Regulating Public Utility Performance:
The Law of Market Structure, Pricing and Jurisdiction

Chapter Twelve

The Federal–State Relationship

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> *The concept [of federalism] does not mean blind deference to 'States' Rights' any more than it means centralization of control over every important issue in our National Government and its courts. The Framers rejected both these courses. What the concept does represent is a system in which there is sensitivity to the legitimate interests of both State and National Governments, and in which the National Government, anxious though it may be to vindicate and protect federal rights and federal interests, always endeavors to do so in ways that will not unduly interfere with the legitimate activities of the States.*[1]

Our regulated industries live with two historical legacies: the Framers' 1789 decision to have both federal and state governments, and Congress's 1930s decisions to allocate regulatory powers between those two levels. As a result, most utilities today face both federal and state regulation. This bi-jurisdictional context produces three distinct perspectives:

1. Federal regulators want state regulators to promote, or at least not conflict with, federal policies.
2. State regulators want federal regulators to support, or least not preclude, state policies.
3. Regulated utilities want to avoid getting caught in a federal–state conflict, where complying with a state requirement violates a federal requirement, or complying with a federal requirement violates a state requirement.

These wishes are not always granted, for at least four reasons. First, Congress and state legislatures enact statutes at different times for different reasons. Unlike the House and Senate in Congress, they are not legislative partners, enacting laws jointly. There are no conference committees to work out federal–state differences before enactment. Second, federal and state statutes drafted in the 1920s and 1930s allocated state and federal powers based on then-clear distinctions between national policies and local services. Those distinctions have blurred: due to technology, physical interconnectedness and efforts to encourage competition over multi-state territories, in-state actions have multi-state effects and national decisions have in-state effects.[2] Third, the political process does not update statutes continuously to adjust jurisdiction to new industry facts. Fourth, at any point in time, state and federal regulators can hold different views on the relative roles and merits

1. Younger v. Harris, 401 U.S. 37, 44 (1971).
2. *See, e.g.*, New York v. FERC, 535 U.S. 1, 16 (2002) (explaining that "the landscape of the electric industry has changed since the enactment of the FPA, when the electricity universe was 'neatly divided into spheres of retail versus wholesale sales'" (quoting Transmission Access Policy Study Grp. v. FERC, 225 F.3d 667, 691 (D.C. Cir. 2000))); MCI Telecomms. Corp. v. AT&T Co., 512 U.S. 218, 220–21 (1994) (describing structural changes wrought by technology and competition).

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of regulation and competition as alternative means to induce industry performance, and on the techniques that can best advance those views.[3]

So we have disputes: cases going to court because one jurisdictional level is accused of interfering with the other. The federal–state relationship is unavoidably a struggle, but it is not a zero-sum game. This challenge of dual regulation—to embody "sensitivity to the legitimate interests of both State and National Governments"—is the subject of this chapter. It addresses two major questions:

What are the limits on federal and state actions? Our constitutional system has five possible trip wires—limits on regulatory action that, when violated, mean that one level has unlawfully diminished the powers of the other. (In this context, "regulatory action" means action by a commission or legislative body, since the wire can be tripped by either a commission order or a statute.) The first three are limits on federal power to protect state policies; the last two are limits on state power to protect federal policies:

1. The Commerce Clause authorizes Congress to regulate only those business activities that involve "commerce between the states."
2. The Tenth Amendment prohibits Congress from acting on matters reserved to the states.
3. A federal agency cannot act outside the authority granted by Congress.
4. The "dormant" Commerce Clause prohibits a state from discriminating against, or unduly burdening, interstate commerce.
5. The Supremacy Clause prohibits states from taking actions that undermine the goals of federal statutes.

For each of the five limits, we explain its constitutional source and provide illustrations from inside and outside utility regulation.

Within those five limits, how do federal and state regulators interact? There are six models of federal–state interaction: (1) bright line divisions, where each level operates within its assigned statutory domain; (2) federal regulator enlists the states in carrying out a federal program; (3) state regulators request the federal regulator's help carrying out a state program; (4) joint boards of federal and state regulators produce advice for the federal regulator; (5) regional compacts; and (6) concurrent jurisdiction, where both levels act on the same transaction independently of each other. For each of these six models, we provide statutory examples and explain their workings.

3. For additional discussion of the reasons for federal–state differences in regulatory policies, see the following essays by the author, all available at http://www.scottemplinglaw.com/essays: Federal–State Jurisdictional Relations: Pick Your Metaphor, Coordinated Regulation or Jurisdictional Wrestling: Which Will Produce Better Industry Performance?, Jurisdictional Peace Requires Joint Purpose, Federal–State Relations: A Plea for Constitutional Literacy.