

Exhibit No. \_\_\_\_\_  
Witness: John W.. Mayo  
Type of Exhibit: Surrebuttal Testimony  
Party: Sprint Nextel Corporation  
Case No. IO-2006-0086

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

Application of Sprint Nextel Corporation       )  
for Approval of the Transfer of Control of       ) Case No. IO-2006-0086  
Sprint Missouri, Inc., Sprint Long               )  
Distance, Inc. and Sprint Payphone             )  
Services, Inc. From Sprint Nextel               )  
Corporation to LTD Holding Company.           )

**SURREBUTTAL TESTIMONY OF JOHN W. MAYO**

**ON**

**BEHALF OF**

**SPRINT NEXTEL CORPORATION**

**PUBLIC VERSION**

**JANUARY 5, 2006**

1    **Q.     Please state your name and business address.**

2    A.     My name is John W. Mayo. My business address is Georgetown University,  
3           McDonough School of Business, Old North Building, 37<sup>th</sup> and O Streets, N.W.,  
4           Washington, D.C. 20057.

6    **Q.     Have you testified before in this proceeding?**

7    A.     Yes.

9    **Q.     Have you reviewed the Amended Response to Staff Testimony of Ms.**  
10          **Goldman from the Communications Workers of America (CWA) regarding**  
11          **the proposed corporate restructuring of Sprint Nextel?**

12   A.     Yes. She expresses a number of concerns ranging from the financial structure of  
13          the proposed restructuring to the quality of services that will be provided by the  
14          Applicant in the wake of the restructuring.

16   **Q.     Did Ms. Goldman substantively address the benefits of the restructuring that**  
17          **you identified in your Direct Testimony?**

18   A.     No. As I indicated in my Direct Testimony, a complete public interest assessment  
19          in this case requires not only a legal but also an economic lens through which to  
20          view the proposed restructuring. In this regard, I find that the proposed  
21          restructuring represents a very natural consequence of the firm seeking ways to  
22          organize itself in a manner that is most efficient. Similar restructurings have  
23          rather routinely been found to be favorably received by financial markets. The

1 reasons for this favorable evaluation tend to include an increased ability of  
2 managers to more efficiently engage in decision making within their enterprises,  
3 the ability of managers to strategically focus on more manageable markets, and  
4 the ability to sharpen managerial incentives through refined, more targeted  
5 compensation schemes.

6 In the specific case at hand, these benefits are quite likely to occur as the  
7 separation will permit Sprint Missouri, Inc. (“Sprint Missouri”) and LTD Holding  
8 Company to focus more clearly on their core strategic assets – local customers;  
9 and for shareholders to more keenly discern the successes and failures of  
10 managers to nurture that asset base. As I noted in my Direct Testimony, “This  
11 heightened focus and reliance on its local customers for its financial success  
12 means that the company will have maximal incentives to create valued and  
13 innovative services for these customers” (page 8). Similarly, when separated  
14 from Sprint Missouri and its other local wireline companies, Sprint Nextel (with  
15 its strong wireless base) will have the opportunity to clearly and strategically turn  
16 toward pursuing telecommunications customers’ patronage regardless of where  
17 they are located. And, for its part, Sprint Missouri will offer a portfolio of  
18 telecommunications services (including de novo wireless and long distance  
19 services and plans that are targeted at its local customer base), effectively  
20 increasing consumer choice and competition. Thus, the separation will certainly  
21 create benefits to Missouri consumers by heightening competition for their  
22 business. In sum, this change in structure creates the considerable promise of a  
23 more efficient corporate organization and a more satisfied base of customers and

1 shareholders. Unfortunately, Ms. Goldman has either ignored or convoluted these  
2 significant benefits.

3

4 **Q. Given, then, that Ms. Goldman does not directly address the affirmative**  
5 **benefits of the proposed restructuring, are you persuaded by her concerns**  
6 **that the proposed restructuring is not in the public interest?**

7 A. No. Aside from the fact that her analyses virtually ignore the benefits I have  
8 described above, her concerns suffer from at least three fundamental  
9 shortcomings. First, the issues that she raises are often mis-framed. Second, her  
10 testimony engages in exactly the sort of arm-chair quarterbacking that I warned of  
11 in my Direct Testimony.<sup>1</sup> Finally, Ms. Goldman's policy perspectives and  
12 prescriptions are anachronistic. Consequently, I recommend that the Commission  
13 give little weight to her concerns.

14

15 **Q. You say that Ms. Goldman's concerns are often mis-framed. Can you**  
16 **provide an example?**

17 A. Yes. Ms. Goldman [Amended Response to Staff Testimony at pages 20-23]  
18 argues that the quality of service for Sprint Missouri customers has been  
19 deteriorating and speculates that quality of service issues will worsen in the wake  
20 of the restructuring. Her argument, though, rests solely on a perceived financial  
21 inability of Sprint Missouri to invest in, and service, its network. While the  
22 financial strength of the restructured company to fund necessary investment and

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<sup>1</sup> See Direct Testimony of John W. Mayo, p. 5.

1 maintenance projects is dealt with elsewhere,<sup>2</sup> it is important to point out that  
2 regardless of the current level of quality of service, the restructuring will  
3 significantly heighten the incentives for the local company, now exclusively  
4 enmeshed with its base of Missouri customers, to provide high quality, and, as  
5 warranted, improved customer service. Specifically, once the restructuring  
6 occurs, the financial future of the company will be entirely dependent on its  
7 provision of high quality and attractive services to its local base of customers.  
8 Thus, the restructuring will strengthen incentives for the firm to provide the  
9 highest possible quality to its extant and potential customers. Thus, Ms. Goldman  
10 errs in her attribution of the proposed corporate restructuring to her entirely  
11 speculative future quality reductions. Apart from the public commitments of  
12 Sprint Missouri's management to quality and the assurances afforded from  
13 continued regulatory oversight, the restructuring itself should provide increased  
14 comfort that the firm will provide high quality service to its customers. Thus, to  
15 the extent that higher quality provision of services is a relevant issue, such  
16 concerns are actually mollified with the restructuring.

17  
18 **Q. Are there yet other examples in which Ms. Goldman mis-frames issues in this**  
19 **proceeding?**

20 A. Yes. Ms. Goldman (Amended Response to Staff Testimony at page 3) describes  
21 what she sees as a problem with the re-structuring plan. Specifically, she states  
22 that "LTD will be weaker as a stand- alone entity than it was as part of a  
23 diversified communications company." Her observation is, however, mis-framed

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<sup>2</sup> See the testimonies of Sprint Nextel witnesses Kent W. Dickerson and Brian K. Staihr.

1 in several respects. First, a dispassionate reading of the economic literature does  
2 not support Ms. Goldman’s apparent concerns about less diversified companies.  
3 A recent study begins with a summary of the extant literature: “Most studies in  
4 the empirical literature find a negative relationship between diversification and  
5 performance, either measured by profitability, productivity or stock market  
6 returns.”<sup>3</sup> The study (which examines the corporate strategies of leading  
7 European Union firms in the wake of the European economic integration) finds  
8 that when firms face increasingly competitive markets, the pursuit of efficiencies  
9 tends to drive them to refocus on their core markets and away from  
10 diversification.

11 Second, contrary to Ms. Goldman’s statement, there is no indication that  
12 LTD Holding Company will be any less diversified on a going-forward basis.  
13 The restructuring creates LTD Holding Company as a holding company within  
14 which a set of local exchange companies such as Sprint Missouri will continue to  
15 provide an entire portfolio of services, through a blend of outright ownership of  
16 assets (e.g., local exchange facilities) and contracts (e.g., long-distance and  
17 mobile telephony services). This ability to provide services in volatile and rapidly  
18 evolving markets without the commitment of the outright ownership of assets (a  
19 significant fraction of which may be economically sunk) is likely to significantly  
20 reduce the operational risk of LTD Holding Company. Thus, the restructuring  
21 will permit the firm to continue to provide the full portfolio of services that  
22 consumers seek, but to do so through reduced operational risk.

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<sup>3</sup> See, Laura Rondi and Davide Vannoni “Are EU Leading Firms Returning to Core Business? Evidence on Refocusing and Relatedness in a Period of Market Integration,” Review of Industrial Organization, Vol. 27, September 2005, pp. 125-145 [footnote omitted].

1           Finally, with all due respect to Ms Goldman, she cannot confidently know  
2           that a stand-alone local exchange company such as LTD Holding Company will  
3           be weaker than a diversified firm. The entire technology, demand and regulatory  
4           dimensions of the telecommunications industry are in a matter of considerable  
5           flux and, as such, predictions regarding the “correct” firm structure are, I believe,  
6           beyond the grasp of objective, dispassionate students of the industry. Indeed, I  
7           am reminded that upon the divestiture of AT&T from the Bell operating  
8           companies, many believed that the Bell operating companies -- each operating as  
9           a “stand-alone local telephone company” -- would be at a significant disadvantage  
10          in the marketplace. Yet, twenty years later we see that those companies have  
11          emerged as highly successful enterprises.

12

13   **Q.    You mentioned the propensity of Ms. Goldman to engage in “arm-chair**  
14   **quarterbacking”. Can you provide an example?**

15   A.    Yes. Ms. Goldman (Amended Response to Staff Testimony at page 18) states her  
16          concern that “[t]he trend in the communications industry is to provide bundles of  
17          local, long-distance, wireless, Internet access, and video services over one’s own  
18          network” and that, consequently, the restructured company “may not be able to  
19          survive and grow” (page 19). Such judgmental inferences regarding the  
20          advantages or disadvantages of the proposed restructuring extend well beyond  
21          what can be prudently inferred simply based on an observed industry “trend.” As  
22          I emphasized in my Direct Testimony (pages 3-5, 9) different firms, positioned  
23          differently in the marketplace, with different core assets can be expected to adopt

1 different strategic paths, especially in an industry as dynamic as  
2 telecommunications. What we can comfortably know is that Sprint Missouri will  
3 be a fully capable telecommunications provider for a base of Missouri customers  
4 and will have heightened incentives to serve those customers well. Whether it  
5 owns or, alternatively, contracts to supply the panoply of services desired by these  
6 customers is, I believe, best left as a matter of managerial judgment, not  
7 regulatory fiat, as Ms. Goldman advocates.

8

9 **Q. Are there other examples of arm-chair quarterbacking?**

10 A. Yes. Ms. Goldman suggests (Amended Response to Staff Testimony at page 20)  
11 that the contracts for long-distance and wireless services that Sprint  
12 Missouri/LTD Holding Company is negotiating with Sprint Nextel represent a  
13 “sweetheart deal that should not be condoned by the Commission”. Such a call  
14 for prima facie rejection of these contracts is, however, completely unwarranted.  
15 In fact, the decision to purchase Sprint Nextel long-distance and wireless services  
16 creates an immediate benefit to both consumers and Sprint Missouri, relative to a  
17 costly search and implementation process for a de novo provider of these services,  
18 by ensuring continuity of the underlying carrier for these services.<sup>4</sup> Moreover, in  
19 this instance this continuity is complemented by the price and quality protections  
20 afforded by the presence of actively competitive long-distance and wireless  
21 markets. Specifically, the fact that Sprint Nextel sells long-distance and wireless  
22 services in actively competitive markets ensures that its price and quality  
23 offerings for these services -- to wholesale customers such as LTD Holding

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<sup>4</sup> See Surrebuttal Testimony of Kent W. Dickerson at pages 3-6.



1 Company – will be beneficial for ultimate retail consumers. Indeed, in the case at  
2 hand, I understand that contracts will include a Most Favored Nations provision  
3 that will afford LTD Holding Company the lowest price available to similarly  
4 situated purchasers of Sprint Nextel services, thereby ensuring that LTD Holding  
5 Company will be in a position to offer the lowest prices possible to its customers  
6 for these services.<sup>5</sup> In sum, the fact that LTD Holding Company is ensuring the  
7 continuity of supply for long-distance and wireless with Sprint Nextel is not  
8 worrisome and should not be the basis for micro-regulating this restructuring.  
9

10 **Q. How might the concerns expressed by Ms. Goldman reflect an anachronistic**  
11 **regulatory perspective?**

12 A. Ms. Goldman proffers a variety of “conditions” that she wishes to impose on the  
13 restructuring that are both anachronistic and, arguably, perverse to the public  
14 interest. For example, Ms. Goldman (Amended Response to Staff Testimony at  
15 pages 25-26) concludes that the restructuring be conditioned upon the new and  
16 additional regulatory requirements on the firm regarding, inter alia, its  
17 employment levels, its capital structure, its dividend payouts, and its purchasing  
18 processes for wholesale inputs. Such regulatory controls certainly would put the  
19 Commission into the position of micro-managing the business of Sprint Missouri  
20 and neither protects consumers nor the public interest. Extant regulatory  
21 oversight, including price and service regulation of Sprint Missouri, will continue  
22 in full force in the wake of the restructuring. Such regulatory oversight should be  
23 fashioned to promote and complement the efficiency of the firms they oversee.

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<sup>5</sup> *Id.* at p. 4.

1       The imposition of Ms. Goldman's suggested mandated employment levels,  
2       mandated capital structure, and mandated contracting processes however, act to  
3       constrain the ability of the firm to seek the most efficient mode of operating and  
4       will be directly contrary to the pro-efficiency aims of modern regulatory  
5       oversight.

6

7   **Q.    Does this conclude your Surrebuttal Testimony?**

8   A.    Yes.