

Exhibit No. _____
Issues:
Witness: Brian K. Staihr
Type of Exhibit: Surrebuttal Testimony
Party: Sprint Missouri, Inc.
Case No. IO-2003-0281

BEFORE THE PUBLIC SERVICE COMMISSION

STATE OF MISSOURI

In the Matter of the Investigation) **Case No. IO-2003-0281**
Of the State Of Competition in the)
Exchanges of Sprint Missouri, Inc.)

SURREBUTTAL TESTIMONY

OF

Dr. Brian K. Staihr

**ON BEHALF OF
SPRINT MISSOURI, INC.**

July 7, 2003

1 **I. BACKGROUND AND PURPOSE**

2 **Q. Please state your name, title, and business address.**

3 **A.** My name is Brian K. Staihr. I am employed by Sprint Corporation as Senior
4 Regulatory Economist in the Department of Law and External Affairs. My
5 business address is 6450 Sprint Parkway, Overland Park, Kansas 66251.

6
7 **Q. Please briefly describe your educational background and work experience.**

8 **A.** I hold a B.A. in Economics from the University of Missouri-Kansas City, and an
9 M.A. and Ph.D. in Economics from Washington University in St. Louis. My field
10 of specialization is Industrial Organization, including Regulation.

11
12 I have been a part of Sprint's Regulatory Policy Group since 1996. In my current
13 position I am involved with the development of state and federal regulatory and
14 legislative policy for all divisions of Sprint Corporation. I am also involved with
15 the coordination of policy across business units. My particular responsibilities
16 include 1) ensuring that Sprint's policies are based on sound economic reasoning,
17 2) undertaking or directing economic/quantitative analysis to provide support for
18 Sprint's policies, and 3) conducting original research. The specific policy issues
19 that I address include universal service, pricing, costing (including cost of
20 capital), access reform, reciprocal compensation and interconnection, local
21 competition, and more.

22

1 In my position I have appeared before the Kansas Corporation Commission, the
2 Florida Public Service Commission, the New Jersey Board of Public Utilities, the
3 Pennsylvania Public Utility Commission, the North Carolina Utilities
4 Commission, the Public Service Commission of South Carolina, the Public
5 Service Commission of Nevada, the Texas Public Utilities Commission, the
6 Illinois Public Service Commission, and the Missouri Public Service
7 Commission. I have also worked extensively with the Federal Communication
8 Commission's staff and presented original research to the FCC. My work has
9 also been used in congressional oversight hearings.

10
11 In January 2000 I left Sprint temporarily to serve as Senior Economist for the
12 Federal Reserve Bank of Kansas City. There I was an active participant in the
13 Federal Open Market Committee process, the process by which the Federal
14 Reserve sets interest rates. In addition, I conducted original research on
15 telecommunication issues and the effects of deregulation. I returned to Sprint in
16 December 2000.

17
18 For the past seven years I have also served as Adjunct Professor of Economics at
19 Avila University in Kansas City, Missouri. There I teach both graduate and
20 undergraduate level courses.

21
22 Prior to my work in Sprint's Regulatory Policy Group I served as Manager-
23 Consumer Demand Forecasting in the marketing department of Sprint's Local

1 Telecom Division. There I was responsible for forecasting the demand for
2 services in the local market, including basic local service, and producing elasticity
3 studies and economic and quantitative analysis for business cases, opportunity
4 analyses, etc.

5
6 **Q. What is the purpose of your surrebuttal testimony?**

7 **A.** In this testimony I address two issues raised in the rebuttal testimony of Office of
8 Public Council Witness Ms. Barbara Meisenheimer filed June 10, 2003.

9 Specifically, I respond to Ms. Meisenheimer's claim that Sprint is not subject to
10 effective competition in certain exchanges, a claim she makes after calculating a
11 number known as a Herfindahl-Hirschman Index (HHI). I also address the
12 concept of *substitutability* as it applies to basic local service and wireless service.

13
14 **II. HERFINDAHL-HIRSCHMAN INDEX (HHI)**

15 **Q. On page 22 of her rebuttal testimony Ms. Meisenheimer writes, "The HHI**
16 **analysis I conducted on an exchange-by-exchange basis shows that the**
17 **market for basic local service is highly concentrated and not subject to**
18 **effective competition." Is this statement correct?**

19 **A.** No. Not only is the statement incorrect, but it demonstrates an incorrect
20 understanding of the proper use and proper interpretation of the Herfindahl-
21 Hirschman Index. It also demonstrates an incorrect understanding of the role that
22 market concentration plays in determining whether or not any firm has market

1 power or is subject to effective competition. Both of these are addressed in detail
2 below.

3

4 **Q. Before discussing the proper interpretation and usage of the HHI, and the**
5 **role that market concentration plays in determining market power, can you**
6 **give a very simple example of how Ms. Meisenheimer's statement is**
7 **incorrect?**

8 **A.** Yes. According to Ms. Meisenheimer's statement the market for basic local
9 service is *highly-concentrated*, so it is not subject to effective competition. A
10 *highly-concentrated* market is one that has a HHI measure over 1800, according
11 to the Department of Justice guidelines that Ms. Meisenheimer cites. If we use
12 FCC data to examine the market for long-distance calling in the years 1998-99 we
13 find that, in those years, the long-distance market *also* had a HHI well over 1800.¹
14 But in 1998-99 the major inter-exchange carriers were engaged in an all-out price
15 war to see which carrier could add customers fastest (recall the dinner-time
16 telephone calls offering endless variations on calling plans). In 1998-99 the
17 market for long-distance calling was extremely competitive, with customers
18 enjoying a variety of offers and pricing plans, and customers responding by
19 increasing their demand (minutes) at a rapid pace. No one could defensibly
20 suggest that the market for long-distance calling did not exhibit "effective
21 competition" in 1998-99. Yet Ms. Meisenheimer's statement appears to suggest
22 exactly that.

1

2 **Q. What, exactly, does the Herfindahl-Hirschman Index (HHI) measure?**

3 A. It measures market concentration. It does not measure competition, nor does it
4 measure market power. And although there is often a relationship between
5 market concentration and competition, as well as a relationship between
6 competition and market power, the HHI actually *measures* only one of these:
7 market concentration.

8

9 **Q. Does the Herfindahl-Hirschman Index (HHI) measure market dominance?**

10 A. Ms. Meisenheimer, in her testimony, claims that the HHI measures market
11 *dominance*. She writes, “One measure of market dominance (and in turn, the
12 absence of effective competition) is the Herfindahl-Hirschman Index (HHI)”
13 (page 17). That statement is incorrect. Although Ms. Meisenheimer does not say
14 exactly what she means by the term market *dominance*, her statement is incorrect
15 regardless of her interpretation because the HHI does not measure “the absence of
16 effective competition.” In fact, depending on her definition of dominance, the
17 HHI does not even measure market dominance. It is somewhat revealing that the
18 Department of Justice Merger Guidelines, which Ms. Meisenheimer depends on
19 as a source throughout her testimony, contain a thorough discussion of the HHI
20 but do not contain the phrase “market dominance” anywhere in their text.

21

22 **Q. Is there a standard definition of “market dominance”?**

¹ Actual measures range from 2,572 to 3,260. FCC’s Industry Analysis Division’s *Statistics of the Long-*

1 A. There are different definitions. The FCC, in numerous dockets, has said that a
2 dominant firm (carrier) is one that has market power.² Market power is the ability
3 to maintain prices above competitive levels for a significant period of time.³
4 However, that definition is somewhat misleading because any firm that can
5 successfully differentiate its product from its competitors can achieve a degree of
6 market power.⁴ For example, if consumers believe (rightly or wrongly) that there
7 are differences between Levis blue jeans, Wrangler blue jeans, and Gap blue jeans
8 then Levis, Wrangler and Gap all would possess market power. Yet it would be
9 odd to suggest that all three are *dominant* in the market for blue jeans.
10 Furthermore, the HHI itself does not measure market power. It measures market
11 concentration, which may or may not be related to market power.

12
13 Returning to the definition of *dominance*, in standard microeconomic theory there
14 is a well-known model known as the *dominant firm model*.⁵ In this model one
15 firm has a larger market share, and it competes with other firms with smaller
16 market shares that are often referred to as a *competitive fringe*. In this model the
17 larger firm may have significant market power or it may have almost no market
18 power. In the dominant firm model, the larger firm is dominant because it sets a
19 price and the competing firms take that price as given. But with regard to the

Distance Industry, released May 14, 2003. Available at www.fcc.gov. Long-distance market defined as "End-User Service Ordinary Long Distance."

² See, most recently, Further Notice of Proposed Rulemaking in FCC Docket WC 02-112, released May 19, 2003, paragraph 4.

³ See Department of Justice Horizontal Merger Guidelines, available at www.usdoj.gov.

⁴ See, for example, Browning and Zupan, *Microeconomic Theory and Application*, Addison Wesley Educational Publishers, Inc., 1999.

⁵ See (among others) Viscusi, Vernon and Harrington, *Economics of Antitrust and Regulation*, MIT Press, 2000.

1 HHI this cannot be the type of dominance that Ms. Meisenheimer is referring to
2 because the HHI has nothing to do with prices, and the HHI does not measure a
3 single firm's ability to set a price.

4
5 Alternatively Ms. Meisenheimer could simply be suggesting that the HHI
6 measures market concentration, but calling it market dominance. If so then the
7 first part of her statement is correct but the second part is not, because in many
8 cases—particularly in the case of local telephone service—market concentration
9 does not automatically translate to market power, and market concentration does
10 not automatically suggest the absence of effective competition.

11
12 **Q. How does market power relate to effective competition as defined in**
13 **Missouri?**

14 **A.** Although I am not an attorney, as I read the Missouri statutory criteria for
15 evaluating “effective competition” as an economist it appears that, according to
16 the description that is contained in 386.020.13, RSMo 2000 (as cited by Ms.
17 Meisenheimer, page 12) there does not seem to be any specific mention of market
18 power. The criteria refer to *reasonableness of rates*.

19
20 **Q. But don't economists usually consider there to be a connection between**
21 **market power and effective competition?**

22 **A.** Generally, yes. Effective competition is competition that serves as a general
23 controlling factor on prices. That does not mean that effective competition forces

1 all prices to be the same. Nor does it mean that effective competition forces
2 prices to move only in a downward direction. Nor does it mean that in an
3 effectively competitive market no firm has any market power at all. As I
4 mentioned above, in a market that exhibits product differentiation it is an
5 economic fact that rates will reflect some market power. Effective competition
6 controls the extent to which a firm can exercise market power. That is what it
7 means to be a controlling factor on prices. Dr. Janusz Ordovery, a well-known
8 expert in this area, has written:

9 "In an effectively competitive market, one or more firms may possess
10 some degree of market power, yet pose no significant risk to present and
11 future competition."⁶
12

13 **Q. Can you provide a real-world example of markets where the firms face**
14 **effective competition but also have some degree of market power?**

15 **A.** Yes. In fact, that description applies to the many of markets we see in a "market"
16 economy. These range from easily-identifiable markets such as clothing, fast-
17 food, cosmetics, drugs, and gasoline to more non-standard markets such as the
18 market for an MBA or the market for legal services or the market for funeral
19 services. In all of these markets we see variations in price. In all of these markets
20 we see that products (or services) are differentiated, either in reality or in the
21 perceptions of customers.⁷ But in all these markets we do see effective
22 competition.

⁶ Janusz Ordovery, *Effective Telecommunications Service Competition in Australia and the Need for Regulatory Reform*, November 26, 2000. Available at www.pc.gov.au/inquiry/telecommunications.

⁷ An often-used example of perceived product differentiation is the case of aspirin. There is literally no difference between a brand-named aspirin (Bayer) and a generic aspirin, yet some customers are willing to pay a higher price for the brand-named aspirin simply because in their minds there is a difference. As a

1

2 **Q. So would it be correct to say that effective competition results in a control**
3 **over the abuse of market power, rather than the complete elimination of**
4 **market power?**

5 **A.** Yes. The only place where competition eliminates market power totally is in the
6 textbook-world of perfect competition.

7

8 **Q. So, returning to Ms. Meisenheimer's calculation of the HHI, what does**
9 **market concentration, as measured by the HHI, have to do with market**
10 **power and, most importantly, the ability to exercise market power?**

11 **A.** Holding all other things constant, the *potential* to exercise market power increases
12 as market concentration increases. This is why the Department of Justice's
13 Merger Guidelines contain extensive discussions of market power. And this is
14 possibly the reason why Ms. Meisenheimer incorrectly interprets the HHI as a
15 measure that is useful in this instance. On page 13 of her testimony she writes,
16 "with only two firms controlling the lion's share of the market, it is still highly
17 concentrated and does not provide sufficient assurance against the exercise of
18 market power." Unfortunately, in making this statement, Ms. Meisenheimer has
19 missed a vitally important point in understanding how market concentration
20 primarily affects the *potential* to exercise market power: Market concentration can
21 affect market power if the firms that serve a market can *restrict output*. Sprint, in
22 Missouri, cannot restrict output.

result, Bayer possesses a certain amount of market power. But there is no doubt that many people perceive

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Q. Please explain what restricting output has to do with the ability to exercise market power?

A. Consider an example of a monopoly that is not a telephone company, not a utility or a regulated monopoly, but a single firm that just happens to supply the entire market. A monopoly represents the ultimate example of market concentration. If a monopolist faces neither competition *nor the threat of competition*, and the monopolist is not regulated, the monopolist has the ability to choose how much output it will produce, and how much output it will sell. Now, one might think the monopolist will just sell all that it could, but that is not the case. Because the demand for any good is downward-sloping, smaller levels of output can be (and are) sold at higher prices. Larger levels of output can only be sold at lower prices.

In this example the monopolist could, potentially, choose to sell its good at a price that is significantly higher than a competitive price, and thereby exercise market power. But the mechanism by which the monopolist makes this happen is by supplying the market with a smaller amount; that is, by *restricting output*. The monopolist produces a smaller quantity of output than the competitive level of output. And in the process, charges a higher price. As Browning and Zupan write, “By restricting output, the monopolist is able to charge a higher price.”⁸

brand-named aspirin and generic aspirin as substitutes, and therefore they do effectively compete with each other.
⁸ Browning and Zupan, see footnote 4.

1 Now, moving away from the example of a monopolist, when a market is
2 concentrated among a few firms there is the potential that the firms can
3 collectively act as a monopolist, and *restrict output* in the same way. In that way
4 the small group of firms is able to exercise market power like a monopolist, but
5 that ability depends on being able to successfully produce and seller a smaller
6 quantity of the good; that is, on the ability to restrict output. The perfect example
7 of this (on a somewhat global scale) is OPEC and its control over petroleum
8 output.

9
10 **Q. In the Department of Justice Merger Guidelines that Ms. Meisenheimer uses**
11 **as a source, do they discuss this “restricting of output”?**

12 **A.** Absolutely. In a portion of the Merger Guidelines that Ms. Meisenheimer
13 excluded from her exhibit, the Department of Justice writes,

14 Other things being equal, market concentration affects the likelihood that
15 one firm, or a small group of firms, could successfully exercise market
16 power. *The smaller the percentage of total supply that the firm controls,*
17 *the more severely it must restrict its own output in order to produce a*
18 *given price increase, and the less likely that an output restriction will be*
19 *profitable.” (DOJ Merger Guidelines Section 2.0) (emphasis supplied)*
20

21 The DOJ Merger Guidelines go on to state that sometimes collective action
22 (collusion) is necessary to achieve this reduced output, and sometimes merged
23 firms might find it profitable to unilaterally suppress their output (Guidelines,
24 Sections 2.0 and 2.2).

25
26 **Q. Can telephone companies restrict output in the state of Missouri?**

1 **A.** A CLEC can restrict output. For example, ExOp witness Mr. Devoy states in his
2 testimony that ExOp does not provide service to the entire Kearney exchange.
3 (Devoy page 3) But no ILEC that has carrier-of-last-resort status in this state can
4 restrict output. Since all purchasers in the market must be supplied with
5 telephone service there is no way that total output can be restricted by telephone
6 companies in Missouri. In other words, the vital link between market
7 concentration and the potential ability to exercise market power, which Ms.
8 Meisenheimer takes as given in her testimony, does not apply in this case.

9

10 **Q.** **Is there some other way for a small group of firms to increase prices**
11 **significantly above competitive levels, and thereby abuse their market power,**
12 **without restricting output?**

13 **A.** Theoretically a small group of firms could simply collude to charge higher prices.
14 Such collusion is, of course, illegal in this country. It is also well-known in
15 economics that successful collusion is notoriously difficult to accomplish. But the
16 potential for collusion is discussed in the Merger Guidelines, in a section entitled
17 “Lessening of Competition Through Coordinated Action.”

18

19 **Q.** **Do the Merger Guidelines discuss the abuse of market power in the absence**
20 **of collusion?**

21 **A.** Yes they do, but always with regard to restricting output.

22

1 **Q. So when Ms. Meisenheimer writes, on page 13, “with only two firms**
2 **controlling the lion’s share of the market, it is still highly concentrated and**
3 **does not provide sufficient assurance against the exercise of market power”**
4 **is she suggesting that the two firms, the ILEC and the CLEC, will collude or**
5 **will restrict output?**

6 **A.** It is unclear. Throughout her testimony Ms. Meisenheimer provides no real
7 explanations as to *how* firms might be able to exercise market power, she simply
8 assumes—incorrectly—that a concentrated market is one in which the participants
9 will abuse market power and therefore not offer effective competition. In reality,
10 there is absolutely no evidence to support the claim that a market that is served by
11 a small number of competitors does not exhibit “effective competition.”

12
13 **Q. Regarding Ms. Meisenheimer’s discussion of the “control of the bottleneck**
14 **facility” found on page 18 of her rebuttal testimony, could firms potentially**
15 **abuse market power using the bottleneck facility?**

16 **A.** In discussing this issue Ms. Meisenheimer primarily refers to the local loop,
17 which she refers to as “the conduit for carriers to offer consumers a multitude of
18 services.” (page 18 line 2) The arguments she offers are somewhat confusing,
19 and must be addressed on several levels.

20
21 First, Ms. Meisenheimer says that because Sprint retains “almost exclusive
22 control” of the bottleneck that “the potential exists for Sprint to overcharge both
23 retail and wholesale customers and to ward off meaningful competition” (page

1 18). It is unclear as to whether she is referring to competition at the retail level or
2 at the wholesale level, but in either case her statement is questionable. If the
3 concern is competition at the retail level, I am honestly puzzled as to how Sprint
4 could effectively ward off competition by charging retail customers higher prices.
5 Usually a firm wards off competition by charging *lower* prices, not higher ones.

6
7 If the concern is competition at the wholesale level, I am equally puzzled because
8 Sprint has no competition for wholesale offerings as CLECs are not required to
9 unbundle their networks. But even so the claim regarding “overcharging” is
10 foundationless because Sprint does not have any pricing control at the wholesale
11 level with regard to unbundled network elements, since UNE rates are based on
12 TELRIC, approved by this Commission, and are priced per the FCC’s rules.
13 Consequently, Sprint does not have the ability to “exercise some form of market
14 power” in the provision of wholesale offerings.

15
16 Finally, if the concern is market power in the provision of switched access, again
17 Sprint has no pricing control in this market because intrastate switched access
18 rates are controlled by the Price Cap statutes for Sprint and interstate switched
19 access rates are established by the FCC’s CALLS Order.⁹

⁹ It is true that the bottleneck facility argument is most often made with regard to switched access, and long-distance calling: Long-distance providers have no choice but to terminate their calls over the physical loop that is owned by the local telephone company, so they have no choice but to pay whatever access charge the company charges. (In fact, in her testimony Ms. Meisenheimer mentions that this loop is required to terminate calls (page 18 line 4)). The standard argument, often referred to as the “price squeeze,” is that circumstances might create a situation where it might be possible for ILECs to charge unaffiliated long-distance carriers one price for switched access and find a way to charge an affiliated long-distance carrier a different (lower) price, who could then turn around and under-price the competition in the

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But more importantly, when a competitive firm is a facilities-based provider, such as those that have taken customers from Sprint in its Missouri exchanges, the concept of a bottleneck facility applies equally well to the competitor as to the incumbent; the competitor owns exactly the same conduit over which services are provided. In fact, even when a competitor is purchasing UNE-P and using it to provide services, the UNE-P-based competitor now has control of the bottleneck facility. In fact, the classic price squeeze argument (see footnote 9) applies equally well in the case of a UNE-P-purchasing competitor or facilities-based competitor as it does for an incumbent company. So again, Ms. Meisenheimer's assertions are puzzling because if there are two firms serving a market, each using their own facilities, then this purported type of bottleneck-based market power is available to each of them, and neither carrier can use it in a way that the other can't also. Simply put, having a bottleneck facility does not "ward off" a competitor that also has a bottleneck facility OR a competitor that has the ability to replicate the incumbent's bottleneck facility. So the discussion of the bottleneck facility does not provide any insight into Ms. Meisenheimer's unsupported claims as to why the firms in concentrated market will supposedly have the ability to abuse market power and create a market that is without effective competition.

retail market. But because Sprint has made no filing regarding switched access this cannot be the type of market power Ms. Meisenheimer is referring to when she is discussing her HHI measurements.

1 **Q. Please summarize your discussion of Ms. Meisenheimer's use of the**
2 **Herfindahl-Hirschman Index (HHI).**

3 **A.** Ms. Meisenheimer claims that the HHI measures market dominance. She also
4 claims that the HHI measures the absence of effective competition.

5 • If "market dominance" means market concentration, then Ms. Meisenheimer
6 is correct that the HHI measures market concentration.

7 • If "market dominance" means "the amount of market power that a firm has"
8 Ms. Meisenheimer is incorrect.

9 • If "market dominance" means "the ability to abuse market power" Ms.
10 Meisenheimer is also incorrect.

11 • If "effective competition" means "where no firm has market power" Ms.
12 Meisenheimer has mischaracterized efficient competition, because many
13 efficiently competitive markets have firms that exhibit some degree of market
14 power.

15

16 Simply stated, the HHI measures market concentration and nothing else.

17

18 Ms. Meisenheimer also claims that highly concentrated markets do not provide
19 sufficient assurance against the exercise of market power.

20 • The relationship between market concentration and the potential to exercise
21 market power has to do with the potential ability to restrict output. Sprint
22 cannot restrict output in the state of Missouri.

- 1 • The relationship between market concentration and the potential to exercise
2 market power also is affected by how easy it is for firms to collude; all else held
3 equal, fewer firms make collusion more likely. Collusion is criminal activity. If
4 Ms. Meisenheimer thinks Sprint and its competitor(s) will exercise market
5 power by colluding she is accusing us of planning to engage in criminal activity.
6 This is not an accusation that should be made lightly, nor is it one that deserves
7 any serious consideration by this Commission.

8
9 In summary, Ms. Meisenheimer's HHI measures provide no information at all
10 regarding the existence or absence of effective competition in Sprint's exchanges.

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12 **III. WIRELESS SERVICE**

13 **Q. On page 14 of her testimony Ms. Meisenheimer indicates that she does not**
14 **believe wireless phone service is a substitute for wireline phone service, as**
15 **discussed in 386.020.13, RSMo 2000. Could you comment on the criteria Ms.**
16 **Meisenheimer uses to arrive at her conclusion?**

17 **A. Ms. Meisenheimer's conclusion is not based on economic criteria. Instead, it**
18 **appears to be based on her own opinion and experience, and nothing more.**

19
20 **Q. What are the economic criteria for determining when two goods are**
21 **substitutes?**

22 **A. Whether or not two goods or services are substitutes is a function of demand,**
23 **which is a function of market perceptions: *Do two goods or services have the***

1 *ability, actual or potential, to take away significant amounts of business from*
2 *each other? Do they satisfy the same demand? If so, then they are substitutes.*

3

4 Substitutability does not depend on whether the services are functionally
5 equivalent. Cable modems and DSL service are not functionally equivalent, yet
6 they are clearly substitutes for each other. (It is worth noting that 386.020.13,
7 RSMo 2000 does not require that two services be functionally equivalent. The
8 phrase contained in the statute is “functionally equivalent or substitutable” which
9 seems to clearly indicate (again, per my reading of the statute as an economist)
10 that the Legislature intended these two to mean different things.)

11

12 Substitutability does not depend on the two services being identical. Ms.
13 Meisenheimer mentions 911 service and access to pre-subscribed inter-exchange
14 carriers as features that differentiate wireline service from wireless service. The
15 fact that products or services are differentiated does not mean that they are not
16 substitutes. In St. Louis the city bus service and the city’s mass transit service are
17 obviously substitutes for each other, yet they are clearly differentiated.

18

19 Next, Ms. Meisenheimer writes that wireless service is not subject to the same
20 regulation as wireline service. (She states, “Cellular carriers do not recognize the
21 Commission’s regulatory authority...”) Whether or not two services are
22 regulated or not, or regulated in the same way, has absolutely nothing to do with

1 whether or not the market perceives them to be substitutable. Interstate trucking
2 and interstate railway service are obviously substitutes for each other in terms of
3 moving goods cross-country, with each offering different advantages and
4 disadvantages. (In fact, there is an extensive economic literature on how the
5 trucking industry stole business from the railroad industry, which is exactly the
6 “ability to take business away from each other” criteria I mentioned above.) But
7 regulations on interstate trucking are different from regulations on interstate
8 railway service.

9
10 Next, Ms. Meisenheimer says that, based on her own experience, consumers do
11 not use their mobile phones as substitutes for landline basic local service to their
12 homes. Instead, they use it as a mobile connection to the network and to make
13 long-distance calls. While I do not doubt Ms. Meisenheimer’s personal
14 observations regarding wireless phone usage, I have serious doubts as to whether
15 any single person’s personal observations should be considered 1) probative
16 evidence, 2) representative of all mobile phone usage, 3) projectable to the entire
17 universe of Missouri mobile phone users, and 4) a sound basis for regulatory
18 policy. No study—independent or otherwise—is cited in her testimony. No
19 statistics are provided, and there is no evidence that this observation is consistent
20 with the findings of any party who has researched this issue in depth. Ms.
21 Meisenheimer simply offers her personal opinion based on personal experience,
22 not as an illustrative example but as a justification for a policy recommendation.

23

1 But even more importantly, Ms. Meisenheimer's conclusions based on that
2 experience are flawed. She states that neither mobile connectivity nor long-
3 distance calling is an "attribute of basic local service" and that is why it should
4 not be viewed as substitutable. But as I indicated above, two goods that are
5 substitutes do not have to have identical attributes. To the extent that a mobile
6 phone user makes toll calls and makes calls while mobile, these additional
7 benefits have nothing to do with whether or not that user also considers his or her
8 mobile phone substitutable for local phone service. Two goods are substitutes if
9 they satisfy the same demand. If one of the goods also happens to satisfy an
10 additional demand, that does not make it any less of a substitute. For example, an
11 individual can purchase a video tape of a movie or a DVD of the same movie that
12 also includes comments from the film's director. The DVD provides an
13 additional benefit, one that is not available on the video tape. But each good is
14 clearly a substitute for the other. Ms. Meisenheimer's conclusion, that because
15 wireless calling offers additional benefits it is not a substitute for wireline service,
16 is foundationless.

17
18 (It is worth pointing out that all of these same arguments apply equally well to
19 services such as Directory Assistance (DA), discussed in the testimony of Sprint
20 witness Mark Harper. If customers perceive that an online service such as
21 whitepage.com or yellowpages.com satisfies the same demand that (previously)
22 was met by Sprint's DA offering then the two services are substitutes. It does not
23 matter that one exhibits different characteristics or attributes than another (the

1 online service provides the number visually, Sprint's DA provides the number
2 aurally). It does not matter that one offers additional benefits (the online service
3 provides driving directions) that the other does not. And it does not matter that all
4 customers might not perceive the two to be substitutes. Again, what matters is
5 whether the two have the ability (actual or potential) to take business away from
6 each other. As Mr. Harper discusses, in the case of DA much of that business has
7 already left Sprint.)

8

9 **Q. Based on the economic criteria of substitutability, are wireless and wireline**
10 **calling substitutes for each other?**

11 A. There is no question that a portion of the market perceives them to be substitutes.
12 Whether or not that portion is significant enough to exert control over pricing is
13 an empirical issue that should be investigated. At the same time there is also no
14 question that a portion of the market does not perceive them to be substitutes. But
15 it is not necessary that every potential purchaser of one good consider another
16 good substitutable in order for the two to be substitutes. If that were the case then
17 we would never see product differentiation and effective competition in the same
18 market.

19

20 Sprint did not rely solely (or even primarily) on competition from wireless
21 providers in its filings regarding local service, nor is it asking the Commission to
22 rely solely (or even primarily) on competition from wireless carriers in making its

1 decision regarding local service. But from an economic and market-dynamics
2 standpoint it is wrong to prematurely dismiss wireless competition for local
3 service out of hand. And it is equally wrong, as Ms. Meisenheimer suggests, not
4 to “give the existence of cellular service much weight” unless there is solid
5 evidence offered as to why this portion of the market should not be considered.
6 Ms. Meisenheimer presents no such evidence in her rebuttal testimony.

7

8 **Q. Does this conclude your testimony?**

9 **A. Yes it does.**

10