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IDAHO PUBLIC
UTILITIES COMMISSION

Mary S. Hobson, ISB #2142
Stoel Rives LLP
101 S. Capitol Blvd., Suite 1900
Boise, ID 83702-5958
Telephone: (208) 389-9000
Facsimile: (208) 389-9040

Adam L. Sherr, WSBA #25291
Qwest
1600 7th Avenue, Room 3206
Seattle, WA 98191
Telephone: (206) 398-2507
Facsimile: (206) 343-4040

Attorneys Representing Qwest Corporation

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE
APPLICATION OF QWEST
CORPORATION FOR PRICE
DEREGULATION OF BASIC LOCAL
EXCHANGE SERVICES

Case. No. QWE-T-02-25

REBUTTAL TESTIMONY OF

Harry M. Shooshan III

On Behalf of
QWEST CORPORATION

APRIL 21, 2003

TABLE OF CONTENTS

<u>SUBJECT</u>	<u>PAGE</u>
I. IDENTIFICATION OF WITNESS	1
II. PURPOSE OF TESTIMONY	1
III. SUMMARY OF REBUTTAL TESTIMONY	2
IV. DR. JOHNSON'S ECONOMIC ANALYSIS IS FLAWED	3
V. WIRELESS SERVICES ARE REASONABLY AVAILABLE	6
VI. WIRELESS SERVICES ARE FUNCTIONALLY EQUIVALENT	7
VII. THE WIRELESS SERVICE OFFERINGS IN QUESTION ARE COMPETITIVELY PRICED	23
VIII. QWEST'S APPLICATION IS IN THE PUBLIC INTEREST	26

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2
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4
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I. IDENTIFICATION OF WITNESS

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND CURRENT POSITION.

A. My name is Harry M. Shooshan III. I am a principal and co-founder of Strategic Policy Research, Inc. ("SPR"), a public policy and economics consultancy located at 7979 Old Georgetown Road, Suite 700, Bethesda, Maryland 20814.

Q. HAVE YOU PREVIOUSLY PROVIDED TESTIMONY IN THIS PROCEEDING?

A. Yes. I filed direct testimony in this proceeding on December 17, 2002.

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. My testimony rebuts portions of the testimony of Wayne Hart and Ben Johnson filed on behalf of the Staff of the Commission. In particular, I offer rebuttal on claims made by Mr. Hart and Dr. Johnson that the wireless services available throughout the seven exchanges in

1 Boise, Caldwell, Idaho Falls, Meridian, Nampa, Pocatello
2 and Twin Falls do not provide the functional equivalent of
3 basic local exchange service, that these wireless services
4 are not competitively priced and that these offerings will
5 not constrain the rates that Qwest elects to charge for
6 basic local exchange service, thereby making the relief
7 being sought by Qwest in this proceeding not in "the
8 public interest."

9

10 **III. SUMMARY OF REBUTTAL TESTIMONY**

11 **Q. WILL YOU PLEASE PROVIDE AN OVERVIEW OF YOUR**
12 **REBUTTAL TESTIMONY?**

13 A. Yes. My rebuttal testimony demonstrates that,
14 contrary to Staff's assertions, competition from wireless
15 services in the seven exchanges satisfies the statutory
16 standard for price deregulation of Qwest's basic local
17 exchange service in those exchanges. Further, while
18 wireless and wireline services offer a variety of
19 different features and capabilities, they are functional
20 equivalents when it comes to making and receiving voice
21 telephone calls. I discuss how Dr. Johnson misapplies
22 certain economic concepts in his analysis or offers only

1 very narrow interpretations of these concepts that are
2 largely unsupported by any authority. I then rebut Dr.
3 Johnson's unsupported assertions that wireless service is
4 a complement to—not a substitute for—basic local exchange
5 service. Next, along with Mr. Teitzel and Dr. Lincoln, I
6 respond to the arguments of Staff that wireless services
7 are not competitively priced with basic local exchange
8 service. Finally, I respond to Staff's view that the
9 "public interest" should be construed so as to form a
10 basis for rejecting this application by Qwest that clearly
11 satisfies the statutory requirements. I conclude that the
12 level of wireless competition now present in these seven
13 Idaho exchanges is sufficient to support a determination
14 by the Commission that Qwest's basic local exchange
15 service should be deregulated.

16

17 **IV. DR. JOHNSON'S ECONOMIC ANALYSIS IS FLAWED**

18 **Q. WHAT IS YOUR VIEW OF DR. JOHNSON'S ECONOMIC**
19 **ANALYSIS OF THE ISSUES IN THIS PROCEEDING?**

20 **A.** While Dr. Johnson invokes relevant economic
21 concepts, he often misapplies those concepts or offers
22 only very narrow interpretations. For example, in his

1 discussion of substitute and complementary goods, Dr.
2 Johnson offers no support for the conclusions he reaches.
3 Contrary to Dr. Johnson's view, two goods may be substi-
4 tutes, even though one good may be preferred over the
5 other by some consumers because of certain features it
6 possesses.¹ Indeed, different features are expected to
7 satisfy different preferences.² As I discuss below, Dr.
8 Johnson's enumeration of the differences between wireless
9 and wireline services is simply illustrative of the
10 different features they possess that may cause a customer
11 to choose one over the other depending on that customer's
12 personal preferences.

¹ 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. Unlike Dr. Johnson, these well-known economists broadly consider substitute pairs such as Toyota and Honda vehicles; coffee and tea; and air conditioners and fans (at 63). (hereinafter, Katz and Rosen.)

² Many producers engage in product differentiation, meaning that their products are placed in the market space according to their features, and different features would 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.

1 Further, contrary to Dr. Johnson, a good may be
2 broadly conceived of so as to include a wide range of
3 products that could be considered substitutes. As Katz
4 and Rosen state simply: "Intuitively, substitutes are
5 goods that satisfy about the same want, so that, if one
6 becomes more expensive, the consumer turns to the other"
7 [emphasis added]. They also point out that goods need not
8 be "perfect substitutes" (i.e., where one good is com-
9 pletely abandoned for the other good).³ Yet, Dr. Johnson
10 never acknowledges this possibility in his discussion of
11 economic principles.

12 Dr. Johnson also introduces economic concepts that
13 have little or no bearing on the issues in this proceed-
14 ing. For example, he offers "an economist's concept of
15 effective competition" [Johnson at 21-22] for which he
16 provides no support in the economic literature⁴ and which

³ Katz and Rosen at 63.

⁴ Indeed, his "economist's concept of effective competition" is not widely shared. See, for example, F.M. Scherer and David Ross, "The Welfare Economics of Competition and Monopoly," *Industrial Market Structure and Economic Performance* (Houghton Mifflin Company, Boston: 1990) at 52-55, for an enumeration of the characteristics of "workable competition" (as "effective competition" is often called in economic literature). Dr. Johnson asserts that effective competition requires that no one firm have a dominant market share. Scherer-Ross, a widely used text in graduate economics courses, says nothing about this. Additionally, Dr. Johnson believes that it is important that the products are "reasonably uniform," whereas Scherer-Ross, as well as
(footnote continued)

1 introduces a number of factors that are not referenced in
2 the statute being applied in this proceeding.

3 The Commission must carefully consider Dr. Johnson's
4 use of economic concepts. He sometimes misapplies the
5 concepts he raises and also introduces concepts that have
6 no relation whatsoever to the finding the Commission is
7 directed by the statute to make in this proceeding.

8

9 V. WIRELESS SERVICES ARE REASONABLY AVAILABLE

10 Q. DO MR. HART AND DR. JOHNSON DISPUTE THE FACT
11 THAT WIRELESS SERVICES ARE REASONABLY AVAILABLE IN THE
12 SEVEN QWEST EXCHANGES THAT ARE THE SUBJECT OF THIS
13 PROCEEDING?

14 A. No. Mr. Hart effectively concedes that wireless
15 is reasonably available in the seven exchanges except for
16 some unspecified "minority" of customers who may not be
17 able to receive wireless signals. [Hart at 27.] Even if
18 Staff's concerns about a few randomly-located pockets of

(continued)

Martin, cited above, anticipate some product differentiation. Workable competition provides a more realistic description of most markets today, as the theoretical model of perfect competition is so rare. See J.M. Clark, "Toward a Concept of Workable Competition," *The American Economic Review*, Vol. XXX, No. 2, June 1940.

1 poor wireless reception are well-founded, no witness in
2 this case has challenged the incontrovertible fact that
3 wireless service from numerous carriers offering a
4 multitude of service plans is available in nearly every
5 location within the seven exchanges. In the Burley
6 deregulation case [Docket No. USW-99-15; Order No. 28369],
7 the Commission opined that it could probably not find
8 competition to be effective and "throughout a local
9 exchange area" if fewer than half of the customers in the
10 exchange had a choice of providers. Here, even Staff
11 admits that nearly every customer in the seven exchanges
12 has access to multiple wireless providers' services.
13 Assuming the Commission intended to establish a floor of
14 50% availability by its discussion in Order No. 28369,
15 that standard is clearly met in this case.

16

17 **VI. WIRELESS SERVICES ARE FUNCTIONALLY EQUIVALENT**

18 **Q. WOULD YOU RESPOND TO THE CLAIMS BY MR. HART AND**
19 **DR. JOHNSON THAT WIRELESS SERVICES ARE NOT "FUNCTIONALLY**
20 **EQUIVALENT" TO BASIC LOCAL EXCHANGE SERVICE?**

21 **A. Yes. In the first place, Mr. Hart and Dr.**
22 **Johnson appear to be fundamentally at odds with each other**

1 on this point. Mr. Hart correctly reads the statute as
2 providing that services that are not technically the same
3 might nevertheless be substitutes for each other. [Hart
4 at 5.] A close reading of Dr. Johnson's testimony
5 suggests that he believes the statute requires two
6 services to have precisely the same attributes in order
7 for them to be substitutes—that is, *they must do all of*
8 *the same things in the same way.* [Johnson at 13.] For
9 example, Dr. Johnson suggests—without any support—that,
10 because the handsets used to make and receive wireless
11 calls are "ergonomically different" than the handsets used
12 with a wireline phone, the two services cannot be
13 functionally equivalent. [Johnson at 27.]

14 Moreover, both Mr. Hart and Dr. Johnson confuse
15 applications, features and consumer preferences that are
16 unrelated to the functionality of the service at issue in
17 this case—basic local exchange service. The Idaho
18 statute, Idaho Code §62-603(1), defines "basic local
19 exchange service" as "the provision of access lines to
20 residential and small business customers with the
21 associated transmission of two-way interactive switched
22 voice communication within a local exchange." It does not

1 incorporate connections to Internet Service Providers
2 ("ISPs") or include data services such as the transmission
3 of faxes.⁵ Thus, even if they were correct in asserting
4 that wireless service does not support Internet access or
5 facsimile—which they are not⁶—Mr. Hart's and Dr.
6 Johnson's assertions [Hart at 23-24; Johnson at 30] would
7 be irrelevant to the finding the Commission must make in
8 this proceeding.

9 The fallacy in their reasoning is illustrated by Dr.
10 Johnson's statement that Internet access connections and
11 fax transmissions "take place using sounds that occur
12 within the same frequency range as the human voice..."
13 [Johnson at 32.] Like much of what Dr. Johnson states as
14 "fact" in his testimony, this statement is not exactly

⁵ Indeed, this Commission lacks jurisdiction over both calls to ISPs and data communications. See, FCC, *Order on Remand and Report and Order, In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-Bound Traffic*, Docket Nos. 96-98 and 99-68 (rel. April 27, 2001), in which the FCC determined that traffic to ISPs was interstate traffic subject to its jurisdiction. See also, Peter W. Huber, Michael K. Kellogg, and John Thorne, *Federal Telecommunications Law* (Gaithersburg, MD: Aspen Law and Business, 1999) at 1093, where the authors discuss that the courts upheld the FCC's *Computer Inquiry II* decision in which the FCC preempted state commissions on the regulation of data communications.

⁶ See Shooshan Direct at 8-9. Although it is not relevant to the finding required in this proceeding, I note that, contrary to the Staff's assertions, wireless services do support fax communications. Mr. Teitzel explains this in greater detail in his rebuttal testimony.

1 true. Fax and Internet transmissions are not "sounds,"
2 although they can be heard if presented to a telephone
3 handset. These are electrical signals that traverse the
4 telephone network—all within the same frequency band—but
5 which carry different types of information. What any
6 particular user does with those signals depends on his or
7 her needs and preferences, and the equipment he or she
8 chooses to attach to the end of the phone line that
9 carries those signals (much in the same way that one's
10 personal preferences about what options are most important
11 determines what type and model of car one chooses to
12 purchase). The fact that the same phone line can be used
13 both to carry voice calls—which are the subject of this
14 proceeding—and to provide a fax connection or dial-up
15 Internet access is irrelevant to a finding that wireline
16 and wireless are functional equivalents in the provision
17 of local two-way switched voice calling.

18 Similarly, the fact that some households choose to
19 use extension phones—as opposed, say, to having multiple
20 phone lines [Johnson at 26]—is also not relevant in
21 determining whether the wireless services available to
22 subscribers in each of the seven exchanges can be used for

1 two-way switched voice communications and, therefore,
2 considered to be the functional equivalents of Qwest's
3 basic local exchange service.⁷

4

5 Q. DR. JOHNSON CLAIMS THAT YOU AND OTHER QWEST
6 WITNESSES MISAPPLY THE CONCEPTS OF SUBSTITUTABILITY AND
7 FUNCTIONAL EQUIVALENCY. [JOHNSON AT 9-11.] HOW DO YOU
8 RESPOND TO HIS CRITICISMS?

9 A. Dr. Johnson's discussion of these concepts is
10 muddled, mistaken and misleading. Consider the first
11 analogy he uses comparing automotive vehicles. Dr.
12 Johnson says sports cars and pickup trucks may be
13 substitutes "sometimes," but for a product to be
14 "functionally equivalent" it must be *precisely* the same
15 product. In other words, to use Dr. Johnson's example,
16 the *only* functional equivalent of a dark blue Honda Accord
17 is a light blue Honda Accord. The test Dr. Johnson would
18 have the Commission apply is one that would find services
19 "functionally equivalent" only if they were the same

⁷ As an aside, Mr. Teitzel details in his rebuttal testimony that Staff's and the Intervenor's concern about extension phones is factually incorrect (besides being legally irrelevant to this case), as wireless phones can be used in one's home or business with extensions.

1 service in every respect or were "virtually identical."
2 [Johnson at 11.]

3 Ironically, under Dr. Johnson's test, the only
4 functional equivalent of Qwest's basic local exchange
5 service would be that same service repackaged under some
6 other label. Dr. Johnson's narrow definition of
7 "functionally equivalent" in effect eliminates §62-
8 622(3)(b) as a method of demonstrating "effective competi-
9 tion" and would require Qwest in every case to prove (at a
10 minimum) that Qwest faces competition from a "facilities
11 based competitor," as required by §62-622(3)(a). This is
12 one of several instances in which Staff's advocacy seeks
13 to rewrite the Idaho statute to support its position.
14 Obviously, if the legislature had intended that subparts
15 (a) and (b) both refer to competition from competitors
16 using the same traditional landline technology used by
17 Qwest, they would not have enacted subpart (b).
18 Similarly, had the legislature intended that the only
19 "functionally equivalent service" would be the same
20 service resold by a competitor, it would have used the
21 more familiar and explicit term "resale" to describe the
22 type of competition intended.

1 Common sense—as well as economic theory—illuminates
2 Dr. Johnson's flawed reasoning. In terms of their ability
3 to transport a person from point A to point B (their basic
4 function), sports cars and pickup trucks are functionally
5 equivalent. The fact that some people also use their
6 vehicles to transport potatoes or feed grain while others
7 use their vehicles on the weekends for recreational
8 driving is a matter of customer preference, not an
9 attribute of the basic function being provided.

10 The most stunning assertion made by Dr. Johnson is
11 that, even if nearly all consumers stopped using one
12 service completely when they purchase another, one might
13 conclude that the two services were close substitutes *but*
14 *still not functionally equivalent*. [Johnson at 12.] Dr.
15 Johnson uses satellite television and cable as examples of
16 two products that are "close substitutes," but which still
17 do not count as functional equivalents despite the fact
18 that virtually all television consumers disconnect cable
19 when they purchase satellite television. Yet, if con-
20 sumers substitute one service for another—or even if they
21 know they could substitute but choose not to—it shows that
22 the services are both substitutes and equivalent in the

1 basic function they provide (in Dr. Johnson's example, the
2 delivery of multichannel video) even though they may
3 differ in some other attributes (e.g., one requires an
4 antenna while the other does not).

5 Dr. Johnson states that, if two services were
6 functionally equivalent, they would be redundant and that
7 it would be "a waste of money" to pay for both. He
8 concludes that, since most wireless users also maintain
9 wireline service, the two cannot be functionally
10 equivalent. [Johnson at 13.] He is wrong. To adapt one
11 of his many analogies, an apple and an orange each may
12 satisfy part of my minimum daily requirement for fruits,
13 but I may choose to keep both on hand because I sometimes
14 like to make apple pie. Similarly, while both wireless
15 and wireline services allow me to make and receive local
16 voice calls, I may subscribe to both for other reasons,
17 e.g., redundancy. I may have two vehicles in part so that
18 if one is in the shop or with my spouse I still have
19 access to transportation.

20

1 Q. DO YOU HAVE ANY OTHER COMMENTS ON DR. JOHNSON'S
2 OBSERVATIONS THAT WIRELINE AND WIRELESS SERVICES ARE
3 COMPLEMENTS AND NOT SUBSTITUTES?

4 A. Yes. In reaching his conclusion that wireline
5 and wireless services are complements rather than
6 substitutes, Dr. Johnson considers the concept of cross-
7 elasticity; that is, the price/demand responsiveness be-
8 tween the two services. He explains that, in the case of
9 two goods that are complements, demand for both goods move
10 in the same direction (i.e., both increase or decrease) in
11 response to a change in the price of one of the goods. In
12 the case of substitutes, when the price of one good
13 changes, demand for the other good moves in the opposite
14 direction. In other words, when goods are substitutes and
15 the price of one increases, demand for that good decreases
16 while demand for the substitute increases.

17 Applying these price/demand observations to wireline
18 and wireless services would mean that, if Dr. Johnson is
19 correct that wireless and wireline services are comple-
20 ments, when the price for wireline service increases,
21 demand for wireless service will decrease. Likewise,
22 under Dr. Johnson's theory, if the price for wireless

1 service decreases, demand for both wireless and wireline
2 services will increase. These scenarios defy logic and
3 are contrary to what we observe as industry trends; i.e.,
4 wireless usage continues to increase while wireline voice
5 usage continues to decrease.⁸

6 One does not need to conduct a formal, empirical
7 study of cross-elasticity of demand when experience tells
8 us that Dr. Johnson is wrong. With all due respect, we
9 are not talking about hamburgers and hamburger buns.
10 [Johnson at 18.] Further, the customer survey introduced
11 by Dr. Lincoln in this proceeding provides ample evidence
12 that Idaho wireline consumers in the seven exchanges view
13 wireless service as a substitute for basic local exchange
14 service. [Lincoln Direct at 32.]

15

16 Q. MR. HART SAYS THAT THE COMMISSION MUST CONSIDER
17 THE EXTENT TO WHICH WIRELINE AND WIRELESS SERVICES DIFFER

⁸ See, for example, Christine Nuzum, "Fourth Quarter Another Difficult One for Telecom Carriers," *Dow Jones Business News* (January 29, 2003); Tim Schooley, "More People are Hanging Up Land-Line Phones in Favor of Cell Phones," *Pittsburgh Business Times* (July 5, 2002); and "Wireless to Capture 25% of US Telecom Traffic by 2004 as The Low Mobility Miser Segment Ramps Up," *Strategy Analytics Insight*, Strategy Analytics (September 11, 2002).

1 AS WELL AS THEIR SIMILARITIES. [HART AT 5.] DO YOU
2 AGREE?

3 A. I suppose that is something to be considered in
4 order to determine overall functional equivalency. But
5 once again, Mr. Hart appears to be attempting to divert
6 the Commission's attention from the central issue in this
7 proceeding. While wireline and wireless services ob-
8 viously differ (for example, in the "platform" over which
9 they are delivered and the ergonomics of the handset), the
10 question the Commission must answer is whether the
11 numerous wireless services available in the seven
12 exchanges permit subscribers to perform the same function
13 as basic local exchange service. That function is to make
14 and receive local voice calls (as defined in the statute⁹),
15 to have access to emergency services, directory and
16 operator assistance, and long-distance calling, and to be
17 able to obtain a directory listing, if wanted.¹⁰ The

⁹ Idaho Code §62-603(1).

¹⁰ See Mr. Souba's Rebuttal Testimony where he cites the testimony from the Burley case in which Staff witness Cusick agreed with a similar definition of local exchange service proposed by Qwest in that proceeding.

1 evidence presented by Qwest overwhelmingly demonstrates
2 that they do.

3

4 Q. MR. HART AND DR. JOHNSON CLAIM THAT WIRELESS AND
5 WIRELINE SERVICES CANNOT BE CONSIDERED FUNCTIONALLY
6 EQUIVALENT FOR A NUMBER OF REASONS INCLUDING DIFFERENCES
7 IN SERVICE QUALITY AND ACCESS TO 911. HOW DO YOU RESPOND?

8 A. I think the Commission should look critically at
9 what Mr. Hart and Dr. Johnson say. Mr. Teitzel's rebuttal
10 testimony responds to each of the "ten key attributes"
11 that Dr. Johnson claims distinguish wireless from wireline
12 service. I limit my response to Johnson's and Hart's
13 claims about "service quality" and access to 911. As to
14 "service quality," I would point out that Mr. Hart's
15 "test" resulted in only one of fifty (or 2%) calls being
16 dropped. [Hart at 18-19]. He notes that this squares
17 with the *Consumer Reports* nationwide figures. However,
18 the most common reason for dropped wireless calls is the
19 failure of a cell site to "hand off" the call to another
20 cell site.¹¹ This is a function of mobility and can

¹¹ William Schaff, "Taking Stock: Superconductors May Become More Important with 3G Wireless," *Information Week* (November 26, 2001).
(footnote continued)

1 happen, for example, when either a calling or called party
2 is on a mobile phone and moves from a digital to an analog
3 coverage area. When the call is placed from or received
4 at a fixed location (home or business)—which is the proper
5 basis for comparison in this proceeding—there is no
6 functional difference between a wireline and a wireless
7 call in this respect. Indeed, the one dropped call out of
8 fifty that Mr. Hart experienced when dialing from his
9 wireless phone while in his office could have been placed
10 to a wireless subscriber who was moving between coverage
11 areas or cells at the time. In response to a data request
12 in this proceeding, Mr. Hart is unable to provide any
13 documentation surrounding that one dropped call to which
14 he attaches so much weight in his analysis.¹²

15 On access to 911, Mr. Hart concedes that the *Consumer*
16 *Reports* findings are inapt here since the calls in that

(continued)

From <http://www.informationweek.com/story/IWK20011120S0015>.

¹² Staff Response to Qwest Request for Production No. 9 and Staff Response to Qwest Interrogatory No. 8. On the issue of service quality, the FCC recently rejected the contention that wireline and wireless "cannot be considered economically meaningful substitutes if there are substantial quality differences between the services." See *Memorandum Opinion and Order, In the Matter of Application by Qwest Communications International, Inc. for Authorization To Provide In-Region, InterLATA Services in New Mexico, Oregon and South Dakota*, WC (footnote continued)

1 study were placed from remote locations outside the home
2 or business. [Hart at 20.] Mr. Hart and Dr. Johnson
3 concede that wireless services do provide access to 911.
4 [Ibid.] However, Mr. Hart asserts—without any
5 support—that access to 911 from the home or business may
6 be compromised by network congestion or weather-related
7 signal blockage. Network congestion can occur on both
8 wireline and wireless networks based on how they are
9 engineered. I am not clear what weather-related problems
10 Mr. Hart is referring to (he produces no references), and
11 I am unaware of there being widespread problems with
12 service at those frequencies. Indeed, in response to data
13 requests in this case, the Staff was unable to identify
14 any such problems specifically occurring in Idaho within
15 the past twelve months.¹³ Of course, there may be
16 comparable problems with wireline access to 911; e.g., the
17 deterioration of a loop over time, a line cut due to

(continued)

Docket No. 03-11 (rel. April 15, 2003) (hereinafter Qwest 271 Order)
at fn. 46.

¹³ In response to Qwest Request for Production No. 11, Staff responds that it "is not aware of any Idaho-specific evidence of Consumer's [sic] having difficulty in reaching E-911 PSAPs via wireless telephones in the past 12 months."

1 construction or a natural disaster (problems one does not
2 encounter with a wireless connection).

3

4 Q. ARE THERE OTHER DEVELOPMENTS IN THE
5 TELECOMMUNICATIONS INDUSTRY THAT SUPPORT YOUR OPINION THAT
6 WIRELESS SERVICE PROVIDES THE FUNCTIONAL EQUIVALENT OF
7 BASIC LOCAL EXCHANGE SERVICE AND UNDERCUT DR. JOHNSON'S
8 AND MR. HART'S VIEWS TO THE CONTRARY?

9 A. Yes. The FCC very recently granted petitions
10 filed by Qwest and by SBC Communications seeking relief
11 under Section 271 of the Telecommunications Act of 1996 in
12 order to provide in-region InterLATA services in New
13 Mexico and Nevada, respectively.¹⁴ In both cases, the
14 showings made by the companies under "Track A" rested on
15 the existence of wireless competition for local exchange
16 service. In the New Mexico case, the FCC found that
17 wireless service "is a commercial alternative to Qwest
18 customers."¹⁵ The FCC noted that it "had recognized in

¹⁴ See FCC, *Memorandum Opinion and Order, In the Matter of Application by SBC Communications Inc., Nevada Bell Telephone Company, and Southwestern Bell Communications Services, Inc., for Authorization To Provide In-Region, InterLATA Services in Nevada*, WC Docket No. 03-10 (rel. April 14, 2003) and Qwest 271 Order.

¹⁵ Qwest 271 Order at ¶ 20.

1 other contexts increased substitution between wireless
2 mobile telephony and local telephony service..." [emphasis
3 added].¹⁶

4 The FCC also concluded that, while there were
5 technical differences and differences in features, the
6 wireless offerings provided an alternative to the
7 telephone exchange service offered by Qwest.¹⁷ The key
8 evidence of wireless competition presented by both Qwest
9 and SBC—and relied upon by the FCC—in these 271
10 proceedings (as is the case in this proceeding) was a
11 customer survey.

12 I should emphasize that the FCC based its decision on
13 the existence of a single wireless alternative (the
14 Cricket service offered by Leap Wireless), not the
15 numerous cellular and broadband PCS offerings available in
16 the seven exchanges in this proceeding.

17

¹⁶ Qwest 271 Order at fn.53.

¹⁷ Qwest 271 Order at ¶ 18.

1 effect that price cuts are expected to return and that
2 "many plans still offer more minutes than before the
3 promotions." [Hart Exhibit 103.] A report by the INSIGHT
4 Research Corporation in January 2003 noted that prices of
5 some wireless plans have dropped dramatically.¹⁸ This is
6 behavior that apparently eludes Mr. Hart; that is, prices
7 rising and falling over time in a competitive market. A
8 report by UBS Warburg, citing industry trends, found that
9 the effective price per minute was the same across
10 wireline and mobile networks.¹⁹ This is the problem of
11 relying on a "snap-shot" view of the market as opposed to
12 looking at the market over time.

13 As to Dr. Johnson's off-hand dismissal of Leap
14 Wireless (which he acknowledges does offer an unlimited
15 local calling plan that is competitively priced with
16 Qwest's basic local exchange service) as being financially
17 troubled [Johnson at 38-39], I think he misses the point.

18 In granting Qwest 271 authority in New Mexico (as
19 discussed above), the FCC specifically rejected arguments

¹⁸ "The 2003 Telecom Industry Review: An Anthology of Market Facts and Forecasts," The INSIGHT Research Corporation (January 2003).

¹⁹ See *Mobile Communications Report*, Warren Publishing, Inc. (November 11, 2002).

1 that Cricket should not be considered as an actual
2 provider due to Leap's financial difficulties (including
3 its recent filing for protection under Chapter 11 of the
4 U.S. Bankruptcy Code). The FCC noted that there is no
5 evidence that Cricket has ceased adding customers and that
6 Leap has stated that daily operations will continue
7 normally, stores will remain open and network service will
8 not be interrupted.²⁰ In fact, there is every reason to
9 expect that Leap—and its Cricket subsidiary—will emerge
10 from Chapter 11 a stronger and even more viable competitor
11 to Qwest in the provision of basic local exchange
12 service.²¹

13 Moreover, there are many other wireless carriers
14 providing service in the seven exchanges. Among them is
15 Clear Talk which advertises its offering as "the Mobile
16 Local Phone" which "includes all your local calls."²²

²⁰ Qwest 271 Order at fn. 94.

²¹ See "Leap Moves to Reorganize Capital Structure," CBS MarketWatch (4/14/03) at <http://cbs.marketwatch.com/tools/quotes/newsarticle.asp?siteid=mktw&sid=11732&quid=%7B9BB4521C%2D9ECE%2D47BB%2DA7BB%2DA3CF%2D41ECB4B3910E%7D>.

²² See Clear Talk web site at www.clear-talk.net/T7fxc98/ and www.clear-talk.net/T7fxc98/coverage.html. I note further that Clear Talk has applied for "ETC status" in Idaho and has promised to provide unlimited local calling which is one of the Commission's requirements. Idaho Public Utilities Commission Order No. 27715, Case No. GNR-T-98-7 USF.

1 Second, many other wireless providers have plans that
2 provide generous amounts of "any distance" calling.
3 Third, I cited Leap Wireless as an example of a company
4 that has targeted its service at those who primarily make
5 local calls in order to demonstrate the wide range of
6 options provided by the numerous wireless providers
7 serving customers in the seven exchanges and did not
8 suggest that Leap was the only such option available to
9 consumers.²³

10

11 **VIII. QWEST'S APPLICATION IS IN THE PUBLIC INTEREST**

12 Q. BOTH MR. HART AND DR. JOHNSON ARGUE THAT QWEST'S
13 APPLICATION SHOULD BE REJECTED BECAUSE IT IS NOT "IN THE
14 PUBLIC INTEREST." [HART AT 40; JOHNSON AT 47.] HOW DO
15 YOU RESPOND TO THEIR ARGUMENTS?

16 A. In the first place, I would distinguish the two
17 lines of argument. Mr. Hart, I believe, is simply
18 mistaken in his view that wireless services do not—and
19 more importantly would not in the future—constrain Qwest's

²³ Indeed, as I pointed out, at least one other wireless operator, Nextel, proposes that its phone can do everything a customer needs. [Shooshan Direct at 6-7.]

1 pricing decisions. Dr. Johnson's logic is much more
2 dangerous since it would result in the public interest
3 finding "swallowing" the rest of the statute and thereby
4 frustrate the clear intent of the legislature.

5 To his credit, Mr. Hart concedes that Qwest has lost
6 some lines to wireless providers and says that it may be
7 about 3-5%—consistent with the national estimates that I
8 cited in my Direct Testimony. [Shooshan Direct at 9.] He
9 then goes on to suggest that this represents a "narrow
10 niche market" without specifically defining the charac-
11 teristics of that market. The fact that Qwest subscribers
12 have dropped Qwest's basic local exchange service for a
13 wireless alternative and that they are aware that they can
14 substitute wireless for wireline service [Lincoln Direct
15 at 28] demonstrates, in my opinion, that the prices of
16 wireless services will adequately constrain the prices of
17 Qwest's basic local exchange service in the absence of
18 regulation.

19 In fact, Mr. Hart concedes that Qwest's decision to
20 increase the "cost" of wireline service by tightening its
21 credit policy has "driven" some subscribers "to find
22 alternatives." [Hart at 29.] While he doesn't specify

1 precisely what he thinks those "alternatives" might be,
2 presumably they are chiefly wireless options. If so, his
3 observation appears to be at odds with Staff's contention
4 that wireless is a complement to—rather than a substitute
5 for—basic local exchange service

6 Dr. Johnson would go even further. He maintains that
7 "[e]ven if the majority of customers were willing to 'cut
8 the cord'," there would be some customers who would not be
9 willing to do so due to personal preferences (they prefer
10 cars to pickup trucks even though both can provide them
11 basic transportation) and, therefore, Qwest "will continue
12 to have substantial monopoly power." [Johnson at 42.] He
13 is wrong. For a firm to exercise market power, it must be
14 able to raise prices *profitably*.²⁴ If a substantial number
15 of customers would substitute wireless service for basic
16 local exchange service should Qwest increase the price of
17 the latter, Qwest cannot *profitably raise its prices*.

18 Although Qwest is not relying on the existence of
19 CLECs to make the showing required by the statute in this
20 proceeding, at least one CLEC has already collocated in

²⁴ Katz and Rosen at 420.

1 each of the seven exchanges. With CLECs present in the
2 market and actively offering service—and others able to
3 enter rapidly using unbundled network elements (“UNEs”)
4 and resale—Qwest risks significant competitive losses to
5 CLECs as well if it raises prices.

6 Both Dr. Johnson and Mr. Hart urge the Commission to
7 deny Qwest’s petition because it is clear to them that
8 Qwest *may* raise the price it charges for basic local
9 exchange service. [Hart at 39; Johnson at 43-44, 47.] As
10 we have seen with wireless providers that compete in an
11 unregulated, competitive market, prices go up and down
12 over time. To force Qwest to “commit” in advance to
13 disclose what it will or will not do with its pricing
14 freedom in order to satisfy the Staff’s concept of “public
15 interest” would eviscerate the price deregulation statute.
16 In essence, Mr. Hart and Dr. Johnson seek a determination
17 that the exercise of pricing *flexibility* (the ability to
18 drop or raise prices and package services in response to
19 market forces) is itself inconsistent with the public
20 interest and thus precludes price deregulation of basic
21 local exchange service. Again, Staff’s witnesses appear
22 to favor a reading and application of public interest that

1 is so broad that it swallows the plain meaning of the
2 statute and makes the legislature's test for proving
3 effective competition impossible to satisfy.

4

5 Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

6 A. Yes.

CERTIFICATE OF SERVICE

I hereby certify that on this 21st day of April, 2003, I served the foregoing **REBUTTAL TESTIMONY OF HARRY M. SHOOSHAN III ON BEHALF OF QWEST CORPORATION** upon all parties of record in this matter as follows:

Jean Jewell, Secretary	<u> X </u>	Hand Delivery
Idaho Public Utilities Commission	<u> </u>	U. S. Mail
472 West Washington Street	<u> </u>	Overnight Delivery
Boise, ID 83720-0074	<u> </u>	Facsimile
Phone: (208) 334-0300	<u> </u>	Email
Fax: (208) 334-3762		
<u>jjewell@puc.state.id.us</u>		

Weldon Stutzman, Deputy Attorney General	<u> X </u>	Hand Delivery
Idaho Public Utilities Commission	<u> </u>	U. S. Mail
472 West Washington Street	<u> </u>	Overnight Delivery
P.O. Box 83720	<u> </u>	Facsimile
Boise, ID 83702	<u> </u>	Email
Telephone: (208) 334-0300		
Facsimile: (208) 334-3762		
<u>Wstutzm@puc.state.id.us</u>		

Marlin D. Ard	<u> </u>	Hand Delivery
Willard L. Forsyth	<u> X </u>	U. S. Mail
Hershner, Hunter, Andrews, Neill & Smith LLP	<u> </u>	Overnight Delivery
180 East 11 th Avenue	<u> </u>	Facsimile
P.O. Box 1475	<u> </u>	Email
Eugene, OR 97440-1475		
<i>Attorneys for Verizon</i>		
<i>Executed protective agreement</i>		

John Gannon, Esq.	<u> X </u>	Hand Delivery
1101 West River – Suite 110	<u> </u>	U. S. Mail
Boise, ID 83702	<u> </u>	Overnight Delivery
Telephone: (208) 433-0629	<u> </u>	Facsimile
<i>Attorney for Meierotto, Padget, Herrick & Neal</i>	<u> </u>	Email

Dean J. Miller
McDevitt & Miller LLP
420 West Bannock Street
P.O. Box 2565
Boise, ID 83701
Telephone: (208) 343-7500
Facsimile: (208) 336-6912
joe@mcdevitt-miller.com
Attorneys for WorldCom, Inc.
Attorneys for AT&T
Attorneys for Time Warner Telecom
Executed protective agreement

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email

Dean Randall
Verizon Northwest Inc.
17933 NW Evergreen Parkway
Beaverton, OR 97006-7438
dean.randall@verizon.com
Executed protective agreement

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email

Mary Jane Rasher
10005 South Gwendelyn Lane
Highlands Ranch, CO 80129-6217
Telephone: (303) 470-3412
mjrasher@msn.com

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email

Adam Sherr
Qwest
1600 7th Avenue - Room 3206
Seattle, WA 98191
Telephone: (206) 398-2507
Facsimile: (206) 343-4040
asherr@qwest.com

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email

Clay R. Sturgis
Moss Adams LLP
601 West Riverside – Suite 1800
Spokane, WA 99201-0663

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email

Brian Thomas
TimeWarner Telecom
223 Taylor Avenue North
Seattle, WA 98109
Brian.Thomas@twtelecom.com

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email

Susan Travis
WorldCom, Inc.
707 17th Street – Suite 4200
Denver, CO 80202
Telephone: (303) 390-6333
Susan.a.Travis@worldcom.com

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email

Conley E. Ward, Jr.
Givens Pursley LLP
277 North 6th Street – Suite 200
P.O. Box 2720
Boise, ID 83701-2720
Telephone: (208) 388-1200
Facsimile: (208) 388-1300
cew@givenspursley.com
Attorneys for Idaho Telephone Association
Executed protective agreement

Hand Delivery
 U. S. Mail
 Overnight Delivery
 Facsimile
 Email



Brandi L. Gearhart, PLS
Legal Secretary to Mary S. Hobson
Stoel Rives LLP