Swerving to Avoid the Takings and Ultra Vires Potholes on the Information Superhighway: Is the New York Collocations and Telecommunications Policy a Taking under the New York Public Service Law

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by

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Table of Contents

I. Takings Jurisprudence ................................... 55
   A. Takings by Physical Invasions .................... 57
   B. Takings by Regulatory Action ...................... 61

II. Collocation Decisions of the New York Public Service Commission ............................................ 64
   A. The New York Public Service Commission Requires Virtual Collocation for Private Line Service ........ 65
   B. Implementation of Virtual Collocation for Private Line Service ........................................ 67
   C. Task Force Recommendations ...................... 70
   D. Physical Collocation for New York Telephone's Private Line Services .................................... 71

III. New York Collocation: Is It a Per Se or Regulatory Taking? .............................................. 73
   A. Analysis of New York Collocation as a Per Se Taking ................................................. 73
      1. Traditional Loretto Analysis ..................... 73

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2. Consent .................................................. 76

B. Analysis of New York Collocation as a Regulatory Taking .............................................. 76
   1. Rational Basis—Do the Collocation Decisions Substantially Advance A Legitimate State Interest? .................................................. 76
   2. Character of the Government Action .......... 78
   3. Diminution in Economic Value ................. 79

IV. Is the New York Public Service Commission’s Decision to Order Collocation Ultra Vires? ................. 81

V. Conclusion .................................................. 83
Introduction

In its land use regulation cases, the Supreme Court has set out fairly definitive tests for determining whether a regulation is a taking. It should come as no surprise that regulatory agencies dealing with land use issues will attempt to structure their regulations in such a way as to avoid a taking. Agencies follow this course because of the fear and uncertainty that all takings—no matter how small—must be compensated at fair market value.

1. Recently, with the advent of more conservative justices, the Supreme Court has handed down two rulings likely to make regulators more cautious by setting new boundaries limiting the leeway that regulators have in avoiding a taking. In Nollan v. California Coastal Comm'n, 483 U.S. 825 (1987), the Nollans owned a beachfront lot in Ventura County, California. The Nollans originally leased their property with an option to buy. The building on the lot was a small bungalow, which for a time the Nollans rented to summer vacationers. After years of rental use, the building on the lot had fallen into disrepair and could no longer be rented. The Nollans' option to purchase was conditioned on their promise to demolish the bungalow and replace it. To complete the demolition, they were required to obtain the permission of the California Coastal Commission. The California Coastal Commission conditioned the Nollans' acquiring a coastal development permit on the Nollans' agreement to provide a public easement across their property. The Supreme Court invalidated this condition because it did not substantially advance a legitimate state interest. The California Coastal Commission believed that these burdens on "access" would diminish if the Nollans gave the public "lateral access" to the beach. The Nollan decision was a far cry from prior rulings, which paid mere lip service to the nexus between the regulation and state interest that the regulation was designed to address. In the past, the causal nexus was generally found to be presumptively valid. See Charles M. Haar & Jerold Kayden, Private Property v. Public Use, N.Y. Times, July 29, 1987, at A23; Frank Michelman, Takings, 1987, 88 Colum. L. Rev. 1600, 1605-1614 (1988); Steven J. Lemon et al., Comment, The First Applications of the Nollan Nexus Test: Observations and Comments, 13 Harv. Envtl. L. Rev. 585 (1989).

Similarly, in Dolan v. City of Tigard, 114 S. Ct. 2309 (1994), the regulator attempted to condition a landowner's acquisition of a permit to build a bigger building upon the granting of a deed to the city; part of the landowner's property was to be used as a bicycle path and greenway. The Supreme Court held that the condition was unconstitutional and devised the rough proportionality test, which put the burden on the state to prove that there was a nexus between the condition and the legitimate state interest that was to be achieved. The Court essentially elevated the level of scrutiny that it would employ in these types of cases.

2. Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982); FCC v. Florida Power Corp., 480 U.S. 245 (1987); Leonard M. Baynes, How Much is the Toll to Access the Information Superhighway: An Analysis of the Appropriate Level of Compensation for the Partial Taking of Public Utility Property, 62 Tenn. L. Rev. 141 (Fall 1994). In many areas of the law, the effective lawyer will advise clients of the status of the law and the permissible ways for the clients to achieve their goals. These permissible ways are colloquially known as loopholes. Because clients expect their attorneys to provide them with this type of advice, it is not surprising that land use regulators attempt to find and use
This Article first examines the current takings jurisprudence that would be applicable to the New York collocation regime:3 (1) per se takings used when the regulation is of a physically invasive nature, and (2) regulatory takings used at other times and employing an ad hoc analysis. The ad hoc analysis considers (1) the character of the regulation, (2) the economic impact on the landowner's investment-backed expectations, and (3) whether the regulation advances a legitimate state interest.

This Article then analyzes each of the relevant New York Public Service Commission (NYPSC) orders in developing its collocation policy4 to determine whether they constitute a taking of New York Telephone Company's property and are ultra vires under the New York Public Service Law. This analysis shows how the NYPSC was able to swerve around the “takings” and “ultra vires” potholes at each step of its proceedings. Through its rulemaking proceedings, the NYPSC was able to set parameters that presented New York Telephone with a Hobson's choice: New York Telephone could either voluntarily agree to a physical invasion of its property—physical collocation—or submit to the NYPSC's order mandating a non-physical invasion—virtual collocation—which would be administratively burdensome.5 Virtual collocation would also increase the risks of po-

3. The Fifth Amendment of the United States Constitution provides that “No person... be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.” U.S. CONST. amend. V. This clause is often referred to as the Takings Clause. For purposes of this article, the Takings Clause shall serve as the basis for takings jurisprudence. The Fifth Amendment is made applicable to the states through the Fourteenth Amendment. See Chicago, Burlington and Quincy R.R. v. Chicago, 166 U.S. 226, 239 (1897). The Fourteenth Amendment of the United States Constitution specifically applies to the states. It provides that “[n]o State... deprive any person of life, liberty, or property, without due process of law.” U.S. CONST. amend. XIV.

4. Collocation involves the placement of a competitor's interconnection equipment in, or in close proximity to, the central offices of a local telephone company. See generally Leonard M. Baynes, The On-Ramp to the Information Superhighway: A Case Study of the New York Collocation and Telecommunications Policy, 7 DEPAUL BUS. L.J. 1 (1994); Baynes, supra note 2, at 147. This placement enhances competition by reducing the costs of interconnection between the networks of local telephone companies and their competitors, which facilitates the competitor's access to the information superhighway. Id. Since the competitor's network is usually less extensive than that of the local telephone company, the competitor often must interconnect with the local telephone company's network to complete telephone calls. Id.

5. New York Telephone also had the option of amending its rate structure in a manner that would foster collocation. See Baynes, supra note 4, at 3-4. Because it would also be administratively difficult to determine who was eligible for special rates and what the rates would be, New York Telephone initially chose a virtual collocation regime. Id. How-
tential antitrust liability, though it probably would not result in a taking. This choice constituted virtually no choice, and led New York Telephone to agree to physical collocation, which was the more invasive, though more administratively efficient measure, in fostering competition.

The NYPSC’s actions and methods in ordering collocation have national implications for takings jurisprudence. They represent a means to force the parties to agree to a burdensome invasion of property without the regulator actually ordering the invasion. This “means to an end” allows regulators to avoid the just compensation requirement of the Takings Clause.

I

Takings Jurisprudence

The cases involving government regulations that take a person’s property cover the spectrum from eminent domain to solely government regulation. The eminent domain cases are classic examples of a government taking of a private person’s property: the government condemns a person’s land for public use and must pay the landowner just compensation for the land. Historically, a taking occurred only when the state condemned land in eminent domain actions. Pennsylvania Coal Co. v. Mahon expanded the scope of takings jurisprudence.

ever, since the PSC imposed increasingly onerous requirements on virtual collocation, New York Telephone found itself in the anomalous position of selecting, monitoring, controlling, and repairing equipment dedicated to its competitors. Id. at 28-33.

6. Id. at 33.

7. Interestingly, the NYPSC also set parameters that presented New York Telephone’s competitors with the same administrative nightmare. The competitors objected to virtual collocation because they were unable to own the collocation equipment and were put in the anomalous position of relying on their competitor—New York Telephone—to select, monitor, control, and repair the equipment. See id. at 28-33.

8. The implications extend far beyond telecommunications and collocation to actions of other regulators, e.g., zoning commissions and environmental protection agencies. These regulators can shape the parameters of their orders to get the desired result: They first regulate the parties in a manner that is, although constitutional, objectionable to the regulated entities. Such regulation may encourage (some may say coerce) the regulated parties to agree to the more burdensome regulation. This more burdensome regulation, if initially ordered by the regulator, would be unconstitutional as a per se taking. However, by first ordering a program that is initially unworkable, the regulator creates an environment that leads the regulated entity to agree to something less burdensome, but perhaps unconstitutional. By the parties agreeing to this otherwise unconstitutional program, the regulator avoids the just compensation requirements of the Takings Clause.


10. 260 U.S. 393 (1922).
dence to include government regulations that went too far, constituting excessive exercises of a state’s police power.\textsuperscript{11}

Since the \textit{Mahon} decision, the Supreme Court has established somewhat rigid boundaries in defining which government regulations are so excessive as to constitute a taking. In essence, there are two relevant categories\textsuperscript{12} for takings cases, which will be employed to ana-

\begin{itemize}
\item \textsuperscript{11} In the \textit{Mahon} case, a landowner transferred title to the surface of his property, but retained title to the subsurface and the right to remove coal from it. \textit{Id}. A statute enacted after the sale of the surface rights prohibited mining so as “to cause the caving-in, collapse, or subsidence” of any occupied land. \textit{Id.} at 393. The Court held the statute violated the takings clause because the prohibition exceeded the state’s police power. The Court stated: “To make it commercially impracticable to mine certain coal has very nearly the same effect for constitutional purposes as appropriating or destroying it.” \textit{Id.} at 414. Therefore, when regulation reaches too great a “magnitude, in most if not in all cases there must be an exercise of eminent domain and compensation to sustain the act.” \textit{Id.} at 413.

\item \textsuperscript{12} The Supreme Court recently established another category for takings analysis, which is not relevant to the issue addressed in this Article. The Supreme Court found a per se taking when a state regulation denied a landowner all economically beneficial or productive use of land. \textit{Lucas v. South Carolina Coastal Council}, 112 S. Ct. 2886, 2893 (1992). The Supreme Court justified its creation of this new per se category on the ground that total deprivation of beneficial use is, from the landowner’s perspective, the equivalent of physical appropriation. \textit{Id.} at 2894 (citing \textit{San Diego Gas & Elec. Co. v. San Diego}, 450 U.S. 621, 652 (1981) (Brennan, J., dissenting)). Such limitations cannot be newly legislated or promulgated without compensation unless they are consistent with the state’s pre-existing law of property and nuisance. \textit{Lucas}, 112 S. Ct. at 2901.

The Supreme Court limited this new rule to regulatory actions that effectively eliminate the land’s only economic productive uses, but it did not proscribe regulatory action against productive uses that are impermissible under relevant property and nuisance principals. \textit{Id.} at 2900-01. The Supreme Court gave two examples: First, the owner of a lake bed would not be entitled to compensation when denied the relevant permit to engage in landfill operations that would have the effect of flooding others’ land. Second, the corporate owner of a nuclear generating plant, found to be sitting above an earthquake fault, would not be entitled to compensation when directed to remove all improvement from its land. \textit{Id.} at 2900.

In \textit{Lucas}, the Supreme Court invalidated a state statute that had the direct effect of barring the landowner from constructing any permanent habitable structure on his property. The 1977 South Carolina Coastal Zone Management Act required any owner of coastal zone land that qualified as “critical area” to obtain a permit from the South Carolina Coastal Council prior to committing the land to “a use other than the use that the critical area was devoted to on [September 28, 1977].” \textit{Id.} at 2889. A critical area was defined in the legislation to include beaches and immediately adjacent sand dunes. \textit{Id.}

In 1986, Lucas purchased the two lots at issue for $975,000. \textit{Id}. The two lots were located on the Isle of Palms in Charleston County, South Carolina. \textit{Id}. The landowner intended to build single family homes on these lots. \textit{Id}. At that time, because no portion of the lots qualified as a “critical area” under the 1977 statute, he was not required to obtain a permit from the Council before engaging in any development activity. \textit{Id.}

In 1988, the South Carolina Legislature enacted the Beachfront Management Act. \textit{Id}. In implementing the Act, the Council expanded the protected beachfront and prohibited Lucas from constructing any occupiable improvements. \textit{Id}. The Act, however, did allow the construction of certain nonhabitable improvements, e.g., “wooden walkways no larger in width than six feet,” and “small wooden decks no larger than one hundred forty-four square feet.” \textit{Id.} at 2890 n.2.
\end{itemize}
alyze New York’s collocation regime. First, physical invasions of a landowner’s property constitute a per se taking and are tantamount to eminent domain. The seminal case on this matter is *Loretto v. TelePromp ter Manhattan CATV Co.* Second, other state regulatory actions that have a deleterious effect on private property are analyzed under a balancing test employed by the Supreme Court in *Penn Central Transportation Co. v. New York City.* Pursuant to this test, employing an ad hoc factual inquiry, the degree of intrusion to the landowner is balanced against the societal benefit of the regulation. If the public derives a great deal of benefit from the governmental regulation and the restraint on the private property owner is not excessive, then the regulation is constitutional. On the other hand, if little public benefit is derived from the governmental regulation and the restraint on the private property owner is excessive, the regulation is unconstitutional.

A. Takings by Physical Invasions

*Loretto v. TelePromp ter Manhattan CATV Co.* illustrates the principle that a government order allowing a third party to occupy private property constitutes a taking. In *Loretto,* the plaintiff brought a class action to challenge the constitutionality of Section 828 of the New York Executive Law. This statute required landlords to allow
the installation of cable television (CATV) facilities on their property. In addition, the statute prohibited landlords from receiving payments for the CATV installation in excess of the rate set by the State Commission on Cable Television. Although the Court emphasized the narrowness of its holding, the Loretto Court established the rule that "a permanent physical occupation is a government action of such a unique character that it is a taking without regard to other factors that a court might ordinarily examine."18 Quoting Penn Central, the Court further stated that "[a] 'taking' may more readily be found when the interference with property can be characterized as a physical invasion by government, than when the interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good."

19 The Supreme Court in Loretto refused to consider whether the permanent physical occupation served any public interest and specifically stated that "a permanent physical occupation authorized by government is a taking without regard to the public interests that it may serve."20

In Loretto, the Supreme Court would not even consider the magnitude of the physical occupation. It stated that "whether the installation is a taking does not depend on whether the volume of space it

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a. interfere with the installation of cable television facilities upon [her] property or premises, except that a landlord may require:
   i. that the installation of cable television facilities conform to such reasonable conditions as are necessary to protect the safety, functioning and appearance of the premises, and the convenience and well being of other tenants;
   ii. that the cable television company or the tenant or a combination thereof bear the entire cost of the installation, operation or removal of such facilities; and
   iii. that the cable television company agree to indemnify the landlord for any damage caused by the installation, operation or removal of such facilities.

b. demand or accept payment from any tenant, in any form, in exchange for permitting cable television service on or within [her] property or premises, or from any cable television company in exchange therefor in excess of any amount which the commission shall, by regulation, determine to be reasonable.

Id.

18. 458 U.S. at 432. The Loretto Court stated that its holding basically reaffirmed prior Supreme Court precedent. The Loretto Court specifically referred to the case of Pumpelly v. Green Bay Co., 80 U.S. (13 Wall.) 166 (1872), in which a unanimous Supreme Court held that "where real estate is actually invaded by superinduced additions of water, earth, sand, or other material, or by having any artificial structure placed on it, so as to effectually destroy or impair its usefulness, it is a taking, within the meaning of the Constitution . . . ." Pumpelly, 80 U.S. (13 Wall.) at 181.


20. Id.
occupies is bigger than a breadbox.”21 The Supreme Court’s rationale for this rule rests on the notion that physical occupation of a property—no matter how insignificant—deprives the landowner of an important stick in the bundle of rights, i.e., the right to exclude others from the property.22

In *FCC v. Florida Power Corp.*,23 the Supreme Court established certain limits on the *Loretto* decision. The Eleventh Circuit Court of Appeals raised, *sua sponte*, the issue of whether the Pole Attachments Act was an unconstitutional taking of property without due process of law.24 Prior to the adoption of the Pole Attachments Act, utility com-

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21. *Id.* at 438 n.16.

22. The *Loretto* Court also distinguished between cases that involve permanent physical occupation and those involving physical invasion just short of a permanent occupation. In permanent physical occupation cases the per se test is used. Where there is a physical invasion just short of permanent physical occupation, the ad hoc balancing test should be used, but the invasive character of the governmental action would be emphasized.

The *Loretto* Court cited to *United States v. Causby*, 328 U.S. 256 (1946), in which the Court ruled that frequent flights immediately above a land-owner’s property constituted a taking:

> If, by reason of the frequency and altitude of the flights, respondents could not use this land for any purpose, their loss would be complete. It would be as complete as if the United States had entered upon the surface of the land and taken exclusive possession of it.

*Id.* at 261.

The *Loretto* Court also cited *Kaiser AETNA v. United States*, 444 U.S. 164 (1979), in which a government action, (imposing a navigational servitude that required public access to a pond), was held a taking. The Court stated that the landowner had reasonably relied on government consent in connecting the pond to the navigable water. In its decision, the Court emphasized that the navigational servitude took away the landowner’s right to exclude “one of the most essential sticks in the bundle of rights that are commonly characterized as property.” *Id.* at 176. The Court explained its decision:

> This is not a case in which the Government is exercising its regulatory powers in a manner that will cause an insubstantial devaluation of petitioner’s private property; rather the imposition of the navigational servitude in this context will result in an *actual physical invasion* of the privately owned marina . . . . And even if the Government physically invaded only an easement in property, it must nonetheless pay compensation.

*Id.* at 180 (emphasis added).

Another case that highlights the distinction between actual physical invasions and physical occupations just short of permanent occupations is *Pruneyard Shopping Ctr. v. Robins*, 447 U.S. 74 (1980). In *Pruneyard*, the Court held that a state constitutional requirement that shopping center owners permit individuals to exercise free speech and petition rights in areas where the owners had invited the general public did not constitute a taking under the U.S. Constitution. The *Pruneyard* case can be distinguished from other cases on the ground that the property owner had not exhibited an interest in excluding all persons from his property. Therefore, “the fact that [the solicitors] may have ‘physically invaded’ [the owner’s] property cannot be viewed as determinative.” *Id.* at 84.


24. The Pole Attachments Act empowered the Federal Communications Commission (FCC), in the absence of parallel state regulation, to determine “just and reasonable” rates
panies leased space on utility poles to CATV companies. In response to allegations of overcharging by the utility companies, Congress passed the Pole Attachments Act authorizing the FCC to regulate pole attachments.

The Florida Power Corp. Court distinguished the Loretto case on the ground that the statute considered in Loretto explicitly required landlords to permit permanent occupation of their property by CATV companies. By contrast, the Pole Attachments Act (as interpreted by the FCC) does not permit CATV companies to permanently occupy utility company property. Under the Pole Attachments Act, the CATV companies do not have the right to occupy space on utility poles, and utility companies can refuse to enter into attachment agreements with CATV companies. The Court decided that the per se rule articulated in Loretto is applicable only when the government regulation requires the landowner to acquiesce in the occupation. The per se rule should not be used when the landowner consents to the third party’s presence on the property, as in Florida Power Corp. (the Pole Attachments Act contemplates voluntary commercial leases). Thus, the Supreme Court held that the Court of Appeals erred in applying the per se rule to the Pole Attachments Act.

The Act provides that:

a rate is just and reasonable if it assures a utility the recovery of not less than the additional costs of providing pole attachments, nor more than an amount determined by multiplying the percentage of the total useable space, or the percentage of the total duct or conduit capacity, which is occupied by pole attachment by the sum of the operating expenses and actual capital costs of the utility attributable to the entire pole, duct, conduit, or right of way.


25. CATV companies use utility company poles to run the cable that transports television signals to CATV customers. Often no other physical medium is available to the CATV companies.

26. These leases usually provided that the CATV companies would pay an annual rent for space on each pole to which cables were attached and would pay the fixed costs of modifying the poles to make them useable by the CATV companies.

27. Florida Power Corp., 480 U.S. at 251-52.

28. Id. at 253.

29. Of course, this analysis assumes that a utility would not be governed by the essential facility doctrine, which requires a utility when it owns an essential facility to give reasonable access to its competitors. See Otter Tail Power Co. v. United States, 410 U.S. 366 (1973). If the utility is governed by such doctrine, a strong argument can be made that the utility’s decision to allow pole attachments was not wholly voluntary since the utility may have consented in order to avoid antitrust liability. See generally Baynes, supra note 2, at 155 n.59. See also Richard J. Pierce, Jr., Public Utility Regulatory Takings: Should the Judiciary Attempt to Police the Political Institutions? 77 Geo. L.J. 2031 (1989).

B. Takings by Regulatory Action

When a government regulation fails to cause a permanent physical occupation of private property, fails to deny the landowner of all economically beneficial or productive use of the property, and is not a nuisance control, the regulation is analyzed under the ad hoc analysis articulated in the Penn Central case. The ad hoc test considers the following factors: (1) the economic impact of the regulation on the landowner, particularly the extent to which the regulation has interfered with the landowner’s distinct investment-backed expectations; (2) the character of the governmental action; and (3) whether the government is regulating private property by an exercise of legitimate police power. To determine whether the government regulation is an exercise of legitimate police power, the regulation must be analyzed to see whether it was designed to advance the “health, welfare, morals or safety” of the community.

In Penn Central, the Supreme Court employed the ad hoc test. New York City adopted its Landmarks Preservation Law to encourage or require the preservation of historic or aesthetically significant buildings and areas. The case involved the application of the New York City Landmarks Preservation Law to Grand Central Terminal (the “Terminal”), which was owned by Penn Central. Penn Central, 438 U.S. at 125. On August 2, 1967, the New York City Landmarks Preservation Commission designated the Terminal a “landmark.” Id. at 115-16. On January 22, 1968, Penn Central entered into a renewable 50-year lease and sublease with UGP Properties, Inc. (UGP). Id. at 116. “Under the terms of the agreement, UGP was to construct a multi-story office building above the Terminal.” Id. UGP and Penn Central applied to the Landmarks Preservation Commission for permission to construct the office building. Id. The Landmarks Preservation Commission rejected the two proposals submitted. Id. at 117. The first proposal, Breuer I, provided for the construction of a fifty-five story office building cantilevered above the existing facade and to rest on the roof of the Terminal. Id. at 116. The second proposal, Breuer II Revised, provided for the tearing down of a portion of the Terminal, stripping off some of the features of the Terminal’s facade, and constructing a fifty-three story office building. Id. at 116-17.

31. See Loretto, 458 U.S. at 441.
35. Penn Central, 438 U.S. at 125.
36. Id.
37. Id. at 123-24.
39. The Terminal, opened in 1913, was an example of the French Beaux arts style. Penn Central, 438 U.S. at 115. The Terminal was owned solely by Penn Central. Id. On August 2, 1967, the New York City Landmarks Preservations Commission designated the Terminal a “landmark.” Id. at 115-16. On January 22, 1968, Penn Central entered into a renewable 50-year lease and sublease with UGP Properties, Inc. (UGP). Id. at 116. “Under the terms of the agreement, UGP was to construct a multi-story office building above the Terminal.” Id. UGP and Penn Central applied to the Landmarks Preservation Commission for permission to construct the office building. Id. The Landmarks Preservation Commission rejected the two proposals submitted. Id. at 117. The first proposal, Breuer I, provided for the construction of a fifty-five story office building cantilevered above the existing facade and to rest on the roof of the Terminal. Id. at 116. The second proposal, Breuer II Revised, provided for the tearing down of a portion of the Terminal, stripping off some of the features of the Terminal’s facade, and constructing a fifty-three story office building. Id. at 116-17.
tral brought suit in state court alleging that the Landmark Preservation Commission's rejection of its building proposals constituted a taking.40

The Supreme Court discussed several cases in which it had rejected "takings" challenges.41 In these cases, although the challenged regulation sometimes caused the landowner severe economic harm, it did not interfere with the landowner's reasonable investment-backed expectations in such a way as to constitute a taking of "property" under the Fifth Amendment.42 The Supreme Court also noted that it was not uncommon to reject the takings challenge even though the challenged regulation caused substantial harm to the landowner by prohibiting a previous use to which individual parcels had been devoted.43

The Penn Central Court analyzed the Landmarks Preservation law from the standpoint of whether the interference was of such magnitude that "there must be an exercise of eminent domain to sustain [it]."44 The Court said that its inquiry could be confined to the severity of the law's impact on the landowner's parcel—the Terminal site.45 The Court noted that the law failed to interfere with the then-present

40. Id. at 119.


42. The Court cited United States v. Willow River Power Co., 324 U.S. 499 (1945) (interest in high-water level of river for tailwaters runoff maintaining power head was not property) and United States v. Chandler-Dunbar Water Power Co., 229 U.S. 53 (1913) (no property interest in navigable waters).

43. The Court used Miller v. Schoene, 276 U.S. 272 (1928), as an example. In Miller, a state entomologist acting pursuant to state statute ordered the claimants to cut down a large number of ornamental red cedar trees because they produced a cedar rust fatal to nearby apple trees. Id. at 277. Although the statute provided for recovery of any expense incurred in removing the cedars, and permitted the claimants to use the cut trees, it failed to provide compensation for the value of the standing trees or for the resulting decrease in market value of the properties as a whole. Id. The Supreme Court did not find cause to invalidate the statute for its failure to provide compensation. Id. at 277-81. The Court held that the state might properly make "a choice between the preservation of one class of property and that of the other." Id. at 279. Since the apple industry was important in the state involved, the Court concluded that despite the lack of compensation for depreciation in reality, the state was within "its constitutional powers by deciding upon the destruction of one class of property in order to save another which, in the judgment of the legislature, is of greater value to the public." Id.

44. Penn Central, 438 U.S. at 136 (quoting Pennsylvania Coal Co., 260 U.S. at 413).

45. Id.
uses of the Terminal. The landmark designation permitted the landowners to use the property exactly as it had been used in the past: as a railroad terminal containing office space and concessions. Therefore, the landmarks law did not interfere with the landowner's primary investment-backed expectation concerning the use of the property.

Moreover, the Court stated that the landmark law permitted the landowner to profit from the Terminal by obtaining a "reasonable return" on its investment. The Court also stated that the Landmark Commission's rejection of the landowners' previous attempts to use the air rights above the Terminal did not preclude the landowners from ever using the space. The Court explained:

First, it simply cannot be maintained, on this record, that [landowners] have been prohibited from occupying any portion of the airspace above the Terminal. While the Commission's actions in denying applications to construct an office building in excess of 50 stories above the Terminal may indicate that it will refuse to issue a certificate of appropriateness for any comparably sized structure, nothing the Commission has said or done suggests an intention to prohibit any construction above the Terminal.

The Court noted that because the landowners had not sought approval for the construction of a smaller structure, the Court did not know whether the Landmarks Preservation Commission would deny landowners any use of any portion of the airspace above the Terminal.

The Court also noted that even though the landowners had been denied the right to build above the Terminal, they possessed transferable development rights which allowed them to use air rights in other city locations. The Court noted:

While these [transferable development] rights may well not have constituted 'just compensation' if a 'taking' had occurred, the rights nevertheless undoubtedly mitigate whatever financial burdens the...

46. Id.
47. Id.
49. Penn Central, 438 U.S. at 136.
50. Id. at 136-37 (emphasis added).
51. Id. at 137.
law has imposed on [landowners] and, for that reason, are to be taken into account in considering the impact of regulation.\(^5\)

The Court held that the application of New York City's Landmark Law failed to constitute a "taking" of the landowner's property because the restrictions were substantially related to the promotion of the general welfare.\(^5\) Furthermore, the law permitted reasonable beneficial use of the landmark site. It also afforded the landowners opportunities to enhance the Terminal site and other properties.\(^5\)

As seen above, two frameworks exist for analyzing takings challenges: (1) per se takings, and (2) regulatory takings. However, if the regulated entity voluntarily consents to the regulation, then there is no taking.

The following sections will explore the factual details of collocation and its implementation in New York, and whether the New York collocation regime is a taking.

II

Collocation Decisions of the New York Public Service Commission

Collocation is achieved by either requiring the placement of competitor's equipment in the central office of a local telephone com-


\(^5\) The failure of the Penn Central Court to explicitly use the nuisance control rationale has been criticized by commentators. It has been said that "[o]nly by resort to some such concept as nuisance or noxiousness can we tell losses of value that count from losses of value that do not." James E. Krier, The Regulation Machine, 1 Sup. Ct. Econ. Rev. 1, 7 (1982).

\(^5\) Penn Central, 438 U.S. at 138. Justice Rehnquist wrote a strong dissent, stating that he would have remanded the case back to the New York Court of Appeals. Id. at 152. Justice Rehnquist stated that the majority in Penn Central misapplied the takings law in two instances. First, landmark preservation is not like nuisance, which usually involves a substantial state interest in regulating the use of land. Id. at 144-46. Second, landmark preservation in this instance is not like zoning, a situation in which the benefits and prohibitions apply over a broad cross section of land, thereby securing "an average reciprocity of advantage." Id. at 147 (quoting Pennsylvania Coal, 260 U.S. at 415). In nuisance and zoning cases, land use restrictions are often struck down; because Penn Central presented neither situation, Justice Rehnquist would have found a taking. Id. at 151-53. Justice Rehnquist would have remanded on the issue of just compensation and would have required the New York Court of Appeals to determine whether the transferable development rights would have provided landowners with just compensation. Id. at 151-52.
pany—physical collocation—or by requiring a local telephone company to dedicate proprietary equipment located in its central office to providing interconnection with its competitor's equipment—virtual collocation. Under a virtual collocation regime, the competitor's equipment could also be located just outside the local telephone company’s central office.\(^5\)

The New York Public Service Commission has been at the forefront of the collocation issue.\(^5\)6 The remainder of this Article focuses on the actions of the NYPSC in approving the New York collocation regime; it details each of the NYPSC collocation orders to show how the New York virtual collocation regime evolved into the current physical collocation requirement.

### A. The New York Public Service Commission Requires Virtual Collocation for Private Line Service

In Case 29469, *Proceeding on Motion of the Commission to Review Regulatory Policies for Segments of the Telecommunications Industry Subject to Competition*,\(^5\)7 a competitor, Teleport, sought to collocate its fiber optic facilities inside the central offices of New York Telephone\(^5\)8 to duplicate New York Telephone’s ability to aggregate low volume traffic.\(^5\)9 Teleport alleged that New York Telephone refused Teleport’s request for interconnection and that this refusal improperly prohibited Teleport from effectively competing against New York Telephone.\(^5\)0 Teleport requested that the NYPSC require New York Telephone to collocate Teleport’s fiber optic facilities at New York Telephone’s central office locations.\(^5\)1 Although the Administrative Law Judge found no basis for adopting Teleport’s proposal,\(^5\)2 the NYPSC overruled that decision.\(^5\)3 The NYPSC stated:

> The Judge’s view of competition is too restrictive, and it clashes with emerging open network architecture concepts that encourage unbundling the telephone network into elemental components and offering them on a non-discriminatory basis. With some limitations, therefore, Teleport’s proposal is acceptable. Allowing liberal inter-

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56. *Id.* at 16. The FCC and many other states have also considered this issue. See generally *id*.
58. New York Telephone is a local telephone company that provides local exchange service within New York State.
60. *Id.* at 27.
61. *Id*.
62. *Id.* at 27-28.
63. *Id.* at 28.
connections with the local exchange network generally fosters competition and will likely provide more effective and efficient carrier access service.\(^6\)

The NYPSC held that "Teleport, as well as other interconnectors and similar networks of large users,\(^6\) should be allowed comparably efficient interconnections (or, in other words, virtual collocation) for the purpose of competing with New York Telephone for the transport portion of private line . . . services."\(^6\) The NYPSC ordered New York Telephone to establish comparably efficient interconnections at its local central offices, with registered or certified carriers for the transport of intrastate private line traffic in the New York metropolitan Local Access Transport Area (LATA).\(^6\) The NYPSC stated that the "physical location of the interconnection point may be outside of a New York Telephone building, but the interconnection must be technically and economically comparable to actual collocation and the terms must be reasonable."\(^6\)

The PSC justified its decision as fostering competition.\(^6\) However, the PSC acknowledged that its decision could have unreasonable or extraordinarily adverse impacts on other ratepayers.\(^7\) Collocation would make the local telephone company competitors a more viable competitive alternative, causing New York Telephone to lose its most lucrative segment of business: big-business customers.\(^7\) As such, New York Telephone might have to raise rates to residential and small business customers to meet its revenue requirements.\(^7\) Recognizing that collocation would make the local exchange market more competi-

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64. Id.

65. The PSC decision is rather broad in that it also allows private companies that bypass the local telephone network solely for their individual telephone needs to collocate. Id. at 28-29.

66. Id. at 28.

67. Id. at 28-29. A LATA generally comprises a standard metropolitan area; it does not necessarily coincide with the area code for that area. For example, the Commonwealth of Massachusetts is divided into two LATAs. The area codes "508" and "617" are part of the LATA for Eastern Massachusetts, whereas the area code "413" is part of the LATA for Western Massachusetts. LATAs are important because the consent decree divesting AT&T prohibited local telephone companies from transporting calls between LATAs. Only long distance companies, e.g., AT&T, Sprint, and MCI can transport calls between LATAs. Local telephone companies can transport calls only within each LATA. Baynes, supra note 4, at 19 n.79.


69. Id.

70. Id.

71. Id. at 29.

72. Id.
tive, the NYPSC granted New York Telephone greater pricing flexibility for two of its private line services.\textsuperscript{73}

B. Implementation of Virtual Collocation for Private Line Service

New York Telephone initially proposed a virtual collocation plan, which was unacceptable to its competitors and the NYPSC; the initial proposal did not provide the competitors with technological or economic benefits comparable to physical collocation.\textsuperscript{74} Through informal discussions, the NYPSC staff worked with the parties to arrive at a tariff more closely conforming to the NYPSC collocation order.\textsuperscript{75}

As a result of these discussions, New York Telephone introduced its transport interconnection arrangement (TIA) service.\textsuperscript{76} This service gave the New York Telephone competitor an option: it could provide the entire fiber optic link from the competitor's premises to the New York Telephone building that houses the wire center to which the competitor desires interconnection.\textsuperscript{77} New York Telephone would

\textsuperscript{73} Specifically, PSC granted New York Telephone the authority to increase rates for high capacity and interoffice private line services by twenty-five percent annually, and to decrease them without limitation, so long as the rates covered relevant incremental costs. This tariff flexibility applied throughout the New York Metropolitan area. New York Telephone was also authorized to offer individual case billing arrangements on a nondiscriminatory basis for services in response to competitive requests. \textit{Id.} at 31.

\textsuperscript{74} See Baynes, supra note 4, at 4, 22. To implement the decision in \textit{Case 29469}, New York Telephone filed with the PSC a tariff for a new service, then-called "the transport interconnection arrangement" (TIA), now known as "Optical Transport Interconnection Service" (OTIS). \textit{Id.} at 21-22. This proposal as initially submitted did not achieve the objectives of the PSC in fostering more competition between the competitive access providers (CAPs) and New York Telephone. \textit{Id.} at 22. As initially proposed by New York Telephone, the CAPs had the option of either having the interconnection made at the CAPs' premises or at the nearest manhole to the New York Telephone central office. \textit{Id.} Neither of these options allowed the CAPs to avoid a transport charge for interconnection with the local exchange network while providing a relatively high quality service. \textit{Id.} at 24-25. There were also requirements that locked the CAPs into the equipment and service for a significant period of time. \textit{Id.} The CAPs objected to New York Telephone's initial proposal because they believed it was not equivalent to physical collocation. \textit{Id.} at 22-23. The CAPs argued that this initial proposal was not technically or economically comparable to physical collocation because the technology was outdated, actual physical collocation cost less, and long term contracts locked the CAPs into lease arrangements. \textit{Id.} at 22-25. The PSC staff also found the initial New York Telephone proposal lacking because it was not comparable to physical collocation. \textit{Id.} The CAPs again demanded that the PSC require New York Telephone to provide physical collocation of its facilities to CAP equipment. \textit{Id.} The PSC staff disagreed with the CAPs' position that because the service offerings by New York Telephone were problematic, physical collocation was necessitated. \textit{Id.} at 23-24. The staff stated that the PSC "specifically declined to order actual physical collocation" and instead ordered "virtual, comparably efficient, interconnection arrangements."\textit{Id.}

\textsuperscript{75} Baynes, \textit{supra} note 4, at 19.

\textsuperscript{76} The TIA service later became known as the OTIS I Tariff.

\textsuperscript{77} Op. No. 89-12, \textit{supra} note 57.
supply the collocation equipment, but it would be selected by the competitors within a range of options provided by New York Telephone.

Teleport, however, remained dissatisfied with the revised Optical Transport Interconnection Service (OTIS) virtual collocation arrangement. Teleport’s concerns revolved around what constituted “equal interconnection.” It wanted a broader array of interconnections, control of the type of equipment utilized, and responsibility for monitoring and control. Teleport contended that if its concerns were not addressed, a more competitive market for private line service would not be achieved.

The NYPSC waffled on Teleport’s demands. It approved the OTIS Tariff and appeared to side with New York Telephone. The NYPSC stated that Teleport’s demands to “monitor and control” its circuits, to utilize specific types of equipment, and to have a broader array of interconnection went beyond the scope of the proceeding.

But then the NYPSC straddled in favor of Teleport. The NYPSC stated that New York Telephone and Teleport should be able to utilize the Open Network Architecture principles inherent in the PSC’s or-

78. The collocation equipment was an Optical Line Terminating Multiplexer (OLTM). Baynes, On-Ramp to Information Superhighway, supra note 3, at 19.
79. See supra note 74.
80. See supra note 73.
82. Id.
83. The NYPSC stated that Teleport’s argument raised two issues: one, whether Teleport had the right to request use of specific equipment within New York Telephone’s central office, and two, if Teleport were granted that right, did Teleport also have the right to perform the supervision and control functions essential to assure adequate service? Id. The NYPSC stated that the answers to both questions were unclear. Id.
84. The NYPSC noted, however, that in its recent ruling in the Open Network Architecture proceeding, the NYPSC required additional unbundling of the local telephone network so that “users can create their own services or networks.” Re Telecommunications Indus. Interconnection Arrangements, Open Network Architecture, and Comparably Efficient Interconnection, 106 Pub. Util. Rep. 4th (PUR) 420, 425 (1989). Open Network Architecture requires the local exchange carriers to give independent firms equal access to the local exchange carrier’s features and functions present in the central offices. Again, this equal access is done to foster competition between these independent firms and the local exchange carrier.

The term “unbundling” refers to the shearing off and splitting up of the telephone network and services into many parts. An historical note should prove explanatory. It is important to remember that many years ago AT&T provided fully integrated telephone service. AT&T had objected to placing competitive telephone sets on the network for fear
order to resolve the outstanding issues, and New York Telephone should strive to satisfy Teleport's remaining objectives as soon as possible. The NYPSC established a task force (the “Task Force”) consisting of NYPSC staff, New York Telephone, Teleport, and other competitors to resolve issues of central office multiplexing arrangements, including a control hierarchy adequate to meet the needs of all parties.

From a takings perspective, the NYPSC order and subsequent developments avoided a permanent physical occupation of New York Telephone's property, which would have amounted to a per se taking under Loretto. The OTIS I virtual collocation tariff did not entail any physical collocation of the competitor's equipment onto New York Telephone's property. Instead, it authorized a virtual collocation regime in which the collocation equipment was owned and operated by New York Telephone. Moreover, New York Telephone was not required to allow the competitors entry to monitor and control the collocation equipment. This arrangement, from an administrative standpoint, was still not wholly satisfactory to New York Telephone because it remained responsible for selecting, monitoring, and repairing the equipment of a competitor. The NYPSC even noted that this obligation could very well lead to potential antitrust liability.

At this stage of the proceedings, the competitors' only objections were that they could neither select the equipment nor monitor and control it. From a practical standpoint the competitors' concerns were justified. They wanted to ensure that there were no problems with the service they provide customers. One way to achieve that result: obtain as much control as possible over every aspect of the service. The OTIS I virtual collocation tariff did not provide the competitors with that opportunity. The competitors had to rely on New York Telephone to select, monitor, and repair crucial equipment. Given the fact that both sides were still not happy with the OTIS I virtual collocation regime, it was not surprising that the discussions and negotiations continued. New York Telephone continued to modify its position.

that it would denigrate the quality of its service. Now, the market for telephone sets is very competitive, with many competitors providing a range of telephone sets in terms of quality and price. Similarly, with respect to collocation, even the local telephone network is not safe from unbundling.

86. Id.
87. See Loretto, 458 U.S. 419.
88. See Baynes, supra note 4, at 37. There was a risk of antitrust liability because New York Telephone would be a competitor as well as a supplier of services to its customers. It was feared New York Telephone might use its in depth knowledge of the competitors' business activities (that New York Telephone acquired in providing virtual collocation service) to steal customers away from the competitors.
C. Task Force Recommendations

The Task Force submitted its report to the NYPSC on March 15, 1990. The Task Force report recommended that the competitors have the right to specify the functions and features integral to the collocation equipment supplied by New York Telephone. The competitors had the right—superior to New York Telephone—to monitor and control New York Telephone-owned collocation equipment and to train New York Telephone to do likewise. New York Telephone also had the right to jointly monitor and control the competitor's collocation equipment, once New York Telephone did not interfere with the competitor's right to do the same.

New York Telephone was the only member of the Task Force to dissent from the findings. New York Telephone argued that the then-current state of technology allowed only one party to monitor and control. The Task Force recommendations placed the competitors at the top of the hierarchy in terms of monitoring and control, with rights superior to the owner of the equipment—New York Telephone. Of course, in those central offices that the competitors chose not to perform the monitoring and control function, they could train New York Telephone to monitor and control its own equipment. As a result of the NYPSC order, New York Telephone was stuck with a regulatory regime that, although entitled "virtual collocation," was very similar to physical collocation.

89. Op. No. 89-12, supra note 57, at 4-6. Along with New York Telephone, they have the right to prepare, issue, and review any Requests For Proposals for the collocation equipment. Id. The CAPs would work with New York Telephone to identify vendors whose equipment meets the CAPs' specifications. Id.
90. Id.
91. Id.
92. Id.
93. New York Telephone owned the equipment that it was required to place on its premises for the benefit of the competitors. See Baynes, supra note 4, at 33. It had no control over the functions that this equipment would perform and was not primarily responsible for monitoring and controlling it. Id. But there was no clear demarcation for how much responsibility New York Telephone did have as to the equipment. Id. New York Telephone's responsibility to the equipment could potentially vary in many ways. Id.

For instance, a competitor and New York Telephone could agree that New York Telephone would be responsible for monitoring and controlling collocation equipment when the competitor is unavailable. They could also agree that New York Telephone would have principal responsibility for monitoring and controlling equipment only in certain locations, on certain dates, or at certain times. Id. So, even though New York Telephone's administrative role would be reduced because it "shared" the monitor-and-control obligation with the competitors, New York Telephone would be in a much more precarious position because the demarcation of the monitor-and-control role between New York Telephone and the competitors would be much more fuzzy. Id. This fuzziness would increase the likeli-
The NYPSC was the primary beneficiary of this ruling. It promulgated a virtual collocation regime closely approximating physical collocation. It accomplished its plan to foster competition. Moreover, since it did not order physical collocation, the NYPSC did not have to worry about a per se taking challenge. Instead, the ruling encouraged (some would say coerced) the parties to agree to the more administratively practical solution of physical collocation.

D. Physical Collocation for New York Telephone's Private Line Services

As a result of the NYPSC decisions ordering virtual collocation, the parties began active negotiations to ensure full compliance with the NYPSC's order. Since neither New York Telephone nor the competitors were satisfied with the NYPSC virtual collocation regime, it was no surprise that New York Telephone changed its position by announcing in November 1990 its intention to offer actual physical collocation to any competitor that desired it.

On May 8, 1991, the NYPSC approved New York Telephone's OTIS II tariff, which provided for physical collocation of a competing carrier's facilities within any New York Telephone central office. This arrangement applied only to private line service. The salient provisions of the OTIS II tariff were as follows: The competitors could establish "multiplexing nodes" at any New York Telephone wire

hood that New York Telephone would make a mistake as to its role in monitoring and controlling, increasing the potential for antitrust liability. Id.

94. The competitors got a virtual collocation regime instead of physical collocation. Baynes, supra note 4, at 33. Although the competitors could select functions and features, they still did not own the equipment, so they were unable to upgrade, remove, or replace it as easily. Id. In addition, they were unable to select the actual model of collocation equipment they desired. Id. Although the competitors were primarily responsible for monitoring and controlling the equipment, they were still dependent on New York Telephone, because in some circumstances New York Telephone would be performing this role. Id. As will be seen, these parameters, which were conceived by the NYPSC, provided the perfect opportunity for the parties to reach their own deal, since the current regime was still not wholly satisfactory to either of them. Id.

95. Order Regarding OTIS II Compliance Filing, Case No. 29469 and Case No. 88-C-004, 6 (N.Y.P.S.C. May 8, 1991) [hereinafter OTIS II].

96. Id. at 7.

97. Id. The NYPSC noted that this arrangement was the first of its kind in the nation. Id. The OTIS I Tariff had a sunset provision that expired on December 1991. All OTIS I tariffed arrangements rolled over into OTIS II. Id. The NYPSC said that under the proposals, the competitors would gain physical access to the "last mile" to all users, and the real ability to extend their own network to users; this, without the costs of building facilities directly, by accessing them at a point where they have already been aggregated—the central office building itself. Id.

98. The multiplexing node could contain any of the following equipment: OLTMs, DS3-to-DS1 and DS1-to-DS0 multiplexers, and 3/1 and 1/0 Digital Cross-connect systems. Id. Equipment supplied must either be on a New York Telephone approved list of prod-
center or central office specified by the competitor and into which the competitor would construct fiber optic cables. New York Telephone would designate the floor space within each wire center or central office that would constitute the multiplexing node and could enclose that space in a cage or room. The competitor's employees would have access, at all times, to the multiplexing nodes, cable, and associated equipment. The competitor would be responsible for installing and maintaining its equipment within the multiplexing node and its fiber optic cables.

As a result of the NYPSC order, New York Telephone did not own the equipment that was placed in its central offices; the competitors owned the equipment. Thus, New York Telephone avoided the administrative nightmare of selecting, monitoring, and controlling its competitors' collocation equipment. As a result, the potential for antitrust liability was diminished. However, New York Telephone was now disadvantaged in that a competitor owned equipment located on New York Telephone property.

99. The wire center/central office had to be listed in the National Exchange Carrier Association (NECA) Tariff No. 4. Id.

100. The minimum space would be 100 square feet per node; additional space was necessary. Id. New York Telephone would provide the environmental support necessary for the competitor's multiplexing node in the same manner that New York Telephone provides for its own equipment. Id. This environmental support would consist of electric power, battery and generator backup power, heat, and air conditioning. Id.

101. The collocation service was tariffed, but a license agreement would govern the terms, conditions, and rental rate for the collocated space. The tariff also provided that New York Telephone would provide certain cross-connect frames within each central office/wire center to serve as a demarcation point between the competitor and New York Telephone services. Id. New York Telephone bears the responsibility for maintenance and related activities on its side of the demarcation point. Collocation space is allocated among competitors on a "first come, first served" basis.

102. The NYPSC even acknowledged this factor; when New York Telephone decided to employ "physical" collocation, the NYPSC stated that New York Telephone was then released from the onerous administrative burdens related to "improving" OTIS I. Id. Moreover, the NYPSC noted that by providing "physical" collocation, New York Telephone was released from possible charges of anti-competitive practices were it to find itself in the business of provisioning equipment for competitors' end users under a virtual collocation arrangement, while simultaneously negotiating for the same end-users in a competitive marketplace. Id. New York Telephone realized, the Staff believed, that no matter how hard it tried to deal honestly with this dual role, it would always run some risk of being accused of anticompetitive practices. Id.

103. As a result of the New York NYPSC order, the competitors received a physical collocation regime. Because they were able to own their equipment, they could upgrade, remove, or replace it easily. In addition, they were able to select the actual model of collocation equipment they desired. The competitors were primarily responsible for moni-
As a result of its order, the NYPSC established a physical collocation regime to which the parties consented. Since its initial ruling required virtual collocation—not physical collocation—the NYPSC did not have to worry as much about a per se taking challenge.

By agreeing to physical collocation, New York Telephone also benefitted. In exchange for its consent, New York Telephone received inducements from the NYPSC and competitors: The competitors agreed to pay New York Telephone an amount for interconnection that would serve as contribution\(^{104}\) for the expected revenue losses that New York Telephone would incur as a result of physical collocation. This contribution would allow New York Telephone to continue providing low cost service to its embedded base of residential customers. New York Telephone also received certain pricing flexibility\(^{105}\) for the private line market—the very market in which the NYPSC is trying to foster competition. This pricing flexibility will likely allow New York Telephone to compete more effectively against the competitors.

### III

**New York Collocation: Is It a Per Se or Regulatory Taking?**

**A. Analysis of New York Collocation as a Per Se Taking**

1. *Traditional Loretto Analysis*

   In its collocation orders, the NYPSC failed to consider whether its collocations policy was an unconstitutional taking. The NYPSC merely ordered, at first, that the local telephone company choose between a modification of rates or virtual collocation, without any explanation or discussion of the constitutionality of the order. The local telephone company first chose virtual collocation, and then, due to increasingly more difficult requirements, agreed to physical collocation.

   If the NYPSC had ordered physical collocation, this form of regulation would be presumptively unconstitutional as a permanent physi-

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104. Contribution is the amount of revenue that New York Telephone receives, for example, from its private line services that can be used to subsidize its basic services. With collocation, the fear is that New York Telephone's contribution amounts from its private line services would decrease, thereby causing New York Telephone to increase its prices for its basic services to residential customers.

105. To a regulated entity, deregulation in the form of pricing flexibility has a great deal of value.
cal occupation of the local telephone companies' property without just compensation. A physical collocation order would have resembled the *Loretto* statute, a physical invasion of the landowner's property, and thus, a per se taking. Like *Loretto*, a physical collocation order would have required placement of equipment owned by third parties on the private property of another, a permanent physical occupation resulting in a per se taking.

The NYPSC never ordered physical collocation. Instead, it offered the local telephone companies a choice, and they chose virtual collocation. Under *Loretto*, virtual collocation is not a per se taking because it does not involve the permanent physical occupation of property by a third party. The NYPSC's virtual collocation regime is similar to regulations requiring landlords to install utility connections, mailboxes, smoke detectors, or fire extinguishers. The installation of such devices would not entail a traditional physical invasion because the equipment is owned and operated by the landowner.

As Justice Blackmun pointed out in his *Loretto* dissent, analyzing the New York collocation regime is much more complex than simply addressing physical touching:

Under the Court's test, the "third party" problem would remain even if [the landowner] herself owned the cable. So long as [the CATV company] continuously passed its electronic signal through the cable, a litigant could argue that the second element of the Court's formula—a "physical touching" by a stranger—was satisfied and that [the statute] therefore worked a taking. Literally read the Court's test opens the door to endless metaphysical struggles over whether or not an individual's property has been "physically" touched.

Even though under a virtual collocation regime there is no physical invasion, there is a physical touching of the New York Telephone collocation equipment by the competitors' signal transmissions. The U.S. Supreme Court has not adopted the per se test for these types of invasions. In fact, the majority in *Loretto* rejected the dissent's analysis, deciding that the per se taking test should be employed narrowly for actual physical occupation of physical property, but not for other types of "invasions," e.g., access to wires and cables that merely involve the regulation of property. Under virtual collocation, the equip-

107. See *id.* at 440 (The Court's holding did not alter the analysis governing the state's power to require landlords to comply with building codes and provide certain facilities to tenants. The Court stated that "so long as these regulations do not require the landlord to suffer the physical occupation of a portion of [her] building by a third party, they will be analyzed under the multifactor inquiry generally applicable to nonpossessory takings.").
ment is dedicated to the competitors, but still owned by New York Telephone. This invasion of third party signals by way of the equipment is less burdensome to New York Telephone than having a third party's equipment on its premises. New York Telephone expects to have relatively undisturbed possession of its premises, i.e., no physical invasions. As a regulated entity, however, New York Telephone expects to have restrictions and affirmative duties regarding the use of its property, which is essentially what the virtual collocation order is imposing. These restrictions and affirmative duties are infinitely less burdensome than having the collocation equipment owned by a third party. Physical "invasions" are more onerous than the physical "invasion" of equipment, which in this situation is merely the regulation of such equipment.\(^{109}\)

From a policy standpoint, applying the per se takings test to such metaphysical invasions would open a pandora's box. With the advancement of technology, situations arise in which electrical, magnetic, and sound waves transgress a landowner's property, undetected, unseen, and unfelt. To allow compensation under the per se test would likely inhibit the development of the nascent industries that use these technologies. Moreover, to require compensation in these circumstances goes beyond the policy justifications of *Loretto*.\(^{110}\)

In *Loretto*, the Supreme Court created the per se test for permanent physical occupations because these invasions affect the landowner's most important stick in the bundle of rights—the right to exclude.\(^{111}\) A permanent physical invasion of real property is akin to eminent domain; it hurts the landowner most because it affects the privateness of property—the right to exclude. In contrast, physical "invasions" of utility equipment through pipes, wires, or cables deal with the manner in which the landowner can use property; this invasion is considerably less burdensome than a traditional physical invasion. Thus, the per se test should not be used in this circumstance.\(^{112}\)

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109. See infra part IV.B., analyzing the NYPSC collocation orders under the ad hoc test.

110. *Loretto*, 458 U.S. at 440 (The Court discusses the most salient distinction among these types of installations—who owns them. If an installation is owned by a third party, a per se analysis of regulatory takings is used. If it is owned by the landowner, an ad hoc analysis is used because the landowner would generally have more control over the installation.).

111. *Id.* at 419.

112. The cases dealing with this issue have not directly addressed the issue of "physical touching" of a landowner's facility under the *Loretto* test. The New York State Court of Appeals dealt with a similar issue in Rochester Gas & Elec. Corp. v. NYPSC, 520 N.E. 2d 528 (N.Y. 1988), in which the New York NYPSC required utilities to transport natural gas owned by customers through the utilities' pipelines. Rochester Gas brought suit, alleging
2. Consent

The local telephone company ultimately agreed to physical collocation. Under the doctrine established in Florida Power Corp., voluntary submission to a physical invasion by a landowner precludes a claim that the property was unconstitutionally taken.

B. Analysis of New York Collocation as a Regulatory Taking

The Loretto Court stated that where there is no permanent physical occupation of a landowner's property, a court, in analyzing whether the government's action is a taking, should use the ad hoc test. Courts consider the following factors in applying the ad hoc test: (1) whether there is a rational basis for the government's actions, i.e., whether the government's regulation substantially advances a legitimate state interest; (2) the character of the government's actions; and (3) the economic impact of the regulation, focusing on the landowner's investment-backed expectations.

1. Rational Basis—Do the Collocation Decisions Substantially Advance A Legitimate State Interest?

In determining whether the regulation is a legitimate exercise of police power, the courts analyze whether the regulation is designed to advance the "health, safety, morals, or general welfare" of the com-

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113. Loretto, 458 U.S. at 426.
115. Penn Central, 438 U.S. at 124.
116. Id.
As far as due process is concerned, "a state is free to adopt whatever economic policy may reasonably be deemed to promote public welfare, and to enforce that policy by legislation adapted to its purpose." Courts will usually sanction such economic legislation, provided it is not arbitrary or discriminatory.

In its orders dealing with collocation, the NYPSC emphasized that it was ordering collocation to foster competition in the local exchange market. Thus, the collocation orders are a form of economic regulation. These collocation orders are distinguishable, however, from many cases that deal with economic regulation because the NYPSC is not only regulating the rates or economic viability of the local telephone company, but also permitting a physical invasion of the local telephone company's property. Because a great deal of discretion is given to administrative agencies in devising economic regulations, that factor in itself should not be determinative. Moreover, by initially allowing the local telephone company to adopt a virtual collocation, the NYPSC did not order the invasion of telephone company property. Because a relationship exists between the regulation and its intended purpose, the NYPSC is secure under this prong of the analysis.

In addition, the Rochester Gas case provides precedent; it established a rational basis for virtual collocation. In Rochester Gas, the legislature required a gas company to give customers access to the company's pipelines. The Court held that the law was "a reasonable regulation consistent with the public interest in developing the state's resources, furthering competition, and controlling the cost of natural gas in the retail market." Similarly, the NYPSC implemented a collocation policy for the purpose of fostering competition and reducing retail prices.

There is some question whether the Supreme Court has recently required a tighter nexus between the purposes of the regulation and

117. Id. at 125.
118. Nebbia v. New York, 291 U.S. 502, 537 (1934). Acting pursuant to a state statute authorizing it to set milk prices, the New York Milk Control Board set the price of milk at nine cents per quart. Nebbia, a grocery store owner, sold two quarts of milk for thirteen cents and was convicted for violating the board's order.
119. Id.
120. See Op. No. 89-12, supra note 57.
122. Id. at 529.
123. Id. at 532.
124. See Baynes, supra note 4, at 18 n.70.
The actual regulation. The NYPSC could have pursued other means of achieving the intended purpose—competition—that would have been less burdensome to the property owner.

2. Character of the Government Action

The Pennsylvania Coal Court, as a general proposition, stated that when a regulation is excessive, there is a taking. Courts have considered a variety of factors in reviewing the character of government actions. The Penn Central Court listed the factors that a court should weigh in reviewing the character of a government action: whether the government’s action is discriminatory, whether the government is using the landowner’s property for a government enterprise, whether the government is devising the regulation as nuisance control, and whether the government action constitutes a permanent physical occupation of the property. None of these considerations are present here. Furthermore, the list of items mentioned in Penn Central should be exclusive.

In the collocation proceedings, a strong argument can be made that the NYPSC went too far. The NYPSC first gave the local telephone company a choice between rate regulation and a virtual collocation regime. The local telephone company chose a virtual collocation regime. The NYPSC then imposed additional regulations on the virtual collocation regime. These additional regulations were particularly burdensome and ultimately caused the local telephone company to agree to physical collocation.

The additional regulations gave the competitors of the local telephone company the right to select the functionality of collocation equipment and to jointly monitor and control it. The NYPSC determined that the competitors had a superior right over the local telephone company to monitor and control the collocation equipment. This right required a balancing act by the local telephone company because it would have been jointly responsible for ordering the maintenance and repair of competitive equipment. As the NYPSC said,

125. See Nollan v. California Coastal Comm’n, 483 U.S. 825, 837 (1987); Dolan v. City of Tigard, 114 S. Ct. 2309, 2317 (1994). These cases, though they need not be addressed here, raise the issue whether the standard for review is elevated in cases that do not involve a condition placed on a development permit. Nollan and Dolan can be limited to regulations that condition physical invasions on specific types of land uses. In these cases, the invasion is a taking unless it substantially promotes a legitimate government interest.

126. For instance, the NYPSC could have exclusively pursued a rate regulation approach to foster competition. See Baynes, supra note 4, at 4 n.6.


128. See supra note 115 and accompanying text.
this power to monitor and control, albeit jointly, a competitor's equipment might lead to the leveling of anticompetitive charges against the local telephone companies. In sum, these requirements severely restricted New York Telephone's options regarding the equipment. It also gave the competitors access to New York Telephone's facilities to monitor its equipment, and gave the competitors a role in the placement of the equipment. These requirements were tantamount to ownership of the equipment by the competitors.

3. Diminution in Economic Value

The final factor that is considered under the ad hoc test is the economic impact of the regulation on the landowner, and particularly the extent to which the regulation has interfered with the landowner's investment-backed expectations.

Collocation does not diminish the economic value of the local telephone company's property since the local telephone company has no investment-backed expectation with respect to the collocation property. First, the relevant space in the local telephone company central offices is often useless. With the installation of modern computerized switching equipment, many telephone company central offices contain a great deal of spare, unused space. Collocation will open this space to competitors, and the local telephone companies will receive rent for space that previously was unproductive. However, the local telephone company can argue that, because it may want to use the space for itself in the future, opportunity costs are involved. In addition, the local phone company may want to rent the space to

129. See Op. No. 89-12, supra note 57.
130. Although the virtual collocation regime devised by the NYPSC was tantamount to physical collocation, it was still unacceptable to the competitors. They wanted physical collocation so they could select the specific brand of equipment that would be placed in the New York Telephone central offices, and so they could solely monitor and control the collocation equipment.

Under a virtual collocation regime, the competitors probably feared that New York Telephone, by jointly monitoring and controlling their equipment, would gain access to valuable competitive information. Moreover, New York Telephone might have used its role (in monitoring and controlling) to act in an anticompetitive manner towards the CAPs, e.g., not repairing competitor equipment within a reasonable time.
131. Penn Central, 438 U.S. at 124.
132. An argument can also be made that New York Telephone is a public utility. "Thus its general investment expectations included the knowledge that it was subject to extensive regulation." See Rochester Gas & Elec. Co. v. NYPSC, 520 N.E.2d 528, 534 (N.Y. 1988).
133. 5ESS equipment replaced much of the local telephone company's antiquated yet voluminous switching equipment.
134. Of course, because of the potential concomitant decrease in revenues from increased competition and loss of transport charges from competitors, collocation may harm the local telephone companies. See Baynes, supra note 4, at 12.
third parties other than its competitors, something the collocation regu-
lation and antitrust laws make it very difficult to do. These argu-
ments are not particularly strong, however, because the local tele-
phone companies can now receive rent for this spare space, as op-
posed to speculating about future needs.

In considering the economic impact of the collocation regime, a 
court could also consider the rights that New York Telephone received 
regarding pricing flexibility and the universal service element—contri-

bution. These rights are analogous to the transferable development 
rights that the landowners had in the Penn Central case. In Penn 

Central, the Court stated that “the rights nevertheless undoubtedly 
mitigate whatever financial burdens the law has imposed on appel-

lants and, for that reason, are to be taken into account in considering 
the impact of regulation.” The contribution amount in the univer-
sal service element is designed to make up revenues lost by New York 
Telephone as a result of collocation. These lost revenues would have 
made it more difficult for New York Telephone to maintain its overall 
rates. Without contribution, New York Telephone might have had to raise its rates for some vital services, leading to a possible concomitant decrease in revenues.

To a regulated utility, pricing flexibility has a great deal of value. 
This very pricing flexibility allowed New York Telephone to compete 
more vigorously in the same market that the NYPSC, through colloca-
tion, is making more competitive. The actual monetary value of pric-
ing flexibility is difficult to quantify, but is akin to untying one arm of 
a prizefighter: the prizefighter still may lose, but is saved from certain 
defeat as a result of the prior bound condition. Each of these regul-
atory rights, won as concessions to the collocation regime, are major 
pluses to New York Telephone and help to diminish the economic im-

pact of collocation.

Economic regulation is very routine and usually passes constitu-
tional muster unless the action involves confiscation and has no ra-

tional basis. Here, the local telephone company cannot hang its hat

135. As noted earlier, the essential facility doctrine requires the owners of an essential 
facility to make it reasonably available to competitors. Thus, if a local telephone company 
has space available, it would be difficult for it to deny access to a competitor. If a local 
telephone company did deny access to a competitor, it might be liable under the antitrust 
laws.

136. See Penn Central, 438 U.S. at 137.

137. Id. The Court conceded that if a taking had occurred, this might not constitute 
“just compensation.” Id.

138. By providing contribution from the competitors, New York Telephone avoided this 
potential trap. In addition, it will be able to continue to provide reasonable rates to its 
residential customers.
on this expected decrease in revenues because the NYPSC granted it pricing flexibility to compete more effectively against competitors. Moreover, the NYPSC ordered the competitors to provide contribution for the expected loss in private line revenues.

In summary, the New York collocation decisions do not constitute a regulatory taking. Although the character of the government action is relatively invasive, the collocation orders do not violate the other ad hoc requirements. The economic value of the local telephone company property is not diminished. In addition, collocation substantially advances a legitimate state interest—competition.\textsuperscript{139} On balance, the benefits to the public outweigh the harms to the company.

\textbf{IV}

\textbf{Is the New York Public Service Commission's Decision to Order Collocation Ultra Vires?}

Every administrative agency derives its power from the legislature through an enabling act. The administrative agency has the power to act only within the bounds of that statute. If the administrative agency oversteps the bounds of the statute, then its action is ultra vires and thereby invalid. Noticeably absent from the NYPSC's collocation decisions is any discussion of where the NYPSC derives its power to order collocation.

As with the takings issue, the NYPSC crafted its collocation orders in an effort to avoid their invalidation on ultra vires grounds. Although the Public Service Law does not expressly give the NYPSC power to order physical collocation, it may rather easily be interpreted as giving the NYPSC power to order virtual collocation.

Article 1, Section 5(1)(d) of the New York Public Service Law gives the NYPSC the power to regulate "telephone lines." It provides:

The jurisdiction, supervision, powers and duties of the public service commission shall extend under this chapter: to every telephone line which lies wholly within the state and that part within the state of New York of every telephone line which lies partly within and partly without the state and to persons or corporations owning, leasing or operating any such telephone line.\textsuperscript{140}

The New York Public Service Law defines the term "telephone line" to mean the following:

\textsuperscript{139} See supra note 126.
\textsuperscript{140} N.Y. PUB. SERV. LAW, art. 1, § 5(1)(d) (McKinney 1985) (emphasis added).
The term "telephone line," when used in this chapter, includes conduits, ducts, poles, wires, cables, cross-arms, receivers, transmitters, instruments, machines, appliances and all devices, real estate, easements, apparatus, property and routes used, operated or owned by any telephone corporation to facilitate the business of affording telephonic communication.\textsuperscript{141}

Physical collocation involves the placement of a competitor's transmission equipment in the local telephone company's central office. The New York Public Service Law gives the NYPSC power to regulate telephone lines, which may be defined as property or real estate "owned by any telephone corporation used to facilitate ... telephonic communication."\textsuperscript{142} At first blush, this statute could be construed as giving the NYPSC the legal authority to order physical collocation, which requires the local telephone companies to use real estate or property in a certain way, i.e., placing competitor's equipment in central offices. However, since the statute does not expressly give the NYPSC the power to order eminent domain\textsuperscript{143} or physical collocation, a stronger argument can be made that these actions would be ultra vires.\textsuperscript{144} This conclusion is supported from a policy standpoint: society does not want administrative agencies to overstep their bounds. An agency should exercise only those powers expressly granted by statute. Because physical collocation is in the nature of eminent domain, involving the placement of a third party's equipment on the property of a local telephone company, this policy interest would be very strong here. The Public Service Law is clearly silent on whether the NYPSC has the power to order eminent domain.

The definition of "telephone line" in the New York Public Service Law, which gives the NYPSC power to regulate real estate and property owned by local telephone companies, can easily be construed as giving the NYPSC authority to order virtual collocation. Virtual collocation merely involves the regulation of the use of local telephone company real estate or property. Therefore, the NYPSC could order the local telephone companies to place certain equipment in their central offices. Under virtual collocation, the collocation equipment is

\textsuperscript{141} N.Y. PUB. SERV. LAW, art. 1, § 2(18) (McKinney 1985) (emphasis added).

\textsuperscript{142} Id.

\textsuperscript{143} In implementing its collocation order, it was not necessary for the NYPSC to condemn the local telephone company's property. The NYPSC could hang its hat on the fact that it was simply regulating the use of the local telephone company's property. The New York Public Service Law permits this regulation.

\textsuperscript{144} Based on its authority to regulate "interconnections" under the Federal Communications Act, the FCC recently ordered physical collocation. See 47 U.S.C. § 201(a) (1991). The D.C. Circuit found that the FCC order was ultra vires because the statutory language giving the FCC the power to order interconnections did not also grant the FCC power to order physical collocation. See Bell Atl. Tel. Cos. v. FCC, 24 F.3d 1441 (D.C. Cir. 1994).
owned by the local telephone company but is used exclusively for the benefit of competitors.

These conclusions are supported by the New York courts’ strong policy of deferring to the regulatory aegis of the NYPSC. For instance, a court has held that the NYPSC is responsible for administering the Public Service Law, and that a decision to apply that law to an area of communications assigned to it for regulation will not be set aside if there is a rational basis for the conclusion. Moreover, the NYPSC is the delegate and alter ego of the New York State legislature acting pursuant to the police power.

It should come as no surprise that the NYPSC did not order physical collocation, but instead initially presented the parties with an option to foster competition. Once the local telephone company chose virtual collocation, the NYPSC helped to devise requirements that made the virtual collocation regime the equivalent of physical collocation and an administrative difficulty for the local telephone company. This revised collocation regime might have resulted in antitrust liability for the actions taken by New York Telephone. New York Telephone eventually agreed to a physical collocation regime.

V

Conclusion

The New York NYPSC decisions ordering collocation were not a per se taking because the NYPSC did not actually order physical collocation, i.e., a permanent physical occupation of a landowner’s property. Instead, the parties eventually agreed to physical collocation. Because of the problems that administration and application of virtual collocation caused New York Telephone and its competitors, the NYPSC’s initial decision caused the parties to move toward physical collocation consensually. The parties’ decision to permit physical collocation allowed the NYPSC to merely sit back and approve whatever agreement the parties reached. The NYPSC was aware of the implication of its virtual collocation ruling—no one was happy with it. It realized that the administrative burdens New York Telephone incurred, as a result of the virtual collocation regime, in selecting, monitoring, and controlling a competitor’s equipment, could potentially

147. This course of action allowed the NYPSC to implement physical collocation in New York, without actually mandating it and possibly “dirtying its hands.”
result in antitrust liability. However, under *Florida Power Corp.*, the agreement to allow physical collocation on the local telephone company's property was not a taking because it was consensual.¹⁴⁸

From a policy standpoint, the NYPSC's decision-making process, i.e., beginning with virtual collocation and ending with physical collocation, and its acquiescence on the takings issue, were sensible choices. As a result, the NYPSC more effectively regulated to foster competition—through physical collocation—without paying the required compensation the initial ordering of physical collocation would have entailed.

¹⁴⁸ The NYPSC's actions do raise questions concerning whether the agreement of the local telephone company was in fact consensual.