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Date Prepared:	October 29, 2004

SOUTHWESTERN BELL TELEPHONE, L.P. d/b/a SBC MISSOURI

CASE NO. TO-2005-0035

DIRECT TESTIMONY

OF

HARRY M. SHOOSHAN

St. Louis, MO
October 29, 2004

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of the Second Investigation into the State of Competition in the Exchanges of Southwestern Bell Telephone, L.P., d/b/a/ SBC Missouri.	) Case No. TO-2005-0035)

AFFIDAVIT OF HARRY M. SHOOSHAN

STATE OF NEW HAMPSHIRE)
SS
TOWN OF BEDFORD)

I, Harry M. Shooshan, of lawful age, being duly sworn, depose and state:

1. My name is Harry M. Shooshan. I am presently President, Strategic Policy Research.
2. Attached hereto and made a part hereof for all purposes is my direct testimony.
3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct to the best of my knowledge and belief.

Harry M. Shooshan

Subscribed and sworn to before this 19TH day of October, 2004

Notary Public

My Commission Expires: 2 June 2009.

MELANIE CYNTHIA STRINGER
Notary Public, State of New Hampshire
My Commission Expires 2 June 2009.

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CASE NO. TO-2005-0035
SOUTHWESTERN BELL TELEPHONE, L.P.
D/B/A SBC MISSOURI
DIRECT TESTIMONY OF HARRY M. SHOOSHAN

1. BACKGROUND AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Harry M. Shooshan. My business address is 7979 Old Georgetown Road, Bethesda, MD 20814.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT POSITION?

A. I am a principal in, and co-founder of, Strategic Policy Research, Inc. ("SPR"), a public policy and economics consulting firm that specializes in telecommunications.

Q. PLEASE BRIEFLY STATE YOUR QUALIFICATIONS.

A. Before co-founding SPR, I served for eleven years on Capitol Hill. I was chief counsel and staff director of what is now the Subcommittee on Telecommunications and the Internet of the U.S. House of Representatives. As a consultant, I have specialized in communications public policy analysis, regulatory reform and the impact of new technology and competition. I have presented evidence of wireless competition and wireless substitution in competitive classification cases before five state commissions.

I have testified before several Congressional committees, before the Federal Communications Commission ("FCC"), before the Canadian Radio-television and Telecommunications Commission and over two dozen state commissions. My testimony before state commissions has been on topics related to price regulation, the introduction of competition and the reclassification of services. I also served as an advisor to the Iowa Utilities Board and to the staff of the Arizona Corporation Commission, where my work included the development of alternative regulation/price regulation plans and implementation of the Telecommunications Act of 1996.

I have also been involved in our firm's work with OFTEL (now OFCOMM), the telecommunications regulatory body in the United Kingdom, which adopted the first price regulation plan for an incumbent provider in 1983. The U.K. regulator has since gradually withdrawn from regulating retail prices as competition has developed.

I received a B.A. from Harvard University in Government and a J.D. from Georgetown University Law Center. From 1978 to 1991, I was an adjunct professor of law at Georgetown University Law Center, teaching regulation and communications law.

A copy of my curriculum vitae is contained in Shooshan—Schedule 1.

2. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to support the Southwestern Bell Telephone, L.P. d/b/a/ SBC Missouri ("SBC Missouri") petition for competitive classification of its services. My testimony establishes the existence of effective competition from wireless providers in the St. Louis, Kansas City and Springfield metropolitan areas. I base my conclusion on Missouri-specific evidence—including surveys of both wireline and wireless customers—as well as my general expertise. This evidence of competition from numerous wireless providers is in addition to the evidence of competition from CLECs and other sources that SBC Missouri is citing in this proceeding.

Q. WHAT ARE THE MAIN POINTS THE COMMISSION SHOULD TAKE FROM YOUR TESTIMONY?

A. The Commission should take the following main points from my testimony:

- Wireless services are available from at least seven different providers in the St. Louis, Kansas City and Springfield metropolitan areas and are widely used by residents in a substantial majority of Missouri households;
- The wireless services being offered are substitutable at comparable rates, terms and conditions to basic local service offered by SBC Missouri and Missouri consumers indeed do see them as substitutes; and

- The existence of these wireless alternatives will help ensure that consumers are charged reasonable rates by SBC Missouri in the absence of regulation because a majority of Missouri consumers believe that wireless service is a satisfactory alternative.

Q. WILL YOU SUMMARIZE THE KEY FINDINGS OF THE SURVEYS OF MISSOURI CONSUMERS YOU RELY ON?

A. Yes. The key findings are as follows:

- 18 percent of wireless customers do not have traditional telephone service in their homes; furthermore, of the remainder that still use traditional telephone service:
  - 64 percent nevertheless frequently use their cell phones in their homes to make and receive calls; 16 percent use their cell phones as their primary home phone;
  - 72 percent believe that cellular service would be a satisfactory replacement for *all* the calls that they make or receive in their homes;
- There is a wireless user in 70 percent of households; in those households:
  - 56 percent frequently use their cell phones in their homes; 7 percent use their cell phones as their primary home phone;

- Consumers use their cell phones in their homes to make and receive both local and long-distance calls, with about one in four using cell phones primarily to make and receive local calls;
- 61 percent believe that cellular service would be a satisfactory replacement for *all* the calls that they make or receive in their homes; and
- 26 percent have considered discontinuing traditional telephone service and relying entirely on their cell phones.

3. EVIDENCE OF WIRELESS AVAILABILITY AND SUBSTITUTABILITY

Q. ON WHAT EVIDENCE DO YOU BASE YOUR CONCLUSION THAT WIRELESS SERVICES ARE AVAILABLE IN THE ST. LOUIS, KANSAS CITY AND SPRINGFIELD METROPOLITAN AREAS?

A. I rely on a range of evidence. In the first place, I understand that SBC Missouri currently has interconnection agreements with 14 wireless carriers in Missouri. The major wireless carriers currently serving Missouri are Verizon, Alltel, Cingular, AT&T, Sprint, T-Mobile, Nextel and U.S. Cellular.[1] Of these eight providers, all but two offer service in all three metropolitan areas.[2] Verizon

[1] This does not include companies operating in Missouri, such as Virgin Mobile, which re-brand or resell the wireless services of these carriers. These firms provide additional competition, but I have chosen not to include them since their "service footprints" would be the same as the carrier whose services they were reselling. This also does not include other regional wireless carriers that operate in Missouri such as Mid-Missouri Cellular.

[2] Cingular is partly owned by SBC Missouri's parent company, SBC Communications. The merger of Cingular and AT&T Wireless has just been approved by the federal government. Even if these two firms

operates in St. Louis and Kansas City, but not in Springfield. Alltel offers service in Springfield, but not in the St. Louis and Kansas City metropolitan areas.

In addition, in an exhibit to this testimony, I have included printouts from the websites of these carriers demonstrating that they offer service in these metropolitan areas. In that same exhibit, I have also included some examples of the advertising for these wireless providers carried in local newspapers. *See* Shooshan—Schedule 2.

Finally, as I discuss in greater detail subsequently, we have surveyed consumers in all three metropolitan areas and have determined that they subscribe to wireless services provided by these carriers.

Q. IN GENERAL TERMS, PLEASE DESCRIBE HOW WIRELESS SERVICE PROVIDES A SUBSTITUTE FOR WIRELINE BASIC LOCAL EXCHANGE SERVICE.

A. Wireless service is a substitute for wireline basic local exchange service in two respects. In the first place, wireless service can provide a substitute for the wireline connection. As discussed in greater detail below, some consumers are actually disconnecting—or never connected in the first place—wireline phones in favor of wireless phones. This can be referred to as "line substitution." For some time, this has been happening with second lines, but it is now also occurring with

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are not considered, there are at least five other wireless providers serving each of the three metropolitan areas.

primary lines. Even consumers who choose not to drop their wireline connections know they have a choice.

Second, there is also growing evidence that even those consumers who elect to retain a wireline connection are using their wireless phone more and more for voice calling within their homes. This is what I refer to as "usage substitution."

Q. CAN YOU RELATE THE TWO TYPES OF SUBSTITUTION YOU HAVE JUST DISCUSSED TO THE APPROACH THIS COMMISSION HAS TAKEN TO DETERMINE WHETHER SERVICES ARE SUBSTITUTES?

A. Yes. This Commission has long recognized that services may be substitutes without being the "same" or "equivalent." *See* Case No. TO-93-116, Public Service Commission of the State of Missouri, 1992 Mo. PSC LEXIS 23 at 5 ("Case No. TO-93-116"). This view is consistent with economic thinking. Two goods may be substitutes, even though one good may have certain features that the other one lacks and thus be preferred by some consumers.[3] Indeed, different features are expected to satisfy different preferences.[4]

[3] Michael L. Katz and Harvey S. Rosen, *Microeconomics*, Second Edition (Boston: Richard Irwin Inc., 1994) at 32-33, 63, where the concepts of substitutes and complements, including "perfect" substitutes and complements, are discussed. Katz and Rosen broadly consider substitute pairs such as Toyota and Honda vehicles; coffee and tea; and air conditioners and fans (at 63) (hereinafter, Katz and Rosen).

[4] Many producers engage in product differentiation, recognizing that different features appeal to different consumers. In "vertical differentiation," producers' goods are unanimously perceived as distinguished by their quality differences, reflected in price differences. For example, a Mercedes Benz and a Hyundai would be examples of two products that are vertically differentiated. In "horizontal differentiation," producers place their products along a continuum based on differences in features that the relevant set of goods might have. Prices will likely vary among horizontally differentiated goods as well. A pickup truck and a passenger car would fit this model of differentiation, as would wireless and wireline services. *See*, for example, a brief explanation in Stephen Martin, *Advanced Industrial Economics* (Blackwell: 1993) at 261.

Consider an analogy to competition in the automobile industry. There are many models of vehicles offered by various manufacturers at a range of prices. However, these vehicles also differ in size, safety features, fuel consumption, frequency of repair and included options. Yet, in economic terms, it is clear that the largest SUV is a substitute for the smallest compact car in terms of their primary function—transportation. Some people value interior size and safety over fuel consumption and ease of parking. Thus, those consumers will pay a different price to get what they want than other consumers who have different preferences and/or needs. But in each case, consumers are purchasing a means of transportation.

Thus, even though wireline and wireless services differ in some characteristics, they are still substitutes and compete with each other for many of the same customers. Those differences may simply cause a customer to choose one over the other based on personal preferences. Further, a good may be broadly conceived of so as to include a wide range of products that could be considered substitutes. As Katz and Rosen state simply: "Intuitively, substitutes are goods that satisfy *about the same want*, so that, if one becomes more expensive, the consumer turns to the other" [emphasis added]. They also point out that goods need not be "perfect substitutes" (i.e., where one good is completely abandoned for the other good).[5]

[5] Katz and Rosen at 63.

This Commission is also of the view—correctly, I believe—that there are a number of factors that go into determining whether or not two services are substitutes and that no one factor (e.g., market share) should be determinative. Case No. TO-93-116 at 5.

Q. HOW DOES SUBSTITUTABILITY FACTOR INTO THE FINDING THE COMMISSION MUST MAKE IN THIS PROCEEDING?

A. One of the factors enumerated in the statute for determining whether there is effective competition for a particular service is the extent to which the services of other providers are functionally equivalent *or substitutable* at comparable rates, terms and conditions. *See* Section 386.020(13).

Q. WHAT EVIDENCE CAN YOU POINT TO THAT WIRELESS IS A SUBSTITUTE FOR BASIC TELEPHONE SERVICE?

A. I begin by observing how wireless carriers are offering their services in Missouri. *See generally* Shooshan—Schedule 2. The design of many wireless calling plans, coupled with the functionality of the service, makes them effective substitutes for basic local exchange service. These plans typically include various-sized "buckets" of minutes that can be used for "any distance calling" (i.e., local and long distance) coupled with unlimited minutes for certain time periods (e.g., nights and weekends). Wireless plans usually include numerous vertical features such as Caller ID and Call Waiting as part of the standard package. Wireless phones are now offered "free" with many plans and many carriers no longer

require long-term contracts. Others are offering pre-paid plans that are attractive for occasional users or those without an adequate credit history.

Nationally, I observe that the prices for wireless service have fallen rapidly in recent years, driven down by increased competition. The price differences one observes between wireline and wireless service offerings are, for the most part, superficial. When one makes a true "apples-to-apples" comparison, some existing wireless packages are priced comparably to popular wireline packages offered by SBC Missouri. If one takes into account all of the vertical features, larger local calling areas and, in some cases, long-distance calling allowances built into wireless plans, the price points are quite comparable. Also, in order to make an "apples-to-apples" comparison, one has to take into account the additional value from features such as portability and immediate activation inherent in wireless service.

For example, in Missouri, cell phone plans are available at prices as low as $19.99 a month, with popular plans running $39.95 a month. *See* Shooshan—Schedule 2. The T-Mobile Basic Plan ($19.95) is aimed at "budget-conscious customers who need a phone for light daily use and emergencies."[6] This plan includes 60 "whenever minutes" and 500 "weekend minutes" that can be used for local and long-distance calls. It includes: Voicemail with Paging, Caller ID, Conference Calling, Call Waiting and Call Hold, Customer Care, Directory Assistance, Emergency Calls, and Detailed Billing. By comparison, the $39.95

[6] http://www.t-mobile.com/plans/NationalRatePlanDetails.asp?PlanID=3182.

plans provide for up to 400 "anytime minutes" and unlimited "in network" calling.

Not surprisingly, the increased value of wireless calling plans, coupled with the advantage of portability and the improvements in service quality that have come with new digital technology, has spurred substitution of wireless service for wireline service. Nationally, the number of wireless phones is approaching that of wireline phones. According to the International Telecommunications Union, wireless phones represent 43 percent of all phones in use in the United States, up from 37 percent in 2000.[7]

The FCC has recognized for some time the increasing substitution of wireless service for wireline service. In its 2002 report on the mobile wireless industry, the FCC noted studies that estimate that between 3 percent and 5 percent of wireless subscribers had disconnected their wireline phone.[8] Significantly, a year later the FCC found that there is "much evidence that consumers are substituting wireless service for traditional wireline communications."[9] Earlier this year, the

[7] "Millions doing away with their landline phones," *USA TODAY* (8/4/03) at www.usatoday.com/ tech/news/ 2003=08=04-cell-only_x.htm.

[8] FCC, In the Matter of Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; *Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services* (rel: July 3, 2002), FCC 02-179, at 32 (www.wireless.fcc.gov.cmrs_crforum.html).

[9] FCC, In the Matter of Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; *Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services* (rel: July 14, 2003), FCC 03-150, at ¶102 (8th *CMRS Report*) (www.wireless.fcc.gov.cmrs_ crforum.html).

FCC noted that the *2004 Current Population Survey of the Census Bureau* estimates that 5 to 6 percent of households now only have wireless phones.[10]

The Yankee Group, which regularly conducts research on wireless communications markets, reported a year ago that 12 percent of 18-to-24-year-olds have gone "totally wireless" for their phone service and as many as 28 percent more plan to do so over the next five years.[11] Nationally, one prediction is that nearly 30 percent of *all* wireless subscribers will not have a wireline phone by 2008.[12] These trends were supported by an article earlier this year in the *Kansas City Business Journal* which reported on Missourians who were "cutting the cord."[13]

The phenomenon of people "cutting the cord" is prevalent enough to have confounded public opinion pollsters in this important election year. One report stated that "…one of the hottest topics among pollsters is their inability to reach

[10] FCC, *Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services* (rel: September 28, 2004), FCC 04-111, at ¶212 (*9th CMRS Report*) (http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-04-216A1.pdf)

[11] Yankee Group News Release, "Twelve Percent of U.S. Young Adults Are Totally Wireless, According to the Yankee Group" (August 5, 2003). A senior analyst for the Yankee Group concludes that "[t]he mobile phone has become the essential means of communications, making the landline phone a supplemental and increasingly non-essential item, particularly among young adults and college students who are often not at home and who frequently change addresses."

[12] Josh Long, "Landline Displacement to Increase as More Wireless Subscribers Cut Cord",In-SatMDR Press Release (February 25, 2004) (http://www.instat.com/press.asp?Sku=IN0401644MCM&ID=895).

[13] Charlie Anderson, "Wireless Cuts Stranglehold of Local Carriers," *The Business Journal of Kansas City (*February 9, 2004) (http://kansascity.bizjournals.com/kansascity/stories/2004/02/09/story2.html).

cellular phone customers who are dropping their home phone lines in favor of going entirely wireless."[14]

The FCC acknowledges claims by wireline telecommunications carriers that the numbers of access lines and of minutes of use on their networks have decreased as a result of increasing use of mobile services.[15] The FCC acknowledges an analyst's report that "wireless cannibalization remains a key driver of [ILEC] access line erosion." The FCC also recognizes that usage substitution is increasing, with 23 percent of voice minutes being carried by wireless providers, up from 7 percent in 2000.[16]

A 2004 study by J.D. Power and Associates found that wireless calling (along with email, Instant Messaging and VoIP) was displacing local telephony for a substantial portion of local calls; that is, these other "platforms" were being used for local communication that otherwise would have been made as voice calls on the telephone network.[17] For example, J.D. Power found that, for consumers between the ages of 25 and 34, wireless calling accounted for 21 percent of their local communications, with email and Instant Messaging accounting for another 13 percent.

[14] "Pollsters can't connect with cell phone users," *The Arizona Republic* (January 4, 2004) (found at *The Detroit News* website: http://www.detnews.com/2004/politics/0401/04/a07-25519.htm.). This same story notes that the FCC restricts pollsters from using random dialing equipment to call cell phones. David Moore, senior editor for the Gallup poll, talked about the likely impact: "In the future, as more and more households drop their land-line phones and rely on cellular phones, we pollsters will indeed have to reevaluate our telephone methodology" (http://www.zogby.com/Soundbites/ReadClips.dbm?ID=9590).

[15] *8th CMRS Report* at ¶103.

[16] *9th CMRS Report* at ¶213.

[17] J.D. Power and Associates, *2004 Residential Wireline & ISP Study* (conducted late 1st quarter, 2004).

The trends in wireless substitution can be expected to accelerate now that number portability has been implemented. In November 2003, the FCC adopted a rule requiring wireline carriers to permit customers to transfer their wireline phone numbers to wireless carriers.[18] This is yet another indication that wireline and wireless service are considered substitutes.

The national trends are confirmed by the survey research on wireless usage that I have directed here in Missouri.

4. SURVEY OF MISSOURI CONSUMERS: METHODOLOGY AND RESULTS

Q. WOULD YOU PLEASE DESCRIBE THE METHODOLOGY YOU EMPLOYED FOR THE SURVEY?

A. Yes. Two different questionnaires were used. One was administered to wireline customers, and the other, to wireless customers. The wireless survey was undertaken to ensure representation of the increasing number of wireless customers who no longer have (or never had) wireline telephone service in their homes.

Each of the questionnaires was administered by telephone during the months of September and October, 2004. Respondents were located in Missouri in the metropolitan areas of Kansas City, St. Louis and Springfield. For the purposes of these surveys, the metropolitan areas were defined as the same geographic coverage as the Metropolitan Calling Area ("MCA") plans.

[18] FCC News Release, "FCC Clears Way for Local Number Portability Between Wireline and Wireless

The interviews were conducted by Knowledge Systems & Research ("KS&R"), a firm with extensive experience conducting surveys related to telecommunications. I directed the design of the questionnaires, in consultation with KS&R.

A simple random sample was selected in each of the three metropolitan areas (with additional screening questions, as described below) for both the wireline study and the wireless study. The sampling goal was to have at least 200 wireline and 200 wireless interviews in each metropolitan area, for a total of 1,200 interviews. In actuality, a few extra interviews were administered and are included in the results. This large number of interviews ensures that the sampling error will be acceptably small. (Sampling errors for each question are given in Shooshan—Schedule 3.)

The wireline sample was selected for each metropolitan area from the list of NPA-NXXs shown in Table 3-1 in Shooshan—Schedule 3. I understand that the geographic areas served by these NPA-NXXs correspond to the MCA areas in Missouri.

The wireline study includes a screening question that inquires whether the household is served by SBC Missouri. If not, the interview is terminated and not included in the study. This screening question was included to ensure that the survey results apply to SBC Missouri customers, rather than to the population as a whole.

Carriers" (rel. November 10, 2003).

Both surveys included a screening question about the age of the respondent. If the respondent was less than 18 years old, the interview was terminated and not included in the study. The goal of this screening question was simply to ensure that the questions were answered by adults, not by children.

The wireless sample was selected for each metropolitan area from the list of NPA-NXXs shown in Table 3-2 in Shooshan—Schedule 3. Wireless carriers have been assigned these NPA-NXXs, and they have designated points of presence ("POPs") for them in the three metropolitan areas.

Wireless customers do not, however, necessarily reside in the metropolitan area of the wireless carriers POP. For that reason, we included a screening question regarding the zip code of the respondent's home. If the zip code is not on the list shown in Table 3-2 in Shooshan—Schedule 3, the interview was terminated and not included in the study. I understand that geographic areas spanned by these zip codes are approximately the same as those spanned by the NPA-NXXs in Table 3-1. Thus, the geographic areas represented by the wireline and wireless surveys are approximately the same (and the same as the metropolitan areas as defined by the MCA plans).

Q. HOW ARE THE SURVEY RESULTS REPORTED?

A. Survey results are given below for both the wireline and wireless surveys. Results for each the two surveys are reported both in aggregate and separately for the three metropolitan areas. The numbers I present in this testimony are the aggregate numbers, but separate results for each of the three metropolitan areas

are reported in Shooshan—Schedule 3. The range of sampling errors is given for each question.

Q. WOULD YOU PLEASE SUMMARIZE THE RESULTS OF THE SURVEY PRESENTED IN SHOOSHAN—SCHEDULE 3?

A. The survey yielded a number of important results. First, 18 percent of wireless phone users said they did not have wireline service at their home (Q3). As another gauge of substitutability, 86 percent of the wireless respondents who did not have wireline service in their homes said that they would choose to have wireline service in their home if they did not have their wireless phone (Q13).

The survey of wireline customers was equally revealing. That survey showed that 61 percent of wireline residence customers surveyed who also use cellular service say that cellular would be a satisfactory substitute for *all* the calls they make and receive in their home (Q11).

The survey of Missouri consumers also confirms the trends in the substitution of wireless usage for wireline usage. We asked both wireless and wireline respondents whether they made or received phone calls on their wireless phone in their homes. 16 percent of the wireless users surveyed who have retained a wireline connection said that they primarily use their cell phones when making calls from their homes (Q7). 70 percent of wireline respondents said a cellular phone is used by the household (Q3). 56 percent of those respondents indicated that they use either their cell phone—or their cell phones and their wireline phone interchangeably—for making and receiving calls at home (Q6). Clearly, these

consumers are substituting wireless calls for calls that otherwise would have been made from their traditional home phones.

Finally, a significant portion of consumers give out *only* their wireless phone number to their contacts. Of wireless respondents who still subscribe to basic telephone service, 26 percent give out only their cell phone number while 45 percent give out both (Q9). 12 percent of wireline households in which there is a wireless user give out only their wireless number while 37 percent give out both (Q8).

The point of all these observations is that, in addition to those Missouri consumers who have elected not to subscribe to or have disconnected basic telephone service, Missouri consumers are making and receiving calls on their wireless phones that they would otherwise have made and received on their wireline phones. These users see wireless calling as a *substitute* for wireline calling, not merely a *complement*. While these users typically make and receive some calls away from home, the fact is that they are additionally using their cell phones *at home* as a substitute for basic telephone service. This is further evidence consumers consider wireless service as a competitive alternative to SBC Missouri's basic telephone service.

5. EFFECTIVE COMPETITION FROM WIRELESS SERVICES

Q. IN YOUR OPINION, HOW WILL THE PRESENCE OF THESE WIRELESS ALTERNATIVES AFFECT THE RATES THAT SBC

MISSOURI CAN CHARGE FOR BASIC SERVICE IN THE ABSENCE OF PRICE REGULATION?

A. Although it is not possible to quantify precisely, it is clear that SBC Missouri is losing lines to wireless providers. As I noted previously, nearly one in five wireless users in Missouri does not have traditional wireline telephone service in his or her home. In both surveys, of those customers who still have wireline service, one in four has considered dropping that service entirely. The fact that SBC Missouri subscribers *have* dropped—or chosen not to subscribe to—SBC Missouri's basic local service in favor of a wireless alternative and that they have considered substituting wireless for wireline service demonstrates, in my opinion, that the prices of wireless services can be expected to constrain the prices of SBC Missouri's basic local service in the absence of regulation.

Any changes SBC Missouri makes in its retail rates will have to take into account wireless competition and customers' ability to shift their voice calling to any one of several alternative providers, especially as prices for these wireless alternatives continue to decrease and their capabilities continue to expand.

Q. IS THIS TRUE EVEN THOUGH THERE ARE A SUBSTANTIAL NUMBER OF CONSUMERS WHO, ALTHOUGH THERE IS A CHOICE, MAY DECIDE TO RETAIN BASIC TELEPHONE SERVICE BASED ON THEIR PERSONAL PREFERENCES?

A. Yes. Wireless service need not be seen as a substitute by every consumer—or even a majority of consumers—in order for the prices of wireless service to

constrain SBC Missouri's pricing of basic telephone service. For a firm to exercise market power, it must be able to raise prices *profitably.*[19] If a substantial number of customers would substitute wireless service for basic telephone service should SBC Missouri increase the price of the latter, SBC Missouri cannot *profitably raise its prices.* Where, as is the case in Missouri, a large enough subset of consumers see wireless as a substitute, are using wireless phones for a significant portion of their calling from home today and have already considered disconnecting home wireline service, SBC Missouri knows that it will risk losing those consumers (and the considerable revenue they generate including access revenues, toll revenues and revenues from vertical features) to wireless providers if it raises basic telephone service prices. This likelihood serves to protect *all* consumers—even those who are *not* inclined to switch to wireless.

6. CONCLUSION

Q. WHAT CONCLUSION DO YOU REACH REGARDING WIRELESS AS EFFECTIVE COMPETITION FOR THE BASIC TELEPHONE OFFERINGS OF SBC MISSOURI?

A. I believe that the existence of no fewer than seven wireless providers in the St. Louis, Kansas City and Springfield metropolitan areas currently provides effective competition for the basic telephone offerings of SBC Missouri. Based on the surveys I have overseen of Missouri consumers, it is my opinion that a

[19] Katz and Rosen at 420.

substantial percentage of those consumers see wireless as a substitute for traditional telephone service. Coupled with the evidence of other competition presented by SBC Missouri, I conclude that consumers will be charged reasonable rates for basic telephone service by SBC Missouri if price regulation is withdrawn.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes.