

Changes in the Telecommunications Industry

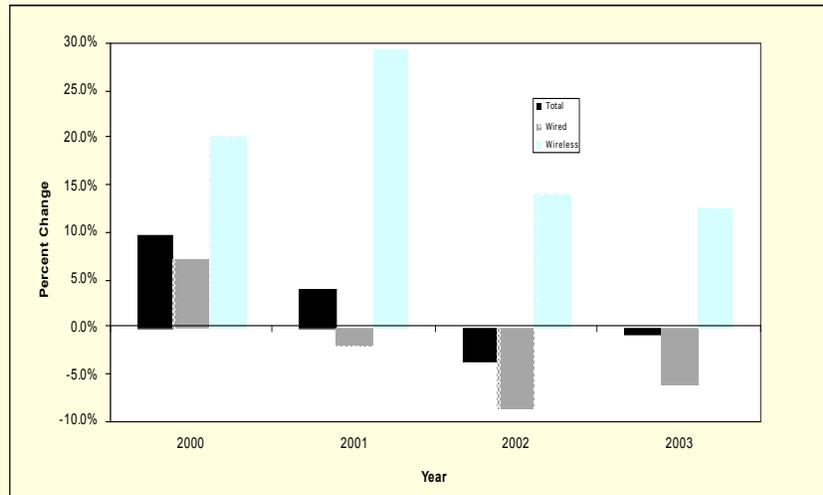
Federation of Tax Administrators
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Outline

- Telecommunications revenue trends by industry segment
- 2005 Developments
- Recent BOE valuation trends
- CA emergency telephone users' surcharge
- Factors
 - Technology
 - Prices
 - Substitution of closely related products
- Details: See paper on following web site reference:
<http://www.boe.ca.gov/proptaxes/pdf/economiccontext-2005.pdf>

U.S. Industry Trends



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Wireless Growing, Wired Declining

- The wireless industry has grown rapidly in recent years, mostly at the expense of wired phone services.
- In 1998, wired services accounted for 80 percent of total U.S. telecommunications revenues and wireless services accounted for 15 percent.
- By 2003, the wired market share had dropped to 64 percent of total U.S. telecommunications revenues and the wireless share had risen to 31 percent.

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Wireless Growing, Wired Declining

- From 1998 to 2003, revenues for U.S. cellular telecommunications providers increased from \$35.2 billion to \$104.2 billion.
- Over the same time period, revenues for U.S. wired telecommunications providers declined from \$227.9 billion to \$222.6 billion.

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Trends Continuing

- Available data indicate that these trends continued in 2004.
- Revenues from U.S. long distance wired service providers declined 8.8 percent in 2004.
- Revenues from U.S. local wired service providers declined 5.9 percent.

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Trends Continuing

- The wireless provider industry saw revenue increases of 18.8 percent in 2004.^[1]
- According to an article in the *New York Times* citing industry data, “More than 61 percent of Americans now have cellphones, almost twice as many as 2000.”^[2]

^[1] “The Shifting Telecommunications Landscape,” *Businessweek*, February 28, 2005.

^[2] “Urge to Merge Could Hit Small Cellphone Companies,” *New York Times*, January 7, 2005.

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2005 Developments (Cont.)

- RBOC Mergers
 - AT&T was purchased by SBC
 - MCI was purchased by Verizon
 - AT&T and MCI combined accounted for about 53 percent of the long distance telephone market in 2002

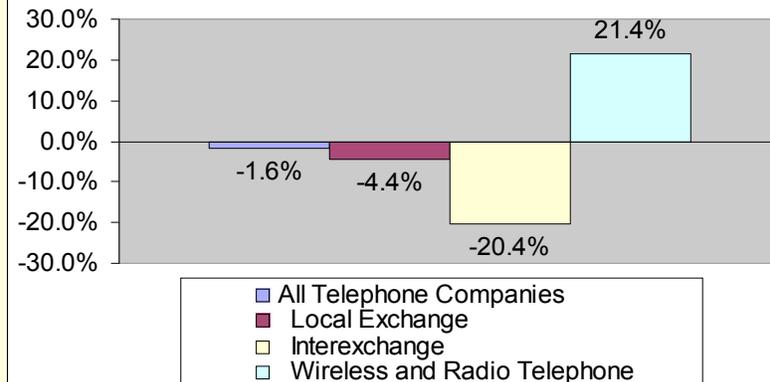
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2005 Developments (Cont.)

- These long distance telephone service providers were facing financial difficulties amid a competitive environment and falling prices
- AT&T expected its revenue to decline 16 percent in 2005
- Both regulatory and technological industry trends have generally been running contrary to the health of long distance providers

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Changes in BOE-Assessed Values from 2004-05 to 2005-06



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State-Assessed Properties, BOE Web Site

- Source: *Recommendation for Assessment of State-Assessed Property*, California Board of Equalization
- <http://www.boe.ca.gov/proptaxes/sappcont.htm>

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CA Emergency Telephone Users' Surcharge

- Tax Base: Charges for intrastate telephone communications services
- Rate: Set each year, current rate is 0.65%
- Paid by telephone service suppliers
- Revenues: \$136.1 million in FY 2003-04, up 3.7%
- \$128.5 million in FY 2004-05 (preliminary figure), down 5.6% (Rate declined from 0.72% to 0.65%)
- Source: *2003-04 BOE Annual Report*, Table 35, http://www.boe.ca.gov/annual/table35_04.pdf

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CA Emergency Telephone Users' Surcharge (Cont.)

- Governor's January 2005 Budget Projection: ETUS revenues decline 10% in FY 2004-05 (10% rate decline), increase 4% in FY 2005-06
- Note: rate declined 10% in FY 04-05, implying flat revenue base forecast
- Source: Department of Finance web site:
<http://www.dof.ca.gov/DOF.asp>
- Governor's Budget, Schedule 8:
ftp://ftpgovbud.dof.ca.gov/pub/BudgetSummary/BS_SCH8.pdf

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Convergence

- "The telecommunications industry is undergoing rapid change due to technological advances and deregulation. The industry that previously was identified with the telephone now includes television, radio, wireless and satellite communications, and the Internet. Cable television companies now offer phone service and Internet access, telephone companies similarly offer cable or video services along with Internet access, and the Internet has become a medium through which telephone and video services can be delivered. This technological convergence or blending of telecommunications, information, and computer services, together with the Telecommunications Act of 1996, has significantly changed the industry's competitive structure..."^[1]

^[1] *The Taxation of Telecommunications in California in the Information Age*, James F. Prieger, Terri A. Sexton, and Annette Nellen, California Policy Research Center, University of California, Berkeley, 2003.

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Expected Future

- Telecommunications industry is expected to continue to face radical changes in the years ahead.
- “Our industry and our business is going to change more in the next five years than it has during the last 20 combined.” Duane Ackerman, chairman and chief executive officer of BellSouth, [1]

[1] “Phone Industry Faces Upheaval As Ways of Calling Change Fast,” *Wall Street Journal*, August 25, 2004.

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Some Factors

- Rapidly changing technology
- Falling prices
- Close substitutes

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Factors in Long Distance Decline

Three major factors:

- 1) increased competition from wireless calling
- 2) increased competition from local phone companies
- 3) the proliferation of e-mail as a substitute for long distance calls.

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Increased Wireless Competition

- 60% of U.S. households were wireless telephone subscribers in December 2004
- More than twice as many households as in 1999
- Real price of a wireless minute has fallen by 81 percent for the ten-year period ending in 2004 (FCC data).

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Broadband Growing Rapidly

- Revenues for local phone companies would have declined even more in recent years were they not also broadband Internet service providers.
- The number of U.S. broadband subscribers has increased from 4.3 million in June 2000 to 32.4 million by 2004.^[1]

^[1] *Broadband Deployment in California*, (draft report), February 1, 2005, California Public Utilities Commission.

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Fewer Access Lines

- Total U.S. wired access lines declined from a peak of 192.5 million in 2000 to 180.1 million in 2004, a 6.5 percent decline.
- Access lines declined 2.0 percent from June 2002 to June 2003 and 2.9 percent from June 2003 to June 2004.^[1]

^[1] "Federal Communications Commission Releases Data on Local Telephone Competition," press release, December 22, 2004.

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VOIP Technology Gaining

- VOIP may cause even more changes in the revenue and regulatory structure of telecommunications companies in the near future.
- VOIP is relatively inexpensive
- By 2008 VOIP may account for 25 to 40 percent of total intrastate telecommunications revenues in California.[1]

[1] "PUC to Determine Extent of Regulation on VOIP Carriers," California Public Utilities Commission press release, February 11, 2004.

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Questions ???

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