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The Telecommunications Act of 1996, the Takings Clause, and Tensions in Property Theory

Eric R. Claeys

This Article draws on general takings scholarship to evaluate the telecommunications law and scholarship to date on takings challenges to the local-exchange provisions of the Telecommunications Act of 1996. Recent cases and scholarship have proposed many different rules of decision for these takings challenges: "per se" categorical pro-compensation rules, confiscatory-ratemaking formulas, and "ad hoc" interest-balancing formulas. The authorities that have advanced each of these proposals are to a large degree informed by contestable assumptions about the nature of property and its constitutional protection. Takings law and scholarship both reflect deep disagreements between two overarching understandings of property—a Libertarian worldview and a Legal Realist worldview. These general understandings help make sense of and give context to many of the specific legal arguments advanced in the context of the takings challenges to the 1996 Act. But to the extent that telecommunications lawyers and scholars are relying on one or the other of these general understandings, their arguments are no more persuasive than their general understandings are valid. Although this Article cannot resolve the disputes about the 1996 Act definitively, the Article does help identify the questions central to the takings analysis, by showing how sound takings doctrine integrates the narrow concerns of telecommunications policy with the broader concerns of constitutional property theory.

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Introduction

This Article examines the use and abuse of takings property theory in the specialized telecommunications law and scholarship about local-exchange takings claims. Congress significantly transformed the structure of federal telecommunications regulation in the Telecommunications Act of 1996 ("the Act," or "the 1996 Act"). In the same year, the Federal Communications Commission promulgated regulations to execute the provisions of the Act that restructured the market for local phone service throughout the United States. These statutes and regulations require the Baby Bells and other local-exchange carriers ("the incumbents") to interconnect their local exchanges to the facilities of competing local-service providers ("the competitors"). These duties, in turn, raise serious claims for just compensation under the Takings Clause, which guarantees that "private property" may not "taken for public use without just compensation." In the 2002 decision Verizon Corp. v. FCC, the Supreme Court declined to speak broadly to the merits of these takings claims, instead encouraging the incumbents to litigate such claims state by state in ongoing proceedings.

Although virtually all the legal authorities contend that these takings issues are quite simple and admit of only one answer, they still propose three different answers. Some authorities have claimed that the incumbents' constitutional claims raise questions within the framework of confiscatory-ratemaking doctrine, which guarantees regulated utilities the power to recover their capital and a reasonable rate of return. Other authorities have suggested that when the Act requires incumbents to interconnect their competitors to local exchanges, it inflicts a regulatory burden tantamount to a "classic physical taking," which per se entitles the incumbents to just compensation worth the going market value of the physical infrastructure and access rights taken. A few

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3 U.S. CONST. amend. V.
courts and commentators have suggested that the FCC's rate regulations are innocuous under strongly deferential "regulatory-takings" principles associated with the Supreme Court's decision in *Penn Central Transportation Co. v. City of New York.* Those three frameworks—confiscatory ratemaking, per se compensation, and *Penn Central* interest balancing—exhaust all the important possibilities in takings law. It is strange that all the authorities seem so certain that the legal issues are easy to settle and yet remain so widely divided on how to settle them.

This Article suggests that the various authorities diverge sharply because they presuppose different and quite contestable views about property, its regulation, and its proper constitutional protection. The law and scholarship specific to post-*Verizon* takings claims is influenced to a striking degree by the worldviews lawyers and scholars choose to embrace in relation to property and takings. Of course, overarching theories of property policy and behavior do not and cannot prescribe outcomes in specific policy disputes by themselves. The particulars of such disputes matter at least as much as the general worldviews that policy makers might apply. Even so, a policy maker's worldview can subtly affect policy analysis in a specialized field like telecommunications. To oversimplify slightly, the choice of approach can act as a tie-breaker. Different approaches create different default presumptions to decide issues—in favor of government action or inaction, or of compensation or no compensation—when a judge or industry specialist runs out of more specific factual information and can no longer apply policy expertise to fill the gaps.

To illustrate such dependencies, this Article shows how different authorities rely on two principled theoretical positions in the law and scholarship on takings. One is called the "Libertarian" view, for it lays out principles of regulation and just compensation that govern takings law if government's overriding goal ought to be to protect and cultivate free initiative and action through property rights. The other perspective is herein called, for want of a better term, the "Legal Realist" view. This label is probably inaccurate in some respects, because many of the key claims of this view have emerged in takings law and scholarship only in the last quarter century. At the same time, many of its key claims draw heavily on ideas about property and

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7 438 U.S. 104 (1978). For examples of these authorities, see Texas Office of Public Utility Counsel v. FCC, 183 F.3d 393, 429 (5th Cir. 1999) (suggesting, in dicta relating to a company's takings challenge to the 1996 Act, that the claim lacked merit under *Penn Central*'s three-part interest balancing); Paul W. Garnet, Forward-Looking Costing Methodologies and the Supreme Court's Takings Clause Jurisprudence, 7 COMM. LAW CONSPECTUS 119, 122 n.19 (1999) (suggesting that recent Supreme Court rate-of-return takings cases have applied a test mirroring the standards that apply to land-use regulatory-taking challenges); and Michael J. Legg, Verizon Communications, Inc. v. FCC—Telecommunications Access Pricing and Regulator Accountability Through Administrative Law and Takings Jurisprudence, 56 FED. COMM. L.J. 563, 581-84 (2004) (analyzing post-*Verizon* takings claims within the parameters of *Penn Central*'s factors).
regulation that originated during the Legal Realist era.\footnote{I have demonstrated how contemporary takings doctrine depends on Legal Realist theory in Eric R. Claeys, \textit{Takings and Private Property on the Rehnquist Court}, 99 NW. U. L. REV. 187, 191-93, 216-19 (2004).} This approach captures many assumptions about takings that follow if the institution of private property needs to be reconciled to the redistributive and welfarist aims of the post-New Deal regulatory state. To be sure, the Libertarian and Realist approaches do not exhaust all the different ways in which takings law may be understood. Nevertheless, both have respectable pedigrees in takings precedent. Libertarian ideas heavily influenced takings and substantive due process property-rights law throughout the nineteenth century, and they predict the arguments to which courts appeal today on the few occasions when the Supreme Court concludes that governments have inflicted takings. Realist ideas developed during the early twentieth century in large part in response to the Libertarian influences in the law at the time, influences which impeded the growth of the modern regulatory state.\footnote{See id. at 191-99.} Tensions between these two views inform many contemporary debates about takings in contemporary scholarship.\footnote{Compare \textit{id.} (advocating an approach to regulatory-takings law consistent with Libertarian principles), with Stewart E. Sterk, \textit{The Inevitable Failure of Nuisance-Based Theories of the Takings Clause: A Reply to Professor Claeys}, 99 NW. U. L. REV. 231 (2004). Compare Frank Michelman, \textit{Takings}, 1987, 88 COLUM. L. REV. 1600, 1628 (1988) (describing Libertarian takings decisions in terms of their "obtuseness"), with Douglas W. Kmiec, \textit{The Original Understanding of the Taking Clause Is Neither Weak nor Obsolete}, 88 COLUM. L. REV. 1630 (1988).}

If Libertarian principles govern the key questions about the 1996 Act, the law takes a per se approach to the takings issues and a ratemaking approach to just compensation. The 1996 Act preempts incumbents' exclusive-franchise agreements under state and local law and requires the incumbents to interconnect competitors to their local exchanges. Under the Libertarian approach, those legal changes inflict per se takings because they extinguish different aspects of the incumbents' rights to exclude. Ratemaking principles then shape the incumbents' just compensation. The compensation comes primarily from the discounted present value of the rates that the incumbents would have recovered in state ratemaking proceedings if the 1996 Act had not terminated those proceedings. These specific rules about takings and just compensation err on the side of encouraging long-term investment in local exchanges and else where. In telecommunications, as in other utilities, there always exists a strong danger that regulators may discourage long-term utility investment by using the power to regulate to expropriate capital. If takings law provides a per se guarantee that incumbents will recover as just compensation any stranded costs that they cannot recover in ratemaking, it encourages long-term investment in telecommunications and other regulated industries.

On the other hand, if Realist principles govern the relevant questions, it is also easy to generate an account quite deferential to Congress and the FCC. On
The Telecommunications Act of 1996

this account, the 1996 Act treats incumbents as innocuously as rent-control regulations treat landlords. It leaves the incumbents with a wide zone of freedom to profit in the telecommunications sector, and it provides them with new and valuable benefits, including rights to charge competitors for access to their local exchanges and the long-sought right to compete in long-distance markets. The overarching deferential framework expresses a strong preference for different policy goals: takings law need not compensate incumbents as extensively as the Libertarian view insists in order to guarantee efficient long-term investment in utility infrastructure. If anything, such compensation rules frustrate more immediate and concrete goals, in this case competition in the market for local landline phone service.

These connections and results do not refute or disprove any of the current law and scholarship on the takings issues raised by the 1996 Act. However, they do suggest that the relevant issues are more complicated than has been suggested to date, for at least two reasons. One is doctrinal. Although most commentators treat per se takings, ad hoc Penn Central takings, and confiscatory ratemaking takings as three separate doctrinal categories, in reality it is difficult to distinguish each category from the others.11 These categories are useful at a broad level, but it is hard to reconcile them or prevent them from overlapping. In large part, the tensions exist because different cases and lines of doctrine embrace either the Libertarian or Realist approaches. As a result, it is perilous to apply the various doctrines as fixed black-letter law. Even diehard doctrinalists must account for the influence of Libertarian and Realist ideas.

The second complicating factor is that telecommunications scholarship and takings scholarship seem to have different objectives. From my limited experience with the literature, telecommunications scholarship seems to be a field guided by what James Landis called "expertness," a standard for policymaking and scholarship according to which "the art of regulating an industry requires knowledge of the details of its operation."12 The scholarship to date about the 1996 Act, for instance, tends to focus on the policy questions most directly connected to the Act's local-interconnection provisions. Because this scholarship focuses on immediate policy questions, it tends to treat takings doctrine as one of several available instruments to use to solve the most specific and urgent problems in the telecommunications industry. By its focus and interests, then, scholarship about the 1996 Act tends to postpone or defer other questions that preoccupy takings scholarship—more abstract and comprehensive political-theory questions about property, regulation, and constitutionalism. Because these two bodies of scholarship focus on different

11 David Dana and Thomas Merrill restate the conventional doctrinal wisdom and highlight many of its ambiguities in David A. Dana & Thomas W. Merrill, Property: Takings 86-168 (2002). As they cogently explain, the worst problems arise when determining how to reconcile confiscatory-ratemaking doctrine with the other two categories. See id. at 164-68.

questions, they also seem to pay different degrees of respect to different kinds of knowledge. While the relevant telecommunications scholarship seems to stress specialized knowledge about the telecommunications industry or the overarching economic problems in that industry, takings scholarship often deals with comprehensive behavioral or normative claims. The takings claims associated with the 1996 Act raise several questions so far-reaching. Perhaps generous just compensation will broadly encourage investment and innovation, in telecommunications and elsewhere, by sending a strong message that capital is secure in regulated industries; perhaps such compensation will instead send a message that regulated industries can make it expensive and therefore impossible for Congress to reform industries to encourage competition or other pressing goals. Many of the relevant telecommunications articles to date tend to downplay these broader considerations—perhaps because, by the standards of telecommunications scholarship, these considerations are hard to quantify and take a long time to surface. In doing so, however, such articles make a tradeoff: by looking only where the light is, they risk missing something important lurking in the dark.

As a result, this Article helps readers who follow telecommunications law or takings law evaluate this debate more critically than the case law and scholarship thus far on the 1996 Act. Many of the most relevant cases and scholarly authorities assume that the leading takings cases prescribe more certain results than those cases really do. Perhaps these cases and authorities underestimate the conflicts in the doctrine; if not, they are probably assuming that the doctrine advances firm normative positions when in reality the doctrine reflects deep normative disagreements stemming from the political questions raised in scholarship on takings. And if such claims are hotly contested in the takings literature, by all rights those claims should be subject to even more rigorous examination according to the technical and expertise-driven expectations of telecommunications scholarship. Even if this Article does not settle the most important policy questions, then, it does highlight important limitations in the scholarship to date and it clarifies the overarching issues.


The takings lawsuits in question arose out of a quid pro quo effectuated by the Telecommunications Act of 1996. Incumbent local-exchange carriers received permission to provide long-distance service in competition with AT&T, MCI, and other long-distance services, on condition that they relinquished the dominant positions they enjoyed in local markets as franchisees. On the long-distance side, previous law had barred incumbents created from the AT&T break-up from providing long-distance service. The

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13 See, e.g., CHARLES H. KENNEDY, AN INTRODUCTION TO U.S. TELECOMMUNICATIONS LAW 54-60 (1st ed. 1994).
The 1996 Act opened up long-distance markets to those incumbents, provided that they demonstrated to the FCC's satisfaction that they met a fourteen-point statutory checklist.  

The 1996 Act opened up local markets along similar lines. Before 1996, local telephone service was largely a regulated monopoly. While one must be careful not to over-generalize about how regulators in different states and localities regulated local phone service, all regulated by some combination of contractual franchise and public-utility regulation, with more of the former earlier and more of the latter later. (In this regard, changes in phone regulation broadly tracked changes in franchise regulation generally.) Usually, state or local utility regulators gave franchises to local-exchange carriers—to AT&T before its break-up in 1983 and to the Bell Operating Companies and other incumbent local-exchange carriers thereafter. Consistent with traditional principles of utility regulation, state utilities regulated the incumbents' rates to customers for intrastate service. It also gave the incumbents exclusive franchise monopolies within their territories. Before 1996, AT&T and the incumbents owed a few targeted duties to interconnect outsiders to their local exchanges. The primary duties were to carry interexchange carriers (long-distance companies that needed to connect to local exchanges to reach their customers) and competitive access providers (which connect end users to interexchange carriers through dedicated lines off of the local exchanges). However, in other respects, the incumbents' franchise monopolies were largely exclusive. In particular, for the better part of the twentieth century it was widely agreed that the incumbents owed no duty to carry signals for potential competitors in the local phone-service market. Policymakers justified the exceptions on the ground that it was impossible to foster competition for local phone service. The wires that connect phones to phone lines, they believed, established a "bottleneck" through which all competitors would need to pass to reach local customers. The exceptions for interexchange carriers and others

14 47 U.S.C. § 271(c), (d)(3).
15 See, e.g., Peter Huber et al., Federal Telecommunications Law § 2.1.2 (2d ed. 1999).
16 See, e.g., Kennedy, supra note 13, at 5-17.
20 See, e.g., Kennedy, supra note 13, at 32-39.
21 See Stuart M. Benjamin et al., Telecommunications Law & Policy 715 (2001) ("[A] central premise of the Bell divestiture was that the provision of local telephone service was a monopoly enterprise. This view had taken hold back in the 1920s and had led to the system of state-sanctioned local monopolies that both pre-dated and survived the Bell breakup."); Huber et al., supra note 15, § 2.1.2, at 86 (claiming that "[t]he 1996 Act reversed the presumption" that local phone service was a legal monopoly).
22 See, e.g., Kennedy, supra note 13, at 31-32.
only reinforced the basic presumption that local exchanges were natural monopolies and best regulated as such.\textsuperscript{23} Within such expectations, as Peter Huber, Michael Kellogg, and John Thorne explain, “[e]qual access obligations within the monopoly would have been useless or worse.”\textsuperscript{24}

This monopoly approach began to lose favor in the 1970s, in telecommunications and in other public-utility fields. Joseph Kearney and Thomas Merrill have thoroughly documented these changes in their article The Great Transformation in Regulated Industries Law.\textsuperscript{25} Regulators began to promote a new paradigm, which sought to “subject to ordinary contractual relations all common carrier and public utility services that can be provided by multiple competing providers.”\textsuperscript{26} For those sectors of an industry that could not be organized around ordinary principles of contract and competition, the new paradigm established “a new set of regulatory obligations—including the duty to interconnect, to lease unbundled network elements, and to sell services for resale.”\textsuperscript{27} As Merrill and Kearney aptly explain, in the new paradigm “the owners of such bottleneck facilities... [became] the focal point of regulatory attention. In effect, the owners of natural monopoly facilities assume[d] new common carrier duties toward their competitors, and these duties [were] regarded as more important than those they owe[d] to their traditional customers.”\textsuperscript{28} This transformation eventually reached telecommunications law. As Peter Huber, Michael Kellogg, and John Thorne explain, in telecommunications, “both state and federal regulators had been moving steadily in th[e] direction” of this paradigm shift starting in the 1980s.\textsuperscript{29} In the early 1990s, the FCC launched regulatory initiatives to encourage incumbents to interconnect phone-service providers to their exchanges.\textsuperscript{30} In the years leading up to 1996, many states established either a regime of full competition for the provision of switched local exchange service, or a statutory mandate to open their local exchanges to competition in the near future.\textsuperscript{31}

The 1996 Act completed this change. It abandoned the natural-monopoly conception of local phone service for the competition-antitrust conception that had developed in other similar industries. As one supporter of the 1996 Act

\begin{itemize}
  \item \textsuperscript{23} See, e.g., Verizon Communications v. FCC, 535 U.S. 467, 475 (2002). The FCC proposed new rules in the late 1980s and early 1990s to create targeted duties to interconnect, see Peter W. Huber et al., Federal Telecommunications Law § 2.4 (Cum. Supp. 2004); Huber et al., supra note 15, § 5.4, but the rulemakings only reinforced the impression that the duty broke new ground from the paradigm that prevailed at the time. See, e.g., Bell Atlantic Tel. Cos. v. FCC, 24 F.3d 1441 (D.C. Cir. 1994).
  \item \textsuperscript{25} Kearney & Thomas, supra note 18, at 1323.
  \item \textsuperscript{26} Id. at 1363.
  \item \textsuperscript{27} Id. at 1364.
  \item \textsuperscript{28} Id. at 1364.
  \item \textsuperscript{29} Huber et al., supra note 23, § 2.4, at 70 (Cum. Supp. 2004).
  \item \textsuperscript{30} See id. § 2.4, at 70-71.
  \item \textsuperscript{31} See id. § 2.4, at 74.
\end{itemize}
explained, the Act broke new ground because it told incumbents "to let the
competitors come in and try to beat your economic brains out." First, the Act
extinguished the incumbents' franchise monopolies by preempting all state and
local laws that "prohibit[ed] the ability of entity to provide any interstate or
intrastate telecommunications service." With the franchises out of the way,
sections 251 and 252 of the Act proceeded to impose "must-carry"
requirements on the incumbents. Section 251(a) imposes on each incumbent a
general duty to interconnect its local exchange to the facilities and equipment of
other carriers. To discharge this general duty, section 251(c) lays out several
specific duties. The first is physical "collocation": under section 251(c)(6),
incumbents must provide to competitors the office space and other physical
plant necessary for them to interconnect to the local exchange or to unbundled
network elements. Sections 251(c)(2) and (3) require incumbents to
interconnect to competitors' local networks and to competitor unbundled
network elements, respectively.

The 1996 Act anticipated that the incumbent local-exchange carriers
would get compensated for assuming these interconnection duties. Sections
251(c)(2), (3), and (6) specify that incumbents are entitled to charge rates that
"are just, reasonable, and nondiscriminatory." With regard to interconnection
and unbundled network elements (covered by sections 251(c)(2) and (3)),
section 252(d) goes on to provide that rates that "may include a reasonable
profit" and "shall be based on the cost . . . of providing the interconnection or
network element." Section 252(d) also specifies, however, that whatever this
term "cost" means, it must be "determined without reference to a rate-of-return
or other rate-based proceeding."

These provisions gave the FCC considerable leeway to identify the proper
measure of "cost," rate formulas that would be "just, reasonable, and
nondiscriminatory." That choice raised sensitive policy questions. On one
hand, the FCC could have spread historical costs—the costs the incumbents
had expended building or maintaining their exchanges in the past—by
including historical costs as an element of the "cost" competitors were required
to pay incumbents for forced access. Distributional concerns could have

488.
33 47 U.S.C. § 253(a) (emphasis added).
35 See 47 U.S.C. § 251(c)(6). Incumbents can avoid providing physical space if they can
provide an adequate substitute with virtual collocation and show that physical collocation is not
practical for technical or space reasons. See id.
36 See 47 U.S.C. § 251(c)(2)-(3).
38 See id.
39 Dissenting in Verizon, Justice Breyer thought the text, structure, and purpose of the 1996
Act required this interpretation of cost. See Verizon, 535 U.S. at 548-49 (citing ALFRED KAHN, THE
ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS 330 (1988)).
justified such an approach, because the incumbents could have argued that the competitors ought to share in the costs used to create and maintain the exchanges they are using to their benefit. 40 Perhaps dynamic-efficiency concerns could have justified this approach as well. Such concerns entitle incumbents to compensation, from some source, for stranded investments, to promote efficient research and development for local-exchange infrastructure over the long haul. 41 On the other hand, the FCC could also have insisted on leaving stranded costs where they fell. If the FCC had billed competitors for stranded costs using interconnection rates, it would have increased interconnection rates above the marginal cost of providing service through the local exchange. That increase would then have discouraged the efficient use of, and competition over, network elements by incumbents and competitors. 42

The FCC preferred to promote the latter concerns rather than the former. 43 When it promulgated the rate regulations for the interconnectivity provisions of section 251, the FCC interpreted “cost,” “just,” “reasonable,” and “nondiscriminatory” to require a formula based on “TELRIC”—“total element long-run incremental cost” pricing. When an incumbent provides a competitor access to a network element, the incumbent is entitled to the sum of TELRIC costs plus a reasonable allocation of forward-looking common costs. 44 The latter addend, “forward-looking common costs,” consist of “economic costs efficiently incurred in providing a group of elements or services . . . that cannot be attributed directly to individual elements or services.” 45 The regulations specify that the former addend, TELRIC costs, “should be measured based on the use of the most efficient telecommunications technology currently available and the lowest cost network configuration, given the existing location of the incumbent LEC’s wire centers.” 46 TELRIC rates thus keep rate payments at or below an incumbents’ actual costs. If someone invents a new technology that makes the local exchange more efficient than anyone in the industry could have expected, TELRIC frees the competitors from sharing the costs of the incumbents’ less-than-optimal investments. The regulations reinforce this result when they exclude “embedded costs,” defined as “the costs that the incumbent LEC incurred in the past.” 47

This general background brings to light most of the factual and policy issues relevant to the Takings Clause. The FCC’s interconnectivity rates do

45 47 C.F.R. § 51.505(c).
46 47 C.F.R. § 51.505(b)(1).
47 47 C.F.R. § 51.505(d).
not allow incumbents to spread and share stranded historical costs with competitors. In principle, it is possible that incumbents suffered a bait and switch, most likely if, before 1996, state and local ratemaking proceedings were dominated primarily by the political demands of residential customers. If so, local phone-service rates were probably low, regulators probably stretched incumbents’ amortization schedules far into the future, and TELRIC rates therefore cut short a substantial stream of compensation for historical costs. On the other hand, it is also possible that incumbents were not harmed seriously, especially if, before 1996, they influenced state and local ratemaking proceedings more effectively than customers and consumer groups. If so, pre-1996 ratemakings were probably generous to the incumbents, in which their post-1996 stranded historical costs are now low or non-existent. This is a crucial issue of fact to be litigated case by case and state by state. Another issue of fact is how valuable long-distance service is to the incumbents. On one hand, perhaps incumbents will recoup a substantial portion of their stranded costs after they enter and profit in long-distance markets. On the other hand, if long-distance markets involve close to perfect competition, profits will remain quite small for the foreseeable future. In the latter scenario, long-distance markets would be small compensation for the cost of losing exclusive control over local exchanges. These questions of fact point to crucial questions of policy, particularly how the 1996 Act’s effect on local-exchange investment compares with its effects in encouraging competition across those exchanges.

II. Tensions Within Takings Law

Nevertheless, a huge conceptual obstacle makes it difficult to analyze these questions within existing takings law and scholarship: there is no consensus in either the law or scholarship about how to conceive of “takings” or “private property.” Thomas Merrill and William Baumol have aptly described the case law. While the Supreme Court has shown “a pronounced tendency to talk tough about property rights” in some cases, it often “beat[s] a hasty retreat” in cases that involve “complex regulatory schemes generating pools of winners and losers.”

While this division stems from several factors, one particularly important factor is the tension between two understandings of property theory. As explained in the Introduction, one consists of a body of Libertarian thought that has influenced constitutional property-rights law largely before 1900, and to a lesser but still noticeable extent more recently. The other, called here the Legal Realist approach, provides an account of constitutional property rights that reconciles such rights at a high theoretical level to key features of post-New

Deal redistributive regulation. While the following account runs the risk of being overly general, it integrates into two comprehensive frameworks many arguments and tendencies that are familiar to scholars who know takings law.

A. Libertarian Property Theory

Consider first the Libertarian approach. Virtually all writers who embrace this approach start from the claim that property reflects and encourages inherent human tendencies to work, produce, and acquire for one's own chosen ends. Chancellor James Kent, a New York state judge and author of a leading nineteenth-century legal treatise influenced heavily by natural-rights ideas, described "the sense of property [as] graciously implanted in the human breast, for the purpose of rousing us from sloth, and stimulating us to action..."49 Jeremy Bentham made basically the same claim within a utilitarian framework: "If I despair of enjoying the fruits of my labour, I shall only think of living from day to day: I shall not undertake labours which will only benefit my enemies."50 The Libertarian approach accepts that claim as true, at least politically—if not accurate in every case, accurate enough to rely upon when establishing government institutions.

Several important descriptive and prescriptive consequences follow. Descriptively, because self-love and acquisitiveness tie people's interests and attachments to what they own, the owners of assets generally have better information than the government or other individuals about how to use their assets. As Friedrich Hayek claimed,

[1]here would be no difficulty about efficient control or planning were conditions so simple that a single person or board could effectively survey all the relevant facts. It is only as the factors which have to be taken into account become so numerous that it is impossible to gain a view of them that decentralization becomes imperative.51 Prescriptively, one of the overriding objects of government becomes the establishment of laws that recognize, take advantage of, and encourage these links between human initiative and external assets. As John Locke put it, the proper object of property regulation is "by established laws of liberty to secure protection and encouragement to the honest industry of mankind."52 In one sense, when the laws promote what Locke called "honest industry," private property becomes the overriding object of government. But in another sense, the protection and encouragement of property is simply a different way of saying that the law should, to the extent that it can, transfer control and use decisions from legislative majorities and public officials to individual owners. If the

49 2 JAMES KENT, COMMENTARIES ON AMERICAN LAW 257 (1st ed. 1827).
51 FRIEDRICH A. HAYEK, THE ROAD TO SERFDOM 49 (1944).
52 JOHN LOCKE, SECOND TREATISE ON GOVERNMENT para. 42 (J.W. Gough ed., 1946).
institution of property recognizes that different people have different talents, tastes, and needs, the law ought to presume that individual owners can use what is closest to them to fit their own needs more effectively than a legislative majority can with a large class of commercial assets.

These overarching claims lead to several important claims that become relevant in takings law. First, they create a presumption that “private property” ought to be conceived of broadly. Because property ordinarily encourages tendencies that are generally productive, as a starting presumption, owners should be left with the fullest range of use rights consistent with the rights of others. Adam Mossoff has described this approach as an “integrated” approach to property. Thomas Merrill and Henry Smith have called it an “in rem” conception of ownership. The Supreme Court reflects the same understanding when it insists from time to time that “private property” normally covers every sort of interest the citizen may possess—not only the “vulgar and untechnical sense of the physical thing,” but also “the group of rights inhering in the citizen’s relation to the physical thing, as the right to possess, use and dispose of it.”

One important corollary of this claim is that Libertarian property theory tends to resist conceiving of property solely in terms of owners’ expectations or future plans. Property protects not any one concrete set of expectations but a freedom to make choices. Libertarian theory usually presumes that economic life is characterized by change more than by stasis, that owners’ interests differ more than they resemble one another, and that owners are better-positioned than neighbors, rivals, or planners to know how best to use their own assets. If these generalizations describe economic life with tolerable accuracy, it follows that the law should protect not only owners’ current plans but also their rights to change their minds. The law may take account of owners’ expectations, but expectations play a largely secondary role. Expectations help assess owners’ just compensation when they lose property rights, because strong expectations suggest that the rights taken are quite valuable to the owner. But Libertarian property theory seeks to protect initiative in many situations in which an owner has not yet acquired hard expectations, particularly the freedoms to change and adapt. This claim follows, as Thomas Merrill and Henry Smith explain, from a “deep design principle” by which owners are entitled to control “the future use and enjoyment of particular resources . . . that holds against all the world.”

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57 Merrill & Smith, supra note 54, at 359, 361.
Second, Libertarian property theory presumes that, in the absence of some compelling justification, government ought to preserve security in property by paying just compensation whenever it restrains the free exercise of property rights. Courts appreciate this connection when they say, as the Supreme Court often says in the run-of-the-mill cases, that the Takings Clause’s overriding purpose is “to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.” If society makes a strong commitment to protecting and encouraging property rights, the common good seems to be the aggregation of the rights of all citizens. That relation entitles the government to act for the common good by taking property for public uses, but at the same time it requires the government to spread private losses across the entire public. The compensation may come in-kind, through other consequences of the government action, or explicitly, through a cash payment. In either case, the owner is entitled to the fair value of rights extinguished by government actions. By paying that fair value, Libertarian theory maintains, government encourages security in property; over the long run, that security encourages many forms of productive and gainful activity that would not be easy to anticipate ex ante.

In utility law, this basic attitude creates at least some presumption that, other things being equal, utilities’ investments and franchise rights count as constitutionally protected “private property.” This presumption explains an otherwise strange feature about takings law. If one were to read only the leading Supreme Court cases and scholarship, it would be reasonable to suspect that utilities should not be protected by takings principles. The leading authorities tend to focus on regulatory-takings issues associated with land, and particularly land use. Zoning, rent-control, environmental, and other similar regulations generate strong pressures to narrow the scope of regulatory-takings limitations. In response, the Supreme Court now assumes that “takings” principles were originally meant to apply only to outright interferences with title ownership and the right to exclude. If the law followed this claim to its logical conclusion, takings protections should apply to utilities only barely, if at all. In fact, however, utility regulation generates hundreds if not thousands of judicial and administrative takings disputes. Courts and commentators may disagree about the substance of takings principles as they apply to utilities, but at some minimal level they agree that, in John Drobak’s words,

"constitutional ratemaking doctrine embodies the principles of the takings clause."61

Third, the Libertarian approach presumes that it is conceptually possible and substantively necessary to enforce a relatively fixed conception of the power to "regulate." Laws that "regulate" may restrain property without triggering just-compensation requirements. In Libertarian theory, "regulations" are primarily laws that "make property rights regular"—laws that define the zone of free use, control, and transfer rights that are fairly proportional to any asset, laws that define and enforce abuses of those rights, and laws that facilitate the orderly use and transfer of property.62

That general understanding of "regulation" narrows the permissible grounds for "regulating" the property conflicts that arise in telecommunications law. In telecommunications, the main "regulatory" limit allows government to restrain operators' rights to exclude and control their rates. Under any understanding of how to apply general social-compact principles, when an owner receives a monopoly from the state, he cedes the right to exclude customers on any basis.63 When the state grants him control over an asset with an obvious public use, it imposes on him the responsibility to ensure that the asset is used consistent with the rights of all. In general, then, the owner assumes duties not to discriminate among customers and to sell or rent the monopoly good at rates reasonable in comparison with rates of return for comparable investments.64

That general proviso still leaves the state free to choose how to enforce the basic substantive limitation. As explained in the previous part, traditional common-carrier principles apply this limitation to the utility in relation to its customers, while contemporary antitrust/bottleneck principles apply the limitation between the utility and its competitors. In either case, utilities retain all property rights not necessary to enforce the underlying understanding of publici juris regulation. When a law restrains the free use of property more than necessary to enforce this understanding of, it therefore "takes" the property rights of the utility.

61 Id. at 68.
63 The best illustration of this position, even by a judge jealous of private-property rights, comes from Justice Field's dissenting opinion in Munn v. Illinois, 94 U.S. 113 (1876).
64 See id; Spring Valley Water Works v. Schotter, 110 U.S. 347, 354 (1883); Railroad Comm'n Cases, 116 U.S. 307, 331 (1886); Reagan v. Farmers' Loan & Trust Co., 154 U.S. 362 (1894).
For a historical perspective on Munn and the concept of publici juris, see Harry N. Scheiber, The Road to Munn: Eminent Domain and the Concept of Public Purpose in the State Courts, in LAW IN AMERICAN HISTORY 327, 338-55 (Donald Fleming & Bernard Bailyn eds., 1971). There is another way to understand ratemaking regulation—that it takes investors' capital per se for public uses, and merely asks whether the investors are getting just compensation for the taking. This view has been endorsed in Epstein, supra note 40, at 274-77; Dana & Merrill, supra note 11, at 165-66. However, this view ends up relying on or more or less the same substantive principles as the "regulatory takings" understanding advanced in text.
Last, Libertarian property theory encourages lawyers to think of property in "formalist" terms. It encourages them to treat different takings cases as analogous. This claim follows from Libertarian theory's expansive "integrated" or "in rem" conception of property rights. If an owner in a case involving land wins just compensation for losing a particular right in the proverbial bundle, the decision presumptively counts as precedent for protecting that same right to dispose in the context of water rights, franchises, or intellectual property. Of course, that presumption can be reversed, if one can show that the exercise of a specific right will be harmful to the public or disadvantageous to the rights of all for one species of property. Separately, the same right may be more or less valuable for different species of property. But under Libertarian principles, as long as the basic starting presumption has not been rebutted, it is possible to compare and contrast rights like use, control, and disposition across a wide range of species of property. If a given right seems more valuable to one species than to another, that difference can be considered not when determining whether a taking has occurred; rather, a taking has occurred, and the difference goes to determining how much to pay for it in just compensation. What may seem to be casuistic analogies, then, instead protect a strong general expectation among owners that, as long as they do not threaten their neighbors, they will retain control over the use and enjoyment of their property to the exclusion of the rest of the world.

B. Realist Property Theory

The Realist approach breaks from the Libertarian approach on a wide range of fronts. Most fundamentally, it questions the account of human nature that grounds the Libertarian approach. For instance, Margaret Jane Radin has challenged the Libertarian arguments of Richard Epstein because she questions Epstein's "Hobbesian model of human nature," within which "[n]othing will get produced unless people are guaranteed the permanent internalization of the benefits of their labor." By calling that claim into question, the Realist approach expands the realm of the possible for the state. If selfish, industrious, productive, and acquisitive passions do not limit the realm of the possible for the state, then the state may achieve a relatively wide range of goals. The general welfare, as determined by an encompassing majority, becomes the overriding object of legislative policy. By the same token, property becomes subordinate to one of many possible goals such a majority might or might not choose to pursue. As Frank Michelman recognized, once a state has embraced "the economically active and regulatory state with its licenses, franchises, and

the like... the claims of popular sovereignty and classical property cannot, in truth, be stably reconciled at a very high level of abstraction or generality.66

The character of property changes to keep pace with the expanding horizons of possible political action. First, if property is "integrated" within the Libertarian approach, it is "disintegrated" in the Penn Central approach.67 Each property right must be justified and defended de novo on its merits. Owners enjoy "property" only in the rights that are judged to have merit. Thus, Legal Realist Wallace Hamilton defined "property" in the 1937 edition of the Encyclopedia of the Social Sciences as "a euphonious collection of letters which serves as a general term for the miscellany of equities that persons hold in the commonwealth."68 That is also why Penn Central warned that "'takings' jurisprudence does not divide a single parcel into discrete segments and attempt to determine whether rights in a particular segment have been entirely abrogated."69 To borrow Thomas Merrill and Henry Smith's description, the Realist/Penn Central approach applies a "list of uses" approach to property: "as a list of particularized use rights that individuals have in resources.70

This "list of uses" understanding of property creates a slight presumption, which is rebuttable but no less perceptible, against recognizing particular use rights as property. As Thomas Merrill and Henry Smith describe the nerve of Realist property theory, "property has no fixed core of meaning, but is just a variable collection of interests established by social convention [that] the state [may] freely expand or... contract... in the name of the general welfare."71 From this starting perspective it follows that owners ought not to be entitled to property in specific control, use, or transfer rights unless and until they can show that such rights contribute to the general welfare. In individual cases, owners may be able to make this showing. But where the Libertarian approach presumes that particular rights are useful and part of "property" until specifically shown to be harmful, the Realist approach presumes that particular rights are not useful until specifically shown to redound to the general welfare. Because policymakers make that determination, the Realist list-of-uses approach also transfers policymaking power from owners to policymakers.

To be sure, within the Realist approach, property still means more than the right to use one's own property consistent with the state's conception of what contributes to the general welfare. But to determine whether owners have special attachments to any stick in the proverbial bag of rights, private property

70 Merrill & Smith, supra note 54, at 366.
71 Id. at 365.
tends to focus on owners' expectations. Frank Michelman contributed to this view when he argued that, for takings purposes, private property ought to be conceived of largely in reference to an owner's "investment-backed expectations." The U.S. Supreme Court embraced Michelman's argument by making "investment-backed expectations" a crucial element of regulatory-takings law in *Penn Central*. This focus, however, subtly builds in a presumption that owners are not entitled to claim property rights in development potential, or more generally in the right to put existing property to new and different uses.

Next, because the Realist approach presumes that many different social policies may be desirable in different circumstances and for different people, it tends to doubt that the law can draw clear distinctions between government actions that "regulate" and "take." This tendency comes out most often in law and scholarship about the concepts of "harm" and "benefits." In *Lucas v. South Carolina Coastal Council*, Justice Scalia explained "[t]he transition from [the Court's] early focus on control of 'noxious' uses to [its] contemporary understanding of the broad realm within which government may regulate without compensation was an easy one, since the distinction between 'harm-preventing' and 'benefit-conferring' regulation is often in the eye of the beholder." Frank Michelman lent a great deal of respectability to this view in his 1967 article *Property, Utility, and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*, which concluded that "there is no basis for a general rule dispensing with compensation in respect of all regulations apparently of the 'nuisance-prevention' type..." If one subscribes to such sentiments, one is skeptical that the law can maintain clear distinctions between regulations and takings—in nuisance law, in common-carrier law, or anywhere else.

Finally, where the Libertarian approach presumes that the law can draw analogies about the same right from one species of property to another, the Realist approach presumes the opposite. This presumption follows because the Realist approach prefers to treat questions of property on a right-by-right basis, and it expects different legislative majorities in different settings to use the power to regulate to different ends. Thus, Margaret Jane Radin praises the Realist approach because it is "'ad hoc'... essentially particularist, essentially context-bound and holistic; each decision is an all-things-considered intuitive weighing." As Frank Michelman explains, "the emergence of the economically active and regulatory state" creates a strong trend toward the

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73 See *Penn Central*, 438 U.S. at 124.
75 Michelman, supra note 72, at 1197.
76 Radin, supra note 65, at 1680.
The Telecommunications Act of 1996

"denaturalization and positivization (implying the politicization) of property."\textsuperscript{77} Under those assumptions, it becomes more difficult to claim that property protects a regular set of expectations from one species to another. If anything, as Michelman says, it is "obtuseness" to assume that there is any such commonality, or to analogize between different species by using the forms of property rights.\textsuperscript{78}

III. The 1996 Act and Tensions Under The Takings Clause

Both of these approaches are well represented in the law and scholarship on takings. A takings doctrine that seems straightforward on the surface can vary sharply in application depending on whether the Libertarian or the Realist understanding seems to fit better with a judge's or policymaker's views on the facts of a challenged regulation. That tension seems to be informing the debate over the local-exchange provisions of the 1996 Act.

A. Confiscatory Ratemaking Versus Regulatory Takings

Consider first whether the 1996 Act ought to be viewed as a ratemaking case or a "regulatory-taking" case. Many telecommunications lawyers agree that confiscatory-ratemaking principles do and should govern takings challenges to the local-exchange provisions of the Act and the FCC's regulations. Thomas Merrill and William Baumol,\textsuperscript{79} Stuart Buck,\textsuperscript{80} Michael Legg,\textsuperscript{81} and Jim Chen\textsuperscript{82} have all assumed as a matter of course that ratemaking cases should control and that regulatory-takings principles should not. As Chen puts it, "[t]he Supreme Court . . . has consistently distinguished takings clause restraints on ratemaking from the takings clause doctrine that governs physical occupations of real property."\textsuperscript{83} In Verizon, the Supreme Court applied to the takings issues it discussed leading ratemaking precedents including Smyth v. Ames, FPC v. Hope Natural Gas, and Duquesne Light Co. v. Barasch.\textsuperscript{84}

There are several reasons to prefer the ratemaking model. One reason is that regulated industries may be special. As the next section will show, many strands of regulatory-takings law are strongly deferential to the government and strongly oriented against paying just compensation to individual claimants.

\textsuperscript{77} Michelman, \textit{supra} note 10, at 1627.
\textsuperscript{78} See id. at 1628.
\textsuperscript{79} See Baumol & Merrill, \textit{supra} note 5, at 1042-45.
\textsuperscript{80} See Stuart Buck, TELRIC vs. Universal Service: A Takings Violation?, 56 FED. COMM. L.J. 1, 38 (2003) ("[T]he confiscatory rate doctrine by definition relates to an unfair rate structure, which would be precisely the [incumbents'] complaint.").
\textsuperscript{81} Legg, \textit{supra} note 7, at 581-84.
\textsuperscript{82} See Chen, \textit{supra} note 5, at 1685.
\textsuperscript{83} Id. at 1686.
\textsuperscript{84} See Verizon, 535 U.S. at 624 (citing Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989); Smyth v. Ames, 169 U.S. 466 (1898); FPC v. Hope Natural Gas, 320 U.S. 591 (1944)).
Perhaps these cases sanction regulations that discourage individual investments, perhaps not. Such questions raise difficult empirical and policy questions, as one can see by reviewing the debate over whether rent control restricts the available supply of apartments.\(^8\) But the telecommunications industry may present a more compelling case for constitutional protection. In telecommunications and other regulated industries, investors' up-front investments may be so substantial that the law must provide investors with some credible guarantees that the government will not expropriate their sunk capital.\(^6\) If so, it is better to create in takings law a firewall between regulated industries and less capital-intensive industries. Whether or not the doctrines were meant to reflect such a distinction, they are written as if they were. Both the confiscatory ratemaking and \textit{Penn Central} doctrines are ad hoc, but the ad hoc factors point in different directions. As the next section will explain, the \textit{Penn Central} factors usually cooperate to discourage compensation. Ratemaking doctrine, in contrast, favors capital, because the factors focus primarily on whether the challenged regulation guarantees investors a rate of return commensurate with the rates for similarly risky investments.\(^7\) William Barr, Henry Weissmann, and John Frantz have advanced such a view of ratemaking law in their contribution to the scholarship on post-1996 Act takings claims.\(^8\)

Other, more pragmatic arguments for ratemaking, however, fit Realist background assumptions about takings law. \textit{Penn Central} claims that all takings cases are "ad hoc," and it warns lawyers and judges off from using conceptual severance and other formalistic tools to draw analogies across different classes of takings cases.\(^9\) If one agrees with that sentiment, it makes comparatively little sense to organize takings analysis around the property rights taken or around overarching normative questions. By the same token, however, it makes a great deal of sense to organize law around the economics and industry where the alleged takings occur. Factors that seem ad hoc from the standpoint of takings law may be salient and regular features of an industry's business structure. If so, ratemaking principles ought to govern in


\(^{86}\) Brian Levy and Pablo Spiller have collected several especially thorough studies exploring how governments might provide credible commitments to capital in telecommunications in \textit{Regulations, Institutions, and Commitment: Comparative Studies of Telecommunications} (Brian Levy & Pablo T. Spiller eds., 1996).

\(^{87}\) See Daquesne, 488 U.S. at 308.


\(^{89}\) See \textit{Penn Central}, 436 U.S. at 123.
telecommunications and other regulated industries, while broader regulatory-takings principles ought to govern in real estate cases and cases that are otherwise hard to classify.

But these arguments do not seem compelling within a Libertarian understanding of property. Again, the Libertarian approach pays a great deal of respect to the forms of private property. Rights are important proxies for zones of freedom that allow owners either to engage in productive activity or to hedge against uncertainty and change. Ratemaking cases focus on whether the state is "regulating" the dangers of monopoly, specifically by regulating a utility's prices and relations to its consumers. By contrast, the 1996 Act extinguishes rights to exclude—the incumbents' franchises, and their rights not to interconnect competitors.

Now, as Section III.C will make clear, ratemaking considerations may be relevant to the incumbents' entitlement to just compensation. As Stuart Buck recognizes, if takings law concludes that Congress effected a regulatory taking, "the real question would then become: does the price structure allowed to the [incumbents] amount to just compensation or not," a question for which the law "would likely have to consult the confiscatory rate doctrine." Even so, under general Libertarian background assumptions, at the takings stage, ratemaking cases raise the wrong question: ratemaking regulations raise questions about whether regulators are holding incumbents to an unacceptably low level of return, while exclusivity regulations raise questions about whether the regulators have extinguished the means by which utilities can recover any return at all. At least without specific reference to telecommunications economics, in the abstract it seems more serious for incumbents to lose the latter rights than the former. If so, the 1996 Act implicates not ratemaking doctrine but regulatory-takings doctrine.

B. Taking a Common Carrier's Right To Exclude Competitors

Takings law, however, does not decide a case simply by applying regulatory-takings principles instead of ratemaking principles. "Regulatory-takings" law is deeply split in its tendencies. Some portions of regulatory-takings law incline toward the Libertarian approach, others toward the Realist approach.

To appreciate the tensions, it is worthwhile to dispel a perception that causes a great deal of confusion in the commentary on takings law. Many commentators portray the categorical and balancing regulatory-takings cases as two sharply, almost hermetically-separate, fields of takings law. This portrait, while accurate and useful in many run-of-the-mill cases, is highly misleading in some respects, particularly in its tendency to elevate black-letter doctrine over

90 Buck, supra note 80, at 36.
91 See, e.g., id. at 35-38; Legg, supra note 7, at 581-82.
substance. All of the Supreme Court's recent regulatory-takings cases, balancing or categorical, respect *Penn Central* as the "polestar" of regulatory-takings law.\textsuperscript{92} As a result, all apply *Penn Central's* three-part test: they balance (1) the owner's economic losses and (2) the owner's lost reasonable investment-backed expectations against (3) the character of the government action.\textsuperscript{93} However, this test has virtually no content on its own; it takes whatever content it has from the legal and political theory on which the Court relies to determine which expectations are "reasonable" and which government actions have a high "character."

To appreciate the shifts, consider how the Supreme Court first announced the per se rule for physical occupations, in *Loretto v. Teleprompter Manhattan CATV Corp.*\textsuperscript{94} A New York state law authorized cable companies to install cable lines and directional taps on landlords' buildings to service not only the tenants but also other buildings in the neighborhood. The Court respected *Penn Central* as the leading regulatory-takings case,\textsuperscript{95} but then used the second and third *Penn Central* factors to require per se compensation whenever the government permanently and physically occupies property.\textsuperscript{96} The Court placed huge social value on the control of land. It did so by insisting that owners have strong expectations that they will be able to control their land: "[t]he power to exclude...[is] one of the most treasured strands in an owner's bundle of property rights."\textsuperscript{97} Similarly, the Court then downgraded the third prong, the character of the government action. Because the Court regarded an invasion of land as "perhaps the most serious form of invasion of an owner's property interests,"\textsuperscript{98} it explained that "when the 'character of the government action'...is a permanent physical occupation of property, our cases uniformly have found a taking to the extent of the occupation, without regard to whether the action achieves an important public benefit or has only minimal economic impact on the owner."\textsuperscript{99}

On the other hand, *Penn Central* itself highlights how the factors change if the regulation under challenge seems to have more social value. In such cases, the Court plays up the character of the government action by deferring to it under rational-basis principles.\textsuperscript{100} This deference tacitly presumes that the property right at issue has little or no social value worth protecting over the constitutional long term. The Court then uses *Penn Central's* first and second

\textsuperscript{93} See *Penn Central*, 438 U.S. at 124.
\textsuperscript{94} 458 U.S. 419 (1982).
\textsuperscript{95} Id. at 426, 432.
\textsuperscript{96} Id. at 427, 434-37.
\textsuperscript{97} Id. at 435.
\textsuperscript{98} Id.
\textsuperscript{99} Id.; see also Claeys, supra note 8, at 193; Claeys, supra note 56, at 1556-58.
\textsuperscript{100} See *Penn Central*, 438 U.S. at 131 ("reasonably related to the promotion of the general welfare").
prongs to narrow the owner’s ability to claim the right at issue as constitutional “private property.” The owner’s claim is weak unless she can show that by dint of long effort and investment she has acquired strong expectations in protecting that right. Likewise, the law discounts the owner’s economic losses using the “denominator” approach: even if the losses are substantial in dollars-and-cents terms, they still may not be severe if put in the context of the productive uses and economic gains still left to the owner.101

Much of the scholarship relevant to the 1996 Act does not sufficiently appreciate these two sides to Penn Central. Because the case law is deeply split, the crucial question about the 1996 Act is one that Penn Central’s doctrine does not even address: should common carriers be entitled to exclude competitors and other outsiders on the same terms as land owners, intellectual-property owners, and owners of other forms of property? If the answer is “yes,” takings law can easily turn to a per se compensation rule; if “no,” the law can just as easily tip towards deferential interest balancing.

Consider first the debate between Daniel Spulber and Christopher Yoo on one hand, and Jim Chen on the other, about per se takings requirements. Spulber, Yoo, and Chen agree that section 251(c)(6) triggers Loretto’s per se compensation rule when it forces incumbents to collocate and therefore give competitors physical access to their offices.102 Yoo and Spulber, however, proceed to argue that the interconnection requirements of sections 251(c)(2) and (3) force “virtual collocation[s]” analogous to physical takings, and therefore also trigger per se compensation.103 Chen disagrees, arguing that interconnection requirements do not inflict takings because they do not impose physical occupations.104

However, takings doctrine is not as rule-bound as Chen, Spulber, and Yoo assume. The vagaries become clearer if one turns away from Penn Central and Loretto to other, less-known takings cases formally analogous to the Act’s local-exchange provisions and regulations. To begin with, consider section 251’s interconnection provisions, which resemble easements and rights of way. Kaiser Aetna v. United States is particularly instructive here.105 Kaiser Aetna owned land around a Hawaii lagoon completely sealed off from the Pacific Ocean. Under Hawaii law, the lagoon was private property, unencumbered by any public-trust servitude, on the same terms as the dry land around the lagoon. As part of a project to develop the land around the lagoon, Kaiser Aetna dug a channel connecting the lagoon to a nearby bay. Before it dug, it notified the U.S. Army Corps of Engineers staff, who acquiesced with little

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102 See Spulber & Yoo, supra note 6, at 977 (citing Qwest v. United States, 48 Fed. Cl. 672 (2001)).
103 Spulber & Yoo, supra note 6, at 979.
comment. After it dug, however, the Corps claimed that the channel subjected Kaiser Aetna's lagoon to the federal navigational servitude.\[106\]

*Kaiser Aetna* is especially analogous to the 1996 Act because in both cases the owners' property claims stand in a similar gray area between pure private property and public trust. While Kaiser Aetna's lagoon was pure private property as long as it was not connected to the Pacific Ocean, there was always a real possibility that it would become publici juris when connected. In telecommunications law, the incumbents (and before them AT&T) have never held an unqualified right to exclude. True, their franchise agreements generally gave them the right to exclude competitors from using their local exchanges. At the same time, the FCC did require them to connect interexchange carriers and, more significantly, they had always owed a duty of access to customers. In both cases, the legal ambiguities cloud the question whether the claimants have constitutional "private property" in the right to exclude. In *Kaiser Aetna*, the Court resolved this ambiguity by appealing to the idea that "not all economic interests are 'property rights'; only those economic advantages are 'rights' which have the law back of them."\[107\]

The Corps' conduct, he concluded, led "to the fruition of a number of expectancies embodied in the concept of 'property'—expectancies that, if sufficiently important, the Government must condemn and pay for..."\[108\] It would take a thorough survey of twentieth-century telecommunications policy to confirm the point, but it is at least possible that incumbents can show that AT&T and they reasonably held similar "expectancies" toward their phone lines.

Similarly, if section 251 can be viewed as establishing telecommunications' equivalent of a right of way, section 253 can be viewed as extinguishing telecommunications' equivalent of an intellectual-property right.\[109\] Again, pre-1996, incumbents (and before them, AT&T) enjoyed franchise monopolies under state or local law to provide local phone service on an exclusive basis. Section 253 preempted any and all local franchise laws still in effect when the 1996 Act took effect. Section 253 thus extinguished incumbents' right to exclude, similar to the way in which the government extinguishes an intellectual property owner's right to sue and enjoin infringements of her intellectual property.

The Supreme Court has rendered very few takings decisions about intellectual property, but the leading recent case follows the same approach as *Kaiser Aetna* and *Loretto*. In *Ruckelshaus v. Monsanto Co.*,\[110\] Congress changed federal pesticide-registration laws so as to authorize the EPA to disclose manufacturer trade secrets it had previously been required to keep

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106 See *id.* at 166-69.
107 *Id.* at 178 (quoting United States v. Willow River Co., 324 U.S. 499, 502 (1945)).
108 *Id.* at 179.
confidential. In other words, Monsanto and other pesticide manufacturers still retained the right to use the ideas in their trade secrets, but they lost the right to exclude others from using those ideas. The Court recognized that for trade secrets "the right to exclude others is central to the very definition of the property interest" for which just compensation was sought. Monsanto, again like Kaiser Aetna, and like incumbents post-1996, did not lose all of its property when the law extinguished its right to exclude. Even so, the Court insisted:

That the data retain usefulness for Monsanto even after they are disclosed... is irrelevant to the determination of the economic impact of the EPA action on Monsanto's property right. The economic value of that property right lies in the competitive advantage over others that Monsanto enjoys by virtue of its exclusive access to the data, and disclosure or use by others of the data would destroy that competitive edge.\textsuperscript{112}

That factor caused \textit{Penn Central's} expectations prong to tip decisively in favor of Monsanto for those trade secrets disclosed while the law had promised EPA secrecy.\textsuperscript{113}

On the other hand, other regulatory-takings decisions create analogies much more favorable to Congress and the FCC, in particular rent-control regulations. Rent-control laws parallel section 251's interconnection provisions in that they relate in part to the right to exclude. A tenant may not move into an apartment until the apartment owner has in one way or another surrendered the right to exclude. Rent control laws also parallel section 252's rate-regulation provisions in that they restrict the price the landlord may set for surrendering his right to exclude.

The rent-control cases are especially revealing because they highlight the tensions between the Libertarian and Realist renditions of \textit{Penn Central}. Courts can easily shift the focus in rent-control cases on the ground that they do not really implicate the right to exclude. Rather, Realists argue, they merely implicate the lesser right to alienate a present estate, and even then they merely limit the price at which the estate may be alienated. At a high level of generality, the Supreme Court settles rent-control cases on the basis of a factor it calls "required acquiescence." The legal notion of required acquiescence has its roots in another case involving the FCC—\textit{FCC v. Florida Power Corp.}\textsuperscript{114}

The law under challenge in \textit{Florida Power Corp.} regulated the negotiations between local utility companies and cable companies that wanted to buy or

\textsuperscript{111} \textit{Id. at} 1011.
\textsuperscript{112} \textit{Id. at} 1012.
\textsuperscript{113} \textit{Id. at} 1013-14. For a closer analysis of trade-secret takings cases, see Richard A. Epstein, \textit{The Constitutional Protection of Trade Secrets Under the Takings Clause}, 71 U. Chi. L. Rev. 57 (2004).
\textsuperscript{114} 480 U.S. 245 (1987).
lease access to utility poles. The law did not deserve Loretto treatment because it concentrated only on regulating prices and because it did not impose on the utilities any duty to provide the cable companies with access to their poles. In the Court’s explanation: “it is the invitation, not the rent, that makes the difference. The line which separates [this case] from Loretto is the unambiguous distinction between a . . . lessee and an interloper with a government license.” By inference, if the law in question gives an interloper license to trespass, it triggers the concerns that informed Loretto, Kaiser Aetna, and other cases that balance the Penn Central factors in a Libertarian spirit.

But many of the rent-control cases follow Realist tendencies much more than cases such as Florida Power Corp. would suggest. The Supreme Court generally does not believe that governments will disrupt owner expectations or encourage bad social consequences if they restrain landlords’ power to rent at the prices of their choosing. Moreover, if a rent-control law deprives a landlord of a few incidents of the right to exclude while still respecting his right to get out of the business, the law does not raise the same concerns about chilling effects as Loretto. Thus, in Yee v. City of Escondido, the Supreme Court declined to give per se Loretto treatment to a combination of rent-control laws and a law that restrained trailer-park landlords’ rights to veto tenants’ attempts to assign their leases, in part because the landlords could evict tenants upon deciding to change the use of their land.

As these case analogies suggest, the key issues are not doctrinal but substantive—the substantive issues that divide Libertarian property theory from Realist property theory. To conclude that the incumbents deserve just compensation, it helps to appeal to behavioral and normative claims closely associated with the Libertarian approach, including the following: at least presumptively, common carriers have substantially as much claim to the right to exclude competitors as do land owners and intellectual-property owners. This claim may follow because phone companies deserve to reap what they sow on the same terms as other owners, because most regulated industries need to be secure in the contours of their businesses to protect their sunk costs, or perhaps because investments in telecommunications are especially deep and precarious in comparison to land and the property held in other industries.

If this starting presumption is valid, it is not crucial that the right to exclude plays different roles for land owners, intellectual-property owners, and utilities. Takings law can adjust for any differences between different species of property when it comes time to determine just compensation. Nor is it crucial

115 Id. at 247-50.
116 Id. at 251-53.
118 See, e.g., Block v. Hirsh, 256 U.S. 135 (1921).
119 503 U.S. at 522-32.
120 See Regulation, Institutions, and Commitment, supra note 86.
to inquire whether particular state or local franchise agreements guaranteed to incumbents, in any clear terms, the right to exclude competitors from their networks. The incumbents' rights and regulatory treatment, in the words of *Kaiser Aetna*, could still have led "to the fruition of a number of expectancies embodied in the concept of 'property'—expectancies that, if sufficiently important, the Government must condemn and pay for..."\(^{121}\) Of course, these expectancies can be hard to identify, especially in an area such as telecommunications where common-carrier obligations blur the lines between access and exclusion. Even so, the Libertarian approach still insists that it is worthwhile to draw such lines. The right to exclude serves as a formal proxy for the substantive end of protecting some domain within which incumbents are free to deploy and redeploy capital, invest in new technology, make pricing decisions, and do all of the foregoing secure in the knowledge that they and only they will reap the good and bad consequences of their choices. When the law extinguishes or sharply rearranges those zones of freedom, it disrupts a wide web of expectations about the connection between legal rights, work, and reward. These disruptions would be felt most directly in local telephony, and to a lesser but still-perceptible extent in other industries in which Congress could apply the same principles. The 1996 Act ought to be discounted, general Libertarian principles suggest, by the extent to which those disruptions chill the productive use and control of property in the future.

Understood in these terms, a per se compensation rule does not compensate out of sheer formalism: the formal requirements of just compensation have the substantive effect of discounting the 1996 Act as much or as little as it shortchanges incumbents' stranded costs. The more that the incumbents (and AT&T before them) have already recovered in state and local ratemaking proceedings, the less they will deserve in just compensation. Similarly, the higher the profits that the incumbents recover in the long-distance industry post-1996, the less they will deserve in just compensation. A per se or near-per se taking rule would require Congress simply to make up any shortfall left by these two sources and the FCC's TELRIC payments. Within Libertarian horizons, such payments would be a small price to pay to secure investment and innovations in research-intensive industries.

On the other hand, to conclude that Congress and the FCC ought to prevail, it helps to appeal to corresponding behavioral and normative claims that follow from the Realist understanding of property. Within this understanding, one presumes that the right to exclude, like any other formal right, is not transferable from land and intellectual property to common carriers unless specific evidence suggests otherwise. And a Realist could plausibly conclude that there is not enough evidence to rebut this presumption in the field of telecommunications. Land might be special because it is tangible and

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\(^{121}\) 444 U.S. at 179.
because Americans, by long history and tradition, have built up strong expectations about it. Intellectual property rights might be special because patent and copyright monopolies are more time-sensitive than utility franchise monopolies. In addition, in contrast with land and intellectual-property owners, telecommunications companies have never had an unqualified right to exclude. They have always owed a duty to provide access to customers. While they may have enjoyed the right to conduct the operations of their franchises exclusively, the broad distinctions between the exclusive and open aspects of their businesses have always left gray areas. In particular, they have owed a duty to interconnect competitive access providers, which the FCC imposed on the incumbents by regulation in the 1980s. Similarly, as William Baumol and Thomas Merrill have argued, many state and local franchise agreements did not specifically guarantee that incumbents would enjoy exclusive control over local exchanges. They merely provided a "permissive authorization" to build such exchanges. And even if telecommunications companies are exposed to the threat that governments might expropriate their capital, that risk is just a risk. Strictly in principle, it is just as likely that telecommunications companies have extracted rent from governments and customers as it is that the latter have extracted rent from them.

A good Realist would also stress all the social costs that would follow if Congress were required to pay just compensation whenever it should readjust the rights and obligations of common carriers. Congress would never have considered innovations as far-reaching as the pro-competitive effects of the 1996 Act. If Congress's hands were thus tied, it would have a very difficult time responding if telecommunications carriers captured the FCC, or if economic conditions changed in ways that required new approaches to regulation. In principle, a Realist would argue, there is no reason to value long-term investment goals more than short-term competitiveness goals; as an empirical matter, he would add, there is no way to say which would have a greater impact long-term. Indeed, the gains from opening local phone markets are more specific and concrete than the relatively diffuse gains from encouraging investment. Such instincts explain and lend force, for instance, to Jim Chen's argument that per se compensation rules would "pose a serious obstacle to structural reform of utility markets."123

Finally, a good Realist would want to view the 1996 Act holistically, and argue that it would exalt form over substance to say that the Act extinguished incumbents' right to exclude competitors. Both pre- and post-1996, the incumbents had ceded the right to exclude, and they owed duties not to discriminate and to provide access to the local exchange at reasonable rates. Pre-1996, the companies owed those duties to customers, while post-1996, they owed those duties to competitors, but in either case the incumbents never

122 Baumol & Merrill, supra note 5, at 1047 & n.39 (citing Priest, supra note 17, at 303).
123 Chen, supra note 5, at 1688.
The Telecommunications Act of 1996 enjoyed an unqualified right to exclude. Moreover, the 1996 Act guaranteed the incumbents some compensation from competitors, in the form of TELRIC rates. The Act also created new opportunities for them to profit in long-distance markets. Given this complex redistribution, better not to insist on a rigid approach that formalistically treats these various rights as different; better instead to treat the whole redistribution as a legislative policy judgment. Since the Act aimed to promote competition, the character of Congress's action would rate high, and the Penn Central balance would tip in favor of Congress.

C. Just Compensation

The same policy questions also lurk beneath the questions relevant to just compensation. Let us assume that the 1996 Act's local-exchange provisions do inflict regulatory takings on the incumbents. Under any theory of the Takings Clause the 1996 Act takes private property for public use, because it restructures a public network while still keeping it public. The next and last doctrinal step is to determine the just level of compensation to which the incumbents are entitled. If one subscribes to Libertarian assumptions about property and takings, the doctrine leaves room for the incumbents to receive the value they expected to receive in state rate proceedings, minus the money they receive from TELRIC payments, ongoing local service, and new benefits that the 1996 Act conferred to them. But if one subscribes to Realist assumptions, the doctrine also leaves room to limit the incumbents' just compensation only to the value of the rights that the Act gives them anyway—the rights to ratemaking payments and long-distance service.

At a high level of generality, it is well accepted that owners are entitled to fair value for the private property taken from them, minus any compensation that the condemning law makes in the form of money payments or in-kind compensation. As the Supreme Court has explained, the owner who suffers a taking should be placed "in as good a position pecuniarily as if his property had not been taken." If one passes over exceptions not relevant here, as a starting point the owner is entitled to receive "what a willing buyer would pay in cash to a willing seller." If, however, the law that inflicts the taking also provides other sources of compensation, the claimant's compensation needs to

124 This conclusion is beyond cavil under prevailing federal law, which decides public-use issues on deferential "rational basis" grounds. See, e.g., Haw. Hous. Auth. v. Midkiff, 467 U.S. 229 (1984); Berman v. Parker, 348 U.S. 26 (1954); see also Baumol & Merrill, supra note 48, at 1130 n.39. But even the most suspicious public-use cases allow the government to take private property and create a public right of access to it. See, e.g., Southwestern Ill. Dev. Auth. v. Nat'l City Envtl., 768 N.E.2d 1, 9 (Ill. 2002) ("Gateway's racetrack may be open to the public, but not 'by right.'"). In substance, the interconnection and franchise-repeal provisions of the Act create a public right of access in local exchanges.


126 United States v. 546.54 Acres of Land, 441 U.S. 506, 511 (1979) (citing United States v. Miller, 317 U.S. 369 (1943)).
be discounted appropriately. This requirement has long been recognized in takings case law,\textsuperscript{127} is supported by the Supreme Court’s “reciprocity of advantage” case law,\textsuperscript{128} and has been developed extensively in recent takings scholarship about implicit in-kind compensation.\textsuperscript{129}

It is fairly easy to identify the factors that drop the incumbents’ compensation to reflect offsetting reciprocal advantages. The first is a source of explicit compensation. The TELRIC rates explicitly compensate the incumbents for carrying the local services of the competitors.\textsuperscript{130} The second source consists of any source of in-kind compensation provided by the Act. The most obvious in-kind compensation consists of the new right, conferred on incumbents by section 271 of the Act, to compete in long-distance markets.\textsuperscript{131} As William Baumol and Thomas Merrill argue (and as no one seriously disagrees), incumbent carriers will receive a “valuable quid pro quo . . . in the form of access to the long-distance market.”\textsuperscript{132} To the extent that other provisions of the Act compensate the incumbents in kind along the lines of section 271, the incumbents’ just compensation should be discounted appropriately:

A third source to consider are incumbents’ ongoing and forward-looking profits in the local phone-service business. This downward adjustment is needed to preserve the symmetry between the interconnectivity rules and a hypothetical case in which Congress completely extinguishes the incumbents’ rights over local service. This symmetry is comparable to the symmetry in land cases between total condemnations which takes the fee, and a

\textsuperscript{127} See, e.g., Paxson v. Sweet, 13 N.J.L. 196 (1832) (rejecting a takings challenge to a law that required home owners to pave the sections of public streets in front of their homes on the ground that the owners received just compensation in the form of better access to public facilities and their neighbors’ homes).


\textsuperscript{129} See, e.g., Michelman, supra note 72, at 1225.

\textsuperscript{130} To the extent that TELRIC payments are part of the incumbents’ constitutional just compensation, courts will need to consider many procedural details of TELRIC that might not otherwise take on constitutional significance. For example, incumbents and the FCC are now engaged in administrative disputes about the uncollectibility problem. Incumbents want the right to refuse to interconnect a competitor on the ground that the competitor stands a real chance of not being able to pay its TELRIC bills after it gets access, or at least to require such a competitor to front security deposits or advance payments as a condition before interconnecting. By contrast, the FCC has not ruled these procedures out, but it has discouraged the incumbents from invoking them. See, e.g., In the Matter of Verizon Petition for Emergency Declaratory and Other Relief, WC Docket No. 02-202 (Released Dec. 23, 2002), FCC 02-337, available at http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-02-337A1.doc (last visited Apr. 18, 2005). The FCC spelled out its recommended procedures in id. ¶ 26. Assuming that the Act effects a taking, such rules drive down the just compensation that incumbents get through rates set under section 252 of the Act, and drive up any payment to which they are entitled after discounting for the rates they get and the sources of implicit in-kind compensation discussed in this part.


condemnation for a right of way, such as in *Kaiser Aetna*. When an owner loses a right of way, she loses her right to exclude outsiders, but not her right to possession of the right of the way. A similar symmetry applies in *Monsanto* and other cases involving exclusive intellectual property. If the government nationalizes a trade secret and takes over the owner’s monopoly, the owner is entitled to just compensation for the fair market value of the secret. By contrast, if the government only discloses the trade secret, it leaves the owner to compete in the newly-competitive market. The owner’s just compensation still compensates the owner for losing its monopoly, but no longer for losing its right to compete. In telecommunications, although the incumbents lose franchises and exclusive control over local exchanges, they still retain ownership of the local exchanges and the right to compete in local markets.

However, while it is easy to identify the factors that lower the appropriate measure of just compensation, it is not as easy to put a dollar value on the crucial rights taken. A few are easy to identify, particularly the physical-collocation requirements of section 251(c)(6). These provisions entitle the incumbents to the market value of the office space taken by competitors and any costs the incumbents must spend to help the competitors use that office space productively. However, it is much more difficult to determine the just level of compensation for the interconnectivity provisions of section 251 and the franchise-preemption language of section 253. Common-carrier regulation often applies to industries that are natural monopolies; it is difficult to assess the value of businesses that have no natural competitors.

On this point, the most relevant precedent is probably *Monongahela v. United States*. In that case, Pennsylvania had chartered a franchise with the Monongahela company to build locks and dams along the Monongahela River. Pennsylvania compensated the company with an exclusive franchise to operate the locks and the power to set tolls in order to recoup its investments. Later, however, Congress passed a law directing the Secretary of War to take one lock and dam. The act that provided for the taking also specified that, when the Secretary calculated just compensation, “the franchise of said corporation to collect tolls shall not be considered or estimated.” The federal condemnation stands in the same relation to the 1996 Act as the Pennsylvania act of incorporation stands to the state laws and agreements that vested franchises in

133 *See* Epstein, supra note 113, at 62-63.
136 148 U.S. 312 (1893).
137 *See* id. at 313-15.
138 *Id.* at 313.
AT&T and then later in incumbents. In each case, state law created a franchise and federal law subsequently terminated it.\(^{139}\)

The Court concluded that the Monongahela company was entitled to the discounted present value of the tolls it would and could have charged under its state franchise. Generally speaking, the Court observed that just compensation turns on an understanding of value that "is not determined by the mere cost of construction, but more by what the completed structure brings in the way of earnings to its owner."\(^{140}\) When Congress took the lock and dam, it deprived the Monongahela company "of the aggregate amount of such compensation which otherwise it would continue to receive."\(^{141}\) Because Pennsylvania had guaranteed the Monongahela company the right to charge tolls as part of its franchise, "these tolls, in the nature of the case, must enter into and largely determine the matter of value."\(^{142}\) "[I]f the property is held and improved under a franchise from the State, with power to take tolls," the Court insisted, "that franchise must be paid for, because it is a substantial element in the value of the property taken."\(^{143}\)

Under *Monongahela* and the general principles it reflects, the incumbents are entitled to compensation comparable to the value of their franchises under state law. State and local franchises gave incumbents power to recoup their investments by charging regulated rates for local phone service. To measure the economic value of those franchises, one important source of value includes the discounted present value of those regulated rates. If state or local regulators had posted such rates in regular schedules, in regulations or in contractual franchise agreements, the law would discount the scheduled rates to present value. However, as recounted in Part I, many if not most state and local utility regulators shifted from a franchise model to ongoing and ad hoc rate-of-return regulation during the twentieth century.\(^{144}\) Where and when rates are set on such an ad hoc basis, *Monongahela*’s rule of decision requires courts to forecast the rates that the incumbents would have recovered if the 1996 Act had not displaced state regulation, and then discount those rates to their present value.

This conclusion also helps explain why many commentators\(^ {145}\) and the Supreme Court *Verizon v. FCC* opinion\(^ {146}\) have assumed that courts should apply confiscatory-ratemaking principles to takings challenges to the 1996 Act. Even if rate-of-return principles are inapposite at the takings stage, they focus on

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\(^{139}\) *See id.* at 341 (noting that Congress has superior power to take state franchises, "even against the will of the State; but it can no more take the franchise which the State has given than it can any private property belonging to an individual").

\(^{140}\) *Id.* at 328.

\(^{141}\) *Id.*

\(^{142}\) *Id.* at 329.

\(^{143}\) *Id.* at 337; *see also id.* at 329.

\(^{144}\) *See Priest, supra* note 17, at 301-23; *Kennedy, supra* note 13, at 5-17.

\(^{145}\) *See Chen, supra* note 5; *Legg, supra* note 7.

\(^{146}\) *See 535 U.S.* at 523.
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c onsiderations that are extremely relevant to the just compensation issues that follow from a per se theory. To the extent that constitutional rate-of-return principles have long informed and limited incumbents’ local rates under state law, those principles help forecast how much state and local franchises would have been worth if the 1996 Act had not become law.

Under those principles, the incumbents are entitled to recover some measure of their investment and a rate of return reasonable for an industry with a risk profile similar to the profile for local telephony.147 Ratemaking law has traditionally left state regulators with broad discretion to determine how much utilities have lost in sunk costs and whether those costs are prudent. Regulators are “not bound to the use of any single formula or combination of formulae in determining rates.”148 Given this flexibility, Monongahela’s general prescription would probably still leave Congress and the FCC some flexibility to adjust federal compensation to reflect the possibility that incumbents profited in particular states more than prudent rate-of-return principles require. And again, the just-compensation calculus would then need to deduct for what the incumbents continue to make in the local market, the profits they make in long distance, and the rates they recover from the TELRIC formula. But by and large, state ratemaking and its constitutional limits set the benchmark from which these deductions are subtracted.

This approach has come under two separate types of criticism. One criticism holds that this approach does not compensate the incumbents enough. Most recently, Daniel Spulber and Christopher Yoo have argued that the incumbents are entitled to just compensation based not on constitutional-ratemaking law but rather on the fair market value of the access rights that they are required to surrender under the Act and TELRIC regulations. The incumbents’ just compensation for mandatory interconnection, they argue, “depends on what the company could have obtained by selling network services.”149 Since “the emergence of platform competition and the shift from rate regulation to access regulation have now made it possible to base rates on market benchmarks,”150 they conclude that “ideally the purchase cost of inputs would represent a good approximation of the earning potential—and thus the market value—of those inputs.”151

147 See Smyth v. Ames, 169 U.S. 466, 547 (1898) (fair value); FPC v. Hope Natural Gas Co., 320 U.S. 591, 603 (1944) (prudent historical costs). For discussions of the similarities and differences between the two standards, see EPSTEIN, supra note 40, at 307-09; Chen, supra note 5, at 1679-85; Spulber & Yoo, supra note 6, 908-12.

148 Hope Natural Gas, 320 U.S. at 602.

149 Spulber & Yoo, supra note 6, at 903.

150 Id. at 911; see also id. at 900-07 (canvassing several different ways to use market mechanisms to price network rates).

151 Id. at 891.
I cannot render any definitive judgment on the economic merits of Spulber and Yoo’s proposal. At the same time, it is safe to say that their proposal is not required as a matter of black-letter takings law, and that there are understandable policy reasons why not. Ordinarily, as Spulber and Yoo observe, just-compensation looks to the market value of the property taken. In particular, as the U.S. Supreme Court made clear in *Monongahela* (on which Spulber and Yoo rely substantially), when it comes to “property devoted to a public use, the amount of compensation [is] subject to the determination of the . . . State which authorized the creation of the property.” If the state establishes tolls as the method of compensation, “these tolls, in the nature of the case, must enter into and largely determine the matter of value.” Without making any final judgments, this doctrinal exception is not unreasonable as a matter of policy. When a state uses its power to grant a franchise for a bridge, rail line or phone network, more often than not there is no meaningful market for the asset created under the franchise. State-allowed rates are at least as accurate a source of valuation as any other source, and they are especially useful in that they let states control the terms on which—and particularly the exposure under which—they create franchises and other quasi-property.

Another possible criticism of the proposal presented in this Part is that it compensates the incumbents too much. These criticisms have been made most forcefully in opposition to J. Gregory Sidak and Daniel Spulber’s thesis of the “regulatory contract.” In an article and then a subsequent book, Sidak and Spulber have argued that some features of pre-1996 regulation entitled

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152 Their proposal would certainly make takings law easier, for it would be administratively much easier to set just compensation by market value than by the approach prescribed in this Section. That advantage, however, would be a one-time-only benefit, and others have warned that market-value compensation would seriously discourage technological innovation in the long-term market for local telephone services. See Chen, supra note 5, at 1688; Adam Candeub, *Network Interconnection and Takings*, 54 SYRACUSE L. REV. 369, 426-27 (2004). Both Chen and Candeub cite and rely on arguments propounded by Nicholas Economides, *The Tragic Inefficiency of the M-ECPR, in Down to the Wire: Studies in the Diffusion and Regulation of Telecommunications Technologies* 140-51 (A. Shapine ed., 2003). Spulber and Yoo defend their proposal on its substantive merits in Spulber & Yoo, supra note 6, at 895-900, and attack the standard alternatives in id. at 908-14.

153 See Spulber & Yoo, supra note 6, at 952 (citing Olson v. United States, 292 U.S. 246 (1934); Boom Co. v. Paterson, 98 U.S. 403 (1878)).

154 See id. at 953 (citing United States v. 50 Acres of Land, 469 U.S. 24 (1984); Kimball Laundry v. United States, 338 U.S. 1 (1949)).

155 See id. at 950.


157 See id. at 337 (“If that property be improved under authority of a charter granted by the State, with a franchise to take tolls for the use of the improvement, in order to determine the just compensation, such franchise must be taken into account . . . .”).

158 Sidak & Spulber, supra note 6.

incumbents to recover prudent historical costs through ratemaking. Now, the proposal in this Part differs from Sidak and Spulber’s argument in one important respect: while Sidak and Spulber contend that the incumbents are entitled to all prudent historical costs, the analysis presented here suggests that they are entitled only to the likely discounted present value of the rates they expected to recover in each state. If a state refused to pay for prudent historical costs and applied some other, less-generous but still constitutional methodology, the incumbent would be entitled to the latter level and not the former. Even so, both approaches posit that the incumbents were entitled to compensation whenever government regulators extinguished their franchises and their control over local exchanges.

Sidak and Spulber’s claim has come under serious criticism because it seems to run contrary to the “unmistakeability” doctrine, a rule of construction which holds that governments should be held only to contractual promises they make in unmistakable terms. This doctrine has led commentators to criticize Sidak and Spulber’s proposal. If states did not explicitly promise that they would set or maintain rates at any fixed level, the argument runs, the incumbents may not claim that they are legally entitled to any specific rate figures in the future, whether through rate-making under the 1996 Act or in a just-compensation proceeding. As Herbert Hovenkamp argues, “public utility investors get from the state precisely what they are able to bargain for, no more and no less.”

This split between Sidak and Spulber and their critics highlights the last tension between Realist and Libertarian approaches to takings. Both approaches can accommodate some version of the unmistakeability doctrine, but they differ about how aggressively to apply it. Realist theory lends itself to an aggressive interpretation of the doctrine. It tends to construe private owners’ expectations narrowly to preserve in government broad freedom of regulatory action. Libertarian theory, by contrast, construes the unmistakeability doctrine more narrowly. The Supreme Court recognized as much when it insisted in Monongahela that franchises are “a vested right,” which may be retaken only “upon the payment of just compensation.” If and when the government extinguishes franchises, the Libertarian approach suggests, the unmistakeability doctrine need not and should not apply. Claimants are entitled to receive the most likely approximate value of their franchises. If state tolls or rates provide

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160 See Sidak & Spulber, supra note 6, at 878-79.
161 To this extent the analysis presented herein accords with a criticism made of Sidak and Spulber by Baumol & Merrill, supra note 5, at 1050.
164 Monongahela, 148 U.S. at 341.
the best available evidence of that value, then those tolls or rates are relevant, even if the government did not promise unmistakably and unambiguously that it would continue to provide those rates.

Thus, the just-compensation stage raises policy disagreements that are as fundamental and pronounced as the disagreements at the takings stage. If the incumbents have property in their franchises and freedom not to carry to the extent that Libertarian theory prescribes, it follows that the incumbents are entitled to recover from Congress costs left over from state ratemaking after enforcement of the 1996 Act. Just-compensation law commits Congress to pay incumbents the leftover value of future state rate regulation as the price to be paid to protect and encourage long-term investment in telecommunications as elsewhere. But if those franchises and freedom-from-carriage expectations have as little social value as Realist theory suggests, the incumbents should be satisfied with the compensation they get from TELRIC and the profits from current lines of business. Realist theory increases the burden the incumbents need to overcome to prove that they are entitled to the discounted value of now-terminated future state ratemaking proceedings; the theory increases that burden because it doubts that the 1996 Act chills long-term investments as direly as Libertarian theory assumes. The fundamental debates are the same.

IV. Conclusion

Policymakers and telecommunications scholars have tended to assume that the law of takings is straightforward: that takings doctrine comes in one of three simple varieties, and that one of these varieties clearly applies to the 1996 Act. In reality, however, takings doctrine reflects at a higher level of generality many of the same theoretical and policy tensions with which policy makers have been grappling in telecommunications. Some elements of takings theory stress that the law ought to protect long-term interests including individual ownership, flexibility, and the incentive effects that follow. Other elements of takings theory suggest that such long-term interests are nebulous and hard to measure. They prefer to narrow the scope of constitutional private property to owners' firmest expectations. They presume that it is better not to tie Congress's hands and frustrate concrete and immediate legislative goals. Both elements are well enough represented in takings law to give most participants credible takings arguments in the debate over the 1996 Act.

It is both troubling and encouraging to learn that takings law does not resolve the 1996 Act controversy as certainly as has been suggested in the literature to date. On the one hand, it may be troubling to know that takings doctrine cannot impose certainty or order on the policy issues that inform telecommunications law. On the other, it is encouraging to appreciate that the law of takings can at least focus and sharpen the debate. If the cases and the doctrines are understood properly, takings law can connect the most immediate issues that arise under the 1996 Act to the most enduring questions raised by
property—the proper relation between government action and individual initiative.