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Give Peace A Chance: FCC-State Relations After California III

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Give Peace A Chance: FCC-State Relations After *California III*

Jonathan Jacob Nadler*

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INTRODUCTION

For nearly twenty years, the Federal Communications Commission (FCC or Commission) and the states have been engaged in a bitter "border war." The combatants have repeatedly clashed over two related issues: what is the dividing line between federal and state jurisdiction over telecommunications services and equipment¹ and, once that line is established, when may the FCC enter state "territory" to preempt regulations that are inconsistent with federal policies?²

1. As used in this Article, the term "telecommunications services" refers to basic communications transport and enhanced services. The term does not include cable, broadcast, or other types of service subject to FCC regulation. The term "telecommunications equipment" refers to customer premises equipment, inside wiring, and network switching and transport facilities. Except where otherwise noted, all references and conclusions in this Article are limited to regulations governing the provision of telecommunications services and equipment by federally regulated common carriers, such as AT&T, the Bell Operating Companies (BOCs), and the independent telephone companies.

2. Telecommunications regulation is not the only area in which difficult issues of federal-state relations have had to be resolved. See generally Anna Mastracco et al., *Federal*

Three recent appellate decisions—*Georgia Public Service Commission v. FCC (Georgia PSC)*,³ *California II*,⁴ and *California III*⁵—provide an opportunity to bring the long-running dispute to an end. These decisions represent the culmination of a process by which the federal courts have clarified the principles governing FCC-state relations. These principles provide that the FCC and the states have control over telecommunications facilities and services within their respective jurisdictions. They further provide that the FCC is required to accept divergent state *policies* regarding intrastate common carrier facilities and services, but that where state regulation threatens to displace the FCC's *jurisdiction* over interstate common carriers, the FCC may carefully—but forcefully—exercise its preemptive power.

This Article first reviews the basis and history of the federal-state conflict, with particular emphasis on the three most recent judicial decisions. It then lays out a workable set of principles, grounded firmly in the case law, that can provide a basis for the cessation of hostilities between the FCC and the states. The Article concludes by highlighting several additional jurisdictional issues that will have to be resolved in the coming years.

I. THE TWENTY YEARS' WAR

The federal-state conflict has followed a classic format. After experiencing initial victories, an over-confident FCC ventured far into state territory. Thus overextended, the Commission was unable to withstand the inevitable state counter-attack. Stung by several sharp defeats, the FCC strategically retreated, dug in, and successfully fended off further state efforts to redraw the jurisdictional map.

A. *Origins and Basis of the FCC-State Conflict*

The origins of this dispute go back to 1934, when Congress enacted the Communications Act.⁶ In adopting the Act, Congress had to make a

and State Coordination: A Survey of Administrative Law Schemes, 46 ADMIN. L. REV. 385 (1994) (describing the means by which jurisdictional conflicts have been resolved in aviation, trade, education, health, safety, and other areas).

3. *Georgia Pub. Serv. Comm'n*, No. 92-8257, 1993 U.S. App. LEXIS 24458 (11th Cir. Sept. 22, 1993) [hereinafter *Georgia PSC*].

4. *California v. FCC*, 4 F.3d 1505 (9th Cir. 1993) [hereinafter *California II*].

5. *California v. FCC*, 39 F.3d 919 (9th Cir. 1994) [hereinafter *California III*], *petition for cert. denied*, 1995 U.S. LEXIS 2435 (Apr. 3, 1995).

6. For a description of the origin and adoption of the Communications Act, see generally MICHAEL K. KELLOGG ET AL., *FEDERAL TELECOMMUNICATIONS LAW* § 2.1.A (1992) and Richard R. McKenna, *Preemption Under the Communications Act*, 37 FED.

decision: How would it divide the communications regulatory "turf" between the newly created FCC and the existing state regulatory authorities? Pursuant to its powers under the Commerce Clause,⁷ Congress presumably could have ceded control over the entire field to the FCC, leaving no room for state regulation.⁸ Alternatively, Congress might have divided responsibility between the FCC and the states, but authorized the FCC to displace any inconsistent state regulation.⁹ Congress, however, chose neither of these approaches.¹⁰

COMM. L.J. 1, 7-18 (1985). The relevant legislative materials are compiled in MAX D. PAGLIN, *A LEGISLATIVE HISTORY OF THE COMMUNICATIONS ACT OF 1934* (1989). At the present time, Congress is considering fundamental reform of the Act. Any legislation that is enacted could alter the balance of power between the FCC and the states.

7. U.S. CONST. art. I, § 8.

8. See *City of N.Y. v. FCC*, 486 U.S. 57, 63-64 (1987) (quoting *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 369 (1986) [hereinafter *Louisiana*] ("[When the FCC is] 'acting within the scope of its congressionally delegated authority [it] may pre-empt state regulation' and hence render unenforceable state or local laws that are otherwise not inconsistent with federal law.")). Compare *Jones v. Rath Packing Co.*, 430 U.S. 519 (1977) (express statutory provision preempts state regulation) with *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218 (1947) (federal law "occupying the field" implicitly preempts state regulation).

9. There was ample precedent for this approach. Under the Mann-Elkins Act, ch. 309, § 7, 36 Stat. 539 (1910), which was in effect between 1910 and 1934, the Interstate Commerce Commission (ICC) was given authority to regulate interstate telecommunications. The ICC's regulatory authority, which included the right to review tariffs and order interconnection, was based on the agency's existing authority to regulate the railroad industry. In the *Shreveport Rate Case*, the Supreme Court upheld the power of the ICC to regulate rates for the transportation by rail of goods wholly within a single state on the grounds that such rates could "affect" interstate commerce. See *Houston, E. & W. Tex. Ry. v. United States*, 234 U.S. 342 (1914). Like the transportation of goods by railroad, the transport of information by wire or radio—even if physically intrastate—has an effect on interstate commerce. The ICC, therefore, could have used its authority under the Mann-Elkins Act to regulate intrastate telephone service. The agency did not, however, choose to do so.

10. Indeed, the possibility of preserving the jurisdictional arrangement that existed under the Mann-Elkins Act was expressly rejected. See *Regulation of Interstate and Foreign Communications by Wire or Radio: Hearings on S. 2910 Before the Comm. on Interstate Commerce*, 73d Cong., 2d Sess. 156, 179 (1934) (colloquy between Sens. Dill and Long noting that the proposed Act would provide "[p]rotection against the *Shreveport* decision" in the telecommunications area); 78 CONG. REC. 8816-23 (1934) (statement of Senate Commerce Committee Chairman Dill introducing the Communications Act) ("[T]he Interstate Commerce Commission, through the *Shreveport* decision . . . has gone so far in the regulation of railroads that the so-called 'State Regulation' amounts to very little. . . . [T]he State commission representatives were jealous, in the preparation of the bill, that those rights should be protected; and we have attempted to do that."); see also *Computer & Communications Indus. Ass'n v. FCC*, 693 F.2d 198, 216 n.99 (D.C. Cir. 1982) [hereinafter *CCLA*] ("Congress may well have intended Section 2(b) of the Communications Act to prevent . . . [the *Shreveport*] result in the communications area."), *cert. denied*, 461 U.S. 938 (1983); *North Carolina Util. Comm'n v. FCC*, 552 F.2d 1036, 1047 (4th Cir.) [hereinafter *NCUC II*] ("In enacting the Communications Act, Congress sought to deny the

What Congress did do was to create a system of “dual jurisdiction” over communications. Section 1 of the Communications Act grants the FCC authority to “regulat[e] interstate and foreign . . . communication by wire and radio.”¹¹ At the same time, Section 2(b)(1) of the Act states that “nothing in this Act shall be construed . . . to give the Commission jurisdiction with respect to . . . charges, classifications, practices, services, facilities, or regulations for or in connection with *intrastate* communication service of any carrier.”¹²

The Communications Act thus appears to divide the communications world “neatly into two hemispheres—one comprised of interstate service, over which the FCC would have plenary authority, and the other made up of intrastate service, over which the states would retain exclusive jurisdiction.”¹³ However, if Congress hoped to create a clearly marked border and to erect armed fortifications that would keep the FCC and the states on their respective sides, its efforts were destined to fail. As the Supreme Court has recognized, the “realities of technology and economics” make “such a clean parcelling of responsibility” impossible.¹⁴

The reason is simple: the same facilities are used to provide both interstate and intrastate telecommunications services. Thus, a telephone subscriber in Los Angeles must use the same customer premises equipment (CPE),¹⁵ the same inside wiring,¹⁶ the same “local loop,”¹⁷ and the same central office switching facilities¹⁸ to call San Francisco as he does to call New York City. This creates two distinct problems.

FCC of the kind of jurisdiction over local rates approved by the *Shreveport Rate Case*.”), *cert. denied*, 434 U.S. 874 (1977).

11. 47 U.S.C. § 151 (1988) (emphasis added). Section 4(i) of the Act further states that “[t]he Commission may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this Act, as may be necessary in the execution of its functions.” 47 U.S.C. § 154(i) (1988).

12. 47 U.S.C. § 152(b) (Supp. V 1993) (emphasis added).

13. *Louisiana*, 476 U.S. 355, 360 (1986).

14. *Id.*

15. Customer premises equipment (CPE), often referred to as terminal equipment, is communications equipment that is located on the subscriber’s premises. CPE includes simple telephone handsets as well as more sophisticated equipment such as modems, multiplexers, and private branch exchanges.

16. Inside wiring is the physical transmission path located on the customer’s premises that connects CPE to the network.

17. The local loop is the physical transmission path from a subscriber’s premises to the central office of the local exchange carrier (LEC).

18. Switching facilities are used to route communications “traffic” from the LEC’s central office towards its destination.

1. How Can the Federal-State Boundary be Determined?

As is the case with many border wars, the first matter in contention between the FCC and the states is where the boundary line between the two jurisdictions lies. Although Congress may have wished it to be otherwise, the location of the border is not immediately obvious. In the above example, the CPE, inside wiring, local loop, and switches used by the caller in Los Angeles are physically present within California. Moreover, the overwhelming majority of the calls carried over these facilities are likely to terminate within the state.¹⁹ Therefore, regulatory authority over these facilities (and the services provided over them) could be assigned exclusively to the intrastate jurisdiction. On the other hand, because these facilities are used to transport some calls that cross state lines, they could be considered to be within the federal regulatory domain.

The difficulty of "mapping the boundaries" between the federal and state domains has been compounded by the growth of enhanced services, which combine basic communications transport with computer processing applications.²⁰ When a subscriber in Los Angeles places a telephone call to San Francisco, it is usually safe to assume, the transmission does not leave California; when he calls New York, the transmission assuredly crosses the state line. In contrast, when a researcher in Los Angeles accesses a nationwide electronic information service, she may interact—in the course of a single on-line session—with a "gateway" menu in Baltimore, a local server in Beverly Hills, and a remote database in Boston, without ever knowing from where the information has come. Indeed, even the local exchange carrier (LEC) that provides the connection from the researcher's home to the information service provider's local "point of presence" may be unable to determine whether any of the information that it is carrying to the subscriber originated outside the state.²¹

19. At the time the Communications Act was adopted, approximately 98% of all telephone calls originated and terminated within the same state. KELLOGG ET AL., *supra* note 6, § 2.6. Even today, 85% of all basic voice calls originate and terminate within the same jurisdiction. See FCC, INDUSTRY ANALYSIS DIV., TRENDS IN TELEPHONE SERVICE 26 (1994).

20. The FCC has defined enhanced services as:
services, offered over common carrier transmission facilities used in interstate communications, which employ computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information; provide the subscriber additional, different, or restructured information; or involve subscriber interaction with stored information.

47 C.F.R. § 64.702(a) (1994).

21. *But see infra* text accompanying notes 226-31 (discussing the effect of advanced intelligent network technology on the ability to determine the jurisdictional nature of a

2. When is FCC Preemption Permissible?

The location of the border between the interstate and the intrastate jurisdictions is not the only point of contention between the two sides. Regulation of jointly used facilities (or the services provided over them) by state regulatory authorities can significantly affect the FCC's ability to advance its policy goals. For example, a state policy preventing residents from interconnecting user-provided terminal equipment to the telephone network in order to place intrastate telephone calls is likely to impair federal policies allowing the use of such equipment for interstate calls.²² Similarly, a state policy requiring the use of the "whole life" method for depreciating the "intrastate component" of LECs' central office equipment in order to keep local telephone rates low is likely to frustrate federal policies that seek to promote network modernization by requiring the use of accelerated depreciation for the "interstate component" of that equipment.²³ And a state policy requiring common carriers to provide jurisdictionally intrastate enhanced services using separate facilities and personnel is likely to undermine the federal policy promoting the provision of jurisdictionally interstate basic and enhanced services on an integrated basis.²⁴

B. *The Early FCC Victories (1974-1982)*

The opening salvo in the federal-state conflict was fired by North Carolina.²⁵ The issue was whether telephone subscribers should have the right to attach user-provided CPE to the interstate telephone network, rather than being required to use equipment provided by the carrier. After years of litigation, the FCC concluded that subscribers should have this right.²⁶ In 1974, however, the North Carolina Public Utilities Commission (NCUC) announced its intention to prohibit the attachment of user-provided CPE to

telecommunications service).

22. See *infra* text accompanying notes 26-33.

23. See *infra* text accompanying notes 48-51.

24. See *infra* text accompanying notes 57-66.

25. For a more detailed review of the history of the federal-state dispute, see generally McKenna, *supra* note 6, at 20-52 (reviewing cases prior to 1986) and Michael J. Zpevak, *FCC Preemption After Louisiana PSC*, 45 FED. COMM. L.J. 185, 190-205 (1991) (reviewing cases from 1986 to 1990).

26. See *In re Use of the Carterfone Device in Message Toll Tel. Serv. v. AT&T, Decision*, 13 F.C.C.2d 420, *reconsideration denied, Memorandum Opinion and Order*, 13 F.C.C.2d 571 (1968); see also *Hush-A-Phone Corp. v. United States*, 238 F.2d 266, 269 (D.C. Cir. 1956) ("[A subscriber has a right to] use his telephone in ways which are privately beneficial without being publicly detrimental.").

the telephone network—unless the equipment was to be used *exclusively* for interstate calls. The FCC promptly responded, issuing an order preempting state restrictions on interconnection.²⁷

North Carolina challenged the preemption order in the Fourth Circuit. The state argued that the FCC had exceeded its authority under Section 2(b)(1) of the Communications Act which, on its face, deprives the FCC of jurisdiction over carrier-provided intrastate communications services and facilities.²⁸ If necessary, North Carolina suggested, subscribers could be required to purchase two pieces of CPE (and two transmission lines) one for interstate calls, and one for intrastate calls.

The Fourth Circuit was not persuaded. Deferring to the FCC's findings, the court observed that "[u]sually it is not feasible, as a matter of economics and practicality of operation, to limit the use of such equipment to either interstate or intrastate transmission."²⁹ Therefore, the court continued, the "practical effect" of the proposed North Carolina regulation would be to prohibit the attachment of customer-provided CPE to the interstate network, thereby preventing subscribers from exercising their federal right of interconnection.³⁰ The FCC, the court concluded, had the authority to preempt the state regulations in order to avoid being "frustrated in the exercise of that plenary jurisdiction over the rendition of interstate and foreign communication services that the Act has conferred upon it."³¹ The Fourth Circuit reaffirmed these conclusions the following year.³²

Shortly thereafter, California tried a different tack. Rather than challenging the authority of the FCC to enter state "territory" through the exercise of its preemption power, California simply tried to move the border. The precipitating event was a 1975 order in which the FCC directed the pre-divestiture Bell System to allow Southern Pacific Communications Company (the predecessor of Sprint Communications) to interconnect certain specialized facilities—which were capable of being used for both interstate and intrastate communications—to the Bell System's monopoly local exchange facilities.³³ California challenged the order, arguing that the

27. See *In re Telerent Leasing Corp.*, *Memorandum Opinion and Order*, 45 F.C.C.2d 204 (1974), *aff'd sub nom.* North Carolina Util. Comm'n v. FCC, 537 F.2d 787, 791 (4th Cir.) [hereinafter *NCUC I*], *cert. denied*, 429 U.S. 1027 (1976).

28. For the statutory language of Section 2(b)(1), see *supra* text accompanying note 12.

29. *NCUC I*, 537 F.2d at 791.

30. *Id.* at 793.

31. *Id.*

32. See *NCUC II*, 552 F.2d 1036 (4th Cir.), *cert. denied*, 434 U.S. 874 (1977).

33. See *In re AT&T*, *Memorandum Opinion and Order*, 56 F.C.C.2d 14 (1975) [hereinafter *AT&T Order*]. The specific facilities at issue were foreign exchange lines (which permit a subscriber to offer callers in a remote city the ability to access the

FCC lacked jurisdiction over the local exchange facilities because they were physically located within individual states.

In *California v. FCC*,³⁴ the Court of Appeals for the D.C. Circuit rejected this argument. "Even though . . . facilities are located entirely within single states," the court declared, "the physical location . . . is not determinative of whether they are interstate or intrastate for regulatory purposes. . . . [T]he key issue . . . is the nature of the communications which pass through the facilities"³⁵ Because the Bell System's local exchange facilities were used (at least in part) to support interstate calls, the FCC had the authority to mandate interconnection. In the following years, this principle was reaffirmed in a number of cases,³⁶ culminating in *National Ass'n of Regulatory Utility Commissioners v. FCC (NARUC II)*³⁷ in which the the Court of Appeals for the D.C. Circuit stated unequivocally that physically "intrastate facilities and services used to complete even a single interstate call may become subject to the FCC regulation to the extent of their interstate use."³⁸

subscriber by dialing a local telephone number) and common control switching arrangement service (which allows private line network users to dial "off-net" telephone subscribers through interconnection with the local exchange).

34. *California*, 567 F.2d 84 (D.C. Cir. 1977) (per curiam), cert. denied, 434 U.S. 1010 (1978).

35. *Id.* at 86 (quoting *AT&T Order*, supra note 33, paras. 20, 22).

36. See, e.g., *New York Tel. Co. v. FCC*, 631 F.2d 1059, 1065-66 (2d Cir. 1980) (interstate access service subject to FCC regulation).

37. *National Ass'n of Regulatory Util. Comm'rs*, 746 F.2d 1492 (D.C. Cir. 1984) [hereinafter *NARUC II*].

38. *Id.* at 1498. In *NARUC II*, the D.C. Circuit held that physically intrastate wide area telephone service (WATS) lines used to complete interstate calls were subject to federal regulation. *Id.* at 1501; cf. *Southwestern Cable v. FCC*, 392 U.S. 157 (1968) (the FCC's jurisdiction over interstate communications extends to a physically intrastate California cable television system that picked up out-of-state broadcast signals from a station in Los Angeles and carried them by cable or microwave to subscribers in San Diego); *General Tel. v. FCC*, 413 F.2d 390 (D.C. Cir.), cert. denied, 396 U.S. 888 (1969) (the FCC's interstate jurisdiction extends to physically intrastate telephone company "channel service" used to deliver broadcast signals that originate out-of-state).

One case decided during this period, *McDonnell Douglas Corp. v. General Tel. Co.*, 594 F.2d 720 (9th Cir.), cert. denied, 444 U.S. 839 (1979), is sometimes said to have reached a contrary result. That case concerned jurisdiction over a basic communications service, Centrex, that General Telephone provided to its customer, McDonnell Douglas, using facilities entirely within California. Centrex is a network-based service which allows a multi-line customer to make intra-office calls as if it had a premises-based switch.

In an often-quoted passage, the Ninth Circuit observed that the service provided to McDonnell Douglas was not subject to FCC jurisdiction merely "because of the capacity it possesses to be patched into interstate telecommunications nets." *Id.* at 724 n.3. Read in isolation, this language could be interpreted to mean that physically intrastate equipment is not subject to FCC jurisdiction even if used in connection with interstate calls. Such a construction, however, is inconsistent with the dispositive fact in the case: McDonnell

Emboldened by its early victories, the FCC went on the offensive. The Commission previously had determined that carriers could not *require* subscribers to use carrier-provided CPE.³⁹ In the *Second Computer Inquiry*⁴⁰ the FCC took the next step, declaring that the provision of CPE was not a common carrier service subject to regulation under Title II of the Communications Act⁴¹ and, therefore, that telephone companies would not

Douglas used its Centrex service *exclusively* for intrastate calls. *See id.* There was, therefore, no basis for federal jurisdiction in that case. Had McDonnell Douglas used its Centrex service in connection with interstate calls, a different case would have been presented: the service would have been subject to FCC regulation "to the extent of [its] interstate use." *California II*, 4 F.3d 1505, 1515 (9th Cir. 1993) ("[T]he service that General Telephone . . . provided to McDonnell Douglas . . . was solely intrastate."); *see NARUC II*, 746 F.2d at 1498; *see also* Illinois Bell Tel. Co. v. FCC, 883 F.2d 104, 113 (D.C. Cir. 1989) (quoting Furnishing of Customer Premises Equip. by the Bell Operating Tel. Cos. and the Indep. Tel. Cos., *Report and Order*, 2 FCC Rcd. 143, para. 123 (1987)) (finding Centrex service to be jurisdictionally mixed because it usually is used to "support[] both interstate and intrastate communications").

39. *See supra* text accompanying note 26.

40. *In re* Amendment of § 64.702 of the Commission's Rules and Regs. (Second Computer Inquiry), *Final Decision*, 77 F.C.C.2d 384 [hereinafter *Computer II Final Decision*], *modified by Memorandum and Order*, 84 F.C.C.2d 50 (1980) [hereinafter *Computer II Reconsideration Order*], *aff'd and clarified by Memorandum Opinion and Order on Further Reconsideration*, 88 F.C.C.2d 512 (1981) [hereinafter *Computer II Further Reconsideration Order*], *aff'd sub nom. CCLA*, 693 F.2d 198 (D.C. Cir. 1982), *cert. denied*, 461 U.S. 938 (1983), *aff'd on second further reconsideration, Memorandum Opinion and Order*, 56 Rad. Reg. 2d (P & F) 301 (1984).

41. *See Computer II Final Decision, supra* note 40, paras. 122-32, 168-73. The question of when an entity is acting as a common carrier has received considerable attention in the courts. The Communications Act does not provide a clear definition of the term "common carrier." *See* 47 U.S.C. § 153(h) (1988) (defining a common carrier as "any person engaged as a common carrier for hire"). In *NARUC I*, however, the D.C. Circuit concluded that an entity is engaging in common carriage if it "undertakes to carry for all people indifferently." *National Ass'n of Regulatory Util. Comm'rs v. FCC*, 525 F.2d 630, 641 (D.C. Cir.) [hereinafter *NARUC I*], *cert. denied sub. nom. National Ass'n of Radiotelephone Sys. v. FCC*, 425 U.S. 942 (1976) (quoting *Semon v. Royal Indem. Co.*, 279 F.2d 737, 739 (5th Cir. 1960)). In other words, an entity acts as a common carrier when it serves the public on standardized terms, rather than entering into individualized contracts. *See id.* An entity's obligation to serve the public indifferently can arise from either of two sources: a business decision to "hold itself out" as providing service in this matter *or* from a government-imposed obligation to do so. *See id.* at 643-44.

If an entity provides a service on a common carrier basis, that service is subject to regulation under Title II of the Communications Act. Title II imposes a number of obligations. For example, an interstate common carrier must: (1) provide service on reasonable request, 47 U.S.C. § 201(a) (1988); (2) charge rates that are just and reasonable, 47 U.S.C. § 201(b) (1988); (3) not discriminate among customers, 47 U.S.C. § 202 (1988); (4) file and comply with public tariffs governing the terms and conditions on which it provides service, 47 U.S.C. § 203(a) (1988); and (5) obtain FCC approval before constructing new facilities or discontinuing existing services, 47 U.S.C. § 214(a) (1988).

An entity can act as a common carrier for some purposes but not for others. For example, a telephone company is acting as a common carrier when it provides interstate

be *allowed* to offer CPE as part of their regulated interstate transmission service.⁴² Rather, carriers were to offer CPE on a "private contract" basis. The Commission further determined that imposition of common-carrier-type regulation by the states would undermine the FCC's policy of promoting a competitive CPE market. Acting pursuant to its "ancillary authority" under Title I of the Communications Act,⁴³ the FCC preempted all such state regulation.⁴⁴

This decision was upheld by the Court of Appeals for the D.C. Circuit in *Computer & Communications Industry Ass'n v. FCC (CCIA)*.⁴⁵ As in the *NCUC* cases, the court deferred to the FCC's finding that because "consumers use the same CPE in both interstate and intrastate communications and generally wish to purchase both interstate and intrastate transmission services,"⁴⁶ a state policy requiring tariffing of CPE used for intrastate calls could not feasibly coexist with the federal policy requiring the detariffing of CPE. "The conflicting state policy," the court stated, "would unavoidably affect the federal policy adversely. Therefore, here, as in *NCUC I* and *II*, the state regulatory power must yield to the federal."⁴⁷

basic transmission service; it is not acting as a common carrier when it provides enhanced services. See *CCIA*, 693 F.2d at 210. Non-common carrier services—such as the provision of CPE, inside wiring, and enhanced services—also can be provided by entities other than traditional telephone companies. For a discussion of the FCC's jurisdiction over non-carrier-provided services, see *infra* part III.D.

42. *Computer II Final Decision*, *supra* note 40, paras. 8-10.

43. The Supreme Court has held that Title I gives the FCC authority to take "all regulatory actions 'necessary to ensure the achievement of the Commission's statutory responsibilities.'" *Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 700 (1984) (quoting *FCC v. Midwest Video Corp.*, 440 U.S. 689, 706 (1979)). This includes the FCC's responsibility 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." 47 U.S.C. § 151 (1988). Thus, Title I gives the FCC "ancillary" interstate jurisdiction over "those activities and forms of communication that are [not] specifically described by the Act's other provisions." *United States v. Southwestern Cable Co.*, 392 U.S. 157, 172 (1968).

44. See *Computer II Further Reconsideration Order*, *supra* note 40, paras. 33-35, 85; *Computer II Reconsideration Order*, *supra* note 40, para. 155. The FCC also preempted all state regulation of enhanced services. *Computer II Further Reconsideration Order*, *supra* note 40, para. 34 ("[The] efficient utilization and full exploitation of the interstate telecommunications network would best be achieved if [enhanced] services are free from public utility-type regulation."). That decision was not challenged on appeal.

45. *CCIA*, 693 F.2d at 198.

46. *Id.* at 215.

47. *Id.* at 216.

C. *The FCC Overreaches (1982-86)*

In the years that followed, the Commission launched a broad-based attack on state authority. Between 1982 and 1986, the FCC preempted state regulation of telephone company equipment depreciation rates, inside wiring, and enhanced services.

1. Depreciation

The first wave of the FCC attack came in the area of depreciation. Between 1980 and 1983, the FCC issued a series of orders designed to increase the speed with which the cost of regulated telephone company equipment would be "written off" and new equipment deployed.⁴⁸ "Adequate capital recovery," the FCC contended, was necessary to achieve the goal—specified in Title I of the Communications Act—of "mak[ing] available . . . a rapid, efficient . . . communication service."⁴⁹ The Commission therefore required carriers to use a form of accelerated depreciation to recover the cost of the interstate component of their regulated plant.⁵⁰ The FCC also preempted state regulations that required

48. See *In re* Amendment of Part 31 (Expensing of Station Connections), *First Report and Order*, 85 F.C.C.2d 818 (1981) [hereinafter *Part 31 Order*], clarified by *Memorandum Opinion and Order*, 89 F.C.C.2d 1094 (1982), petition for reconsideration dismissed, 89 F.C.C.2d 1094 (1982) [hereinafter *Part 31 Memorandum Opinion & Order*], petition for reconsideration granted and petition for declaration ruling granted by *Memorandum Opinion and Order*, 92 F.C.C.2d 864 (1983) [hereinafter *Part 31 Further Reconsideration Order*]; *In re* Amendment of Part 31 of the Commission's Rules (Property Depreciation), *Report and Order*, 83 F.C.C.2d 267 (1980), petition for reconsideration denied by *Order on Reconsideration*, 87 F.C.C.2d 916 (1981).

49. *Part 31 Further Reconsideration Order*, *supra* note 48, para. 33 (quoting 47 U.S.C. § 151 (1988)).

50. As early as 1930, the Supreme Court recognized that the cost of the local telephone plant jointly used for interstate and intrastate calls should be allocated between the federal and state jurisdictions. See *Smith v. Illinois Bell Tel.*, 282 U.S. 133 (1930). To effectuate this policy, the FCC has adopted regulations that govern the method by which such costs are allocated.

Because some telephone company plant is used to provide both regulated basic telephone service and non-regulated service (such as enhanced services), it is first necessary to allocate costs between the carrier's regulated and non-regulated accounts. This process is governed by the FCC's *Joint Cost Order*. See *In re* Separation of Costs of Regulated Telephone Service From Costs of Nonregulated Activities, *Report and Order*, 2 FCC Rcd. 1298, reconsidered, 2 FCC Rcd. 6283 (1987), further reconsideration, 3 FCC Rcd. 6701 (1988). Under FCC rules, those costs related to telephone company plant subject to Title II regulation are then subject to the jurisdictional separations process. See Letter from Kenneth P. Moran, Chief, Accounting and Audits Div., to Responsible Accounting Officers, 5 FCC Rcd. 5947 (1990) [hereinafter *RAO Letter 16*].

The jurisdictional separations process is governed by Part 36 of the Commission's Rules. See *Jurisdictional Separations Procedures*, 47 C.F.R. § 36 (1993); see also *In re*

use of a different method of depreciating the intrastate component of regulated telephone company equipment. The FCC reasoned that Section 2(b)(1) did not stand as a bar to exercise of its preemptive authority because “[s]tate depreciation rate prescriptions that do not adequately provide for capital recovery in the competitive environment . . . would frustrate the accomplishment of [the FCC’s] policy.”⁵¹

2. Inside Wiring

The Commission also sought to wrest control of the regulation of inside wiring from the states. Historically, the provision of inside wiring had been treated as a regulated common carrier activity. In 1986, however, the FCC directed that inside wiring be unbundled from the carriers’ transmission service and offered on a non-regulated, private contract basis.⁵² As it had done with CPE, the Commission also preempted the states from regulating inside wiring.⁵³

The FCC stated that Section 2(b)(1) did not prevent it from displacing state inside wiring regulations. That provision, the FCC observed, deprived the Commission of jurisdiction over “charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio *of any carrier*.”⁵⁴ Because it had determined that the provision of inside wiring is not *common carriage*, the FCC reasoned, Section 2(b)(1) did not limit its power to preempt state regulation.⁵⁵ The FCC further reasoned that—even if Section 2(b)(1) were applicable—federal preemption was permissible because “a federal program of competitive, deregulated provision of inside wiring cannot coexist with a state system providing for regulated carrier provision of inside wiring

Prescription of Procedures for Separating and Allocating Plant Investment, Operating Expenses, Taxes and Reserves Between the Intrastate and the Interstate Operations of Tel. Companies, *Report and Order*, 16 F.C.C.2d 317, para. 40 (1969). The FCC has exclusive authority to establish the procedure governing this process. *See Hawaiian Tel. Co. v. Public Util. Comm’n*, 827 F.2d 1264, 1277-78 (9th Cir. 1987), *cert. denied*, 487 U.S. 1218 (1988). *See generally In re Policy and Rules Concerning Rates for Dominant Carriers, Notice of Proposed Rulemaking*, 2 FCC Rcd. 5208, paras. 8-12 (1987) (describing the allocation and separations processes).

51. *Part 31 Further Reconsideration Order*, *supra* note 48, para. 31.

52. *See Detariffing the Installation and Maintenance of Inside Wiring, Final Rule*, 51 Fed. Reg. 8498, 59 Rad. Reg. 2d (P & F) 1143 [hereinafter *Inside Wiring Detariffing Order*], *petition for reconsideration granted by Memorandum Opinion and Order*, 1 FCC Rcd. 1190 (1986) [hereinafter *Inside Wiring Detariffing Reconsideration Order*].

53. *Inside Wiring Detariffing Reconsideration Order*, *supra* note 52, para. 13.

54. *Id.* para. 14.

55. *Id.* para. 16.

absent a requirement that consumers obtain two systems of inside wiring."⁵⁶

3. Enhanced Services

The FCC's most ambitious offensive against state jurisdiction came in the area of enhanced services. Under rules adopted during the *Second Computer Inquiry*, and modified following AT&T divestiture,⁵⁷ the Bell Operating Companies (BOCs) were required to provide interstate enhanced services on a non-regulated basis using corporate affiliates that were structurally separate from the carriers' basic transmission service operations.⁵⁸ The structural separation requirement was intended to prevent the BOCs from leveraging their monopoly control over the local exchange to obtain a competitive advantage in the emerging enhanced services market.⁵⁹

The FCC's commitment to structural separation was not long-lived. In *Third Computer Inquiry*, the FCC announced that it had concluded that the cost of structural separation resulting from the reduction of carrier efficiency outweighed the benefits resulting from the reduced risk of BOC anticompetitive conduct.⁶⁰ The FCC therefore replaced structural separa-

56. *Id.* para. 18.

57. Under the terms of the Modification of Final Judgment, AT&T was required to give up its local exchange operations. *See* *United States v. AT&T Co.*, 552 F. Supp. 131, 141-42 (D.D.C. 1982), *aff'd sub nom.*, *Maryland v. United States*, 460 U.S. 1001 (1983). On January 1, 1984, the seven Regional Bell Operating Companies assumed control of these facilities.

58. Under structural separation, AT&T's separate affiliate was required to have separate facilities, personnel, accounts, and corporate identity from the carrier's basic transmission service operations. *See Computer II Further Reconsideration Order*, *supra* note 40, para. 83 n.34; *Computer II Final Decision*, *supra* note 40, para. 191. The FCC issued rules applying structural separation to the BOCs upon their divestiture. *See In re Policy and Rules Concerning the Furnishing of Customer Premises Equip., Enhanced Servs., and Cellular Comms. Servs. by the Bell Operating Cos., Report and Order*, 95 F.C.C.2d 1117 (1983) [hereinafter *BOC Separation Order*], *aff'd sub nom. Illinois Bell Tel. & Tel. Co. v. FCC*, 740 F.2d 465 (7th Cir. 1984), *aff'd denial of petitions for reconsideration*, 49 Fed. Reg. 26,056 (1984), 56 Rad. Reg. 2d (P & F) 581, *aff'd sub nom. North Am. Tel. Ass'n v. FCC*, 772 F.2d 1282 (7th Cir. 1985).

59. There are at least two ways in which the BOCs could do so. First, a BOC could cross-subsidize its own enhanced service offerings with revenues from its monopoly local exchange service—thereby allowing it to “under sell” non-affiliated enhanced service providers (ESPs), who lack access to monopoly revenues necessary for cross-subsidization. Second, a BOC could discriminate in the provision of local exchange service against non-carrier-affiliated ESPs, who rely on the BOCs' underlying transport services to deliver their offerings to end-users. *See BOC Separation Order*, *supra* note 58, paras. 25-47.

60. *In re Amendment of § 64.702 of the Commission's Rules and Regs. (Third Computer Inquiry)*, *Report and Order*, 104 F.C.C.2d 958, para. 348 (1986) [hereinafter *Computer III Phase I Order*], *petition for reconsideration denied by Memorandum Opinion*

tion with a regime under which the BOCs may integrate their interstate basic and enhanced service operations, subject to certain nonstructural safeguards.⁶¹ The nonstructural safeguards included a requirement that the BOCs disclose to enhanced service providers (ESPs) information necessary to achieve interconnection with the carriers' basic transmission network (the network disclosure rule). Such disclosure was to be made at least six months before a BOC's introduction of an enhanced service that uses a network interface that had not been previously disclosed.⁶² The nonstructural safeguards also required the BOCs to allow ESPs to have access to certain information regarding customers' use of the basic transmission network that could be useful in developing and marketing enhanced services (the customer proprietary network information (CPNI) rule).⁶³

Once again, the FCC wielded its preemption sword. The *Computer III Phase I Order* preempted all state structural separation requirements and any state nonstructural safeguards that were in addition to or different from the federal nonstructural safeguards.⁶⁴ The order also preempted all forms of state enhanced service tariff regulation.⁶⁵ The order did not so much as mention Section 2(b)(1).⁶⁶

and Order on Reconsideration, 2 FCC Rcd. 3035 (1987) [hereinafter *Computer III Phase I Reconsideration Order*], *reaff'd and clarified by Memorandum Opinion and Order on Further Reconsideration*, 3 FCC Rcd. 1135 (1988), *reaff'd by Memorandum Opinion and Order on Further Reconsideration and Second Further Reconsideration*, 4 FCC Rcd. 5927 (1989); *Computer III Phase I Order and Computer III Reconsideration Order vacated sub nom. California v. FCC*, 905 F.2d 1217 (9th Cir. 1990) [hereinafter *California I*]; *In re Amendment of § 64.702 of the Commission's Rules and Regs., Report and Order*, 2 FCC Rcd. 3072 (1987) [hereinafter *Computer III Phase II Report & Order*], *aff'd and clarified by Memorandum Opinion and Order on Reconsideration*, 3 FCC Rcd. 1150 (1988) [hereinafter *Computer III Phase II Reconsideration Order*], *reaff'd by Memorandum Opinion and Order on Further Reconsideration and Second Further Reconsideration*, 4 FCC Rcd. 5927 (1989) [hereinafter *Computer III Phase II Further Reconsideration Order*]; *Computer III Phase II Report & Order vacated sub nom. California I*, 905 F.2d 1217 (9th Cir. 1990).

61. See *Computer III Phase I Order*, *supra* note 60, paras. 345-53.

62. *Id.* paras. 252-54.

63. *Id.* paras. 260-62. The *Computer III* orders also replaced the requirement that AT&T provide enhanced services on a structurally separate basis with a modified form of nonstructural safeguards. See *Computer III Phase I Reconsideration Order*, *supra* note 60, paras. 45-53 (discussing the difference between AT&T and the BOCs that justified different regulatory treatment).

64. *Computer III Phase I Order*, *supra* note 60, paras. 347-48; *Computer III Phase I Reconsideration Order*, *supra* note 60, paras. 182-90.

65. See *Computer III Phase I Order*, *supra* note 60, paras. 343-48.

66. The FCC reaffirmed its preemption order in the *Computer III Phase I Reconsideration Order*, *supra* note 60, paras. 198-210, rejecting arguments that it had exceeded its authority under § 2(b)(1).

D. *The States Counter-Attack (1986-90)*

By 1985, the FCC *blitzkrieg* seemed unstoppable. In a landmark article on FCC preemption published that year, Bob McKenna observed that he was “unable to visualize any likely regulatory question or legal issue of any importance affecting telephone companies” where the FCC could not exercise preemption power.⁶⁷ All the FCC need do, he concluded, was to make a “plausible case” that a state rule “substantially affects” the FCC’s exercise of its authority.⁶⁸

Just one year later, however, the tide began to turn. As a result of a series of judicial victories between 1986 and 1990, the states were able to use Section 2(b)(1) to repulse each of the federal incursions into their territory.

1. *Louisiana*

The states’ first, and perhaps most dramatic, victory came in *Louisiana Public Service Commission v. FCC (Louisiana)*.⁶⁹ By a 5 to 2 majority, the Supreme Court struck down the FCC’s order preempting states from adopting depreciation methods for the intrastate component of telephone company equipment that differed from the method that the FCC prescribed for the interstate component of that equipment.⁷⁰ Section 2(b)(1) of the Communications Act, the Court declared, “fences off from FCC reach or regulation intrastate matters.”⁷¹ The FCC did not have the right to stray across that jurisdictional fence—even if it did so to promote the Title I goal of “the creation of a rapid and efficient telephone service.”⁷²

The FCC’s trespass, the Court went on, was not unavoidable. The jurisdictional separations process provided a ready means to facilitate the application of different depreciation methodologies within the interstate and intrastate jurisdictions.⁷³ Therefore, the Court concluded, the FCC must allow the states to apply their own depreciation methodology to the intrastate component of the telephone company plant.

67. McKenna, *supra* note 6, at 59.

68. *Id.* at 59, 62.

69. *Louisiana*, 476 U.S. 355 (1986).

70. *See id.* at 373.

71. *Id.* at 370.

72. *Id.*

73. *Id.* at 375. For a description of the jurisdictional separations process, see *supra* note 50 and accompanying text.

2. *NARUC III*

Rallied by their victory in *Louisiana*, the states went on the offensive.⁷⁴ Their next target was the FCC's decision to preempt all state regulation of inside wiring. Their efforts met success in 1989, when the Court of Appeals for the D.C. Circuit issued a decision that has come to be known as *NARUC III*.⁷⁵

The court rejected the FCC's contention that, because it had determined that the provision of inside wiring did not constitute regulated common carriage at the *interstate* level, the Section 2(b)(1) limit on FCC regulation of common carrier activity at the *intrastate* level did not apply. Such "circular" reasoning, the court chided, would give the FCC "unchecked authority to force state deregulation of any activity it chose to deregulate at the interstate level."⁷⁶ The court further rejected the FCC's argument that, even under Section 2(b)(1), preemption was permissible because the interstate and intrastate components of inside wiring are physically inseparable. As in *Louisiana*, the court concluded, the FCC could use the jurisdictional separations process to preserve a sphere for state regulation.⁷⁷

NARUC III raised considerable concern about the continued validity of *CCLIA*, which had upheld FCC preemption of all state regulation of CPE. CPE and inside wiring are conceptually indistinguishable: both facilities are physically located on a customer's premises and are used in connection with interstate and intrastate calls. If the FCC could not adopt a generalized order preempting all state regulation of inside wiring, how could it adopt

74. Soon after *Louisiana*, the states scored a small, but noteworthy, victory in the *FM Subcarrier Case*, *California v. FCC*, 798 F.2d 1515 (D.C. Cir. 1986). Historically, the FCC had been assumed to have exclusive jurisdiction over all forms of radio-based (as opposed to wireline) communications. This assumption was based on the words of § 301 of the Communications Act, which gives the FCC authority to "maintain the control of the United States over all the channels of radio transmission." 47 U.S.C. § 301 (Supp. V 1993). It is on this basis that the FCC has exercised exclusive authority over the regulation of broadcast television and radio. See *FCC v. Pottsville Brdcast. Co.*, 309 U.S. 134, 137 (1940) (noting that the Communications Act creates a "unified and comprehensive" system of federal broadcast regulation). In the *FM Subcarrier Case*, however, the D.C. Circuit held that § 2(b)(1) deprived the FCC of jurisdiction over the intrastate radio transmissions that are used to provide common carrier services, such as radio paging. See *California*, 798 F.2d at 1518-20.

75. *National Ass'n of Regulatory Util. Comm'rs v. FCC*, 880 F.2d 422 (D.C. Cir. 1989) [hereinafter *NARUC III*].

76. *Id.* at 429.

77. *Id.* at 428.

such an order regarding CPE? The court's effort to rationalize the disparate results was unavailing.⁷⁸

3. *California I*

The low point came for the FCC a year later when the Ninth Circuit, in *California v. FCC (California I)*,⁷⁹ struck down the FCC's principal *Computer III* orders.⁸⁰ *California I* was a double defeat for the FCC. The court first rejected the FCC's decision to replace structural separation with nonstructural safeguards at the interstate level,⁸¹ finding that the FCC had failed to demonstrate that nonstructural safeguards were adequate to reduce the risk of BOC anticompetitive conduct.⁸² The court then turned to the FCC's decision to preempt the states from adopting additional or different regulations at the intrastate level. Following the D.C. Circuit's lead, the court rejected the FCC's assertion that Section 2(b)(1) did not limit the Commission's ability to preempt state regulation of enhanced services because such services were provided on a private contract, rather than a common carriage, basis.⁸³ The court noted that the restriction on FCC regulation applied to "intrastate communication service . . . of any carrier." The court reasoned:

the plain meaning of the language "of any carrier" is that [Section 2(b)(1)] applies to communications services provided by common carriers such as AT&T and the BOCs as distinguished from communications services provided by non-common carriers such as IBM. Thus, the distinction made by the statute is between *providers* of communications services, i.e., between carriers and non-carriers.⁸⁴

Applying Section 2(b)(1), the court went on to strike down the *Computer III* preemption orders in their entirety.⁸⁵

78. The court reasoned that, in *CCLIA*, the FCC had made an adequate showing that preemptively detariffing CPE was necessary to advance the FCC's goal of "developing a free, competitive market in customer telephone equipment." *Id.* at 431. Here, in contrast, the court suggested that merely unbundling inside wiring from transmission service would be sufficient to create "a free and competitive inside wiring market because it would allow customers . . . to forgo the telephone company's charges for inside wiring and to seek an alternative provider." *Id.* at 430. However, the court did not attempt to explain why, if unbundling was adequate to promote competition in the inside wiring market, it was inadequate to create competition in the CPE market.

79. *California I*, 905 F.2d 1217 (9th Cir. 1990).

80. *See supra* text accompanying notes 60-66.

81. The challenge to the decision to lift structural separation was brought by the MCI Telecommunications Company, the nation's second largest interexchange service provider.

82. *California I*, 905 F.2d at 1230-39.

83. *See id.* at 1240.

84. *Id.* (emphasis in original).

85. *Id.* at 1243.

4. The Casualty Count

In a few short years, the FCC's jurisdictional gains had seemingly evaporated. In a thought-provoking article written in the early 1990s, Michael Zpevak concluded that the FCC's preemption powers had been "whittled down to their statutory base" and, perhaps, even "emasculated."⁸⁶ Indeed, Zpevak suggested, it was "unclear . . . how the FCC will continue to set *national* policy . . . while not intruding on *state* territory."⁸⁷

Rumors of the demise of the FCC's preemption authority were premature. To be sure, *Louisiana*, *NARUC III*, and *California I* were stunning blows to the FCC's once-invincible preemption *wehrmacht*. Yet, none of these was an unmitigated loss.

Despite the sweeping language in *Louisiana*, the actual holding was carefully limited to the specific situation before the Supreme Court. The jurisdictional separations process, the Court held, made it possible for disparate federal and state depreciation policies to coexist.⁸⁸ The FCC might not be able to allow carriers to recover costs as quickly as it wished, but it could require application of its chosen depreciation methodology to the interstate component of the carriers' equipment.⁸⁹ Preemption, therefore, was impermissible.

At the same time, the Court recognized that the separations process did not resolve all jurisdictional conflicts. Where it is "*not* possible to separate the intrastate and interstate components of asserted federal regulation" and where "state regulation would negate" FCC regulations, the Court observed, FCC preemption is permissible.⁹⁰ In formulating this so-called "impossibility" exception to Section 2(b)(1), the Court cited with approval the Fourth Circuit's decisions in the *NCUC* cases.⁹¹

Similarly, the D.C. Circuit's opinion in *NARUC III* had some encouraging words for the beleaguered Commission. Relying on *Louisiana*

86. Zpevak, *supra* note 25, at 186.

87. *Id.* (emphasis in original); see also Pierce, *Panic at the Helm*, NETWORK WORLD, July 23, 1990, at 26 (stating that the *California I* decision had "devastated" the FCC and "set the telecommunications and information industry on a course for catastrophe"). Some observers were more sanguine. See, e.g., J. Roger Wollenberg, Roger M. Witten, & Jonathan Jacob Nadler, *California v. FCC: After the Earthquake, Life Goes On*, COMPUTER LAW., Aug. 1990, at 25 (concluding that, while *California I* was a serious "jolt," there was "no reason to conclude that the Commission's preemption power ha[d] been reduced to rubble").

88. *Louisiana*, 476 U.S. 355 (1986).

89. *Id.* at 376.

90. *Id.* at 375 n.4 (emphasis in original).

91. See *supra* notes 29-32 and accompanying text.

and the *NCUC* cases, the court observed that “there are circumstances where state authority must yield to national imperatives.”⁹² Thus, the court went on, the FCC could preempt state regulations that would “negate[] the exercise by the FCC of its own lawful authority over interstate communications.”⁹³ However, the court added, the FCC “has the burden . . . of showing with some specificity” that a particular state regulation would “necessarily thwart or impede” federal policy.⁹⁴ The FCC had simply failed to meet its burden necessary to preempt exercise of “any regulatory authority” by the states over inside wiring.⁹⁵

The court’s observations regarding tariffing of inside wiring were particularly interesting. The court recognized that a state that set the tariffed rates for the intrastate component of carrier-provided inside wiring below cost would “interfere with the Commission’s achievement of its valid goal of providing interstate telephone users with the benefits of a free market . . . [in] inside wiring” because this would “allow telephone companies to undercut alternative providers,” who lacked the ability to cross-subsidize inside wiring with revenues from monopoly local exchange service.⁹⁶ The FCC, the court indicated, could lawfully preempt such tariffs.⁹⁷

Even *California I* provided the FCC with some basis for optimism. Following the D.C. Circuit’s lead, the Ninth Circuit recognized that—notwithstanding Section 2(b)(1)—the FCC has the authority to preempt state regulation of carrier-provided enhanced services that would “thwart or impede valid FCC regulatory goals.”⁹⁸ For example, the court observed, “a state-imposed requirement that carriers use separate physical facilities for all basic telephone and enhanced services offered on an intrastate basis would almost certainly force carriers to separate their interstate services as well.”⁹⁹ Because this would “frustrate” the FCC’s efforts to promote the integration of interstate basic and enhanced services, the FCC could preempt such regulations.¹⁰⁰

At the same time, the court observed that some forms of state-imposed enhanced service regulation plainly would not “negate” federal

92. *NARUC III*, 880 F.2d 422, 429 (D.C. Cir. 1989).

93. *Id.*

94. *Id.* at 430.

95. *Id.* (emphasis in original). For example, the court noted, the states had argued that state-mandated provider-of-last-resort regulations “would not lead to the frustration of a free and competitive market.” *Id.*

96. *Id.*

97. *Id.*

98. *California I*, 905 F.2d 1217, 1243 (9th Cir. 1990).

99. *Id.* at 1244.

100. *Id.*

policy. The court's example, however, was a narrow one. State imposition of structural separation requirements on carrier-provided enhanced services (such as telephone-based alarm services) offered on an *exclusively* intrastate basis, the court stated, would not prevent carriers from offering other interstate enhanced services on an integrated basis.¹⁰¹ Once again, the FCC simply had failed to demonstrate why it was necessary to preempt "all state regulation" in order to achieve its goals.¹⁰²

5. Scattered Federal Victories

Even during this period, the FCC won three significant skirmishes outright. In each case, the D.C. Circuit held that state regulations had to give way to allow the application of the FCC's rules to interstate service.

In *Illinois Bell*,¹⁰³ the D.C. Circuit considered the FCC's preemption of state regulations that were inconsistent with the Commission's requirement that the BOCs allow noncarrier CPE vendors to obtain commissions for marketing Centrex, a BOC-provided basic service used in connection with both interstate and intrastate calls. The court held that there was no practical way to apply different federal and state sales commission rules depending on whether the Centrex service was to be used in connection with interstate or intrastate calls. Federal preemption of state rules that were inconsistent with the federal regulatory regime was, therefore, permissible.¹⁰⁴

The FCC also won a small, but significant, victory in *Public Utility Commission of Texas v. FCC (ARCO)*.¹⁰⁵ *ARCO* concerned an order by the Texas Public Utilities Commission that barred Southwestern Bell Telephone Company from providing one of its customers, Atlantic Richfield Company (ARCO), with additional telephone lines at ARCO's Dallas headquarters. Texas was concerned that ARCO was undermining the state's system of exclusive telephone franchises by transporting calls, via a private microwave system, from its research facility in Plano, Texas (which was served by a different LEC) and delivering them, via Southwestern's lines, to the public-switched telephone network in Dallas. The FCC preempted the Texas order, reasoning that it was inconsistent with the

101. *Id.*

102. *Id.* (emphasis in original).

103. *Illinois Bell Tel. Co. v. FCC*, 883 F.2d 104 (D.C. Cir. 1989).

104. *Id.* at 115. The court went so far as to suggest that "[e]ven if Centrex were a purely intrastate service, the FCC might well have authority to preemptively regulate its marketing if—as would appear here—it was typically sold in a package with interstate services. Marketing realities might themselves create inseparability." *Id.* at 113 n.7.

105. *Public Util. Comm'n of Texas*, 886 F.2d 1325 (D.C. Cir. 1989) [hereinafter *ARCO*].

FCC's policy of allowing customers to interconnect with the public-switched telephone network for the purposes of making interstate calls.¹⁰⁶

As in the *NCUC* cases, it would have been possible for the FCC to have required Southwestern to provide ARCO with two sets of facilities—lines to be used for intrastate calls and lines to be used for interstate calls—and to allow ARCO to interconnect its microwave system only with the interstate lines, thereby allowing federal interconnection and state franchise regulations to coexist. However, the court upheld the FCC's finding that such a requirement would be “impractical and inefficient” and that federal preemption was therefore permissible.¹⁰⁷

A third D.C. Circuit preemption case, *Public Service Commission of Maryland v. FCC (Maryland PSC)*, again upheld an FCC preemption order.¹⁰⁸ In that case, the D.C. Circuit affirmed an FCC order preempting states from setting the rates that LECs charged long distance carriers for cutting off service to customers that did not pay their long distance bills.¹⁰⁹ Once again, the court was confronted with the argument that it was possible for separate federal and state regulations to coexist because “it may be possible technologically to cut off interstate access independently of local service.”¹¹⁰ And, once again, the court deferred to the FCC, noting that “[a]t the time it issued [its order], the FCC believed that such a separation was not practical.”¹¹¹

E. *The FCC Retreats (1991)*

Although the losses in *Louisiana*, *NARUC III*, and *California I* may not have been as dramatic as they initially appeared, they left the FCC badly bruised. In response, the Commission initiated a strategic retreat on all fronts.

The FCC recognized immediately that the “depreciation battle” was a lost cause; the Supreme Court's decision in *Louisiana* had made clear that the states had an incontrovertible right to control the rates at which the intrastate component of common carrier plant was written off. The

106. See *In re Atlantic Richfield Co.*, *Memorandum Opinion and Order*, 3 FCC Rcd. 3089 (1988) [hereinafter *ARCO Order*].

107. *ARCO*, 886 F.2d at 1333 (quoting *ARCO Order*, *supra* note 106, para. 17).

108. *Public Serv. Comm'n of Maryland*, 909 F.2d 1510 (D.C. Cir. 1990) [hereinafter *Maryland PSC*].

109. The service, called Disconnect-Non-Payment (DNP) is a service sold by LECs to interexchange carriers in which the LEC cuts off both interstate and intrastate telephone service when the customer fails to pay its long distance bill.

110. *Maryland PSC*, 909 F.2d at 1516.

111. *Id.*

Commission responded by promptly evacuating from that region.¹¹² In the ensuing years, it has not attempted to venture across the jurisdictional border on this issue.

In contrast, the *NARUC III* and *California I* decisions left the Commission with a fair amount of maneuvering room in the inside wiring and enhanced services areas. Two orders, both adopted on November 21, 1991, signalled that the Commission intended to pull back to more defensible lines.¹¹³

1. Inside Wiring

The more comprehensive FCC pull-back came on the inside wiring front. The FCC returned most of the intrastate regulatory territory it had occupied, leaving only a "strategic outpost" and a "reconnaissance team."

The outpost was an order preempting the states from requiring carriers to bundle inside wiring with charges for tariffed transmission service.¹¹⁴ There was no question the FCC could defend this limited incursion; the D.C. Circuit had expressly authorized it in the *NARUC III* opinion.¹¹⁵ The reconnaissance operation was the Commission's idea. It announced that it would "monitor the states's actions" and "revisit the area in the event that information gained from monitoring and other sources showed that state actions were impeding federal policies or injuring consumers."¹¹⁶ Again taking its cue from the D.C. Circuit,¹¹⁷ the FCC expressly stated that it was not preempting state regulations requiring LECs to function as inside wiring "providers of last resort."¹¹⁸

112. See *In re Mountain States Tel. & Tel. Co., Memorandum Opinion and Order*, 2 FCC Rcd. 6069, para. 1 (1987) ("*Louisiana* held that this Commission does not have preemptive authority over state-imposed depreciation schedules that are used for purposes of computing interstate rates.>").

113. See *Detariffing the Installation and Maintenance of Inside Wiring, Third Report and Order*, 7 FCC Rcd. 1334 (1992) [hereinafter *Inside Wiring Remand Order*]; *In re Computer III Remand Proceedings: Bell Operating Co. Safeguards and Tier 1 Local Exch. Co. Safeguards, Report and Order*, 6 FCC Rcd. 7571 (1991) [hereinafter *Computer III Remand Order*], *vacated in part and remanded sub nom. California III*, 39 F.3d 919 (9th Cir. 1994), *petition for cert. denied*, 1995 U.S. LEXIS 2435 (Apr. 3, 1995).

114. See *Inside Wiring Remand Order*, *supra* note 113, para. 1.

115. *NARUC III*, 880 F.2d 422, 430 (D.C. Cir. 1989) ("[T]he Commission may require that all [states] unbundle inside wiring from basic telephone service.>").

116. *Inside Wiring Remand Order*, *supra* note 113, para. 9. To facilitate its monitoring, the FCC directed telephone companies with annual revenues of \$100 million or more to notify it of any proposed state efforts to regulate the price of carrier-provided inside wiring. See *id.* para. 22.

117. See *supra* note 95 and accompanying text.

118. *Inside Wiring Remand Order*, *supra* note 113, para. 27. This order was not challenged on appeal.

2. Enhanced Services

The FCC's retreat in the enhanced services area was somewhat more limited, although still quite significant.

In *Computer III Remand Order*,¹¹⁹ the FCC reaffirmed its decision—made in the original *Computer III* orders—to lift the requirement that the BOCs provide interstate enhanced services pursuant to structural separation.¹²⁰ In its place, the FCC imposed nonstructural safeguards that it claimed were stronger than the ones found inadequate in *California I*.¹²¹ For example, the FCC required the BOCs to obtain prior consent from customers with more than twenty lines before using customer proprietary network information to develop or market enhanced services.¹²² The Commission also reaffirmed the network information disclosure rule.

Turning to the preemption question, the FCC began by extending the olive branch to the states. "It is inevitable," the FCC observed, that: state commissions will have different experiences and perspectives that may lead them to adopt safeguards that are at variance with each other, and with federal safeguards. These differences should be accommodated wherever possible. Preemption of state regulation in this area should be as narrow as possible to accommodate differing state views while preserving federal goals.¹²³

119. *Computer III Remand Order*, *supra* note 113.

120. No party in the *California I* case challenged the FCC's decision to lift structural separation requirements as applied to AT&T. However, the *California I* decision had the effect of vacating that aspect of *Computer III*. In a separate order, the FCC readopted its decision to lift the AT&T structural separation requirement. See *In re Computer III Remand Proceedings, Report and Order*, 5 FCC Rcd. 7719 (1990). No party challenged that determination.

121. See *Computer III Remand Order*, *supra* note 113, paras. 12-89.

122. The FCC concluded that its new rule would balance its concern about preventing the BOCs from having an unfair competitive advantage in the enhanced services market through their access to CPNI with its desire to allow carriers to provide interstate basic and enhanced services on an integrated basis. A more stringent prior authorization requirement (such as one requiring the BOCs to obtain prior authorization from all customers), the FCC reasoned, would prevent the joint marketing of basic and enhanced services to most customers. See *id.* para. 85. In effect, the FCC's theory was that a BOC would be unable to obtain authorization from all of its customers. As a result, the carrier would be obligated to use separate marketing personnel for basic and enhanced services in order to ensure that enhanced services marketing personnel did not make impermissible use of CPNI. Limiting the prior authorization requirement to multi-line customers, in contrast, would make it possible for a BOC to obtain the necessary consents (or employ appropriate "blocking" technology) so that it would be possible for it to use the same marketing personnel for basic and enhanced services.

123. *Id.* para. 121.

The order that followed demonstrated that the FCC had traded its preemption sword for a finely honed stiletto. Only three forms of state enhanced service regulation were preempted: regulations requiring carriers¹²⁴ to offer the intrastate portion of jurisdictionally mixed enhanced services using personnel or facilities different from those used with basic telephone service;¹²⁵ regulations requiring carrier personnel responsible for marketing enhanced services to obtain customer consent prior to accessing CPNI in circumstances in which FCC regulations allow access without prior customer approval;¹²⁶ and regulations requiring carriers to disclose network information to competing ESPs at a time prior to that required by FCC rules.¹²⁷

In a marked departure from past practice, the FCC carefully justified each element of its preemption order. The Commission began with its preemption of certain state structural separation regulations. In theory, the FCC conceded, a carrier could use separate personnel and facilities to provide intrastate basic and enhanced services while combining its interstate basic and enhanced services in a single entity.¹²⁸ However, the FCC recognized that “[a]s a practical matter” such an arrangement would impose significant inefficiencies.¹²⁹ The result, the FCC stated, would be that “state structural separation requirements [applicable to personnel and facilities used to provide intrastate enhanced services] will compel carriers to use structural separation for interstate services and, therefore, will negate the federal policy for interstate enhanced services.”¹³⁰

The FCC then turned to its preemption of certain state nonstructural safeguards. The FCC justified its decision to bar states from imposing more stringent prior customer authorization requirements before carrier personnel could obtain CPNI as necessary to allow carriers to provide basic and enhanced services on an integrated basis. Allowing a state to impose more stringent requirements, the Commission reasoned, would “effectively require the separation of marketing and sales personnel dealing with interstate enhanced services from personnel dealing with interstate basic services.”¹³¹

124. The preemption order was applicable to state regulation of the BOCs, AT&T, and the independent telephone companies.

125. *Computer III Remand Order*, *supra* note 113, paras. 122-29.

126. *Id.* para. 130.

127. *Id.* para. 131.

128. *See id.* para. 124.

129. *Id.* para. 127.

130. *Id.*

131. *Id.* para. 130.

Finally, the FCC concluded that it was justified in preempting state regulations that required disclosure of network information at a time prior to that provided by the FCC rules. “[I]nitial disclosure [of network information],” it stated, “can occur only once. . . . [A] state rule that required initial disclosure at a time that differs from the time specified in the federal rule would negate the federal timing”¹³²

The FCC went on to expressly describe the limits of its incursion into state territory. According to the Commission, the states were free to adopt structural separation requirements in connection with any purely intrastate (as opposed to jurisdictionally mixed) carrier-provided enhanced service.¹³³ The states also could adopt structural separation requirements (other than those expressly preempted) applicable to jurisdictionally mixed enhanced services.¹³⁴ Finally, the states were free to impose any non-structural safeguard not expressly barred by the order.¹³⁵ The FCC declined to even consider preempting states from imposing entry, exit, and tariff regulation on carrier-provided intrastate enhanced services.¹³⁶

F. *The States Overreach (1991-94)*

While the states had won some significant battles in the late 1980s, they were not in as strong a position as they thought. Their overconfidence led to some serious miscalculations. Following the *California I* decision, the states launched a two-prong attack on the FCC’s powers. First, the states again attempted to redefine the boundary between federal and state authority by trying to carve out an “intrastate segment” of services that previously were viewed as jurisdictionally interstate. Second, the states tried to erect new barriers to federal preemption of those services that were within the intrastate jurisdiction. Just as the courts turned back the FCC’s overreaching, they now rejected the extravagant claims the states advanced.

1. Jurisdictional Challenges

The first prong of the states’ attack was to reopen the debate—seemingly resolved in *NARUC II*¹³⁷—over the ability of the FCC to regulate

132. *Id.* para. 131.

133. *Id.* para. 122.

134. *Id.* For example, a state could require that carriers provide intrastate enhanced services through separate legal entities or use separate accounting rules from those used for basic services.

135. *Id.* para. 121.

136. *Id.* para. 111 n.214.

137. *NARUC II*, 746 F.2d 1492 (D.C. Cir. 1984); see *supra* text accompanying notes 33-38.

the physically intrastate segment of an interstate communication. Most of this effort centered on the rapidly emerging enhanced service market. For example, Florida announced that it would assert jurisdiction over communications between an ESP's customer located in Florida and the ESP's "point of presence" elsewhere in the state. The fact that the communication might terminate at a database located in another state, Florida concluded, "is not relevant."¹³⁸ A number of states also declared that their jurisdiction extended to enhanced services sessions that originate and terminate within their state, even if information passes through other jurisdictions over federally tariffed interstate lines.¹³⁹ California took a different approach, announcing that it would require carriers to allocate 100 percent of the cost of enhanced services to the intrastate jurisdiction, thereby allowing the state to exercise regulatory authority over all carrier-provided enhanced services offered within the state.¹⁴⁰

The most controversial state decision during this period concerned MemoryCall, an enhanced service offered by BellSouth that stores incoming voice messages for subsequent retrieval by the subscriber. An investigation by the Georgia PSC concluded that BellSouth had engaged in a variety of anticompetitive activities in connection with its offering of this

138. An Investigation Into Statewide Offering of Access to the Local Network for the Purpose of Providing Information Service, Docket 880 423-TP, Order No. 21815, at 12-19, 23 (Fla. P.S.C. Sept. 5, 1989).

139. See D.C. PSC Order to Show Cause at 2-3; see also IDAHO CODE § 61-121(2) (1994) (defining "telecommunication service" as "the transmission of two-way interactive switched signs, signals, writing, images, sounds, messages, data, or other information of any nature by wire, radio, lightwaves, or other electromagnetic means . . . which originate and terminate in this state"); N.M. STAT. ANN. § 63-9A-3(L) (Michie 1989 Repl.) (defining "public telecommunications service" as "the transmission of signs, signals, writings, sounds, messages, data or other information of any nature by wire, radio, lightwaves or other electromagnetic means originating and terminating in this state regardless of actual call routing"); OHIO REV. CODE ANN. § 4927.01(D) (Anderson 1991); New England Tel. & Tel., Docket No. 87-290, at 3 (Maine P.U.C. Apr. 25, 1988) (advisory opinion) ("[T]elephone calls which both originate and terminate within a single state, regardless of the route over which they are transported, are *intrastate* calls." (emphasis in the original)); Responsive Comments of the Staff of the Public Service Commission of the District of Columbia, Formal Case No. 904, at 4 (Jan. 24, 1991) (arguing that the D.C. PSC's jurisdiction "include[s] calls to enhanced service providers which originate and terminate in the District of Columbia even though the call may exit the District of Columbia during its transmission").

140. See Application of California for Petition for Review of RAO Letter 16 at 3 (Nov. 16, 1990). California adopted the same approach in connection with carrier-provided inside wiring. See Classification of Inside Wiring Servs. for Accounting Purposes, *Memorandum Opinion and Order*, 5 FCC Rcd. 3521 (1990) [hereinafter *RAO Letter 14*]; Letter from Kenneth P. Morgan, Chief, Accounting and Audits Div., to Responsible Accounting Officers, 4 FCC Rcd. 7110 (1989).

service.¹⁴¹ Seeking to curb these abuses, Georgia issued an order in which it declared that, because the enhanced function (information storage and retrieval) was performed by facilities that were physically present in Georgia, MemoryCall was a purely intrastate service within the Georgia PSC's jurisdiction.¹⁴² Exercising its supposed exclusive authority, Georgia barred BellSouth from providing MemoryCall to new customers for an indefinite period.¹⁴³

At BellSouth's request, the FCC issued a declaratory ruling preempting Georgia's action. The FCC first found that—because MemoryCall can be used to store voice messages that originate both inside and outside of Georgia—it was a jurisdictionally mixed (rather than purely intrastate) service¹⁴⁴ and that the interstate component was within the FCC's plenary interstate jurisdiction.¹⁴⁵ The FCC went on to find that, as a practical matter, Georgia's ban on the use of MemoryCall in connection with intrastate calls would have the effect of preventing subscribers from using the service in connection with interstate calls. This, the FCC concluded, was irreconcilable with its regulation allowing BellSouth to offer MemoryCall to interstate subscribers.¹⁴⁶

Georgia appealed the FCC's order, again arguing that MemoryCall was a "purely intrastate" service and that the FCC had no authority to preempt state regulation. The Eleventh Circuit disposed of the state's claims in a single sentence: "The record fully supports both the jurisdictional aspect and the reasonableness of the order entered by the Federal Communications Commission."¹⁴⁷

The states did not limit their jurisdictional attacks to enhanced services. As part of its *Computer III* orders, the FCC had required the

141. Investigation into Southern Bell Telephone and Telegraph Company's Provisions of MemoryCall Service, Docket No. 4000-U, at 26-42 (Georgia P.S.C. May 21, 1991) [hereinafter *Georgia MemoryCall Order*].

142. *Id.* at 56. Georgia recognized that MemoryCall could be used to store messages that originated out of state. However, it reasoned that the use of MemoryCall in connection with out-of-state calls constituted two separate "communications": a jurisdictionally interstate basic telephone call from an out-of-state caller to the telephone company switch in Georgia, and a subsequent jurisdictionally intrastate enhanced service in which information was routed from the carrier's switch to the carrier's message storage facility. See Petition for Emergency Relief and Declaratory Ruling Filed by the BellSouth Corp., *Memorandum Opinion and Order*, 7 FCC Rcd. 1619 (1992) (describing Georgia's position) [hereinafter *MemoryCall Preemption Order*].

143. *Georgia MemoryCall Order*, *supra* note 141, at 71-72.

144. *MemoryCall Preemption Order*, *supra* note 142, paras. 6, 12.

145. *Id.*

146. *Id.* para. 20.

147. *Georgia PSC*, No. 92-8257, 1993 U.S. App. LEXIS 24458 (11th Cir. Sept. 22, 1993).

BOCs to implement a system of Open Network Architecture (ONA). Under ONA, the carriers were required to "unbundle" their basic communications networks and allow ESPs to obtain the individual "building blocks" needed to provide enhanced services.¹⁴⁸ In its subsequent *ONA Order*, the FCC adopted a "common ONA model," which divided the network "building blocks" into two principal categories: Basic Serving Arrangements (BSAs) and Basic Service Elements (BSEs).¹⁴⁹ BSAs are physically intrastate transmission links that can be used to provide access to the interstate communications network. BSEs are other network "features and functions," such as calling number identification and call routing, that ESPs may find useful in providing service.¹⁵⁰

Because ONA services are used to provide enhanced services on both an interstate and intrastate basis, the *ONA Order* addressed the question of how responsibility for regulating these services should be divided between the Commission and the states. Several states argued that BSEs are subject to exclusive state jurisdiction because they are provided using software that is resident in physically intrastate telephone company switches.¹⁵¹ The FCC rejected these arguments, finding that BSEs used to provide enhanced services that cross state lines are jurisdictionally interstate. It therefore determined that BSEs should be "subject to regulation . . . on both the state and federal levels."¹⁵² The FCC subsequently approved the ONA plans submitted by the BOCs.¹⁵³

California (joined by several other states) appealed the FCC's decision to require joint tariffing of BSEs.¹⁵⁴ The states renewed their argument that BSEs were subject to exclusive state regulation. The states further argued that, even if BSEs were jurisdictionally mixed, the FCC was

148. See *Computer III Phase I Order*, *supra* note 60, paras. 206-17. The Commission elaborated on this requirement in the *Computer III Phase I Reconsideration Order*, *supra* note 60, paras. 106-12.

149. *In re Filing and Review of the Open Network Architecture Plans*, *Memorandum Opinion and Order*, 4 FCC Rcd. 1, para. 56 (1988) [hereinafter *ONA Order*], *on reconsideration*, 5 FCC Rcd. 3079 (1990) [hereinafter *ONA Reconsideration Order*].

150. *ONA Order*, *supra* note 149, para. 57. The *ONA Order* also identified a third category of network "building blocks," Complementary Network Services (CNSs), which are state-tariffed basic services (such as "call waiting" or "distinctive ring") that end-users employ to access the telephone network in connection with both basic and enhanced services.

151. See *id.* para. 252 n.521.

152. *Id.* para. 224; *ONA Reconsideration Order*, *supra* note 149, para. 35.

153. See *In re Filing and Review of Open Network Architecture Plans*, Phase I, *Memorandum Opinion and Order*, 5 FCC Rcd. 3103 (1990) [hereinafter *BOC ONA Plan Amendment Order*].

154. See Brief For Petitioner-Intervenors at 17-18, *California II*, 4 F.3d 1505 (9th Cir. 1993).

obligated to “adopt a federal tariffing requirement [for interstate BSEs] that was narrowly crafted” to avoid interfering with state policies—especially some states’ efforts to require the BOCs to price ONA services above cost in order to create a subsidy for other services.¹⁵⁵

This time it took the court an entire paragraph to dispose of the states’ jurisdictional arguments. In *California II*, the Ninth Circuit held that:

[The ONA orders] clearly establish a dual federal and state tariffing structure for BSEs, and the states will retain authority to set rates for those BSEs that are used for intrastate service. This system complies with the Supreme Court’s decision in *Louisiana* that the Communications Act is designed to establish a dual regulatory scheme. Essentially, the state is seeking to preempt FCC regulations of communications, and this violates the Act just as FCC preemption of state regulation did in *Louisiana* and *California I*.¹⁵⁶

The states’ effort to “shift the boundary” between the interstate and intrastate jurisdictions had been no more successful in the early 1990s than it had been a decade earlier.

2. Preemption Challenges

The states’ final assault started, where the war had begun, with Section 2(b)(1). In the *Computer III Remand Order*, the FCC had significantly scaled back its earlier enhanced service preemption order. Nonetheless, the FCC—relying on its Title I power—had again preempted certain state structural and nonstructural separation requirements applicable to intrastate enhanced services.¹⁵⁷ The states again appealed to the Ninth Circuit, arguing that the FCC had still gone too far.

The states made two principal thrusts at the FCC’s jurisdiction. The first was to assert that the Supreme Court’s decision in *Louisiana* “unequivocally rejected” the claim that the FCC could use its preemption power to advance Title I goals. The second was to contend that, even when acting under Title II, the FCC could only preempt state regulation where simultaneous compliance with divergent federal and state rules was a “literal impossibility.” In a consolidated case, MCI claimed that the FCC’s new structural separation requirements remained inadequate to prevent BOC cross-subsidization and discrimination at the interstate level.

In *California III*, the Ninth Circuit found for MCI, again rejecting the FCC’s decision to replace BOC structural separation with nonstructural

155. *Id.* at 21.

156. *California II*, 4 F.3d at 1515.

157. The *Computer III Remand Order* is described *supra* notes 119-36 and accompanying text.

safeguards at the interstate level.¹⁵⁸ Turning to the preemption issue, the court first addressed the question whether the FCC can preempt under its Title I authority.¹⁵⁹ Again, a paragraph was all that was necessary to dispose of the states' claim. *Louisiana*, the court recognized, had held that Section 2(b)(1) limited the FCC's authority under *both* Title I and Title II.¹⁶⁰ Although the preemption order rejected in *Louisiana* was based on the FCC's Title I power, the Ninth Circuit made clear that—if it could make the proper showing—the FCC could justify preemption under that Title.¹⁶¹

The court then turned to the question of what the proper showing would be. To resolve this issue, it went back to the *NCUC* cases. In those cases, FCC preemption had been permissible because compliance with conflicting federal and state regulations governing interconnection, while possible, was highly unlikely due to practical and economic considerations. The present case, the court concluded, was "similar."¹⁶² While BOC compliance with conflicting federal and state rules governing the use of separate facilities or personnel and access to CPNI was literally possible, the FCC had demonstrated that "as in the *NCUC* cases . . . it would not be economically or operationally feasible for them to do so."¹⁶³ The FCC, therefore, had met its obligation of "demonstrating that [its] order is

158. See *California III*, 39 F.3d 919, 923-31 (9th Cir. 1994), *cert. denied*, 1995 U.S. LEXIS 2435 (Apr. 3, 1995). The court relied on the findings of the Georgia PSC regarding BellSouth's abuses in providing MemoryCall service as well as its prior decision in *California II* which had concluded that—in the years following *Computer III*—the FCC had significantly "diluted" the effectiveness of its ONA program in reducing the ability of the BOCs to discriminate against non-carrier ESPs. *California II*, 4 F.3d at 1511-13. The FCC subsequently initiated a new proceeding to again revisit the adequacy of nonstructural safeguards in preventing BOC anticompetitive abuse. See *In re Computer III Further Remand Proceedings: Bell Operating Provision of Enhanced Services, Notice of Proposed Rulemaking* in CC Dkt. No. 95-20, FCC 95-48 (Feb. 21, 1995).

159. The court failed to explain why, after rejecting the FCC's decision to replace the BOC structural separation requirement with nonstructural safeguards at the interstate level, it was necessary to consider the authority of the FCC to prevent states from adopting certain requirements that were inconsistent with the invalidated federal regulatory scheme. The answer, presumably, is that the FCC's preemption order was not limited to state regulation of the BOCs; it also applied to state regulation of enhanced services provided by AT&T and the independent telephone companies, which are not subject to federal structural separation requirements.

160. *California III*, 39 F.3d at 932-33.

161. *Id.*

162. *Id.*

163. *Id.* The court also affirmed the FCC's conclusion that it would be literally impossible for separate federal and state disclosure dates for network information to co-exist. *Id.* at 933.

narrowly tailored to preempt only such state regulation as would negate valid regulatory goals."¹⁶⁴ The battle had come full circle.

II. FOUR PRINCIPLES OF PEACEFUL COEXISTENCE

The FCC and the states are at a crossroads. After more than a dozen engagements, it has become clear that neither side can conquer the other. The prudent course of action is for both sides to take stock of their experience and try to agree to a set of principles that will allow them to turn their litigators' swords into regulatory pruning hooks. The cases outlined above suggest the basis for such a peace treaty. It is not a peace based on shared values; it is one based on respect for each other's authority. The principles of the proposed peace treaty are as follows:

- Jurisdiction is determined on an end-to-end basis. Any communication that crosses state lines between its point of origin and its point of termination is jurisdictionally interstate. Physically intrastate facilities and services used in connection with interstate communications are jurisdictionally interstate to the extent of their interstate use.
- The FCC has plenary jurisdiction over interstate communications facilities and services. The states may not regulate such facilities and services directly or by reclassifying interstate facilities and services as intrastate.
- The states are entitled, in the first instance, to regulate intrastate communications facilities and services. In so doing, they may adopt common carrier policies that differ from those adopted by the FCC.
- The FCC may preempt state regulations applicable to carrier-provided intrastate communications facilities or services to the extent that the Commission concludes, as a practical matter, that enforcement of such regulations would prevent the application of federal regulations to interstate carrier-provided communications services or facilities.

Each of these principles is discussed below.

164. *Id.* (quoting *California I*, 905 F.2d 1217, 1243 (9th Cir. 1990)).

A. *Jurisdiction is Determined on an End-to-End Basis*

Peace is not possible if the FCC and the states cannot agree on where the border between their jurisdictions lies. Fortunately, the Communications Act provides clear guidance in resolving this question.

The Act defines a “wire communication” as “the transmission of writing, signs, signals, pictures, and sounds of all kinds . . . between the points of origin and reception.”¹⁶⁵ The Act further provides that when such a transmission goes “from any State . . . to any other State,” it is deemed an interstate communication.¹⁶⁶ Taken together, these provisions require that jurisdictional determinations be made on an end-to-end basis. Any communication by wire or radio that crosses state lines at any point between its “origin and reception” is jurisdictionally interstate.¹⁶⁷ Similarly, any communication by wire or radio that does not cross state lines between its point of origin and its point of termination is jurisdictionally intrastate.

The Communications Act further provides that the interstate jurisdiction embraces “facilities and services . . . incidental to transmission” of an interstate communication.¹⁶⁸ Thus, any facility or service used in connection with an interstate communication is jurisdictionally interstate to the extent of its interstate use. The fact that such facilities and services may be physically intrastate is irrelevant.¹⁶⁹ Any facility or service used in

165. 47 U.S.C. § 153(a) (1988).

166. 47 U.S.C. § 153(e) (1988).

167. This recognition pre-dates the adoption of the Communications Act. The seminal case is *Western Union v. Speight*, 254 U.S. 17 (1920). *Speight* was a state common law action arising out of a mistake made by Western Union in the delivery of a telegram from Greenville, North Carolina to Rosemary, North Carolina. Western Union defended on the grounds that, because the telegram had been sent by way of Richmond, Virginia, the plaintiff’s claim was governed by federal—rather than state—law. The Supreme Court agreed, observing that “[t]he transmission of a message through two states is interstate commerce as a matter of fact.” *Id.* at 18; *cf.* *United States v. Yaquinta*, 204 F. Supp. 276 (N.D. W. Va. 1962) (noting that a telephone call placed by a bookmaker from Arroyo, West Virginia to Wheeling, West Virginia, which was routed through Liverpool, Ohio, violated § 1084 of the Federal Criminal Code, 18 U.S.C. § 1084 (Supp. III 1959-61) (current version at 18 U.S.C. § 1084 (1988)), which makes it unlawful to “us[e] a wire communication facility for the transmission in interstate . . . commerce of . . . information assisting in the placing of bets or wagers”).

168. 47 U.S.C. § 153(a) (1988).

169. The Congress that adopted the Communications Act was well aware of this result. As originally drafted, the bills that were to become the Communications Act of 1934 (S. 1290 and H.R. 8301) contained language that deprived the FCC of jurisdiction to approve the construction of communications facilities “within a single state.” This provision was strongly opposed by ICC Commissioner McMannamy. In testimony before both the Senate and House committees in 1934, Commissioner McMannamy explained that physically

connection with an intrastate communication is jurisdictionally intrastate to the extent of its intrastate use.¹⁷⁰

The federal courts initially considered the division of authority between the federal and state jurisdictions in connection with basic telephone service.¹⁷¹ However, the same principles are applicable to enhanced services. Thus, in *Georgia PSC*, the Eleventh Circuit affirmed the FCC's finding that BellSouth's voice messaging service was subject to FCC jurisdiction to the extent that it was used to store messages that originated out-of-state.¹⁷² Conversely, as the Ninth Circuit found in *California I*, voice mail, burglar alarm monitoring services, and remote educational databases that are provided solely to "discrete locales within a state" are subject to exclusive state jurisdiction.¹⁷³

B. *The FCC Has Plenary Jurisdiction over Interstate Communications Facilities and Services*

Once the dividing line between federal and state jurisdiction is established, the next step in the peace process is to determine the authority of each party within its respective realm. In the case of the federal sovereign, the answer is straightforward: the FCC has plenary authority over jurisdictionally interstate communications.

In *Louisiana*, the Supreme Court observed that, under the Supremacy Clause,¹⁷⁴ a federal agency has the exclusive right to adopt regulations in any area in which "Congress has legislated comprehensively, thus occupying an entire field of regulation and leaving no room for the States to supplement federal law."¹⁷⁵ In such cases, state regulations are invalid

intrastate facilities could be used for both jurisdictional interstate and intrastate calls. At his insistence, Congress adopted the language now found in § 214(a) of the Act, 47 U.S.C. § 214(a) (1988), which provides that the FCC lacks jurisdiction over "a [telephone] line within a single State unless that line constitutes part of an interstate line." See McKenna, *supra* note 6, at 15 n.37.

170. Section 221(b) of the Communications Act further authorizes the states to regulate a single local exchange that straddles the border of two states. 47 U.S.C. § 221(b) (Supp. V 1993).

171. See, e.g., *California II*, 4 F.3d 1505 (9th Cir. 1993) (subjecting BSEs, which are physically resident in local switches, to FCC jurisdiction to the extent used in connection with interstate enhanced services); *California v. FCC*, 567 F.2d 84 (D.C. Cir. 1977) (per curiam), cert. denied, 434 U.S. 1010 (1978) (subjecting physically intrastate Bell System local exchange facilities to FCC regulations requiring interconnection of interstate communications lines).

172. See *MemoryCall Preemption Order*, *supra* note 142, paras. 10-12.

173. *California I*, 905 F.2d 1217, 1244 (9th Cir. 1990).

174. U.S. CONST. art. VI.

175. *Louisiana*, 476 U.S. 355, 368 (1986).

even if they do not conflict with federal law.¹⁷⁶ Interstate communications plainly is one such area. The Communications Act vests the FCC with jurisdiction over “all interstate and foreign communications by wire or radio.”¹⁷⁷ As the D.C. Circuit observed in *NARUC II*, regulatory authority over interstate communications is “totally entrusted to the FCC.”¹⁷⁸ There is, quite simply, no room for state regulation in this area.

The FCC’s plenary authority plainly precludes a state from enforcing a regulation that, on its face, purports to regulate interstate communications.¹⁷⁹ The states, moreover, may not do indirectly what they are forbidden to do directly. This explains why the courts have consistently turned back state efforts—such as Georgia’s effort to declare MemoryCall a purely intrastate service,¹⁸⁰ or California’s effort to have all network BSEs subject to exclusive state tariffing¹⁸¹—that would have allowed states to regulate jurisdictionally interstate communications services by “shifting the boundary” between the federal and state jurisdictions.

Other forms of state “jurisdictional gerrymandering” also are suspect. For example, the suggestion made by several states that an enhanced service session in which information crosses state lines can be “sliced up” into a physically intrastate segment (subject to state regulation) and a physically interstate segment (subject to FCC regulation), appears flatly inconsistent with the principle that the jurisdictional nature of a communication is determined on an end-to-end basis. Indeed, the Eleventh Circuit affirmed the FCC’s rejection of just this sort of an argument in the *Georgia PSC* case.¹⁸²

Another seemingly impermissible form of “border shifting” can occur if a state is able to require a carrier to allocate a disproportionate amount of its costs for a given facility or service to the intrastate jurisdiction. In the case of federally regulated basic telephone service, the FCC’s jurisdictional

176. See *Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 698 (1984).

177. 47 U.S.C. § 152(a) (1988) (emphasis added).

178. *NARUC II*, 746 F.2d 1492, 1501 (D.C. Cir. 1984).

179. See *In re Operator Servs. Providers of America, Memorandum Opinion and Order*, 6 FCC Rcd. 4475 (1991) (preempting a Tennessee statute, Public Chapter No. 675 (amending TENN. CODE ANN. §§ 65-5-206, 47-18-104 (1993)), expressly regulating interstate communications services offered by operated service providers on the grounds that the statute infringed on the FCC’s plenary jurisdiction over interstate communications services); see also *AT&T v. Public Serv. Comm’n of Wyoming*, 625 F. Supp. 1204, 1208 (D. Wyo. 1985) (“It is beyond dispute that interstate communication is normally outside the reach of state commissions and within the exclusive jurisdiction of the FCC.”).

180. See *Georgia MemoryCall Order*, *supra* note 141.

181. See *California II*, 4 F.3d 1505 (9th Cir. 1993).

182. *Georgia PSC*, No. 92-8257, 1993 U.S. App. LEXIS 24458 (11th Cir. Sept. 22, 1993); see *supra* text accompanying notes 141-47.

separations process ensures that the correct proportion of costs will be assigned to the intrastate jurisdiction. This division is binding on the states.¹⁸³ The FCC, however, has declined to apply the jurisdictional separations process to facilities and services that are not regulated at the federal level, such as inside wiring and enhanced services.¹⁸⁴ The Commission also has announced that the states may adopt their own methods to determine the proportion of a carrier's costs related to these offerings that is within the intrastate jurisdiction.¹⁸⁵

This approach is perfectly acceptable—so long as the states adopt reasonable measures to determine what portion of the carrier's costs are to be allocated to the intrastate jurisdiction.¹⁸⁶ However, if a state were to require carriers to assign *all* of their enhanced service and inside wiring costs to the intrastate jurisdiction—even though these offerings are jurisdictionally mixed—it would be able to exercise authority over jurisdictionally interstate facilities and services.¹⁸⁷ This seems flatly inconsistent with the Supreme Court's decision in *Smith v. Illinois Bell*, which recognized that, while considerable flexibility is allowed, it is impermissible to “ignore altogether” the division between federal and state jurisdiction by allocating all costs to the intrastate jurisdiction.¹⁸⁸

Finally, the states cannot regulate interstate communications by requiring the FCC to forgo exercise of its plenary interstate jurisdiction in situations in which federal regulation would adversely affect the states in implementing their policies. As the Ninth Circuit recognized in *California II*, such “reverse preemption” has no place in the Communications Act.¹⁸⁹ When the FCC is acting within the scope of its plenary power over interstate communications, it need not seek to accommodate divergent state interests.¹⁹⁰

183. See *Hawaiian Tel. Co. v. Public Util. Comm'n*, 827 F.2d 1264 (9th Cir. 1987), *cert. denied*, 487 U.S. 1218 (1988).

184. See *RAO Letter 16*, *supra* note 50; *RAO Letter 14*, *supra* note 140, at 3522.

185. *RAO Letter 16*, *supra* note 50, at 5947; *RAO Letter 14*, *supra* note 140, at 3523.

186. *Cf. Crockett Tel. Co. v. FCC*, 963 F.2d 1564 (D.C. Cir. 1992) (noting that the FCC may allow states to use a “residual ratemaking” approach which uses industry-wide averages to estimate the portion of small LECs' regulated costs that are within the intrastate jurisdiction).

187. This is precisely what California has informed the FCC it would do. See *supra* note 50.

188. *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133, 150-51 (1930); see *supra* note 140.

189. *California II*, 4 F.3d 1505, 1515 (9th Cir. 1993) (“[T]he state is seeking to preempt FCC regulation of communications, and this violates the [Communications] Act. . .”).

190. Of course, in the interest of comity, the FCC may wish to take state concerns into account. For a further discussion of federal-state comity, see *infra* text accompanying notes 233-40.

C. The States are Entitled to Regulate Intrastate Communications Services and Facilities

Under the division of responsibility embodied in the Communications Act, the states have authority, in the first instance, to regulate common carrier communications by wire or radio that originate and terminate within the same state. They also may regulate physically intrastate facilities and services used in connection with such communications to the extent of their intrastate use. Because the vast majority of telephone calls in the United States originate and terminate within the same state,¹⁹¹ this gives the states significant power within the “dual regulatory” system.

In exercising its power over intrastate common carrier communications, a state may seek to advance policies that are at odds with those favored by the FCC. To the extent that the state is able to limit application of its regulation to facilities and services within its jurisdiction, Section 2(b)(1) provides it with the right to do so, free from federal interference.

D. The FCC May Preempt State Regulations Applicable to Carrier-Provided Intrastate Communications Facilities or Services to the Extent that, as a Practical Matter, Enforcement of Such Regulations Would Prevent the Application of Federal Regulations to Interstate Carrier-Provided Communications Services or Facilities

Avoiding conflicts between federal and state authorities would be a simple matter if the two sides could be kept within their respective jurisdictions, separated by an ironclad boundary. Obviously, they cannot be. The same facilities and services are frequently subject to both FCC and state jurisdiction. Whenever the two regulatory authorities seek to apply different rules to the same offerings, some degree of jurisdictional tension is inevitable.

1. The Preemption Principle

The cases decided over the last two decades provide the basis for resolving federal-state conflicts. The decisions reflect a distinction—evident, although not discussed—between conflicts based on divergent state *policy* regarding intrastate services, and conflicts based on the *de facto* assertion of state *jurisdiction* over interstate facilities and services. The cases teach that Section 2(b)(1) gives the states the right to

191. See *supra* note 19.

advance their policies by applying their own regulations to common carrier facilities and services within their jurisdiction. The fact that a state may adopt a policy that thwarts the FCC's achievements of its policy goals in this area does not, in itself, provide a basis for federal preemption.

There is one—and only one—situation in which Section 2(b)(1) allows the FCC to cross the jurisdictional divide and displace state regulation of intrastate carrier facilities or services. This occurs when, as a practical matter, the application of a state's regulations to jurisdictionally *intrastate* carrier facilities or services would displace the FCC's ability to apply its "rule of decision" to jurisdictionally *interstate* carrier facilities or services. In such case, one sovereign or the other must give way. Under our federal system, as embodied in the Supremacy Clause,¹⁹² it is the states that must defer.

The difference between a state adopting a divergent policy and a state effectively asserting jurisdiction over interstate services is clearly illustrated by comparing *Louisiana* with the *NCUC* cases. *Louisiana* involved a difference in federal and state policy: the FCC wanted carriers to modernize their plant quickly, the states wanted to keep telephone rates low.¹⁹³ The fact that some states sought to achieve their goal by requiring carriers to use relatively conservative depreciation methods for the "intrastate component" of their plant doubtless thwarted the FCC's effort to promote plant modernization. The FCC, however, was powerless to prevent the states from doing so. The reason is simple: nothing the states did in the *intrastate* jurisdiction threatened the ability of the FCC to apply its depreciation rules within the *interstate* jurisdiction.¹⁹⁴

The *NCUC* cases also involved a policy difference. The FCC wanted to allow a competitive CPE market; the states did not. Here, too, application of the state policy would have "thwarted" the FCC's goals. Yet, in this instance, the FCC's preemption order was upheld. The difference is fundamental. In the *NCUC* cases, allowing the states to adopt a rule preventing interconnection of user-provided CPE for intrastate communications, as a practical matter, would have resulted in subscribers using carrier-provided equipment for both interstate *and* intrastate calls. The FCC's ability to apply its "rule of decision" allowing interconnection of user-provided CPE to the interstate network would have been eliminated.¹⁹⁵

The proper resolution of FCC-state conflicts has been made more difficult by the semantic conventions used in the cases. Most courts have

192. U.S. CONST. art. VI.

193. See *Louisiana*, 476 U.S. 355 (1986).

194. See *supra* notes 48-51 and accompanying text.

195. See *supra* notes 25-32 and accompanying text.

phrased the preemption test in terms of goals and policies. The FCC is said to be able to preempt state regulation that would either “thwart or impede” or “frustrate” valid FCC goals.¹⁹⁶ These phrases suggest that preemption involves some sort of “balancing of interests” between federal and state policies. Other decisions have stated that the FCC can only preempt state regulation where it is “not possible to separate the interstate and intrastate components” of a given regulation¹⁹⁷—suggesting that the FCC is powerless to challenge a state regulation if there is any conceivable way in which divergent federal and state regulations can coexist.

What matters, of course, is what the courts do, not what they say. However, considerable confusion would be avoided if the courts were to formulate the preemption test in a manner that more clearly reflects the underlying principles. Such a reformulated test might read as follows: The FCC may preempt state regulations applicable to carrier-provided intrastate communications facilities or services to the extent that the FCC concludes, as a practical matter, that enforcement of such regulations would prevent the application of federal regulations to interstate carrier-provided communications facilities or services.¹⁹⁸

The phrase “as a practical matter” is crucial. There are some cases in which it is literally impossible for conflicting federal and state regulations to coexist. For example, as the Ninth Circuit recognized in *California III*, an FCC rule requiring carriers to disclose network interfaces six months before introducing a new service cannot coexist with a state rule requiring disclosure at an earlier date.¹⁹⁹ Initial public disclosure of a network interface can be made only once; application of a divergent state rule would

196. *California I*, 905 F.2d 1217, 1243 (9th Cir. 1990); accord *NARUC III*, 880 F.2d 422, 430 (D.C. Cir. 1989) (allowing the FCC to preempt state regulations that would “frustrate” or “interfere with the Commission’s valid goal[s]”); *CCLA*, 693 F.2d 198, 214 (D.C. Cir. 1982), *cert. denied*, 461 U.S. 938 (1983) (permitting preemption where state regulation “would interfere with achievement of a federal regulatory goal”).

197. *Louisiana*, 476 U.S. at 375 n.4; see *Illinois Bell Tel. Co. v. FCC*, 883 F.2d 104, 114 (D.C. Cir. 1989) (“[W]here it [is] not possible to separate the interstate and intrastate components of the [] FCC regulation involved . . . the Act sanctions federal regulation of the entire subject matter.”) (emphasis in original); *ARCO*, 886 F.2d 1325, 1333 (D.C. Cir. 1989) (justifying preemption only if technological inseparability also prevents the FCC from separating its regulation into interstate and intrastate components).

198. Interestingly, the very first of the preemption cases, *NCUC I*, provides language that may come closest to best expressing the preemption test. FCC preemption was permissible, the court indicated, where “state jurisdiction over interstate communications is exercised in a way that, in practical effect, . . . [frustrates the FCC’s] exercise of that plenary jurisdiction over the rendition of interstate and foreign communications services that the Act has conferred upon it.” *NCUC I*, 537 F.2d at 793.

199. See *California III*, 39 F.3d 919, 933 (9th Cir. 1994), *cert. denied*, 1995 U.S. LEXIS 2435 (Apr. 3, 1995).

inevitably displace the federal rule. The FCC plainly has the authority to protect its interstate jurisdiction by preempting such rules.²⁰⁰

In most situations, however, it is not "literally impossible" for divergent federal and state rules governing the same facility or service to coexist. In the *NCUC* cases, FCC rules allowing interconnection of CPE to the network for interstate purposes could have coexisted with state rules barring interconnection for intrastate purposes.²⁰¹ In *California III*, requiring carriers to use separate personnel and facilities to provide intrastate basic and enhanced services, while allowing them to use the same personnel and facilities to provide interstate basic and enhanced services, was far from a physical impossibility.²⁰²

The fact that simultaneous application of divergent federal and state rules was possible in the *NCUC* cases and *California III* was not dispositive. The decisive factor in those cases was that, as a practical matter, application of the state rule would have displaced the federal rule. Thus, in the *NCUC* cases, the Fourth Circuit recognized that no rational consumer would have bought a competitively provided telephone to make interstate calls if he was required to use a carrier-provided telephone to make intrastate calls.²⁰³ If the FCC lacked preemptive authority, the state rule barring interconnection of competitively provided CPE would have become the applicable "rule of decision" in the interstate sphere as well. Similarly, in *California III*, the Ninth Circuit recognized that the likelihood that a carrier required to employ separate personnel and facilities to provide intrastate enhanced services would integrate its basic and enhanced services at the interstate level was virtually non-existent.²⁰⁴ In the absence of federal preemption, a state rule requiring structural separation at the intrastate level also would have governed carriers' provision of interstate enhanced services.

In reaching their conclusions about the practicality of divergent FCC-state regulations, the courts have shown substantial deference to the FCC.²⁰⁵ In effect, the courts have treated the FCC's determination as to whether the coexistence of conflicting federal and state regulations is "impractical" or "infeasible" as a matter within the FCC's expert judgment.

200. *See id.*

201. *See supra* notes 25-32 and accompanying text.

202. *See supra* notes 162-64 and accompanying text.

203. *See NCUC I*, 537 F.2d at 791.

204. *See California III*, 39 F.3d at 933.

205. *See, e.g., NCUC I*, 537 F.2d at 792 (deferring to the FCC's conclusion that it would not be practical for customers to use one set of communications facilities for intrastate communications, and another set for interstate communications).

Under established administrative law principles, such determinations are not disturbed unless they are found to lack record support or to be arbitrary and capricious.²⁰⁶

While the FCC's determination as to the *need* to preempt state regulation is entitled to substantial deference, the Commission's decision as to the *extent* of any preemption order is subject to more searching judicial review. The courts have made clear that the FCC is under an affirmative obligation to "narrowly tailor" any preemption order; it may only displace state regulations to the extent necessary to protect its interstate jurisdiction. The burden, moreover, is on the FCC to demonstrate that it has done so.²⁰⁷ Were the Commission to go any further, it would trample the "jurisdictional fence" that Section 2(b)(1) erects around state regulation of intrastate facilities and services.

The FCC's obligation to narrowly tailor its preemption of state common carrier regulation is evident in both *NARUC III* and *California I*. In neither case did the court suggest that the FCC was without preemptive power. To the contrary, the D.C. and Ninth Circuits specifically identified possible subjects of FCC preemption in the inside wiring and enhanced services areas.²⁰⁸ In each case, however, the court found that the FCC's preemption order suffered from the same fatal defect: the order preempted *all* state regulation of the subject. The FCC had made no effort to limit the order to those state regulations that could not feasibly coexist with federal regulations.²⁰⁹

While the FCC's duty to narrowly tailor its preemption orders is a significant one, the Commission need not show that it has crafted the *narrowest possible* preemption order.²¹⁰ Thus, the FCC is free to reject means of narrowing its preemption order that it concludes are not feasible. For example, in *Maryland PSC* the D.C. Circuit rejected a claim that federal preemption of state regulation of an LEC-provided telephone disconnection service could be narrowed by requiring carriers to limit the

206. See *Motor Vehicle Mfrs. Ass'n v. State Farm Mutual Auto Ins. Co.*, 463 U.S. 29, 42-44 (1983).

207. See *NARUC III*, 880 F.2d 422, 430 (D.C. Cir. 1989).

208. See *California I*, 905 F.2d 1217, 1244 (9th Cir. 1990) (noting that the FCC can preempt state regulations requiring the use of separate facilities to provide enhanced services); *NARUC III*, 880 F.2d at 430 (noting that the FCC can preempt state regulations requiring bundling of basic service with CPE).

209. *California I*, 905 F.2d at 1244-45; *NARUC III*, 880 F.2d at 431.

210. This is consistent with the principle, established in the *Smith* case, see *supra* note 50, that in establishing the line of demarcation between federal and state authority "extreme nicety is not required, only reasonable measures being essential." *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133, 150 (1930).

service to one that disconnected intrastate calls only. In reaching its decision, the court deferred to the FCC's finding, based on the record, that it was not technically feasible to limit the service in that manner.²¹¹

The FCC also is not obligated to think of every conceivable method of narrowing its preemption orders. Thus, in the *ARCO* case, the D.C. Circuit declined to consider a suggestion by one of the intervening parties that the FCC could have narrowed its preemption order by requiring ARCO to limit the use of its interconnected microwave facilities to interstate calls. As the court observed, "[t]he FCC bears the burden of showing that its preemption order is necessary on the basis of the record developed before it. The Commission is not, however, required to anticipate any conceivable argument that might be raised by intervenors on appeal."²¹²

Finally, it seems indisputable that the FCC may exercise its preemptive power to protect all aspects of its interstate jurisdiction—including its Title I authority. The Communications Act does not expressly discuss the affirmative scope of the FCC's preemption power. Rather, preemption power is an adjunct to any lawful exercise of the FCC's authority. Thus, the FCC may preempt state regulations under Title I, just as it may under Title II. The only limitation is that, where common carriers are involved, the FCC's preemption power must be exercised in a manner that is consistent with Section 2(b)(1).

This conclusion has been repeatedly upheld in the courts. For example, the *Computer II* order preempting state regulation of CPE was adopted pursuant to the FCC's Title I authority.²¹³ This order was affirmed by the D.C. Circuit in *CCLA*, which specifically considered whether the FCC could preempt under its Title I power. In holding that it could, the court stated that it "perceive[d] no critical distinction between preemption by Title II regulation and preemption by the exercise of ancillary [i.e., Title I] jurisdiction."²¹⁴ Three subsequent D.C. Circuit decisions—*Illinois Bell*,²¹⁵ *NARUC III*,²¹⁶ and *Maryland PSC*²¹⁷—all upheld FCC preemption orders based on the Commission's Title I

211. *Maryland PSC*, 909 F.2d 1510, 1516 (D.C. Cir. 1990) (citing *In re Detariffing of Billing and Collection Servs.*, *Report and Order*, 102 F.C.C.2d 1150, paras. 27-29 (1986)); see *supra* notes 105-06 and accompanying text.

212. *ARCO*, 886 F.2d 1325, 1334 (D.C. Cir. 1989); see *supra* notes 108-11 and accompanying text.

213. *Computer II Final Decision*, *supra* note 40, paras. 122-84.

214. *CCLA*, 693 F.2d 198, 217 (D.C. Cir. 1982), *cert. denied*, 461 U.S. 938 (1983).

215. *Illinois Bell Tel. Co. v. FCC*, 883 F.2d 104 (D.C. Cir. 1989).

216. *NARUC III*, 880 F.2d 422 (D.C. Cir. 1989).

217. *Maryland PSC*, 909 F.2d 1510 (D.C. Cir. 1990).

authority.²¹⁸ The preemption order affirmed in *California III* had the same jurisdictional basis. As the Ninth Circuit recognized, these cases are fully consistent with the Supreme Court's decision in *Louisiana*.²¹⁹

2. The Principle Applied

By its terms, the limit on FCC preemption contained in Section 2(b)(1) of the Communications Act applies equally to state regulations governing "charges, classifications, practices, services, [or] facilities . . . [used] for or in connection with intrastate communication service."²²⁰ In practice, however, the FCC's preemption power may vary significantly from one area to another—depending on the feasibility of applying different rules within the federal and state jurisdictions.

At one extreme is the question of depreciation. As the *Louisiana* case makes clear, state imposition of a depreciation methodology to the jurisdictionally intrastate component of a telephone company plant imposes no impediment to the FCC's application of its own depreciation methodology to the interstate component.²²¹ There is, therefore, no room for FCC preemption in this area.

A second area in which the FCC appears devoid of preemptive authority is state regulation of *purely* intrastate carrier-provided services. An example of such a service might be a burglar alarm service that uses dedicated telephone lines to link residences within a state to a monitoring facility elsewhere within the same state. It is not clear how many purely intrastate carrier-provided communications services exist. Doubtless, however, there are some.²²² What is certain is that a state's decision to apply its own regulations to a purely intrastate carrier-provided service cannot oust the FCC of its jurisdiction over an interstate service. At most, state regulation of such a service could frustrate the implementation of a

218. *Illinois Bell* upheld an FCC order that preempted state regulation inconsistent with an FCC regulation requiring the BOCs to pay commissions to non-carrier CPE vendors that market BOC-provided Centrex service. *Illinois Bell*, 883 F.2d at 116. *NARUC III* upheld in part an FCC order that preempted state tariff regulation of carrier-provided inside wiring. *NARUC III*, 880 F.2d at 431. And *Maryland PSC* affirmed the preemption of Maryland state regulation of the rates of "DNP," a BOC-provided billing and collection service. *Maryland PSC*, 909 F.2d at 1517. All of these carrier-provided services are subject to the FCC's Title I jurisdiction.

219. *California III*, 39 F.3d 919, 932 (9th Cir. 1994), *cert. denied*, 1995 U.S. LEXIS 2435 (Apr. 3, 1995).

220. 47 U.S.C. § 152(b)(1) (Supp. V 1993).

221. See *supra* notes 69-73 and accompanying text.

222. See *California I*, 905 F.2d 1217, 1244 (9th Cir. 1990) (noting evidence that some alarm services, on-line educational database services, and voice mail services appeared to be offered on a purely intrastate basis).

federal policy—such as one favoring the non-regulated provision of enhanced services. Such policy differences, however, do not provide a sufficient basis for FCC preemption.

FCC preemption of state tariffs raises more difficult issues. The D.C. Circuit's decision in *NARUC III* contains language that suggests that, while it cannot preempt all state tariff regulation, the FCC could preempt state tariffs that would "interfere with the Commission's achievement of its valid goal[s]." ²²³ The court's emphasis on advancing the FCC's policy goals seems unsound. The relevant issue is whether imposition of state tariffing requirements on intrastate services, as a practical matter, would prevent the FCC from applying its rules at the interstate level.

In *NARUC III*, the FCC rule at issue required carriers to "detariff" the interstate component of inside wiring. Arguably, it would be possible—if a bit awkward—for the cost of the intrastate component of jointly used inside wiring to be recovered through tariffs, while the cost of the interstate component is recovered through competitively set prices. For example, a state could require that a specified amount of the revenue from carrier sales of inside wiring be applied to the carrier's intrastate regulated accounts. Such a requirement would be inconsistent with the federal policy favoring the detariffing of inside wiring. However, as long as the state tariff was cost-based, the FCC still could apply its rule requiring the cost of carrier-provided inside wiring to be recovered through market transactions, with the proceeds (in excess of the state tariff) assigned to the carrier's interstate unregulated accounts. ²²⁴

At the same time, however, there doubtless are situations in which the FCC may preempt state tariffing regulations. For example, as the D.C. Circuit concluded in *NARUC III*, the FCC was plainly within its authority to preempt state tariff provisions that bundle inside wiring with basic transmission service. ²²⁵ Inside wiring either is, or is not, provided as part of the regulated transmission service. Requiring the "intrastate component" to be provided as part of the regulated transmission offering inevitably would prevent application of the FCC's rule requiring the unbundling of the "interstate component" of inside wiring from the basic interstate common carrier network.

Outside of the tariffing area, the FCC's ability to preempt state regulations of carrier-provided services seems considerably greater. Many state rules govern the terms and conditions under which a communications

223. *NARUC III*, 880 F.2d 422, 430 (D.C. Cir. 1989); see *supra* notes 75-78 and accompanying text.

224. See *id.*

225. *Id.* at 431.

service will be provided or the obligations of the carrier to do, or refrain from doing, a particular act. The FCC's structural separation requirements and nonstructural safeguards plainly fall within this category. In some cases, simultaneous compliance with inconsistent federal and state rules will be a literal impossibility. In many other instances, there will be no practical way for the carrier to comply with inconsistent rules. In either situation, the FCC has ample authority to protect its plenary jurisdiction over interstate communications services through the use of its preemption power.

III. KEEPING THE PEACE

The principles outlined above provide a basis on which the FCC and the states can move forward cooperatively. At the same time, however, it is only natural to anticipate that, as the communications market continues to develop, new issues of intergovernmental relations will need to be addressed. Four of these issues are described below.

A. *Inseverability and the Intelligent Network*

One situation in which FCC preemption is permissible occurs when the inability to *physically* separate the interstate and intrastate components of a given facility or service makes it impossible for divergent federal and state regulation to exist. This situation is sometimes referred to as "inseverability."²²⁶

This situation is illustrated by the *Georgia PSC* and *Maryland PSC* cases. In *Georgia PSC*, the Eleventh Circuit affirmed the FCC's conclusion that there was no possible way, given current technology, to prevent the use of BellSouth's voice messaging service, MemoryCall, in connection with intrastate calls, while allowing the service to be used in connection with interstate calls.²²⁷ Similarly, in *Maryland PSC*, the D.C. Circuit deferred to the FCC's finding that it would not be technically possible for an LEC to offer a service that cuts off customers' ability to use their telephone for

226. Physical inseverability, it should be noted, does not always provide a basis for FCC preemption. FCC preemption is permissible only if physical inseverability makes it impractical for the FCC to apply its regulations to interstate facilities or services. The telephone company plant at issue in *Louisiana*, for example, could not be physically "severed" into discrete interstate and intrastate components. Yet, because the jurisdictional separations process provided a means to apply divergent federal and state depreciation rates, the Supreme Court held that the FCC's order preempting state regulation of carrier depreciation rates was unlawful. See *supra* notes 69-73 and accompanying text.

227. See *MemoryCall Preemption Order*, *supra* note 142, para. 19 ("[I]t is impossible as a practical matter to separate the interstate and intrastate provision of [MemoryCall] to permit effectuation of the *Georgia Order* only for the intrastate provision of the service."); see *supra* notes 148-56 and accompanying text.

intrastate telephone calls, while allowing them to continue to have full use of their telephones for interstate calls.²²⁸ Because it was not possible to limit the physical consequence of state regulation to the intrastate sphere, the courts held that the FCC could preempt state regulations that were inconsistent with the Commission's rules.

Technology is not static. The introduction of new "advanced intelligent network" features, such as Signaling System 7, has increased the capabilities of the carriers' networks.²²⁹ If it is not here already, there will soon come a time when technology makes it possible to determine the jurisdictional nature of any communication. Once this occurs, it will be possible for a carrier to offer an "interstate only" voice messaging service or an "intrastate only" telephone disconnection service, thereby making divergent federal and state regulation physically possible. These technological developments will require the courts to rethink the validity of cases such as *Georgia PSC* and *Maryland PSC*.

One possibility is that the courts will conclude that—where technological advances make physical separation of federal and state components of a facility or service possible—FCC preemption is no longer permissible. That, however, is not the inevitable result. The courts may, for example, decline to require carriers to make use of new technologies to physically separate interstate and intrastate facilities services if the FCC concludes that doing so would be unreasonably costly or would degrade network efficiency.²³⁰

Even if technology makes it practical to physically separate additional services into intrastate and interstate offerings, the courts still might find

228. See *Maryland PSC*, 909 F.2d 1510, 1516 (D.C. Cir. 1990) (citing *In re Detariffing of Billing and Collection Servs., Report and Order*, 102 F.C.C.2d 1150, paras. 27-29 (1986)); see *supra* notes 108-11 and accompanying text.

229. Signalling System 7 has been described as "a form of out-of-band signaling between switches (i.e., signaling separate from the call itself) that dramatically reduces call set-up time, permits queries to centralized databases in the processing of calls, and permits the introduction of such services as Caller ID." KELLOGG ET AL., *supra* note 6, § 11.6.1 n.16.

230. The FCC previously has concluded that requiring carriers to deploy:
expensive additional equipment simply because of jurisdictional conflicts would violate our congressional mandate in Section 1 of the Communications Act to regulate "interstate and foreign commerce in communication by wire or radio so as to make available, so far as possible, to all people of the United States a rapid, efficient, Nation-wide and world-wide wire and radio communications service with adequate facilities at reasonable charges."

In re American Tel. & Tel. Co. & the Associated Bell Sys. Cos. Interconnection with Specialized Carriers in Furnishing Interstate Foreign Exchange (FX) Serv. and Common Control Switching Arrangements (CCSA), *Memorandum Opinion and Order*, 56 F.C.C.2d 14, para. 17 (1975) (quoting 47 U.S.C. § 151 (1970), current version at 47 U.S.C. § 151 (1988)).

that federal preemption is permissible where—as a practical matter—the service could be marketed only on a jurisdictionally mixed basis. As the D.C. Circuit observed in *Illinois Bell*, “[m]arketing realities might themselves create inseparability.”²³¹ Again, the *Georgia PSC* case provides a ready example. A good argument can be made that a voice messaging service that only stores messages that originate out-of-state would not be commercially viable. Therefore, a state regulation that prevents a carrier from offering voice messaging service for use in connection with intrastate calls, as a practical matter, also would prevent it from offering such a service in connection with interstate calls. Because this would preclude application of the FCC’s rules allowing for the provision of interstate voice messaging service, federal preemption might still be appropriate.

B. “Jurisdictional Forbearance” After *MCI v. AT&T*

One way in which conflicts between sovereigns are sometimes avoided is through the exercise of comity. In effect, one sovereign recognizes that—while it has jurisdiction in a given area—it will decline to assert its authority in the interest of good relations with the other sovereign.²³² Within our federal system, such arrangements also can promote administrative efficiency.

The FCC has deferred to state regulations in numerous areas. For example, the FCC has declined to require federal tariffing of certain LEC-provided services, such as Centrex or call waiting, even though these services can be used in conjunction with both interstate and intrastate communications.²³³ Similarly, the Commission has declined to assert authority over private line networks on which less than 10 percent of the traffic is jurisdictionally interstate.²³⁴

The recent decision of the Supreme Court in *MCI Telecommunications Corp. v. AT&T*²³⁵ calls into question the continued ability of the FCC to

231. *Illinois Bell Tel. Co. v. FCC*, 883 F.2d 104, 113 n.7 (D.C. Cir. 1989).

232. The Supreme Court first recognized the concept of international comity in *The Schooner Exchange v. McFaddon & Others*, 11 U.S. (7 Cranch) 116, 144 (1812).

233. See *ONA Order*, *supra* note 149, para. 85 n.156 (noting that services such as “call forwarding and call waiting often are tariffed with states,” but that the FCC had jurisdiction to apply federal ONA requirements to them); *Illinois Bell*, 883 F.2d at 114 (noting that, while the costs of Centrex service are recovered through local tariffs, “this regulatory accounting treatment does not negate the mixed interstate-intrastate character” of the service).

234. See *In re MTS and WATS Mkt. Structure, Decision and Order*, 4 FCC Red. 5660 (1989).

235. *MCI*, 114 S. Ct. 2223 (1994).

decline to regulate jurisdictionally interstate services in the interest of comity. In *MCI*, the Court struck down the FCC's "permissive detariffing" policy, under which the Commission did not enforce the requirement, contained in Section 203 of the Communications Act, that "[e]very common carrier" shall provide interstate basic telephone service pursuant to filed tariffs.²³⁶ The FCC sought to justify its "forbearance" policy on the grounds that exempting "non-dominant carriers" from the tariff filing requirement would promote competition.²³⁷ The Court flatly rejected this argument. "Compliance with [the statutory tariffing] provisions," the Court held, "is utterly central to the administration of the Act."²³⁸ The FCC did not have authority to ignore this requirement in order to achieve its policy goals.²³⁹

Comity, it can be argued, is a kind of forbearance: the FCC declines to regulate basic common carrier service—plainly subject to its jurisdiction under Title II—in order to advance a policy goal, such as better relations with the states or administrative efficiency. The Supreme Court's decision in *MCI v. AT&T* could be read to suggest that such a course of action is impermissible because it ignores the mandatory requirement in the Communications Act that interstate basic services be provided pursuant to federal tariffs. On the other hand, it is possible to distinguish the two situations. The FCC's "permissive detariffing" policy sought to eliminate tariff regulation of more than 40 percent of all interstate basic services. Here, in contrast, the FCC is merely *transferring administration* of certain categories of rate regulation from the federal to the state level. This

236. 47 U.S.C. § 203 (1988) (emphasis added).

237. The term "non-dominant carrier" refers to a provider of basic telephone service that lacks market power, defined as the ability to restrict output and keep prices above competitive levels. See *In re Policy and Rules Concerning Rates for Competitive Common Carrier Servs.*, *First Report and Order*, 85 F.C.C.2d 1, paras. 54-65 (1980). This term includes all long distance carriers other than AT&T, which continues to have approximately a 60% share of the interexchange market. FCC, INDUSTRY ANALYSIS DIV., LONG DISTANCE MARKET SHARE THIRD QUARTER 9 (1994). In the *Competitive Carrier* proceeding, the Commission concluded that requiring non-dominant carriers to file tariffs is unnecessary, because such carriers lack the power to charge unreasonable or discriminatory prices, and counter-productive, because it can facilitate oligopolistic pricing. See *In re Policy and Rules Concerning Rates for Competitive Common Carrier Servs.*, *Second Report and Order*, 91 F.C.C.2d 59 (1982), *reconsideration denied*, 93 F.C.C.2d 54 (1983).

238. *MCI*, 114 S. Ct. at 2231 (quoting *Maislin Indus., U.S. v. Primary Steel*, 497 U.S. 116, 132 (1990)).

239. *Id.* at 2233; see also *Southwestern Bell Corp. v. FCC*, 43 F.3d 1515, 1519 (D.C. 1995) ("Congress enacted the Communications Act and the mandates of the Act are not open to change by the Commission The Commission may not . . . ignore congressional directives because it believes 'traditional tariff regulation' is 'unnecessary' and 'counter-productive.'").

distinction may provide a sufficient basis for the continuation of the FCC's comity policy.

C. *Jurisdiction Over Telephone Company-Provided Video Services*

Congress created the rules governing federal-state relations in an age in which communications and voice telephony were nearly synonymous. The convergence of communications and computing during the 1970s and 1980s required the courts and the FCC to apply these rules to enhanced services. The impending "multimedia convergence"—which will see the combination of telephony, consumer electronics, and video programming—doubtless will raise new issues about the division of regulatory authority between the FCC and the states.

For the last several years, the FCC has been developing a regulatory regime designed to allow LECs to enter the video programming market in order to provide a competitive alternative to cable service, which generally is provided on a monopoly basis. The ability of the LECs to do so has been limited, however, by the terms of the "cross-ownership" restriction contained in the Cable Communications Policy Act of 1984, which prevents an LEC from providing "cable service" in its telephone service area.²⁴⁰ To get around this restriction, the FCC in the late 1980s developed the concept of "video dialtone." The notion was that—while the cross-ownership ban precluded them from acting as video program "packagers"—the LECs could act as conduits, delivering programming provided by others. In so doing, the FCC reasoned, LECs would simply be performing their traditional common carrier role.²⁴¹

The *Video Dialtone Second Report and Order*²⁴² considered the division of authority between the FCC and the states regarding video dialtone. The FCC initially concluded that video dialtone was a *purely* interstate service. In reaching this decision, the Commission analogized video dialtone to early cable systems, in which physically intrastate telephone company "channel service" was used to deliver broadcast

240. Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2779 (codified as amended in scattered sections of 47 U.S.C.).

241. See *In re Telephone Co.-Cable TV Cross-Ownership Rules, Further Notice of Proposed Rulemaking, First Report and Order and Second Further Notice of Inquiry*, 7 FCC Rcd. 300 (1991), *reconsidered*, 7 FCC Rcd. 5069 (1992), *aff'd*, National Cable TV Ass'n v. FCC, 33 F.3d 66 (D.C. Cir. 1994).

242. *In re Telephone Co.-Cable TV Cross-Ownership Rules* §§ 63.54-63.58, *Second Report and Order, Recommendation to Congress, and Second Further Notice of Proposed Rulemaking*, 7 FCC Rcd. 5781 (1992) [hereinafter *Video Dialtone Second Report and Order*], *aff'd*, National Cable TV Ass'n v. FCC, 33 F.3d 66 (D.C. Cir. 1994).

signals—which are subject to exclusive federal regulation²⁴³—to end-users. Like channel service, the FCC declared, an LEC's video dialtone facility is an “integral component in an indivisible dissemination system which forms an interstate channel of communication” and, therefore, is subject to exclusive federal regulation.²⁴⁴

The states promptly responded, correctly observing that video dialtone is not simply channel service: the content is not limited to retransmitted broadcast signals, and, moreover, some of the video content originates and terminates exclusively within a single state.²⁴⁵ Recognizing its error, the FCC pulled back. “[W]e have exclusive jurisdiction,” the Commission announced on remand, “over all [interstate] video dialtone services . . . [S]tates have jurisdiction over the delivery by wire of video programming . . . within the same state”²⁴⁶

The devil, as always, is in the details. In its *Video Dialtone Reconsideration Order*, the FCC concluded that the states' jurisdiction over intrastate video dialtone service is limited to situations—such as the operation of a “video library”—in which video program originates at one location within a state and is delivered, *by wire*, to another point within the same state.²⁴⁷ Any transmission involving radio, the Commission insisted, remains subject to exclusive federal regulation. While the *Reconsideration Order* is a step in the right direction, it may not go far enough. In the *FM Subcarrier Case*, the D.C. Circuit held that the states have jurisdiction over the common carrier aspects of intrastate radio.²⁴⁸ Video dialtone service, by definition, is the common carriage of video signals. The FCC's decision to assert jurisdiction over the common carriage by radio of intrastate video dialtone programming is hard to square with the D.C. Circuit's ruling.

The relationship between the FCC and the states in this area is likely to become more complex. In the last year, courts in five circuits have struck down the cable-telco cross-ownership restriction as unconstitu-

243. The Court has long held that broadcasting is subject to exclusive FCC jurisdiction. See, *Turner Brdcast Sys., Inc. v. FCC*, 114 S. Ct. 2445, *reh'g denied*, 115 S. Ct. 30 (1994); *Metro Brdcast., Inc. v. FCC*, 497 U.S. 547 (1990); *CBS, Inc. v. Democratic Nat'l Committee*, 412 U.S. 94 (1973); *Red Lion Brdcast. Co. v. FCC*, 395 U.S. 367 (1969).

244. *Video Dialtone Second Report and Order*, *supra* note 242, para. 72 (quoting *General Tel. Co.*, 413 F.2d 390, 401 (D.C. Cir. 1969)).

245. *In re Telephone Co.-Cable TV Cross-Ownership Rules, Memorandum Opinion and Order on Reconsideration and Third Further Notice of Proposed Rulemaking*, 10 FCC Rcd. 244, paras. 113-19 (1994).

246. *Id.* para. 123.

247. *Id.*

248. The *FM Subcarrier Case* is described *supra* note 74.

tional.²⁴⁹ As a result, most LECs have obtained the right to package their own programming and deliver it directly to subscribers. Arguably, this will allow the LECs to act as cable systems operators, rather than common carriers.

The provision of cable service is governed by Title VI of the Communications Act.²⁵⁰ The jurisdictional division of authority is significantly different in Title VI than it is in Title II. In essence, Title VI gives the states the right to franchise cable systems, but requires them to regulate cable service pursuant to specific federal directives governing the prices, terms, and conditions of service. The net result is that—if LEC-provided video programming is regulated as cable service—states may lose authority to adopt regulations governing even purely intrastate LEC-provided video programming.²⁵¹ The fact that an LEC may provide such programming over the same facilities that it uses to provide basic intrastate telephone service further complicates matters.

D. Jurisdiction Over Non-Carrier Communications Facilities and Services

As a result of the growth of competition during the last decade, many functions—such as the provision of CPE, inside wiring, and enhanced services—that once were performed exclusively by telephone companies are now also performed by entities whose main business is not the provision of basic telephony.²⁵² The ability of the FCC and the states to exercise regulatory authority over these “non-carriers” has yet to be explored by the courts.

Non-carriers, by definition, are not common carriers. Therefore, they are not subject to federal regulation under Title II of the Communications

249. *US West v. United States*, No. 94-35775 (9th Cir. Dec. 30, 1994); *Chesapeake & Potomac Tel. Co. v. United States*, 42 F.3d 181 (4th Cir. 1994); *NYNEX Corp. v. United States*, 153 F.R.D. 1 (D. Me. 1994); *Ameritech Corp. v. United States*, 867 F. Supp. 721 (N.D. Ill. 1994); *BellSouth Corp. v. United States*, 868 F. Supp. 1335 (N.D. Ala. 1994).

250. 47 U.S.C. §§ 521-613 (1988 & Supp. V 1993).

251. The FCC recently issued a *Notice of Proposed Rulemaking* seeking comment on the extent to which LECs that provide their own programming should be regulated pursuant to Title II, Title VI, or some combination thereof. *See In re Telephone Co.-Cable TV Cross-Ownership Rules, Fourth Further Notice of Proposed Rulemaking*, CC Dkt No. 87-266, paras. 9-17 (Jan. 20, 1995).

252. Indeed, in many segments of the market, non-carriers are the leading provider. *See, e.g., OFFICE OF INDUSTRIES, U.S. INTERNATIONAL TRADE COMMISSION, INDUSTRY & TRADE SUMMARY: TELECOMMUNICATION EQUIPMENT 5* (Oct. 1994) (listing selected U.S. firms in the telecommunications industry). One reason for this situation is that, under the terms of the Modification of Final Judgment, *see supra* note 57, the BOCs are prohibited from manufacturing telecommunications equipment and CPE.

Act. Any authority that the FCC has in this area must be grounded in Title I, which authorizes the FCC to regulate interstate "wire and radio communication."²⁵³ The extent to which non-carrier-provided services and equipment can be classified as "communications," however, is unsettled.²⁵⁴

The FCC has avoided the difficult problem of determining the extent of its Title I jurisdiction over non-carriers by deregulating all enhanced services, CPE, and inside wiring at the federal level.²⁵⁵ The states, too, generally have not sought to subject non-carrier-provided equipment and services to regulation. However, some states have suggested that they might be interested in asserting regulatory authority over the intrastate activities of non-carriers in certain instances—especially in the enhanced services

253. 47 U.S.C. § 151 (1988). The extent of the FCC's Title I authority is discussed *infra* note 255.

254. In the *First Computer Inquiry*, the FCC tried to establish a clear line of demarcation between communications, which was to be subject to FCC regulation, and "data processing," which was not. See *In re Regulatory and Policy Problems Presented by the Interdependence of Computer and Comm. Servs. and Facils., Final Decision and Order*, 28 F.C.C.2d 267, paras. 5-11 (1971), *aff'd sub nom. GTE Serv. Corp. v. FCC*, 474 F.2d 724, 732-36 (2d Cir. 1973). Over time, however, it became clear that the dividing line between the two could not be precisely established. For example, enhanced services combine carrier-provided transport service with computer processing applications. Similarly, CPE can facilitate communications and provide information storage and processing applications.

255. See *Computer II Final Decision*, *supra* note 40, paras. 25-26. While the FCC's decision not to regulate these services has obviated the need to determine the extent of the FCC's jurisdiction, a reasonable argument can be made that at least some types of non-carrier-provided CPE, inside wiring, and enhanced services constitute communications facilities and services and, therefore, are subject to its Title I jurisdiction. That is not to say that the FCC's Title I authority is unlimited. To the contrary, as the Supreme Court has observed, the FCC's Title I authority is "restricted to that reasonably ancillary to the Commission's various responsibilities." *United States v. Southwestern Cable Co.*, 392 U.S. 157, 178 (1968). For example, the FCC presumably could not impose the full array of Title II tariff requirements on a service that was subject to its Title I authority. See *California I*, 905 F.2d 1217, 1240 n.35 (9th Cir. 1990) ("[Title I] confers on the FCC such power as is ancillary to its specific statutory responsibilities."); see also *Computer II Final Decision*, *supra* note 40, para. 126 ("Even though an activity falls within [the FCC's Title I] jurisdiction, [the FCC's] ability to subject it to regulation is not without constraints [C]ommission regulation must be directed at protecting or promoting a statutory purpose. In some instances, that means not regulating at all").

area.²⁵⁶ This raises the question of whether, if a state were to adopt such a policy, the FCC could exercise its preemptive authority.

The ability of the FCC to displace inconsistent state regulations is, of course, circumscribed by Section 2(b)(1). However, the Ninth Circuit's statement, in *California I*, that Section 2(b)(1) "applies to communications services provided by common carriers . . . as distinguished from communications services provided by non-carriers"²⁵⁷ suggests that the provision does *not* limit FCC jurisdiction over non-carriers. Where Section 2(b)(1) does not apply, the Supreme Court has recognized that the FCC has plenary power to "pre-empt any state or local law that conflicts with [valid federal] regulations or frustrates the purposes thereof."²⁵⁸ A strong argument can be made, therefore, that the FCC could preempt all state regulation of non-carrier-provided communications equipment and services.²⁵⁹

This interpretation does lead to a somewhat anomalous result: the FCC's ability to preempt state regulation of carrier-provided communications equipment and services (over which the FCC has clear authority) is limited, while its ability to preempt state regulation of non-carrier-provided communications equipment and services (where its authority is more uncertain) is plenary. The fact that this result is anomalous does not, of course, mean that it is incorrect.

CONCLUSION

This Article has proposed principles governing relations between the FCC and the states. These principles recognize the right of the Federal Communications Commission and the states to pursue divergent policies, provided that the two sovereigns remain within their respective juris-

256. See Investigation of the Regulation of Enhanced Services, Formal Case No. 904, Order to Show Cause (D.C. PSC Oct. 31, 1990) (directing all ESPs within the District of Columbia to show cause why they should not be subject to local common carrier regulation); Testimony of California Public Utilities Commission Chairman C. Mitchell Wilk, En Banc Hearing: Networks of the Future (FCC May 1, 1991) (suggesting that, under California law, it might be obligatory to regulate "hundreds" of firms that "offer computer-related services").

257. *California I*, 905 F.2d at 1240.

258. *City of N.Y. v. FCC*, 486 U.S. 57, 64 (1988) (upholding the FCC's preemption of state regulations governing cable signal standards even though there was no conflict with federal law).

259. In a petition filed in 1991, a group of non-carrier ESPs asked the FCC to rule that, in *Computer II*, it had preempted state regulation of non-carrier-provided enhanced services and that the Ninth Circuit's subsequent vacation of the *Computer III Orders* reinstated this decision. See Petition for a Declaratory Ruling that States and the District of Columbia Are Preempted from Imposing Public Utility Regulation on Enhanced Service Providers, *Public Notice*, 6 FCC Rcd. 1363 (1991). The FCC has never acted on this petition.

dictions. They also recognize that, in cases in which divergent federal and state regulations cannot practically coexist, state regulation must give way—but only to the extent necessary to avoid encroaching on the federal domain. By adopting these principles, the FCC and the states can put an end to their internecine conflict. The time has come to give peace a chance.