interstate toll service could hinder it through their regulation of intrastate toll service.

Poised against these arguments are the interest group and institutional concerns of the states and state regulators. Each state's regulated firms will support the state's regulators to the extent that the regulators facilitate the firms' business operations. Indeed, <u>any</u> interest group in a state that has effective input to the state's regulators might oppose a federal preemption of regulatory power. Organizationally, the regulators will fight to preserve their authority and influence within their states. Most importantly, the distinction between interstate and intrastate activities may indeed be "arbitrary" when examining the technical workings of the telephone network, but it has immense political and historical significance under the federalist system of government. Much political and legal resistance to a redefinition of federal jurisdictional boundaries may arise simply from the implied encroachment on state sovereignty.

E. <u>Epilogue</u>

The cases analyzed in this paper do not define the absolute boundaries of state and federal regulatory jurisdiction over the telephone industry. Indeed, state and federal regulators continually adjust and allocate the scope of their jurisdictions through formal and informal agreements.[409] These agreements are guided by the Communications Act, but the vast majority of them never reach the courts. Section 410 of the Act recognizes the importance of such coordination through its provisions authorizing joint boards and less formal consultations.[410]

However, judicial decisions will provide the formal benchmarks for resolving future jurisdictional disputes over regulation of the telephone industry.[411] Even if new legislation replaces the present version of the Communications Act, decisions interpreting the Act may well be valuable in resolving questions under the new statutes.

In the absence of new legislation, the restructuring of the telephone industry will undoubtedly cause new jurisdictional conflicts among regulators. The traditional disputes between the FCC and the state regulators will continue as new manifestations of old problems. For example, how should section 221(b) of the Act govern regulatory jurisdiction in a LATA that straddles state lines? If a new separations scheme is adopted, how should it reflect the holding of Smith v. Illinois Bell Telephone Company? If new technology permits individual telephone messages to be identified as belonging to either the state or federal jurisdiction, should such technology be used to more precisely define the scopes of the jurisdictions?[412]

In addition, the MFJ has introduced other dimensions into the problem of relative federal and state regulatory jurisdiction over telephone. The U.S. District Court for the District of Columbia has retained jurisdiction over the MFJ for purposes of enforcement and for modifying any of the MFJ's provisions.[413] State regulators, the FCC, and all other groups must act within the District Court's reading of the MFJ. Because of the substantial industry changes and restrictions incorporated in the MFJ, the District Court may be a potent regulatory force in its own right.

Indeed, the broad sweep of the MFJ as an affirmative federal antitrust remedy could lead to overt conflicts between FCC regulation under the Communications Act and the goals of the MFJ.[414] Does the potential for such conflict suggest that further change in the structure or goals of telephone regulation is required?

NOTES

1 See Section 3, infra.

2 United States v. American Telephone and Telegraph Company, 552 F. Supp. 131 (D.D.C. 1982), aff'd sub nom. Maryland v. United States, 103 S. Ct. 1240 (1983).

3 47 U.S.C. secs. 151-222, 401-609 (1980)

4 Sherman Act, 15 U.S.C. sec. 2 (1970). See also United State v. American Telephone & Telegraph Company, Plaintiff's First Statement of Contentions and Proof, Civ. Action No. 74-1698 (D.D.C. 1974)

5 47 U.S.C. sec. 153 (1981).

6 47 U.S.C. sec. 152. Other bases for FCC jurisdiction are discussed infra, Section 3.

7 47 U.S.C. sec. 153.

8 See, e.g., Cal. Publ. Util. Code secs. 301, 451, 701, 1001; 25 M.G.L. sec. 1-10B (1981); 1 N.Y. Pub. Serv. L. sec. 2-26 (1982); 66 Pa. C.S. sec. 501, 1101-1509, 2901-2904 (1981).

9 See, e.g., 47 U.S.C. sec. 201 (a) (duty of common carriers to provide service upon reasonable request), sec. 201 (b) (charges must be just and reasonable), sec. 215 (regulation of service and equipment). Compare, e.g., N.Y. Public Service Law sec. 91 (adequate service; just and reasonable charges), sec. 97 (regulation of service).

10 See, e.g., 47 U.S.C. 201 (b).

11 See, e.g., N.Y. Public Service Law sec. 97 (1).

12 Compare 47 U.S.C. sec. 214 with 66 Pa. C.S. secs. 1501, 1503 (extension and discontinuance of service).

13 See, e.g. 47 U.S.C. sec. 215; 47 C.F.R. secs. 68.300-68.314 ("Connection of terminal equipment to the telephone network").

14 Computer and Communications Industry Association v. FCC, 693 F. 2d 198, 214 (D.C. Cir. 1982), cert. denied sub nom. Louisiana Public Service Commission v. FCC, 103 S. Ct. 2109 (1983) (footnotes omitted). See also New York Telephone Company v. FCC, 631 F. 2d 1059 (2d Cir. 1980).

15 Computer and Communications Industry Association v. FCC, 693 F. 2d at 213.

16 U.S. Const. art. I, sec. 8, c. 3.

17 Houston, East & West Texas Railway Company v. United States, 234 U.S. 342 (1914) (the Shreveport Case).

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

19 U.S. Const. art. VI, cl. 2. See Gibbons v. Ogden, 22 U.S. (9 Wheat) 1 (1824).

20 See E.F. Renshaw, On the Distribution of Telephone Communication Subsidies, Pub. Util. Fort., July 21, 1983 at 34; B. Johnson and S.D. Thomas, Deregulation and Divestiture in a Changing Telecommunications Industry, Publ Util. Fort., Oct. 14, 1982 at 17.

21 See R.L. Littell and K.J. Neises, Telecommunications Reform: A Look at Federal and State Relations, in 21 Proceedings of the Iowa State University Regulatory Conference 430 (1982); J.E. Bryson and J. Donner, States Uneasy Partners in Communications Revolution, Legal Times, August 29, 1983, at 12.

22 North Carolina Utilities Commission v. FCC, 537 F. 2d 787, 793 n. 6 (4th Cir. 1976), cert. denied 429 U.S. 1027 (1976).

23 Carol L. Weinhaus and Anthony G. Oettinger, Behind the Telephone Debates - 1, At the Heart of the Debates: Costs, Control, and Ownership of the Existing Network Sec.II (Harvard University, Program on Information Resources Policy, Feb. 1985).

24 North Carolina Utilities Commission v. FCC, 552 F. 2d 1036 (4th Cir. 1977), cert. denied 434 U.S. 874 (1977). See also North Carolina Utilities Commission v. FCC, 537 F.2d 787 (4th Cir. 1976), cert. denied 429 U.S. 1027 (1976); Sherdon v. Dann, 193 Neb. 768, 229 N.W. 2d 531 (1975).

25 Canada regulates telephone service through a complicated allocation of jurisdiction among the national government and the provinces. See J. Schmidt and R. Corbin, Telecommunications in Canada: The Regulatory Crisis, Telecommunications Policy, Sept. 1983 at 215.

26 J.L. Salvaggio, Social Problems of Information Societies: The US and Japanese Experience, Telecommunications Policy, Sept. 1983 at 228.

27 See The Wall Street Journal, December 3, 1984, at 35, col. 1; J.H.M. Solomon, U.K. Strategy - The Momentum of Change, Telecommunications Policy, June 1983, at 6.

28 See generally G. Brock, The Telecommunications Industry, 89-125 (1981) (hereinafter referred to as "Brock"). Some states adopted regulatory statutes before the 1890s, but enforcement of these was limited. See also B. Compaine, R. Pepper and A. Birinyi, Chronology of Telecommunications and Cable Television Regulation in the United States 3-15 (Harvard University, Program on Information Resources Policy, Jan. 1984).

29 Brock, _supra_ note 28, at 114.

30 _Id_. at 112-113.

31 W.K. Jones, _Regulated Industries_ 40 (2d ed. 1976).

32 Brock, _supra_ note 28, at 158.

33 Jones, _supra_ note 31, at 40.

34 The Mann-Elkins Act, 36 Stat. 539, 544 (1910) (repealed by Act of June 19, 1934, 48 Stat. 1102, codified as 47 U.S.C. sec. 602 (1976)).

35 _See_ text _infra_, at notes 293-303.

36 47 U.S.C. secs. 151-714 (1976).

37 T.N. Vail, "Some Truths and Some Conclusions," speech to Vermont State Grange (Dec. 14, 1915) _cited in_ Brock, _supra_ note 28, at 159.

38 Brock, _supra_ note 28, at 161.

39 _Id_, at 159.

40 _See_, e.g., _The Federalist_ No. 10, 28, 41, 47, 51; L. Tribe, _American Constitutional Law_ 2-3, 239-42 (1976).

41 Tribe, _supra_ note 40, at 319-412.

42 D.F. Pegrum, _The Regulation of Industry_ (Chicago: R.D. Irwin, 1949) 25-26.

43 _See_ text _supra_, at notes 16-19.

44 _National League of Cities v. Usery_, 426 U.S. 833 (1976); _Parker v. Brown_, 317 U.S. 341 (1943).

45 _See_, _e.g._, _Raymond Motor Transportation, Inc. v. Rice_, 434 U.S. 429 (1978); _Pike v. Bruce Church, Inc._, 397 U.S. 137 (1970).

46 _See_, _e.g._, E. Schneidewind, _What Do State Regulators Want from Judge Greene?_ in 21 Proceedings of the Iowa State University Regulatory Conference 91 (1982); E. Larkin, _Telephone: It Will Never Be The Same_, Pub. Util. Fort., April 14, 1983 at 15.

47 _See_, _e.g._, L. Garfinkel _Interexchange Markets in Transition_, Pub. Util. Fort., July 21, 1983 at 26; M.R. Irwin, _Local Networks in the U.S. - Technology versus Regulation_, Telecommunications, March 1982 at 21.

48 Note, _Competition in the Telephone Equipment Industry: Beyond Telerent_, 86 Yale L. J. 538 (1977); M.R. Irwin, _The Communication_

Industry and the Policy of Competition, 14 Buff. L. Rev. 256 (1965).

49 L. Garfinkel, Interexchange Markets in Transition, supra note 47, at 27.

50 Final Decision and Order, In re Regulatory and Policy Problems Presented by the Interdependence of Computer and Communication Services and Facilities, 28 F.C.C. 2d 267 (1971) (Computer Inquiry I), aff'd in part and rev'd in part sub nom. GTE Service Corp. v. FCC, 474 F. 2d 724 (2d Cir. 1973), decision on remand, 40 F.C.C. 2d 293 (1973).

51 Final Decision, In re Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), 77 F.C.C. 2d 384 (1980) (Computer Inquiry II Final Decision); Memorandum Opinion and Order, 84 F.C.C. 2d 50 (1980) (Computer Inquiry II Reconsidered Decision); Memorandum Opinion and Order, 88 F.C.C. 2d 512 (1981) (Computer Inquiry II Further Reconsidered Decision). These were affirmed in Computer and Communications Industry Association v. FCC, 693 F.2d 198 (D.C. Cir. 1982).

52 Computer Inquiry II Final Decision, 77 F.C.C. 2d at 388-389.

53 Id. at 474. See also Computer Inquiry II Reconsidered Decision, 84 F.C.C. 2d at 72.

54 See text infra. at notes 300-302.

55 See generally, W.T. Gormley, The Politics of Public Utility Regulation (1983).

56 United States v. AT&T, Complaint and Antitrust Equitable Relief Sought, Civ. Action No. 74-1698 (D.D.C., filed November 20, 1974)(hereinafter cited as "Complaint").

57 15 U.S.C. sec. 2 (1970).

58 Complaint, supra note 56, at 5 - 10.

59 Id. at 13.

60 Id. at 14.

61 Id.

62 Id.

63 Id.

64 See United States v. AT&T, 552 F. Supp. 131, 139-41 (D.D.C. 1982) (description of pretrial proceedings).

65 _Id_., _aff'd_ _sub nom_. _Maryland v. United States_, 103 S.Ct. 1240 (1983).

66 The holding companies are Pacific Telesis, US West, Ameritech, NYNEX, Bell Atlantic, Bell South, and Southwestern Bell.

67 _See_ 552 F. Supp. at 229.

68 _See_ Carol L. Weinhaus and Anthony G. Oettinger, _Behind the Telephone Debates-2_, _Concepts: Understanding Debates Over Competition and Divestiture_ Sec. VIA (Harvard University, Program on Information Resources Policy, Feb. 1985).

69 552 F. Supp. at 170-74.

70 _Id_. at 209.

71 See text _infra_, at notes 163-169.

72 552 F. Supp. at 142-43.

73 See text _infra_ at notes 114-116.

74 552 F. Supp. at 225, 227.

75 See text _infra_, at notes 156-162.

76 552 F. Supp. at 225.

77 _Id_.

78 _Id_.

79 _Id_. at 231-32.

80 _Id_. at 230-31.

81 _United States v. Western Electric Company_, 1956 Trade Cas. (CCH) 68,246 (D.N.J. 1956), _vacated_ 1982-2 Trade Cas. (CCH) 64,900 (D.N.J. 1982).

82 _Computer Inquiry I_, 28 F.C.C.2d 267 (1971), _aff'd in part and rev'd in part sub nom_. _GTE Service Corp. v. FCC_, 474 F.2d 724 (2d Cir. 1973), _decision on remand_ 40 F.C.C. 2d 293 (1973).

83 36 Fed. Reg. 5345, 5353-54 (1971).

84 28 F.C.C. 2d at 295.

85 28 F.C.C. 2d at 276-79, 305.

86 _Computer Inquiry I_ labeled this "maximum separation," 28 F.C.C. 2d at 169, 302-304.

87 See, e.g., AT&T, 62 F.C.C. 2d 21, 30-31 (1977), aff'd sub nom. International Business Machines Corp. v. FCC, 570 F.2d 452 (2d Cir. 1978) (classification of AT&T's Dataspeed 40/4 terminal).

88 See Notice of Inquiry and Proposed Rulemaking, In re Amendment of Section 64.702 of the Commission's Rules and Regulations, 61 F.C.C. 2d 103 (1977). See also Supplemental Notice of Inquiry and Enlargement of Proposed Rulemaking, In re Amendment of Section 64.702 of the Commission's Rules and Regulations, 64 F.C.C. 2d 771 (1977).

89 Computer Inquiry II Final Decision, 77 F.C.C. 2d 384 (1980); Computer Inquiry II Reconsidered Decision, 84 F.C.C. 2d 50 (1980); Computer Inquiry II Further Reconsidered Opinion, 88 F.C.C. 2d 512 (1981).

90 Computer Inquiry II Final Decision, 77 F.C.C. 2d at 419-20.

91 Id.

92 Id.

93 Id.

94 Computer Inquiry II Reconsidered Decision, 84 F.C.C. 2d at 72. Originally, both AT&T and GTE Corp., the largest regulated telephone companies, were required to create separate subsidies, 77 F.C.C. 2d at 387-89, but this was modified upon reconsideration.

95 Computer Inquiry II Final Decision, 77 F.C.C. 2d at 490-95.

96 Computer and Communications Industry Association v. FCC, 693 F.2d 198, 219-20 (D.C. Cir.1982), cert. denied sub nom. Louisiana Public Service Commission v. FCC, 103 S.Ct. 2109 (1983).

97 United States v. AT&T, 552 F. Supp. 131 178-80 (D.D.C. 1982), aff'd sub nom. Maryland v. United States, 103 S.Ct. 1240 (1983).

98 United States v. Western Electric Company, 1982-2 Trade Cas. (CCH) 64,900 (D.N.J. 1982).

99 United States v. AT&T, 552 F. Supp. at 178-80.

100 Id. at 173-74, 178.

101 For example, the customers of Bell system operating companies had to lease terminal equipment manufactured by the Western Electric Company.

102 AT&T Tariff FCC No. 132, filed April 16, 1957 (superseded).

103 Hush-a-Phone Corp. v. United States, 238 F.2d 266, 269 (D.C. Cir. 1956).

104 Hush-a-Phone Corp. v. AT&T, 22 F.C.C. 112 (1957).

105 13 F.C.C. 2d 420 (1968), aff'd 14 F.C.C.2d 571 (1968).

106 47 U.S.C. sec. 202(a).

107 AT&T, 15 F.C.C. 2d 605 (1968)

108 Proposals for New or Revised Classes of Interstate and Foreign Message Toll Tel. Serv. (MTS) and Wide Area Tel. Serv. (WATS), 56 F.C.C. 2d 593 (1975); modified 58 F.C.C. 2d 736 (1976).

109 North Carolina Utilities Commission v. FCC, 537 F. 2d 787 (4th Cir. 1977), cert. denied 434 U.S. 874 (1977).

110 Note, Competition in the Telephone Equipment Industry: Beyond Telerent, 86 Yale L.J. 538, 544-50 (1977).

111 Computer Inquiry II Final Decision, 77 F.C.C. 2d 384 (1980); Computer Inquiry II Reconsidered Decision, 84 F.C.C. 2d 50 (1980); Computer Inquiry II Further Reconsidered Opinion, 88 F.C.C. 2d 512 (1981). The Computer Inquiry II decisions referred to terminal equipment as Customer Premise Equipment (CPE).

112 Computer Inquiry II Final Decision, 77 F.C.C. 2d at 387-89.

113 Computer Inquiry II Reconsidered Decision, 84 F.C.C. 2d at 72.

114 United States v. AT&T, 552 F. Supp. 131, 173-74 178 (D.D.C. 1982), aff'd sub nom. Maryland v. United States, 103 x.ct. 1240 (1983).

115 Id. at 190-93.

116 Id. at 193-94.

117 For in-depth treatment of this subject, see S. Breyer, Regulation and its Reform at 285-314 (1982) (hereinafter cited as Breyer); B. Compaine, R. Pepper, and A. Birinyi, Chronology of Telecommunications and Cable Television Regulation in the United States (Harvard University, Program on Information Resources Policy, Jan. 1984).

118 In the Matter of Allocation of Frequencies in the Bands above 890 MC, 27 F.C.C. 359 (1959), 29 F.C.C. 825 (1960).

119 27 F.C.C. at 413-14.

120 In Re Applications of Microwave Communications, Inc., 18 F.C.C. 2d 953 (1969), recon. denied, 21 F.C.C. 2d 190 (1970).

121 In the Matter of Establishment of Policies and Procedures for Consideration of Applications to Provide Specialized Common Carrier Services in the Domestic Public Point-to-Point Microwave Radio Service, 29 F.C.C. 2d 870 (1971), recon. denied 31 F.C.C. 2d 1106

(1970), aff'd sub nom. Washington Utilities and Transportation Commission v. FCC, 513 F. 2d 1142 (9th Cir. 1975), cert. denied sub nom. National Association of Regulatory Utility Commissioners v. FCC, 423 U.S. 836 (1975).

122 29 F.C.C. 2d at 872.

123 Breyer, supra note 117, at 303-308.

124 Id.

125 47 U.S.C. sec. 202(a) (1980). For examples of such proceedings, see In the Matter of AT&T Changes, Classifications, Regulations, and Practices for and in Connection with Private Line Services and Channels, 34 F.C.C. 244 (1961), 34 F.C.C. 217 (1963), recon. denied, 34 F.C.C. 1094 (1963); In the Matter of TELPAK Tariff Sharing Provisions of AT&T and Western Union, 23 F.C.C. 2d 606 (1970), rev'd on other grounds sub nom. AT&T v FCC, 449 F.2d 439 (2d Cir. 1971); In the Matter of AT&T Charges, Regulations, Classifications and Practices for Voice Grade/Private Line Service (High Density-Low Density), 5.5 F.C.C. 2d 224 (1975), 58 F.C.C. 2d 428 (1976).

126 Resale and Shared Use (Report and Order), 60 F.C.C. 2d 261 (1976), recon. 62 F.C.C. 2d 588 (1977), aff'd sub nom. AT&T v. FCC, 572 F. 2d 17 (2d Cir. 1978), cert. denied, 439 U.S. 875 (1978).

127 United States v. AT&T, 552 F. Supp. 131, 172 (D.D.C. 1982).

128 In the Matter of Bell System Tariff Offerings of Local Distribution Facilities for Use by Other Common Carriers, 46 F.C.C. 2d 413 (1974), aff'd sub nom. Bell Telephone Company of Pennsylvania v. FCC, 503 F. 2d 1250 (3d Cir. 1974), cert. denied 422 U.S. 1026 (1975).

129 In the Matter of MCI Telecommunications Corp. 60 F.C.C. 2d (1976), rev'd sub nom. MCI Telecommunications Corp v.FCC, 561 F. 2d 365 (D.C. Cir. 1977), cert. denied, 434 U.S. 1040 (1978).

130 MCI Telecommunications Corp. v FCC, 561 F. 2d 365 (D.C. Cir. 1977), cert. denied, 434 U. S. 1040 (1978). (Execunet I).

131 Execunet I, 561 F. 2d 365 (D.C. Cir. 1977). See also 47 U.S.C. sec. 214 (c) (1976).

132 AT&T, 67 F.C.C. 2d 455 (1978), rev'd sub nom. MCI Telecommunications Corp. v. FCC, 580 F. 2d 590 (D.C. Cir. 1978), cert. denied 439 U.S. 980 (1978).

133 MCI Telecommunications Corp. v. FCC, 580 F. 2d 590 (D.C. Cir. 1978), cert. denied 439 U.S. 980 (1978). (Execunet II) (referring to Execunet I, 561 F. 2d 365 (D.C. Cir. 1977)).

134 In the Matter of MTS and WATS Market Structure, 67 F.C.C. 2d 757 (1978) (Notice of Inquiry and Proposed Rulemaking).

135 In the Matter of MTS and WATS Market Structure, 81 F.C.C. 2d 177 (1980) (Report and Third Supplemental Notice of Inquiry and Proposed Rulemaking).

136 Id. at 178-95.

137 In the Matter of MTS and WATS Market Structure, 73 F.C.C. 2d 222 (1979) (First Supplemental Notice).

138 Id. Because of the terminology associated with the MFJ, "interstate toll" charges are roughly equivalent to "interstate interLATA" charges.

139 See, e.g., 3 A. Oettinger and C. Weinhaus, Behind the Telephone Debates 14-17 (Harvard University, Program on Information Resources Policy, draft of Mar. 1984).

140 Exchange Network Facilities (ENFIA), 71 F.C.C. 2d 440 (1979).

141 Tariffs were filed with the FCC by the National Exchange Carriers Association, ____ F.C.C. 2d ____ (May 25, 1984).

142 In the Matter of MTS and WATS Market Structure, 77 F.C.C. 2d 224, 225 (1980) (Second Supplemental Notice of Inquiry and Proposed Rulemaking).

143 In the Matter of Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor, 77 F.C.C. 2d 308 (1979) (Competitive Common Carriers).

144 Competitive Common Carriers, 85 F.C.C. 2d 1 (1980) (First Report and Order).

145 Id. at 30-31.

146 Competitive Common Carriers, 91 F.C.C. 2d 59, 64-73 (1982) (Second Report and Order).

147 "Basic Services" are defined in Computer Inquiry II Final Decision, 77 F.C.C. 2d 384 (1980). See also text supra, at notes 126-129.

148 91 F.C.C. 2d at 73.

149 Id. at 61-63.

150 Competitive Common Carriers, __ F.C.C. 2d __, FCC Order 83-481, 48 Fed. Reg. 52,452 (Nov. 18, 1983) (Fourth Report and Order).

151 48 Fed. Reg. at 52,461.

152 Id.

153 For example, the FCC extended streamlined regulation to domestic record services (telegraph), domestic satellite carriers, and video transmission companies. Id. at 52,460-63.

154 Amendment of the Commission's Rules With Regard to Tariffs, __ F.C.C. 2d __, FCC Order 83-402, 48 F.R. 49, 033 (Oct. 24, 1983), 48 F.R. 52492 (Nov. 18, 1983).

155 Long-Run Regulation of AT&T's Basic Domestic Interstate Services, __ F.C.C. 2d __, FCC Order 83-482, 48 Fed. Reg. 51,340 (Nov. 8, 1983). In this order, the FCC specifically refers to interstate basic service, reflecting the terminology of Computer Inquiry II. See text supra, at notes 90-93.

156 United States v. AT&T, 552 F. Supp. 131, 170-173 (D.D.C. 1982) aff'd sub nom. Maryland v. United States, 103 S. Ct 1240 (1983). The decision speaks of "interexchange service" which is roughly equivalent to interLATA service.

157 552 F. Supp. at 171.

158 Id. at 195.

159 Id. at 195-200.

160 Id. at 172.

161 Id. at 170-73.

162 Id. at 171, citing United States v. Grinnell, 384 U.S. 563, 571 (1966).

163 552 F. Supp. at 196.

164 Id.

165 Id.

166 Id. at 199.

167 Id. at 197-198. The court noted that the FCC could revise the national area dialing plan at any time, id. However, for engineering reasons, most existing central offices are incapable of providing 11-digit long distance dialing to more than one long distance carrier. Competing long distance carriers that utilize such central offices may have to utilize up to 21-digit dialing for long distance calls due to such technical limitations, Letter from J.R. Hoffman to A.G. Oettinger (December 17, 1984).

168 Id. at 198-199.

169 Id.

170 Id. at 188-89. However, the divested companies can apply to have this restriction removed, see id. at 227, 231.

171 Id. at 188.

172 Id.

173 Compare the discussions of the "capture" model of regulation and the "organizational" model, text supra at notes 55-78.

174 29 F.C.C. 2d 870 (1971).

175 47 U.S.C. sec. 151 et seq. (1980).

176 47 U.S.C. sec. 151 (1980).

177 MCI Telecommunications Corporation v. FCC, 561 F. 2d 365, 380 (D.C. Cir. 1977), cert. denied 434 U.S. 1040 (1978). See also FCC v. RCA Communications, Inc., 346 U.S. 86, 96-97 (1953); Hawaiian Telephone Company v. FCC, 498 F. 2d 771 (D.C. Cir. 1974).

178 47 U.S.C. sec. 201.

179 47 U.S.C. sec. 153 (h).

180 National Association of Regulatory and Utility Commissioners v. FCC, 533 F.2d 601, 608 (D.C. Cir. 1976) (emphasis added).

181 Id. at 609, citing Industrial Radiolocation Service, 5 F.C.C. 2d 197, 202 (1966).

182 47 U.S.C. sec. 201 (a).

183 47 U.S.C. sec. 201 (b).

184 47 U.S.C. sec. 202.

185 See text infra, at notes 300-308, 315-321.

186 47 U.S.C. sec. 214.

187 See, e.g. General Telephone Company of California v. FCC, 413 F.2d 390 (D.C. Cir. 1969)

188 47 U.S.C. sec. 214 (a)(2).

189 47 U.S.C. sec. 151.

190 47 U.S.C. sec. 152(b) as amended (1978)

191 47 U.S.C. sec. 152(b)(1) (emphasis added).

192 See text infra, at notes 338-350.

193 47 U.S.C. sec. 152 (b)(2).

194 47 U.S.C. sec. 153 (u).

195 78 Cong. Rec. 8846 (1934) (statement of Sen. Clark). See also Comtronics, Inc. v. Puerto Rico Telephone Company, 553 F.2d 701 (1st Cir. 1977).

196 Comtronics, Inc. v. Puerto Rico Telephone Company, 553 F.2d 701, 709-10 (1st Cir. 1977).

197 Pub. L. No. 83-345, 68 Stat. 63 (codified as 47 U.S.C. sec. 152(b)(3),(4) (1980)).

198 See S. Rep. No. 1090, 83d Cong., 2d Sess. 1-3 (1954), H.R. Rep. No. 910, 83d Cong., 1st Sess. 1953.

199 Bell Telephone Laboratories, Engineering and Operations in the Bell System 438-40 (1977).

200 See New York Telephone Company v. FCC, 631 F.2d 1059,1065 (2d Cir. 1980), The Shreveport Case, 234 U.S. 342 (1914)

201 78 Cong. Rec. 10,313 (1934)(Statement of Rep. Rayburn). See text supra, at notes 182-184.

202 47 U.S.C. sec. 201(a).

203 559 F. 2d 720 (D.C. Cir. 1977).

204 559 F. 2d at 724 (emphasis added).

205 Id.

206 See 47 U.S.C. sec. 214, described in text supra, at notes 186-188.

207 47 U.S.C. sec. 152 (b)(2)

208 47 U.S.C. sec. 203 (a).

209 47 U.S.C. sec. 205.

210 47 U.S.C. sec. 224 (1980). "Pole attachments" refer to cables physically attached by a cable television system to a utility pole, duct or conduit. See 47 U.S.C. sec. 224 (a)(2). The FCC is authorized to regulate the rates, terms, and conditions for pole attachments except where a state regulates such items, 47 U.S.C. sec. 224 (b), (c). See also Monongahela Power Company v. FCC, 655 F. 2d 1254 (D.C. Cir. 1981).

211 47 U.S.C. sec. 301 as amended.

212 See text supra, at notes 186-188.

213 47 U.S.C. sec. 214 (a)(1).

214 47 U.S.C. sec. 154(i).

215 Lincoln Telephone and Telegraph Company v. FCC, 659 F. 2d 1092, 1108-1109 (D.C. Cir. 1981).

216 General Telephone Company of the Southwest v. the United States, 449 F. 2d 846, 855 (5th Cir. 1971)(footnote omitted).

217 47 U.S.C. sec. 153(h).

218 47 U.S.C. sec. 153(u).

219 47 U.S.C. sec. 214(a)(3).

220 The Willis-Graham Act, Pub. L. No. 15, 42 Stat. 27 (1921) (current version at 47 U.S.C. sec. 221(a) (1976)). See 1 A. Oettinger and C. Weinhaus, The Once and Future Telephone Plant and Costs: At the Heart of Debates 6 (Harvard University, Program on Information Resources Policy, Draft of Dec. 1983).

221 See, e.g. In re Wisconsin Telephone Company, 27 F.C.C. 1 (1959). See also MCI Communications Corporation v. AT&T, 708 F.2d 1081 (7th Cir. 1983), cert. denied 104 S.Ct. 243 (1983).

222 47 U.S.C. sec. 221 (b).

223 47 U.S.C. sec. 153 (r).

224 537 F.2d 787 (4th Cir. 1976), cert. denied 429 U.S. 1027 (1976).

225 537 F.2d at 795. For example, Rep. Rayburn of Texas explained on the floor of the House that section 221(b) "is designed to cover cases of cities located within two States, as Texarkana," 78 Cong. Rec. 10,314 (1934).

226 553 F. 2d 694, 698-99 (1st Cir. 1977).

227 See text infra, at notes 331-337.

228 47 U.S.C. sec. 221 (c).

229 47 U.S.C. sec. 153 (s).

230 47 U.S.C. sec. 410.

231 See, e.g., 5 U.S.C. secs. 556, 557, 3105 (1980).

232 Sections 221 (c), (d) of the Act deal with an aspect of the separations issue. See text supra, at notes 108-109.

233 174 U.S. 761 (1898).

234 14 Stat. at L. 221 (1866), R.S. secs. 5263-69 (repealed by Act of July 16, 1947, c. 256, s. 1, 61 Stat. 327 (1947)).

235 174 U.S. at 775.

236 Id. at 777.

237 Id. at 778.

238 Southern Bell Telephone & Telegraph Company v. City of Richmond, 103 F. 31 (4th Cir. 1900), app. dismissed 22 S. Ct. 134 (1901).

239 See text supra, at notes 34-36. However, a 1901 federal statute governed telephone rights-of-way in the Indian Territory. See text infra, at notes 244-245.

240 174 U.S. at 777.

241 118 F. 382 (8th Cir. 1902)

242 118 F. at 385.

243 Id.

244 Indian Appropriation Act, ch. 832, sec. 3, 31 Stat. 1083 (1901). (Current version at 25 U.S.C. secs. 319, 357 (1980)).

245 118 F. at 385.

246 96 U.S. 1 (1878).

247 Id. at 11.

248 14 Stat. at L. 221 (1866).

249 254 U.S. 17 (1920).

250 Id. at 18.

251 Speight v. Western Union Telegraph Company, 178 N.C. 146, 100 S.E. 351 (1919).

252 162 U.S. 650 (1896).

253 1887 Ga. Laws 111 (current version at Ga. Code secs. 45-5-145, 145 (1982)). The penalty has been reduced from $100 to $25.

254 162 U.S. at 660.

255 Id.

256 251 U.S. 315 (1920).

257 36 Stat. 539, 544-45 (1910) (repealed by Act of June 19, 1934, 48 Stat. 1102, codified as 47 U.S.C. sec. 602 (1976)).

258 36 Stat. at 547-48.

259 _See_ Wheat, _The Regulation of Interstate Telephone Rates_, 51 Harv. L. Rev. 846 (1938) (hereinafter "Wheat").

260 44 I.C.C. 670 (1917).

261 44 I.C.C. at 674, _citing_ 36 Stat. at 544.

262 112 I.C.C. 377 (1926).

263 _Id_. at 379. The $40 deposit was found to be reasonable and not unduly prejudicial, _id_. at 380.

264 Wheat, _supra_ note 259, at 847.

265 _Id_.

266 41 Stat. 493 (1920) (repealed by Act of June 19, 1934, 48 Stat. 1102, codified as 47 U.S.C. 602 (1976)).

267 297 U.S. 471 (1936)

268 282 U.S. 133 (1930)

269 _See_ Wheat. _supra_ note 259, at 866-68.

270 _See_ Wheat, _supra_ note 259, at 868.

271 _See_ Wheat, _supra_ note 259.

272 282 U.S. 133 (1930).

273 U.S. Const. amend XIV, sec. 1.

274 282 U.S. at 148.

275 292 U.S. at 150-151.

276 _See_ _Illinois Bell Telephone Company v. Gilbert_, 3 F. Supp. 595 (N.D. Ill. 1933).

277 292 U.S. 151 (1934).

278 _See_ Wheat, _supra_ note 259, at 868-69, n. 44.

279 _Id_.

280 NARUC, _Standard Procedures for Separating Telephone Property Costs, Revenues, Expenses, Taxes, and Reserves_ (the "_Separations Manual_") (Feb. 1971).

281 See Note, The Proposed Deregulation of Domestic Common Carrier Telecommunications. 69 Cal. L. Rev. 455, 468 (1981).

282 See text supra, at note 274.

283 See Note, supra note 281.

284 Wheat, supra note 259, at 868.

285 3 A. Oettinger and C. Weinhaus, The Telephone Book: Dividing the Costs Between Federal and State Regulators 17-18 (Harvard University, Program on Information Resources Policy, Draft of Dec. 6, 1983).

286 77 A.D. 2d 332, 434 N.Y.S. 2d 727 (1980), app. dismissed, 53 N.Y. 2d 838, 422 N.E. 2d 831, 440 N.Y.S. 2d 186 (1981).

287 77 A.D. 2d at 335, 434 N.Y.S. 2d at 730.

288 "A customer subscribing to FX can make and receive calls from an exchange outside the subscriber's local calling area without payment of a toll charge and is given a telephone listing in the distant exchange. CCSA customers are allowed such toll-free calling to and from a number of distant exchanges via a switched network of foreign exchange lines." 77 A.D. 2d at 334, 434 N.Y.S. 2d at 729.

289 77 A.D. 2d at 335, 434 N.Y.S. 2d at 730.

290 47 U.S.C. sec. 410(c) (1976).

291 631 F. 2d 1059 (2d Cir. 1980).

292 76 F.C.C. 2d 349 (1980).

293 47 U.S.C. sec. 203 (1976).

294 NY Tel, 631 F. 2d 1059 (2d Cir. 1980)

295 Id. at 1066.

296 Id., citing Southern Pacific Communications, 61 F.C.C. 2d 144, 146 (1976).

297 631 F. 2d at 1065.

298 Id. at 1067.

299 Id. at 1068.

300 North Carolina Utilities Commission v. FCC, 537 F. 2d 787 (4th Cir. 1976) (NC I), cert. denied 429 U.S. 1027 (1976), North Carolina

Utilities Commission v. FCC, 552 F. 2d 1036 (4th Cir. 1977) (NC II), cert. denied 434 U.S. 874 (1977).

301 See text supra, at notes 117-174.

302 Telerent Leasing Corp. 45 F.C.C. 2d 204 (1974), aff'd NC I, supra note 336, cert. denied 429 U.S. 1027 (1976).

303 47 U.S.C. sec. 152(b) (1970). Although section 152(b) has been amended since the NC I and II decisions, the amendments did not change the portion of the section considered in the case.

304 NC I, 537 F. 2d at 794, n. 6.

305 47 U.S.C. sec. 152(a) (1970).

306 47 U.S.C. sec. 410(c) (1970).

307 537 F. 2d at 794.

308 Id. at 793.

309 See generally, Note, Competition in the Telephone Equipment Industry: Beyond Telerent, 86 Yale L.J. 538 (1977)

310 See text supra, at notes 222-223. Section 221(b) provides in pertinent part: "[N]othing in this Act shall be construed . . . to give the [FCC] jurisdiction, with respect to charges, classifications, practices. Services, facilities, or regulation for or in connection with . . . telephone exchange service, . . . 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 local governmental authority." 47 U.S.C. sec. 221(b).

311 See text supra, at notes 224-227.

312 NC II, supra note 336, cert. denied 434 U.S. 874 (1977).

313 Proposals for New or Revised Classes of Interstate and Foreign MTS and WATS, 56 F.C.C. 2d 593 (1975) (First Report and Order), 58 F.C.C. 2d 736 (1976) (Second Report and Order).

314 NC II, 552 F.2d at 1044-45.

315 Id. at 1045-50.

316 Id. at 1045.

317 Id. at 1046.

318 See 47 U.S.C. sec. 151.

319 552 F. 2d at 1046.

320 47 U.S.C. sec. 151.

321 552 F. 2d at 1046.

322 Id. at 1048.

323 Id. at 1047.

324 Houston, East & West Texas Railway v. United States, 234 U.S. 342 (1914) (popularly known as the Shreveport Case).

325 234 U.S. at 357-58.

326 NC II, 552 F. 2d at 1048.

327 Id.

328 Id. at 1049.

329 Id. at 1049-50.

330 Accord, Sherdon v. Dann, 193 Neb. 768, 229 N.W. 2d 531 (1975). In Sherdon, the Nebraska Supreme Court adopted NC II's general analysis two years earlier. The court held that the FCC's claim of jurisdiction over a hotel's terminal equipment preempted that of the Nebraska Public Service Commission.

331 719 F. 2d 89 (4th Cir. 1983).

332 719 F. 2d at 90.

333 U.S. Const. art. III, sec. 2, cl. 2.

334 47 U.S.C. sec. 152(a).

335 Id., sec. 201(a).

336 Id., sec. 221(b). See text supra, at notes 258-59; 346-47.

337 304 N.W. 2d 872 (Minn. 1981).

338 See Section 3, supra, at notes 117-129.

339 567 F. 2d 84 (D.C. Cir. 1977), cert. denied, 434 U.S. 1010 (1978). Southern Pacific's service is now known as GTE/Sprint.

340 Id. at 87-88.

341 AT&T Interconnection with Specialized Carriers in Furnishing FX and CCSA, 56 F.C.C. 2d 12 (1975) (Memorandum Order and Opinion), aff'd, People of California v. FCC, 567 F. 2d 84 (D.C. Cir. 1977), cert. denied, 434 U.S. 1010 (1978).

342 Id. at 21.

343 This case occurred before NY Tel v. FCC, supra note 327, in which the FCC asserted jurisdiction over the local portion of interstate FX service.

344 California v. FCC, 567 F. 2d 84 (D.C. Cir. 1977).

345 537 F. 2d 787 (D.C. Cir. 1976).

346 567 F. 2d at 89-90.

347 Id. at 91.

348 Id. at 90.

349 See text infra, at note 411.

350 Southern Pacific Communications Company v. Corporations Commission, 586 P. 2d 327 (Okl. 1978).

351 Computer and Communications Industry Association v. FCC, 693 F. 2d 198 (D.C. Cir. 1982), cert. denied sub nom. Louisiana Public Service Commission v. FCC, 103 S. Ct. 2109 (1983).

352 693 F. 2d at 215.

353 Id. at 217.

354 Id. at 214-15.

355 Id.

356 NC I, 537 F. 2d 787, 793 note 6 (4th Cir. 1976).

357 234 U.S. 342 (1914). See text supra, at notes 322-328.

358 NC II, 552 F. 2d at 1047.

359 693 F. 2d at 216 (emphasis added).

360 47 U.S.C. sec. 202 (1976).

361 The court also adopted the Fourth Circuit's interpretation of section 221(b) of the Act in refusing to bar FCC jurisdiction on that ground, 693 F. 2d at 216-17.

362 Id. at 217 (emphasis added).

363 Id.

364 Cf. G. Orwell, 1984 (1949).

365 47 U.S.C. sec. 201.

366 *Id*. sec. 152(a).

367 *Id*. sec. 153(a).

368 693 F. 2d at 217 (emphasis in original).

369 *Id*., citing *New York State Commission on Cable Television v. FCC*, 669 F. 2d 58 (2d Cir. 1982).

370 *Computer Inquiry II Final Decision*, 77 F.C.C. 2d at 429.

371 47 U.S.C. sec. 221(a). See text *infra*, at notes 389-392.

372 *United States v. AT&T*, 552 F. Supp. 131, 153-159 (D.D.C. 1982), *aff'd sub nom*. *Maryland v. United States*, 103 S. Ct. 1240 (1983).

373 552 F. Supp. at 155.

374 U.S. Const. art. VI., cl. 2.

375 317 U.S. 341 (1943).

376 552 F. Supp. at 157.

377 *Id*.

378 *Id*.

379 445 U.S. 97 (1980).

380 *Id*. at 105.

381 552 F. Supp. at 159.

382 *Id*.

383 *Id*. at 160.

384 U.S. Const. amend. X, "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States . . . ."

385 426 U.S. 833 (1976).

386 *Id*. at 852.

387 426 U.S. at 845.

388 552 F. Supp. at 156-57, *citing Hodel v. Virginia Surface Mining and Reclamation Ass'n*., 452 U.S. 264, 286 (1981).

389 *Id*. at 157.

390 See United States v. AT&T, 461 F. Supp. 1314 (D.D.C. 1978) (Opinion on procedural motions).

391 Id. at 1320-30.

392 See text supra, at note 16. See also 552 F. Supp. at 154-55, 158-59.

393 See United States v. AT&T, 524 F. Supp. 1336, 1345 (D.D.C. 1981) (AT&T's motion to dismiss suit denied); United States v. AT&T, 461 F. Supp. 1314 (D.D.C. 1978).

394 282 U.S. 133 (1930)

395 537 F. 2d 787 (4th Cir. 1976), cert. denied 429 U.S. 1027 (1976).

396 567 F. 2d 84 (D.C. Cir. 1977), cert. denied 434 U.S. 1010 (1978).

397 552 F. 2d 1036 (4th Cir. 1977), cert. denied 434 U.S. 874 (1977).

398 552 F. Supp. 131 (D.D.C. 1982), aff'd. sub nom. Maryland v. United States, 103 S.Ct. 1240 (1983).

399 118 F. 382 (8th Cir. 1902).

400 254 U.S. 17 (1920).

401 631 F. 2d 1059 (2d Cir. 1980).

402 Computer and Communications Industry Association v. FCC, 693 F. 2d 198 (D.C. Cir. 1982), cert. denied sub nom. Louisiana Public Service Commission v. FCC, 103 S. Ct. 2109 (1983).

403 See text supra, at notes 284-285.

404 New York Telephone Company v. FCC, 631 F. 2d 1059 (2d Cir. 1980); New York Telephone Company v. Public Service Commission, 77 A.D. 2d 332, 434 N.Y.S. 2d 727 (1980), app. dismissed, 53 N.Y. 2d 838, 422 N.E. 2d 831, 440 N.Y.S. 2d 186 (1981).

405 162 U.S. 650 (1896).

406 304 N.W. 2d 872 (Minn. 1981).

407 See, e.g. S. 898, 97th Cong., 1st Sess. sec. 103, 127 Cong. Rec. sec. 3545 (daily ed. April 7, 1981) (amending 47 U.S.C. 152); S. 2827, 96th Cong., 2d Sess. sec. 103, 126 Cong. Rec. sec. 7016 (daily ed. June 13, 1980) (amending 47 U.S.C. sec. 152); H.R. 6121, 96th Cong., 2d Sess. sec. 2(a) (1980) (amending 47 U.S.C. sec. 201).

408 See, e.g., Note, The Proposed Deregulation of Domestic Common Carrier Telecommunications, 69 Calif. L. Rev 455, 477-79 (1981).

409 See, e.g., Diamond International Corporation v. FCC, 627 F. 2d 492 (D.C. Cir. 1980) (FCC may determine that some charges for PBX service may be contained in state tariffs rather than interstate tariffs).

410 47 U.S.C. sec. 410.

411 See, e.g., Virginia State Corporation Commission v. FCC, 737 F.2d 388 (4th Cir. 1984) (FCC order, which prescribes depreciation methods for telephone facilities and equipment used for both interstate and intrastate service, preempts conflicting state regulations; application of NC I and NC II; Southwestern Bell Telephone Company v. Arkansas Public Service Commission, 738 F.2d 901 (8th Cir. 1984), petition for cert. filed 53 U.S. L.W. 3290 (U.S. September 26, 1984) (No. 84-483) (Telephone company enjoined from using any intrastate depreciation methods other than those specified by the FCC until final decision in the courts regarding preemption).

412 See California v. FCC, supra note 339, at 89-91. See also discussion in text supra, at notes 346-49.

413 United States v. AT&T, supra note 372, at 231-32.

414 See text supra, at notes 389-92.