

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of AT&T)
Communications of Michigan, Inc. for)
Commission determination of switched access)
rates pursuant to MTA 310(2).)
_____)

Case No. U-13977

DIRECT TESTIMONY

OF

MICHAEL P. GRASSO

ON BEHALF OF SBC MICHIGAN

DATED: March 4, 2004

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1 **I. INTRODUCTION AND QUALIFICATIONS**

2 **Q1. PLEASE STATE YOUR NAME AND POSITION.**

3 A1. My name is Michael Paul Grasso. I am currently employed with SBC Operations, Inc. as
4 Executive Director Consumer Marketing, where my job duties include managing the SBC
5 consumer products, including promotions, marketing communications, and sales channel
6 coordination. My current responsibilities include oversight of marketing and promotions
7 activities for toll and long distance services, including those offered in Michigan.

8 **Q2. PLEASE STATE YOUR BUSINESS ADDRESS.**

9 A2. My business address is SBC Operations, Inc., 530 McCullough, Room 7T05, San
10 Antonio, Texas 78215.

11 **Q3. PLEASE PROVIDE A SHORT DESCRIPTION OF YOUR EDUCATIONAL
12 BACKGROUND AND PREVIOUS JOB HISTORY.**

13 A3. I received a Bachelor of Arts degree in Computer Science and Applied Statistics in 1992
14 from St. Mary's University in San Antonio, Texas. In 1995, I earned a Master of Science
15 degree in Telecommunications Management from Washington University in St. Louis,
16 Missouri.

17 I have been employed with SBC companies in various capacities since 1992,
18 which have included responsibility for consumer marketing for DSL and, most recently,
19 SBC Long Distance services, the selection of retail long distance products which are
20 offered through the subsidiaries of SBC Communications, Inc.. From March 15, 2003
21 until September 30, 2003, I served as Executive Director Product and Offer Planning
22 within the SBC consumer marketing organization where I developed and implemented
23 the SBC Long Distance consumer product marketing strategy. During my tenure in that

1 position, I oversaw the planning and launch of SBC Long Distance consumer products
2 and services in Michigan. Prior to that, beginning in 2000, I served as Executive Director
3 Internet Product Marketing in which I was responsible for the sales, marketing, and
4 management of various data products including DSL, dial-up internet and broadband
5 CPE. Thus, from 2000 onwards I have had regional responsibilities for consumer
6 products within Michigan and other states.

7 This case marks the first time that I have been called upon to testify before the
8 Michigan Public Service Commission. Previously I have offered testimony to other
9 Commissions including the Federal Communications Commission ("FCC") and the
10 California Public Utilities Commission ("CPUC"). In 2002 I testified before the FCC in
11 the support of SBC Long Distance's application to provide interLATA services in
12 California. The purpose of my testimony in that proceeding was to show that the
13 promotional pricing of SBC Internet Services products was consistent with offers of other
14 competitors in the industry. My experience before the California Public Utilities
15 Commission has included filing testimony in 1998 regarding my employment as Director
16 of Diversity Marketing for SBC Operations, Inc., in a proceeding involving Pacific Bell's
17 marketing policies.

18 **II. SBC LONG DISTANCE'S GENERAL PROCEDURE FOR PRICING SERVICES**

19 **Q4. PLEASE DESCRIBE THE PROCESS BY WHICH PLANS AND PRICES WERE**
20 **CHOSEN FOR SBC LONG DISTANCE'S INTEREXCHANGE**
21 **TELECOMMUNICATIONS SERVICES AT THE TIME OF LAUNCH IN**
22 **SEPTEMBER, 2003.**

1 A4. Under federal law, SBC Long Distance is required to offer the same price, terms, and
2 conditions for each interstate telecommunications service in each state where it offers
3 such services. 47 U.S.C. § 254(g). This concept is referred to as "rate integration" and
4 essentially mandates that SBC Long Distance offer the same optional calling plans in
5 each state where it offers interstate long distance services.

6 Before we began offering interstate long distance services to Michigan customers
7 in September 2003, we had already launched long distance services in other states
8 including California, Nevada, Texas, Missouri, Arkansas, Oklahoma, and Kansas. Under
9 the requirements of rate integration, therefore, we offered the same plans and interstate
10 prices in Michigan that we were already offering in those states.

11 **Q5. HOW DID YOU CHOOSE THE LONG DISTANCE PRODUCTS, PLANS, AND**
12 **PRICES THAT SBC LONG DISTANCE ALREADY OFFERED IN OTHER**
13 **STATES?**

14 A5. In Michigan, as in every state in which we entered the interLATA long distance business,
15 we began with zero percent market share competing with national providers such as
16 AT&T, MCI, Sprint, and Talk America Nationwide; aggressive regional competitors
17 such as Sage Telecom; and hundreds of other IXC's. Our experience with interLATA
18 long distance market entry confirmed that, in order to attract customers, we needed to
19 meet the existing price competition in the marketplace. This was especially important in
20 Michigan, which is one of the most competitive areas for interLATA long distance
21 service in the SBC 13-state Telco service area as reflected in the prices competitors

1 charge for long distance service.¹ Therefore, SBC Long Distance surveyed competing
2 price plans offered by other long distance service providers before developing its own
3 long distance products and prices. We then continued to monitor the competing plans to
4 determine whether changes to our current plans and/or prices were required. In this way,
5 all of SBC Long Distance's interLATA long distance plans and prices in Michigan and
6 elsewhere were set to meet the competitive threat of the incumbent IXCs.

7 **III SBC LONG DISTANCE PRICED SPECIFIC PLANS TO MEET THE**
8 **COMPETITION**

9
10 **Q6. MICHAEL STARKEY ASSERTS THAT THE SBC "ALL DISTANCE**
11 **CONNECTION" IS AN EXAMPLE OF "AGGRESSIVE MARKETING WHICH**
12 **INCLUDE[S] PRICING PACKAGES THAT EXPLOIT THE COMPETITIVE**
13 **ADVANTAGE THEY HAVE THAT IS INHERENT IN THE CURRENT ACCESS**
14 **CHARGES ASSESSED TO THEIR COMPETITORS." (Starkey Testimony, p.11,**
15 **lines 14-16). DO YOU AGREE WITH THIS ASSERTION?**

16 A6. No, the pricing is set to compete with other packages already offered by competitors at
17 similar or lower prices, rather than being developed around the SBC access charges as
18 AT&T claims. Currently and at launch in Michigan, the SBC "All Distance Connection"
19 package provided unlimited local and long distance calling as well as voice mail, caller

¹ For example, in October of 2003, MCI offered its "Neighborhood Complete" plan at \$49.99 in Michigan but at \$55.99 in other states including Nevada, Missouri, Oklahoma, and Kansas. At the same time, the non-promotional rate of Sprint's Complete Sense Unlimited plan in Michigan was \$54.99, while in other states including Missouri, Arkansas, Oklahoma, and Kansas this rate ranged from \$60.99 to \$64.99.

1 ID, and two additional features for a short-term promotional rate of \$43.95 in Michigan;
2 the rate reverted to the regular package price of \$48.95 after 12 months. This
3 promotional rate was offered only to customers who subscribed to the All Distance
4 package through January 31, 2004. However, even before SBC Long Distance entered
5 Michigan's interLATA business, competitors were offering bundled packages at similar
6 [or even lower] rates. For example, Talk America Nationwide was already offering and
7 still offers unlimited local and long distance calling, voice mail, and a choice of twenty-
8 seven other features in Detroit for \$42.95. Sage Telecom, an aggressive competitor in the
9 SBC Southwest region, also offered, then and now, an unlimited local and long distance
10 bundle with voice mail and eight additional custom features for \$44.90 in Detroit.
11 Corecom offered a similar local and long distance bundle for just \$39.95.

12 Bigger IXC's like MCI and Sprint were each offering packages with unlimited
13 local and long distance calling that included voice mail and a host of custom features for
14 \$49.99 through the MCI Neighborhood Complete bundle and the Sprint Complete Sense
15 Unlimited II bundle; they continue to offer these plans at \$49.99. Before the SBC Long
16 Distance launch, AT&T offered similar terms (without voice mail) through its One Rate
17 USA package for \$49.95, then subsequently lowered this rate to \$48.95 where it has since
18 remained. AT&T also offers a bundle featuring unlimited long distance and unlimited
19 calling to Canada for \$54.95. These rates are similar to the All Distance Connection non-
20 promotional rate of \$48.95, noted above.

21 The SBC "All Distance Connection" package was priced to meet this competition.

1 **Q7. MICHAEL STARKEY SIMILARLY ASSERTS THAT SBC LONG DISTANCE'S**
2 **"BLOCK OF TIME" PLAN IS ANOTHER EXAMPLE OF "AGGRESSIVE**
3 **MARKETING" THAT "EXPLOIT[S] [SBC MICHIGAN'S] COMPETITIVE**
4 **ADVANTAGE." (Starkey Testimony, p.11, lines 14-16). DO YOU AGREE WITH**
5 **THIS ASSERTION?**

6 A7. No. Again, our Block of Time pricing is set to compete with other offerings and not
7 developed because of the SBC access charges. The SBC Long Distance Block of Time
8 plans provide bundles of minutes at a flat fee. As part of its launch strategy, SBC Long
9 Distance has offered short-term promotional rates on three Block of Time plans: 60
10 minutes for \$2; 200 minutes for \$5; and 500 minutes for \$10. For each of these plans, the
11 promotional overage rate was 5 cents per minute. Customers must subscribe to these
12 plans by March 31, 2004, and will keep these promotional rates for 12 months, at which
13 time the overage rates will revert to the regular price of 7 cents per minute. In addition,
14 the monthly recurring charge for the 60 minute Block of Time plan will revert to \$3. If a
15 customer used every minute at the applicable promotional rate and no more, then these
16 plans would provide long distance services for approximately 3.3 down to 2 cents per
17 minute. At the regular plan rate, the 60 minute Block of Time would provide an effective
18 rate of 5 cents per minute, if all of the plan minutes were used (and no overage minutes
19 were charged). A number of competing carriers offered comparable terms. For example,
20 Global Fibernet and Pioneer Telephone each offered long distance at \$0.029 cents per
21 minute (<http://long-distance.50megs.com>), and offer even lower rates to customers who
22 commit to paying for a certain number of minutes per month, just like the Block of Time

1 plan. Other competitors offer similar cents-per-minute deals. *See, e.g.,*
2 <http://www.telcompare.com>, <http://www.lowermybills.com>, and
3 <http://www.discountlongdistancerates.com>.

4 Once again, SBC Long Distance was a new entrant in the Michigan interstate long
5 distance business. A new entrant cannot expect to win customers away from its
6 established competitors with rates that are higher than those prevailing in the
7 marketplace. This should not surprise AT&T – on the contrary, AT&T intentionally
8 undercuts RBOC prices when entering a new market as a matter of course. As recently
9 explained by AT&T's Senior Vice President of Marketing and Sales, Kevin Crull, "[w]e
10 are not substantially pricing below the RBOC. We typically come in with our entry five
11 percent below their pricing in order to try and get some of that initial ramp-up of
12 scaling."²

13 **Q8. MICHAEL STARKEY INCLUDES SBC LONG DISTANCE'S OFFER OF**
14 **"UNLIMITED NATIONWIDE CALLING FOR ONLY \$20 PER MONTH" AS A**
15 **FINAL EXAMPLE OF "AGGRESSIVE MARKETING" THAT "EXPLOIT[S]**
16 **[SBC MICHIGAN'S] COMPETITIVE ADVANTAGE." (Starkey Testimony, p.11,**
17 **lines 14-16; p.12, lines 5-6). DO YOU AGREE WITH THIS ASSERTION?**

18 A8. No, because like the other offers, the unlimited nationwide calling plan is intended to
19 compete with other plans in the marketplace rather than exploit some imagined
20 competitive advantage. Beginning in December 2003 in Michigan, SBC Long Distance's

² Transcript of AT&T's February 25th, 2004 Analyst Meeting at 214.

1 National Connections plan has offered unlimited nationwide calling for \$20 per month
2 only to those customers who also purchased certain services such as an SBC access line
3 and certain local custom calling features. Again, somewhat similar deals were already
4 being offered in Michigan before SBC Long Distance launched. MCI offered an
5 unlimited evening calling bundle for \$17.95, with daytime calls charged at a 5 cent per
6 minute rate. AT&T offered an unlimited long distance plan for \$29.95 and another plan
7 providing unlimited calling to AT&T customers for \$19.95 where additional calls are
8 charged 7 cents per minute. AT&T also offered both Unlimited Weekend and Unlimited
9 Sunday deals for \$14.95 and \$9.95, respectively. In November 2003, Sprint announced
10 the Sprint Unlimited at Home plan which offered Sprint PCS customers unlimited
11 monthly long distance minutes from their home phone for \$15 per month. Sprint also
12 announced new wireless technology offering all Sprint PCS Wireless customers who
13 subscribed to ReadyLink press-to-talk service for \$15 per month unlimited long distance
14 calling to other ReadyLink subscribers. See Dan O'Shea, *Telephony*, "Sprint Ends
15 Suspense with P2T Launch," Nov. 17, 2003, available at
16 http://telephonyonline.com/ar/telecom_sprint_ends_suspense/.

17 As explained above, SBC Long Distance did not and could not create its long
18 distance plans and prices in vacuum. We studied the plans and rates being offered by our
19 competitors and then developed plans and rates that would allow SBC Long Distance to
20 compete as a newcomer in the business.

1 **IV. THE EFFECT OF WIRELESS SUBSTITUTION ON LONG DISTANCE**

2 **Q9. HAS WIRELESS SUBSTITUTION HAD AN EFFECT ON INTEREXCHANGE**
3 **LONG DISTANCE SERVICE?**

4 A9. Yes. The monthly minutes of wireline use per subscriber have declined from 71 minutes
5 in 1995 to a mere 41 minutes in 2002. *FCC's Statistics of the Long Distance*
6 *Telecommunications Industry*, May 2003, at 37. A variety of telecommunications
7 providers and financial analysts have attributed much of this decline to wireless
8 substitution. For example, in reporting a 10% decline in consumer long distance voice
9 volumes, Sprint attributed the majority of this loss to wireless substitution.³
10 Correspondingly, where wireline long distance minutes have dropped off, wireless
11 minutes have increased dramatically. Over the last decade, national wireless use has
12 exploded from 17 billion minutes of use in 1995 to 293 billion minutes of use in June,
13 2002. CTIA's Wireless Industry Indices, December 2002, at 202-03. We expect that,
14 within the SBC "footprint," wireless communications will continue to displace wireline
15 long distance opportunity in the future.

16 Even AT&T has acknowledged that increased wireless usage has affected its long
17 distance business. AT&T's press release announcing its 2003 fourth quarter revenues
18 admits that its 15-17 % decline in long distance consumer revenues was due in part to
19 "wireless and Internet substitution."⁴ In a conference call discussing these financial

³ Merrill Lynch, "Bell South Corp." January 27, 2003, at 5.

⁴ "AT&T Announces Fourth-Quarter and Full-Year 2003 Earnings," January 22, 2004, available at <http://www.att.com/news/item/0,1847,12777,00.html>.

1 results, a senior AT&T executive noted that "wireless substitution has been a big effect in
2 the consumer market. So this intermediation from land-line long distance to wireless has
3 been a big factor in the decline in consumer [revenues]." See AT&T Fourth Quarter 2003
4 Earnings Conference Call, available at <http://www.att.com/ir/>.

5 **Q10. WHAT EFFECT, IF ANY, DOES WIRELESS SUBSTITUTION HAVE ON SBC**
6 **LONG DISTANCE'S PACKAGES AND PRICING?**

7 A10. In planning the Michigan launch and earlier long distance launches in other states, we
8 were aware that attractive wireless plans involving bundles of minutes or flat fees were
9 displacing customer use of wireline long distance services. Wireless substitution acted as
10 another impetus to offer fully competitive long distance services and prices; unless SBC
11 Long Distance could compete at this level, gaining a foothold in the increasingly
12 competitive long distance business would be difficult. To prevent the loss of customers to
13 wireless services, SBC Long Distance must price its services with the awareness that
14 some customers are replacing their landlines with wireless services or are choosing to
15 make long distance calls from a wireless phone.

16 For example, SBC Long Distance was aware of the previously cited Sprint plan,
17 announced in November, 2003, that offered unlimited long distance calling between
18 Sprint PCS wireless subscribers to the ReadyLink Press-to-Talk technology service
19 available for \$15 per month. This wireless offer was relevant to SBC Long Distance's
20 \$20 unlimited nationwide calling offer available to those customers who purchased
21 certain services such as an access line and certain custom calling features, which SBC
22 Long Distance began offering in Michigan in December, 2003

1 **V. VOICE OVER INTERNET PROTOCOL AND ITS ANTICIPATED EFFECT ON**
2 **LONG DISTANCE**

3
4 **Q11. WHAT IS VOIP?**

5 A11. Voice over Internet Protocol ("VoIP") technology permits packetized voice traffic to be
6 sent and received in the Internet Protocol ("IP") format over the various IP platforms and
7 backbones that comprise the Internet. IP networks transport both voice and data packets,
8 allowing several services to be layered over the network and leading to greater service
9 functionality and efficiency. For instance, with IP-based technology and services, a
10 business can utilize a single broadband facility to support its voice and data traffic, thus
11 obviating the need for multiple transmission facilities in the same location. IP technology
12 also allows for the seamless and dynamic integration of various voice and data
13 applications, thus infusing voice communications with a level of functionality, control,
14 and mobility that previously did not exist.

15 **Q12. WHAT EFFECT DO YOU ANTICIPATE VOIP WILL HAVE ON THE**
16 **PACKAGES AND PRICING OF THE LONG DISTANCE INDUSTRY?**

17 A12. VoIP is quickly becoming a key competitive threat to existing providers of long distance
18 services. Independent carriers such as Vonage have rapidly grown in scale; for example,
19 Vonage currently exceeds one hundred thousand subscribers. Furthermore, the larger
20 facilities-based competitors, *i.e.*, the cable Multiple System Operators ("MSOs"), have
21 accelerated their plans to enter the voice space. Specifically, in 2003 Comcast (1)
22 announced that VoIP was one of its top five priorities for 2004; (2) filed a tariff to offer
23 circuit switched, digital phone service in Michigan; and (3) began updating its existing
24 plant infrastructure in the Detroit suburban area with VoIP equipment so that in the future

1 the plant could be used for both voice and data. Companies such as Net2Phone have
2 become more aggressive in the VoIP space by offering PC2Phone domestic long distance
3 rates at 2 cents per minute and international rates to the United Kingdom, France, and
4 Spain for as low as 5 cents per minute. Other VoIP providers such as VoEX, with offices
5 in Grand Rapids and Brighton, have already entered the Michigan market and are
6 promising that they "can reduce per minute usage charges by 40% or more."⁵

7 In addition, AT&T's own executives have stressed the enormous effect VoIP may
8 have on AT&T's business, noting that the technology "may be the killer application the
9 industry has been seeking," *See* Remarks from AT&T Conference Call re Fourth
10 Quarter, 2003 Earnings, Jan. 22, 2004, *file available at*
11 <http://www.att.com/news/item/0,1847,12777,00.html>>. AT&T's CEO Dave Dorman
12 recently remarked that "VoIP is the future. With time, investment and innovation, today's
13 telecom services will be akin to the black rotary phone of the past. This is an exciting
14 time for our industry and VoIP is lighting the flames and leading our way out of the
15 darkness." *See* "AT&T Chairman Says Competition Is the Key Driver for the
16 Communications Industry," Feb. 11, 2004, *available at*
17 <http://www.att.com/news/item/0,1847,12867,00.html>>.

18 SBC Long Distance fully expects that VoIP will have a significant effect on the
19 long distance business within the foreseeable future. We expect to monitor the services

⁵ *See* the VoEX website at <http://www.voex.com/story.htm>. VoEX's business accounts include Independent Campaign Marketing Inc of Grand Rapids. *See* <http://www.voex.com/news/20040120.htm>.

1 and pricing of competing VoIP plans, and consider adjustments to our own offerings, in
2 the same manner that we monitor the services and pricing of other competitors.

3 **VI. CONCLUSION**

4 **Q13. PLEASE PROVIDE A SUMMARY OF YOUR TESTIMONY IN THIS**
5 **PROCEEDING.**

6 A13. SBC Long Distance's plans, packages, and prices in Michigan have been developed in
7 order to compete with similar offers from competitors in Michigan. As a new entrant in
8 Michigan, SBC Long Distance needed to offer similar or lower prices than those that
9 already existed in order to compete. Several of the specific prices cited by AT&T were
10 promotional offers available for only a limited amount of time. In addition to
11 competitive wireline long distance plans and packages, SBC Long Distance must price its
12 plans and packages with an awareness of other services that compete with wireline long
13 distance products, such as wireless services and newer technologies including Voice over
14 Internet Protocol, or VoIP.

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In the matter of the application of AT&T)
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rates pursuant to MTA 310(2).)
_____)

Case No. U-13977

DIRECT TESTIMONY

OF
MICHAEL A. CARNALL

ON BEHALF OF

SBC MICHIGAN

DATED: March 4, 2004

INTRODUCTION AND PURPOSE OF TESTIMONY..... 1

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1 **INTRODUCTION AND PURPOSE OF TESTIMONY**
2

3 **Q1. PLEASE STATE YOUR NAME AND POSITION.**

4 **A1.** My name is Michael A. Carnall. I am a Senior Managing Economist at LECG; my business address is
5 2000 Powell Street, Suite 600, Emeryville, CA 94608.

6 **Q2. PLEASE DESCRIBE YOUR PROFESSIONAL QUALIFICATIONS.**

7 **A2.** I earned my Doctor of Philosophy degree in Economics from the University of Illinois at Urbana-
8 Champaign, in 1996. I also earned Bachelors and Masters degrees in Civil Engineering from Bradley
9 University in 1977 and 1986. My professional experience prior to joining LECG in 1996 includes eight
10 years of involvement in the measurement and analysis of product quality and reliability at Caterpillar Inc.
11 in Peoria, Illinois. When I left Caterpillar in 1991 to enter the doctoral program at the University of
12 Illinois, I was retained by the Company as a consultant to develop a system which gathers production
13 quality data, matches that data with the subsequent field information and examines the correlation
14 between the two experiences. At LECG, I have focused on telecommunications, including economic and
15 cost issues, and the analysis and evaluation of service quality information. I have made presentations or
16 testified before the Federal Communications Commission ("FCC") and several state Commissions on
17 issues of service quality and the appropriate cost associated with unbundled elements including the high
18 frequency portion of the loop. Before the Michigan Public Service Commission ("Commission") I
19 testified in Case No.U-12540 (*In the matter of the application of Ameritech Michigan for approval of*
20 *cost studies and resolution of disputed issues related to certain new UNE offerings*) and Case No. U-
21 12598 (*In the matter, on the Commission's own motion, to establish service quality standards, including*
22 *enforcement provisions, for Ameritech Michigan*).

23 With regard to intercarrier compensation issues, I provided expert testimony on behalf of Qwest
24 Corporation, in *Qwest Corporation, Plaintiff, vs. IP Telephony, Inc, d/b/a Mountain Solutions Telecom*
25 *Group, Inc.* (Case No.99CV8252, District Court, City and County of Denver, Colorado). While working
26 at LECG's London office I advised one of the largest wireless carriers on pricing issues, including mobile
27 termination charges, in conjunction with OFTEL's Effective Competition Review.

28 In the electric power industry, I have been involved in projects concerned with power quality and
29 transmission pricing. I have also been involved in the analysis of pricing practices and competition
30 issues related to airline alliances. My curricula vitae is attached as Exhibit R-____ (MAC-1).

31 **Q3. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

1 **A3.** In its December 9, 2003 Application for Commission Determination of Switched Access Rates Pursuant
2 to the Michigan Telecommunications Act ("MTA") Section 310(2), AT&T Communications of
3 Michigan AT&T proposes that this Commission set intrastate switched access rates at TSLRIC plus a
4 markup "not to exceed that approved by the Commission for SBC Michigan for unbundled network
5 elements and/or interconnection services." In the testimony of Ms. Cate Hegstrom and Mr. Michael
6 Starkey, AT&T states that SBC Michigan's current rates are not reasonable, provide an "unfair
7 advantage" to SBC and are "anticompetitive" in that they will allow SBC Michigan to "re-monopolize
8 the interLATA toll market" and "squeeze" AT&T and other competitors from the local market.

9 The purpose of my testimony is to evaluate AT&T's claims from economic and public interest
10 perspectives. I will also evaluate SBC Michigan's position that the Commission should continue to allow
11 SBC Michigan to mirror interstate access rates, which are in turn regulated by the FCC using a "market-
12 based" approach.

13 **Q4. PLEASE SUMMARIZE YOUR CONCLUSIONS**

14 **A4.** I find that SBC Michigan's current intrastate switched access rates comply with all of the requirements of
15 the MTA, are therefore just and reasonable, and further, are among the lowest charged by carriers in the
16 state of Michigan. As a result of my analysis regarding the possibility that SBC Michigan could engage
17 in a predatory price squeeze and "re-monopolize" the interLATA toll market, I conclude that none of the
18 economic conditions necessary for a successful "squeeze" exists and that AT&T's concern is misplaced.
19 Continued mirroring of interstate switched access rates, on the other hand, provides substantial benefits
20 by simplifying regulation and maximizing ease of administration, eliminates the incentive for and risk of
21 arbitrage, and positions IXCs to receive the intrastate benefits of any further modifications to access rates
22 or intercarrier compensation by the FCC.

23 **RATES ARE NOT EXCESSIVE OR DISCRIMINATORY**

24
25 **Q5. WHAT IS THE BASIS FOR AT&T'S REQUEST FOR REDUCTION OF SBC MICHIGAN'S**
26 **INTRASTATE ACCESS RATES?**

27 **A5.** AT&T asserts that the current SBC Michigan intrastate access rates are not reasonable, provide an
28 "unfair advantage" to SBC and are in fact "anticompetitive."¹ AT&T's basis for these assertions is that

¹ Direct Testimony of Cate Hegstrom on behalf of AT&T Communications of Michigan, Inc., *AT&T Communications of Michigan, Inc. v. Michigan Bell Telephone Company d/b/a SBC Michigan*, State of Michigan, Before the Michigan Public Services Commission, MPSC Case No. U-13977, December 9, 2003, p. 8. (Hereinafter referred to as "Hegstrom Direct"); Direct Testimony of Michael
Footnote continued on next page ...

1 the contribution margin above TSLRIC provided by intrastate access charges is "too high," and that the
2 current level of intrastate access charges may allow SBC Michigan to conduct an anticompetitive "price
3 squeeze" against its competitors. AT&T further asserts that, along with approval of SBC's Section 271
4 application, these rates put SBC in a "position to not only re-monopolize the interLATA toll market, it is
5 in an even better position to 'squeeze' AT&T and other CLECs out of the local market as well."²

6 **Q6. DOES THE MICHIGAN TELECOMMUNICATIONS ACT PROVIDE GUIDANCE FOR THE**
7 **SETTING OF SBC MICHIGAN'S INTRASTATE ACCESS RATES?**

8 **A6.** Yes, the MTA specifies both a floor and a cap for SBC Michigan's intrastate access rates. The floor,
9 specified in Section 321, requires that intrastate access rates be set at or above their estimated TSLRIC
10 cost. This requirement precludes the possibility of cross subsidization of intrastate access by other
11 services. Section 310(2) of the MTA prohibits SBC Michigan from setting intrastate access rates above
12 its interstate access rates. The MTA establishes that it is the provider which shall set the rates within
13 these two parameters, not the Commission or the IXCs: "A provider of toll access services shall set the
14 rates for toll access services."³ SBC Michigan's interstate access rates are, in turn, set in accordance with
15 the CALLS agreement, of which AT&T was a participant and signatory.⁴

16 **Q7. ARE SBC MICHIGAN'S CURRENT INTRASTATE ACCESS RATES WITHIN THE**
17 **PARAMETERS SPECIFIED IN THE MTA?**

18 **A7.** Yes, current SBC Michigan access rates meet both of these criteria, i.e. they cover TSLRIC and do not
19 exceed interstate levels, and as Ms. Hegstrom points out, rates which are set in accordance with the MTA
20 are "just and reasonable."⁵

Continued from previous page ...

Starkey on behalf of AT&T Communications of Michigan, Inc., *AT&T Communications of Michigan, Inc. v. Michigan Bell Telephone Company d/b/a SBC Michigan*, State of Michigan, Before the Michigan Public Services Commission, MPSC Case No. U-13977, December 9, 2003, p. 8. (Hereinafter referred to as "Starkey Direct").

² Hegstrom Direct, p. 10.

³ MTA §310(2).

⁴ FCC, "Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45," *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Low-Volume Long-Distance Users, Federal-State Joint Board On Universal Service*, CC Docket Nos. 96-262, 94-1, 99-249, 96-45, May 31, 2000. (Hereinafter referred to as "CALLS Order").

⁵ Ms. Hegstrom states that "Rates set in accordance with AT&T's proposal would be just and reasonable as they would be within the parameters of MTA §102, which prohibits rates below

Footnote continued on next page ...

1 **Q8. ARE SBC MICHIGAN'S CURRENT INTRASTATE ACCESS RATES EXCESSIVE?**

2 **A8.** No they are not. In fact, SBC Michigan's rates are among the lowest of all the local exchange carriers in
3 Michigan. In Exhibit R-___ (SD-1) Ms. Sandra Douglas shows that SBC Michigan's average access rate
4 of \$.005211 per minute is lower than the comparable rates of 42 of the 45 carriers identified. Indeed,
5 SBC Michigan's average access rate is less than 1/12th of the highest rate (0.062629) and less than 1/5th
6 of the rates charged by MCI (0.030526) and Sprint (0.033830).

7 **PRICING AT TSLRIC IS NOT SOUND**

8 **Q9. WOULD SETTING ACCESS AT TSLRIC PLUS A FIXED MARKUP, AS PROPOSED BY**
9 **AT&T, MEET THE CONSUMER WELFARE AND COMPETITION GOALS OF THE MTA?**

10 **A9.** No, it would not. AT&T's plan contradicts the MTA's goal, described in Section 101(2)(b), the
11 encouragement of competition, because the proposal neither allows market-based forces to establish
12 rates, nor moves current regulation in that direction. In fact, the AT&T proposal to utilize TSLRIC-plus
13 pricing is a backward step toward direct, cost-plus, rate-of-return regulation. AT&T proposes to end
14 "mirroring," which links the intrastate access rate to the interstate access rate, and which, under the
15 FCC's guidance, is a market-based approach. Accordingly, AT&T's proposal is a step back from
16 competition and toward perpetuating a type of command and control regulation that is ill-suited to
17 accommodate the rapid changes which characterize telecommunications markets.

18 AT&T's proposal also contradicts MTA goal 101(2)(c), to rely less on direct command-and-control
19 regulation and more on general state and federal law regarding antitrust, consumer protection and fair
20 trade laws to protect consumers. AT&T's proposal would perpetuate the imposition of regulatory
21 authority to hold rates at levels that would never occur (and, indeed, would not be optimal) in even the
22 most competitive of real-world markets.

23 **Q10. MS. HEGSTROM ASSERTS THAT THE BUNDLING OF LOCAL AND TOLL SERVICE BY**
24 **SBC WILL SOMEHOW BE 'BYPASSING THE PRICING LIMITATIONS IMPOSED BY THE**
25 **COMMISSION IN ITS EFFORTS TO CREATE A PRO-COMPETITIVE LOCAL EXCHANGE**
26 **ENVIRONMENT.'**⁶ **DO YOU AGREE?**

27 **A10.** I certainly do not agree. It is ironic that AT&T complains that SBC Michigan, since receiving 271
28 approval in September of 2003, is competing aggressively by offering bundled local and toll service.

Continued from previous page ...

TSLRIC, and MTA §310(2) which prohibits rates above the corresponding federal rates." Hegstrom
Direct, p. 6.

⁶ Hegstrom Direct, p.11.

1 AT&T, and all CLECs, have had the ability to offer bundled local and toll service since the passage of
2 the Telecom Act in 1996. It is the availability of unbundled network elements at regulated prices that
3 substantially reduces the effect on IXCs of SBC Michigan's access service pricing. Using UNEs,
4 CLECs, including those that are also interexchange carriers, can offer bundles of local and long distance
5 service which do not depend on SBC Michigan's originating access service. Indeed, it is my
6 understanding that such competitive packages are currently offered by several CLECs in Michigan and in
7 fact were available before SBC Michigan received its 271 approval.⁷

8 SBC is indeed competing vigorously in the long distance markets. That is one of the benefits to
9 consumers foreseen by Congress in the Telecommunications Act, and recognized by this Commission,
10 and by the FCC in approving SBC's 271 application. As noted by Mr. Starkey, "the industry is clearly
11 moving toward package offerings." That customers would prefer one stop shopping was also recognized
12 in the Telecom Act.⁸ Furthermore:

13 [S]tudies showed that 66 percent of businesses and 63 percent of consumers are interested in
14 purchasing bundles containing at least two services. According to James Mendelson, an
15 analyst with The Strategis Group and lead author of the study at that time, "[t]elecom bundling
16 is the new reality of the market. Consumers demand it, businesses demand it, and operators are
17 finally beginning to provide the service. It's now a race among carriers to become the
18 customer's one-stop communications partner. . . ."⁹

19 The FCC and this Commission recognized the value of bundling. Their concern that all competitors
20 be able to offer local service as part of their package led to the stringent requirements that SBC had to
21 meet before receiving approval to enter the long distance markets. There is no question that SBC
22 Michigan has met the requirements set by the FCC and the State of Michigan and has won the right to
23 compete in these markets. To expect SBC Michigan to compete less than vigorously would be a
24 corruption of the competitive process and would preclude the residents of Michigan from reaping the full
25 benefits of that process.

26 Moreover, AT&T's Chairman and CEO, Mr. Dorman, reported on December 11, 2003, that the
27 telecom industry is transforming from "standalone local, long distance" to "Bundled Services." He also
28 noted that as of that date, AT&T was offering bundled services in 24 states, including Michigan. As he

⁷ Grasso Direct, pp. 5-6 .

⁸ Section 271(e)(1) prohibits joint marketing of local and long distance service until 271 approval has been obtained. Telecommunications Act of 1996, Pub. LA. No. 104-104, 110 Stat.56 (1996). (Hereinafter referred to as "TA 96").

⁹ Ridley, Ahmad D., et. al, "Bundled Services: A Change in Telecommunications Service Offerings," *The Telecommunications Review* 2003,p. 41. <http://www.mitrotek.org/home.nsf/Publications/TelecommReview2003>.

1 declared, AT&T had already successfully migrated customers to bundles from stand alone services, with
2 an 85% year-over-year growth in the number of AT&T bundled customers accounting for 22% of total
3 AT&T 3Q03 consumer revenue.¹⁰ AT&T strongly reiterated this position in its press release on
4 February 25, 2004.¹¹

5 Every RBOC that is now competing in the long distance markets has met these requirements. If,
6 through vigorous competition, they are "quickly becoming some of the nation's largest long distance
7 providers,"¹² it is testimony to their ability to compete and recognize what customers value.

8 **Q11. MS. HEGSTROM ASSERTS THAT SINCE UNE PRICES ARE SET AT TSLRIC-PLUS,**
9 **ACCESS RATES SHOULD ALSO BE SET AT TSLRIC PLUS. DO YOU AGREE?**

10 **A11.** I do not. The governance model laid out by the federal Telecom Act contemplates cost-plus rates for
11 unbundled network elements, not for whole telecommunications services. It recognized that such an
12 environment would not encourage competition. The model envisions cost as the basis for prices of
13 network elements until alternatives to those elements develop. Along with the cost-based pricing of
14 UNEs, the model described by the federal Telecom Act contemplates substantial pricing freedom at the
15 service level.¹³

16 Thus, the governance model encourages free-market competition at the service level while
17 temporarily retaining regulation at the network element level to ensure that firms can enter the market
18 and compete at the service level. It is for that purpose that the Telecom Act specified market-opening
19 initiatives and mandated that prices of UNEs be based on cost. Competitors are able to enter the local
20 market and provide local exchange and exchange access services to their customers using any
21 combination of their own facilities and those of the incumbent LEC. Where CLECs can purchase UNEs
22 at regulated cost-based prices and use them in competition with the incumbent LEC, there is no need to
23 regulate prices at the service level. Service level prices are driven by market forces once local
24 competition is established.

¹⁰ Dorman Speech to the Credit Suisse First Boston Media and Telecom Week Conference on
December 11, 2003.

¹¹ "Dorman Outlines Aggressive, Continuing Transformation of AT&T as the 'World's Networking
Company,'" *AT&T News Release*, February 25, 2004.

¹² Starkey Direct, p.6.

¹³ Section 251 of TA 96 describes interconnection and unbundling, Section 252 describes pricing of
these elements. Competition, facilitated by the availability of resale and unbundled elements, is the
mechanism for setting of service prices under the Act.

1 **Q12. AT&T IMPLIES THAT MARGINS ON ACCESS SERVICE SHOULD BE THE SAME AS**
2 **MARGINS ON UNES. IS IT NORMAL FOR MARGINS TO VARY ACROSS A PRODUCER'S**
3 **LINE OF PRODUCTS?**

4 **A12.** Yes, in a market open to competition, firms set prices so that the price of each product covers at least
5 the incremental cost of the product. Prices also include a share of joint and common costs. The portion
6 of those costs born by each product is not set by some allocation scheme but rather by the market. If one
7 firm attempts to capture more of its joint and common costs from a particular product or service than its
8 competitors, customers will simply choose the competitors' products, and the firm will be forced to
9 reduce its price or its output. If it does not reduce the price of that product, it will have to increase its
10 prices on other products in order to recover all of its joint and common costs. That price increase will in
11 turn affect sales of other products and their ability to contribute to recovery of joint and common costs.
12 The final prices therefore have a range of markups over cost, which, in the aggregate, recover all costs.

13 Regulation that forces equal apportionment of joint and common costs leads to inefficient outcomes
14 that are harmful to society and the overall economy. The resulting inefficient pricing results in under
15 consumption of some products and over consumption of others, leading to less than optimal innovation,
16 deployment of infrastructure and economic growth. In general, margins will vary with the elasticity of
17 demand. The more elastic the demand, the lower the margin. Competition affects the elasticity of
18 demand seen by each supplier, i.e. more competition leads to higher elasticity. For example, a single
19 supplier of corn sees infinite elasticity, i.e. he cannot supply or withhold enough corn to affect the price.
20 In this scheme, terminating access, which has a relatively low elasticity, will naturally have a relatively
21 high markup.

22 **Q13. CAN YOU PROVIDE EXAMPLES OF PRICES WHICH HAVE WIDE VARIATION IN**
23 **MARKUP?**

24 **A13.** AT&T itself realizes that profit margins vary between services and customers. The company
25 recognizes that a higher share of its profits is obtained from the segment of "high-value customers."
26 According to Betsy Barnard, President and CEO:

27 Greater than 70 percent of our contributions comes from about 25 percent of our customers,
28 and so we are keenly focused on them...The other thing that's happening, which we're thrilled
29 about is as this loss accelerates, the customers that are going to the RBOCs are customers who
30 have a 20 percent lower revenue to spend. So our focus on the high-value customers is paying

1 off, and their focus on whatever they're focusing on is clearly advantaging us in terms of who's
2 with us at the end of the period.¹⁴

3 Prices in the automotive industry demonstrate wide variation in markup over incremental cost.
4 Many carmakers produce both luxury models as well as economy models. Economy models usually
5 have very low margins over cost. The cost of building an economy car is certainly less than building a
6 luxury car, but the difference is not as much as the sticker price would seem to indicate. According to
7 one industry analyst:

8 Consequently, vehicles that sell for upwards of \$35,000 may provide \$10,000 or more in profit,
9 while cars being sold for less than \$15,000 are not providing much, if anything, to an
10 automaker's bottom line.¹⁵

11 However:

12 Automakers consider these buyers important because they want to establish brand loyalty. For
13 example, Ford believes customers who make a Focus their first purchase will eventually move
14 up to an Explorer as their income level grows. The same holds true with Opel Astra or
15 Chevrolet Cavalier customers at GM and A-Class or Dodge Neon buyers at DaimlerChrysler.¹⁶

16 Without the ability to vary margins, luxury cars might be cheaper, but economy cars would be more
17 expensive and fewer people could afford to own an automobile. Simply put, the point is that there is
18 nothing inherently anticompetitive or anti-consumer about variations in profit margins between various
19 services and market segments.

20 **Q14. WHAT ARE THE LIKELY CONSEQUENCES OF THE REDUCTION IN INTRASTATE**
21 **ACCESS RATES PROPOSED BY AT&T?**

22 **A14.** A reduction in intrastate access rates will reduce the revenue SBC Michigan receives from that
23 source. Since its costs will not have changed, it will be necessary to replace the lost contribution by
24 increasing margins on other services or by seeking an increase in the intrastate end user common line
25 charge ("EUCL") or in basic local exchange service rates. As noted by Ms. Hegstrom, MTA Section

¹⁴ "A Presentation by Betsy Bernard, President and Chief Executive Officer," *AT&T Consumer, Salomon Smith Barney Entertainment, Media and Telecommunications Conference*, January 7, 2002.

¹⁵ Harbour, Ron, "Small-Car Profit Strategies," *Looksmart*, January 2001, http://www.findarticles.com/cf_dls/m3012/1_181/69711901/p1/article.jhtml [downloaded 2/4/2004 3:31:57 PM].

¹⁶ Harbour, Ron, "Small-Car Profit Strategies," *Looksmart*, January 2001, http://www.findarticles.com/cf_dls/m3012/1_181/69711901/p1/article.jhtml [downloaded 2/4/2004 3:31:57 PM].

1 310(6) requires AT&T to "flow through" further reductions in intrastate access charges to its end users.
2 However, the form of that flow through is not specified by that provision of the MTA.¹⁷

3 AT&T could, therefore, pass the savings through to its most favored high volume customers, and
4 therefore the majority of its customers who make few long distance calls would see little savings. The
5 additional net revenue will allow AT&T to reduce its margins on customers for whom competition is
6 strongest, those with high long distance usage. Others are unlikely to see any reduction in rate. Since
7 access rates are applied without discrimination to all minutes, the net result of a reduction is likely to be a
8 redistribution of benefits among customers, possibly from a wide spectrum of consumers to a narrower,
9 high volume long distance usage group.

10 **Q15. ARE THERE OTHER BENEFITS FROM A POLICY OF CONTINUED MIRRORING OF**
11 **INTERSTATE ACCESS RATES?**

12 **A15.** Yes there are. As I have already noted, SBC Michigan's current intrastate access rates are within the
13 parameters set by the MTA, are among the lowest in Michigan, and have declined along with interstate
14 rates as envisioned by the MTA. Continued mirroring also provides the advantage of administrative
15 simplicity which will be important if significant changes are made to the structure of access charges.
16 There are several dockets related to intercarrier compensation currently open before the FCC. For
17 example, in its NPRM *In the Matter of Developing a Unified Intercarrier Compensation Regime*, the
18 FCC states that:

19 [T]here are currently two general intercarrier compensation regimes: (1) access charges for
20 long-distance traffic; and (2) reciprocal compensation. We believe it essential to re-evaluate
21 these existing intercarrier compensation regimes in light of increasing competition and new
22 technologies, such as the Internet and Internet-based services, and commercial mobile radio
23 services ("CMRS"). We are particularly interested in identifying a unified approach to
24 intercarrier compensation—one that would apply to interconnection arrangements between all
25 types of carriers interconnecting with the local telephone network, and to all types of traffic
26 passing over the local telephone network.¹⁸

27 Such a unified regime of intercarrier compensation is likely to be substantially different from that
28 currently in place. The outcome of these dockets will affect not only the level of access charges but also
29 will decide whether carriers using some technologies, VoIP for example, will be exempt from access
30 charges. To break the mirror between interstate and intrastate access charges at this time would provide

¹⁷ §310(6) of the MTA states that: "If a toll access service rate is reduced, then the provider receiving the reduced rate shall reduce its rate to its customers by an equal amount. The commission shall investigate and ensure that the provider has complied with this subsection."

¹⁸ FCC, "Notice of Proposed Rulemaking," *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Released April 27, 2001, ¶2.

1 little, if any, benefit to Michigan consumers at the risk of creating additional administrative costs for both
2 SBC Michigan and the MPSC. These benefits of mirroring are further discussed in the testimony of Ms.
3 Douglas.

4
5 **CURRENT RATES WILL NOT LEAD TO AN ANTICOMPETITIVE PRICE SQUEEZE**
6

7 **Q16. AT&T HAS ASSERTED THAT CURRENT SBC INTRASTATE SWITCHED ACCESS**
8 **RATES WILL ALLOW SBC TO CONDUCT A PREDATORY PRICE SQUEEZE TO**
9 **"SQUEEZE ITS COMPETITORS FROM THE LOCAL AND/OR TOLL MARKET SEGMENTS**
10 **WITHIN THE STATE OF MICHIGAN."¹⁹ COULD YOU PLEASE EXPLAIN WHAT IS**
11 **MEANT BY A PREDATORY PRICE SQUEEZE?**

12 **A16.** As the FCC has pointed out: "Price squeeze developed as a complaint under antitrust law and was
13 eventually applied in the area of regulated industries."²⁰ The classic definition of a price squeeze under
14 the antitrust law is that (1) the firm conducting the squeeze has monopoly power at an upstream industry
15 level, (2) its price at this level is "higher than a 'fair price,'" (3) its price at the downstream industry level
16 is so low that its competitors cannot match the price and still make a profit, (4) thereby insuring that it
17 will achieve monopoly power in the downstream industry level as well, giving it the ability to raise
18 prices to supracompetitive levels at the downstream level without losing customers or sales.²¹
19 "Monopoly power is the power to raise price well above competitive levels before customers will turn
20 elsewhere."²² "[T]he traditional, Alcoa-type price squeeze occurs when a monopolist uses its control
21 over the *monopolized* product (e.g., ingot) to obtain a monopoly at a second industry level (e.g.,
22 sheet)."²³ Although these are legal definitions, they are based on sound economic principles.

23 The courts and commentators have frequently criticized the "price squeeze" doctrine because it is
24 highly unlikely to occur, and an alleged price squeeze may have substantial pro-competitive impacts.

¹⁹ Starkey Direct, p. 9.

²⁰ FCC, "Order on Remand," *In the matter of Joint Application by SBC Communications Inc., Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance for Provision of In-Region, InterLATA Services in Kansas and Oklahoma*, FCC 03-285, CC Docket No. 00-217, November, 12, 2003, ¶6. (Hereinafter referred to as "Kansas-Oklahoma Order").

²¹ See, e.g., *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 18 (1st Cir. 1990), (Hereinafter referred to as "Town of Concord"); *United States v. Alcoa*, 148 F.2d 416 (2nd Cir. 1945) (Hereinafter referred to as "Alcoa").

²² *Town of Concord*, supra at p.31.

²³ *Town of Concord*, supra at p.29.

1 For example, if the alleged upstream monopolist is more efficient than its rivals at the downstream level,
2 then the "price squeeze" is likely to have pro-competitive effects by removing a less efficient rival and
3 thus lowering costs and prices to consumers at the second level.²⁴ Any consideration of AT&T's claim
4 that absent a rate reduction, SBC Michigan will be able to impose a price squeeze, should therefore
5 consider the relative efficiency of the major market participants at the long distance ("LD") level,
6 including AT&T.

7 In addition, the leading commentators, Professors Areeda and Hovencamp, take the position that
8 only a price squeeze involving below-cost, predatory prices at the downstream industry level can be
9 anticompetitive and arguably unlawful.²⁵ AT&T does not claim that SBC Long Distance's pricing is
10 below-cost and predatory. Thus, under the Areeda and Hovencamp approach, the claim would fail
11 regardless of other factors.

12 **Q17. WHAT CIRCUMSTANCES ARE NECESSARY BEFORE ONE COULD IMPOSE A**
13 **SUCCESSFUL PRICE SQUEEZE?**

14 **A17.** Successful operation of a price squeeze requires several conditions. First of all, the perpetrator of the
15 squeeze must truly have a monopoly in the upstream input market. If competitors in the downstream
16 market can provide that product with alternative inputs, then there can be no squeeze. Second, the price
17 of the input must be set so high that equally efficient downstream competitors cannot make a profit and
18 thus will be forced to leave the downstream market. If they can continue to earn a profit, even using
19 revenues from other products or services, then the squeeze itself is doomed. Third, elimination of the
20 downstream competitors that relied on the input must leave the perpetrator with a monopoly in the
21 downstream market. If there are competitors in the downstream market whose product does not require
22 the "essential" input, they will continue to compete and the "monopolist" will not be able to increase
23 prices. Likewise, if there are relatively low barriers to new entry into the downstream market, then even
24 the exclusion of all existing competitors cannot give the perpetrator durable market power. Once it seeks
25 to raise its downstream price to supracompetitive levels, new entrants will flow into the market and
26 defeat its scheme.

27 The objective of the law related to price squeezes, like other antitrust laws, is to protect competition
28 and consumers, not to protect individual competitors, such as AT&T. Conduct which is simply vigorous
29 competition on the merits may well harm individual, less efficient competitors, but that conduct should

²⁴ Town of Concord, supra at p.24.

²⁵ IIIA Antitrust Law 767c (2d ed. 2002)

1 not be deemed anticompetitive unless it harms the process of competition.²⁶ Conduct cannot be
2 anticompetitive "simply because it harms competitors."²⁷ "Rather, a practice is 'anticompetitive' only if it
3 harms the competitive process."²⁸ Thus, the ultimate evil the antitrust laws are designed to prevent is not
4 harming competitors, but raising prices to consumers. If that result is not likely, then no anticompetitive
5 scheme to "re-monopolize" a market can ever succeed.

6 **Q18. MR. STARKEY IS CONCERNED THAT THE FCC HAS STATED THAT RBOCS SUCH AS**
7 **SBC HAVE THE INCENTIVE TO EXERCISE A PREDATORY PRICE SQUEEZE IN THE**
8 **INTEREXCHANGE MARKETS.²⁹ DO YOU SHARE THAT CONCERN?**

9 **A18.** I do not. While the FCC has recognized that such an incentive may exist, it has, more importantly,
10 consistently rejected claims (such as AT&T's here) that a price squeeze exists for several independent
11 reasons. In the Order approving the SBC-Ameritech merger, the FCC rejected AT&T's concerns that a
12 price squeeze would occur for three reasons: First, "adequate safeguards are in place to prevent price
13 squeezes."³⁰ In other words, the ILECs "do not have a significant ability to act on this incentive."³¹
14 Second, "the existence of price caps reduces the ability to raise prices on access."³² Third, "the presence
15 of extensive sunk facilities in both local and interexchange markets suggests that the merged firm would
16 be unable successfully to raise prices if any competitors were driven out of the market by the price
17 squeeze."³³

18 In its Order approving the Bell Atlantic-NYNEX merger, the FCC likewise found that "we believe
19 that price squeeze tactics are likely to fail under the circumstances presented here as a predatory tactic
20 aimed at eliminating competition among interexchange competitors."³⁴ One added reason for this
21 failure, according to the FCC, is that: "It is unlikely . . . that one or more of these national companies

26 Town of Concord, supra at p.31.

27 Town of Concord , supra at p.21.

28 Town of Concord , supra at p.21.

29 Starkey Direct, p. 14.

30 FCC, "Memorandum Opinion and Order," *In re Applications of Ameritech Corp., Transferor, and SBC Communications, Inc., Transferee, For Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95, and 101 of the Commission's Rules*, CC Docket No. 98-141, October 8, 1999, ¶¶ 231-35. (Hereinafter referred to as "SBC-Ameritech Order").

31 SBC-Ameritech Order, ¶ 233.

32 SBC-Ameritech Order, ¶ 234.

33 SBC-Ameritech Order, ¶ 234.

34 FCC, "Memorandum Opinion and Order," *In the Applications of NYNEX Corp. Transferor, and Bell Atlantic Corp., Transferee, for Consent to Transfer Control of NYNEX Corp. and its Subsidiaries*, FCC 97-286, August 14, 1997, ¶¶ 115-18. (Hereinafter referred to as "NYNEX Order").

1 [AT&T, MCI and Sprint] can be driven from the market with a price squeeze" and that even if it could be
2 done, "it is doubtful that the LEC's interexchange affiliates would later be able raise, and profitably
3 sustain, prices above competitive levels."³⁵

4 In addition, in the Access Charge Reform docket the FCC concludes that "we have in place
5 adequate safeguards against such [price squeeze] conduct."³⁶ The FCC also specifically relied on the fact
6 it had set the challenged rates "based on the economic costs of providing such services and facilities."³⁷
7 Thus, the rates charged for the inputs had a legitimate business purpose and could not be deemed to be
8 predatory or exclusionary. This Order also acknowledged that the FCC expected that increasing access
9 service competition would provide unaffiliated IXCs alternative sources of access that would further
10 reduce any risk of a price squeeze by an existing ILEC.³⁸

11 In its Kansas-Oklahoma Order, the FCC yet again rejected AT&T's claimed price squeeze on the
12 merits. The FCC reasoned that for Kansas, AT&T provided no evidence of its available margins and for
13 Oklahoma, its margins of 18.5% and 27% in the areas that accounted for 75% of the population in the
14 state did not support a price squeeze claim.³⁹

15 Most recently, on February 20, 2004, the FCC rejected ATT's price squeeze allegations with respect
16 to Verizon's 271 authorization for Massachusetts.⁴⁰

17 The point of these decisions is that after extensive consideration by the FCC, it has found that the
18 very price squeeze AT&T alleges here is not likely to occur. For AT&T to prevail here, or for this
19 Commission to find that access rates should be reduced in order to prevent an anticompetitive price
20 squeeze from arising, it would have to reject these FCC decisions. As the FCC has consistently found,

³⁵ Nynex Order, ¶281.

³⁶ FCC, "First Report and Order," *In the Matter of Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing End User Common Line Charges*, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, Released May 16, 1997, ¶¶276-80. (Hereinafter referred to as "Access Charge Order").

³⁷ Access Charge Order, ¶117.

³⁸ Access Charge Order, ¶280. Because the acknowledged pro-competitive impacts of a price squeeze, and other factors, there is a degree of continuing debate over some of the elements set forth in classic definition in *Alcoa*. While reserving its right to litigate the precise details of the classic elements, we draw primarily upon the classic *Alcoa* elements to show that AT&T's Application should be dismissed.

³⁹ Kansas-Oklahoma Order, ¶20.

⁴⁰ FCC, "Order on Remand," *In the matter of Application of Verizon New England, Inc., Bell Atlantic Communications, Inc. (d/b/a Verizon Long Distance), NYNEX Long Distance Company (d/b/a Verizon Enterprise Solutions) And Verizon Global Networks, Inc., for Authorization to Provide In-Region, InterLATA Services in Massachusetts*, CC Docket No. 01-9, February 20, 2004.

1 SBC Michigan has no ability to affect such an anticompetitive price squeeze, and then this argument in
2 favor of reducing switched access rates completely dissolves.

3 **Q19. DO THE CONDITIONS FOR A SUCCESSFUL ANTICOMPETITIVE PRICE SQUEEZE**
4 **EXIST IN THE MICHIGAN INTRASTATE TOLL MARKETS?**

5 **A19.** No, they do not. In fact, it is my opinion that none of the conditions required for a successful
6 anticompetitive price squeeze is present.

7 *No Monopoly in the Upstream Market*

8 AT&T's witness Mr. Michael Starkey alleges that SBC Michigan "has control over bottleneck
9 access facilities" which gives it the power "to exert pressure, or squeeze its competitors from the local
10 and/or toll market segments within the state of Michigan."⁴¹ Mr. Starkey does not define what he means
11 by "bottleneck access facilities," and he does not attempt to define the "relevant market" at this upstream
12 level. However, I interpret his testimony as suggesting that SBC Michigan has monopoly power in the
13 provision of switched access facilities in Michigan which he believes provides it with the "ability to
14 utilize access pricing to the detriment of its competitors"⁴² and thereby "create price squeezes in all
15 market segments . . . to the detriment of its competitors . . ."⁴³ While I offer no formal opinion on
16 whether switched access facilities in Michigan constitute the relevant market for purposes of analysis, it
17 is nonetheless clear to me that SBC Michigan does not have a monopoly in the asserted provision of
18 "switched access facilities" in Michigan for several reasons.

19 First, access can be, and is, provided by CLECs, whether they be facilities based or UNE based. Even
20 AT&T has admitted in this proceeding that "in some instances there might be an alternative source for
21 transport between the customer's local switch and the toll provider's point of presence [POP]."⁴⁴ For
22 many high volume users, AT&T and other IXCs use special access service or build their own dedicated
23 facilities to carry traffic between their POP and the customers' premises. In addition, the MPSC
24 recognizes the strong growth of competition in the upstream access market:

25 [B]ased on available data that staff has gathered through its surveys over the four-year period,
26 there is continued growth in the percentage share of CLEC lines in Michigan from a 4% share

⁴¹ Starkey Direct, p. 9.

⁴² Starkey Direct, p. 7.

⁴³ Starkey Direct, p. 8.

⁴⁴ AT&T Response to SBCATT0029, attached as Exhibit R-____ (MAC-2).

1 in 1999 to a 6.5% share in 2000, a 12.8% share in 2001 to a 21.7% share in 2002. This is a
2 positive trend.⁴⁵

3 Second, AT&T itself is a facilities-based CLEC which could build its own switched access
4 facilities, and by that means reduce or eliminate its alleged dependence on SBC's claimed "bottleneck"
5 facilities.

6 Third, the switched access rates in question remain subject to the statutory upper limit of interstate
7 rate levels. If interstate rates are determined to be too high by the FCC or otherwise reduced, Section
8 310(2) of the MTA provides that those same reductions be made in intrastate rates.

9 Fourth, even AT&T has now been forced to admit that: "In certain wireless/cellular scenarios, a
10 wireless call may not employ facilities deployed by wireline local exchange carriers."⁴⁶ "For example,
11 where a wireless caller calls another wireless caller in a nearby locality and the call is switched and
12 transported entirely by the wireless carrier, this call would at no time be transported using physical
13 wireline facilities of the local exchange carriers operating in that location."⁴⁷ "Similarly, where a
14 wireless caller calls another wireless caller located several states away, that call may, in many instances,
15 be carried solely on facilities operated by the originating and terminating wireless carriers and an
16 interstate long distance carrier."⁴⁸ This means that wireless calls may bypass SBC Michigan's switched
17 access services in whole or in part.

18 In the financial conference call held by AT&T to announce its 4Q03 results, on January 22, 2004,
19 AT&T's senior management conceded that: "wireless substitution has been a big effect in the consumer
20 market. So this intermediation from land-line long distance to wireless has been a big factor in the
21 decline in consumer."⁴⁹ Obviously, with wireless substitution now an admitted "big factor" for AT&T,
22 SBC Michigan's ownership of certain switched access facilities is very unlikely to give it market power
23 in the "upstream market."

24 Significantly, this Commission has noted that a trend toward migration to wireless has already
25 affected local exchange service, pointing out that recently in Michigan "the total number of customer

⁴⁵ Michigan Public Services Commission, "Report on the Status of Competition in Telecommunications Service in Michigan," June 2003, p. 9. (Hereinafter referred to as "2003 MPSC Telecom Report").

⁴⁶ AT&T response to SBCATT0012.

⁴⁷ AT&T response to SBCATT0012.

⁴⁸ AT&T response to SBCATT0012.

⁴⁹ Conference Call Transcript at 28:5-29:5.

1 lines decreased from 7.0 million in 2001 to 6.7 million in 2002, reflecting a migration to wireless, email
2 and Internet telephony.⁵⁰

3 Fifth and finally, an even newer technology is now poised to compete with traditional wireline long
4 distance services. That is Voice Over Internet Protocol or "VoIP." As AT&T's senior management
5 reported during its recent financial conference call announcing its 4Q03 results:

6 If current interest is any indication of future adoption, we're on the verge of a Voice-over-IP
7 revolution, which AT&T intends to lead at both the consumer and business level. As the
8 industry leader in carrying IP traffic, we understand the networking challenges and the industry
9 direction better than anyone. We currently have hundreds of Voice-over-IP customers of all
10 sizes and at various stages of deployment. As we previously announced, we will offer Voice
11 over IP as an option on AT&T's industry-leading VPN service by second quarter '04. We were
12 the first to offer a voice-call quality guarantee for VoIP.⁵¹

13 AT&T anticipates that the migration to VoIP could save it at least \$8-9 billion in access charge
14 payments.⁵² The prospect of the entry of VoIP into Michigan, and its current limited presence in the State
15 as an alternative means of providing voice communication, also undermines the ability of SBC Michigan
16 to exercise market power in the provision of switched access facilities in Michigan. I am aware that the
17 FCC recently ordered that computer-to-computer voice telecommunications, which do not use originating
18 or terminating switched access facilities to complete the call, constitute "an unregulated information
19 service."⁵³ Thus, pulver.com is able to provide long distance voice communications while bypassing SBC
20 Michigan's switched access facilities entirely. I also understand that AT&T itself has asked the FCC to
21 relieve it of the obligation to pay switched access rates for its long distance services using VoIP backbone
22 transport even when the calls originate or terminate over an ILEC's switched access facilities.⁵⁴

23 These facts show that however one might define the relevant upstream input market, it is highly
24 unlikely that SBC Michigan could exercise market power in the market that includes switched access
25 facilities in Michigan.

⁵⁰ 2003 MPSC Telecom Report, p. 5.

⁵¹ Conference Call Transcript at 5:25-6:12 (emphasis added).

⁵² "How VoIP Hits the Sticks," Business Week Online, March 2, 2004,
http://www.businessweek.com/technology/content/mar2004/tc2004032_2726_tc076.htm
[downloaded 3/3/2004 9:37:40 PM].

⁵³ FCC, "Memorandum Opinion and Order," *In re Petition for Declaratory Ruling that pulver.com's Free World Dialup is Neither Telecommunications Nor a Telecommunications Service*, WC Docket No. 03-45, February 19, 2004, ¶1.

⁵⁴ AT&T, "Petition for Declaratory Ruling that AT&T's Phone-to-Phone IP Telephony are Exempt from Access Charges," *In the Matter of Petition for Declaratory Ruling that AT&T's Phone-to-Phone IP Telephony Services Are Exempt from Access Charges*, WC Docket No. 02-361, October 18, 2002.

1 ***Input Prices do not Preclude Profitable Competition in the Downstream Market***

2 As noted above, price squeezes require that the price of the input is "higher than a 'fair price'" and
3 the price in the downstream market is so low that downstream competitors cannot survive. Yet, here, the
4 facts indicate that SBC Michigan's switched access rates are among the lowest of all providers in
5 Michigan. MCI and Sprint charge more than five and six times, respectively, what SBC Michigan
6 charges for the same switched access service.⁵⁵ Similarly, since the rates are set to mirror interstate rates
7 set by the FCC, it is not possible to characterize them as "higher than a 'fair price.'" Indeed, in its several
8 proceedings considering mirrored access rates, this Commission has repeatedly found such mirrored
9 rates to be just and reasonable.

10 In addition, AT&T does not even attempt to claim that it cannot make a profit in the downstream
11 market. Indeed, in discovery in this proceeding, AT&T has now admitted that "over the past twelve
12 months, taking into account all interLATA, intraLATA, interstate and intrastate long distance calls made
13 by its customers in Michigan, and all revenues received by AT&T in connection with its interstate and
14 intrastate long distance services (including without limitation fixed and minimum monthly fees) in
15 Michigan, AT&T's provision of long distance services in Michigan has been profitable."⁵⁶ Obviously,
16 the current price of SBC Michigan's switched access services does not – as the FCC put it – "doom"
17 AT&T "to failure."⁵⁷ More recently, in its February 25 investor's presentation, AT&T states, "Our long
18 distance business is big, profitable and sustainable."⁵⁸

19 As a result, the price of the alleged input in the upstream market cannot support a claimed
20 anticompetitive price squeeze.

⁵⁵ Exhibit R-___ (SD-1).

⁵⁶ AT&T Response to SBCATT0022, attached as Exhibit R-___ (MAC-2). I understand that SBC Michigan served AT&T with a number of discovery requests seeking specific information concerning the profit margins and underlying costs of toll, long distance, and other AT&T services. The responses to these requests, if required by the Commission, could provide additional information to demonstrate that AT&T's profits and profit margins are of such a magnitude that it does not need additional access rate reductions to be able to continue to profitably compete with SBC Michigan and its long distance affiliate. I am advised that there is a pending appeal to the Commission of the Administrative Law Judge's ruling denying SBC Michigan's Motion to Compel Discovery.

⁵⁷ Kansas-Oklahoma Order, ¶13.

⁵⁸ Polumbo, John, "AT&T Consumer Overview: Bending the Trends," *AT&T Investor Presentation*, February 25, 2004, slide 16, <http://att.com/ir/2004analyst/>.

1 ***No Dangerous Probability of Monopolization of Downstream Market***

2 AT&T claims that the alleged price squeeze will propel SBC Michigan to "re-monopolize the
3 interLATA toll market" and put it in a better position "to 'squeeze' AT&T and other CLECs out of the
4 local market as well."⁵⁹ Here again, as in the case of the alleged upstream market, AT&T has not
5 attempted to define the relevant market other than through these broad, self-serving assertions. As in the
6 case of the alleged upstream market, I do not offer any formal opinion on the precise contours of the
7 downstream relevant markets. Rather, for purposes of my analysis I assume that AT&T's allegations are
8 correct and that there is a downstream market that at least includes interLATA toll and another that at
9 least includes local service.

10 The available facts show that these potential "markets" are highly competitive and face every
11 increasing consumer substitution of newer technologies – all of which deprive SBC Michigan of the
12 ability to exercise market power.

13 First, market data show fierce competition within the interLATA and intraLATA toll segments in
14 Michigan. SBC Michigan's share of these segments is lower than AT&T's share was in 1995 when the
15 FCC concluded that AT&T was not a dominant carrier.⁶⁰ Second, wireline long distance usage has
16 shrunk substantially over the last decade, while capacity has increased. Third, barriers to entry in these
17 segments are low. Finally, as I will discuss in detail following this section, consumers are increasingly
18 substituting wireless and VoIP services for traditional wireline interLATA and intraLATA toll services.
19 These facts effectively prevent SBC Michigan from exercising market power in the downstream toll
20 "markets."

21 **InterLATA And IntraLATA Toll Segments:**

22 AT&T has already admitted that "the market for the sale of wireline toll services at retail in
23 Michigan is very competitive."⁶¹ Over 200 toll providers presently operate in Michigan.⁶² Nationally,
24 according to the most recent FCC data, in 2001, AT&T had 37.4% of all "Toll Service Revenues," while

⁵⁹ Hegstrom Direct, p. 10. .

⁶⁰ FCC, "Order," *In the Matter of Motion of AT&T Corp. to Be Reclassified as a Non-Dominant Carrier*, Released October 23, 1995. (Hereinafter referred to as "AT&T Reclassification Order").

⁶¹ AT&T Response to SBCATT0001, attached as Exhibit R-___ (MAC-2). AT&T qualified this response: "[T]o the extent the phrase 'very' is intended to be more or less synonymous with 'significant and long-standing' as stated by Ms. Hegstrom in the referenced testimony, AT&T admits that the market for the sale of wireline toll services at retail in Michigan is very competitive." *Id.*

⁶² AT&T Response to SBCATT0001, p. 2, attached as Exhibit R-___ (MAC-2).; AT&T Response to SBCATT0003, attached as Exhibit R-___ (MAC-2).

1 SBC has less than 1%.⁶³ For 2002, among residential households, the FCC reports that AT&T had
2 36.7% while SBC had 3.8%.⁶⁴ While the FCC does not report state figures, with respect to households in
3 the Mid-West Region in 2002, the FCC reports that AT&T had 40.9%, whereas SBC had 0.3%.⁶⁵ These
4 "market" share numbers are significant because the SBC shares fall far below the roughly 60 percent
5 market share that AT&T enjoyed at the time the FCC declared it non-dominant in interstate, domestic,
6 interexchange telecommunications services.⁶⁶

7 **Increased Capacity and Decreased Use:**

8 In addition, the wireline industry has undergone a transformation over the past decade, with
9 "Average Residential Monthly Toll Minutes" of all types plummeting from 143 in 1995 to 90 in 2002.⁶⁷
10 This decline has occurred despite a glut of long haul capacity that has multiplied from 6 million
11 kilometers of long haul fiber in 1996 to 36 million kilometers of fiber deployed in 2001.⁶⁸ As AT&T has
12 previously admitted, such a level of excess capacity makes it nearly impossible to gain monopoly power
13 in the long distance services.⁶⁹

14 Finally, as toll providers have had to work harder to maintain market share as capacity increased
15 and minutes of use declined, competition has increased and consumer prices have generally gone down.
16 For example, the average interstate and international revenue per minute, restated in 2001 dollars, has
17 declined from \$0.55 in 1984 to \$0.20 in 1995 to \$0.10 in 2001.⁷⁰ This is not the picture of a "market"
18 that has been or is likely to be monopolized.

19 **Low Entry Barriers:**

20 It is axiomatic that low barriers to entry or re-entry will prevent any incumbent participant in a
21 market from exercising market power. The reason is, as one court has explained it, "[i]f it is easy to

⁶³ FCC, Industry Analysis & Technology Division, Wireline Competition Bureau, *Statistics of the Long Distance Telecommunications Industry*, Table 7, May 2003. (Hereinafter referred to as "2003 FCC Long Distance Report").

⁶⁴ 2003 FCC Long Distance Report. Table 14.

⁶⁵ 2003 FCC Long Distance Report. Table 15.

⁶⁶ AT&T Reclassification Order, ¶62, n.173.

⁶⁷ 2003 FCC Long Distance Report, Table 20.

⁶⁸ KMI Corp., "Fiber optics Networks of Long Distance Carriers in North America: Market Developments and Forecast," A-1, November 1999.

⁶⁹ "AT&T contends that, because supply is elastic, it cannot possess or exercise market power," *AT&T Reclassification Order*, ¶45; Furthermore, "AT&T contends that, because excess capacity controlled by facilities-based carriers could be used to provide virtually any type of long-distance service, no interexchange carrier can charge supra-competitive rates for any service," *Id. at* ¶48.

⁷⁰ 2003 FCC Long Distance Report at Table 5.

1 enter the [market], [the firm's] scheme is doomed to failure: any attempt to recoup by charging
2 supracompetitive prices . . . simply will attract new (or old) [rivals] who will undercut [the firm] and
3 force prices back down to competitive levels."⁷¹

4 AT&T has now admitted in this proceeding that "in comparison to barriers to entry into some
5 markets within the telecommunications industry it can be said the barriers to entry into the market for the
6 sale of wireline toll services at retail in Michigan are relatively low."⁷² This admission by itself is
7 sufficient to demonstrate that SBC Michigan is highly unlikely to "re-monopolize the interLATA toll
8 market" as AT&T's witnesses assert here.⁷³ Moreover, this admission is not new. AT&T has long
9 conceded that "there are virtually no barriers to entry . . . into the interexchange market."⁷⁴

10 **Local Exchange Competition:**

11 According to the most recent statistics issued by the MPSC, SBC Michigan's share of Michigan
12 local exchange lines decreased by nearly one fourth in just three years, declining from 81 percent in 1999
13 to 62.9 percent in 2002.⁷⁵ While the number of CLECs providing local exchange service in Michigan
14 has doubled during that time from 25 to 54, their market share has multiplied more rapidly, with their
15 percentage of lines increasing steadily from a mere 4 percent in 1999 to 21.7 percent in 2002, as
16 illustrated by the following chart.

17 **Table 1**
18 **Michigan Local Exchange Statistics⁷⁶**
19

	1999	2000	2001	2002
Licensed CLECs	120	167	173	219
CLECS providing service	25	37	52	54

71 *See, e.g.,* Advo, Inc. v. Philadelphia Newspapers, Inc., 51 F.3d 1191, 1200 (3d Cir. 1995).

72 AT&T Response to SBCATT0002, attached as Exhibit R-___ (MAC-2).

73 Hegstrom Direct, p. 10.

74 AT&T, "Reply Comments," *In the Matter of Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations*, CC Docket No. 79-252, June 30, 1995, ¶23.

75 2003 MPSC Telecom Report, p. 5.

76 2003 MPSC Telecom Report, p. 5. FCC data for Michigan generally confirms these CLEC statistics, and further demonstrates that CLEC percentages of end-used switched access lines in Michigan outpaced the nationwide average since December, 2001. *See* FCC, "Local Telephone Competition: Status as of June 30, 2003," *FCC Wireline Competition Bureau*, Released December 2003, Table 7. (Hereinafter referred to as "2003 FCC Local Competition Report"). While the report does not show RBOC local exchange percentages, it confirms that Michigan ILECs' total number of local exchange lines have continued their decreasing trend from June 2000 through June 2003. *See Id.* at Table 9.

Total Lines in MI	6,726,971	6,901,813	7,014,263	6,668,124
CLEC %	4%	6.5%	12.8%	21.7%
SBC %	81%	78%	72.2%	62.9%

1
2 The Commission has also noted that because "virtually all" of CLEC entry in the local market
3 through 2002 has occurred within SBC Michigan's territory, "[a]s a percent of the SBC market, the
4 CLEC market share is therefore approximately 26%."⁷⁷ AT&T itself attained particular success in the
5 local exchange market: according to Chairman and CEO David Dorman, AT&T "[a]chieved 6% market
6 share in Michigan in just 5 months."⁷⁸

7 This vigorous transfer of market share from SBC Michigan to CLECs is inconsistent with
8 SBC Michigan having the ability to exercise market power with respect to local telecommunications
9 services. If market power means anything, it means having the ability to retain one's market share. In
10 antitrust terms, courts have found little danger of monopolization where competitors have "steadily been
11 eating away" the allegedly dominant player's share of the market where, for example, its share dropped
12 from 93 to 75 percent over a two-and-a-half year period.⁷⁹ The MPSC reached a consistent conclusion in
13 its 2003 report, finding that the "positive trend" in CLEC lines between 1999 and 2002 demonstrated a
14 "continued robust growth in competitive local lines in Michigan" which established that "a viable
15 competitive market in telecommunications services has been achieved and that competition continues to
16 grow."⁸⁰

17 **Consumer Substitution:**

18 As discussed further below, wireless carriers provide the most prevalent form of competition to
19 traditional wireline local and long distance service. In just the last five years, wireless subscribership

⁷⁷ Michigan Public Service Commission, Staff Report, "Results of 4th Competitive Market Conditions Survey, Case No. U12320," May 2003, p. 2.

⁷⁸ Presentation by David Dorman, *UBS Warburg Global Telecom Conference*, at 8 (2002).

⁷⁹ *United States v. Syfy Enterprises*, 903 F.2d 659, 666 (9th Cir. 1990). Note that although 75% is an even higher market share than SBC Michigan's percentage here, the Ninth Circuit encouraged the government to "plot these [market share] points on a graph and observe the pattern they form [rather] than to focus narrowly on Syfy's market share at a particular time." *Id.*

⁸⁰ 2003 MPSC Telecom Report, 8; "Supplemental Report of the Michigan Public Service Commission," *In the Matter of the Application Filed by SBC Communications, Inc., et al., for Provision of In-Region, InterLATA Services in Michigan*, Case No. 03-138, July 2, 2003, pp. 4, 10.

1 grew from 23 percent to 60 percent of the U.S. population above age 15;⁸¹ average price per minute
2 dropped 70 percent;⁸² and average usage per subscriber increased from approximately 100 to 500
3 minutes per month. ⁸³ Voice over Internet Protocol ("VoIP") service provides another alternative to
4 wireline service. These substitutes undercut the ability of any competitor offering wireline local or LD
5 services from exercising market power. If any such competitors sought to raise prices to supra-
6 competitive levels, consumers would merely flock to the lower priced substitute.

7 **Q20. WHY ARE SERVICES SUCH AS WIRELESS VOICE TELECOMMUNICATIONS AND**
8 **VOIP SERVICE RELEVANT IN CONSIDERING WHETHER AN ALLEGED PRICE**
9 **SQUEEZE IS LIKELY TO OCCUR AND LIKELY TO PROPEL SBC MICHIGAN TO "RE-**
10 **MONOPOLIZE INTERLATA TOLL" OR LOCAL SERVICES AS AT&T ASSERTS?**

11 **A20.** These new technologies are relevant for two reasons: First, since they allow competing sellers of
12 long distance voice communications services to effectively bypass SBC Michigan's switched access
13 services in whole or in part, they reduce or eliminate the opportunity for the wireline switched access
14 provider to impose the alleged price squeeze. Second, since consumers are increasingly substituting
15 other technologies for traditional wireline services, it highly unlikely that any provider of traditional
16 wireline local or LD services could ever achieve or exercise monopoly power in wireline local or LD
17 services. If consumers can switch to an alternative technology for essentially the same service, then the
18 providers of the traditional wireline services can never successfully raise prices to supracompetitive
19 levels while retaining their customers.

20 It is also important to consider products which are not currently present in the market but would
21 appear in response to an increase in price. Such products on the edge of entry into the market can exert

⁸¹ Wireless subscribers from Cellular Telecommunications and Internet Association, ("CTIA") Semi-Annual Wireless Industry Survey, 2003, www.wow-com.com; Population data from the U.S. Census Bureau. www.census.gov.

⁸² FCC, "Eighth Report," *In the Matter of Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, Annual Report of Competitive Market Conditions With Respect to Commercial Mobile Services*, WT Docket No. 02-379, July 14, 2003, Table 9.

⁸³ FCC data is as of year-end. J.D. Power data is reported in September of each year. FCC, *Seventh CMRS Report*, p. C-12. See also "J.D. Power and Associates Reports: Wireless Usage Continues to Climb as Hat-Rate Pricing and Free Minutes Become More Prevalent in the Marketplace," *J.D. Power Press Release*, September 26, 2000; "J.D. Power and Associates Reports: Wireless Phone Penetration Among U.S. Households Climbs Above 50 Percent As More First-Time Subscribers Enter the Marketplace," *J.D. Power Press Release*, September 26, 2001; and Berman, Dennis K., "BOOMTOWN: We May Be Reaching Our Limit for Yakking On All of Our Phones," *The Wall Street Journal*, December 23, 2002.

1 strong price constraining influences on the incumbents. As a result, whether one treats VoIP as currently
2 available in Michigan as an alternative to traditional wireline services,⁸⁴ or as merely a new technology
3 that is about to begin competing with traditional wireline services, it is likely to constrain the ability of
4 the wireline incumbents from raising prices to supracompetitive levels.

5 **Q21. HOW SIGNIFICANT ARE WIRELESS TELEPHONE SERVICES TODAY?**

6 **A21.** Over the last several years, mobile wireless has become the predominant form of voice
7 communications for many consumers. As noted above, AT&T has acknowledged that "wireless
8 substitution" has had a "big effect" on the consumer LD business⁸⁵. As wireline minutes of use have
9 decreased over the past decade, wireless minutes of use have increased dramatically, from 17 billion total
10 minutes of use in 1995⁸⁶ to almost 400 billion minutes in the first half of 2003.⁸⁷ Figure 1 shows the
11 rapidly increasing wireless usage per subscriber over the last several years.

⁸⁴ AT&T intends to deploy VoIP nationwide to consumers in the top 100 markets by the end of the first quarter of 2004. Shawn Young, "AT&T to Launch Internet-Based Telephone Service," *The Wall Street Journal*, December 11, 2003; see also AT&T Response to SBCATT 0008, attached as Exhibit R-___ (MAC-2).

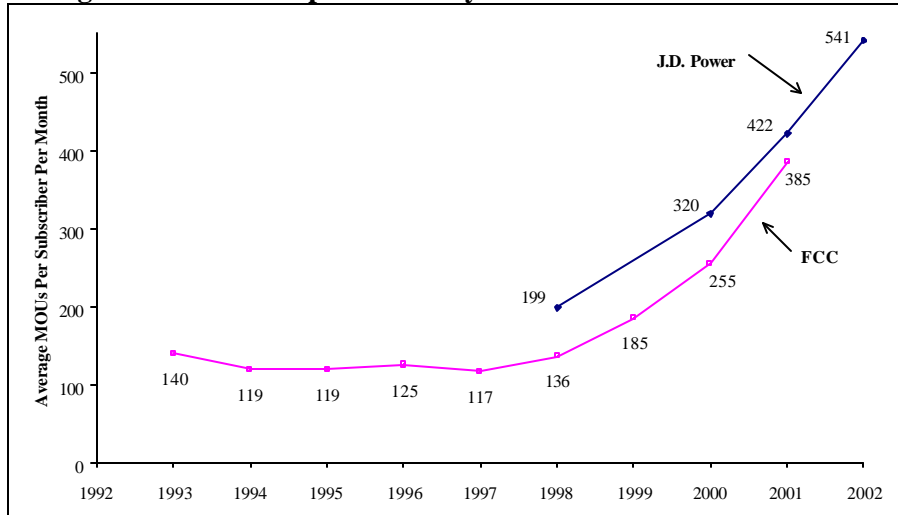
⁸⁵ Jan. 22, 2004 Transcript 28:5-29:5.

⁸⁶ CTIA's Wireless Industry Indices, December 2002, at 202-03.

⁸⁷ CTIA, Semi-Annual Wireless Industry Survey, 2003, p. 8.

1
2
3

Figure 1
Average Minutes of Use per Month by Wireless Subscribers Nationwide⁸⁸



4
5

6 As of December 2002, the number of mobile wireless subscribers in Michigan (4.5 million)
7 exceeded the number of households (approximately 4.4 million).⁸⁹ While some households do not have a
8 wireless phone, many other households have two or more wireless phones, and usage in these households
9 can exceed one thousand minutes per month.

10 Analysts and competitors agree that calls over the wireless network are displacing traditional
11 intrastate toll market calls. Sprint, for example, stated that its consumer long distance voice volumes
12 were down 10%, attributing the majority of the impact to wireless substitution.⁹⁰ Furthermore, it is
13 estimated that AT&T's consumer long distance revenues would fall 25% over year-end 2002, with more

⁸⁸ FCC data is as of year-end. J.D. Power data is reported in September of each year. FCC, *Seventh CMRS Report*, p. C-12. See also "J.D. Power and Associates Reports: Wireless Usage Continues to Climb as Flat-Rate Pricing and Free Minutes Become More Prevalent in the Marketplace," *J.D. Power Press Release*, September 26, 2000; "J.D. Power and Associates Reports: Wireless Phone Penetration Among U.S. Households Climbs Above 50 Percent As More First-Time Subscribers Enter the Marketplace," *J.D. Power Press Release*, September 26, 2001; and Berman, Dennis K., "BOOMTOWN: We May Be Reaching Our Limit for Yakking On All of Our Phones," *The Wall Street Journal*, December 23, 2002.

⁸⁹ Households estimated based on 1 percent annual growth rate. *FCC Local Competition Report 2003*, Table 13; U.S. Census Bureau, "[H]ousing unit estimates: April 1, 2000 to July 1, 2002." [Downloaded from <http://eire.census.gov/popest/data/household/HU-EST2002-01.php> on February 10, 2004].

⁹⁰ *SBC Ex-parte Presentation to the FCC on the Sunset FNRPM*, October 24, 2003, p. 11.

1 than half the decline attributable to wireless replacement.⁹¹ Citing to the Yankee Group, *RCR Wireless*
2 *News* predicted the landline displacement market could be worth as much as \$50 billion by 2006 with
3 more than 40 percent of all landline calls being usurped by wireless calls over the next several years.⁹²
4 This is an increase from less than 7% in 1999.⁹³ Survey information provides additional evidence that
5 mobile wireline usage competes with wireline local and long distance usage. For example, in its 2002
6 U.S. Mobile User Survey, the Yankee Group found that 26 percent of wireline minutes have been
7 displaced by wireless minutes.⁹⁴ The Yankee Group predicts that personal wireless calls will overtake
8 wireline calls in 2006.⁹⁵ In addition, roughly 29% of all interstate long distance traffic originated or
9 terminated on a wireless network.⁹⁶ In survey results that SBC presented to the FCC, when asked: "If
10 you're at home and you need to place a phone call, do you primarily use your cellular/PCS phone,
11 landline phone, or do you use your landline and cellular/PCS phone about equally as much?" 40% of
12 respondents reported that they primarily used their wireless phone, and 15% of respondents said they use
13 wireline and wireless equally as much.⁹⁷

14 One reason consumers freely use wireless is the "free" nationwide, as well as intrastate, long
15 distance included in many plans. AT&T Wireless offers their *National Plan 600*, advertised as one of
16 their "most popular," which, in addition to 550 "anytime" minutes which are not limited to a local toll
17 area, includes unlimited long distance calling on nights and weekends over their nationwide network.⁹⁸
18 The package is priced at \$39.99.⁹⁹ Comparable is Cingular's *Cingular Nation GSM 600*, available for
19 \$49.99. This package, which also does not discriminate between local and long distance calls,¹⁰⁰
20 includes 600 anytime minutes, 5000 "mobile-to-mobile" minutes, and 5000 nights and weekend

⁹¹ SBC Ex-parte Presentation to the FCC on the Sunset FNRPM, October 24, 2003, p. 11.

⁹² "Landline Displacement to be continued market driver," *RCR Wireless News*, November 4, 2002.

⁹³ "Carriers said to Need New Tactics to Combat LD Substitution," *Communications Daily*, March 15, 2002.

⁹⁴ Mallinson, Keith, "Landline Displacement Fuels Mobile Growth but Market Still Cries Out for Wireless Carrier Consolidation," *The Yankee Group*, October 30, 2002, Slide 9.

⁹⁵ Mallinson, Keith, "Landline Displacement Fuels Mobile Growth but Market Still Cries Out for Wireless Carrier Consolidation," *The Yankee Group*, October 30, 2002, Slide 11.

⁹⁶ SBC Ex-parte Presentation to the FCC on the Sunset FNRPM, October 24, 2003, p. 12.

⁹⁷ SBC Ex-parte Presentation to the FCC on the Sunset FNRPM, October 24, 2003, p. 13.

⁹⁸ AT&T Wireless website, <http://www.attwireless.com/personal/plans/plans.jhtml?planpage=national> [downloaded 2/9/2004 12:34:04 PM].

⁹⁹ AT&T Wireless website, <http://www.attwireless.com/personal/plans/plans.jhtml?planpage=national> [downloaded 2/9/2004 12:34:04 PM].

¹⁰⁰ This is provided that you are on Cingular's Preferred Wireless Network.

1 minutes,¹⁰¹ altogether, many more minutes than the average person spends on a wireless phone. AT&T,
2 and perhaps others, recently announced that all on-network calls are free.¹⁰²

3 Similar to the perception of free Instant Messaging ("IM") service after purchasing on-line access,
4 consumers view unlimited (or virtually unlimited) long distance as "free" once they have purchased a
5 monthly plan. Thus, in addition to the convenience of a wireless phone, consumers naturally take
6 advantage of their free wireless minutes, leading to the displacement that we see today of calls from the
7 wireline switched network.

8 **Q22. DO YOU CONSIDER VOIP TO BE A VIABLE COMPETITOR TO TRADITIONAL**
9 **WIRELINE VOICE SERVICE?**

10 **A22.** Yes I do. It has been predicted that by the end of the decade all international voice calls will be
11 carried over VoIP¹⁰³ and some industry executives even predict that "VoIP will eventually replace the
12 circuit-switched technology that telephone networks have used for more than a century."¹⁰⁴ *The Wall*
13 *Street Journal* reported that VoIP "is almost completely unregulated for now and requires little capital,
14 and the improvements in technology make even the smallest start-ups a credible threat."¹⁰⁵ AT&T touts
15 it as the "new technology that is going to change phone service forever" and advertises its "unlimited
16 local and nationwide calling, [p]opular features like voicemail and call waiting, [i]nnovative new call
17 management services [accessible] online or on the phone, [and] [o]ne flat monthly rate for unlimited
18 local and nationwide calling and all available features, plus substantially lower international rates – no
19 surprises."¹⁰⁶ While AT&T pricing for the service has not yet been established, the company remarks
20 that "[a]ll we can say right now is that the new technology costs less than the old technology – in many

¹⁰¹ Cingular website,
<http://onlinestore.cingular.com/webapp/wcs/store...=12851&langId=1&storeAlias=detame&svcAreaId=SBC> [downloaded 2/16/2004 4:16:20 PM]

¹⁰² AT&T Wireless website:
http://www.attwireless.com/personal/plans/plans.jhtml?planpage=local&_requestid=23364 (1 of 3)
[3/3/2004 10:30:18 PM]

¹⁰³ "Supercomm is Told VOIP Is Emerging As Dominant Force," *Communications Daily*, June 3, 2003.

¹⁰⁴ Grant , Peter and Latour, Almar, "Circuit Breaker: Battered Telecoms Face New Challenge: Internet Calling—Once a Minor Player, Service Captures Growing Share of Home, Business Market—the 'Pac-Man' of Protocalls," *The Wall Street Journal*, October 9, 2003.

¹⁰⁵ Grant , Peter and Latour, Almar, "Circuit Breaker: Battered Telecoms Face New Challenge: Internet Calling—Once a Minor Player, Service Captures Growing Share of Home, Business Market—the 'Pac-Man' of Protocalls," *The Wall Street Journal*, October 9, 2003.

¹⁰⁶ AT&T website, <http://www.consumer.att.com/voip/>.

1 cases a lot less."¹⁰⁷ The President of AT&T Labs says that IP, the Internet programming language at the
2 heart of the technology "is like Pac-Man...[e]ventually it will eat everything in its way."¹⁰⁸

3 Several carriers offer VoIP, with Vonage reputed to be the largest. The company announced in
4 September that it had activated 50,000 lines on its network since launching service in April 2002.¹⁰⁹
5 Even more startling, it doubles its subscriber base every 12 weeks.¹¹⁰ *Phoneplugmag.com* cites research
6 firm In Stat/MDR forecast of 1.3 million subscribers in 2003 — a small fraction of the total U.S. voice
7 services market.¹¹¹ Vonage predicts that the current 20 million broadband homes will double to 50
8 million by 2006, giving the company ample opportunity to convert more voice customers.¹¹²

9 There is currently a filing with the FCC regarding the status of VoIP.¹¹³ Regardless of the outcome
10 of the FCC proceeding with regards to issues such as state levied fees and taxes and 911 services,
11 however, it is still obvious that consumers are increasingly able to substitute a voice conversation over
12 the switched network with a voice conversation transmitted over an IP network. The Minnesota Public
13 Utility Commission agrees with this. The FCC filing was brought as an appeal when the MPUC made
14 the following findings:¹¹⁴

15 ...The Commission finds that Vonage offers unlimited local and long distance calling as well as
16 Caller ID, Call Waiting, and Voicemail. Vonage itself holds itself out as providing all-
17 inclusive home phone service and advertises that it replaces a customer's current phone
18 company.

¹⁰⁷ AT&T website, <http://www.consumer.att.com/voip/>.

¹⁰⁸ Grant, Peter and Latour, Almar, "Circuit Breaker: Battered Telecoms Face New Challenge: Internet Calling—Once a Minor Player, Service Captures Growing Share of Home, Business Market—the 'Pac-Man' of Protocalls," *The Wall Street Journal*, October 9, 2003.

¹⁰⁹ Long, Josh, "No More Free Ride? Regulators Consider Rules for Internet Phone Companies," *Phoneplusmag.com*, December 2003, <http://www.phoneplusmag.com/articles/3c1feat04.html> [downloaded 2/5/2004 11:02:21 AM].

¹¹⁰ SBC *Ex-parte Presentation to the FCC on the Sunset FNRPM*, October 24, 2003, p. 14.

¹¹¹ Long, Josh, "No More Free Ride? Regulators Consider Rules for Internet Phone Companies," *Phoneplusmag.com*, December 2003, <http://www.phoneplusmag.com/articles/3c1feat04.html> [downloaded 2/5/2004 11:02:21 AM].

¹¹² SBC *Ex-parte Presentation to the FCC on the Sunset FNRPM*, October 24, 2003, p. 14.

¹¹³ "McCain Plans Hearing on VoIP Regulation," *TR Daily*, January 21, 2004.

¹¹⁴ Minnesota Public Utilities Commission, "Order Finding Jurisdiction and Requiring Compliance," *In the Matter of the Complaint of the Minnesota Department of Commerce Against Vonage Holding Corp. Regarding Lack of Authority to Operate in Minnesota*, Docket No. P-6214/C-03-108, September 11, 2003; Also see FCC, "Comments of the Minnesota Public Utilities Commission Regarding the Petition of Vonage Holdings Corporation for Declaratory Ruling Concerning an Order of the Minnesota Public Utilities Commission," *In the Matter of Vonage Holdings Corporation Petition for Declaratory Ruling Concerning an Order of the Minnesota Public Utilities Commission*, WC Docket No. 03-211, October 27, 2003, pp. 2-4.

1 With the Vonage service the customer uses an ordinary touch-tone phone to make calls and
2 carry on conversations. The customer must have an ISP and a computer modem. Although the
3 phone is plugged into an MTA router, which, in turn, is plugged into the modem, the consumer
4 is being provided with service that is functionally the same as any other telephone service.
5 Further, the Vonage service intersects with the public switched telephone network.

6 The Commission finds that what Vonage is offering is two-way communication that is
7 functionally no different than any other telephone service.

8 Furthermore, Vonage is not the only company vying for customers as an Internet telephone
9 company. Other such companies include Net2Phone, and, as noted above, AT&T.¹¹⁵

10 In evaluating the potential for a firm to exercise market power, the Justice Department and FTC
11 examine not only current and recent market entry, but also consider "committed entry alternatives that
12 can be achieved within two years from initial planning to significant market impact."¹¹⁶ VoIP is likely to
13 have such an effect in Michigan.

14 **Q23. MR. STARKEY ASSERTS THAT "IF THE COMMISSION ELECTS TO LEAVE THESE**
15 **RATES AT THEIR CURRENT LEVEL IT WOULD BE PROVIDING SBC WITH AN**
16 **INHERENT ADVANTAGE WHEN COMPETING AGAINST LONG DISTANCE CARRIERS -**
17 **OR CARRIERS WHO PROVIDE PACKAGE SERVICES WHICH INCLUDE BOTH LOCAL**
18 **AND LONG DISTANCE SERVICES - THROUGHOUT THE STATE OF MICHIGAN IN THAT**
19 **SBC'S PROFIT MARGINS WILL ALWAYS BE HIGHER THAN EQUALLY EFFICIENT**
20 **COMPETITORS."**¹¹⁷ **DO YOU AGREE WITH THAT STATEMENT?**

21 **A23.** I most certainly do not. Mr. Starkey's statement completely ignores the realities of the
22 telecommunications market in Michigan. First of all it ignores the almost 5 million wireless subscribers
23 in Michigan, all of whom have available "packages of local and long distance" service. It also ignores
24 the 22 percent of customers in SBC's local service territory who are served by CLECs, the increasing
25 number of customers who receive their local and long distance service through VoIP carriers, and those
26 served by providers of cable telephony. The profit margins of the carriers serving this large fraction of
27 Michigan consumers are not determined by SBC Michigan's intrastate access rates because that service is
28 a relatively minor input to the service they provide.

¹¹⁵ On December 11, 2003, David Dorman announced that AT&T would be expanding its VoIP service to consumers in the top 100 markets in the first quarter of 2004.

¹¹⁶ Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines*, April 1992, §3.2.

¹¹⁷ Starkey Direct, p. 8.

1 Furthermore, with this wide range of choices available to consumers, if SBC were to attempt to
2 increase the price of its access service in order to drive out competitors, it would only reduce its own
3 revenue in the process. SBC receives access revenue only from those carriers who require that service.
4 If the price of that input makes those carriers' services unattractive to consumers their customers will
5 migrate to one of the many carriers whose services do not rely on SBC's intrastate switched access.
6 Competition will be reduced very little so SBC would be unable to increase its prices, but its revenue
7 will be diminished because fewer calls require its access service.

8 **Q24. MR. STARKEY HAS TESTIFIED THAT "IMPUTATION" IS A "PARTIAL SAFEGUARD"**
9 **THAT DOES NOT APPLY TO SBC'S LONG DISTANCE AFFILIATE AND AS A RESULT,**
10 **"WHERE INTRASTATE INTERLATA AND INTERSTATE TRAFFIC ARE CONCERNED,**
11 **THERE IS NO PROTECTION OFFERED FROM A STATE MANDATED IMPUTATION**
12 **REQUIREMENT." HOW DO YOU RESPOND TO THAT STATEMENT?**

13 **A24.** As I understand the requirements of the federal Telecommunications Act, "imputation" is a concept
14 that Congress chose to apply when a single entity provides a service to itself. Where there is a
15 structurally separate affiliate, such as in the case of interLATA services offered by SBC Michigan's
16 affiliate, Section 272(e) of this Act requires that the Telco (SBC Michigan) charge the affiliate for those
17 services "no less than the amount SBC Long Distance charged to any unaffiliated interexchange carriers
18 for such service."¹¹⁸ Thus, whatever "protection" the doctrine of "imputation" provides is unnecessary
19 in the case of a structurally separate affiliate as here. If Mr. Starkey's concern is broader than this and
20 relates to the fact that SBC and the affiliate are part of the same vertically integrated enterprise, then his
21 views appear to be in conflict with those of Congress itself. Congress created the Section 272 structure
22 precisely so that vertically integrated enterprises could offer interLATA toll services and provide Telco
23 services. All that is required is authorization under Section 271 and compliance with the structural
24 separation requirements of Section 272. Obviously, SBC has satisfied both of these standards. As a
25 result, whatever benefits it may derive from its vertical integration are benefits that Congress chose to
26 permit under these circumstances.

27 **Q25. PLEASE SUMMARIZE YOUR TESTIMONY.**

28 **A25.** AT&T has requested a substantial reduction in SBC Michigan's intrastate switched access rates on the
29 basis that if they are not reduced, the current rates will allow SBC Michigan to impose an
30 anticompetitive price squeeze on its competitors' profits which will drive them out of the business and

¹¹⁸ TA 96, Section 272(e).

1 allow SBC to "re-monopolize the interLATA market." I find that SBC Michigan's current intrastate
2 switched access rates comply with all of the requirements of the MTA, are therefore just and reasonable
3 and further, are among the lowest charged by carriers in the state of Michigan.

4 On the price squeeze allegation, I find that none of the circumstances exists which would permit the
5 effective imposition of such an anticompetitive price squeeze which would propel SBC Long Distance to
6 "re-monopolize the interLATA market" or local services as AT&T's witnesses assert.

7 First, the facts demonstrate that SBC Michigan does not have monopoly power at the alleged
8 upstream input level for switched access services. CLECs provide alternative access services. AT&T
9 itself can use its own facilities to bypass all or portions of SBC Michigan's access facilities. The
10 challenged rates remain subject to regulatory oversight which will prevent any such anticompetitive price
11 squeeze from being imposed. Wireless services continue to supplant large portions of traditional
12 wireline LD and thereby bypass SBC Michigan's switched access facilities in whole or in part. And, an
13 even newer technology—VoIP—is poised to bypass those facilities all together in computer-to-computer
14 applications or at least in part when calls are made to or from a wireline phone.

15 Second, the current prices for the switched access services do not prevent SBC's IXC rivals from
16 competing effectively. AT&T itself has recently admitted that it remains profitable in Michigan.

17 Third, there is virtually no likelihood that SBC will "re-monopolize the interLATA market" or the
18 alleged local "market." SBC is one of the newest entrants into the interLATA toll business in Michigan,
19 starting just 6 months ago with zero share. There also remains substantial excess capacity at a time when
20 usage has diminished markedly. Further, the barriers to new entry into interLATA toll remain quite low
21 and there are a large number of rivals in Michigan today. At the local level, Michigan has evolved to be
22 one of the most competitive markets in the United States. Finally, wireless and VoIP promise continued
23 consumer substitution which bar any incumbent wireline provider from exercising market power.

24 **Q26. DOES THIS CONCLUDE YOUR TESTIMONY.**

25 **A26.** Yes.

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EDUCATION

Ph.D., Economics, University of Illinois, Urbana-Champaign, IL, USA, 1996.
M.S., Economics, University of Illinois, Urbana-Champaign, IL, USA, 1995.
M.S., Civil Engineering, Bradley University, Peoria, IL, USA, 1986.
B.S., Civil Engineering, Bradley University, Peoria, IL, USA, 1977.

PRESENT EMPLOYMENT

LECG LLC, Emeryville CA, USA, 2002 – present

LECG Limited, London UK, 2001-2002

LECG Inc, Emeryville CA, USA, 1996-2001

Senior Managing Economist, January 1999 – present

Senior Economist, July 1996 – December 1998

Economic consulting in regulation, antitrust and competition policy. Emphasis on network industries such as telecommunications, electric power and air transportation also including water distribution.

Major cases in the telecommunications industry have included evaluation of damages in a Baltic telecommunications arbitration, analysis of pricing by UK mobile phone providers, analysis of alleged antitrust violations involving competitive local exchange carriers, provision of DSL service and provision of payphone service, evaluation of unbundled network element (UNE) cost models and development and implementation of methods for statistical assessment of service quality parity. Cases in other utility industries include evaluation of the performance of a water distribution concessionaire in the Asia Pacific region and various cases in the electric power and gas industries requiring evaluation of policies for recovery of transmission losses, power market transactions and finance of transmission infrastructure investments. Activities in the air transportation industry have included evaluation of pricing policies proposed by the US Department of Transportation, analysis of alleged antitrust violations in the US, evaluation of the impact of specific international code sharing agreements and evaluation of the impact of reallocating resources at a major international airport in the UK.

RESEARCH INTERESTS

Industrial Organization, business reactions to regulatory changes and more generally the relationship between business and government.

TEACHING EXPERIENCE

1995-1996: Teaching Assistant, Economic Statistics, University of Illinois.

1991-1992: Teaching Assistant, Introductory Economics, University of Illinois.

1986-1987: Instructor, Illinois Central College, Peoria, IL (part-time). BASIC and dBASE language programming for personal computers.

1986: Instructor, Fluid Mechanics, Bradley University, Department of Civil Engineering, Peoria, IL.

PROFESSIONAL EXPERIENCE

HAAS SCHOOL OF BUSINESS, University of California, Berkeley, 1993 - 1995.
Visiting Researcher

INSTITUTE OF GOVERNMENT AND PUBLIC AFFAIRS, University of Illinois at Urbana-Champaign, 1991 - 1993.
Research Assistant

CATERPILLAR INC. Peoria, IL, USA
Independent consultant, 1991 - 1992.

Develop a system to integrate collection and analysis of internal and external defect records at Leicester, UK manufacturing facility.

Senior Reliability Analyst, Service Engineering, Peoria, IL, 1982 - 1991.

Responsible for providing analytical support to Service Engineering Department, the corporate division responsible for liaison between customers, design and manufacturing.

Responsibilities included:

- Develop the quality and reliability measures used as part of the performance standards used to determine each product division's profit sharing potential. Presentation of quarterly reports of these measures to all divisions.
- Host the annual corporate conference presenting new developments in product reliability and quality measurements. The conference was attended by representatives from all subsidiaries.
- Develop systems and procedures to allocate warranty expenses among the product divisions.
- Estimate corporate liability under extended warranty terms.

Facilities Planning Staff Engineer, Mapleton Foundry, 1980 - 1982

Planning, including assessment of need, design liaison, acquisition and installation of capital equipment.

Environmental Engineer, Mapleton Foundry, 1978 - 1980.

Technical assistance to utility operating personnel, acquisition and maintenance of all state and federal permits, review of proposed changes to plant equipment and operating procedures to assure compliance with all environmental regulations.

PRESENTATIONS, TESTIMONY AND REGULATORY PROCEEDINGS

- Written expert testimony and cross-examination on behalf of Ameritech Wisconsin regarding the pricing of the High Frequency Portion of the local loop (Docket No. 6720-TI-161, February, 2001)
- Expert testimony on behalf of Qwest Corporation, in QWEST CORPORATION, PLAINTIFF, VS. IP TELEPHONY, INC., d/b/a MOUNTAIN SOLUTIONS TELECOM GROUP, INC., Case No.99CV8252, District Court, City and County of Denver, Colorado.
- Written expert testimony and cross-examination on behalf of Ameritech Michigan regarding service quality standards in (Case No. U-12598, November 2000)
- Written expert testimony and cross-examination on behalf of Ameritech Illinois in proceedings to determine the price of “line sharing.” Illinois (C.C. Docket 00-0312 and 00-0313, July 2000, C.C. Docket No. 00-0393, September, 2000), Michigan (Case No. U-12540, October 2000)
- Advise U S WEST on appropriate statistical methods for Arizona OSS tests associated with its section 271 application. (May 2000)
- Written expert testimony and cross-examination on behalf of U S WEST regarding statistical methods in rate deaveraging in consolidated cost dockets in Washington (Dockets UT-9603769, UT-960370 and UT-960371, January 2000)
- Ex Parte presentation to FCC on behalf of U S WEST, regarding statistical methods for testing equality of service quality, June 1999.
- Affidavit on behalf of Ameritech Michigan regarding the statistical validity of the sampling procedure used in Ameritech’s current AFAM cost model. (MPSC Case No. U-11831, June 1999).
- Oral testimony and written comments on behalf of U S WEST regarding wholesale service quality rules in Colorado (Docket No. Docket No. 97R-153T, February 19, 1998).
- Written expert testimony and cross-examination on behalf of U S WEST regarding statistical measurements of service quality, Arizona (Docket No. U-3021-96-448, June 1998), Utah (Docket on Rules R746-365, June 1998), Iowa (Docket Nos. AIA-96-1 (ARB-96-1), AIA-96-2 (ARB-96-2), March 1998), Minnesota (Docket No. P-442,5321,421/CI-97-381, June 1998)
- Written comments regarding statistical methods for measuring service quality on behalf of U S WEST to the FCC in regard to the FCC NPRM “Performance Measurements and Reporting Requirements for Operations Support Systems, Interconnection, and Operator Services and Directory Assistance” (Docket No. 98-56, RM-9101, June 1998)
- Declaration regarding statistical measurement on behalf of Pacific Bell in “Investigation on the Commission’s Own Motion into the Establishment of a Forum to Consider Rates, Rules, Practices and Policies of Pacific Bell and GTE California Incorporated” (Docket No. 90-02-047, August 1998).

- Statement in reply to the U.S. Department of Transportation's "Enforcement Policy Regarding Unfair Exclusionary Conduct in the Air Transportation Industry" (Docket OST-98-3713, September 1998)
- Participant in panel discussion on airline competition at the annual meeting of the National Association of State Aeronautics Officials. (October 1998)
- Written expert testimony and cross-examination on behalf of U S WEST for consolidated cost dockets in Washington (Dockets UT-9603769, UT-960370 and UT-960371, June 1997) and Utah (Docket No. 94-999-01, May 1997).
- Participant in cost workshops on behalf of U S WEST with the Utah Division of Public Utilities (February 1997), Washington (March 1997), Minnesota (May 1997).
- Oral testimony and cross-examination on behalf of U S WEST in Wyoming (Docket No. 70000-TR-96-323, June 1997).

DISSERTATION TOPIC

"Three Essays on Demand and Cost in the Deregulated Domestic Airline Industry"

Topics include:

"Airline Hubs: Costs, Markups and the Implications of Customer Heterogeneity"

"Evolution of Demand and Marginal Cost in the U.S. Airline Industry from 1985 to 1993"

"The Effects of Bankruptcy on the Demand and Marginal Cost of Passenger Airlines"

PUBLICATIONS

"Airline Hubs: Costs, Markups and the Implications of Customer Heterogeneity", with Steven Berry and Pablo T. Spiller, NBER Working Paper 5561, May 1996.

HONORS AND PROFESSIONAL ACTIVITIES

Licensed Professional Engineer, State of Illinois

Member: American Society of Civil Engineers

Member: Institute of Electrical and Electronics Engineers (IEEE)

Member: Tau Beta Pi, engineering honorary.

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