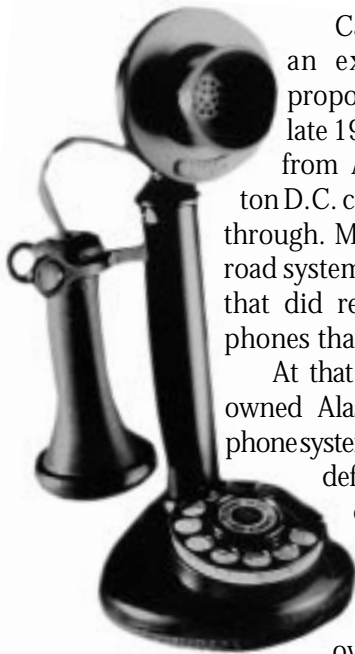




GOING PRIVATE: THE 1968 SALE OF THE ALASKA COMMUNICATION SYSTEM



Calling long distance was an expensive and chancy proposition for Alaskans in the late 1960s. A three-minute call from Anchorage to Washington D.C. cost \$7.00—when it went through. Most communities off the road system had no phones; the few that did relied on marine system phones that worked now and then.

At that time the U.S. Air Force owned Alaska's long-distance telephone system, established for national defense and later opened for civilian use. But by 1967, the Air Force wanted to quit the telephone business and let a private owner take over. The system—called the Alaska Communication System—hadn't been improved in nearly a decade.

In November 1967 Congress gave the Air Force approval to sell the Alaska Communication System, and in 1968 RCA bought it for \$28 million.¹ RCA began operating as Alascom in 1971.

That transfer from public to private ownership was an early example of the so-called "privatization" of government-owned businesses common worldwide today. But unlike most governments privatizing businesses today, the U.S. government and others with an interest in the sale wanted more than just the highest bid. They wanted a modern, reliable telephone system throughout Alaska—and lower rates for calls.

So the terms of the sale were unusual: RCA agreed to pay for the existing equipment, but also promised to invest a specific amount, cut the price of calls, and improve service.

How well did the transfer to private ownership succeed? Douglas Jones of Ohio State University and Bradford Tuck from the University of Alaska Anchorage recently looked at that question (see back page).

They found that putting the system in private hands was a success, resulting in cheaper rates and major improvements—but that some changes (especially better service for bush communities) took much longer than others.

The results of private ownership are clearest in the period from 1971-1979, when the original buyer still owned the system and Alascom was the only long-distance carrier in the state.

Many of the more recent changes in long-distance telephone service here and nationwide can be traced to de-regulation of the industry in 1982; to increased competition; and to technological improvements.

The researchers looked especially at what happened to the long-distance system in the 1970s—but they also make the case that the change from public to private ownership set the stage for more recent changes.

The timeline at the bottom of the page shows the major changes in Alaska's long-distance phone system since 1967 and how the price of long-distance calls dropped along the way. Alascom has changed hands several times since 1967, and since 1982 has competed in the Alaska market with GCI. Anchorage's municipal telephone utility, ATU, also moved into long-distance service in 1997.

THE CHANGES IN COSTS OF CALLING

(Cost of a 3-minute call from Anchorage to Washington D.C., daytime rates, no special plan)

\$7.00	\$4.75	\$2.37	\$1.59	87¢	93¢*
1967	1971	1979	1982	1995	1997
Congress approves sale	RCA starts operating	RCA sells to Pacific Telecom	Telephone industry de-regulated; GCI enters interstate market	AT&T buys Alascom	ATU enters long-distance market

*Costs as low as 10 cents per minute under special plans

REASONS FOR SALE

At least nine Latin American, a dozen European, and half a dozen Asian countries are shifting ownership of businesses from public to private. Arguments in favor of privatization today are similar to those used in Alaska 30 years ago.² Backers hoped the sale would:

- **Increase money for traditional public services**

Operating Alaska's long-distance system cost money the Air Force preferred to spend on military personnel or weapons and equipment. In other countries, state-owned businesses are often described as a drain on public budgets.

- **Speed investment in new technology**

The Air Force didn't want to spend the money needed to upgrade the Alaska Communication System, which lacked many of the features common to telecommunications systems in other states by the late 1960s—including direct-dial systems and capacity to transmit live television broadcasts. Government-owned businesses in other countries have also been described as slow to modernize.

- **Promote economic growth**

When the Air Force decided to sell the telephone system, Alaska had been a state only a few years. The new state government and private businesses supported the sale. They hoped a new owner would improve the system—which would, by improving Alaska's infrastructure, help promote economic growth. Promoting economic development is a major reason other countries currently cite for privatizing state-owned businesses.

- **Increase tax base**

Alaska's local governments and others saw a privately-owned telephone system as a boost to their small tax bases. Other countries have also used an increased tax base as an argument for shifting to private ownership.

- **Create private jobs and income**

And finally, when the Air Force put the telephone system on the market in the late 1960s, Alaska's population was becoming large enough to make a long-distance system profitable—and a profitable system could generate private jobs and income. There hadn't been much pressure to put the system in private hands as long as it wasn't profitable.

TERMS OF THE SALE

When RCA bought the Alaska Communication System, it agreed to: (1) pay \$28 million for existing equipment; (2) save consumers about \$40 million in reduced rates over three years; (3) spend about \$27 million on improvements within three years—including increased service to 142 remote communities.

MEASURES OF SUCCESS

What happened after the sale? We can look at how well the original buyer met the terms of the sale from 1971 to 1979. After 1979, the picture becomes more complicated—by new owners, by industry deregulation, and by competition. Still, if the shift from public to private ownership was intended to help create a modern telecommunications system for Alaska, we can see how well that change succeeded over the entire 30-year period.

Costs of Calling

The most obvious change since 1970 has been the steep and almost continuous drop in the price Alaskans pay to call long distance. Privatization certainly contributed to that drop—but keep in mind that other factors were also at work.³

- *RCA sharply cut the cost of calling from Alaska when it took over the long-distance system. As the timeline on the front page shows, the cost of a 3-minute call from Anchorage to Washington, D.C. dropped from \$7.00 in 1967 to \$4.75 in 1971.*

- *Calling long-distance got cheaper throughout the 1970s, with the price of a 3-minute call from Anchorage to Washington D.C. falling from \$4.75 to \$2.37.*

- *Competition has helped cut the costs of calling since the 1980s. GCI entered the interstate long-distance market in 1982 and in 1991 entered the intrastate market. ATU, Anchorage's telephone utility, began offering long-distance service in 1997.*

- *By 1997, Alaskans could call out of state (daytime rates, no special calling plan) for about 10 percent of what they paid in 1967. (If adjusted for inflation, the 1997 price is only about 3 percent of the 1967 price.) Current special calling plans offer rates as low as 10 cents per minute.*

Improvements and Investment in System

Construction of the trans-Alaska pipeline, development of the Prudhoe Bay oil field, a boom in the Alaska economy, and rapid technological change all caused RCA to invest far more than anticipated in Alascom in the 1970s. As the system grew, RCA saw its income rise sharply.

- *RCA invested an estimated \$400 million for direct-distance dialing, satellite technology, and improved switching networks in the 1970s.⁴*

- *Anchorage had a direct-dial system by 1972 and other large communities had such systems by 1975.*

- The completion rate for long-distance calls was less than 40 percent in Alaska's largest communities in 1971. By 1976 rates had improved, but still ranged from only 42 percent in Fairbanks to 69 percent in Juneau.⁵ Current figures on completion rates are hard to come by, but are estimated to be near the national rate of 95 to 99 percent.

- Alascom's gross income (income before expenses) grew from \$28 million in 1971 to \$150 million in 1979 (Figure 1).

- Alascom's real (adjusted for inflation) income grew an average of 38 percent annually during the 1970s.

- Real income continued to grow sharply until 1983. After that, competition from another company, an economic slowdown, and other factors cut into Alascom's income.

Growth in Jobs

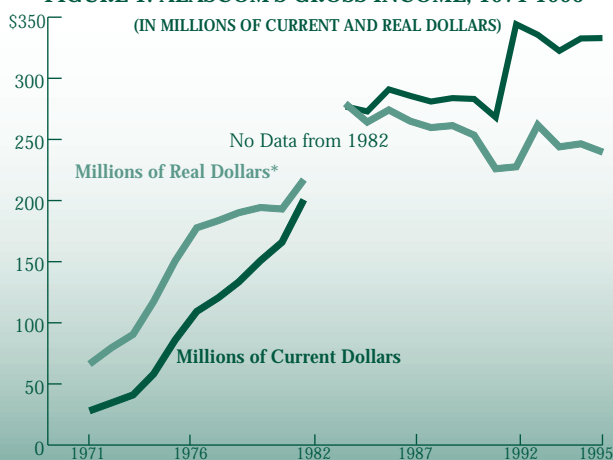
Alaskans hoped a better long-distance system would create new jobs—and it did. The numbers in Figure 2 include all jobs in the telephone industry, whether with local or long-distance carriers. Some of the new telephone jobs in the 1970s were in the long-distance system, but many were in local exchanges.⁶ After 1982, a second long distance carrier (GCI) also began creating jobs in Alaska.

- The number of jobs in the Alaska telephone industry increased from 150 in 1970 to about 2,000 during construction of the trans-Alaska oil pipeline (1975-1977).

- After 1980, the number of telephone jobs leveled off and then began a slow climb again in the 1990s, reaching 2,240 by 1996 (Figure 2).

- The telephone industry was among Alaska's fastest growing over the past 30 years—numbers of telephone jobs increased 15 times, while jobs in all industries tripled. Still, telephone jobs make up less than 1 percent of Alaska jobs.

FIGURE 1. ALASCOM'S GROSS INCOME, 1971-1995



Source: Alaska Public Utilities Commission, *Annual Reports*.
* Adjusted with Anchorage Consumer Price Index (base, 1982-84=100)

FIGURE 2. JOBS IN TELEPHONE INDUSTRY, 1971-1996



Source: Alaska Department of Labor

Increased Tax Base

- RCA paid the state government about \$2 million and local governments close to \$1 million in taxes in 1977 (the earliest year for which we have data). It also paid the federal government \$10 million in taxes.⁷

- By 1995, Pacific Telecom paid \$8 million in state and local taxes and \$30 million in federal taxes.⁸

More Rural Service

Fewer than half of rural households had phones available (meaning somewhere in the community) in 1960 (Table 1). Even that figure overstates phone service in off-road places, because the Census Bureau's definition of "rural" includes many towns on the road system.

RCA promised to install at least one community phone—or improve service—in 142 bush communities. But the improvements it made were slow and few.

- RCA installed marine telephone systems in about 50 communities in the first half of the 1970s—but several communities often shared one channel and call completion rates as low as 10 percent were reported.⁹

- By 1975, both RCA and the state government (frustrated by RCA's slow progress) were considering satellite technology to improve bush service. Then the state and RCA reached a compromise, under which the state bought 100 small earth stations and RCA operated them.¹⁰

- About 45 communities off the highway system had phone service via satellite technology by the late 1970s—but call completion rates were still only about 67 percent.¹¹

- Between 1980 and 1989, Pacific Telecom added or improved service in more than 135 rural communities.¹²

CONCLUSIONS

Putting the Alaska long-distance system in private hands was a public policy success. Except for improved service for bush communities, the goals of the sale were all met or exceeded within 10 years.

Problems with the adequacy, quality, and reliability of service persisted under RCA. Some problems can be traced to the ownership and management of RCA—but the fast growth of demand; an uncertain regulatory environment; lack of a comprehensive telecommunications plan; and state intervention in the industry also contributed.

The sale of the Alaska Communication System was unusual, because it looked to the future: it took into account Alaska's telecommunications needs, rather than just going for the highest bid. Other countries selling public businesses to private owners might want to consider a plan like Alaska's—instead of the more common plan of asking for the top dollar and potentially saddling future consumers with higher costs.

ENDNOTES

1. In 1968 AT&T declined to bid on the system—which it bought for a reported \$365 million in 1995.
2. We need to keep in mind, though, that the U.S. (unlike many countries) has a tradition of private ownership; the change from public to private ownership in Alaska wasn't nearly as major as it can be elsewhere.
3. Other such factors include not only the increased competition resulting from industry de-regulation, but less obvious things—like changes in the way charges for local and long-distance calls are distributed and other changes in the rate structure of telephone utilities.
4. George Shaginow, "Alaska and Alascom: A Decade of Telecommunications Development," in *Telecommunications in Alaska*, edited by Robert M. Walp; published by Pacific Telecommunications Council, Honolulu, Hawaii, 1982.
5. William Melody, "Telecommunications Networks: Internal Subsidies and System Extension in Alaska," page 55 in *Telecommunications in Alaska*; full citation in note 4.

TABLE 1. PERCENTAGE OF ALASKA HOUSEHOLDS WITH PHONES

Year	Alaska	Urban	Rural
1960	60.0%	74.2%	47.8%
1970	73.4%	84.8%	61.1%
1980	83.3%	82.0%	65.3%
1990	91.7%	95.2%	83.4%

Note: In 1960 and 1970 the census asked if there was a phone "available," which in rural areas often meant a single phone somewhere in a village. In 1980 and 1990, the census asked if there was a phone in the household itself—so the increase between 1970 and 1980 was likely larger than it appears.

Source: U.S. Bureau of the Census, *Alaska Census of Housing, 1960-1990*

6. *Employment in local exchanges in Alaska grew rapidly, beginning in the late 1970s, as local and long distance rates were re-structured; see Vinod K. Batra, "Local Exchange Growth in Bush Alaska," in Telecommunications in Alaska (full citation in note 4). Also, not all the employment in the telephone industry is private; several local telephone exchanges (including Anchorage's telephone utility) are publicly owned.*

7. *Annual reports of RCA and Pacific Telecommunications to the Alaska Public Utilities Commission, various years.*

8. *Same as note 7.*

9. *Vinod K. Batra, cited in note 6.*

10. *George Shaginow, full citation in note 4.*

11. *Arthur D. Little, Inc., Management Performance Audit of RCA Alaska Communications; prepared for the Communications Common Carrier Bureau and Alaska Public Utilities Commission, March 1979.*

12. *Proceedings of the Chugach Conference: Discussing the Future of Communications in Alaska; August 18 and 19, 1989.*

This Summary is based on Privatization of State-Owned Utility Enterprises: The Alaska Case Revisited Thirty Years Later, by Douglas N. Jones, School of Public Policy and Management, Ohio State University; and Bradford H. Tuck, College of Business and Public Policy, University of Alaska Anchorage, October 1996. Copies of the full paper are available for \$29.95 from The National Regulatory Research Institute, 1080 Carmack Road, Columbus, Ohio 43210-1002. Phone: (614)-292-9404; Fax: (614)-292-7196 E-mail: nrri@osu.edu; Web site: www.nrri.ohio-state.edu

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