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⁴/₁₉ Technology Convergence and Federalism: The Case of VoIP Regulation

Daniel A. Lyons — April 19, 2012

The Vermont Supreme Court may soon consider whether federal law permits the Public Service Board to regulate certain voice-over-internet-protocol (VoIP) services.¹ Across the Hudson, Governor Andrew Cuomo recently sought to bar the New York Public Service Commission from adopting similar regulations.² And these states are not alone: from Maine to Florida, several states are considering whether their jurisdiction over traditional telephone service encompasses this new technology, through which nearly one-third of American landline households receive telephone service.³ If so, nationwide VoIP providers could face up to fifty new legal regimes with which they must comply before offering service. If not, consumer migration away from traditional telephone service could leave state regulators with little to regulate.

The VoIP battle is the latest example of regulatory confusion caused by the increasingly anachronistic Communications Act.⁴ The Act allocates jurisdiction between the federal government and the states based on the nature of the service and the network over which it is offered. As convergence increasingly blurs lines that the Act seeks to keep distinct, companies and regulators struggle in vain to fit new technologies into outdated regulatory categories.⁵ The fight illustrates the need for a new platform-neutral model that avoids the uncertainty and disparity that the silo-based model engenders.

The Challenge of VoIP

VoIP illustrates the seemingly simple, yet deceptively complex, regulatory challenge posed by convergence. Traditional telephone service is governed by Title II of the Act, which grants the Federal Communications Commission jurisdiction over interstate service but leaves intrastate communications to the states.⁶ By comparison, most Internet services are Title I “information services,” which are largely preempted from state regulation.⁷ VoIP mimics traditional telephone service, but transmits over the Internet rather than the public switched telephone network. Can states regulate a Title II service carried over a Title I network?

For nearly a decade, the Commission has refused to answer this question. It has explained that “non-interconnected” VoIP service, which uses the Internet rather than the telephone network to carry voice traffic between two computers, is exempt from state regulation under Title I.⁸ When Minnesota sought to regulate Vonage’s “interconnected VoIP” service, which can carry calls between a computer and a traditional telephone, the Commission preempted the state without classifying the service.⁹ Even if, as Minnesota claimed, interconnected VoIP falls under Title II, state regulation would be preempted under the “impossibility” exception,⁶ which treats a service as interstate if one cannot separate its interstate and intrastate components. The Commission explained that although Vonage customers used normal telephone numbers, it was impossible to determine the geographic location of a Vonage user because a user could place a call from a computer anywhere in the country. Therefore, VoIP calls simply could not be classified with precision as intrastate or interstate.

Shortly thereafter, several states identified a potential gap in the Vonage decision. While the impossibility

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exception applied to “nomadic” VoIP services such as Vonage, the same logic did not apply to “fixed” VoIP service. Like nomadic VoIP, fixed VoIP service delivers calls primarily over the Internet. But unlike nomadic VoIP, fixed VoIP uses a normal telephone that plugs into a wall jack. To the end user, therefore, fixed VoIP looks nearly identical to traditional telephone service; the only difference is the way the call is delivered. More importantly, because the telephone is fixed, the caller’s geographic location is easy to identify. This distinction is potentially significant: fixed VoIP providers are becoming an ever-increasing portion of the telephone market. For example, Comcast Corporation’s DigitalVoice fixed VoIP service has become America’s third-largest telephone company. The question whether the Communications Act distinguishes between nomadic and fixed VoIP service will thus dictate whether state regulators will continue to remain relevant as the industry evolves.

The Future of VoIP

The states’ ongoing struggle illustrates the regulatory uncertainty fostered by the Act. That uncertainty also affects the industry: while VoIP has been gaining market share, many telecommunications companies admit failing to embrace the technology fully because they do not yet know the regulatory costs of doing so. Or in economic terms, this regulatory uncertainty leads companies to under-invest in VoIP technology because the costs of regulatory compliance are unknown, and therefore the potential benefit must be discounted by that risk. For this reason, Verizon and others have lobbied states with limited success to preemptively deregulate VoIP service. Both the states’ ongoing efforts and the industry’s lobbying represent substantial transaction costs attributable solely to the Act’s artificial divide.

In the short run, the Commission should end this battle by classifying all VoIP under Title I. State regulation of intrastate telephone service is an artifact from an era when customers distinguished between local and long-distance service, and when state services were dominated by local monopolies that needed regulatory oversight. Since wireless companies began offering bundled local and long-distance service, this distinction has grown increasingly irrelevant. And in almost all areas, VoIP service competes against the incumbent telephone company, and often other landline telephone companies and wireless providers, for customers. If states are permitted to regulate these new emerging services like they did the old telephone monopoly, it could create barriers to entry that can hinder the growth of this new technology and retard the benefits of competition in voice service.

More fundamentally, the VoIP battle shows why the Act must yield to the telecommunications infrastructure of the future. Companies simply do not offer monoline telecommunications services over single-purpose networks anymore, and the law should reflect this reality. Even AT&T, the original telephone monopoly, admits that “with each passing day, more and more communications services migrate to broadband and IP-based services, leaving the public switched telephone network and plain old telephone service as relics of a by-gone era.”¹¹ Hulu and Netflix are harbingers of a similar transition with regard to video service. Going forward, voice and video will be simply two of many applications that ride on top of the public Internet, which consumers may reach through myriad potential platforms. Congress should allocate jurisdiction over that network between the federal government and the states in a platform-neutral manner. The federal government is in the best position to regulate issues such as rates, market entry, and universal service, issues that, if left to the states, would create substantial spillover effects that could disrupt national economies of scale. By comparison, states should regulate issues such as rights-of-way access, which depend on local knowledge and which federal regulators lack the ability and inclination to adjudicate properly. This unified framework would better fit the telecommunications architecture of the next century and would avoid the uncertainty and distortion inherent in the existing silo-based model.

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1. See Order Closing Docket, Vermont Public Service Board Docket No. 7316 (Feb. 2, 2012), available at <http://psb.vermont.gov/sites/psb/files/orders/2012/7316%20ClosingOrder.pdf>.
2. See Beecher Tuttle, *Cuomo Loosens VoIP Regulation*, TMCNET.COM (Mar. 26 2012), <http://www.tmcnet.com/channels/mobile-voip/articles/280779-cuomo-loosens-voip-regulation-may-encourage-industry-expanding.htm>.
3. *FCC Extends Outage Reporting Requirements to VoIP Providers*, TR DAILY, Feb. 15, 2012.
4. 47 U.S.C. § 151 (2006).
5. See Daniel A. Lyons, *Technology Convergence and Federalism: Who Should Decide the Future of Telecommunications Regulation?* 43 U. MICH. J.L. REFORM 383 (2010).
6. 47 U.S.C. § 152(b) (2006).
7. See, e.g., Vonage Holdings Corp., 19 FCC Rcd. 22404, 22416–17 (2004) (describing Commission’s longstanding policy of preempting information services regulations).
8. Petition for Declaratory Ruling that Pulver.com’s Free World Dialup is Neither Telecommunications nor a Telecommunications Service, 19 FCC Rcd. 3307 (2004).
9. Minn. Pub. Util. Comm’n v. FCC, 483 F.3d 570, 575–76 (8th Cir. 2007).
10. 47 U.S.C. § 152(b) (2006).
11. International Comparison and Consumer Survey Requirements in the Broadband Data Improvement Act, GN Docket No. 09–47, 09–51, 09–137 (Fed. Commc’ns Comm. 2009) (cmt. of AT&T Inc.), available at http://www.teledynamic.com/_uploads/AT&T%20Comments%20On%20Ending%20PSTN.pdf.

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