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The Wires Go to War: The U.S. Experiment with Government Ownership of the Telephone System During World War I

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Articles

The Wires Go to War: The U.S. Experiment with Government Ownership of the Telephone System During World War I

Michael A. Janson* & Christopher S. Yoo**

One of the most distinctive characteristics of the U.S. telephone system is that it has always been privately owned, in stark contrast to the pattern of government ownership followed by virtually every other nation. What is not widely known is how close the United States came to falling in line with the rest of the world. For the one-year period following July 31, 1918, the exigencies of World War I led the federal government to take over the U.S. telephone system. A close examination of this episode sheds new light into a number of current policy issues. The history confirms that natural monopoly was not solely responsible for AT&T's return to dominance and reveals that the Kingsbury Commitment was more effective in deterring monopoly than generally believed. Instead, a significant force driving the re-monopolization of the telephone system was the U.S. Postmaster General, Albert Burleson—not Theodore Vail, President of AT&T. It also demonstrates that universal service was the result of government-imposed emulation of the postal system, not, as some have claimed, a post hoc rationalization for maintaining monopoly. The most remarkable question is, having once obtained control over the telephone system, why did the federal government ever let it go? The dynamics surrounding this decision reveal the inherent limits of relying on war to justify extraordinary actions. More importantly, it shows the difficulties that governments face in overseeing industries that are undergoing dynamic technological change and that require significant capital investments.

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Introduction

One of the characteristics of the U.S. telephone system generally thought to distinguish it from all others is that it has always been privately owned. In all other major countries, telephone systems have generally been owned and operated by the government, most commonly through an organization known as a Post, Telephone, and Telegraph (PTT).¹ The United States took a notably different course, having private ownership of telephone and telegraph systems.² Indeed, the American emphasis on individualism

1. Philip J. Weiser, *The Ghost of Telecommunications Past*, 103 MICH. L. REV. 101, 103 (2005) (reviewing PAUL STARR, *THE CREATION OF THE MEDIA: POLITICAL ORIGINS OF MODERN COMMUNICATION* (2004)).

2. See ROBERT MILLWARD, *PRIVATE AND PUBLIC ENTERPRISE IN EUROPE* 245 (2005) (“[P]ublic ownership by a single enterprise of a national network was the rule by 1950 and reflected, in part, the unwillingness of governments . . . to use arm’s-length regulation of private

and lack of a legacy of strong sovereign states has led some to regard government ownership of the telephone in the United States as unthinkable.³ The wave of privatizations that began worldwide in the 1980s is widely regarded as an implicit endorsement of the American approach.⁴

What is not widely known is how close the United States came to falling in line with the rest of the world. For the roughly one-year period following July 31, 1918, the federal government took over the U.S. telephone system.⁵ This period of history is important for many reasons. It provides a fascinating insight into the dynamics of institutional change, particularly regarding the role of individuals, political processes, and technology.

The episode also sheds light on many central issues of telecommunications policy today. For example, the analysis reveals that the reassertion of the Bell System's monopoly, long blamed on natural monopoly,⁶ or the Antitrust Division's failure to curb the ambitions of AT&T President Theodore Vail,⁷ was assisted and encouraged by the deliberate policies of the Postmaster General to consolidate the industry.⁸ Moreover, the Kingsbury Commitment of 1913 may have been more effective at preventing consolidation than generally realized.⁹ Further, contrary to the criticism that universal service was a concept that arose during the 1960s to rationalize the Bell monopoly after the fact,¹⁰ history reveals that universal service has its roots during the government takeover, much earlier than previously thought.¹¹ The episode marked a nascent revolution in federal-state relations that would ultimately collapse due to the unpopularity of rate increases.¹² Perhaps most revealing is the government's surprising decision, after having taken over the telephone system, to once again return it to

monopolies"); RICHARD B. KIELBOWICZ, *POSTAL ENTERPRISE: POST OFFICE INNOVATIONS WITH CONGRESSIONAL CONSTRAINTS, 1789–1970*, at 51 (2000), *available at* <http://www.prc.gov/prc-docs/library/refdesk/techpapers/Kielbowicz/enterprise.pdf> (“Except for the United States, virtually every nation regarded the telegraph and telephone as natural extensions of the state’s mail monopoly and operated them under a postal ministry.”).

3. ALAN STONE, *PUBLIC SERVICE LIBERALISM: TELECOMMUNICATIONS AND TRANSITIONS IN PUBLIC POLICY* 42 (1991).

4. See Wei Li & Lixin Colin Xu, *The Impact of Privatization and Competition in the Telecommunications Sector Around the World*, 47 J.L. & ECON. 395, 395–96 (2004) (documenting the dramatic increase in privately owned telephone systems during the 1980s and 1990s and showing that privatization improved industry performance).

5. Comment, *The Telegraph Industry: Monopoly or Competition*, 51 YALE L.J. 629, 633 (1942).

6. See GERALD R. FAULHABER, *TELECOMMUNICATIONS IN TURMOIL: TECHNOLOGY AND PUBLIC POLICY* 107 (1987) (“Indeed, until the late 1960s few questioned that the telephone industry was a natural monopoly.”); PETER W. HUBER ET AL., *FEDERAL TELECOMMUNICATION LAW* § 2.1.2, at 86 (2d ed. 1999) (“Is the telephone industry (or any part of it) a natural monopoly? Until the 1960s, the answer was generally presumed to be yes, from end to end.”).

7. TIM WU, *THE MASTER SWITCH: THE RISE AND FALL OF INFORMATION EMPIRES* 56 (2010).

8. See *infra* section II(B)(1).

9. See *infra* section III(A)(2).

10. MILTON L. MUELLER, *UNIVERSAL SERVICE* 6, 150–64 (1997).

11. See *infra* subpart III(B).

12. See *infra* subpart III(C).

private control.¹³ The government's reasons for doing so are quite revealing about the realities of management and ownership in an industry characterized by dynamic technological change.

Despite the importance of this episode in history, it has been largely overlooked by the scholarly community. Many histories discussing the competitive dynamics of this period fail to mention it at all.¹⁴ Other accounts offer a passing reference to it¹⁵ or devote a few pages to it.¹⁶ Indeed, only a handful of published works examine the history of the government takeover at any length,¹⁷ and these accounts focus on the political consequences of this

13. See *infra* subpart III(D).

14. E.g., FAULHABER, *supra* note 6; HUBER ET AL., *supra* note 6; KENNETH LIPARTITO, *THE BELL SYSTEM AND REGIONAL BUSINESS: THE TELEPHONE IN THE SOUTH, 1877-1920* (1989); ALAN STONE, *WRONG NUMBER: THE BREAKUP OF AT&T* (1989); Glen O. Robinson, *The Federal Communications Act: An Essay on Origins and Regulatory Purpose*, in *A LEGISLATIVE HISTORY OF THE COMMUNICATIONS ACT OF 1934*, at 3 (Max D. Paglin ed., 1989).

15. See, e.g., GERALD W. BROCK, *THE TELECOMMUNICATIONS INDUSTRY: THE DYNAMICS OF MARKET STRUCTURE* 156 (1981) (mentioning the government's control of telephone systems during World War I); JEFFREY E. COHEN, *THE POLITICS OF TELECOMMUNICATIONS REGULATION* 38 (1992) (referencing the government's experimentation with nationalization during World War I); CLAUDE S. FISCHER, *AMERICA CALLING: A SOCIAL HISTORY OF THE TELEPHONE TO 1940*, at 50 (1992) (making mention of the government's one-year takeover of the telephone industry); AMY FRIEDLANDER, *NATURAL MONOPOLY AND UNIVERSAL SERVICE* 77 (1995) (citing the telephone system's brief nationalization during World War I); 1 LEONARD S. HYMAN ET AL., *THE NEW TELECOMMUNICATIONS INDUSTRY: EVOLUTION AND ORGANIZATION* 81 (1987) (noting the Post Office's control of AT&T from August 1, 1918 to August 1, 1919 as part of the war effort); SUSAN E. MCMASTER, *THE TELECOMMUNICATIONS INDUSTRY* 47 (2002) (same); MUELLER, *supra* note 10, at 133 (mentioning centralization); PETER TEMIN, *THE FALL OF THE BELL SYSTEM* 11 n.3 (1987) (referencing the Postmaster General's control over the telephone system); William P. Barnett & Glenn R. Carroll, *How Institutional Constraints Affected the Organization of Early U.S. Telephony*, 9 J.L. ECON. & ORG. 98, 112 (1993) (indicating the government's brief period of control over the telephone industry); Kenneth A. Cox & William J. Byrnes, *The Common Carrier Provisions—A Product of Evolutionary Development*, in *A LEGISLATIVE HISTORY OF THE COMMUNICATIONS ACT OF 1934*, *supra* note 14, at 29 (mentioning the Post Office's control of the telephone and telegraph companies as a wartime measure); Geoffrey M. Peters, *Is the Third Time the Charm? A Comparison of the Government's Major Antitrust Settlements with AT&T This Century*, 15 SETON HALL L. REV. 252, 257 (1985) (pointing out the government's operation of the telephone systems during World War I).

16. E.g., JOHN BROOKS, *TELEPHONE: THE FIRST HUNDRED YEARS* 150-53, 157-59 (1975); ROBERT BRITT HORWITZ, *THE IRONY OF REGULATORY REFORM: THE DEREGULATION OF AMERICAN TELECOMMUNICATIONS* 101-02 (1989); GEORGE P. OSLIN, *THE STORY OF TELECOMMUNICATIONS* 278-79 (1992); J. WARREN STEHMAN, *THE FINANCIAL HISTORY OF THE AMERICAN TELEPHONE AND TELEGRAPH COMPANY* 175-81 (Augustus M. Kelley Publishers 1967) (1925); STONE, *supra* note 3, at 197-99; RICHARD H.K. VIETOR, *CONTRIVED COMPETITION* 172-73 (1994); Adam D. Thierer, *Unnatural Monopoly: Critical Moments in the Development of the Bell System Monopoly*, 14 CATO J. 267, 275-76 (1994); *The Telegraph Industry: Monopoly or Competition*, *supra* note 5, at 633-37.

17. N.R. DANIELIAN, *A.T.&T.: THE STORY OF INDUSTRIAL CONQUEST* 243-70 (1939); RICHARD R. JOHN, *NETWORK NATION: INVENTING AMERICAN TELECOMMUNICATIONS* 395-406 (2010); CHRISTOPHER N. MAY, *IN THE NAME OF WAR: JUDICIAL REVIEW AND THE WAR POWERS SINCE 1918*, at 26-59 (1989). The only unpublished discussions of any significance of which we are aware are a dissertation by political scientist Kenneth Bickers and a brief note by an FCC economist. Kenneth N. Bickers, *The Politics of Regulatory Design: Telecommunications in Historical and Theoretical Perspective* 134-56 (1988) (unpublished Ph.D. dissertation, University of

episode without discussing its consequences for the telecommunications system in general or its role in paving the way for AT&T's return to monopoly and the establishment of universal service in particular. The omission is rendered all the more curious by the recent heightening of interest in government ownership of communications networks, reflected in the support for municipal WiFi,¹⁸ the Dutch government's efforts to promote the buildout of municipal broadband networks,¹⁹ the inclusion of government funds for U.S. broadband deployment in the 2009 stimulus package,²⁰ and the Australian government's decision to fund more than three quarters of the cost to build fiber optic cable to the home.²¹ In addition, some scholars have either advocated government funding of broadband networks²² or proposed giving the postal system a greater role in the Internet.²³ These calls for the postalization of the Internet would do well to take into account the lessons from our nation's past experience with the postalization of telecommunications.

This Article is organized as follows: Part I discusses certain developments that set the stage for the takeover. These include the proposed takeover of the U.S. telegraph system, the nationalization of the British Telephone System, the wartime takeover of the U.S. railroad system, the early debates about nationalizing the U.S. telephone system, and the antitrust

Wisconsin-Madison) (on file with authors); Douglas Galbi, *Government Takeover of All Telephone Systems*, PURPLE MOTES (Apr. 4, 2010), <http://purplemotes.net/2010/04/04/government-takeover-of-all-telephone-systems/>.

18. See François Bar & Namkee Park, *Municipal Wi-Fi Networks: The Goals, Practices, and Policy Implications of the U.S. Case*, 61 COMM. & STRATEGIES 107, 107 (2006) (commenting on the growing number of municipal Wi-Fi networks in the United States and abroad).

19. Willem van Winden & Paulus Woets, *Urban Broadband Internet Policies in Europe: A Critical Review*, 41 URB. STUD. 2043, 2046, 2049–51 (2004).

20. See Lynne Holt & Mark Jamison, *Broadband and Contributions to Economic Growth: Lessons from the US Experience*, 33 TELECOMM. POL'Y 575, 575 (2009) (examining the connection between information and communications technologies and economic growth, and noting that Congress approved \$7.2 billion in funding for broadband planning and deployment initiatives as part of the American Recovery and Reinvestment Act of 2009).

21. See Roland Montagne & Valérie Chaillou, *Public Funding & FTTx: Assessing the Impact of Public Action*, 80 COMM. & STRATEGIES 153, 161 (2010) (noting that Australia represents a prime example of a national project to build a neutral, national FTTH network and reporting that Australia has invested €30 billion in the construction of an open national network); see also *National Broadband Network—Overview*, DEP'T BROADBAND, COMM. & THE DIGITAL ECON., AUSTRAL. GOV'T, http://www.dbcde.gov.au/broadband/national_broadband_network/nbn_overview (last modified Dec. 18, 2012) (describing Australia's National Broadband Network).

22. E.g., SUSAN P. CRAWFORD, CAPTIVE AUDIENCE: THE TELECOM INDUSTRY AND MONOPOLY POWER IN THE NEW GILDED AGE 263–67 (2013); LAWRENCE LESSIG, THE FUTURE OF IDEAS 244 (2002); BARBARA VAN SCHEWICK, INTERNET ARCHITECTURE AND INNOVATION 370 (2010).

23. See PRESIDENT'S COMM'N ON THE U.S. POSTAL SERV., EMBRACING THE FUTURE: MAKING THE TOUGH CHOICES TO PRESERVE UNIVERSAL MAIL SERVICES 143–58 (2003), available at http://www.treasury.gov/press-center/press-releases/Documents/pcusps_report.pdf (positing that “a digital postal network will enhance the value of the mail as a 21st century communications mode and improve virtually every aspect of the nation's postal service”).

scrutiny of AT&T that led to the Kingsbury Commitment. Part II lays out the history of the takeover, analyzing its enactment by Congress, its operation by the Postmaster General, and the decision to return the wires. Part III examines the lessons of the takeover, discussing the Postmaster General's active promotion of AT&T's return to monopoly, the origins of universal service, the transformation of federal-state relations, and the acknowledgement of the limits of government control implicit in the decision to return the wires.

I. Setting the Stage

The failure of the Soviet bloc's pattern of state-owned enterprises and the wide-scale privatization of telephone systems in recent years make it all too easy to reject government ownership as a viable policy option in modern history. During the Progressive Era, however, "the specter of nationalization was present and gaining momentum," a "fact [that] is often lost on historians of telephony during this era."²⁴ In fact, nationalization of the telephone system was not the exclusive province of socialists: A wide range of respectable voices, including many conservatives, supported government ownership.²⁵ A better appreciation for key aspects of the historical context, including proposals for government ownership of the U.S. telegraph system, the 1911 nationalization of the British telephone system, Progressive hostility toward large enterprises that led to the Kingsbury Commitment, and early debates over nationalization, helps put the debates over government ownership into perspective.

A. *Proposals for Government Ownership of the U.S. Telegraph System*

The telegraph preceded the telephone as the dominant means of telecommunications, and policy makers debated the merits of public ownership since its earliest days.²⁶ The history of the electromagnetic telegraph in the United States began on September 4, 1837, when Samuel Morse made a successful transmission across 1,700 feet of wire arranged in his classroom.²⁷ Ill suited to commercializing the invention himself, he

24. COHEN, *supra* note 15, at 38.

25. JOHN, *supra* note 17, at 363–65, 372–74; STONE, *supra* note 3, at 141, 195.

26. A report submitted by the Post Office to Congress in 1914 provides a useful overview of the early advocacy for government ownership of telecommunications. POSTMASTER GEN., GOVERNMENT OWNERSHIP OF ELECTRICAL MEANS OF COMMUNICATION, S. DOC. NO. 63-399, at 19–36 (2d Sess. 1914).

27. OSLIN, *supra* note 16, at 19. Morse was neither the first nor the only inventor working on telegraphy. Beginning in 1793, France deployed an optical telegraph system that used a series of towers topped by a set of movable arms that could send signals in a semaphore-like manner. In 1809, a German inventor developed a telegraph that used electrochemical processes connected by thirty-five wires to communicate. European inventors were also independently experimenting with electromagnetic telegraphs at more or less the same time as (indeed, perhaps slightly before) Morse. A.N. HOLCOMBE, PUBLIC OWNERSHIP OF TELEPHONES ON THE CONTINENT OF EUROPE 3–8 (1911). The U.S. Supreme Court would ultimately rule that Morse's invention came first. O'Reilly

convinced Congress to appropriate \$30,000 to establish a telegraph connection between Washington, D.C. and Baltimore,²⁸ through which Morse successfully sent a message on May 24, 1844.²⁹

At the time, many observers thought that the telegraph network should be owned and operated by the government. For example, Henry Clay found that the telegraph “is destined to exert great influence on the business affairs of society. In the hands of private individuals they will be able to monopolize intelligence and to perform the greatest operations in commerce I think such an engine ought to be exclusively under the control of the [G]overnment.”³⁰ Postmaster General Cave Johnson’s 1845 and 1846 Reports similarly supported government ownership of the entire telegraph system.³¹

In 1866, Congress enacted legislation that gave the government a five-year right to purchase all the telegraph lines at a value appraised by five disinterested arbitrators.³² The following year, Andrew Johnson’s Postmaster General, Alexander Randall, urged Congress to study the possibility of a postal takeover of the telegraph system.³³ In 1871, shortly after the government’s option to purchase the telegraph system expired, Postmaster General John Creswell endorsed the idea of a postal telegraph, pointing to the fact that Great Britain had nationalized its telegraph system in 1870.³⁴ This recommendation drew the approbation of President Ulysses S. Grant, who “recommend[ed] favorable consideration of the plan for uniting the telegraphic system of the United States with the postal system.”³⁵ Not only would public ownership reduce rates while rendering the same level of service, if not better³⁶: “It would secure the further advantage of extending

v. Morse, 56 U.S. (15 How.) 62, 108 (1853); *see also* Smith v. Downing, 22 F. Cas. 511, 513 (C.C.D. Mass. 1850) (No. 13,036) (holding that Morse had a right to patent the new method).

28. Act of Mar. 3, 1843, ch. 84, § 1, 5 Stat. 618; OSLIN, *supra* note 16, at 32.

29. OSLIN, *supra* note 17, at 32–33.

30. Letter from Henry Clay to Alfred Vail (Sept. 10, 1844), *reprinted in* Frank G. Carpenter, *Henry Clay on Nationalizing the Telegraph*, 154 N. AM. REV. 380, 382 (1892).

31. CAVE JOHNSON, REPORT OF THE POSTMASTER GENERAL, S. DOC. NO. 29-1, at 861 (1st Sess. 1845); CAVE JOHNSON, REPORT OF THE POSTMASTER GENERAL, S. DOC. NO. 29-1, at 688–89 (2d Sess. 1846). Morse even offered to sell the patent to the federal government for \$100,000, *see* S. DOC. NO. 63-399, at 19, and apparently attempted to give the patent to the Republic of Texas in 1838. OSLIN, *supra* note 16, at 23.

32. Act of July 24, 1866, ch. 230, § 3, 14 Stat. 221, 221–22.

33. ALEXANDER RANDALL, REPORT OF THE POSTMASTER GENERAL, H.R. EXEC. DOC. NO. 40-1, pt. 4, at 29 (2d Sess. 1867).

34. JOHN CRESWELL, REPORT OF THE POSTMASTER GENERAL, H.R. EXEC. DOC. NO. 42-1, pt. 4, at 28–9 (2d Sess. 1871).

35. President Ulysses S. Grant, Third Annual Message (Dec. 4, 1871), *in* 7 A COMPILATION OF THE MESSAGES & PAPERS OF THE PRESIDENTS 1789–1897, at 149–50 (James D. Richardson ed., 1898).

36. “[B]y such a course the cost of telegraphing could be much reduced, and the service as well, if not better, rendered.” *Id.* at 150.

the telegraph through portions of the country where private enterprise will not construct it,” as well as promote commerce and education.³⁷

During 1871 and 1872, Congress seriously debated government ownership of the telegraph system, dividing between one proposal (endorsed by the President and the Postmaster General) under which the federal government would take possession of the entire telegraph system and merge it with the post office,³⁸ and another proposal (backed by Gardiner Hubbard, who would eventually become President of the Bell System as well as Alexander Graham Bell’s father-in-law) that would place the entire industry in the hands of a single private company that was granted special privileges by the government and give the government preferential terms.³⁹ Congress deadlocked over these proposals and failed to enact either of them.⁴⁰ Creswell would repeat his call for government ownership of the telegraph system in 1872 and 1873 to no avail.⁴¹

The matter lay quiescent until 1880, when a visit to the British post office prompted Postmaster General Horace Maynard to ask whether the federal government should once again take up the issue of public ownership of the telegraph system.⁴² These calls were renewed in 1882 and 1883 by Postmasters General Timothy Howe and Walter Gresham.⁴³ Minority political party platforms in the 1880s echoed these sentiments. The Greenback Party platform of 1884 demanded “the establishment of a

37. *Id.*

38. Gardiner Hubbard, *The Proposed Changes in the Telegraph System*, 117 N. AM. REV. 80, 102–03 (1873).

39. *Id.* at 103–04.

40. *Cf. id.* at 104 (stating that time ran out before the proposal could be considered that session, and history shows us that they ultimately were not successful).

41. JOHN CRESWELL, REPORT OF THE POSTMASTER GENERAL, H.R. EXEC. DOC. NO. 42-1, pt. 4, at 21–35 (3d Sess. 1872); JOHN CRESWELL, REPORT OF THE POSTMASTER GENERAL, H.R. EXEC. DOC. NO. 43-1, pt. 4, at xxxiii–xxxvii (1st Sess. 1873). Congressional consideration of government ownership occurred contemporaneously with national political parties advocating for increased government regulation of the telegraph. The Labor Reform Party’s platform of 1872 resolved that “it is the duty of the government to so exercise its power over railroads and telegraph corporations that they shall not in any case be privileged to exact such rates . . . as may bear unduly or inequitably upon either producer or consumer.” LABOR REFORM PLATFORM OF 1872, *in* 1 NATIONAL PARTY PLATFORMS, 1840–1956, at 43 (Donald B. Johnson ed., 1978). Likewise, the Prohibition Party’s platform of 1872 called for reduction of telegraph rates “to the lowest practical point, by force of laws wisely and justly framed, with reference not only to the interest of capital employed but to the higher claim of the general good.” PROHIBITION PLATFORM OF 1872, *in* 1 NATIONAL PARTY PLATFORMS, 1840–1956, *supra*, at 46. In 1876, the Prohibition Party also called for the “reduction of the rates of inland and ocean postage of telegraphic communication.” PROHIBITION REFORM PLATFORM OF 1876, *in* 1 NATIONAL PARTY PLATFORMS, 1840–1956, *supra*, at 52.

42. HORACE MAYNARD, REPORT OF THE POSTMASTER GENERAL, H.R. EXEC. DOC. NO. 46-1, pt. 4, at 42 (3d Sess. 1880).

43. TIMOTHY HOWE, REPORT OF THE POSTMASTER GENERAL, H.R. EXEC. DOC. NO. 47-1, pt. 4, at xxvii–xxx (2d Sess. 1882); WALTER GRESHAM, REPORT OF THE POSTMASTER GENERAL, H.R. EXEC. DOC. NO. 48-1, pt. 4, at 33–37 (1st Sess. 1883).

government postal telegraph system.”⁴⁴ The Union Labor Party of 1888 declared, “The means of communication and transportation shall be owned by the people, as is the United States postal system.”⁴⁵ In accord with these calls for government action, between 1871 and 1884, Congress considered over two dozen proposals to nationalize the telegraph system, three quarters of which were apparently reported favorably out of committee.⁴⁶ None, however, was ever enacted.⁴⁷

In 1901, the Industrial Commission heard testimony from Professor Frank Parsons advocating government ownership.⁴⁸ The Postal Service Appropriations Act of 1901 contained a provision directing the Postmaster General “to report to Congress the probable cost of connecting a telegraph and telephone system with the postal service by some feasible plan,”⁴⁹ although it does not appear that the Postmaster General ever did so.⁵⁰ Aside from a passing mention by George Cortelyou in 1906 including the postal telephone in a laundry list of future improvements to the postal system,⁵¹ no further action was taken for more than a decade despite continuing support from minority parties.⁵²

Interest returned in 1912, when Postmaster General Frank Hitchcock once again proposed, “The telegraph lines in the United States should be made a part of the postal system,”⁵³ only to see that recommendation specifically disavowed by President Taft’s message transmitting this report. Taft “believe[d] that the true principle is that private enterprise should be permitted to carry on such public utilities under due regulation as to rates by proper authority rather than that the Government should itself conduct them.”⁵⁴ Taft thought it would be bad public policy “greatly to increase the

44. GREENBACK NATIONAL PLATFORM OF 1884, *in* 1 NATIONAL PARTY PLATFORMS, 1840–1956, *supra* note 41, at 69–70.

45. UNION LABOR PLATFORM OF 1888, *in* 1 NATIONAL PARTY PLATFORMS, 1840–1956, *supra* note 41, at 83.

46. *See* POSTMASTER GEN., GOVERNMENT OWNERSHIP OF ELECTRICAL MEANS OF COMMUNICATION, S. DOC. NO. 63-399, at 30 (2d Sess. 1914) (explaining that over seventy bills had been introduced to Congress for the purpose of establishing a postal telegraph and sixteen times the House and Senate Committees had reported favorably on the issue).

47. *Id.*; COHEN, *supra* note 15, at 37.

48. S. DOC. NO. 63-399, at 33.

49. Postal Service Appropriations Act of 1901, ch. 851, 31 Stat. 1099, 1104.

50. S. DOC. NO. 63-399, at 35.

51. GEORGE B. CORTELYOU, ANNUAL REPORT OF THE POSTMASTER-GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1906, H.R. DOC. NO. 59-4, at 81 (2d Sess. 1906).

52. The People’s Party platform of 1908 stated: “To perfect the postal service, the Government should own and operate the general telegraph and telephone systems and provide a parcels post.” PEOPLE’S PLATFORM OF 1908, *in* 1 NATIONAL PARTY PLATFORMS, 1840–1956, *supra* note 41, at 155.

53. FRANK H. HITCHCOCK, ANNUAL REPORT OF THE POSTMASTER GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1911, H.R. DOC. NO. 62-118, at 14 (2d Sess. 1912).

54. PRESIDENT WILLIAM H. TAFT, MESSAGE OF THE PRESIDENT OF THE UNITED STATES, H.R. DOC. NO. 62-559, at 8 (2d Sess. 1912).

body of public servants.”⁵⁵ Although the argument for government ownership would be strong if government could operate the system “at a less price . . . and with equal efficiency,” Taft was

not satisfied from any evidence that if these properties were taken over by the Government they could be managed any more economically or any more efficiently or that this would enable the Government to furnish service at any smaller rate than the public are now required to pay by private companies.⁵⁶

In any event, Taft believed that any such initiatives should be postponed until after the Post Office had established a postal savings bank and a parcel post.⁵⁷

Still, at this point, AT&T was sufficiently optimistic to predict in its annual report that “[t]he discussion of the government ownership of wire companies is not likely to become anything more than academic, at least for the present.”⁵⁸ The company was sufficiently concerned, however, to devote four additional pages to laying out arguments against government ownership of the telegraph system.⁵⁹ The report concluded, “The facts are, that there is hardly a telegraph or telephone system in the world now operated by any government which shows a profit, even under accounting methods employed, and not one that would not show a deficit under accounting methods obligatory upon private enterprise.”⁶⁰

Undeterred by the President’s opposition, Postmaster General Hitchcock’s next report in 1912 did not back down, arguing that government ownership of the telegraph lines would lower rates, and that the successful creation of the postal savings system and the parcel post justified renewing attention on the proposal.⁶¹

The advent of the Wilson Administration brought in a new Postmaster General, Albert S. Burleson, who would play a pivotal role in the debates over government ownership. Indeed, Burleson would advocate government ownership of the telephone system with a zeal that strained the limits of even the most ardent Progressive.⁶² On December 1, 1913, Burleson submitted his initial annual report, which adhered to Hitchcock’s position: “The

55. *Id.*

56. *Id.*

57. *Id.*

58. AT&T CO., ANNUAL REPORT OF THE DIRECTORS OF AMERICAN TELEPHONE & TELEGRAPH COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1911, at 36 (1912).

59. *Id.* at 36–40.

60. *Id.* at 39–40.

61. FRANK H. HITCHCOCK, ANNUAL REPORT OF THE POSTMASTER GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1912, H.R. DOC. NO. 62-931, at 13 (3d Sess. 1913).

62. See Adrian Anderson, *President Wilson’s Politician: Albert Sidney Burleson of Texas*, 77 SW. HIST. Q. 339, 345 (1974) (noting that Burleson’s advocacy of government ownership of the telephone system was “a goal that was really a little too radical even for most Progressives”).

monopolistic nature of the telegraph business makes it of vital importance to the people that it be conducted by unselfish interests, and this can be accomplished only through Government ownership.”⁶³ Expanding his point to include the telephone system, Burleson wrote, “Every argument in favor of Government ownership of telegraph lines may be advanced with equal logic and force in favor of the Government ownership of telephone lines.”⁶⁴ The report indicated that the Post Office Department was conducting an investigation and promised to submit a legislative proposal shortly.⁶⁵

B. The Nationalization of the British Telephone System

Another consideration that framed and colored debates over nationalization was the global trend toward governmental ownership of telephone systems. Manitoba had nationalized its telephone system in 1907.⁶⁶ Even more importantly, Great Britain had nationalized its telephone system in 1911.⁶⁷ Indeed, by 1913, the United States was the only major country whose telephone system was not publicly owned.⁶⁸

The fact that Britain implemented a highly successful rate cut immediately following the government takeover made government ownership seem alluring to many.⁶⁹ The demand for nationalization in the United Kingdom also came from the postal service’s fear of loss of revenue.⁷⁰ As Harper explains it: “The reason [for nationalization] was fear that [private telegrams] would damage the revenues of the postal service, coupled with serious dissatisfaction among the business community about the service being given by competing private interests.”⁷¹

63. ALBERT S. BURLESON, ANNUAL REPORT OF THE POSTMASTER GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1913, H.R. DOC. NO. 63-712, at 15 (2d Sess. 1914).

64. *Id.* at 16.

65. *Id.*

66. JAMES MAVOR, GOVERNMENT TELEPHONES: THE EXPERIENCE OF MANITOBA CANADA 26–28 (1917).

67. STONE, *supra* note 3, at 141. For the classic study on public ownership of telephone systems in Europe, see generally HOLCOMBE, *supra* note 27.

68. *See supra* note 2 and accompanying text.

69. *See* STONE, *supra* note 3, at 41–42 (“Earlier regulatory statutes had failed to bring rates down, leading to the drive to nationalize a business that was widely conceived as a public service.”); *Revision of Telephone Rates*, TIMES (London), Jan. 27, 1912, at 13 (quoting Postmaster General Herbert Samuel as stating that “it would be necessary before long to revise the rates of telephone users” and explaining that the rates “were at present unequal, in some cases not wholly equitable”); *Telephone Trunk Calls: Introduction of Lower Rates*, TIMES (London), Aug. 8, 1912, at 2 (reporting the announcement of Postmaster General Samuel that “he proposes to introduce lower rates for the use of telephone trunk lines during the less busy hours of the day,” with reductions ranging from one-quarter to three-quarters of the ordinary rates).

70. JOHN HARPER, MONOPOLY AND COMPETITION IN BRITISH TELECOMMUNICATIONS: THE PAST, THE PRESENT AND THE FUTURE 5 (1997).

71. *Id.*

C. *The Government Takeovers of the U.S. Railroad and Radio Systems*

The takeover of the telephone system also took place in the shadow of the federal government's decision to take over the railroad system.⁷² Unlike the telephone system, after years of corporate mismanagement and restrictive rate regulation by the ICC, the railroad industry was in a state of financial and operational disarray.⁷³ The flood of traffic to the Atlantic ports pushed the rail network to the brink of collapse.⁷⁴ Moreover, the industry had long sought coordination of the entire industry by a single entity to curb what it viewed as the excesses of competition.⁷⁵

Congress had anticipated the need for the government to take control of the railroads by including a provision in the Army Appropriations Act of 1916 authorizing the President to do so in the event of war.⁷⁶ Wilson issued the proclamation taking over the railroad system on December 28, 1917.⁷⁷ Congress ratified his decision by enacting the Federal Control Act on March 21, 1918.⁷⁸ The takeover was supported both by the industry, which welcomed cartelization as a sanctuary from unbridled competition, and the U.S. Chamber of Commerce, which embraced the idea of "Scientific Management."⁷⁹

Government operation of the rail system under the direction of the U.S. Railway Administration (USRA) (headed by William Gibbs McAdoo, Treasury Secretary and Wilson's son-in-law) proved controversial. Most controversial was the approval of a 28% across-the-board increase in rates.⁸⁰ McAdoo's determination to maintain labor peace and avoid strikes led him to order a series of wage increases, extend the eight-hour day to all rail employees, promote union membership by encouraging collective bargaining, and create an elaborate system of job classifications.⁸¹ The increased costs caused the railroads to operate at a substantial deficit.⁸²

72. See BROOKS, *supra* note 16, at 150 ("With the coming of war, agitation for government ownership [of the telephone system] greatly increased Government takeover of the railroads [in December 1917] fanned the flames; thereafter, advocates of a telephone takeover argued that government-run railroads and privately run wire communications constituted a logical inconsistency.").

73. JAMES W. ELY, JR., *RAILROADS AND AMERICAN LAW* 241 (2001).

74. *Id.*; Landon H. Rowland, *The Last Hurrah for the Gilded Age: The 1917 Nationalization of U.S. Railways*, Remarks at the World War I Museum 5 (Nov. 29, 2008), *available at* <http://www.landonrowland.com/RailroadSpeechFINAL.pdf>.

75. Rowland, *supra* note 74, at 5–6.

76. Army Appropriations Act of 1916, ch. 418, 39 Stat. 619, 645.

77. President Woodrow Wilson, Proclamation (Dec. 26, 1917), *in* 17 *A COMPILATION OF THE MESSAGES AND PAPERS OF THE PRESIDENTS* 8409, 8410 (James D. Richardson ed., 1921).

78. Federal Control Act, ch. 25, 40 Stat. 451 (1918).

79. Rowland, *supra* note 74, at 9.

80. *Id.* at 10; *see also* ELY, *supra* note 15, at 244 (discussing rates increases generally); GABRIEL KOLKO, *RAILROADS AND REGULATION 1877–1916*, at 228 (1965) (discussing specific rate increases).

81. ELY, *supra* note 73, at 244–45.

82. *Id.* at 245.

The cessation of hostilities raised the question of what to do next. The Federal Railroad Control Act of 1918 only authorized government control through twenty-one months after the end of hostilities,⁸³ which Wilson noted in his Annual Message expired in January 1921.⁸⁴ The fact that the USRA had been more generous in rates than the ICC made the railroads in no hurry to reclaim control.⁸⁵ The generous wage increases and work rules made the labor unions supportive as well.⁸⁶ The shippers who had borne the burden of the rate and wage increases disagreed.⁸⁷

Senator Albert Cummins (R-Iowa) introduced legislation on September 2, 1919, that would have consolidated the industry into a single entity, outlawed strikes, and based rates on a “fair” return on capital.⁸⁸ Although this bill passed the Senate, it faced opposition in the House, led by shippers complaining about the rate increases and who preferred the more shipper-friendly ICC.⁸⁹ Pressured by Wilson’s announced intention to end federal control on March 1, 1920,⁹⁰ Congress enacted compromise legislation.⁹¹ The effect of the legislation was to reinstate the prewar status quo, while protecting the industry from competition by authorizing pooling arrangements (subject to ICC approval), authorizing the ICC to set minimum as well as maximum rates, and forcing the most profitable lines to subsidize weaker lines.⁹² It also gave railroads a two-year guarantee of 5.5% return on investment and established a Railroad Labor Board to settle labor disputes.⁹³

The government’s contemporaneous takeover of the U.S. radio system has drawn less attention. The Navy had argued for government control over radio communications even before the war broke out.⁹⁴ Representative Joshua W. Alexander, Chairman of the committee with jurisdiction over the issue, introduced legislation in December 1916 that would have authorized

83. Federal Railroad Control Act, ch. 25, § 14, 40 Stat. 451, 458 (1918).

84. President Woodrow Wilson, Sixth Annual Address (Dec. 2, 1918), in 18 A COMPILATION OF THE MESSAGES AND PAPERS OF THE PRESIDENTS, *supra* note 77, at 8645.

85. Rowland, *supra* note 74, at 12.

86. ELY, *supra* note 73, at 245.

87. *Id.*

88. S. 2906, 66th Cong. (1919).

89. Rowland, *supra* note 74, at 13.

90. President Woodrow Wilson, A Proclamation (Dec. 24, 1919), in 18 A COMPILATION OF THE MESSAGES AND PAPERS OF THE PRESIDENTS, *supra* note 77, at 8804, 8804–05.

91. Transportation Act of 1920, ch. 91, 41 Stat. 456, 457.

92. ELY, *supra* note 73, at 246–47.

93. Rowland, *supra* note 74, at 13.

94. SUSAN J. DOUGLAS, INVENTING AMERICAN BROADCASTING, 1899–1922, at 258 (1987); PHILIP T. ROSEN, THE MODERN STENTORS: RADIO BROADCASTERS AND THE FEDERAL GOVERNMENT, 1920–1934, at 21–22 (1980); Ronald E. Sutton, *The Nationalization of the United States Radio System in 1917*, 10 J. VISUAL LITERACY 8, 9, 12 (1990). Some lower Navy officials disagreed. ROSEN, *supra*, at 22.

the Navy to take control over the entire radio system.⁹⁵ After hearings conducted in January 1917,⁹⁶ these proposals were allowed to die in committee.⁹⁷ The outbreak of war allowed the President to invoke the provision of the Radio Act of 1912 authorizing him to close or take control of all radio stations during times of war,⁹⁸ which Wilson asserted on the very day the Senate ratified his declaration of war on Germany.⁹⁹

The Navy ran the radio system with an iron fist. It incorporated more than fifty commercial stations into its network and closed all of the others.¹⁰⁰ It shut down all amateur operators, requiring that they certify that they had lowered their antennae and disconnected and sealed all of their transmitting and receiving equipment.¹⁰¹ Then, Undersecretary of the Navy Franklin D. Roosevelt broke the logjam caused by blocking patents¹⁰² by indemnifying all companies from liability for patent infringement.¹⁰³ The Navy also acquired radio companies both to consolidate patents and the industry structure.¹⁰⁴ As we shall see, during this time, the Navy testified in support of the federal takeover of the telephone system.¹⁰⁵

95. H.R. 19350, 64th Cong. § 6 (2d Sess. 1916); *see also* *Wireless Bill Introduced*, N.Y. TIMES, Dec. 20, 1916, at 12, <http://query.nytimes.com/mem/archive-free/pdf?res=9A06EEDD153BE633A25753C2A9649D946796D6CF> (noting the date of introduction).

96. *Radio Communication: Hearings Before the H. Comm. on the Merch. Marine & Fisheries on H.R. 19350*, 64th Cong. 3 (1917) (statement of Joshua W. Alexander, Chairman).

97. DOUGLAS, *supra* note 94, at 282; Sutton, *supra* note 94, at 12–13.

98. Act of Aug. 13, 1912, ch. 287, § 2, 37 Stat. 302, 303.

99. President Woodrow Wilson, Executive Order 2582 (Apr. 6, 1917), in 17 A COMPILATION OF THE MESSAGES AND PAPERS OF THE PRESIDENTS, *supra* note 77, at 8241.

100. JOSEPHUS DANIELS, ANNUAL REPORT OF THE SECRETARY OF THE NAVY FOR THE FISCAL YEAR 1917, H.R. DOC. NO. 65-618, at 44 (2d Sess. 1917).

101. Sutton, *supra* note 94, at 14.

102. In 1917, the Second Circuit upheld the validity of a Marconi-held patent that was essential to the vacuum tube. *See* *Marconi Wireless Tel. Co. of Am. v. De Forest Radio Tel. & Tel. Co.*, 243 F. 560, 565–67 (2d Cir. 1917) (upholding the lower court's finding of a valid Marconi-held patent and rejecting De Forest's counterclaim for patent infringement). Other key patents needed by vacuum tubes were held by AT&T and Columbia student Edwin H. Armstrong. 1 ERIK BARNOUW, *A TOWER IN BABEL: A HISTORY OF BROADCASTING IN THE UNITED STATES* 47 (1966). General Electric held the patent on another key vacuum-tube technology known as the Alexanderson alternator. *Id.* at 48–49.

103. GLEASON L. ARCHER, *HISTORY OF RADIO TO 1926*, at 137, 138 n.12 (1938); Sutton, *supra* note 94, at 15. The government's initial position was that the Act of June 25, 1910, Pub. L. No. 61-305, ch. 423, 36 Stat. 851, transferred any liability for patent infringement from the government contractors to the government. OFFICE OF NAVAL RECORDS & LIBRARY, *HISTORY OF THE BUREAU OF ENGINEERING OF THE NAVY DURING THE WORLD WAR* 128–29 (1922). The Supreme Court rejected this conclusion. *Marconi Wireless Tel. Co. of Am. v. Simon*, 246 U.S. 46, 55–56 (1918). Congress subsequently enacted legislation establishing that the only remedy for patents infringed by government contractors would be against the United States. *Naval Appropriations Act*, Pub. L. No. 65-182, ch. 114, 40 Stat. 704, 705 (1918).

104. OFFICE OF NAVAL RECORDS & LIBRARY, *supra* note 103, at 113–14; ROSEN, *supra* note 94, at 23; Sutton, *supra* note 94, at 15–16.

105. *See infra* note 197 and accompanying text. Support within the Navy was not universal. Chief of Naval Operations Captain David Todd argued that unlike radio communications, wireline

On November 21, 1918, ten days after the end of the war, Chairman Alexander submitted a bill supported by both Wilson and Secretary of the Navy Josephus Daniels that would have given the Navy permanent control.¹⁰⁶ Daniels's Annual Report of December 1 opined that the Navy's successful operation of the commercial radio system "presages the way for making this service entirely governmental."¹⁰⁷ Alexander's committee conducted hearings on the proposal from December 12–19.¹⁰⁸ The Navy found little industry support, having tactlessly alienated both the large industry players and amateur enthusiasts.¹⁰⁹ It also dissipated its energies jousting with other federal departments such as the Post Office, the Commerce Department, and the Army, which were also attempting to assert control over the radio industry, and failed to marshal popular and congressional support.¹¹⁰ The new Republican Congress proved less amenable than its Democratic predecessor.¹¹¹ The Committee was particularly angered by the Navy's acquisition of radio companies, which led to the tabling of the bill,¹¹² the enactment of an appropriations rider prohibiting further acquisitions,¹¹³ and calls for the divestiture of the acquired properties¹¹⁴ and even Daniels's impeachment.¹¹⁵ The Navy tried again in July 1919,¹¹⁶ only to face similar opposition.¹¹⁷

The Navy's belief that the American Marconi Company was controlled by British interests led it to view returning the radio industry to its prior owners as unacceptable.¹¹⁸ It approached Owen D. Young, who was General Counsel to General Electric, to form a new company known as the Radio

communications were less subject to interference and were provided by companies that were more cooperative. Sutton, *supra* note 94, at 16–17.

106. H.R. 13159, 65th Cong. (2d Sess. 1918).

107. JOSEPHUS DANIELS, ANNUAL REPORT OF THE SECRETARY OF THE NAVY, H.R. DOC. NO. 65-1450, at 22 (3d Sess. 1918).

108. *Government Control of Radio Communication: Hearings Before the H. Comm. on the Merch. Marine & Fisheries on H.R. 13159*, 65th Cong. (1918).

109. Sutton, *supra* note 94, at 19.

110. *Id.* at 10, 19.

111. DOUGLAS, *supra* note 94, at 282.

112. *Id.* at 283.

113. *Blocks Purchase of Radio Systems: House Amends Naval Bill to Prevent Diversion of Steam Engineering Bureau Funds*, N.Y. TIMES, Feb. 8, 1919, <http://query.nytimes.com/mem/archive-free/pdf?res=F0061FF73B5D147A93CAA91789D85F4D8185F9>.

114. *Wants Radios Returned: Congressman Rowe Also Thinks \$3,000,000 Should Be Recovered*, N.Y. TIMES, Jan. 18, 1919, <http://query.nytimes.com/mem/archive-free/pdf?res=F50E1FF6385D147A93CAA8178AD85F4D8185F9>.

115. *Wants Daniels Ousted: Mann Says He Should Be Impeached for Radio Purchases*, N.Y. TIMES, Jan. 30, 1919, <http://query.nytimes.com/mem/archive-free/pdf?res=F20A14FB3B5D147A93C2AA178AD85F4D8185F9>.

116. S. 3399, 66th Cong. (1st Sess. 1919).

117. DOUGLAS, *supra* note 94, at 284.

118. *Id.*

Company of America (RCA) guaranteed to be under American control.¹¹⁹ American Marconi transferred all of its assets into the company in exchange for RCA stock.¹²⁰ RCA, General Electric, and AT&T entered into cross-licensing agreements that neutralized the patent thicket obstructing U.S. development.¹²¹ The effect was to create a government-sanctioned monopoly.¹²²

D. *Labor Conflict*

These debates took place in the shadow of a looming telegraph operators' strike designed to force Western Union to unionize.¹²³ The Commercial Telegraphers' Union initially called the strike for April 9, 1918, but postponed it to permit arbitration by the War Labor Board.¹²⁴ After that failed, the union called for another strike on July 8, only to relent once again at the request of the Secretary of Labor.¹²⁵ The war footing made the strike particularly controversial. As one contemporary editorialist put it, labor strife and labor rights "must be instantly swept aside if they in the slightest degree threaten the country's efforts to win the war."¹²⁶ Some advocates saw government control as a means of maintaining service levels despite rising labor militancy and the corresponding increased threat of strikes.¹²⁷

E. *Progressive Sentiment and the Kingsbury Commitment*

Debates over government ownership of the telephone system were also framed by the rise of the Progressive movement. Some Progressives expressed strong distrust for large organizations and advocated strong antitrust enforcement to return to an economy dominated by small businesses.¹²⁸ Although they were suspicious of big government, they generally distrusted corporations more.¹²⁹ Others accepted corporations as a

119. RCA's charter stipulated that only U.S. citizens could serve as officers or directors and required that foreigners own no more than 20% of the stock. BARNOUW, *supra* note 102, at 59.

120. *Id.*

121. *Id.* at 60.

122. DOUGLAS, *supra* note 94, at 288.

123. MAY, *supra* note 17, at 28–30; OSLIN, *supra* note 16, at 278.

124. OSLIN, *supra* note 16, at 278.

125. *Washington Plea Prevents Strike on Western Union: Operators' Chief Yields to the Appeals of Secretary Wilson and Gompers*, N.Y. TIMES, July 8, 1918, <http://query.nytimes.com/mem/archive-free/pdf?res=F60911FB355F157A93CAA9178CD85F4C8185F9>.

126. George Harvey, *The Postal and the Western Union*, N. AM. REV.'S WAR WKLY., June 22, 1918, at 7.

127. See OSLIN, *supra* note 16, at 278 (indicating that President Wilson's reaction to the increased risk of strikes was to announce that Postmaster General Bureson would take over the telegraph and telephone systems for the government).

128. For a classic statement, see Louis D. Brandeis, *A Curse of Bigness*, HARPER'S WKLY., Jan. 10, 1914, at 21, available at <http://hdl.handle.net/2027/mdp.39015022184223> (recommending implementing legislation with an antitrust focus in order to "remedy the evils" of railroad monopolies).

129. RICHARD HOFSTADTER, *THE AGE OF REFORM* 229, 231, 233 (1955).

part of modern life and instead favored curbing them through technocratic regulation.¹³⁰ To these Progressives, the goal of returning to the old competitive order was a chimera.¹³¹

This ambivalence created a large gap between rhetoric and reality.¹³² Notwithstanding his reputation as the preeminent trustbuster in history, Theodore Roosevelt expressed reservations about aggressive antitrust enforcement, criticizing “the impossible task of restoring flintlock conditions of business sixty years ago.”¹³³ He therefore brought surprisingly few antitrust cases and limited the Antitrust Division to five attorneys and an annual budget of \$100,000.¹³⁴ Woodrow Wilson similarly regarded the emergence of large enterprises as “characteristic of our time” and “normal and inevitable” and stated that “we shall never return to the old order of individual competition.”¹³⁵ To them, bigness was not bad per se; instead, it was culpable only when it crossed certain lines.¹³⁶ Ironically, it was the non-Progressive William Howard Taft who asserted the antitrust laws most vigorously.¹³⁷

This ambivalence became apparent in the government’s policies with respect to AT&T. When competition first emerged in 1894, AT&T’s initial reaction was to attempt to outbuild the independents.¹³⁸ The result was a boon to consumers. The number of telephone connections, which had been growing at the somewhat languid annual rate of 6% prior to 1894, jumped to 20%.¹³⁹ Initially, the independents focused on areas that the Bell System had ignored, such as rural areas, small towns, and the suburbs of major cities.¹⁴⁰ Over time, they began to enter into direct competition with Bell. By 1902, competition existed in more than half of all cities with populations of greater than five thousand people.¹⁴¹ Consumers who purchased both connections

130. HERBERT CROLY, *THE PROMISE OF AMERICAN LIFE* 357 (1909); G. EDWARD WHITE, *PATTERNS OF AMERICAN LEGAL THOUGHT* 104 (1978).

131. CROLY, *supra* note 130, at 358–59.

132. HOFSTADTER, *supra* note 129, at 252–53.

133. President Theodore Roosevelt, Theodore Roosevelt’s Confession of Faith at the National Convention of the Progressive Party 27 (Aug. 6, 1912).

134. HOFSTADTER, *supra* note 129, at 245.

135. WOODROW WILSON, *THE NEW FREEDOM* 163 (1913); Woodrow Wilson, Response of Woodrow Wilson to Notification Address at the Democratic National Convention (Aug. 7, 1912), in *OFFICIAL REPORT OF THE PROCEEDINGS OF THE DEMOCRATIC NATIONAL CONVENTION OF 1912*, at 400, 407 (Urey Woodson ed., 1912).

136. HOFSTADTER, *supra* note 129, at 248.

137. Bickers, *supra* note 17, at 108.

138. Richard Gabel, *The Early Competitive Era in Telephone Communication, 1893–1920*, 34 *LAW & CONTEMP. PROBS.* 340, 354 (1969); Stanley M. Besen & Joseph Farrell, *Choosing How to Compete: Strategies and Tactics in Standardization*, 8 *J. ECON. PERSP.* 117, 122, 124 (1994).

139. Gabel, *supra* note 138, at 350 tbl.4.

140. *See id.* at 343–44 (arguing that Bell’s method of providing service prevented it from developing residential, suburban, and rural service went largely undeveloped, which restricted Bell’s growth).

141. VIETOR, *supra* note 16, at 170; Gabel, *supra* note 138, at 344.

could typically connect to five to ten times the number of other customers while paying less than the cost of buying a single connection during the monopoly period.¹⁴²

From AT&T's standpoint, this strategy turned out to be a dismal failure. AT&T's prices, profits, and stock price plummeted, and the capital requirements strained the company's ability to raise capital.¹⁴³ By 1907, AT&T's market share had fallen below 50%.¹⁴⁴ The financial markets had had enough. The Morgan banking interests took over the company and forced a change in management, installing Theodore Vail as president.¹⁴⁵ Under Vail's leadership, the company stopped competing directly with the independents and instead began pursuing two classic anticompetitive strategies. As an initial matter, they attempted to merge to monopoly by offering to buy out independents with whom they competed directly.¹⁴⁶ If the independent refused to sell, they pursued a classic division of markets by offering to withdraw from direct competition in return for a promise from the independent that it would not expand its territory and would interconnect with AT&T's long-distance network.¹⁴⁷

Vail justified the consolidation of all telephone companies into a single system with his "belie[f] that the telephone system should be universal, interdependent and intercommunicating, affording opportunity for any subscriber of any exchange to communicate with any other subscriber of any other exchange."¹⁴⁸ AT&T backed its strategy of withdrawing from competition with what has been described as the first major corporate public-relations campaign in history decrying the cost and inconvenience of having to maintain two separate connections, each with its own lines and handsets (known as dual service).¹⁴⁹ To compensate for the lack of price discipline

142. MUELLER, *supra* note 10, at 94; Robert Bornholz & David S. Evans, *The Early History of Competition in the Telephone Industry*, in *BREAKING UP BELL* 7, 30 (David S. Evans ed., 1983); David F. Weiman & Richard C. Levin, *Preying for Monopoly? The Case of Southern Bell Telephone Company, 1894–1912*, 102 J. POL. ECON. 103, 123–24 (1994); *see also* G. JOHNSTON, *SOME COMMENTS ON THE 1907 ANNUAL REPORT OF AT&T* 15–16 (1908) (describing the dramatic drop in the Bell System's rates).

143. Gabel, *supra* note 138, at 345–46; Weiman & Levin, *supra* note 142, at 109–23; MUELLER, *supra* note 10, at 70.

144. U.S. CENSUS BUREAU, *CENSUS OF ELECTRICAL INDUSTRIES: 1917—TELEPHONES* 11 (1920), available at <http://www2.census.gov/prod2/decennial/documents/1917telephones.pdf> (noting that Bell reported 51.2% of the market share in 1907).

145. Gabel, *supra* note 138, at 345.

146. *See, e.g.*, AT&T CO., *ANNUAL REPORT OF THE DIRECTORS OF THE AMERICAN TELEPHONE & TELEGRAPH COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1910*, at 21 (1911) ("Wherever it could be legally done, and done with the acquiescence of the public, opposition companies have been acquired and merged into the Bell System.").

147. Daniel F. Spulber & Christopher S. Yoo, *Toward a Unified Theory of Access to Local Telephone Networks*, 61 FED. COMM. L.J. 43, 71 (2008).

148. AT&T CO., *supra* note 146, at 22–23.

149. Spulber & Yoo, *supra* note 147, at 71.

resulting from the elimination of competition, AT&T dropped its long-standing opposition to government oversight and willingly submitted to rate regulation.¹⁵⁰

The result was an abrupt end to the erosion of AT&T's market share.¹⁵¹ Some competitors began to complain that the mergers represented a violation of the antitrust laws.¹⁵² These complaints did not prompt any immediate action by the Taft Administration, which despite its willingness to use the antitrust laws to break up Standard Oil and American Tobacco,¹⁵³ viewed each telephone merger as an independent event instead of evaluating them as part of a systematic campaign.¹⁵⁴ Independents warned that although each individual acquisition involved purely intrastate commerce, "[t]he avowed purpose of the Bell Company is to buy or crowd out the independent companies, which in the end will give them a complete monopoly of the telephone."¹⁵⁵ The Attorney General referred the matter to the ICC, which declined to act and eventually dropped the investigation.¹⁵⁶

Toward the end of the Taft Administration, however, the Justice Department began to view AT&T's acquisition campaign with greater skepticism. Concerned about acting too hastily and giving the appearance of political grandstanding on the eve of a presidential election, the Attorney General simply asked AT&T not to consummate any pending transactions until after the election,¹⁵⁷ a request with which AT&T complied.¹⁵⁸ The Wilson Administration successfully settled the case on December 13, 1913, when AT&T agreed to the so-called Kingsbury Commitment, named after the AT&T Vice President, Nathan Kingsbury, who brokered it.¹⁵⁹ According

150. AT&T CO., ANNUAL REPORT OF THE DIRECTORS OF AMERICAN TELEPHONE & TELEGRAPH COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1907, at 18 (1908).

151. Spulber & Yoo, *supra* note 147, at 73.

152. *See, e.g.*, Letter from Edward F. Murray, President, Murray's Line, to George W. Wickersham, Att'y Gen. (Nov. 13, 1912), *cited in* Bickers, *supra* note 17, at 116 n.64. *See generally* Letter from George W. Wickersham, Att'y Gen., to Charles A. Prouty, Chairman, Interstate Commerce Comm'n (Jan. 7, 1913), *quoted in* Bickers, *supra* note 17, at 113–14 (summarizing these complaints).

153. *United States v. Standard Oil Co.*, 221 U.S. 1, 81–82 (1911); *United States v. Am. Tobacco Co.*, 221 U.S. 106, 188 (1911).

154. Bickers, *supra* note 17, at 115.

155. Letter from Edward F. Murray, President, Murray's Line, to George W. Wickersham, Att'y Gen. (Nov. 23, 1912), *quoted in* Bickers, *supra* note 17, at 116.

156. Press Release, Interstate Commerce Comm'n, Investigation of Telephone and Telegraph Companies, Docket No. 5462 (Apr. 15, 1914), *cited in* Bickers, *supra* note 17, at 115 n.63.

157. Memorandum from George W. Wickersham, Att'y Gen., to J.A. Fowler, Assistant to the Att'y Gen. (Aug. 29, 1912), *quoted in* Bickers, *supra* note 17, at 117.

158. Letter from Theodore Vail, President, AT&T, to the presidents of all associated Bell telephone companies (Aug. 6, 1912), *cited in* Bickers, *supra* note 17, at 118 n.69.

159. Burleson stated, "If the efficient management and direction is given the telegraph and telephone that has been given the Postal Service, the probability is that they never will be returned to private control." DANIELIAN, *supra* note 17, at 246; *see also* Bickers, *supra* note 17, at 147

to the terms of the agreement, AT&T pledged to stop acquiring directly competing companies.¹⁶⁰ AT&T also promised to divest its ownership stake in Western Union and to permit the independents to interconnect with its long-distance network.¹⁶¹

Commentators have not been kind to the Kingsbury Commitment. Some complain that by allowing the Bell System to keep the properties instead of breaking it up as it did with Standard Oil, the antitrust authorities effectively condoned monopoly by refusing to undo the existing acquisitions and leaving them intact.¹⁶² Others have complained that the Kingsbury Commitment was toothless. For example, the Commitment did not prevent AT&T from acquiring independent local telephone companies with which it did not directly compete.¹⁶³ Even where companies competed directly, other scholars claim that the Justice Department permitted mergers so long as AT&T divested an equal number of lines elsewhere.¹⁶⁴ Others are somewhat less critical, insisting that the Kingsbury Commitment was successful in slowing down mergers temporarily.¹⁶⁵ As discussed below, the Kingsbury Commitment was more effective than commonly thought at slowing consolidation.¹⁶⁶ In any event, the Kingsbury Commitment was an important progressive policy preceding the nationalization of the wires.

F. *Early Debates over Nationalizing the U.S. Telephone System*

Interest in government ownership of the telegraph system began to extend to the telephone system as well in late 1913. The *New York Times* reported in October of that year, “Notwithstanding efforts at profound secrecy, it has become known here that the Wilson Administration is

(characterizing the temporary nationalization of the telephone lines as an experiment in government control as a permanent policy); STEHMAN, *supra* note 16, at 177 (same).

160. DANIELIAN, *supra* note 17, at 76.

161. *Id.* Before the Kingsbury Commitment, courts had been reluctant to rely on the antitrust laws to justify mandating interconnection with the long-distance network. *See* U.S. Tel. Co. v. Cent. Union Tel. Co., 202 F. 66, 72 (6th Cir. 1913) (declining to discuss whether an exchange could be compelled to provide long-distance service); Pac. Tel. & Tel. Co. v. Anderson, 196 F. 699, 705 (E.D. Wash. 1912) (holding that a company had no right to demand a physical connection with another line).

162. WU, *supra* note 7, at 56; *see also* Dean Burch, *Common Carrier Communications by Wire and Radio: A Retrospective*, 37 FED. COMM. L.J. 85, 87 (1985) (a former FCC Chairman noting that “by the time of the so-called Kingsbury Commitment in 1913, . . . AT&T’s monopolization of the telephone industry was well on its way to becoming an accomplished fact”); Harry M. Trebing, *Common Carrier Regulation—The Silent Crisis*, 34 LAW & CONTEMP. PROBS. 299, 305 (1969) (calling the reestablishment of monopoly “a *fait accompli* by 1913”).

163. COHEN, *supra* note 15, at 48; VIETOR, *supra* note 16, at 172; Gabel, *supra* note 138, at 352–53.

164. BROCK, *supra* note 15, at 155–56; Thierer, *supra* note 16, at 272.

165. HUBER ET AL., *supra* note 6, § 4.4.2; MUELLER, *supra* note 10, at 134.

166. *See infra* section III(A)(2).

engaged in preparing the groundwork” for nationalization of the nation’s telegraph and telephone lines.¹⁶⁷

On December 1, 1913, Postmaster General Burleson’s second annual report confirmed these suspicions, revealing that the Post Office had been studying the possible acquisition of the telegraph and telephone systems since the previous June.¹⁶⁸ On December 20, Representative David J. Lewis (D-Md.) introduced a resolution directing the relevant committees to consider a bill providing for the postalization of the telephone network.¹⁶⁹ He followed that with an extended defense of the merits of postalizing the telephone system that occupied thirty-five pages of the *Congressional Record*.¹⁷⁰ A December 23 meeting between Burleson and President Wilson left Burleson reluctant to press the issue, suggesting that the Administration was not unified in its support of Burleson’s proposal.¹⁷¹

The debate continued into early 1914. On January 29, the Senate passed a resolution directing the Postmaster General to send the results of his investigation to the Senate.¹⁷² Burleson complied on January 31, submitting a nearly 150-page report laying out the case for government ownership of both the telephone and telegraph system¹⁷³ that apparently drew the support of the Navy.¹⁷⁴ The House Committee on the Post Office and Post Roads would subsequently conduct hearings on “The Postalization of the Telephone” on January 15, 1915.¹⁷⁵ At these new hearings, Representative Lewis made a speech that was quite similar to his speech of December 1913, emphasizing the public benefits of government control.¹⁷⁶ The only other witness at the hearing was an officer of the second largest telegraph company

167. *Federal Wires New Wilson Plan: Policy Afoot to Control Nation’s Telephones as Key to Government Telegraph*, N.Y. TIMES, Oct. 2, 1913, <http://query.nytimes.com/mem/archive-free/pdf?res=FA0D11F63D5913738DDDAB0894D8415B838DF1D3>.

168. ALBERT S. BURLESON, ANNUAL REPORTS FOR THE FISCAL YEAR ENDED JUNE 30, 1913, H.R. DOC. NO. 63-712, at 16 (2d Sess. 1914).

169. 51 CONG. REC. 1377 (1913).

170. *Id.* at 1377–412.

171. *Lewis Opens Fight for U.S. Telephones*, N.Y. TIMES, Dec. 23, 1913, <http://query.nytimes.com/gst/abstract.html?res=FB0910F63A5813738DDDAA0A94DA415B838DF1D3>; accord BROOKS, *supra* note 16, at 149 (noting that “the government advocates of nationalization seemed to hang back awaiting their opening”).

172. Senate Resolution 242 was submitted on January 12 and was initially passed by unanimous consent. 51 CONG. REC. 1503 (1914). The next day, passage of the resolution was reconsidered, and the resolution was referred to the Committee on Post Offices and Post Roads. *Id.* at 1569. The Committee reported the resolution favorably January 29, and the Senate passed it. *Id.* at 2503–04.

173. POSTMASTER GEN., GOVERNMENT OWNERSHIP OF ELECTRICAL MEANS OF COMMUNICATION, S. DOC. NO. 63-399 (2d Sess. 1914).

174. ROSEN, *supra* note 94, at 21–22.

175. *The Postalization of the Telephone: Hearing Before the H. Comm. on the Post Office and Post Roads on H.R. 20471*, 63d Cong. (1915).

176. *Id.* at 3–143.

who testified in support of postalization in order to curb supposed abuses of his chief rival, Western Union.¹⁷⁷

AT&T responded with a vigorous campaign against postalization that attempted to stake out a middle ground in favor of a private monopoly subject to government regulation.¹⁷⁸ Its most extensive statement was a thirty-four-page discussion in its annual report on 1913, which asserted “no government owned telephone system in the world is giving as cheap and efficient service as the American public is getting from all its telephone companies.”¹⁷⁹ Other prominent examples of AT&T efforts to counter the rising sentiment in favor of nationalization include publishing a point-by-point rebuttal of Representative Lewis’s floor statement,¹⁸⁰ public speeches made by Vail and other Bell officials,¹⁸¹ as well as language in its annual reports.¹⁸²

Although Progressives were willing to use the antitrust laws and regulation to curb monopolies, they were far more ambivalent about government ownership. Although some commentators have simplistically seen Progressivism as favoring nationalization,¹⁸³ Progressives’ attitudes were much more complex. Specifically, government ownership pitted Progressives’ faith in scientific administration and centralized control against their intuitive distrust of uncontrolled economic power.¹⁸⁴ Wilson’s scholarly work placed him in the camp of the government-ownership skeptics. In a book published within two years of his inauguration, Wilson argued that, although natural monopolies can harm the public interest, in

177. *Id.* at 145–56.

178. Bickers, *supra* note 17, at 142–44.

179. AT&T Co., *supra* note 159, at 28–62.

180. AT&T Co., GOVERNMENT AND PRIVATE TELEGRAPH AND TELEPHONE UTILITIES: AN ANALYSIS (1914), reprinted in SELECTED ARTICLES ON GOVERNMENT OWNERSHIP OF TELEGRAPH AND TELEPHONE 129–57 (Katharine B. Judson ed., 1914).

181. Theodore Newton Vail, Some Observations on Modern Tendencies (Oct. 1915), in VIEWS ON PUBLIC QUESTIONS: A COLLECTION OF PAPERS AND ADDRESSES OF THEODORE NEWTON VAIL 1907–1917, at 240, 258–63 (1917); F.H. Bethell, Some Comment on Government Ownership of Telephone Properties (Feb. 25, 1914), reprinted in SELECTED ARTICLES ON GOVERNMENT OWNERSHIP OF TELEGRAPH AND TELEPHONE, *supra* note 152, at 159.

182. AT&T Co., ANNUAL REPORT OF THE DIRECTORS OF AMERICAN TELEPHONE & TELEGRAPH COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1915, at 50 (1916); AT&T Co., ANNUAL REPORT OF THE DIRECTORS OF AMERICAN TELEPHONE & TELEGRAPH COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1916, at 49–51 (1917).

183. See, e.g., COHEN, *supra* note 17, at 37 (highlighting the impact the rise of the Progressive movement had on proposals to nationalize the telegraph). See generally RICHARD EPSTEIN, HOW PROGRESSIVES REWROTE THE CONSTITUTION (2006) (characterizing Progressives as supporters of economic nationalism).

184. Bickers, *supra* note 17, at 88–89. On the conflicts within the Progressive movement, see HOFSTADTER, *supra* note 129, at 215–71 (describing the tension between business monopoly and political freedom in an era of increased reliance on government regulation); Michael J. Sandel, *Democracy’s Discontent: America in Search of a Public Philosophy*, 85 GEO. L.J. 2073, 2076–77 (1996) (detailing the varied responses among the Progressives to the threat corporate power posed to self-government).

most cases government ownership would be inferior to government regulation.¹⁸⁵

Public reaction was also largely critical of government ownership. A number of scholars criticized the methodology of Burleson's analysis.¹⁸⁶ The popular press was largely critical as well, raising concerns about efficiency of government operations as well as the potential abuse of patronage.¹⁸⁷ They also denigrated the performance of government-owned telephone systems in Europe, with one industry executive quipping, "And as to service—Government service would be a joke as compared with present service. If you don't believe it just try the Government service—telegraph and telephone—in Europe."¹⁸⁸

The imposition of the Kingsbury Commitment in December 1913 diverted Wilson's interest in pursuing government ownership.¹⁸⁹ Burleson maintained a steady drumbeat in support of nationalization in his annual reports, focusing some of his energy on the more limited goal of nationalizing the telephone systems of Alaska, Hawaii, and Puerto Rico.¹⁹⁰ The Navy did conduct a successful three-day test mobilization during May 6–8, 1916, during which the Navy used AT&T's network for all communication between all naval facilities and ships.¹⁹¹

In January and February 1917, the House Committee on the District of Columbia conducted extensive hearings on the possibility of the federal government taking over the D.C. telephone system, well before the U.S.

185. WOODROW WILSON, *THE STATE: ELEMENTS OF HISTORICAL AND PRACTICAL POLITICS* ¶¶ 1524–26 (1913).

186. *E.g.*, A.N. Holcombe, *Public Ownership of Telegraphs and Telephones*, 28 Q.J. ECON. 581, 583–86 (1914).

187. COHEN, *supra* note 15, at 38; STONE, *supra* note 3, at 197.

188. STONE, *supra* note 3, at 197; *see also* *Wilson Gets Facts on Wire Control*, N.Y. TIMES, Oct. 3, 1913, <http://query.nytimes.com/mem/archive-free/pdf?res=940CE1DF133FE633A25750C0A9669D946296D6CF> (citing Vail as saying government help with long-distance service could be welcome); *C.H. Mackay Derides Federal Ownership*, N.Y. TIMES, Dec. 19, 1913, <http://query.nytimes.com/mem/archive-free/pdf?res=F40F13F73B5B13738DDDA00994DA415B838DF1D3> (projecting that government ownership would result in operating at a loss as it had in the English context).

189. STONE, *supra* note 3, at 197–98.

190. *See* ALBERT S. BURLESON, ANNUAL REPORT OF THE POSTMASTER GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1914, H.R. DOC. NO. 63-1387, at 14–16 (3d Sess. 1914) (emphasizing that nationalizing the telegraph and telephone systems remained desirable, particularly in Alaska, Hawaii, and Puerto Rico); ALBERT S. BURLESON, ANNUAL REPORT OF THE POSTMASTER GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1915, H.R. DOC. NO. 64-358, at 51–52 (1916) (same); ALBERT S. BURLESON, ANNUAL REPORT OF THE POSTMASTER GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1916, H.R. DOC. NO. 64-1728, at 46–48 (1917) (same); ALBERT S. BURLESON, ANNUAL REPORT OF THE POSTMASTER GENERAL FOR THE FISCAL YEAR ENDED JUNE 30, 1917, H.R. DOC. NO. 65-770, at 79 (1918) (reiterating, generally, the claims contained in previous reports but omitting the claims regarding Hawaii and Puerto Rico).

191. DEP'T OF THE NAVY, ANNUAL REPORT OF THE NAVY DEPARTMENT FOR THE FISCAL YEAR 1916, H.R. DOC. NO. 64-1480, at 29 (2d Sess. 1917); BROOKS, *supra* note 16, at 150.

entry into World War I on April 6, 1917.¹⁹² On March 4, 1918, Burleson responded to a Senate request for information with a scathing criticism of the telephone service provided in Washington, D.C.¹⁹³ Ten days later, the House Committee on the District of Columbia favorably reported a bill authorizing the government takeover of the D.C. phone system.¹⁹⁴ Advocates clearly regarded the D.C. takeover more as an experiment in a permanent policy than a wartime measure.¹⁹⁵ Proposals for long-term government control enjoyed little support. Legislation authorizing permanent government operation of the entire telephone system submitted in January 1918 by the same Representative who would sponsor the successful temporary takeover legislation died in committee.¹⁹⁶

II. The History of the Government Takeover

The federal government's decision to take control of the U.S. telephone system was part of a broader debate over the proper role of the government during times of both peace and war. In reviewing this history, it is important to keep in mind that the forces driving the decision both to take the telephone system over and to give it back are complex. Were it simply a matter of reflexive support for the state during times of armed conflict, one would expect the takeover to have occurred as soon as war was declared, as was done with respect to radio. Instead, Congress waited eight months to take over the railroads and another nine months to assume control of the telephone system, pointedly declining to take action on an earlier proposal until the measure was framed as a prophylactic, emergency measure and the President gave it his political support. Perhaps even more interesting is the manner in which the underlying technology and the way that the government ran the telephone network influenced the decision to return the wires a year later.

A. *Enacting of the Takeover*

The legislation that would lead to the government takeover was introduced on June 27, 1918. The House Committee on Interstate and Foreign Commerce conducted hearings on July 2, at which the only witnesses were three government officials who were widely recognized as advocates of a permanent takeover: Burleson, Secretary of War Newton

192. *Government Monopoly of Telephone Communication in the District of Columbia: Hearing Before the H. Comm. on the D.C. on H.R. 18723*, 64th Cong. (1917).

193. ALBERT S. BURLESON, POSTMASTER GENERAL'S STATEMENT, H.R. REP. NO. 65-379, at 23-27 (2d Sess. 1918).

194. H.R. REP. NO. 65-379.

195. STEHMAN, *supra* note 16, at 177.

196. H.J. Res. 206, 65th Cong. (1918).

Baker, and Secretary of the Navy Josephus Daniels.¹⁹⁷ The Committee issued a report supporting the bill.¹⁹⁸ The Senate Committee on Interstate Commerce declined to conduct full hearings,¹⁹⁹ choosing on July 9 only to hear from Western Union President Newcomb Carlton, who testified that he saw no necessity that would justify taking over the telegraph system and that even if that were to happen, there was even less justification for taking over the telephone system.²⁰⁰ He did state publicly that he would prefer a government takeover to yielding to unionization.²⁰¹ No representative from AT&T participated in either hearing, although there is some ambiguity about whether AT&T actively opposed the measure.²⁰²

The war added a new dimension to the debate over nationalizing the telephone system. On June 28, Burleson wrote to Representative Thetus W. Sims (D-Tenn.) that government control was necessary “to prevent communications by spies and other public enemies” and “imperative to safeguard public interests.”²⁰³ Burleson said “paralysis of a large part of the system” was threatened, and there were “possible consequences prejudicial to our military preparations and other public activities that might prove serious or disastrous.”²⁰⁴ Comparing the American response to those of European states, Burleson concluded, “We are reminded that there is not a nation engaged in the war that [e]ntrusts its military or other communications to unofficial agencies.”²⁰⁵ Burleson as well as Secretary of War Baker and Secretary of the Navy Daniels all indicated that government ownership was

197. *Federal Control of Systems of Communication: Hearings Before the H. Comm. on Interstate and Foreign Commerce on H.J. Res. 309*, 65th Cong. (1918) [hereinafter *1918 House Hearings*]. On all three witnesses’ established support for government ownership, see 56 CONG. REC. 8717 (1918) (statement of Rep. Martin Madden).

198. H.R. REP. NO. 65-741 (1918).

199. *Votes 7 to 3 for Wire Control*, N.Y. TIMES, July 10, 1918, <http://query.nytimes.com/mem/archive-free/pdf?res=FB0F17F8355F157A93C2A8178CD85F4C8185F9>.

200. *1918 House Hearings*, *supra* note 197, at 7–8, 17.

201. *House Votes Wire Control; Senate Waits*, N.Y. TIMES, July 6, 1918, <http://query.nytimes.com/mem/archive-free/pdf?res=F00D1FF83C5A11738DDDAF0894DF405B888DF1D3>.

202. Some commentators point out that AT&T did not oppose the measure and indicate that “it was freely said that President Vail was in favor of government control.” DANIELIAN, *supra* note 10, at 246. Company legend holds that Vail went to Wilson in early 1918 and stated, “As long as you’ve taken over the railroads, you might as well take us over, too.” BROOKS, *supra* note 9, at 151. AT&T Vice President Kingsbury later denied that AT&T supported the takeover and said that he had attempted to gain admission to both the House and Senate Committee hearings, but was denied in both cases. *Return of the Wire Systems: Hearings Before the H. Comm. on Interstate and Foreign Commerce on H.R. 421*, 66th Cong. 22–23 (1919) [hereinafter *Return of the Wire Systems Hearings*] (statement of Nathan C. Kingsbury, Vice President, American Telephone & Telegraph Company).

203. Letter from A.S. Burleson, Postmaster Gen., to Thetus W. Sims, Chairman, H. Comm. on Interstate & Foreign Commerce (June 28, 1918), in 56 CONG. REC. 8719 (1918).

204. *Id.*

205. *Id.*

needed to prevent government secrets from falling into enemy hands.²⁰⁶ They also suggested that a strike by telecommunications workers would be particularly debilitating to the war effort.²⁰⁷

Most importantly, President Wilson signaled his support for a temporary takeover by sending a letter endorsing Burleson's arguments in support of the bill.²⁰⁸ His support was pivotal. During the House floor debate, Representative Martin B. Madden (R-Ill.) noted the absence of the President's explicit support.²⁰⁹ At the same time, he conceded, "If the President says to the House that he wants any power that will enable him to successfully conduct the war, there is no man in the House who will not vote to give it to him."²¹⁰ Supporters of the bill thereupon produced the letter, and it passed the House by a vote of 222 to 4.²¹¹

The debate forced supporters of the government takeover to place important limitations on the bill. Although Burleson and Daniels clearly harbored ambitions to make the takeover permanent,²¹² Congress had rejected earlier legislation that was not limited to wartime.²¹³ The bill carefully avoided this problem by limiting its effect to the duration of the war.²¹⁴ Indeed, the bill's sponsor, Representative James D. Aswell (D-La.), specifically disavowed any intention of making government ownership permanent.²¹⁵

The absence of any emergency to justify the takeover as well as concerns that Burleson might use a wartime measure as a prelude to a more permanent takeover of the wires²¹⁶ led Wilson to assure that the power would only be used in case of a telegraph strike and to emphasize the importance of

206. *1918 House Hearings*, *supra* note 197, at 3 (statement of Newton D. Baker, Secretary of War), 19 (statement of Josephus Daniels, Secretary of the Navy), 45 (statement of Albert S. Burleson, Postmaster General).

207. *Id.* at 41 (statement of Albert S. Burleson, Postmaster General).

208. Letter from President Woodrow Wilson to Thetus W. Sims, House of Representatives (June 28, 1918), in 56 CONG. REC. 8718 (1918).

209. 56 CONG. REC. 8717 (1918) (statement of Rep. Madden).

210. *Id.* at 8718.

211. *Id.* at 8735.

212. Burleson stated, "If the efficient management and direction is given the telegraph and telephone that has been given the Postal Service, the probability is that they never will be returned to private control." DANIELIAN, *supra* note 17, at 246; *see also* Bickers, *supra* note 17, at 147 (arguing the advocates of government control viewed it as an experiment for permanent government control); MAY, *supra* note 17, at 31-32, 36-38 (same); STEHMAN, *supra* note 16, at 177 (same).

213. *See* 56 CONG. REC. 8719 (1918) (statement of Rep. Sims) ("[T]he resolution introduced by Mr. Aswell in January was not a war-time proposition. . . . It was not confined to the operation of the war, and therefore never considered by the committee.").

214. *Id.* at 8721 (statement of Rep. Esch).

215. *Id.* at 8720 (statement of Rep. Aswell).

216. *Id.* at 8719 (statement of Rep. Madden) (noting that "[e]verybody knows the Postmaster General is a 'bug' on Government ownership").

putting such authority in place before it was needed.²¹⁷ Burleson's statement in support of the proposal was similarly contingent, urging passage of the resolution "in order that the President may act, *if necessary*."²¹⁸

Indeed, the tone of the debate suggested that the authority was a prophylactic measure. Although no exigency currently existed, Congress felt that giving the President the authority would allow him to act promptly should the need arise.²¹⁹ Representative Sims, who was the floor manager, similarly noted that "this power might be needed at any moment" and that the Administration simply asked that "the President be clothed with the power, so that he might exercise it *if the emergency arose*."²²⁰ Aswell emphasized that the takeover authority was not permanent,²²¹ as did other members in the debate.²²²

After a rancorous Senate floor debate²²³ that forced postponement of a planned recess²²⁴ and despite several editorials opposing the move,²²⁵ Congress subsequently adopted the resolution, and Wilson signed it into law on July 16, 1918.²²⁶ The text of the proposal made clear that it was an emergency measure. The takeover was to be exercised only when the President "shall deem it necessary for the national security or defense."²²⁷ Moreover, the statute explicitly provided that the takeover would end with the ratification of a peace treaty ending the war.²²⁸

Wilson, however, wasted little time and exercised this power via a proclamation on July 22, 1918, that gave the federal government control of

217. *President Asks Power to Control All Wire Systems*, N.Y. TIMES, July 2, 1918, <http://query.nytimes.com/gst/abstract.html?res=F50713FB3C5F15738DDDAB0894DF405B888DF1D3>.

218. 56 CONG. REC. 8719 (1918) (emphasis added).

219. *Id.* at 8716 (statement of Rep. Sims); *see also* Bickers, *supra* note 17, at 148–49 (referencing Representative Sims's statement concerning the need for Presidential authority if exigent circumstances arose).

220. 56 CONG. REC. 8716 (1918) (statement of Rep. Sims) (emphasis added).

221. *Id.* at 8720 (statement of Rep. Aswell) (calling the "fear of permanent Government ownership resulting from this legislation . . . ill founded").

222. *Id.* at 8717 (statement of Rep. Sims) (noting that unlike Aswell's previous proposal, the current proposal "continued the control only during the existence of war").

223. *Id.* at 8741–47, 8841–43, 8934, 8937, 8959–62, 9069–78.

224. *Congress Recess Held up by Fight on Wire Control*, N.Y. TIMES, July 7, 1918, <http://query.nytimes.com/gst/abstract.html?res=F60C12F63B5F1B7A93C5A9178CD85F4C8185F9>.

225. Editorial, *Government Control*, N.Y. TIMES, July 6, 1918, <http://query.nytimes.com/gst/abstract.html?res=9A00E7D8173EE433A25755C0A9619C946996D6CF&scp=2&sq=governme nt+control&st=p>; *The Unrepresented Public*, N.Y. TIMES, July 11, 1918, <http://query.nytimes.com/gst/abstract.html?res=9E07E5D7173EE433A25752C1A9619C946996D6CF>.

226. H.R.J. Res. 309, 65th Cong., 40 Stat. 904 (1918).

227. *Id.*

228. *Id.*

the wires effective July 31.²²⁹ In his proclamation, Wilson directed Burleson to undertake “the supervision, possession, control and operation of [the] telegraph and telephone systems.”²³⁰ Wilson assured stock and bondholders that their interests would not be jeopardized. He stated, “Regular dividends hitherto declared, and maturing interest upon bonds, debentures, and other obligations, may be paid in due course.”²³¹ On November 2, Wilson issued a proclamation taking over the submarine cables as well.²³² Although hostilities ended on November 11, 1918,²³³ and the Treaty of Versailles ending the war was signed on June 28, 1919,²³⁴ the government would continue to operate the wires until midnight July 31, 1919, just slightly more than one year after taking them over.

B. Running the Telephone System

The Post Office that took over the telephone system on July 31, 1918 faced some seemingly insurmountable challenges.²³⁵ Most basically, the Post Office lacked the experience and administrative capacity to manage a large telecommunications network.²³⁶ In stark contrast to the takeover of the railroads, Congress had failed to provide any detailed guidance as to how the system should be run or what the terms of compensation should be.²³⁷ Moving quickly to address his lack of experience running the wires, Burleson’s first step was to issue Bulletin No. 1 on July 23 forming a Wire Control Board consisting of Burleson, two other members of the post office, and David J. Lewis, the once and future Congressman who supported nationalization so avidly and who was then serving as a U.S. Tariff Commissioner after a failed bid for the Senate.²³⁸ Next, on July 29, Burleson

229. President Woodrow Wilson, A Proclamation (July 22, 1918), in 18 A COMPILATION OF THE MESSAGES AND PAPERS OF THE PRESIDENTS, *supra* note 77, at 8551–53.

230. *Id.* at 8552.

231. *Id.*

232. President Woodrow Wilson, A Proclamation (Nov. 2, 1918), in 18 A COMPILATION OF THE MESSAGES AND PAPERS OF THE PRESIDENTS, *supra* note 77, at 8630–31. Indications that the government may not have taken control of the undersea cables until after hostilities had ended provoked accusations that the government’s actions were motivated not by military exigency, but rather by a desire to assert permanent control over the wireline communications system. MAY, *supra* note 17, at 38–42.

233. MARGARET MACMILLAN, PARIS 1919: SIX MONTHS THAT CHANGED THE WORLD 157–58 (2001).

234. *Id.* at 485.

235. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., RETURN OF THE WIRE SYSTEMS, ORDER NO. 3380 (July 30, 1919), reprinted in U.S. POST OFFICE, GOVERNMENT CONTROL AND OPERATION OF THE TELEGRAPH, TELEPHONE AND MARINE CABLE SYSTEMS, AUGUST 1, 1918, TO JULY 31, 1919, at 56, 92 (1921).

236. Bickers, *supra* note 17, at 151.

237. See DANIELIAN, *supra* note 17, at 250 (detailing that Postmaster General Burleson relied on Bell’s executives in deciding how to operate the wires and how to compensate the companies).

238. The other members from the Post Office aside from Burleson were John Koons, First Assistant Postmaster General, and William Lamar, Solicitor for the Post Office. U.S. POST OFFICE,

summoned Vail to meet with him in Washington, D.C., amid wide speculation that the first order of business would be to fire Vail.²³⁹ Given the breadth of discretion that had been granted to Burleson, Vail felt almost entirely at Burleson's mercy.²⁴⁰ Vail pledged that all of AT&T's officers and employees would do everything in their power to support the war effort.²⁴¹ Indeed, Vail regarded it as an opportunity to see what could be accomplished when both telephone and telegraph systems were operated by the same management.²⁴² Vail was unconcerned with compensation, stating, "You fix it, and I'll be satisfied."²⁴³

Burleson told Vail's biographer that he had expected Vail to be "in a class with the average railroad president—an autocrat, interested only in the success of his road as shown by profits accruing to his stockholders, and also largely concerned as to the continuance of his salary."²⁴⁴ Instead, he quickly grew to regard Vail as "a great, unselfish patriot" and "a warm and true friend" who "never made a suggestion . . . that was in the slightest degree tinged with selfishness and that was not prompted by the highest motive."²⁴⁵ Thoroughly disarmed, Burleson reassured Vail that he did not plan to operate the telephone system permanently and eventually regarded him as a "confidential adviser and counselor in all matters pertaining to the telephone."²⁴⁶

Given the absence of administrative personnel within the Postal Service to run the telephone system, on August 1, Burleson issued Bulletin No. 2 ordering that "[u]ntil further notice, the telegraph and telephone companies shall continue operation in the ordinary course of business through regular channels."²⁴⁷ In addition, "[a]ll officers, operators, and employees of the telegraph and telephone companies will continue in the performance of their present duties, reporting to the same officers as heretofore and on the same

OFFICE OF POSTMASTER GEN., BULL. NO. 1, WIRE CONTROL BOARD, ORDER NO. 1744 (July 23, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 61, 61–62.

239. BROOKS, *supra* note 16, at 151–52.

240. Vail reportedly told the two Vice Presidents who were accompanying him:

Well, I never in my life felt so helpless as I do at this moment. These people we are going up to see have got us entirely in their hands—they have taken our property and probably intend to keep it. They can do what they please with us, and we cannot help ourselves. For once in my life I am completely at sea.

ALBERT BIGELOW PAINE, *IN ONE MAN'S LIFE: BEING CHAPTERS FROM THE PERSONAL & BUSINESS CAREER OF THEODORE N. VAIL* 320 (1921).

241. *Id.* at 321.

242. *Id.* at 322.

243. *Id.* at 323.

244. *Id.* at 322.

245. *Id.* at 323–24.

246. *Id.* at 323.

247. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 2, ORDER ASSUMING POSSESSION AND CONTROL, ORDER NO. 1783 (Aug. 1, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 62, 62.

terms of employment.”²⁴⁸ Thus, the takeover was more akin to a change in management, rather than a change in ownership. On December 13, Burluson gave industry executives an even larger role when he transferred operational authority from the Wire Control Board to a new operating board consisting entirely of industry executives.²⁴⁹ The operating board was expanded to include additional industry executives on January 10 and March 6, 1919.²⁵⁰

Burluson also effectively ensured that AT&T would do quite well by the deal. On October 5, Burluson approved a contract that was quite generous from AT&T’s perspective. The contract promised to operate the system at the same level of efficiency achieved in the past and to maintain the property in its current state of repair and gave AT&T the right to inspect the books at reasonable times.²⁵¹ The government agreed to cover all taxes, licensee fees, and charges.²⁵² The contract preserved the 4.5% license contract fee that the local operating companies had been paying to the Bell System’s long-distance arm and included a fairly generous depreciation rate of 5.72%.²⁵³ The government also agreed to maintain AT&T’s stock dividend of eight dollars per share.²⁵⁴ Finally, the government agreed to hold AT&T harmless for any injuries or expenses that were incurred.²⁵⁵ In short, the government effectively guaranteed AT&T’s previous rate of return while assuming all of the risks of operating the system.

In addition, the Post Office took several actions that would have a lasting impact on the telephone system. These included ordering the industry to resume merging to monopoly, quelling labor unrest, and ordering rate increases.

248. *Id.*

249. The Board consisted of Union N. Bethell and F.A. Stevenson of AT&T; G.M. Yorke of Western Union; and A.F. Adams to represent the independent telephone companies. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., APPOINTMENT OF OPERATING BOARD, ORDER NO. 2479 (Dec. 13, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 238, at 74, 74; *see also* DANIELIAN, *supra* note 17, at 256–57 (describing each man’s corporate affiliations). It took control on January 1, 1919. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., OPERATING BOARD TO ASSUME OPERATION, ORDER NO. 2534 (Dec. 23, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 238, at 82, 82 n.3.

250. Specifically on January 10, the operating board appointed F.B. MacKinnon of the U.S. Independent Telephone Association to serve as liaison to the independents. On March 6, the operating board placed N.T. Guernsey (AT&T’s general counsel) in charge of the board’s legal department, named Bancroft Gherardi (AT&T’s acting chief engineer) head of the engineering department, and designated W.S. Gifford (AT&T’s Comptroller) as head of the accounting department. DANIELIAN, *supra* note 17, at 257.

251. U.S. POST OFFICE, PROPOSAL FOR COMPENSATION OF — TELEPHONE CO. TO THE POSTMASTER GENERAL, *reprinted in* U.S. POST OFFICE, *supra* note 235, at 23, 24–25.

252. *Id.* at 26.

253. DANIELIAN, *supra* note 17, at 252.

254. *Id.* at 251.

255. U.S. POST OFFICE, *supra* note 251, at 23, 25, 28.

1. *Mandating the Return of Monopoly.*—Burleson moved quickly to declare the scope of his intentions and his perspective on the future of the system. In Bulletin No. 2 (issued the day after he took over the telephone system), Burleson made clear that the purpose of government control was “to coordinate and unify these services so that they may be operated as a national system.”²⁵⁶

On August 7, Burleson issued Bulletin No. 3 on “Consolidation of Competing Telephone Systems,” which noted, “The Governmental operation and control of the telephone systems of the country *will undoubtedly cause the coordination and consolidation of competing systems wherever possible.*”²⁵⁷ To encourage the unification of the service, Burleson indicated that “negotiations . . . already under way for the consolidation of a number of competing telephone systems at the time the Government assumed control” would not be disturbed.²⁵⁸ Even where such negotiations were not yet underway, Burleson made clear that he had “no objection to the companies taking up such negotiations.”²⁵⁹

Burleson backed up his rhetorical support for consolidation with directives to the operators. Bulletin No. 4, issued on August 15, ordered companies “[t]o proceed as expeditiously as possible with the plans heretofore instituted for consolidating and unifying the telephone plants and properties.”²⁶⁰ In areas where such plans were not yet underway, the Bulletin ordered that consolidation plans “should be formulated as soon as practicable” wherever consolidation “is manifestly desired by the public” and “can be effected on fair terms and in accordance with law.”²⁶¹ Where two competing operators continued to operate, Burleson ordered them to “cooperate in making extensions and betterments,” in order to promote “unification and the elimination of waste.”²⁶² On the same day, Burleson issued another order creating a Committee on Solicitation of Telephone Systems consisting of AT&T Vice President Nathan C. Kingsbury and the president of one of the independents “for the purpose of making the necessary investigations, conducting negotiations, and arriving at agreements *for the unification and consolidation of the various telephone companies*

256. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., *supra* note 247, at 62, 62.

257. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 3, CONSOLIDATION OF COMPETING TELEPHONE SYSTEMS (Aug. 7, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 62, 62 (emphasis added).

258. *Id.* at 63.

259. *Id.*; Office of Information, Post Office Department (Aug. 7, 1918). Papers of Albert Sydney Burleson, Manuscripts Collection, Library of Congress (ASB), Box 21.

260. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 4, EXTENSIONS AND BETTERMENTS CURTAILED, ORDER NO. 1858 (Aug. 15, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 63, 63.

261. *Id.*

262. *Id.*

*operating in the same communities.*²⁶³ In all, Burleson would approve thirty-four consolidations of competing telephone operations.²⁶⁴ In addition, Burleson deviated from the established principle that the common carriage obligation to provide nondiscriminatory service applied only to consumers and not to business rivals²⁶⁵ by issuing a Bulletin indicating that he would order long-distance companies to interconnect with any requesting local telephone companies that did not have long-distance facilities “if upon investigation it is found practicable to do so.”²⁶⁶

Burleson’s advocacy for integration and consolidation extended beyond just the telephones. On November 18, 1918, Burleson ordered that as of November 18, all of the telegraph systems “shall hereafter be operated as one” and as of December 1, “all telegraph offices shall accept for transmission all classes of messages now accepted by any one of them at the prescribed tariff rates.”²⁶⁷ The same day, Burleson issued an order taking control over the submarine cable system, using the same language contained in his order taking over the telephone and telegraph systems, indicating that his goal was “to coordinate and unify these services so that they may be operated as a national system.”²⁶⁸

The next day, Burleson stated that an effective communication system required “intimate relations under which a continuous circuit can be established The effectiveness of the service is dependent upon the extent of the common control of circuits.”²⁶⁹ Burleson drew support for his conclusion from the fact that each of the telegraph systems had its own

263. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., COMMITTEE ON CONSOLIDATION OF TELEPHONE SYSTEM, ORDER NO. 1855 (Aug. 15, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 63, 63–64.

264. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., REPORT OF THE POSTMASTER GENERAL ON THE SUPERVISION AND OPERATION OF THE TELEGRAPH, TELEPHONE, AND CABLE PROPERTIES (Oct. 31, 1919), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 5, 11.

265. The seminal decision is *The Express Package Cases*, 117 U.S. 1 (1885), in which the Supreme Court held that while railroads were obligated to carry passengers, they were not obliged to carry business rivals (including express package services), reasoning that railroads were not obligated to be a “common carrier of common carriers.” *Id.* at 21. For descriptions of decisions extending this principle to telephony and holding that long-distance companies need not interconnect with local telephone companies, see HUBER ET AL., *supra* note 6, § 1.3.1, at 15–16, § 5.1.1, at 407–08; MUELLER, *supra* note 10, at 48–50. For an early deviation from this principle, see MUELLER, *supra* note 10, at 116 (citing *U.S. Tel. Co. v. Cent. Union Co.*, 171 F. 130, 143 (C.C.N.D. Ohio 1909)).

266. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 13, LONG DISTANCE CONNECTIONS FOR ALL SYSTEMS (Nov. 18, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 67, 67.

267. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 16, TELEGRAPH SYSTEMS OPERATED AS ONE, ORDER NO. 2353 (Nov. 18, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 70, 70.

268. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 14, ORDER ASSUMING POSSESSION AND CONTROL OF CABLES, ORDER NO. 2351 (Nov. 18, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 238, at 68, 68.

269. OFFICE OF INFO., POST OFFICE DEP’T (Nov. 19, 1918), ASB, Box 22.

“independent cable systems.”²⁷⁰ Moreover, Burleson pointed to recent problems to make his case:

The recent breakdown in connection with one of the cable systems has demonstrated the absolute necessity of being able to utilize at will the facilities of either cable system with all of the land line systems, in order that traffic may be adjusted in the same hands as it is on the land lines.²⁷¹

Burleson laid out the multifaceted rationale for these moves in his letter of December 4, 1918, ordering Western Union to place its European submarine cables under the control of its chief rival, the Commercial Cable Company.²⁷² First, there was the notion that the war required greater unity. Burleson explained that the “present emergency” demanded “unification in operation to the fullest extent possible [of] the cable systems” and that it could only be accomplished “through the operation of the two systems under one management.”²⁷³ Second, and perhaps most importantly, Burleson had a fixed set of beliefs about the importance of consolidation. He envisioned a national economy linked by a common communications system. Burleson wrote:

To do this efficiently and economically requires the combination of every kind of electrical transmission of intelligence into one system over which the most efficient service could be rendered through the development of new and useful services, and the wire plant and other facilities being utilized to their fullest extent.²⁷⁴

The public was demanding “one telephone system,”²⁷⁵ and the only real barrier to development was the disunity in the current system. Burleson argued:

The transmission of speech or electrical continuous signals is now practically from every commercial industrial or social community as a center, to the limits of *effective common control over a continuity of circuits*. Any limitations are wholly in the lack of continuity in the facilities—not in the “state of the art.”²⁷⁶

Echoing statements made by defenders of monopoly, Burleson said that a long-distance system required “perfect co-ordination which can only come from one unified system.”²⁷⁷ Burleson allowed that interconnection could

270. *Id.*

271. *Id.*

272. Letter from Albert S. Burleson, U.S. Postmaster General, to Clarence H. Mackay, President, Commercial Cable Co. (Dec. 4, 1918), ASB, Box 22.

273. *Id.*

274. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., REPORT ON POST OFFICE DEPARTMENT WIRE SYSTEM (Dec. 6, 1918), ASB, Box 22.

275. *Id.*

276. *Id.*

277. *Id.*

work, but only with a reciprocity equaling “virtual subordination” during the time of control by the other system.²⁷⁸

Burleson’s belief was further underscored by his anger when the Commercial Cable Company refused to unify its facilities with Western Union’s. Burleson declared that “the present emergency necessitated the unification in operation to the fullest extent possible of the cable systems leading from this country to Europe.”²⁷⁹ Indeed, it was manifest that full utilization “could only be accomplished through the operation of the two systems under one management.”²⁸⁰ Burleson underscored the importance that

the operation of the said cable systems be unified not only for improvement of service but also that important economies in operation may be effected during the period of Government control which can be accomplished only by placing such unified operation under the management of persons in complete accord with the ends desired[.]²⁸¹

When Mackay refused to interconnect his cables with Western Union’s in December 1918, Burleson removed the leadership of the Commercial Cable Company from any management role in the marine cable system and transferred those responsibilities to Western Union, ordering the president of Western Union to “carry into effect directions which have been given for the unification of the operation.”²⁸² When the Commercial Cable Company continued to resist unification, Burleson removed its officers, board of directors, and owners from any supervisory responsibility and placed operating board member A.F. Adams in charge of the company.²⁸³

Burleson backed up such strong measures with broad statements evincing his support for consolidation. For example, Burleson’s belief in unification was trumpeted in his first report. He sought to promote “the coordination and unification of all service rendered by [the telephone and telegraph] properties” by promoting “consolidations for the purpose of getting rid of pernicious competition and wasteful operation” as well as through “a general standardization of rates and rules of operation.”²⁸⁴ These statements reflected Burleson’s belief in the “potential economies under a

278. *Id.*

279. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., APPOINTMENT OF MANAGER OF CABLES, ORDER NO. 2474 (Dec. 12, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 72, 73.

280. *Id.*

281. *Id.* at 74.

282. *Id.*

283. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., REMOVAL OF CERTAIN OFFICES OF POSTAL TELEGRAPH SYSTEM, ORDER NO. 2904 (Mar. 19, 1919), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 84, 85.

284. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., REPORT OF THE POSTMASTER GENERAL ON THE SUPERVISION AND OPERATION OF THE TELEGRAPH, TELEPHONE, AND CABLE PROPERTIES (Oct. 31, 1919), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 10.

national system of telegraphs and telephones, provided such a system were brought under an efficient and intelligent management.”²⁸⁵ Based in part on the “[i]nterchange in the use of wires,” such a system was “further illustrated by the steps taken for the consolidation of competing properties.”²⁸⁶

In this regard, Burleson’s vision of the telephone network was remarkably similar to Vail’s.²⁸⁷ Both clearly thought that the telephone system should consist of a single system under unitary control. During the government takeover, Burleson had the opportunity to put that vision into practice, not merely through gradual consolidation of the industry, but through executive fiat.

2. *Labor Unrest.*—Despite (or perhaps due to) his best efforts, Burleson never shook the labor troubles that he inherited when the Post Office took over the wires. Even before taking over the wires, Burleson’s testimony before the House Committee on Interstate and Foreign Commerce had already put him on record as stating his belief that if the government were to take over the telegraph and telephone systems, their employees “should not be affiliated with any outside organization; that their sole allegiance and loyalty should be to the Government, and that no outside organization should have a voice in shaping their action.”²⁸⁸ Apparently Burleson thought that “outside organizations” included unions.²⁸⁹

The mutual dislike between Burleson and the labor movement served as the backdrop for Burleson’s attempts to accommodate the wage demands of the telephone and telegraph operators. In an attempt to buy some time, Burleson appointed a committee on September 14, 1918, to “investigate the working conditions of and wages paid to employees of the telegraph and telephone companies, and report as to what improvements, if any, should be made in the working conditions, the wages which should be paid the various classes of employees, and the feasibility of standardizing the same.”²⁹⁰ The committee consisted of Union N. Bethell of AT&T; F.B. MacKinnon of the United States Independent Telephone Association; William S. Ryan, Assistant Superintendent, Division of Post Office Service; John B. Colpoys, Special Agent of the Department of Labor, and Julia S. O’Connor, “representing the organized telephone workers of the country.”²⁹¹

285. *Id.* at 11.

286. *Id.*

287. *See supra* subpart I(E).

288. *1918 House Hearings, supra* note 197, at 41.

289. *Quotes Burleson as Opposing Union: Head of Western Union Says Government Would Not Permit Workers to Organize*, N.Y. TIMES, July 5, 1918, <http://query.nytimes.com/gst/abstract.html?res=FA0611F83C5A11738DDDAC0894DF405B888DF1D3>.

290. OFFICE OF INFO., POST OFFICE DEP’T, ORDER 2005 (Sept. 14, 1918), ASB, Box 21.

291. *Id.* O’Connor’s title was not mentioned in the initial report announcing the committee, but she was reported to be President of the Boston Local 1A of the Telephone Operators’ Division of the International Brotherhood of Electrical Workers in June, 1919. *Congress Moves to Return*

Shortly after the Committee's appointment, Burleson issued a bulletin attempting to dispel widespread rumors "that it is the desire of the Government that employees of the telegraph and telephone companies should join the Commercial Telegraphers' Union, the International Brotherhood of Electrical Workers, or other unions."²⁹² Burleson averred that "[t]hese representations have no foundation in fact whatever" and "the Post Office Department will not distinguish between nonunion and union employees."²⁹³

The conflict boiled over the following April, and a large strike swept portions of New England.²⁹⁴ Not surprisingly, Burleson took a hard line against the strikers. He released a statement on April 16, 1919, saying that the government could not authorize wage increases "merely upon demand from the employees. A strike on the part of employees working for the Government is not permissible."²⁹⁵ On April 19, Burleson telegraphed President Wilson to explain the situation. Seeing strikes against the government as entirely illegitimate, he wrote, "To yield means for the Government to surrender to a strike demand without an opportunity to pass on the question whether it is a just demand. . . . To do this in my opinion would be a fatal mistake and will result in multiplying and aggravating these troubles."²⁹⁶

On the actual economics involved, Burleson was convinced that settlement on the terms that the union demanded would be cost prohibitive to AT&T and the independent operators. To support his position, he telegraphed President Wilson the results of a study that he had commissioned. According to Burleson, if the union's demands in Boston were applied to all operators nationwide, "it would increase operating expenses of Bell Company alone by nearly forty million dollars and Independents by nearly twelve million dollars."²⁹⁷ Government control had not, as some advocates had hoped, quieted or resolved the labor issues in the industry. The demands and frustrations of the operators and the cost issues remained the same as when the wires were under private control. The most salient difference was simply that labor now found itself in open conflict with the government, as the owner of the system and ostensibly representing the interests of all, rather than with executives, representing the interests of

Wires, N.Y. TIMES, June 17, 1919, at 8, <http://query.nytimes.com/mem/archive-free/pdf?res=F20C1FFA3C5E157A93C5A8178DD85F4D8185F9>.

292. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 9, EMPLOYEES JOINING UNIONS, ORDER NO. 2067 (Oct. 2, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 66, 66.

293. *Id.*

294. *Telephone Strike Ties Up 5 States*, N.Y. TIMES, Apr. 16, 1919, at 1, <http://query.nytimes.com/mem/archive-free/pdf?res=FB0615FA395C1B728DDDAF0994DC405B898DF1D3>.

295. OFFICE OF INFO., POST OFFICE DEP'T (April 16, 1919), ASB, Box 23.

296. Telegram from Albert Sydney Burleson to President Woodrow Wilson 5 (Apr. 16, 1919) ASB, Box 23.

297. Telegram from Albert Sydney Burleson to Woodrow Wilson (undated, circa Apr. 19, 1919), ASB, Box 23.

shareholders. The result was one that neither labor nor the Wilson Administration had sought: continuing labor conflict in a context in which the government's interests in containing costs conflicted with the wage increases being demanded.

3. *Rate Increases.*—As noted earlier, the government takeover left Vail with the helpless feeling of being unable to control the financial health of his company. Indeed, Vail confided in Western Union President Newcomb Carlton that he feared that the government takeover would make it impossible for him to raise the capital needed to continue expanding.²⁹⁸ Carlton soothed Vail, replying, “It’s your salvation. The government will be able to raise your rates and get you new money.”²⁹⁹

Carlton’s words would turn out to be prophetic. On August 28, 1918, just four weeks after assuming control, Burleson issued Bulletin No. 5 authorizing telephone companies to begin charging installation fees, which had been one of AT&T’s longstanding goals.³⁰⁰ The size of the charge varied with the cost of service: the installation fee was \$5 when the monthly rate was \$2 or less, \$10 when the monthly rate was between \$2 and \$4, and \$15 when the monthly rate was more than \$4.³⁰¹ Burleson said that the charge was due “to the necessity for conserving labor and material.”³⁰² In his final report on running the wires, Burleson indicated that wartime shortages made it “essential that the telephone companies . . . curtail their normal expenditures for extensions and temporarily arrest the normal development of their business.”³⁰³ As such, these fees had “no reference to the cost of installation.”³⁰⁴ Instead, their “prime purpose . . . was military in character, to be justified as a war measure and not as the expression of a commercial purpose.”³⁰⁵ A few weeks after the fees were enacted, Burleson began to refer to them as “service connection charges” and provided that changes of name where no lapse of service occurs and relocations of equipment within the same premises would result in a charge of \$3.00.³⁰⁶

On November 18, Burleson concluded that the end of “the necessity for conserving labor and material” associated with the cessation of hostilities

298. OSLIN, *supra* note 16, at 278.

299. *Id.*

300. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 5, SERVICE CONNECTION CHARGES, ORDER NO. 1931 (Aug. 28, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 64, 64; *see also* AT&T CO., 1911 ANNUAL REPORT 10–11 (1912) (explaining that installations paid for by the company represent a “large expenditure” that is “a burden not only on the capital but on the net revenue of the telephone, from which other service companies are free”).

301. *Id.*

302. *Id.*

303. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., *supra* note 264, at 5, 12.

304. *Id.*

305. *Id.*

306. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 8, SERVICE CONNECTION CHARGES (Sept. 14, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 65, 65–66.

justified revising the service connection charge in line with “the average cost of the initial expense of establishing service for new subscribers.”³⁰⁷ Consequently, he reduced the charge for new installations to \$3.50.³⁰⁸ As Burleson indicated in his final report, while the initial schedule of charges “must be regarded as a war measure,” the revised schedule “rests on commercial considerations” and “a sound commercial principle” and now “must be regarded as one item in the unified and standardized system of telephone charges.”³⁰⁹

On December 13, 1918, after persistent lobbying by Vail, Burleson also authorized a 20% increase in long-distance rates effective January 21, 1919, which augmented AT&T’s revenues by roughly \$10 million.³¹⁰ He justified the rate increase in part by the abnormal economic conditions brought about by the war.³¹¹ In addition, “[t]he purpose of the new schedule of telephone toll rates is to standardize the long distance service throughout the country and to establish uniform charges.”³¹² Burleson lamented the interconnectivity problems that variations in rates had caused and cast standardization as a program to include all Americans in the telecommunications system: “Under the toll rates now established, the toll service is an intercommunity, interstate, and interregional service, available to all Americans, at all times, everywhere.”³¹³

The order raising long-distance rates also called for a fifty percent reduction between the hours of 8:30 p.m. and midnight as well as a seventy-five percent reduction in rates between midnight and 4:30 a.m.³¹⁴ The final report indicated that night rates were the application of a business principle

307. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 15, MODIFIED SERVICE CONNECTION CHARGES, ORDER NO. 2352 (Nov. 18, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 68, 68.

308. *Id.* at 69.

309. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., *supra* note 264, at 5, 13.

310. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 22, TOLL RATE SCHEDULE, ORDER NO. 2495 (Dec. 13, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 75, 77; DANIELIAN, *supra* note 17, at 256.

311. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., *supra* note 264, at 5, 14.

312. OFFICE OF INFO., POST OFFICE DEP’T (Feb. 6, 1919), ASB, Box 22.

313. *Id.* One of the other service changes was the addition of person-to-person calling that precluded charges when the particular person being called could not be located. *Id.*

314. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., *supra* note 264, at 78. This followed a similar order imposing reduced telegraphy rates for “night messages.” U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., BULL. NO. 17, TELEGRAPH RATES ON “NIGHT MESSAGES”, ORDER NO. 2354 (Nov. 18, 1918), *reprinted in* U.S. POST OFFICE, *supra* note 235, at 70, 70. The night message would be transmitted to a receiving station which would transcribe the message and then place the message in the regular mail. Burleson explained the importance of this service: “A very great increase of traffic between distant points is expected to result from this low rate. A letter may take four or five days with no alternative but the payment of one dollar. This gives the alternative of one-half dollar service, and brings together the distant parts of the country about three days closer together.” OFFICE OF INFO., POST OFFICE DEP’T (Nov. 19, 1918), ASB, Box 22.

developed in the context of the telegraph that was both “simple and of universal recognition”³¹⁵:

It recognizes the fact that the facilities of any industry must provide for carrying the maximum business load, and that if this load can be distributed over the 24 hours of each day, a larger amount of business can be carried on with relatively less investment than if the business done is crowded into relatively few hours of each day.³¹⁶

In short, Burleson recognized that telecommunications networks must be sized according to the peaks in traffic and engaged in an early example of traffic shaping through peak-load pricing in an attempt to increase the efficiency of the network and to reduce the cost of service.

On March 19, 1919, Burleson also approved an increase in local rates recommended by the operating board.³¹⁷ Together these rate increases totaled roughly \$50 million.³¹⁸ Unsurprisingly, these rate increases were quite unpopular with consumers. In April, Burleson sought to address criticisms by releasing data showing that the proposed rate increase was more modest than the overall rate of wartime inflation:

The increase of 20% in telegraph rates should be considered in comparison with the 100% increase in other prices, and it is less than that found necessary to add to the railroad freight rates and is no greater than has been made generally in other public utility rates, in order to obviate financial collapse.³¹⁹

Burleson further explained that despite being required to carry unprofitable business, e.g., government communications, the Post Office had not been able to reduce the price paid for the materials involved.³²⁰ The problem also included the expansion of the system into rural underserved areas. As Burleson explained:

The extension of the telegraph service into fields that are less profitable than are the great business centers, and the handling of Government business claimed by both companies to be at a loss of 50% of the operating cost, are a charge upon the gross revenues which is escaped by a company which avoids the rendering of this necessary public service.³²¹

These rate increases engendered public anger, as one of the primary rationales for government ownership had been that the absence of desire for

315. U.S. POST OFFICE, OFFICE OF POSTMASTER GEN., *supra* note 264, at 5, 14.

316. *Id.* at 14.

317. Letter from Albert Burleson, Postmaster Gen., to U. N. Bethell, Chairman, U.S. Telegraph and Telephone Administration’s Operating Board (Mar. 19, 1919), *quoted in* DANIELIAN, *supra* note 17, at 258.

318. DANIELIAN, *supra* note 17, at 260.

319. OFFICE OF INFO., POST OFFICE DEP’T 1 (Apr. 12, 1919), ASB, Box 23.

320. *Id.* at 2.

321. *Id.* at 1.

profit would lead to lower rates.³²² Burleson's decision to increase local rates also antagonized state regulatory agencies, which successfully obtained injunctions against \$16 million of the rate increases in ten states across the country.³²³ The Supreme Court overturned these injunctions in *Dakota Central Telephone Co. v. South Dakota*,³²⁴ which was argued on May 5–6, 1919, and decided on June 2, 1919.³²⁵ Writing for an 8–1 majority, Justice White held that the war power was complete and sufficient to uphold Congress's decision to take over a public utility.³²⁶ Moreover, the state police power did not require that the judiciary carve out realms of state prerogative.³²⁷ In other words, Congress's authority over the telecommunications system under the War Power was complete and included the ability to set rates for intrastate services.³²⁸

Despite the rate increases, the telephone system still operated at a substantial loss, which under the terms of the agreement the government had to make good.³²⁹ As such, the government owed AT&T a deficiency payment of \$13 million, although AT&T forgave \$4 million of it "to facilitate prompt and economical settlement."³³⁰ The Treasury allocated an additional \$4 million to compensate the independents.³³¹

C. *Returning the Wires*

On December 13, 1918, Chairman John Moon (D-Tenn.) of the House Committee on the Post Office and Post Roads introduced a proposal directing the Postmaster General "to negotiate contracts for the purchase of any or all telephone lines . . . subject to the approval of Congress."³³² The House Committee on the Post Office and Post Roads reviewed the bill in January 1919 in a series of hearings.³³³ On January 29, the Committee issued a report entitled "Extension of Government Control of Telegraph and Telephones."³³⁴ While the report indicated that "many of the committee desired a longer time

322. COHEN, *supra* note 15, at 38.

323. DANIELIAN, *supra* note 17, at 260–62.

324. 250 U.S. 163 (1919).

325. *Id.* at 163.

326. *Id.* at 183. Justice Brandeis dissented without opinion. *Id.* at 188.

327. *Id.* at 185–87.

328. *Id.* at 187.

329. DANIELIAN, *supra* note 17, at 268.

330. *Id.* (citation omitted).

331. *See id.* at 268–69 (noting that the bill to the Treasury totaled just over \$13 million after totaling the \$9 million paid to AT&T and the payments due to telegraph and independent telephone companies).

332. H.R.J. Res. 368, 65th Cong. (1918), reprinted in *Government Control of the Telegraph and Telephone Systems: Hearings on H.R.J. Res. 368 Before the H. Comm. on the Post Office and Post Roads*, 65th Cong., pt. 1, at 3 (1919).

333. *Government Control of the Telegraph and Telephone Systems: Hearings on H.R.J. Res. 368 Before the H. Comm. on the Post Office and Post Roads*, 65th Cong., pts. I–III (1919).

334. H.R. REP. NO. 65-1012 (3d Sess. 1919).

for extension of Government control of telegraph and telephone lines, the majority are of the opinion that the lines should be returned to the owners on December 31, 1919.”³³⁵

On May 19, Vail and the President of the United States Independent Telephone Association sent a letter to Congress requesting the return of their telephone properties.³³⁶ The Senate Committee on Interstate Commerce conducted hearings on May 29,³³⁷ while the House Committee on Interstate and Foreign Commerce conducted hearings on May 30–31 and June 4–5.³³⁸

By this time, government ownership had lost many of its key constituencies. The Supreme Court had just handed down its decision upholding the local rate increase on June 2, much to the dismay of the state regulatory commissions and consumers.³³⁹ Labor tensions were brewing that would culminate in the second telegraph operators’ strike on June 11, and the unions were frustrated by the fact that government ownership appeared to hurt their bargaining position.³⁴⁰ The armistice had been in place for over half a year, and the negotiations that would culminate in the June 28 signing of the Treaty of Versailles were approaching their conclusion.³⁴¹ The change in the political winds is well illustrated by the titles of the hearings. Unlike the January hearings, which referred to “Extension of Government Control,” the hearings of late May and early June spoke of the “Relinquishment” and the “Return” of the telephone system.³⁴²

After the war, the public emergency rationale for government ownership of the wires ceased. Public hostility to the rate increases and labor strife had dogged the period of government control.³⁴³ Government operation continued to be dogged by accusations of widespread censorship.³⁴⁴ In this context, Congress held hearings before the House Committee on Interstate and Foreign Commerce on whether to return the wires in June 1919.³⁴⁵ The

335. *Id.* at 5.

336. Letter from T. N. Vail, President, Am. Tel. & Tel. Co., & G. W. Robinson, President, U.S. Indep. Tel. Ass’n, to Congress (May 19, 1919), reprinted in DANIELIAN, *supra* note 17, at 266.

337. *Relinquishment of Government Control of Telephone and Telegraph Lines: Hearings Before the S. Comm. on Interstate Commerce*, 66th Cong. (1919).

338. *Return of the Wire Systems Hearings*, *supra* note 202.

339. *N. Pac. Ry. Co. v. North Dakota*, 250 U.S. 135, 151–52 (1919).

340. See STEPHEN H. NORWOOD, LABOR’S FLAMING YOUTH: TELEPHONE OPERATORS AND WORKER MILITANCY, 1827–1923, at 200–01, 207–08 (1990) (describing a strike called by the Commercial Telegraphers’ Union of America during a large-scale strike of telephone operators and noting that government ownership benefited management).

341. See RODNEY P. CARLISLE, WORLD WAR I 289–90 (2007) (chronicling the negotiation of the Treaty of Versailles from the armistice to the signing of the treaty).

342. *Relinquishment of Government Control of Telephone and Telegraph Lines: Hearings Before the S. Comm. on Interstate Commerce*, 66th Cong. (1919); *Return of the Wire Systems: Hearings Before the H. Comm. on Interstate and Foreign Commerce on H.R. 421*, 66th Cong. (1919).

343. DANIELIAN, *supra* note 17, at 267; NORWOOD, *supra* note 340, at 157–58.

344. Douglas, *supra* note 94, at 283.

345. *Return of the Wire Systems Hearings*, *supra* note 202; DANIELIAN, *supra* note 10, at 267.

companies launched a full-fledged lobbying effort to convince Congress to relinquish control.³⁴⁶ Burleson fought in vain to hold back the tide. He wanted the wires to stay under government control, although “at lower rates.”³⁴⁷

Representative John J. Esch (R-Wis.) presided over the hearings, and they began with consideration of a written statement by Burleson.³⁴⁸ Burleson argued that private control would not solve the basic problem that the government had faced during the war: increased costs of materials and labor. He wrote, “The extraordinary increased cost of operation and maintenance which has been fastened on [the telephone and telegraph operators] as a result of the war will continue for some time after control passes from the Government.”³⁴⁹ Burleson remained adamant that “the various systems should be coordinated as to operation.”³⁵⁰ Monopoly was not necessary to maximize efficiency, but consolidation was necessary to avoid “wasteful competition and the economic loss occasioned by duplication of plant and force.”³⁵¹ In order to facilitate this consolidation, Burleson recommended that Congress enact a law allowing any telecommunications company to “purchase the property of any telegraph or telephone company, or any part thereof, or consolidate with any other telegraph or telephone company, or pool its traffic and facilities with any other telegraph or telephone company,” subject to the approval of the ICC.³⁵² Burleson recognized that if government ownership was going to end, then the best that he could hope for was that Congress would encourage consolidation of the industry via relaxation of the antitrust regulatory scheme.

State regulators did not necessarily share Burleson’s belief in consolidation. For instance, Carl D. Jackson, chairman of the Railroad Commission of Wisconsin, which oversaw telecommunications in the state, testified that Congress simply needed to return the wires to private control, rather than encouraging consolidation via additional legislation.³⁵³ Jackson explained that the problem of duplication, and attendant waste, was nonexistent in his state because Wisconsin prohibited duplication and required interconnection.³⁵⁴ Although Wisconsin had approximately one thousand independent operators and diverse rates, costs were low and the

346. DANIELIAN, *supra* note 17, at 266–68.

347. *Id.* at 269–70.

348. *Return of the Wire Systems Hearings*, *supra* note 210, at 5–9 (statement of A.S. Burleson, Postmaster General).

349. *Id.* at 6.

350. *Id.*

351. *Id.*

352. *Id.*

353. *Id.* at 10, 12 (statement of Carl D. Jackson, Chairman, Railroad Commission of Wisconsin).

354. *Id.* at 10.

technology in use was adequate to cover present needs.³⁵⁵ He disagreed with Burleson's belief in uniform rates, stating that urban service cost more than rural service due to the increased need for central stations in dense areas.³⁵⁶ Jackson explained that in a city like Milwaukee, density actually drove up costs because of the expenses related to operating central stations.³⁵⁷ If Wisconsin moved to a uniform rate, then it could unfairly hurt rural customers.³⁵⁸ Jackson declared, "Such a thing as a uniform postage-stamp rate for telephone service throughout the United States is unthinkable."³⁵⁹ And, on the general question of return of the wires, Jackson was clearly in favor of the resumption of private control.³⁶⁰

Also at issue in the hearings was why the rates had gone up during the war. There were lingering suspicions that nationalization, in and of itself, had driven up costs.³⁶¹ Nathan Kingsbury, Vice President of AT&T, took a different approach and testified that costs had skyrocketed during the war years for three reasons.³⁶² First, wages had increased approximately 50% during the war years, AT&T's payroll rising from \$110 million in 1915 to \$175 million in 1919.³⁶³ Second, the price of copper had increased by 100% in 1917 over the cost in 1914, although it had dropped some in the most recent years.³⁶⁴ The cost of lead-covered cable increased 45%, the cost of in-house manufactured goods increased 25%, and the cost of purchased manufactured goods increased 75%.³⁶⁵ Third, the cost of capital had also increased. Prewar, capital was relatively cheap and AT&T's credit was good; during the war, interest rates for AT&T had risen 2%, with capital only being available at close to 7%.³⁶⁶ Kingsbury explained that this was a particular hardship on telephone companies because they had constant need for new capital. He stated, "You have got to keep on building all the time every day."³⁶⁷ Every new phone required, on average, a \$150 capital investment, and AT&T installed 168,000 new phones in the first quarter of

355. *Id.* at 10–11.

356. *Id.* at 12.

357. *Id.*

358. *Id.*

359. *Id.*

360. *Id.* at 11 ("We certainly are against any further control of the companies by the Federal Government. We see no benefit to be derived from it, and we ask that they be returned to private ownership . . .").

361. *See id.* at 45 (question from Rep. Alben Barkley to Nathan Kingsbury, Vice President, AT&T) (asking whether increases in costs were larger under government control than they would have been under private control).

362. *Id.* at 15.

363. *Id.* at 16.

364. *Id.*

365. *Id.*

366. *Id.* at 16–17.

367. *Id.* at 16.

1919.³⁶⁸ Considering the entire situation, Kingsbury explained, “Up to the time we went to war in 1917 it had been possible to get along without large increases in revenue” via increases in efficiency.³⁶⁹ Now, AT&T needed rate increases to keep up with rising costs.³⁷⁰

Considering the effect of government control during the war, Kingsbury stated that Burleson had not interfered in the operations of AT&T.³⁷¹ Nationalization caused a small loss of morale and increased pressure on wages.³⁷² Recasting the rationale for Burleson’s connection charge, Kingsbury stated that rather than it being a subsidy for rural development, “the principal purpose” of the charge was to depress demand during the war years given the material shortages.³⁷³ Kingsbury’s explanation of why the government lost money during the takeover was simply “[b]ecause it could not get the rates up as soon as the expenses went up.”³⁷⁴ Pressed on this point by Congressman Edward L. Hamilton (R-Mich.), Kingsbury reiterated that the failure of the rates to adjust quickly to increased costs during the war was “the whole story” of why the government lost money.³⁷⁵

F.B. MacKinnon, vice president of the U.S. Independent Telephone Association, also believed that the wires should be returned, and he agreed with Kingsbury on the need for remedial legislation.³⁷⁶ MacKinnon, like Kingsbury, blamed any deterioration of service on war shortages.³⁷⁷ Specifically, he blamed the “general labor conditions, scarcity of labor, and inability to hold operators.”³⁷⁸

Joseph P. Hayes, National President of the Association of Western Union Employees, also encouraged Congress to return the wires.³⁷⁹ The unions resented that they had lost ground on wages during Burleson’s tenure, and they sought to return the wires to private control so that they could better

368. *Id.*

369. *Id.* at 17.

370. *Id.* at 17–18.

371. *Id.* at 21.

372. *Id.* at 23, 36.

373. *Id.* at 19.

374. *Id.* at 46.

375. *Id.* The entire dialogue between Kingsbury and Hamilton is worth reproducing:

Mr. HAMILTON. In brief, what are the prime reasons why the Government has lost money on the operation of the lines?

Mr. KINGSBURY. Because it could not get the rates up as soon as the expenses went up.

Mr. HAMILTON. That is the whole story?

Mr. KINGSBURY. That is the whole story practically, and that is going to be the reason. If these properties are turned back to us without some legislation, we will not be able to get those rates up in time to prevent very serious loss and financial embarrassment on the part of these companies, which is going right down to our stockholders.

Id.

376. *Id.* at 112.

377. *Id.* at 120.

378. *Id.*

379. *Id.* at 73–74.

pressure the companies for wage increases.³⁸⁰ Hayes reported that his members were eager to end government control, stating, “I find that our people, the workers, as a whole throughout the country, unlike the railroad workers, are very much committed to private control.”³⁸¹

John C. Koons, First Assistant Postmaster General, represented the Administration at the end of the hearings.³⁸² Koons stated that he was not opposed to the return of the wires, and he recognized the need for some remedial legislation.³⁸³ Koons sought to deflect blame for the perceived deterioration in service during the takeover. He stated that service had suffered because the telephone companies “had released thousands of people for service in the Army. Hundreds of their very best men were in the Army.”³⁸⁴ Seeking to counter Kingsbury’s explanation of the connection charge, Koons said that the primary rationale was to take the burden of installations off of those that did not change lines.³⁸⁵ Koons said that some businesses moved frequently, and thus steady subscribers subsidized those moves.³⁸⁶ He explained, “So we fixed an installation charge in order to take the burden off of the subscribers who did not make changes and ought not to be made to bear the cost, and also in order to reduce the demand for extensions and installations. We had to do it.”³⁸⁷

Rounding out the hearing was the statement of J.A. Pratt, representing the United Telephone Company of the State of Wisconsin and the Wisconsin State Telephone Association.³⁸⁸ Pratt decried the takeover, and was blunt about its effect, “I do not believe anything in the last 12 years of the history of regulation in the State of Wisconsin has done more to weaken in the minds of the people of that State the theory of regulation than the acts of the Post Office Department.”³⁸⁹ For Pratt, the takeover had eroded citizen confidence not just in publicly owned telecommunications, but also in regulation generally.

380. *See id.* at 74–75 (stating that Sunday pay had been reduced from time-and-a-half basis to straight-time basis, that maximum pay increases had been reduced from 15% to 10%, and that the union “[felt] that the company ha[d] shown an inclination to deal with us . . . squarely and fairly”).

381. *Id.* at 74.

382. *Id.* at 183.

383. *Id.* at 183–84.

384. *Id.* at 199.

385. *Id.* at 209.

386. *Id.*

387. *Id.* Koons’s explanation is not mutually exclusive with Kingsbury’s. Both could be correct: the connection charge could have been both a deterrent to new service requests and a reduction of the subsidy for businesses that frequently changed lines. In the hearings, however, the political question was what would be the public rationale for the charge. Kingsbury was willing to bluntly state that it was to deter new requests, while Koons wanted to portray it as a fair allocation of costs. When Kingsbury was pressed on why, if material were so short, AT&T did not just cease installations, he responded, “Telephone companies can not go out of business,” meaning that they could not afford to go out of the business of new installations. *Id.* at 20.

388. *Id.* at 219.

389. *Id.*

Considering the hearings as a whole, the voices for retaining government control were few.³⁹⁰ AT&T, the independent operators, the state regulators, and the operators' unions all wanted the wires returned to private control. AT&T wanted to return to its business plan, which included continued expansion and gradual rate increases approved by state commissions.³⁹¹ Federal control chafed the independent operators, and they too, like AT&T, wanted to get back to their prewar business plans.³⁹² The state regulators had been stripped of their power to set rates while the wires were under government control by the just announced *Dakota Central* decision on June 2, 1919.³⁹³ Not surprisingly, they yearned for the prewar system in which they exercised influence by setting state-by-state rates.³⁹⁴ The unions, having been stymied by Burleson and the issues surrounding striking against the government during the war, also sought return to private control.³⁹⁵ All that stood on the other side was a diffuse set of ideas about the inefficiencies of a competitive and private decentralized system. Burleson, overwhelmed by the negative impression of his tenure, could not hold onto the wires.

On June 4, the Senate Committee issued a report entitled "Return of Telephone, Telegraph, and Cable Lines" that proposed setting the outer limit of the return of the wires at sixty days after the bill's enactment.³⁹⁶ On June 16, the House Committee issued a report entitled "To Repeal the Telephone and Telegraph Act" that would require the restoration of the wires at midnight on the last day of the calendar month the bill was signed into law.³⁹⁷ Both chambers adopted the House's language on June 27,³⁹⁸ and the President signed the legislation into law on July 11.³⁹⁹ Per the terms of the statute, the telephone system left government control at midnight on

390. Considering what would have happened to AT&T had the government not nationalized the wire, Kingsbury stated, "If the companies had continued to be managed by their owners, we would have been diligently at work during all that time on these rate matters." *Id.* at 152.

391. *See id.* at 18 (statement of Nathan Kingsbury, Vice President, AT&T) (discussing AT&T's plans for expansion and rate increases prior to government take over).

392. *See, e.g., id.* at 10 (stating that independent operators in Wisconsin see "nothing relating to Government control since the Government has taken possession of the telephone companies which has appealed to the patrons of the telephone companies").

393. *Dakota Cent. Tel. Co. v. South Dakota*, 250 U.S. 163 (1919).

394. Charles M. Elmquist, President and General Solicitor of the National Association of Railway and Utility Commissioners, testified during the congressional hearing on returning the wires that state commissions set rates in forty-five states at that time. *Return of the Wire Systems Hearings*, *supra* note 202, at 163.

395. *See id.* at 74 (statement of Joseph P. Hayes, National President, Association of Western Union Employees) ("I find that our people, the workers, as a whole throughout the country, unlike the railroad workers, are very much committed to private control.").

396. S. REP. NO. 66-4, at 1 (1919).

397. H.R. REP. NO. 66-45, at 2 (1919).

398. 58 CONG. REC. 1906-07, 1924-25 (1919).

399. Act of July 11, 1919, ch. 10, 41 Stat. 157.

July 31.⁴⁰⁰ The act provided that the rate increases that Burleson had approved would continue in force for up to four months.⁴⁰¹

In the end, a number of factors brought the nation's experiment with a publicly owned telephone system to an end. As an initial matter, assurances that the initial proposal was only temporary placed a natural limit on the prospects for extending the period of government ownership. Indeed, Burleson continued to be dogged by accusations of trying to make the arrangement permanent.⁴⁰² The rate hikes that Burleson had authorized were intensely unpopular. Representative Aswell, the sponsor of the original legislation, said, "I owe it to my people and to Congress to apologize for my resolution if government control means increase in rates."⁴⁰³ Burleson's decisions had alienated key constituencies, such as the labor unions and the state regulatory authorities, not to mention the consumers that had hoped for less expensive service.⁴⁰⁴ And both legislators and the public had the strong sense that the network had been poorly run by the government.⁴⁰⁵

After signing the order returning the wires to private control,⁴⁰⁶ Burleson wrote a personal letter of thanks to Theodore Vail, then Chairman of the Board of Directors of AT&T.⁴⁰⁷ Reflecting on this period, Burleson wrote "to express [his] heartfelt appreciation" for Vail's assistance.⁴⁰⁸ Burleson praised Vail's unselfishness, and hoped that the future of the wire service would involve "the same successful control and direction" which it had received under Vail's administration.⁴⁰⁹ Wishing Vail "many years of health and happiness," Burleson signed off, "[y]our sincere friend," and an exceptional experiment in American telecommunications came to an end.⁴¹⁰

AT&T emerged from this period in decent shape. Rates were raised and standardized.⁴¹¹ The state regulatory commissions had been prevented from

400. *Id.*

401. *Id.*

402. *See* 58 CONG. REC. 1347 (1919) (reporting debate over the government's authority to control the wire systems and change rates).

403. *The First Step*, TELEPHONY, Apr. 19, 1919, at 11.

404. *E.g.*, *Burleson Rapped on All Sides*, FOURTH EST., May 10, 1919, at 15, 15-16; Kenneth N. Bickers, *Transformations in the Governance of the American Telecommunications Industry*, in GOVERNANCE OF THE AMERICAN ECONOMY 77, 90 (John L. Campbell et al. eds., 1991); JOHN, *supra* note 17, at 403; MAY, *supra* note 17, at 50.

405. *See, e.g.*, 58 CONG. REC. 1347 (1919) (decrying the inefficiency of the wire systems under government control); *Representative Aswell Apologizes*, 43 AM. ECONOMIST 235, 235 (1919) (attacking the government's "experiment[ing] at the expense of the public" by seizing the wires and reporting widespread opposition to the same).

406. OFFICE OF INFO., POST OFFICE DEP'T, ORDER 3380 (July 30, 1919), ASB, Box 24.

407. Letter from Albert Sydney Burleson to Theodore N. Vail, AT&T (July 30, 1919), ASB, Box 24.

408. *Id.*

409. *Id.*

410. *Id.*

411. BROOKS, *supra* note 16, at 158-59.

blocking national rate increases.⁴¹² New universal service charges were added that subsidized development, and AT&T was permitted to retain its long-desired service connection charge despite the fact that it was justified as a war measure.⁴¹³ The unpopularity of the rate hikes and the labor troubles blunted calls for nationalization.⁴¹⁴ The Republican Party platform of 1920 was able to crow that we “took from the incompetent Democratic administration the administration of the telegraph and telephone lines of the country and returned them to private ownership.”⁴¹⁵ Proposals to revive government ownership of the telephone system would continue to appear throughout the 1920s, but none were able to garner any substantial support.⁴¹⁶ Indeed, the nation’s unhappy experience with government control of the telephone system is widely regarded as the death knell for calls for government ownership of telecommunications.⁴¹⁷

III. Implications of the Government Takeover

The government takeover yields new insight into several key questions of telecommunications policy. First, it provides a new view of the reasons that the telephone network collapsed into a monopoly. Second, it provides a new perspective on the origins of universal service. Third, it adds a new twist to the development of state–federal relations. Fourth, it sheds new light on the proper scope of government intervention by identifying characteristics that are well and poorly suited to governmental control.

A. *The Reemergence of Monopoly*

One of the historical puzzles concerning the early telephone industry is how AT&T was able to reestablish its monopoly. By 1907, AT&T’s market share had dropped below 50%.⁴¹⁸ And yet, the Bell System’s market share had reached 80% by 1934.⁴¹⁹ Commentators typically attribute the

412. Bickers, *supra* note 404, at 90–91.

413. BROOKS, *supra* note 16, at 157–58.

414. *See id.* at 158 (discussing opposition to nationalization); COHEN, *supra* note 15, at 38 (noting opposition to rate increases brought about by nationalization); Bickers, *supra* note 17, at 152–54 (explaining why labor troubles in part made lowering rates infeasible and detailing objections to these rate increases).

415. Republican Platform of 1920, *in* NATIONAL PARTY PLATFORMS 1840–1972, *supra* note 41, at 232.

416. Cox & Byrnes, *supra* note 15, at 30 n.39.

417. JOHN, *supra* note 17, at 405 (“The failure of ‘postalization’ legitimated the ownership and operation of the telephone, telegraph, and cable by private corporations that would become a hallmark of managerial capitalism and a defining feature of the twentieth-century American political economy. Never again in the twentieth century would government ownership of the telephone and the telegraph occupy so prominent a place on the national political agenda.”); MAY, *supra* note 17, at 54 (calling “the most lasting effect” of the takeover “was to discredit the principle of state socialism”).

418. COHEN, *supra* note 15, at 27.

419. BROCK, *supra* note 15, at 177.

reestablishment of monopoly to one of two causes. First, they suggest that the presence of scale economies or network economic effects rendered telephony a natural monopoly.⁴²⁰ Second, they argue that the reemergence of monopoly is the result of the unwillingness of antitrust authorities to curb Theodore Vail's ambitions.⁴²¹ A close look at the history of the government takeover and the data that it generated reveals that neither factor was decisive. Instead, industry consolidation was directly influenced by deliberate government policy.

1. Natural Monopoly.—One possible explanation for the reemergence of Bell dominance is that the telephone network is a natural monopoly. Indeed, many distinguished observers regard this as uncontroversial.⁴²² Natural monopoly is believed to be the result of the supply-side scale economies associated with constantly declining costs or the demand-side scale economies associated with network economic effects. The circumstances surrounding the takeover make clear that neither provides a convincing explanation.

a. Scale Economies.—The most frequently cited explanation for the reemergence of monopoly is the economies of scale associated with high fixed costs.⁴²³ The presence of unexhausted economies of scale causes unit costs to decline as volume increases.⁴²⁴ When average costs decline, the firm with the largest volume can underprice its rivals, which causes it to take even more share of the market. If the economies of scale remain unexhausted, markets that begin as competitive will collapse into natural monopolies.

A revisionist history has emerged pointing out that telephone service was not a declining cost industry. In particular, when switching was performed manually by operators sitting at a switchboard, it did not scale.⁴²⁵ The deployment of mechanical switches would eventually change this limitation, but AT&T did not begin deploying mechanical switches until the

420. Weiman & Levin, *supra* note 142, at 104.

421. See BROOKS, *supra* note 16, at 143–45 (discussing Vail's view of regulation and the government's initial nonregulation of telephone rates).

422. See, e.g., FAULHABER, *supra* note 6, at 107 (“Indeed, until the late 1960s few questioned that the telephone industry was a natural monopoly.”); HUBER ET AL., *supra* note 6, at 86 (“Is the telephone industry (or any part of it) a natural monopoly? Until the 1960s, the answer was generally presumed to be yes, from end to end.”); 3B PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶787c, at 366 (3d ed. 2008) (“Until the 1960s or 1970s long distance telephone connections between local exchanges in the United States were considered as much a natural monopoly as the local exchanges themselves.”).

423. Cf. BROOKS, *supra* note 16, at 133–34 (outlining how AT&T's economies of scale advantage allowed it to buy up competitors and work towards a monopoly); JEFFREY CHURCH & ROGER WARE, INDUSTRIAL ORGANIZATION 55 (2000) (identifying long-run fixed costs as a source of economies of scale).

424. CHURCH & WARE, *supra* note 423, at 54.

425. Milton Mueller, *The Switchboard Problem: Scale, Signaling, and Organization in Manual Telephone Switching, 1877–1897*, 30 TECH. & CULTURE 534, 559 (1989).

1920s.⁴²⁶ Both AT&T and its competitors found a need to request rate increases as their operations grew.⁴²⁷

Interestingly, contemporary observers recognized the absence of scale economies in the telephone industry.⁴²⁸ Indeed, Nathan Kingsbury made precisely this point in his testimony regarding the return of the wire systems. Kingsbury stated that installation cost more in the cities than in the rural areas because of the need for additional central switching stations.⁴²⁹ Each central station could only take about 10,000 lines, and as a city grew, AT&T was forced to install new central stations, with new trunk lines between those stations.⁴³⁰ Trunk lines were exceedingly expensive.⁴³¹ Moreover, as the central stations grew in a city, the company was required to employ additional inter-operator connectors.⁴³² While automatic switches could overcome some of these issues, the costs of installing new trunk lines between new central stations could not be ameliorated.⁴³³ Summing up this situation, Kingsbury stated, “The profit per unit decreases as the number of units increases.”⁴³⁴

Interestingly, the takeover provided data in which the diseconomies of scale were apparent. In 1916, the government collected data on the operations of telephone systems,⁴³⁵ apparently to assist it with the management of these companies.⁴³⁶ Plotting cost per telephone against the

426. *E.g.*, H.R. DOC. NO. 76-340, at 261 (1939); A HISTORY OF ENGINEERING AND SCIENCE IN THE BELL SYSTEM: THE EARLY YEARS (1875–1925), at 552–53, 611–12 (M.D. Fagen ed., 1975); ROBERT J. CHAPUIS, 100 YEARS OF TELEPHONE SWITCHING (1878–1978), at 249 (1982); Joan Nix & David Gabel, *The Introduction of Automatic Switching into the Bell System: Market Versus Institutional Influences*, 30 J. ECON. ISSUES 737, 738 (1996).

427. MUELLER, *supra* note 10, at 36–37; *see also* Weiman & Levin, *supra* note 142, at 104 (discussing AT&T’s growth and the increasing costs that ensued).

428. *E.g.*, J. MAURICE CLARK, STUDIES IN THE ECONOMICS OF OVERHEAD COSTS 321 (1923) (“Telephone companies . . . show no signs of economy with increased size, but rather the opposite.”).

429. MUELLER, *supra* note 10, at 41.

430. Kingsbury said, “[A]s the city grows it is necessary to install a larger and larger number of central offices because a girl’s arm is just so long, and as the manual switchboards are constructed she can only reach about 10,000 stations with her arm.” 1919 House Hearings, *supra* note 338, at 31 (statement of Nathan Kingsbury, Vice President, AT&T).

431. *Id.*

432. *Id.* at 32.

433. *See Return of the Wire Systems Hearings*, *supra* note 202, at 35 (describing technology that eliminated the 10,000-line limit but still required trunk lines).

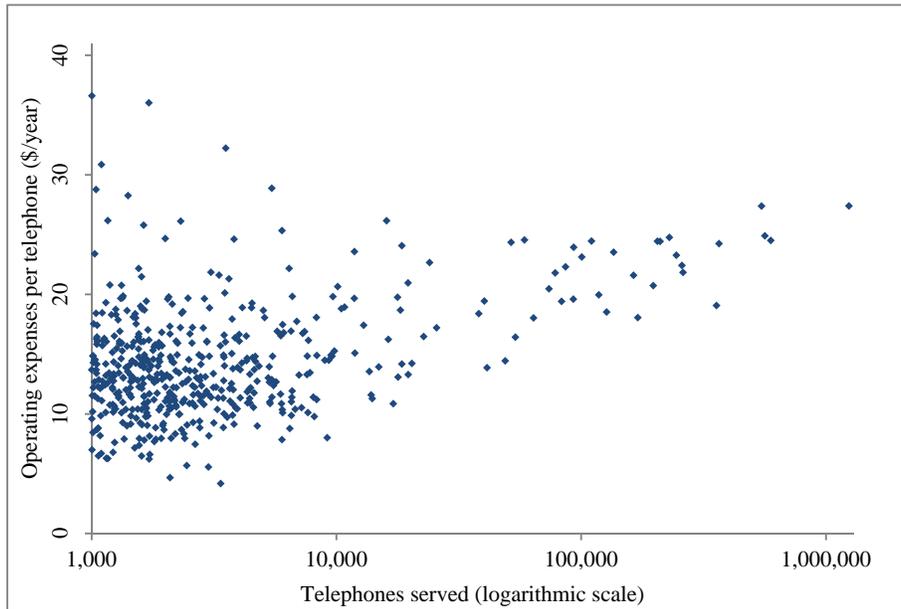
434. *Id.* at 30. “The difficulty is that the larger the number of units you serve in the telephone business, under conditions that exist requiring a larger and larger investment per unit, a larger and larger operating cost per unit, that larger investment and larger cost goes up so fast that the larger the number of units you serve, the more it costs per unit to serve them.” *Id.*

435. Memorandum from Bureau of Statistics, Interstate Commerce Comm’n on Tel. Cos. & Tel. Cos. Reporting to the Interstate Commerce Comm’n for the Calendar Year 1916 (Aug. 20, 1918) *available at* <http://archive.org/details/TelephoneAndTelegraphCompaniesReportingToTheIccFor1916>.

436. Douglas Galbi, *Early U.S. Telephone Industry Data*, GALBITHINK.ORG, <http://www.galbithink.org/telcos/early-telephone-data.htm>.

number of subscribers reveals a clear upward trend, suggesting the presence of diseconomies of scale rather than scale economies.

Figure 1. Cost Scaling Among U.S. Telephone Companies in 1916



Source: Douglas Galbi, *Dis-Economies in Communications Networks*, PURPLE MOTES (Apr. 25, 2010), <http://purplemotes.net/2010/04/25/economies-and-dis-economies-in-communications-networks/>.

Telephone companies facing increasing costs found themselves constantly having to ask municipal regulators to approve rate increases.⁴³⁷ This was particularly difficult for the independents who offered the benefits of cheaper rates as the principal reason for being allowed to enter.⁴³⁸

b. Network Economic Effects.—Dominant positions are also often attributed to another economic concept known as network economic effects. Network economic effects exist when the value of a network increases with the number of subscribers.⁴³⁹ To use a classic example, consumers during the 1980s who were choosing between the two leading videocassette recorder (VCR) formats (Sony Betamax and VHS) did not really care about their

437. MUELLER, *supra* note 10, at 66.

438. *Id.* at 37.

439. DANIEL F. SPULBER & CHRISTOPHER S. YOO, NETWORKS IN TELECOMMUNICATIONS 4 (2009).

technical capabilities.⁴⁴⁰ What determined the value is which format the majority of other VCR owners would adopt.⁴⁴¹ The telephone system is regarded as a paradigmatic example of a network that exhibits network economic effects.⁴⁴² As AT&T noted in its 1901 Annual Report:

That the system be complete and of the greatest utility, it is necessary that as many persons as possible should be connected to it as to be able to talk or be talked to by telephone. . . . [The user's] advantage as a telephone subscriber is largely measured by the number of persons with whom he may be put in communication.⁴⁴³

AT&T similarly observed in its 1908 Annual Report, "A telephone—without a connection at the other end of the line—is . . . one of the most useless things in the world. Its value depends on the connection with the other telephone—and increases with the number of connections."⁴⁴⁴

Network economic effects can give large companies a competitive advantage. The fact that larger networks are more valuable provides strong incentives for new customers to opt for the larger network.⁴⁴⁵ This in turn makes the largest network still larger, further reinforcing its competitive advantage.⁴⁴⁶ This advantage can come from having more local subscribers.⁴⁴⁷ The market leader could ensure that it alone enjoyed those advantages simply by refusing to interconnect with the other network.⁴⁴⁸

440. See Hiroshi Ohashi, *The Role of Network Effects in the US VCR Market, 1978–1986*, 12 J. ECON. & MGMT. STRATEGY 447, 449 (2003) (explaining that improvements in Beta's product quality were not enough to overcome network effects).

441. *Id.* at 448.

442. See Christopher S. Yoo, *Network Neutrality, Consumers, and Innovation*, 2008 U. CHI. LEGAL F. 179, 223 n.139 (collecting authorities).

443. Ithiel de Sola Pool et al., *Foresight and Hindsight: The Case of the Telephone*, in THE SOCIAL IMPACT OF THE TELEPHONE 127, 131 (Ithiel de Sola Pool ed., 1977) (ellipsis and alteration in original) (quoting AT&T CO., ANNUAL REPORT OF THE DIRECTORS OF AMERICAN TELEPHONE & TELEGRAPH COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1901, at 6 (1902)).

444. AT&T CO., ANNUAL REPORT OF THE DIRECTORS OF AMERICAN TELEPHONE & TELEGRAPH COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1908, at 21 (1909).

445. Howard A. Shelanski & J. Gregory Sidak, *Antitrust Divestiture in Network Industries*, 68 U. CHI. L. REV. 1, 8 (2001).

446. *Id.* at 8–9.

447. See Mark A. Lemley, *Antitrust and the Internet Standardization Problem*, 28 CONN. L. REV. 1041, 1046 n.19 (1996) (recognizing network effects in phone service and noting that phone companies were originally successful as local-only providers); MUELLER, *supra* note 10, at 72–73 (noting that demand for long-distance service was initially very low).

448. Shelanski & Sidak, *supra* note 445, at 8; see also BROOKS, *supra* note 16, at 114 (describing how Bell's policy against interconnection gave it a competitive advantage over independents). *But see* LIPARTITO, *supra* note 14, at 250 n.4 ("The notion that Bell's refusal to interconnect was a potent competitive weapon is an article of faith in telephone literature.").

Alternatively, others have suggested that greater reach made possible by AT&T's key long-distance patents made its network more desirable.⁴⁴⁹

Looking at only the national numbers, arguments that AT&T's overall size gave it a strategic advantage are hard to reconcile with the fact that in 1907, the independents controlled more subscribers than did AT&T.⁴⁵⁰ The independents could thus nullify whatever advantages AT&T enjoyed simply by interconnecting with one another.⁴⁵¹ That said, national numbers are somewhat misleading in that subscribers during the World War I era made almost exclusively local calls.⁴⁵² What mattered, then, was the percentage of customers that any particular company controlled locally, not nationally. Although AT&T continued to enjoy a strong position in the northeast and mid-Atlantic states, the independents were the market leaders in the Midwest.⁴⁵³ The independents were also stronger in small towns and rural communities that AT&T had neglected.⁴⁵⁴ In those areas, local network economic effects would have favored the independents, not AT&T.⁴⁵⁵ The fact that AT&T also lost market share in markets which it entered first further cuts against network economic effects as a source of competitive advantage.⁴⁵⁶

Moreover, it is recognized that customer heterogeneity can ameliorate network economic effects.⁴⁵⁷ If subscribers place a higher value on a small subset of people, what matters is not the total number of people who subscribe, but rather whether the people most important to that subscriber join the network.⁴⁵⁸ When this is the case, different groups can segregate into

449. BROCK, *supra* note 15, at 119; FAULHABER, *supra* note 14, at 3; John V. Langdale, *The Growth of Long-Distance Telephony in the Bell System: 1875–1907*, 4 J. HIST. GEOGRAPHY 145, 155 (1978).

450. See Langdale, *supra* note 449, at 152 (providing a breakdown of 1907 phone ownership).

451. See Roger G. Noll & Bruce M. Owen, *The Anticompetitive Uses of Regulation: United States v. AT&T*, in *THE ANTITRUST REVOLUTION* 290, 292 (John E. Kwoka, Jr. & Lawrence J. White eds., 1989) (noting that the independents were able to effectively compete by interconnecting).

452. See Robert MacDougall, *The People's Telephone: The Political Culture of Independent Telephony*, 1 BUS. & ECON. HIST. ONLINE 1, 13 (2003), www.thebhc.org/publications/BEHonline/2003/MacDougall.pdf (remarking that even as late as 1930, less than half of 1% of all telephone calls crossed state lines).

453. Jeffrey E. Cohen, *The Telephone Problem and the Road to Telephone Regulation in the United States, 1876–1917*, 3 J. POL. HIST. 42, 49 (1991).

454. *Id.* at 48.

455. MUELLER, *supra* note 10, at 59, 62.

456. Cohen, *supra* note 453, at 49.

457. See Christopher S. Yoo, *When Antitrust Met Facebook*, 19 GEO. MASON L. REV. 1147, 1151–53 (2012) (noting that increased heterogeneity can work to counterbalance certain network effects); SPULBER & YOO, *supra* note 439, at 140 (“[N]etwork externalities may be substantially mitigated if user preferences are nonuniform.”).

458. See Bob Briscoe et al., *Metcalfe's Law Is Wrong: Communications Networks Increase in Value as They Add Members—But by How Much? The Devil Is in the Details*, IEEE SPECTRUM, July 2006, at 34, 37 (pointing out that different connections within a network have different values).

different networks without any significant loss in value.⁴⁵⁹ What little loss remains can be substantially ameliorated if gateways exist between the networks.⁴⁶⁰

As Milton Mueller has pointed out, this is precisely what occurred in the early telephone network.⁴⁶¹ “Classes and neighborhoods divided themselves into user communities.”⁴⁶² When they needed to call the other network, they had easy access to bridge technologies, such as payphones or free phones maintained by drugstores and saloons to attract business.⁴⁶³ Perhaps the best evidence that network economic effects did not give AT&T any advantage in local markets is the fact that the independents expressed little interest in interconnecting with AT&T.⁴⁶⁴ Clearly, the independents did not see their inability to reach a larger number of customers as a competitive disadvantage.

All of these considerations undercut the suggestion that AT&T was able to use network economic effects in local telephone markets to restore its dominance. But what about long distance? As an initial matter, interstate long-distance calling represented a trivially small fraction of overall telephone revenues.⁴⁶⁵ As one customer noted in 1909, truly long-distance telephoning was “of little commercial or social importance.”⁴⁶⁶

459. See S.J. Liebowitz & Stephen E. Margolis, *Are Network Externalities a New Source of Market Failure?*, in 17 RESEARCH IN LAW AND ECONOMICS 1, 18–19 (Richard O. Zerbe, Jr. & William Kovacic eds., 1995) (describing two scenarios where a network increases in value not only by increasing the sheer number of users, but also by increasing the desirability of communication between those users).

460. Yoo, *supra* note 457, at 1153–54.

461. MUELLER, *supra* note 10, at 20–29.

462. *Id.* at 85; see also MacDougall, *supra* note 452, at 13 (describing the choice between AT&T’s extensive network and an independent’s intensive network was often one that divided along class lines).

463. MUELLER, *supra* note 10, at 82, 85; see also BROCK, *supra* note 15, at 110 (observing that there was often not much to be gained in the first place by connecting telephone networks with each other).

464. MUELLER, *supra* note 10, at 10, 51, 78–79; Gabel, *supra* note 138, at 353–54.

465. See MUELLER, *supra* note 10, at 72–73 & n.50 (noting that “[t]he demand for telephone connections between points over 200 miles apart was still restricted to a tiny minority of users” and citing an AT&T report from 1900 that 98% of calls placed from cities and 95% of calls placed from small towns were to points within 50 miles); MacDougall, *supra* note 462, at 13 n.46 (citing a 1905 statement by an Independent that 98% of all long-distance calls were placed to points within a one hundred-mile radius). For later statements to the same effect, see *Smith v. Ill. Bell Tel. Co.*, 282 U.S. 133, 147 (1930) (reporting that interstate calls constituted 0.5% of all telephone traffic); *Hearings on S. 6 Before the Comm’n. on Commc’ns of the H. Comm. on Interstate Commerce*, 71st Cong. 1565, 1585–86 (1930) (statement of Joseph B. Eastman, Comm’r, Interstate Commerce Comm’n) (reporting that interstate traffic represented 0.47% of all exchange calls and 0.46% of total exchange revenue and that if exchange and toll calls were combined, intrastate traffic represented 1.36% of all calls and 9.9% of revenue).

466. Gansley R. Johnson, *Telephone Combination: Would It Serve a Good Purpose?*, TELEPHONY, Jan. 2, 1909, at 5, 7.

What little long distance traffic existed tended to be regional.⁴⁶⁷ In regional long distance, AT&T enjoyed no technological advantage, as both the independents and the Bell System simply connected adjacent exchanges.⁴⁶⁸ Indeed, AT&T President Frederick Fish was forced to concede in 1903 that the company held “no controlling patents on long distance telephone apparatus or systems” and that “long distance lines of some commercial value [could] be constructed and operated by anyone.”⁴⁶⁹

Moreover, AT&T had focused most of its attention on connecting distant points.⁴⁷⁰ The skeletal pattern that resulted made AT&T weaker with respect to short-haul long distance.⁴⁷¹ The independents’ focus on intensive coverage of smaller areas put them in a stronger position.⁴⁷² In the words of the president of one independent, his company “has the near long distance points, the Bell [has] the far-off.”⁴⁷³ Between the two, it was the near-long-distance points that mattered more.⁴⁷⁴

It is thus hard to see how either scale economies or network economic effects could have been the means through which AT&T reestablished its monopoly. The answer must lie elsewhere.

2. *The Supposedly Lax Enforcement of the Antitrust Laws.*—Other commentators attribute the reemergence of monopoly to a failure of antitrust enforcement in two ways. First, some assert that government intervention occurred after AT&T had reestablished its monopoly position and that the authorities should have forced AT&T to divest its newly acquired properties.⁴⁷⁵ Second, some argue that antitrust authorities implemented the Kingsbury Commitment in a way that permitted the Bell System to continue to merge to monopoly.⁴⁷⁶ Specifically, the Commitment did not prevent AT&T from acquiring independent local telephone companies with which they did not directly compete.⁴⁷⁷ Many scholars have claimed that the

467. See MUELLER, *supra* note 10, 72–73 (noting that “[n]o more than 5 percent of all telephone calls were to points more than fifty miles away” and that “the real source of competitive advantage was comprehensive coverage of a particular region corresponding to the interest of the majority of telephone users”).

468. *Id.*

469. *Id.* at 72 n.49.

470. See *id.* at 73 (noting that prior to 1894 Bell pursued the long-distance market “to the exclusion of most others” and that “[t]he new emphasis on intensive toll line development within the licensee companies’ territories was actually a sharp departure from the old Bell vision”).

471. *Id.* at 73, 90.

472. See MacDougall, *supra* note 462, at 11–12 (arguing that AT&T “regarded its long lines as a major competitive weapon” but that “middle distance connections became a key competitive weapon for the independents”).

473. FREDERICK S. DICKSON, *TELEPHONE INVESTMENTS AND OTHERS* 41 (1905).

474. *Id.*

475. See *supra* note 162 and accompanying text.

476. See *supra* notes 163–64 and accompanying text.

477. See *supra* note 163 and accompanying text.

antitrust authorities allowed mergers of competitive companies so long as the transaction involved a swap of lines.⁴⁷⁸

Claims that the Kingsbury Commitment arrived too late are belied by the fact that the independents still controlled 45% of the national market at the time of the settlement,⁴⁷⁹ leaving AT&T's share well below the threshold needed to constitute a monopoly.⁴⁸⁰ Moreover, as noted above, regional share mattered more than national share, and in many regions, independents still enjoyed majority positions.⁴⁸¹ Had the Kingsbury Commitment simply stabilized the industry structure that existed in 1913, it would not have inevitably collapsed back into monopoly.

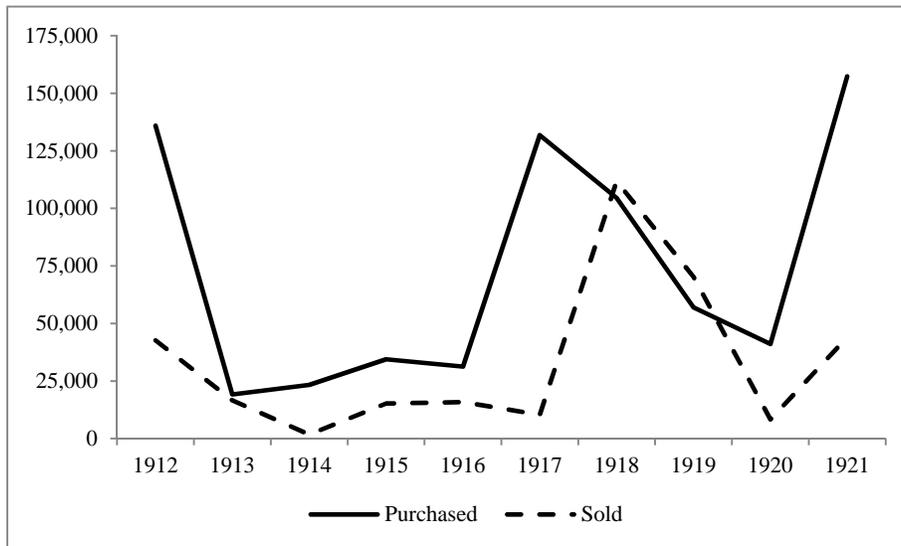
478. See *supra* note 164 and accompanying text.

479. U.S. DEP'T OF COMMERCE, HISTORICAL STATISTICS OF THE UNITED STATES: COLONIAL TIMES TO 1970 (pt. 2) 783 (Bicentennial ed. 1975); see also COHEN, *supra* note 15, at 27 (stating that AT&T's market share "dipped below 50 percent"); MUELLER, *supra* note 10, at 133 (noting that at the time of the agreement dual service remained in 13% of all communities with exchanges in the United States); Krishna P. Jayaker & Harmeet Sawhney, *Universal Service: Beyond Established Practice to Possibility Space*, 28 TELECOMM. POL'Y 339 (2004) (noting that "significant market share remained with the independents until 1921, when the Willis-Graham Act again permitted the Bell System to acquire non-affiliated companies"); Steve G. Parsons & James Bixby, *Universal Services in the United States: A Focus on Mobile Communications*, 62 FED. COMM. L.J. 119, 125 (arguing that independents maintained significant market share until 1921).

480. See *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 424 (2d Cir. 1945) (expressing doubts that 60% to 64% market share would be enough to constitute a monopoly in the aluminum market).

481. See *supra* notes 453–54, 472 and accompanying text.

Figure 2. Telephone Lines Purchased and Sold by the Bell System, 1912–1921



Source: FED. COMM'NS COMM'N, REPORT ON CONTROL OF TELEPHONE COMMUNICATIONS: CONTROL OF INDEPENDENT TELEPHONE COMPANIES 42 tbl.v (1937).

The suggestion that the Kingsbury Commitment did nothing to slow AT&T's acquisition strategy is also belied by the facts. As Figure 2 shows, the three years following the imposition of the Kingsbury Commitment saw a sharp drop in the number of lines acquired by the Bell System. Had AT&T been simply allowed to swap lines with its competitors, its acquisition numbers would have remained high and been counterbalanced by an equal number of lines acquired by the independents. Yet this is not the pattern observed following 1913. The fact that the number of lines acquired by the Bell System dropped in 1913, 1914, 1915, and 1916 suggests that the Kingsbury Commitment was effective in slowing AT&T's acquisition policy for at least three years.

3. Government-Mandated Consolidation as a Missing Consideration.—The biggest factor missing from the explanation of the reestablishment of the Bell System is the government takeover during World War I. As noted above, industry consolidation was one of Burleson's central policies during the takeover. Consequently, acquisitions spiked in 1918, only to drop off again in 1919 and 1920 after the return of the wires until the Willis-Graham Act completely abrogated antitrust review of telecommunications mergers in

1921.⁴⁸² From this explanation, monopoly was not the sole result of the antitrust authorities' refusal to curb the corporate ambitions of Theodore Vail. Instead of being asleep at the switch, the government was one of the primary drivers of the return to monopoly.

There is one aspect of the data that does not completely fit this story: the upsurge in Bell acquisitions in 1917.⁴⁸³ The impetus for this change came not from Bell, but rather from the independents. Having finished the build out of the areas that Bell had ignored, independents found that further revenue growth required going head-to-head with Bell.⁴⁸⁴ Intensive competition is much more expensive and less profitable than an extensive race for the market.⁴⁸⁵ Faced with the prospects of vigorous competition, many independents began to explore reaching some form of accommodation.

In 1915, the independents appointed a committee to explore consolidating into the Bell System.⁴⁸⁶ It was this committee that proposed complying with the spirit, if not the letter, of the Kingsbury Commitment by “permit[ting] the acquisition by the Bell System of Independent properties by means of a division of territory, so long as in such a division the Bell System should not acquire more property or territory than it relinquished.”⁴⁸⁷ This solution “would conform to the probable spirit” of the Kingsbury Commitment “by continuing the prohibition on the expansion of the Bell System at the expense of competition” while still allowing a division of territory.⁴⁸⁸ The Justice Department effectively accepted this modification in 1917.⁴⁸⁹

The critical support for the reemergence of mergers in 1917 thus came from the independents, who also provided the impetus for the Willis-Graham Act's abolition for all antitrust scrutiny of telecommunications mergers.⁴⁹⁰

482. *See supra* Figure 2.

483. *See Bickers, supra* note 17, at 126–27 (remarking on the increase in consolidations of telephone companies during this time).

484. *See MUELLER, supra* note 10, at 55–60 (discussing phases of expansion employed by independents).

485. Christopher S. Yoo, *Product Life Cycle Theory and the Maturation of the Internet*, 104 *Nw. U. L. REV.* 641, 646–47, 666–67 (2010).

486. Bickers, *supra* note 17, at 123–24.

487. Letter from H.D. Critchfield, Sales Dep't, Automatic Electric Co., to F.H. Woods 2 (May 18, 1915), *quoted in Bickers, supra* note 17, at 125.

488. *Id.* (emphasis omitted) (internal quotation marks omitted).

489. Bickers, *supra* note 17, at 126; CHARLES A. PLEASANCE, *THE SPIRIT OF INDEPENDENT TELEPHONY* 86 (1989); *see also* H.R. Doc. No. 340, 76th Cong., 1st Sess. (1939) (noting that the Kingsbury Commitment was generally understood to permit acquisition of competing telephone companies until after January 1918, when it became generally understood that it was not a violation of The Kingsbury Commitment for the Bell System to acquire competing telephone stations, if at the same time the Bell System sold an equal or comparable number of Bell-owned stations to an independent).

490. 61 *CONG. REC.* 1983 (1921) (remarks of Rep. Winslow) (“The bill was brought to the attention of the committee by . . . the so-called independent telephone companies of the United States. . . . [T]hey have represented to the committee . . . that if the opportunity to sell or

Consolidation enjoyed the support of key consumer groups who needed both services and did not want to pay for two subscriptions.⁴⁹¹ This fact makes it difficult to lay this development at the feet of Theodore Vail. The fact that both competitors and consumers endorsed the change makes it hard to characterize it as government capitulation to a monopolist, as antitrust enforcement authorities find it difficult to oppose mergers when neither competitors nor consumers object.

This was particularly so in the case of telephony, which as noted above is largely intrastate in character.⁴⁹² Because federal jurisdiction extended only to interstate matters, mergers between two local telephone companies were arguably beyond the Justice Department's jurisdictional reach.⁴⁹³ That is why on September 7, 1914, when authorizing AT&T's acquisition of a competing local telephone company in Spokane, Washington, the Justice Department announced that the Kingsbury Commitment was not meant to prevent communities from eliminating dual service if they so chose.⁴⁹⁴ Similarly, on December 7, 1914 (less than a year after the issuance of the Kingsbury Commitment), the Report of the Attorney General noted that the settlement "does not mean that where there are two telephone systems in a city or town there never can be a consolidation into a single system."⁴⁹⁵ On the contrary, it "leaves local communities generally free to have one telephone system, if they desire," so long as the resulting consolidated company maintained all previous long-distance interconnections.⁴⁹⁶ If sufficient local political support existed for the merger, the Justice Department would be hard pressed to oppose it.⁴⁹⁷

In any event, all of these dynamics were soon rendered moot by the government takeover, as Burleson condoned and accelerated the process of industry consolidation.⁴⁹⁸ The strength of the Postmaster General's convictions rendered the views of both AT&T and the independents irrelevant. Even if it was not the only factor, Burleson's relentless support

consolidate is not afforded to them they are liable to go through the condition of bankruptcy . . ."); *see also* Bickers, *supra* note 17, at 127; Gabel, *supra* note 138, at 353 ("[T]he independents joined Bell in seeking passage of the Willis-Graham Act of 1921, which permitted the merger or consolidation of competing telephone companies."); Robinson, *supra* note 14, at 8 ("[T]he independents joined AT&T in supporting a lifting of restrictions on AT&T acquisitions.").

491. COHEN, *supra* note 15, at 33; MUELLER, *supra* note 10, at 140–44; Gabel, *supra* note 138, at 348; Weiman & Levin, *supra* note 142, at 122, 124.

492. *See supra* notes 465–73 and accompanying text.

493. STONE, *supra* note 3, at 193.

494. United States v. AT&T Co., No. 6082 (D. Or. Sept. 7, 1914) (order modifying decree), *reprinted in* DECREES AND JUDGMENTS IN FEDERAL ANTI-TRUST CASES, JULY 2, 1890–JANUARY 1, 1918, at 497, 497–99 (Roger Shale ed., 1918).

495. ATT'Y GEN. ANN. REP. 14 (1914).

496. *Id.*

497. MUELLER, *supra* note 10, at 133–34.

498. STONE, *supra* note 3, at 199; VIETOR, *supra* note 16, at 172–73.

for industry consolidation has been largely overlooked as one of the reasons for AT&T's return to dominance.⁴⁹⁹

B. *The Origins of Universal Service*

A vibrant debate has emerged over the origins of universal service. The conventional wisdom argues that universal service was the result of AT&T's commitment to broad geographic coverage, exemplified by AT&T's endorsement of "'One System,' 'One Policy,' 'Universal Service.'"⁵⁰⁰ Critics of this position suggest that the concept of universal service is more modern, being the product of AT&T's attempt to justify the continuation of its monopoly when facing the emergence of competition during the 1960s and 1970s.⁵⁰¹ Richard John has offered an intriguing third interpretation, arguing that universal service represents Theodore Vail's attempt to emulate the postal system, influenced by his experience running the Railway Mail System in between his stints at AT&T.⁵⁰²

There can be no question that AT&T endorsed the idea of providing telephone service to all Americans. For example, its 1907 Annual Report intoned that the "'universality'" that was the Bell System's strength "carries with it . . . the obligation to occupy and develop the whole field," including semi-urban and rural areas as well as urban areas.⁵⁰³ Its 1910 Annual Report affirmed the company's "belie[f] that some sort of connection with the telephone system should be within the reach of all" and that the telephone network would ultimately become a medium for all electronic

499. Only a handful of works acknowledge Burleson's role, and those that do offer no more than a few words. See H.R. Doc. No. 340, 76th Cong., (1939) (devoting a single sentence to the government's conscious policy of "caus[ing] the coordination and consolidation of competing systems wherever possible"); FISCHER, *supra* note 15, at 50 (devoting a single sentence to how "the wartime experience of coordination between AT&T and the independents accelerated the unification of the industry"); HUBER ET AL., *supra* note 14, § 4.4.1, at 354 ("During World War I, from 1918 to 1919, the Postmaster General took over operation of the telephone industry and . . . directed the competing local systems to consolidate into a single national network."); MUELLER, *supra* note 10, at 133 (making a passing reference to "World War I-induced centralization"); VIETOR, *supra* note 16, at 172-73 (devoting a single sentence to how government control "ran squarely up against the Justice Department's prohibition on consolidation of competing exchanges," as Burleson "sought to eliminate competition and integrate operations wherever possible"); Peters, *supra* note 15, at 257 (noting Burleson's view that "government operation and control of the telephone system 'would undoubtedly cause the coordination and consolidation of competing systems wherever possible'").

500. AT&T CO., ANNUAL REPORT OF THE DIRECTORS OF AT&T COMPANY TO THE STOCKHOLDERS FOR THE YEAR ENDING DECEMBER 31, 1909, at 18 (1910); see Pool et al., *supra* note 444, at 131 ("[T]he goal of universality, which became one of the watchwords of the Bell system, was there from the beginning.").

501. MUELLER, *supra* note 10, at 150-52; see also ROBERT W. CRANDALL & LEONARD WAVERMAN, WHO PAYS FOR UNIVERSAL SERVICE? 6-8 (2000) (explaining that although the phrase was first used by Theodore Vail, the company "revived the notion of universal service" with a "new definition" in response to competition during the 1960s and 1970s).

502. JOHN, *supra* note 17, at 388; Richard R. John, *Theodore N. Vail and the Civic Origins of Universal Service*, 28 BUS. & ECON. HIST. 71, 76-79 (1999).

503. AT&T, *supra* note 146, at 28.

communications “from every one in every place to every one in every other place, a system as universal and as extensive as the highway system of the country which extends from every man’s door to every other man’s door.”⁵⁰⁴

Critics such as Milton Mueller have dismissed these statements as nothing more than an “oratorical jab.”⁵⁰⁵ It was not until the independents forced AT&T’s hand that the company began to live up to the promise of its earlier rhetoric.⁵⁰⁶ Instead, they regard universal service as an invention of the late 1960s and 1970s to justify the continuation of the Bell monopoly.⁵⁰⁷ The primary mechanism was to use the process of separations to allocate a higher proportion of network elements used both for local and long-distance service, such as the loop and the switch, to long-distance rates.⁵⁰⁸ The effect was to overcharge for long-distance service in order to cross subsidize local service.⁵⁰⁹ This process did not begin until the 1950s and did not reach full stride until the late 1960s and 1970s.⁵¹⁰

While it is true that long distance–local cross subsidies did not emerge until later in the history, it was only one of several cross subsidies built into telephone rates. Another key cross subsidy takes advantage of the fact that the higher density makes providing service less costly in urban areas than rural areas.⁵¹¹ Using rate averaging to impose a uniform price effectively permits rates paid by urban users to cross subsidize those paid by rural users.⁵¹²

Although these scholars are correct that the long distance–local cross subsidy did not emerge until the 1960s and 1970s, the urban–rural cross subsidy associated with rate averaging was well established in the postal service before World War I.⁵¹³ The takeover allowed this postal concept to become a staple of telephone policy as well.⁵¹⁴ In the words of one commentator:

During this period of government ownership, the decision was made to set standard long-distance rates throughout the country, based on average costs. In other words, subscribers calling from large cities would pay above costs in order to provide a subsidy to those in rural areas. So, early in the century cross-subsidization began, embraced by the industry, which rarely question the premise behind the

504. *Id.* at 23.

505. MUELLER, *supra* note 10, at 100.

506. *Id.* at 101–03.

507. *Id.* at 151–52.

508. *Id.* at 151–55.

509. *Id.* at 159.

510. *Id.* at 160–61.

511. Thierer, *supra* note 16, at 277.

512. *Id.* at 276–77.

513. JOHN, *supra* note 17, at 379; John, *supra* note 502, at 75–76.

514. 52 CONG. REC. 849 (1915) (statement of Rep. David Lewis); POSTMASTER GEN., *supra* note 26, at 10; JOHN, *supra* note 17, at 379, 387.

arrangement that the ability to communicate with subsidized subscribers was of value to the subsidizing subscribers.⁵¹⁵

Following the war, the state public utility commissions would follow the federal government's example when setting local rates.⁵¹⁶ By the 1920s, statewide rate averaging had become a standard feature of the regulatory landscape.⁵¹⁷

So John's suggestion that the postal model of universal service provided an early influence on universal service policy in the telephone industry appears to be well taken, but with a somewhat different twist. As noted above, John believed that the mechanism through which these concepts were incorporated into telecommunications policy was Vail's experience with the Railway Mail Service.⁵¹⁸ While John is correct about the influence of the postal system on telephone rates, Vail's experiences were reinforced by a much more direct mechanism: Rate averaging was imposed on the telephone system by the Postmaster General himself.

C. *Federal–State Relations*

The government takeover during World War I also had a profound influence on federal–state relations. Burleson's order to raise and standardize national rates was met with immediate resistance from state regulatory agencies who sought to enjoin the rate increases.⁵¹⁹ Injunctions were granted in ten states across the country, from Florida to Pennsylvania to South Dakota.⁵²⁰ AT&T's general counsel, N.T. Guernsey worked with Post Office Solicitor William Lamar to get a test case quickly to the Supreme Court.⁵²¹ In March, the South Dakota Supreme Court enjoined the Dakota Central Telephone Company from raising rates.⁵²² Guernsey convinced Lamar to fight the injunction, and Lamar obtained approval from the Attorney General to challenge the ruling.⁵²³ As Danielian describes it, "Thus the United States Attorney General's office, the Post Office Department, and the Bell System were mobilized, hand in hand, to defend the Postmaster General's order for increased Bell telephone rates."⁵²⁴

515. 1 LEONARD S. HYMAN ET AL., *THE NEW TELECOMMUNICATIONS INDUSTRY: EVOLUTION AND ORGANIZATION* 81 (1987), *quoted in* Thierer, *supra* note 16, at 276.

516. Thierer, *supra* note 16, at 277.

517. VIETOR, *supra* note 16, at 173–74; Warren G. Lavey, *The Public Policies that Changed the Telephone Industries into Regulated Monopolies*, 39 *FED. COMM. L.J.* 171, 188–89 (1987).

518. *See supra* note 502 and accompanying text.

519. DANIELIAN, *supra* note 17, at 260.

520. *Id.* at 262.

521. *Id.*

522. *Id.*

523. *Id.* at 263.

524. *Id.*

The case of *Dakota Central Telephone Co. v. South Dakota* was argued on May 5–6, 1919, and decided on June 2, 1919.⁵²⁵ As noted earlier, the Supreme Court upheld the rate increases by a vote of 8–1.⁵²⁶ The Court depicted the issue as similar to the one recently resolved in *Northern Pacific Railway Co. v. North Dakota*,⁵²⁷ where the Court upheld the federal government’s ability to set intrastate railroad rates under Congress’s war power.⁵²⁸ In the case at bar, Justice White saw the same principle at work: Congress could lawfully take over a public utility under its war power,⁵²⁹ and state police power did not create protected enclaves of state prerogative.⁵³⁰ Justice White wrote:

Conceding that it was within the power of Congress, subject to constitutional limitations, to transplant the state power as to intrastate rates into a sphere where it, Congress, had complete control over telephone lines because it had taken possession of them and was operating them as a governmental agency, it must follow that, in such sphere there would be nothing upon which the state power could be exerted except upon the power of the United States, that is, its authority to fix rates for the services which it was rendering through its governmental agencies.⁵³¹

Accordingly, the Court overruled the injunction and Burleson’s rate hikes were upheld.⁵³² The victory ended up being somewhat pyrrhic. Frustration with the rate increases approved by the Court led the states to lend their support to returning the wires to private control as quickly as possible.⁵³³ Moreover, the Supreme Court would subsequently curb federal power in *Smith v. Illinois Bell Telephone Co.*⁵³⁴ by denying the ICC the authority to affect intrastate rates.⁵³⁵ Instead, the states would bear that responsibility after the cost of any assets used for both interstate and intrastate service was apportioned between the two services.⁵³⁶ This movement culminated with the inclusion of a provision in the Communications Act of 1934 disavowing any FCC jurisdiction over

525. 250 U.S. 163 (1919).

526. See *supra* notes 326–28 and accompanying text.

527. 250 U.S. 135 (1919).

528. *Id.* at 151–52.

529. *Dakota Cent. Tel.*, 205 U.S. at 183–84.

530. *Id.* at 187.

531. *Id.*

532. As May notes, the Court’s decisions occurred after “the experiments were marked for extinction,” and thus the Court may have felt less need to become involved with the issues. MAY, *supra* note 17, at 57.

533. Bickers, *supra* note 17, at 154–55.

534. 282 U.S. 133 (1930).

535. *Id.* at 159–60.

536. *Id.* at 148–49.

“charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service.”⁵³⁷

A comparison with how similar issues were resolved in railroading illustrates the strength and influence of state opposition to federal power mobilized by Burleson’s ham-fisted policies.⁵³⁸ When confronted with a similar issue with respect to railroads in *The Shreveport Rate Case*,⁵³⁹ the Court held that the ICC had jurisdiction over interstate rates as well as “all matters having such a close and substantial relation to interstate traffic that the control is essential or appropriate” to the security and efficiency of interstate service.⁵⁴⁰ The Court further concluded, “The fact that carriers are instruments of intrastate commerce, as well as of interstate commerce, does not derogate from the complete and paramount authority of Congress over the latter.”⁵⁴¹ In short, “[w]herever the interstate and intrastate transactions of carriers are so related that the government of the one involves the control of the other, it is Congress, and not the State, that is entitled to prescribe the final and dominant rule.”⁵⁴² The Court reaffirmed “the principle that Congress in the exercise of its paramount power may prevent the common instrumentalities of interstate and intrastate commercial intercourse from being used in their intrastate operations to the injury of interstate commerce” even though “intrastate transactions of interstate carriers may thereby be controlled.”⁵⁴³ Any other conclusion would contradict the principle of federal supremacy.⁵⁴⁴

The Court reiterated this conclusion after the war in *Railroad Commission v. Chicago, Burlington & Quincy Railroad*,⁵⁴⁵ in which it held that “[e]ffective control of [interstate traffic] must embrace some control over [intrastate traffic] in view of the blending of both in actual operation. The same rails and the same cars carry both. The same men conduct them. Commerce is a unit and does not regard state lines”⁵⁴⁶ When interstate and intrastate commerce “are so mingled together that the supreme authority,

537. 47 U.S.C. § 152(b) (2006).

538. See HUBER ET AL., *supra* note 14, § 3.2.3–.5, at 216–18 (noting that states wanted federal authority to be sharply limited).

539. 234 U.S. 342 (1914).

540. *Id.* at 351.

541. *Id.*

542. *Id.* at 351–52.

543. *Id.* at 353.

544. *Accord* Minnesota Rate Cases, 230 U.S. 352 (1913). This case held:

[T]he full control by Congress of the subjects committed to its regulation is not to be denied or thwarted by the commingling of interstate and intrastate operations [and that] the execution by Congress of its constitutional power to regulate interstate commerce is not limited by the act that intrastate transactions may have become so interwoven therewith that the effective government of the former incidentally controls the latter.

Id. at 399.

545. 257 U.S. 563 (1922).

546. *Id.* at 588.

the Nation, cannot exercise complete effective control over interstate commerce without incidental regulation of intrastate commerce, such incidental regulation is not an invasion of state authority or a violation of the proviso.”⁵⁴⁷ The Supremacy Clause gives the federal government the power to “impose any reasonable condition on a State’s use of interstate carriers for intrastate commerce it deems necessary or desirable.”⁵⁴⁸

Had the Court applied these same principles to telephony, it would have found that interstate and intrastate phone calls were just as intertwined as rail traffic and upheld federal jurisdiction over local rates. And yet in *Smith*, the Court mandated that all property used for both interstate and intrastate calling be separated into interstate and intrastate portions, calling this separation “essential to the appropriate recognition of the competent governmental authority in each field of regulation.”⁵⁴⁹ The Court recognized that “the difficulty in making an exact apportionment of the property is apparent,” but nonetheless optimistically concluded that “reasonable measures” would be sufficient.⁵⁵⁰ As noted above, Congress codified this understanding by enacting section 2(b) of the Communications Act of 1934, which courts and commentators have recognized was specifically enacted to prevent the extension of *Shreveport*-type rules to telephony.⁵⁵¹

It is likely that the Post Office’s dismal record running the telephone system and its willingness to brush aside the interests of state regulators rendered policy makers less inclined to condone strong federal jurisdiction over telephony. Moreover, the fact that the Supreme Court’s *Dakota Central* decision upholding federal authority over local telephony was upheld as a war measure may have left the Justices feeling constrained to come to the opposite conclusion after the exigency had passed.

D. *The Limits of Government*

Perhaps the biggest question is that having taken over the telephone system, why did the government give it back? Burleson openly harbored ambitions of making government ownership permanent, as did leaders in the U.S. military.⁵⁵² Doing so would also have brought U.S. policy into conformity with the rest of the world.

547. *Id.*

548. *Id.* at 590.

549. 282 U.S. 133, 148 (1930); *accord id.* at 149 (“The proper regulation of rates can be had only by maintaining the limits of state and federal jurisdiction . . .”).

550. *Id.* at 150; *accord* HUBER ET AL., *supra* note 14, § 3.3.3, at 223–24.

551. *La. Pub. Serv. Comm’n v. FCC*, 476 U.S. 355, 372 (1986); *Computer & Commc’ns Indus. Ass’n v. FCC*, 693 F.2d 198, 216 n.99 (D.C. Cir. 1982); *N.C. Util. Comm’n v. FCC*, 537 F.2d 787, 793 n.6 (4th Cir. 1976); Matthew S. Bewig, *Federalism and Telecommunications: On the Right Wavelength?*, 59 GEO. WASH. L. REV. 1190, 1194–95 (1991); Richard McKenna, *Preemption Under The Communications Act*, 37 FED. COMM. L.J. 1, 13–14 (1985).

552. *See supra* note 197 and accompanying text.

One challenge that government ownership struggles to surmount is the problem of raising risk capital. Unlike private enterprises, which can issue equity, governments must finance any capital improvements through taxes, additional revenue from operations, or debt.⁵⁵³ Thus, because telephone systems in Europe were primarily developed by government actors, capital could not be raised by issuing equity to shareholders willing to assume entrepreneurial risk, and the systems faced political challenges that private enterprises did not need to confront.⁵⁵⁴

In addition, government-owned enterprises tend to avoid risk rather than maximize economic welfare. Government operators in Europe “used their market power to protect themselves from risk rather than to maximize profits.”⁵⁵⁵ These governments had invested heavily in telegraph systems, and the development of the telephone posed significant risks to telegraph revenues: “All the public agencies attempted to protect their telegraph services from telephone competition, even when they controlled both telegraph and telephone.”⁵⁵⁶ Even when European governments did not grant an exclusive monopoly to government agencies, these very same agencies “used similar tactics to those of private companies to extend their power.”⁵⁵⁷ Without the threat of antitrust, there was nothing to restrain unfair practices on the part of the government agencies.

In the United States, development was much more rapid owing to the competitive environment. Competition encouraged innovation and experimentation. For instance, “[t]he existence of several companies allowed various beliefs as to the elasticity of demand to be tested and prevented slow growth through a mistaken belief that the demand was inelastic.”⁵⁵⁸ But the pace and pattern of development in the United States was not merely influenced by the *absence* of government ownership, as discussed above. U.S. development was also influenced by the *presence* of state and local regulation, the possibility of antitrust enforcement, and the possibility of nationalization.⁵⁵⁹

Each of these three factors influenced development of the U.S. network, such that it cannot be accurately said that the development of telecommunications in Europe and the United States diverged because of the presence of one factor, e.g., ideological or political. It is more accurate to

553. See Johannes M. Bauer, *Regulation and State Ownership: Conflicts and Complementarities in EU Telecommunications*, 76 ANNALS PUB. & COOPERATIVE ECON. 151, 155 (2005) (explaining that government-owned enterprises have fewer financing options than their private counterparts).

554. See BROCK, *supra* note 15, at 146–47 (discussing the differences in development of long-distance telegraphs in the United States and Europe).

555. *Id.* at 145.

556. *Id.* at 146.

557. *Id.* at 145.

558. *Id.* at 144.

559. See John, *supra* note 17, at 410 (“Politics always mattered.”).

say that U.S. development at this time was influenced by the example of European regulation, and accordingly began to move towards a more similar result.⁵⁶⁰ In other words, there was a transatlantic dialogue about the proper way to develop a national telephone network.

But perhaps the most important reason cited during the 1919 hearings on whether the government should return the telephone system to private control was the government's inability to control costs.⁵⁶¹ Both of these concerns should serve as cautionary tales to contemporary advocates of networks operated by governments. Indeed, the government's struggles to run the telephone network during World War I are part of a larger tradition identifying circumstances under which common carriage regulation is most likely to work well. It is best suited to industries such as water and natural gas, in which technology is static, market shares are stable, and the fact that a network has already been built out reduces the emphasis on investment incentives.

All of these considerations should give modern proponents of government ownership of telecommunications networks considerable pause. Indeed, the most salient examples appear to confirm these lessons. On a more optimistic note, this episode also provides reassurance about how justifications based on national emergencies need not necessarily be enduring.

Conclusion

The brief, one-year government takeover of the U.S. telephone system during World War I is rarely analyzed at any length by commentators. When it is discussed, it is often dismissed as an ad hoc event with few implications. A closer inspection of the history and dynamics of this episode in history yields a host of answers to a number of ongoing academic disputes. It reveals that the reconsolidation of the telephone industry during the early twentieth century was the result of conscious government policy as well as the consequences of economic features of the market. As such, it provides another example where government actors rather than corporate magnates were movers in curtailing competition.⁵⁶²

The history also sheds new light on the origins of universal service, showing that it was the result of direct application of the ratemaking principles developed for the postal system. In the process, it underscores the

560. See generally, DANIEL T. RODGERS, *ATLANTIC CROSSINGS: SOCIAL POLITICS IN A PROGRESSIVE AGE* (1998) (documenting cross-Atlantic influences on Progressive reformers).

561. See *Return of the Wire Systems*, *supra* note 202, at 33–36 (discussing the high costs associated with telephone systems).

562. See FRED S. MCCHESENEY, *MONEY FOR NOTHING: POLITICIANS, RENT EXTRACTION, AND POLITICAL EXTORTION* 17–19 (1997) (arguing that regulatory bodies often deliberately create economic rents in order to have something to redistribute).

legacy of rate averaging as a source of universal service funding that long antedates the more recent imposition of long distance–local cross subsidies.

It illustrates how the invocation of emergency powers represents a two-edged sword. On the one hand, the exigencies of war make actions easier to justify. On the other hand, courts that have upheld a governmental action on the basis of that exigency may later prove reluctant to uphold similar actions taken under more normal circumstances.

Perhaps most importantly, the episode sheds new light on the circumstances under which governmental operation of a communications network is likely to succeed. The experience suggests that such an arrangement works best when the technology is relatively stable, the risks are well defined, providing service does not require substantial new investments, and the political coalition supporting government operation has realistic expectations. These insights can provide considerable guidance to policy makers considering reversing the trend toward privatization and returning to patterns of government ownership.