ATTACHMENT A

Section 272 Costs

This exhibit provides additional information regarding the development of Verizon's estimates of the costs that Verizon Global Networks Inc. ("GNI") has incurred and anticipates incurring to comply with the Commission's separate affiliate rules under section 272 of the Act as set forth in the Declaration of Fred Howard, filed in WC Docket No. 01-112 and CC Docket No. 96-149.

For each major type of operating expense, capital expenditure, and depreciation, a determination was made as to the percent of this cost that was incurred strictly because of the section 272 structural separation and nondiscrimination requirements. (See Tables 1 and 2 below.) This percentage was applied to actual costs (including the 2002 budgeted expenses) to determine the "sunk cost" of separation. The same percentages were applied to the business plan that GNI developed in 2002 to determine the anticipated costs for 2003 and beyond that would be incurred solely to meet section 272 separation requirements.

It is important to note that the estimated "incremental cost" from this methodology cannot be directly compared to the actual costs/savings of reintegration because, in many cases, abandonment of sunk investment and complete reintegration of GNI's long distance network and operations with the local exchange company's would not be either possible or cost effective. Without knowing the timeline and the extent of reintegration allowed, it is not possible to arrive at an accurate "bottoms up" view of the costs and/or savings attributable to reintegration.

Using the methodology and conservative assumptions described above, GNI's business costs attributable to structural separation were calculated. The results show that GNI incurred approximately $195 million in capital costs and $314 million in expenses, including depreciation on capital, from 1998 through 2002 to meet section 272 requirements. The analysis also shows that GNI will incur an additional $550 million in expenses from 2003 to 2006 to continue to meet these requirements.

Table 1. Incremental Operating Expense Driven by Structural Separation

Expense Category	Description	% of Expenses Driven by Section 272 Requirements
Professional Services	Professional Services consist of the expenses for third-party vendors, primarily to perform field work. If GNI not been restrained by the Commission's rules prohibiting sharing of operating, installation, and maintenance functions with the BOC, this cost could have been avoided almost entirely by using existing BOC field technicians.	95%
Workforce & Employee related expenses	This includes internal GNI technical employees hired to provide OI&M functions. Although GNI startup required employees with skill sets specific to the long distance network architecture, some efficiencies could have been obtained in the absence of the OI&M restriction for job functions that did not require additional staff for the long distance network, including general administration, sourcing functions, and infrastructure for common service (corporate local area network, email, eWeb, training, etc.).	30%
Leased facilities	Without section 272 restrictions, VZ would have built rings instead of leasing facilities (both for use by GNI and by the local exchange company).	15%
Operational Support System (OSS)	Many of the operating support systems that GNI developed separately to comply with the OI&M restriction, such as inventory, provisioning, order management, trouble management, could have been developed through modification of the BOC systems and reused at a fraction of the costs incurred to develop new systems. The operating support system expense category includes software and hardware maintenance, licenses and right-to-use fees, and non-capital software development.	65%
Hub and POP	Absent the section 272 separation requirements, GNI would have collocated with the LEC wherever possible in-region. However, many LEC POP & Hub spaces were or are exhausted. A conservative approach was taken, with 80% of Hub & POP rental expenses driven by 272 requirements.	80%
Network Operations Center (NOC)	The network operations center provides monitoring and control of the long distance network. Although the long distance network requires additional operations, Verizon estimates that some of the incremental costs of the network operations center could have been avoided by using the BOC network operations center to provide these functions.	30%
Other	Miscellaneous (e.g., human resources allocation, Peoplesoft – Accounts Payable System, etc.)	25%
Back Office Provisioning (e.g., Calling Card, Repair)	These back office functions for GNI were driven almost entirely by the OI&M restriction. For instance, Verizon would not have built the Altoona or Worcester operator services facilities if these services could have been obtained from the BOC, and most of the costs of the error management and repair centers could have been avoided by using BOC services.	80%

Table 2. Incremental Investment And Depreciation Expense[1] Driven by Structural Separation

Investment/ Depreciation Category	Description	% of Additional Costs Driven by Section 272 Requirements
Hub and POP Equipment	This includes equipment purchased to provide LD service. Some incremental investment could have been avoided by using LEC facilities and equipment.	60%
Administration	80% of capital expenditures, including leasehold improvements, equipment, computers, and software where administrative functions are clearly identifiable (i.e., document server, Lotus notes, administrative PCs, etc.). Most administrative needs would have been served by existing LEC assets.	80%
NOC	A greater percentage of NOC-related capital expenditures were driven by 272 restrictions than expense (e.g. leasehold improvement on separate 272 NOC space).	60%
OSS	Most capital expenditures to establish stand-alone OSSs for GNI could have been avoided by using and expanding existing LEC OSSs.	65%
Laboratory	Most non-OSS LD laboratory equipment and facilities capital expenditures could have been avoided absent the section 272 requirements. Actual capital expenditure for LD lab is less than "greenfield" because of manufacturer contract provisions. Capital expenditure for OSS support in the LD lab mirrors production OSS capital expenditure (65%) because lab test systems for new OSSs would have been required that did not exist in the LEC. Lucent Lab in Holmdel expenses are 100% driven by section 272 requirements (i.e., GNI would not have contracted with Lucent to develop a lab).	65 to 100%

[1] Depreciation was calculated, depending on capital type and number of years depreciated, using straight-line depreciation.

Estimated Incremental Savings from Reintegration (2003-2006)

The Commission's Notice of Proposed Rulemaking ("NPRM") in WC Docket No. 02-112 suggests a broad range of scenarios for sunset of the section 272 separate affiliate requirements. Given that each scenario could materially affect when and how reintegration of the section 272 network and organizations would be implemented, Verizon used a general approach to assess sunk costs and anticipated savings resulting from reintegration as percentages of actual and planned expenses. In addition, Verizon assumed for sake of this analysis that the section 272 requirements are removed in all of the states in Verizon's territory in 2003.

If the Commission's section 272 rules were to sunset in 2002, it would not be economic to eliminate all of the "sunk" investments that were made in separate facilities and systems to meet the separate affiliate requirements. However, Verizon conservatively estimates that it could save about $247 million over the 2003 through 2006 time period by reintegrating operations with the BOC where it was economically advantageous to do so. Approximately $183 of this amount would be due to elimination of the OI&M restriction.

The incremental costs that are driven by the section 272 requirements cannot be directly compared to the actual costs that would be saved through reintegration. In many cases Verizon has considerable investment sunk in a separate 272-compliant network. For example:

- GNI has long-term lease commitments, and considerable investment in leasehold improvements in those spaces. A "flash cut" to the LEC would not be cost effective.
- The network in the majority of the Verizon East corridor, where the greatest synergies with the LEC are, has already been built. GNI has long-term commitments (leases and RTUs) for fiber and facilities in the Northeast and could not easily move to LEC fiber or facilities.

- OSS suites are in place with considerable software and hardware capital investment ($130 million).

Nonetheless, considerable costs could be saved by use of LEC workforce and facilities if the structural separations rules were to sunset. For example:

- Force & Professional Services resources could be ramped to achieve pre-separation savings.
- Savings could be realized in POP rent and operating expenses in existing sites in the Verizon East footprint by gradually relocating certain POPs as leases and as collocation agreements lapse.

- Some savings could be realized in this planning window for OSSs by consolidating selected systems.
- Some synergies with LEC could be found in future network build.

It should also be noted that the 2003-2006 savings estimate is based on 2002 Business Planning information, which did not fully take into account currently evolving GNI network expansion plans because the 2003 Business Plan is not yet complete. Additional savings may be realized if section 272 restrictions do not apply to the 2003 plan. The current estimate of potential savings due to re-integration starting in 2003 are shown in Table 3 below.

Table 3. Incremental Savings Going-Forward (Percentages)

	2003	2004	2005	2006
Force & Related Expense	10%	20%	30%	30%
Professional Svcs.	40%	80%	95%	95%
Facilities (trunks)	3%	10%	15%	15%
OSS	See below[2]			
Hub/POP Rent	10%	20%	30%	40%
NOC Expenses	10%	20%	30%	30%
Other Expenses	10%	15%	25%	25%
Back Office	30%	60%	80%	80%

Operating, Installation and Maintenance (OI&M) Savings

If the OI&M restriction were eliminated, significant savings could be obtained by consolidating with the LEC the responsibility for the day-to-day provisioning and maintenance of the long distance switch and transport networks in central offices as well as the remote monitoring and provisioning of services from network operations centers. In addition, up-front trouble handling and associated dispatch functions could also be more efficiently managed. The OI&M restrictions affect the expenses in the following categories in the table above: (1) professional services, (2) force and employee related expenses, (3) OSSs, (4) NOC and (5) back office provisioning. Based on this analysis, Verizon estimates that if the OI&M restriction were eliminated, GNI would save approximately $183 million over the 2003 through 2006 time period by sharing these services with the BOCs.

[2] OSS savings could not be calculated as a percentage of future expenses, as was the case with the other expenses. The incremental savings associated with OSS were based on a case-by-case analysis of OSS cost avoidance/potential savings over the planning period.