

Application of Regional Labor Adjustment Factor on Outdoor SAI Installation			
Outdoor SAI Total Pairs Terminated	Installed Outdoor SAI	Labor Content Affected	Investment Affected per Outdoor SAI
7,200	\$10,000	0.164	\$1,640
5,400	\$8,200	0.164	\$1,345
3,600	\$6,000	0.164	\$984
2,400	\$4,300	0.164	\$705
1,800	\$3,400	0.164	\$558
1,200	\$2,400	0.164	\$394
900	\$1,900	0.164	\$312
600	\$1,400	0.164	\$230
400	\$1,000	0.164	\$164
200	\$600	0.164	\$98
100	\$350	0.164	\$57
50	\$250	0.164	\$41

Application of Regional Labor Adjustment Factor on Indoor SAI Installation			
Indoor SAI Distribution Cable Size	Installed Indoor SAI	Labor Content Affected	Investment Affected per Indoor SAI
7,200	\$3,456	0.164	\$567
5,400	\$2,592	0.164	\$425
3,600	\$1,728	0.164	\$283
2,400	\$1,152	0.164	\$189
1,800	\$864	0.164	\$142
1,200	\$576	0.164	\$94
900	\$432	0.164	\$71
600	\$288	0.164	\$47
400	\$192	0.164	\$31
200	\$96	0.164	\$16
100	\$48	0.164	\$8
50	\$48	0.164	\$8

Telco Installation & Repair labor (Drop & NID installation): Regional Labor Adjustment Factor applies to \$20 of the \$35 loaded labor rate (exclusive of exempt material loadings).

Application of Regional Labor Adjustment Factor on NID Installation			
Type of NID	NID Basic Labor	Labor Content Affected	Investment Affected per NID
Residence	\$15.00	0.571	\$8.57
Business	\$15.00	0.571	\$8.57

Application of Regional Labor Adjustment Factor on Aerial Drop Installation			
Density Zone	Installed Aerial Drop	Labor Content Affected	Investment Affected per Drop
0-5	\$23.33	0.571	\$13.33
5-100	\$23.33	0.571	\$13.33
100-200	\$17.50	0.571	\$10.00
200-650	\$17.50	0.571	\$10.00
650-850	\$11.67	0.571	\$6.67
850-2,550	\$11.67	0.571	\$6.67
2,550-5,000	\$11.67	0.571	\$6.67
5,000-10,000	\$11.67	0.571	\$6.67
10,000+	\$11.67	0.571	\$6.67

Application of Regional Labor Adjustment Factor on Buried Drop Installation			
Density Zone	Installed Buried Drop per Foot	Labor Content Affected	Investment Affected per Drop
0-5	\$0.60	0.125	\$0.075
5-100	\$0.60	0.125	\$0.075
100-200	\$0.60	0.125	\$0.075
200-650	\$0.60	0.125	\$0.075
650-850	\$0.60	0.125	\$0.075
850-2,550	\$0.75	0.125	\$0.094
2,550-5,000	\$1.13	0.125	\$0.141
5,000-10,000	\$1.50	0.125	\$0.188
10,000+	\$5.00	0.125	\$0.625

Application of Regional Labor Adjustment Factor on Pole Installation			
Total Pole Investment	Pole Labor	Labor Content Affected	Investment Affected per Pole
\$47	\$216	0.518	\$216

The following chart shows recommended default values for each state.

Regional Labor Adjustment Factor:

Direct Labor costs vary among regions in the United States. A variety of sources can be used for labor adjustment factors.⁵⁶ The following statewide labor adjustment factor indexes can be used as default values:

State	Factor⁵⁷
Alaska	1.25
Hawaii	1.22
Massachusetts	1.09
California	1.07
Michigan	1.01
New York	1.00
New Jersey	1.00
Rhode Island	1.00
Illinois	1.00
Minnesota	0.99
Connecticut	0.98
Pennsylvania	0.97
Nevada	0.95
Washington (State)	0.92
Oregon	0.92
Delaware	0.92
Indiana	0.92
Missouri	0.90
Maryland	0.89

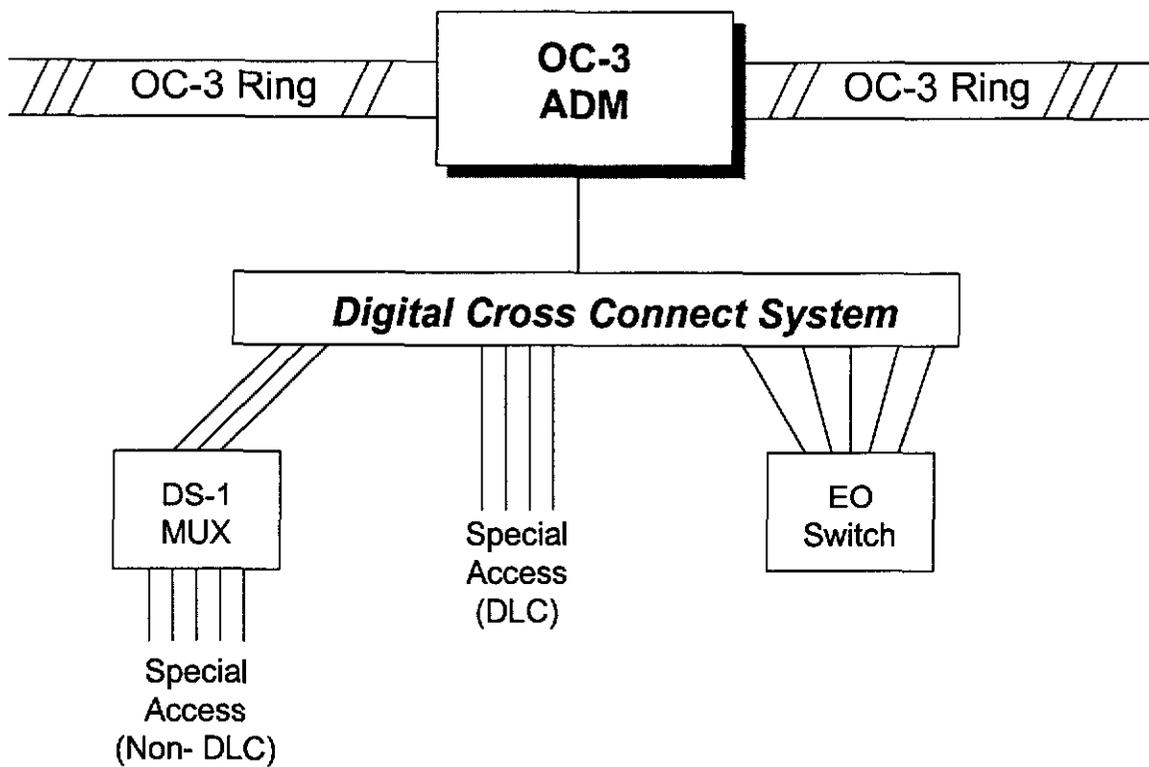
⁵⁶ See, for example, R.S. Means Company, Inc., *Square Foot Costs, 18th Annual Edition*, 1996, p.429-433.

⁵⁷ Martin D. Kiley and Marques Allyn, eds., *1997 National Construction Estimator 45th Edition*, pp. 12-15. [Normalized for New York State as 1.00]

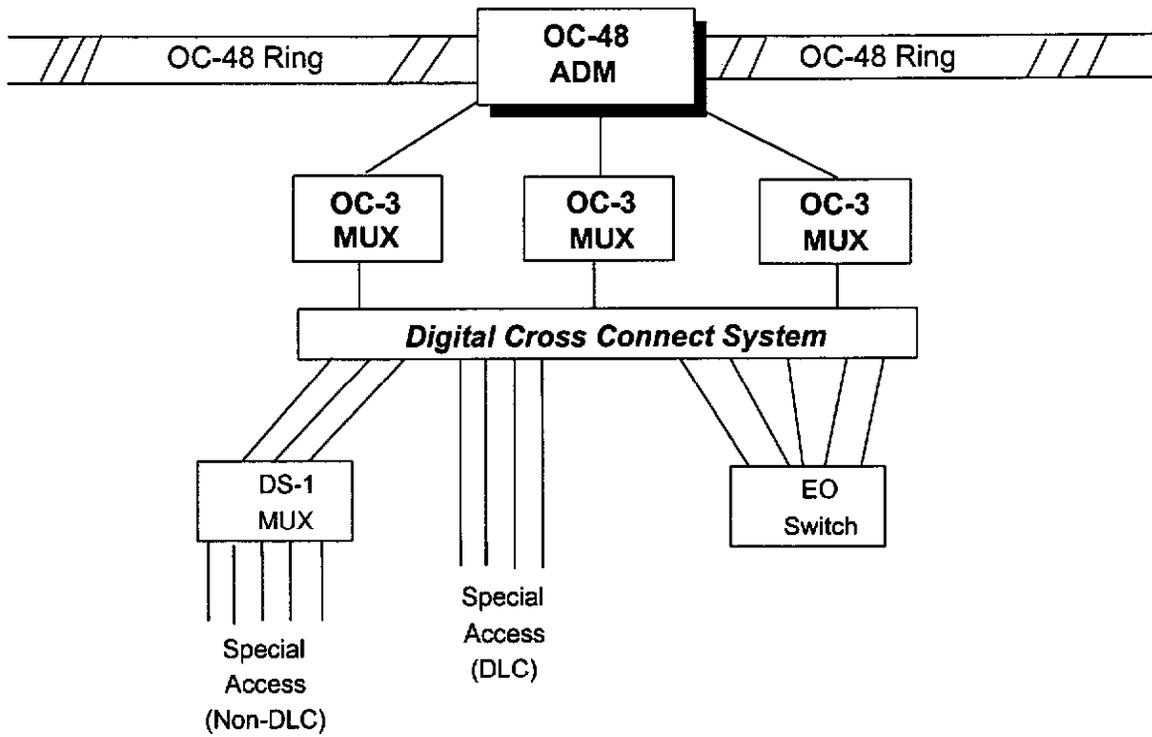
State	Factor ⁵⁷
New Hampshire	0.86
Montana	0.85
West Virginia	0.84
Ohio	0.83
Wisconsin	0.83
Arizona	0.81
Colorado	0.77
New Mexico	0.76
Vermont	0.75
Iowa	0.74
North Dakota	0.74
Idaho	0.73
Maine	0.73
Kentucky	0.73
Louisiana	0.72
Kansas	0.71
Utah	0.71
Tennessee	0.70
Oklahoma	0.69
Florida	0.68
Virginia	0.67
Nebraska	0.65
Texas	0.65
South Dakota	0.64
Georgia	0.62
Arkansas	0.61
Wyoming	0.60
Alabama	0.58
Mississippi	0.58
South Carolina	0.55
North Carolina	0.51

APPENDIX A

Interoffice Transmission Terminal Configuration (OC-3 Fiber Ring)



Interoffice Transmission Terminal Configuration (OC-48 Fiber Ring)



APPENDIX B

Structure Shares Assigned to Incumbent Local Telephone Companies

B.1. Overview

Due to their legacy as rate-of-return regulated monopolies, LECs and other utilities have heretofore had little incentive to share their outside plant structure with other users. To share would have simply reduced the "ratebase" upon which their regulated returns were computed. But today and going forward, LECs and other utilities face far stronger economic and institutional incentives to share outside plant structure whenever it is technically feasible. There are two main reasons. First, because utilities are now more likely to either face competition or to be regulated on the basis of their prices (e.g., price caps) rather than their costs (e.g., ratebase), a LEC's own economic incentive is to share use of its investment in outside plant structure. Such arrangements permit the LEC to save substantially on its outside plant costs by spreading these costs across other utilities or users. Second, many localities now strongly encourage joint pole usage or trenching operations for conduit and buried facilities as a means of minimizing the unsightliness and/or right-of-way congestion occasioned by multiple poles, or disruptions associated with multiple trenching activities.

Because of these economic and legal incentives, not only has structure sharing recently become more common, but its incidence is likely to accelerate in the future – especially given the Federal Telecommunications Act's requirements for nondiscriminatory access to structure at economic prices.

The degree to which a LEC can benefit from structure sharing arrangements varies with the type of facility under consideration. Sharing opportunities are most limited for multiple use of the actual conduits (e.g., PVC pipe) through which cables are pulled that comprise a portion of underground structure. Because of safety concerns, excess ILEC capacity within a conduit that carries telephone cables can generally be shared only with other low-voltage users, such as cable companies, other telecommunications companies, or with municipalities or private network operators. Although the introduction of fiber optic technology has resulted in slimmer cables that have freed up extra space within existing conduits, and thus enlarged actual sharing opportunities, the HAI Model does not assume that conduit is shared because as a forward-looking model of efficient supply, it assumes that a LEC will not overbuild its conduit so as to carry excess capacity available for sharing.

Trenching costs of conduit, however, account for most of the costs associated with underground facilities – and LECs can readily share these costs with other telecommunications companies, cable companies, electric, gas or water utilities, particularly when new construction is involved. Increased CATV penetration rates and accelerated facilities based entry by CLECs into local telecommunications markets will expand further future opportunities for underground structure sharing. In addition, in high density urban areas, use of existing underground conduit is a much more economic alternative than excavating established streets and other paved areas.

Sharing of trenches used for buried cable is already the norm, especially in new housing subdivisions. In the typical case, power companies, cable companies and LECs simply place their facilities in a common trench, and share equally in the costs of trenching, backfilling and surface repair. Gas, water and sewer companies may also occupy the trench in some localities. Economic and regulatory factors are likely to increase further incentives for LECs to schedule and perform joint trenching operations in an efficient manner.

Aerial facilities offer the most extensive opportunities for sharing. The practice of sharing poles through joint ownership or monthly lease arrangements is already widespread. Indeed, the typical pole carries the facilities of at least three potential users – power companies, telephone companies and cable companies. Power companies and LECs typically share the ownership of poles through either cross-lease or

condominium arrangements, or through other arrangements such as one where the telephone company and power company each own every other pole. Cable companies have commonly leased a portion of the pole space available for low voltage applications from either the telephone company or the power company. Methods of setting purchase prices and of calculating pole attachment rates generally are prescribed by federal and state regulatory authorities.

The number of parties wishing to participate in pole sharing arrangements should only increase with the advent of competition in local telecommunications markets. Economic and institutional factors strongly support reliance on pole sharing arrangements. It makes economic sense for power companies, cable companies and telephone companies to share pole space because they are all serving the same customer. Moreover, most local authorities restrict sharply the number of poles that can be placed on any particular right-of-way, thus rendering pole space a scarce resource. The Federal Telecommunications Act reinforces and regulates the market for pole space by prescribing nondiscriminatory access to poles (as well as to conduit and other rights-of-way) for any service provider that seeks access. The aerial distribution share factors displayed below capture a forward-looking view of the importance of these arrangements in an increasingly competitive local market.

B.2. Structure Sharing Parameters

The HAI Model captures the effects of structure sharing arrangements through the use of user-adjustable structure sharing parameters. These define the fraction of total required investment that will be borne by the LEC for distribution and feeder poles, and for trenching used as structure to support buried and underground telephone cables. Since best forward looking practice indicates that structure will be shared among LECs, IXC, CAPs, cable companies, and other utilities, default structure sharing parameters are assumed to be less than one. Incumbent telephone companies, then, should be expected to bear only a portion of the forward-looking costs of placing structure, with the remainder to be assumed by other users of this structure.

The default LEC structure share percentages displayed below reflect most likely, technically feasible structure sharing arrangements. For both distribution and feeder facilities, structure share percentages vary by facility type to reflect differences in the degree to which structure associated with aerial, buried or underground facilities can reasonably be shared. Structure share parameters for aerial and underground facilities also vary by density zone to reflect the presence of more extensive sharing opportunities in urban and suburban areas. In addition, LEC shares of buried feeder structure are larger than buried distribution structure shares because a LEC's ability to share buried feeder structure with power companies is less over the relatively longer routes that differentiate feeder runs from distribution runs. This is because power companies generally do not share trenches with telephone facilities over distances exceeding 2500 ft.⁵⁸

⁵⁸ A LEC's sharing of trenches with power companies, using random separation between cables for distances greater than 2,500 feet requires that either the telecommunications cable have no metallic components (i.e., fiber cable), or that both companies follow "Multi-Grounded Neutral" practices (use the same connection to earth ground at least every 2,500 feet).

Default Values in HM 5.0a

Structure Percent Assigned to Telephone Company						
Density Zone	Distribution			Feeder		
	Aerial	Buried	Under-ground	Aerial	Buried	Under-ground
0-5	.50	.33	1.00	.50	.40	.50
5-100	.33	.33	.50	.33	.40	.50
100-200	.25	.33	.50	.25	.40	.40
200-650	.25	.33	.50	.25	.40	.33
650-850	.25	.33	.40	.25	.40	.33
850-2550	.25	.33	.33	.25	.40	.33
2,550-5,000	.25	.33	.33	.25	.40	.33
5,000-10,000	.25	.33	.33	.25	.40	.33
10,000+	.25	.33	.33	.25	.40	.33

B.3. Support

Actual values for the default structure sharing parameters were determined through forward-looking analysis as well as assessment of the existing evidence of structure sharing arrangements. Information concerning present structure sharing practices is available through a variety of sources, as indicated in the references to this section. The HM 5.0a estimates of best forward-looking structure shares have been developed by combining this information with expert judgments regarding the technical feasibility of various sharing arrangements, and the relative strength of economic incentives to share facilities in an increasingly competitive local market. The reasoning behind the HAI Model's default structure sharing parameters is described below.

Aerial Facilities:

As noted in the overview to this section, aerial facilities (poles) are already a frequently shared form of structure, a fact that can readily be established through direct observation. For all but the two lowest density zones, the HAI Model uses default aerial structure sharing percentages that assign 25 percent of aerial structure costs to the incumbent telephone company. This assignment reflects a conservative assessment of current pole ownership patterns, the actual division of structure responsibility between high voltage (electric utility) applications and low voltage applications, and the likelihood that incumbent telephone companies will share the available low voltage space on their poles with additional attachers.⁵⁹

ILECs and Power Companies generally have preferred to operate under "joint use," "shared use," or "joint ownership" agreements whereby responsibility for poles is divided between the ILEC and the power company, both of whom may benefit from the presence of third party attachers. New York Telephone

⁵⁹ This sharing may be either of unused direct attachment space on the pole, or via co-lashing of other users' low voltage cables to the LEC's aerial cables. See, Direct Panel Testimony of Richard Wolf, Clay T. Whitehead, Donald Fiscella, David Peacock and Dr. Miles Bidwell on Behalf of the Electric Utilities, Case 95-C-0341: Pole Attachments, State of New York Public Service Commission, January 27, 1997.

reports, for example, that almost 63 percent of its pole inventory is jointly owned,⁶⁰ while, in the same proceeding, Niagara Mohawk Power Company reported that 58 percent of its pole inventory was jointly owned⁶¹. Financial statements of the Southern California Joint Pole Committee indicate that telephone companies hold approximately 50 percent of pole units⁶². Although proportions may vary by region or state, informed opinion of industry experts generally assign about 45 percent of poles to telephone companies. Note that both telephone companies and power companies may lease space on poles solely owned by the other.

While the responsibility for a pole may be joint, it is typically not equal. Because a power company commonly needs to use a larger amount of the space on the pole to ensure safe separation between its conductors that carry currents of different voltages (e.g., 440 volt conductors versus 220 volt conductors) and between its wires and the wires of low voltage users, the power company is typically responsible for a larger portion of pole cost than a telephone company.

Because of the prevalence of joint ownership, sharing, and leasing arrangements, it is unusual for a telephone company to use poles that are not also used by a power company. ILEC structure costs are further reduced by the presence of other attachers in the low voltage space. Perhaps the best example is cable TV. Rather than install their own facilities, CATV companies generally have leased low voltage space on poles owned by the utilities. Thus, the ILECs have been able to recover a portion of the costs of their own aerial facilities through pole attachment rental fees paid by the CATV companies. The proportion of ILEC aerial structure costs recoverable through pole attachment fees is now likely to increase still further as new service providers enter the telecommunications market.

As noted above, the other, most obvious reason for assigning a share of aerial structure costs as low as 25 percent to the ILEC is the way that the space is used on a pole. HM 5.0a assumes that ILECs install the most commonly placed pole used for joint use, a 40 foot, Class 4 pole.⁶³ Of the usable space on such a pole, roughly half is used by the power company which has greater needs for intercable separation. That leaves the remaining half to be shared by low voltage users, including CATV companies and competing telecommunications providers.

Thus, a) because ILECs generally already bear well less than half of aerial structure costs; b) because ILECs now face increased opportunities and incentives to recover aerial facilities costs from competing local service providers; c) because new facilities-based entrants will be obliged to use ILEC-owned structure to install their own networks; and, d) because the Telecommunications Act requires ILECs to provide nondiscriminatory access to structure as a means of promoting local competition, on a forward-looking basis, it is extremely reasonable to expect that ILECs will need, on average, to bear as little as 25 percent of the total cost of aerial structure.

⁶⁰ New York Telephone's Response to Interrogatory of January 22, 1997, Case 95-C-0341: Pole Attachments, State of New York Public Service Commission, January 27, 1997.

⁶¹ Direct Panel Testimony of Richard Wolf, Clay T. Whitehead, Donald Fiscella, David Peacock and Dr. Miles Bidwell on Behalf of the Electric Utilities, Case 95-C-0341: Pole Attachments, State of New York Public Service Commission, January 27, 1997. These experts also predicted that sharing of poles among six attachers would not be uncommon.

⁶² "Statement of Joint Pole Units and Annual Pole Unit Changes by Regular Members", Monthly Financial Statements of the Southern California Joint Pole Committee, October, 1996.

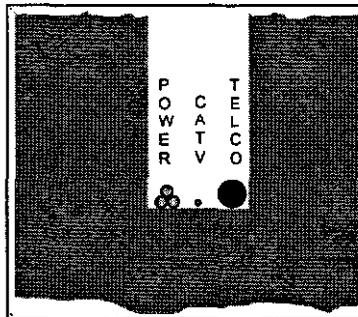
⁶³ Opinion of engineering team. Also, "The Commission {FCC} found that 'the most commonly used poles are 35 and 40 feet high, ...'" {FCC CS Docket No. 97-98 NPRM dtd 3/14/97 pg. 6, and 47 C.F.R. § 1.1402(c)}. A pole's "class" refers to the diameter of the pole, with lower numbers representing larger diameter poles.

Buried Facilities:

Buried structure sharing practices are more difficult to observe directly than pole sharing practices. Some *insight into the degree to which buried structure is, and will be shared can be gained from prevailing municipal rules and architectural conventions governing placement of buried facilities.* As mentioned in the overview, municipalities generally regulate subsurface construction. Their objectives are clear: less damage to other subsurface utilities, less cost to ratepayers, less disruption of traffic and property owners, and fewer instances of deteriorated roadways from frequent excavation and potholes.

Furthermore, since 1980, new subdivisions have usually been served with buried cable for several reasons. First, prior to 1980, cables filled with water blocking compounds had not been perfected. Thus, prior to that time, buried cable was relatively expensive and unreliable. Second, reliable splice closures of the type required for buried facilities were not the norm. And third, the public now clearly desires more out-of-sight plant for both aesthetic and safety related reasons. Contacts with telephone outside plant engineers, architects and property developers in several states confirm that in new subdivisions, builders typically not only prefer buried plant that is capable of accommodating multiple uses, but they usually dig the trenches at their own expense, and place power, telephone, and CATV cables in the trenches, if the utilities are willing to supply the materials. Thus, many buried structures are available to the LEC at no charge. The effect of such "no charge" use of developer-dug trenches reduces greatly the effective portion of total buried structure cost borne by the LEC. Note, too, that because power companies do not need to use a disproportionately large fraction of a trench – in contrast to their disproportionate use of pole space, and because certain buried telephone cables are plowed into the soil rather than placed in trenches, the HM 5.0a assumed LEC share of buried structure generally is greater than of aerial structure.

Facilities are easily placed next to each other in a trench as shown below:



Underground Facilities:

Underground plant is generally used in more dense areas, where the high cost of pavement restoration makes it attractive to place conduit in the ground to permit subsequent cable reinforcement or replacement, *without the need for further excavation.* Underground conduit usually is the most expensive investment per foot of structure -- with most of these costs attributable to trenching. For this reason alone, it is the most attractive for sharing.

In recent years, major cities such as New York, Boston, and Chicago have seen a large influx of conduit occupants other than the local telco. Indeed most of the new installations being performed today are cable placement for new telecommunications providers. As an example, well over 30 telecommunications

providers now occupy ducts owned by Empire City Subway in New York City.⁶⁴ This trend is likely to continue as new competitors enter the local market.

⁶⁴ Empire City Subway is the subsidiary of NYNEX that operates its underground conduits in New York City.

References

Industry experience and expertise of HAI

The knowledge of AT&T and MCI outside plant engineers.

Outside Plant Consultants

Montgomery County, MD Subdivision Regulations

Policy Relating to Grants of Location for New Conduit Network for the Provision of Commercial Telecommunications Services

Monthly Financial Statements of the Southern California Joint Pole Committee.

Conversations with representatives of local utility companies.

New York Telephone's Response to Interrogatory of January 22, 1997, Case 95-C-0341: Pole Attachments, State of New York Public Service Commission, January 27, 1997.

Direct Panel Testimony of Richard Wolf, Clay T. Whitehead, Donald Fiscella, David Peacock and Dr. Miles Bidwell on Behalf of the Electric Utilities, Case 95-C-0341: Pole Attachments, State of New York Public Service Commission, January 27, 1997.

"Statement of Joint Pole Units and Annual Pole Unit Changes by Regular Members", Monthly Financial Statements of the Southern California Joint Pole Committee, October 1996.

APPENDIX C

Expenses in HAI Model 5.0

Expense Group: Network Expenses

Explanation: Maintenance and repair of various categories of investment - outside plant (e.g., NID, drop, distribution, Service Area Interface, Circuit equipment, Feeder plant) and Central office equipment (e.g., switch)

Data Origin: New England Telephone Company Incremental Cost Study (switching and circuit operating expenses), HAI Consultant (NID), FCC 1996 ARMIS 43-03 (everything else).

- 6212 Digital Electronic Expense
- 6230 Operator Systems Expense
- 6232 Circuit Equipment Expense
- 6351 Public
- 6362 Other Terminal Equipment
- 6411 Poles
- 6421 Aerial Cable
- 6422 Underground Cable
- 6423 Buried Cable
- 6426 Intra-building Cable
- 6431 Aerial Wire
- 6441 Conduit Systems

Amount Determination: Expense-to-Investment ratio (NET Study, ARMIS); Dollar per Line for NID.

Application: Determine cost by multiplying Expense-to-Investment ratio times modeled investments; Determine NID cost by multiplying Dollar-per-Line times number of lines

Expense Group: Network Operations

Explanation: Network related expenses needed to manage the network but not accounted for on a plant type specific basis

Data Origin: 1996 ARMIS 43-03

- 6512 Provisioning Expenses
- 6531 Power Expenses
- 6532 Network Administration
- 6533 Testing
- 6534 Plant Operations Administration
- 6535 Engineering

Amount Determination: HAI default Network Operations Factor 50% times the embedded amount in ARMIS.

Application: Determine cost by allocating to unbundled network elements (UNEs) equiproportionally relative to UNE direct costs. Cost of "Network Administration" is allocated to traffic sensitive (i.e., switching, signaling and interoffice) UNEs only.

Expense Group: Network Support and Miscellaneous

Explanation: Miscellaneous expenses needed to support day to day operations

Data Origin: 1996 ARMIS 43-03

- | | |
|-------------------------------|----------------------|
| 6112 Motor Vehicles | HAI: Network Support |
| 6113 Aircraft | HAI: Network Support |
| 6114 Special Purpose Vehicles | HAI: Miscellaneous |
| 6116 Other Work Equipment | HAI: Miscellaneous |

Amount Determination: In essence, embedded ARMIS levels are scaled to reflect the relative change in either cable and wire (C&W) investment for Network Support Expenses or total investment for Miscellaneous Expenses in the modeled results versus ARMIS. For example:

HAI Cost

= Embedded ARMIS Expense x (HAI C&W Inv./ARMIS C&W Inv.)

The rationale is that these costs will be lower in a forward-looking cost study.

Application: Determine cost by allocating to unbundled network elements (UNEs) equiproportionally relative to direct costs

Expense Group: Other Taxes

Explanation: Taxes paid on gross receipts and property (i.e., 7240 Other Operating Taxes)

Data Origin: HAI expert estimate of 5% is based on overall Tier 1 Company ratio of ARMIS 7240 Expenses to ARMIS Revenues.

Amount Determination: Modeled costs are grossed up by 5%.

Application: Determine cost by allocating to unbundled network elements (UNEs) equiproportionally relative to direct costs.

Expense Group: Miscellaneous

Explanation: Miscellaneous expenses needed to support day to day operations

Data Origin: 1996 ARMIS 43-03

6122 Furniture

6123 Office Equipment

6124 General Purpose Computer

6121 Buildings

Amount Determination: In essence, embedded ARMIS levels are scaled to reflect the relative change in total investment in the HAI model versus ARMIS. For example:

HAI Cost

= Embedded ARMIS Expense x (HAI Tot. Inv./ARMIS Tot. Inv.)

The rationale is that these costs will be lower in a forward-looking cost study.

Application: Determine cost by allocating to unbundled network elements (UNEs) equiproportionally relative to direct costs.

Expense Group: Carrier-to-carrier customer service

Explanation: This category includes all carrier customer-related expenses such as billing, billing inquiry, service order processing, payment and collections. End-user retail services are not included in UNE cost development.

Data Origin: 1996 ARMIS 4304 (carrier-to-carrier cost to serve IXC access service)

7150 Service Order Processing

7170 Payment and Collections

7190 Billing Inquiry

7270 Carrier Access Billing System

Amount Determination: HAI multiplies embedded amount (across Tier 1 LECs) times 70% to get \$1.69 per line per year. The cost is determined by multiplying the cost per line times the number of lines. This figure includes the above business office activities, hence there is no need for a separate non-recurring charge to account for this activities. The underlying data that the UNE costs were developed from include other types of non-recurring costs outside the business office. Most of the non-recurring costs are captured in the HAI UNE estimate.

Application: Determine cost by allocating to unbundled network elements (UNEs) equiproportionally relative to direct costs.

Expense Group: Variable Overhead

Explanation: Executive, Planning and General and Administrative costs

Data Origin: 1996 ARMIS 43-03

- 6711 Executive
- 6712 Planning
- 6721 Accounting & Finance
- 6722 External Relations
- 6723 Human Resources
- 6724 Information Management
- 6725 Legal
- 6726 Procurement
- 6727 Research & Development
- 6728 Other General & Administrative

Amount Determination: HAI estimates 10.4% multiplier based on AT&T public data.

	<u>\$Mill</u>	<u>Source</u>
A Rev. Net of Settlements	36,877	Form M 1994
B Settlement Payout	4,238	Intl Traffic Data, 1994 data
C Gross Revenues	41,115	A + B
D Corporate Operations	3,879	Form M 1994
E Revenue less Corp. Op.	37,236	C - D
F Ratio	10.4%	D/E

Application: Cost is determined by multiplying the sum of all costs by 1.104.

Expense Group: Carrier-to-carrier Uncollectibles

Explanation: Revenues not realized associated with services provided (i.e., delinquency, fraud)

Data Origin: Company-specific ratio calculated from 1996 ARMIS 4304 Uncollectibles to 1996 ARMIS Access Revenues.

Amount Determination: Modeled costs are grossed up by the uncollectible rate.

Application: Determine cost by allocating to unbundled network elements (UNEs) equiproportionally relative to direct costs.

APPENDIX D

Network Operations Reduction

No matter what area of network operations one looks at, one observes a rich set of target opportunities for cost savings. In Account 6512, Network Provisioning, new technologies such as the Telecommunications Management Network (TMN) standards, procedures, and systems, and Digital Cross-Connect Systems (DCS) provide for much more centralized access and control, and self-provisioning by customers (including, and especially, knowledgeable CLECs). Given the tiered nature of TMN, where there are element, network, service, and business layers of management, some of the advantages of TMN will redound to the benefit of plant-specific expenses, while others, associated with the network, service and business management layers, will benefit the more-general activities included in network operations. The use of Electronic Data Interchange, intranet technology, and technologies such as bar coding provide substantial opportunities to reduce the costs of the inventory component of this category of accounts. On the human resources side, there is a greater emphasis on quality control in provisioning activities, reducing incipient failures in the services and elements provided.

As far as power expenses, Account 6531, digital components typically consume less power than their analog counterparts. Furthermore, centralization in other expense categories also spills over into this category, since centralization implies fewer buildings to power less of the time. Finally, due to the onset of competition in the electric power industry and the greater regulatory scrutiny of new generation resources, the industry is increasingly willing to provide price reductions to large business (and, increasingly, even residential and small business) customers. It is now quite common for firms to participate in energy programs in which, in exchange for reducing consumption during peak hours, they receive substantial discounts in the cost of power.

Network Administration, Account 6532, benefits from the deployment of SONET-based transport, because many administration activities are oriented to reacting to outages, which are lessened with the deployment of newer technologies. Testing, Account 6533, also benefits from the better monitoring and reporting capabilities provided by TMN and SONET. This can lead to more proactive, better-scheduled preventative maintenance. On the human resources side, there is a growing tendency for testing activities to be taken over by contractors, leading to lower labor costs for the ILECs. To the extent the activities are still performed by telephone company personnel, they can be performed by personnel with lower job classifications. Finally, the use of "hot spares" can reduce the need for out-of-hours dispatch and emergency restoral activities. Overall, fiber and SONET projects are often "proven in" partly on the assumption that they will produce significant operational savings.

Plant Operations and Administration, Account 6534, is likely to require fewer supervisory personnel, and more involvement by the vendors of equipment to the ILECs. For instance, as vendors take over many of the installation and ongoing maintenance activities associated with their equipment, there will be fewer ILEC engineers requiring management. The use of multi-skilled craft people will allow for fewer specialists to be sent out to address particular problems, and less supervision to manage the people that are sent out. It will, for instance, allow for greater span of control in supervisory and management ranks.

Finally, Engineering, Account 6535, will be more focused on activities associated with positioning the ILECs in a multi-entrant marketplace, less on the engineering of specific elements and services, as those activities become more automated and more in the hands of the purchasers of unbundled elements. To the extent that engineering addresses particular projects, or categories of projects, the use of better planning tools, such as the ability to geocode customer locations and sizes, will act to reduce the amount of such activities.

Additional specific reasons for adjusting the embedded level of these expenses include the following:

Recognize industry trends and the opportunities for further reductions. Network operations expenses, expressed on a per line basis, have already declined over the past several years. For the reasons described in the previous section, this trend is expected to continue as modern systems and technologies are deployed.

Eliminate incumbent LEC retail costs from the network operations expense included in the cost for unbundled network elements. A number of the sub-accounts (6533 Testing and 6534 Plant Operations Administration) include costs that are specific to retail operations that are not appropriately included in the cost calculated for unbundled network elements. A portion of the expenses booked to these sub-accounts represent activities that new entrants, rather than the incumbent LEC, will be performing. Analysis indicates that, as a conservative measure, 20% of the expenses in these two sub-accounts represent such retail activities and should be excluded. Since these two sub-accounts represent 56% of the total booked network operations expense, it is reasonable to conclude that, at a minimum, an additional 11% reduction should be applied to the historic booked levels of network operations expense.

Incorporate incumbent LEC expectations of forward-looking network operations expense levels. The Benchmark Cost Proxy Model ("BCPM"), sponsored by PacTel, Sprint, and US West, consistently calculates a level network operations expense per line that is well below historic levels and below the level calculated by the HAI Model. This projection of forward-looking network operations expenses, prepared for and advocated by three incumbent LECs, indicates that the HAI Model adjustment to the embedded levels of these expenses are appropriate and necessary (and may yield cost estimates that are conservatively high).

Minimize double counting of network operations expenses. A careful review of the way ARMIS account 6530 and the related sub-accounts (6531 Power, 6532 Network Administration, 6533 Testing, 6534 Plant Operations Administration, and 6535 Engineering) are constructed makes it clear that further adjustment is necessary to accurately produce forward-looking costs. Many of the engineering and administrative functions that are included in these accounts are recovered by the incumbent LECs through non-recurring charges. Without such an adjustment, these costs may be double-recovered through existing non-recurring charges and simultaneously through the recurring rates based on the HAI Model results. Similarly, double recovery is possible because these accounts are constructed as so-called "clearance accounts" where expenses are booked before they are assigned to a specific project. Without an adjustment, these expenses could be recovered as service or element-specific costs and as the shared costs represented by network operations expense.

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