

**BEFORE THE
PUBLIC SERVICE COMMISSION OF UTAH**

In the Matter of the Joint Application of
Qwest Communications International, Inc.
and CenturyTel, Inc. for Approval of Indirect
Transfer of Control of Qwest Corporation,
Qwest Communications Company, LLC, and
Qwest LD Corporation
-----/

DOCKET NO. 10-049-16

SURREBUTTAL TESTIMONY OF

CHARLES W. KING

On Behalf of
THE DEPARTMENT OF DEFENSE
And
ALL OTHER FEDERAL EXECUTIVE AGENCIES

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October 14, 2010

1 **SURREBUTTAL TESTIMONY OF**
2 **CHARLES W. KING**
3

4 **Q. PLEASE STATE YOUR NAME, POSITION AND BUSINESS ADDRESS.**

5 A. My name is Charles W. King. I am President of the economic consulting firm of
6 Snavelly King Majoros & O'Connor, Inc. My business address is 1111 14th Street,
7 N.W., Suite 300, Washington, D.C. 20005.

8 **Q. ARE YOU THE SAME CHARLES W. KING WHO SUBMITTED DIRECT**
9 **TESTIMONY IN THIS CASE ON BEHALF OF THE DEPARTMENT OF**
10 **DEFENSE AND ALL OTHER FEDERAL EXECUTIVE AGENCIES**
11 **(“DoD/FEA”) ON AUGUST 30, 2010?**

12 A. Yes, I am.

13 **Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

14 A. The purpose of this surrebuttal testimony is to respond to the rebuttal testimony of
15 the Applicants' witness Robert Brigham.

16 **Q. AT PAGE 13 OF HIS REBUTTAL TESTIMONY, MR. BRIGHAM**
17 **ASSERTS THAT WIRELESS SERVICE SERVES AS A PRICE-**
18 **CONSTRAINING SUBSTITUTE FOR WIRELINE SERVICE. DOES THE**
19 **FCC AGREE?**

20 A. No it does not. In a recent (June 22, 2010) decision rejecting Qwest's petition for
21 relaxed regulation in the Phoenix, Arizona metropolitan area, the FCC stated its
22 view that wireless is a usage substitute for wireline that more likely reflects
23 consumer preferences with regard to mobility of communications than the
24 differences in its prices relative to landline prices:

25 As an initial matter, we note that the Commission, the DOJ, and
26 foreign regulators have previously found that mobile wireless
27 service does not constrain the price of wireline service. For
28 example, in 2005 and 2007 the Commission found that mobile

1 wireless substitution does not appear to have a price-constraining
2 effect on wireline service. A recent report by the DOJ likewise
3 found no evidence that mobile wireless access substitution
4 constrains landline telephone service prices. In addition, Ofcom
5 (the telecom regulator for the United Kingdom), in evaluating the
6 retail market for fixed (*i.e.*, wireline) access, found that, “while
7 there is some substitutability between fixed and mobile access,
8 consumers predominantly view the two types of access as meeting
9 different needs and have a strong preference to purchase both fixed
10 and mobile access.” It thus concluded that mobile wireless services
11 should not be included in the same relevant product market as
12 wireline access service.

13 No evidence in the record here causes us to reach a different
14 conclusion. In particular, neither Qwest nor any other commenter
15 has submitted evidence that would support a conclusion that
16 mobile wireless service constrains the price of wireline service.¹

17 **Q. DO YOU AGREE WITH THE FCC?**

18 A. I generally agree, but I believe that wireless may have a price constraining effect
19 on wireline for certain age and economic subgroups of residential customers.
20 However, as I noted in my initial direct testimony, wireless has no price-
21 constraining effect on business wireline service. Businesses must have wireline
22 service regardless of the mobility and price of wireless.

23 **Q. AT PAGE 14 OF HIS REBUTTAL, MR. BRIGHAM ASSERTS THAT**
24 **MARKET SHARE IS NOT A GOOD INDICATOR OF MARKET**
25 **POWER? DO YOU AGREE?**

26 A. No. Mr. Brigham provides several reasons why he believes that market share is
27 not relevant for estimating the market power of the Incumbent Local Exchange
28 Carriers (“ILECs”), and particularly Qwest. First, he states that in the case of a
29 regulated industry, market share is not a valid measure of market power because
30 regulation can overrule market forces. He is absolutely correct, and this is the
31 very reason why I propose that the Utah commission re-impose a very limited
32 degree of regulation on Qwest following the merger.

¹ In the Matter of Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. §160(c) in the Phoenix, Arizona Metropolitan Statistical Area, WC Docket No. 09-135, *Memorandum Opinion and Order* (FCC 10-113, released June 22, 2010) (“*Arizona Forbearance Order*”). ¶¶ 57, 58. Footnotes omitted.

1 Mr. Brigham next claims that market share measures are static and retrospective,
2 and do not consider market trends such as Qwest's declining market share. This
3 argument has some validity, but it overlooks the imperfect nature of the
4 competition, which I will address shortly. In any case, Qwest is still by far the
5 dominant landline carrier of telephone services, even after its claimed losses in
6 market share.

7 Mr. Brigham's final point is that market capacity is a more relevant measure of
8 market power than market share, and he asserts that the cable companies have on
9 the order of 50 percent of the market capacity. I have no idea how Mr. Brigham
10 arrives at this 50 percent, given that digital signals over fiber optic cables have
11 almost unlimited capacity. But even if the cable companies' capacity were at 50
12 percent, that percentage would not be particularly relevant to the business market.
13 As I have noted previously, cable companies typically do not serve business
14 customers.

15 The fact is that market share is conventionally used to evaluate market power,
16 although it is not the sole indication. For example, the Herfindahl-Hirschman
17 Index and Simpson Diversity Index, conventionally used in anti-trust analysis and
18 litigation, are both measures of relative market share and market power.

19 **Q. BEGINNING ON PAGE 20 OF HIS REBUTTAL, MR. BRIGHAM**
20 **CHALLENGES YOUR ASSESSMENT OF THE BUSINESS MARKET.**
21 **WHAT IS YOUR RESPONSE?**

22 A. The basis for most of Mr. Brigham's challenge is the claim that I have understated
23 the market share of the non-ILEC carriers in the landline market. He claims that I
24 have failed to include non-switched Voice over Internet Protocol ("VoIP") in my
25 market share measure and that I did not use the latest FCC report.

26 I do not challenge Mr. Brigham's numbers, although I regard his criticism that I
27 failed to use the latest FCC report as unfair, since that report had not yet been
28 released when I prepared my testimony. But Mr. Brigham still fails to
29 demonstrate that the ILECs, and specifically Qwest, lack market power in the

1 business sector, for two reasons. First, Mr. Brigham’s revised estimates of the
2 ILECs’ market share still show their overwhelming dominance in the market.
3 Second, the market share numbers obscure the dependent nature of the
4 “competitors” relative to the ILECs in the business market.

5 **Q. WHY DO YOU SAY THAT MR. BRIGHAM’S REVISED NUMBER**
6 **INDICATES THE ILECS’ OVERWHELMING DOMINANCE IN THE**
7 **MARKET?**

8 A. If, as the FCC believes, wireless does not offer price-constraining competition to
9 landline service, then the only relevant market share values are those pertaining to
10 landline communications. The highest non-ILEC market share that Mr. Brigham
11 finds is 41 percent of business end user switched access lines and VoIP
12 subscriptions. The complement of that number is 59 percent, the ILEC share of
13 this market.

14 Earlier, I mentioned a measure of market concentration called the Herfindahl-
15 Hirschman (“H-H”) Index. This index is widely used in competition, anti-trust
16 and technology management. It is defined as the square of the market share of a
17 firm or group of firms. The index can range from 1 (1%²) to 10,000 (100%²). As
18 conventionally used, any index over 1,800 is considered to represent evidence of a
19 highly concentrated market.² At 59 percent of the market, the ILECs’ Utah index
20 is 3,481, which indicates overwhelming market dominance.³

21 **Q. WHY DO YOU SAY THAT MR. BRIGHAM’S MARKET SHARE**
22 **NUMBERS OBSCURE THE DEPENDENCE OF THE COMPETITORS**
23 **ON THE ILECS?**

² U.S. Department of Justice and the Federal Trade Commission, “Horizontal Merger Guidelines,” Revised April 8, 1997, p. 10.

³ A complete application of the H-H Index requires a listing of the market shares of each participant in the market. Since the breakdown of the CLECs and VoIP providers’ market share is not available, this application is confined to the ILECs. The H-H indices of the individual CLECs would be much smaller than that of the ILECs, of which there is only one in any given location in Utah.

1 A. Virtually all of the CLECs and most of the VoIP providers are dependent on the
2 incumbent carriers for the “last mile” connection to their business customers.
3 This means that even if they serve 41 percent of the market, the non-ILEC’s are
4 still dependent on the ILECs for a portion of their service. This fact, with
5 particular reference to business services, was the principal basis for the FCC’s
6 refusal to forbear from its regulation of Qwest in the *Arizona Forbearance Order*:

7 Under this analysis and based on the data in the record, Qwest fails
8 to demonstrate that there is sufficient competition to ensure that, if
9 we provide the requested relief, Qwest will be unable to raise
10 prices, discriminate unreasonably, or harm consumers. For
11 example, the record reveals that no carrier besides Qwest provides
12 meaningful wholesale services throughout the Phoenix
13 marketplace, and that competitors offering business services
14 largely must rely on inputs purchased from Qwest itself to provide
15 service.⁴
16

17 **Q. AT PAGE 19 OF HIS REBUTTAL, MR. BRIGHAM REFERS TO YOUR**
18 **PROPOSAL TO “FREEZE” BUSINESS SERVICE RATES. IS THIS AN**
19 **ACCURATE CHARACTERIZATION?**

20 A. No. I have not proposed to freeze rates. I have proposed to cap them at their
21 current levels. Qwest (or its successor) may reduce rates if it wishes. It may then
22 increase them back to the capped level if it chooses.

23 **Q. AT PAGE 20, MR. BRIGHAM ASSERTS THAT BECAUSE THE**
24 **BUSINESS MARKET IS COMPETITIVE, ANY PRICE FREEZE (OR**
25 **CAP) WOULD BE UNNECESSARY. HOW DO YOU RESPOND?**

26 A. I have already discussed why I believe the business market is not adequately
27 competitive to restrain unilateral price increases. But assuming, *arguendo*, that
28 Mr. Brigham is correct that the business market is so competitive that Qwest
29 cannot increase its prices, a price cap would impose little burden on Qwest. The
30 reality, however, is that Qwest, the dominant carrier, is the price leader of the

⁴ *Arizona Forbearance Order*, ¶ 2. The FCC’s detailed findings as to Qwest’s pricing power in the market for enterprise business services are set forth at ¶¶ 87-91 and 99.

1 wireline industry. If Qwest increases its prices, the CLECs would find more
2 pricing “headroom” and would likely increase their prices as well. That is why a
3 price cap is needed regardless of the extent of CLEC competition. It would
4 appear that Qwest might agree. The resistance that Qwest has posed to my
5 proposal suggests that possibly Qwest itself believes that it can increase its prices.

6 **Q. DO YOU HAVE ANY COMMENTS ON THE ISSUE OF SERVICE**
7 **QUALITY?**

8 A The Applicants’ witness Jeremy Ferkin regards my service quality concerns as
9 irrelevant to this merger. For example, he argues at some length that this
10 transaction cannot be compared with the earlier Verizon spinoffs in Hawaii and
11 New England where there was serious service quality deterioration owing to the
12 transactions. Although he never specifically addresses my recommendations
13 regarding service quality oversight, he apparently considers them unnecessary.

14 As I indicated in my direct testimony, I am concerned about the possibility of a
15 deterioration of service quality. That concern also stems from results of the FCC
16 ARMIS Report, which is Exhibit 4 of my Direct Testimony. See the attached
17 Revised Exhibit 4.⁵

18 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

19 A. Yes. It does.

⁵ The line headings in this exhibit were inadvertently reversed, that is, the “Business Lines” should have been labeled “All Lines,” and the “All Lines” should have labeled “Business Lines.” Additionally, some of the entries under “Special Access Lines” were incorrectly transcribed from the Federal Communications Commission (“FCC”) reports. Finally, the heading “CenturyLink” should read “Embarq” because the merger of those two companies did not occur until June of 2009, and the metrics shown are those of Embarq. These non-substantive changes are incorporated into the Revised Exhibit 4 attached to this surrebuttal testimony.