

UNITED STATES OF AMERICA
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

Rate and Service Changes To Implement
Functionally Equivalent Negotiated Service
Agreement With HSBC North America Holdings Inc.

Docket No. MC2005-2

PRESIDING OFFICER'S INFORMATION REQUEST NO. 1

(Issued March 10, 2005)

The proponents are requested to provide the information described below to assist in developing a record for the consideration of their request. In order to facilitate inclusion of the requested material in the evidentiary record, either the Postal Service or HSBC North America Holdings Inc., as appropriate, is to have a witness attest to the accuracy of the answers and be prepared to explain to the extent necessary the basis for the answers. The answers are to be provided by March 22, 2005.

1. (a) Does HSBC create solicitations mailing lists by employing internally generated and maintained databases, or does it rely on purchased lists with list vendors maintaining the accuracy of the addresses? If a combination of different methodologies is used, what is the percentage of each type?
- (b) Please elaborate on what actions HSBC intends on taking after receiving electronic address correction information from the Postal Service, specifically including what steps will be taken to correct addresses contained within each type of solicitations mailing list discussed in (a).

2. Witness Dauer proposes a data collection plan based on the Capital One data collection plan. USPS-T-1 Appendix C. The proposed plan omits the collection of data on volume of HSBC Standard Mail solicitations by rate category as was required by the Capital One data collection plan. It also omits a Commission requirement to provide a comparison of the estimated mailer-specific costs, volumes, and revenues with the actual mailer-specific costs, volumes, and revenues. See rule 193(g). Finally, it does not impose a deadline on the periodic submission of reports. See, e.g., PRC Op. MC2004-3 at 85 fn. 49. The addition of the following three statements to the HSBC data collection plan, appropriately placed, would correct for these deficiencies:

“Volume of HSBC Standard Mail solicitations by rate category.”

“A comparison of the estimated mailer-specific costs, volumes, and revenues with the actual mailer-specific costs, volumes, and revenues.”

“Each report is to be provided within 120 days after the end of each fiscal year during which the Negotiated Service Agreement is in effect. Items 1, 2, 4 through 7, and 11 are to be reported as monthly data for the previous fiscal year.”

Similar changes were incorporated into the Bank One data collection plan. See PRC Op. MC2004-3 at 83-5. Is there any objection (and if so please elaborate) to incorporating the above items into the HSBC data collection plan?

3. The Postal Service Request Attachment E-18 identifies the record testimony from the baseline agreement docket, or any previously concluded docket, on which

the Postal Service proposes to rely. In Docket Nos. MC2004-3 and MC2004-4, the equivalent attachments referenced Library References from Docket No. R2001-1, specifically: USPS-LR-J-58, J-60 (as revised 11/15/2001), and J-69 (as revised 11/5/2001), and PRC-LR-2, 4, and 7. Does the Postal Service intend to rely on these same Library References in the HSBC docket?

Note: The PRC Library References technically are not “record evidence.” However, the Commission found it helpful when the Postal Service included these items in previous dockets under this data requirement item. It is beneficial to have all sources listed in one place. Also, this provides potential intervenors with a single, concise list of materials from previous dockets to be considered in making an intervention decision in the instant docket. (This more inclusive interpretation of rule 196(a)(3) is suitable for comment in ongoing rulemaking Docket No. RM2005-2.)

4. The Negotiated Service Agreement contract defines solicitation mail that contains convenience checks endorsed “Return Service Requested” as First-Class Mail “operational mail.” Request Attachment F at III.C.1. The contract also states that the one exception to the requirement that the CSR endorsement be applied to all First-Class Mail solicitations will be solicitations mail that contains convenience checks, which will continue to be endorsed “Return Service Requested” and treated by the Postal Service in accordance with that endorsement. *Id.* at II.A. Additional information on the characteristics of “conditional check mail” is necessary to assess the financial impact of this type of mail on the Negotiated Service Agreement. Is the volume of “conditional check mail” included in the solicitations mail or operational mail estimates? If the return rate of “conditional check mail” is different from the category where the volumes are accounted for, how is the return rate for “conditional check mail” factored into the financial analysis? If “conditional check mail” volumes are treated as solicitations mail,

please provide for each year of the agreement: (1) the estimated volume of "conditional check mail," and (2) the estimated return rate of "conditional check mail."

5. For the following question refer to the two attached tables (MC2002-2, Attachment A, page 2 and MC2005-2, Appendix A, page 5).

In the baseline Negotiated Service Agreement (Docket No. MC2002-2), the calculation of estimated unit costs by rate category is presented in USPS-T-3, Attachment A, page 2. The "TY 2003 Total Unit Cost" in column 14 is the sum of Mail Processing, Delivery and "Other" unit costs. Mail Processing and Delivery costs are taken directly from PRC library references from the most recent omnibus rate case (Docket No. R2001-1), and the remaining "Other" unit costs are calculated by subtracting the weighted average unit costs of mail processing (column 11) and delivery (column 12) from the total unit "TY 2003 Total Unit Cost" in column 10. This ensures that the two "TY 2003 Total Unit Costs" (columns 10 and 14) are equal. Because the total unit cost in column 10 is the cost for presorted mail in the First-Class Mail Letters subclass (all shapes), the weighted average costs used in the calculation of "Other Unit Cost" include the costs of automation presort flats.

In the two subsequent Negotiated Service Agreements, the unit costs for each rate category from the baseline case were adopted. (See MC2004-3, USPS-T-1, Appendix A at 4-5 and MC2004-4, USPS-T-1, Appendix A at 4-5.)

In the current proposal, the weighted average mail processing and delivery costs are recalculated to reflect only the letter-shaped rate categories. Then, the new weighted average mail processing and delivery costs are subtracted from the total unit cost of presorted mail in the First-Class Letters subclass (all shapes).

Consequently, the “Other” costs are calculated as the difference between the total cost of all shapes and the mail processing and delivery costs of letter-shaped pieces. (See USPS-T-1, Appendix A at 5-6.)

Please explain the rationale for the change in the “TYBR 2003 Other Unit Cost” from the baseline and prior functionally equivalent Negotiated Service Agreements.

MC2002-2, Attachment A, page 2

CAPITAL ONE FIRST-CLASS MAIL PRESORT LETTERS/FLATS UNIT COST ESTIMATES

Capital One Solicitation Return Percentage = 9.5% (1)
 Capital One Solicitation Return Percentage = 9.5% (1)
 Average Letters Return Percentage = 1.3% (2)
 Before Rates Customer Mail Volume = 640,000,000 (4)
 Manual Returns Unit Volume = 768,000,000 (6)
 Manual Returns Unit Cost = \$0.533 (6)
 Electronic Returns Unit Cost = \$0.332 (7)
 Address Change Service (ACS) Success Rate = 85.0% (8)
 Contingency Factor = 1.020 (9)

Rate Category	DOCKET NO. R2001-1 PRC FIGURES - NATIONWIDE MAIL MIX										DOCKET NO. R2001-1 PRC FIGURES - CAPITAL ONE MAIL MIX				
	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)	(21)	(22)	(23)	
	TY 2003 Total Unit Cost (\$/unit)	TY 2003 Mail Proc Unit Cost (\$/unit)	TY 2003 Delivery Unit Cost (\$/unit)	TY 2003 Other Unit Cost (\$/unit)	TY 2003 Total Unit Cost (\$/unit)	FY 2001 Mail Volume (Pieces)	Current Returns Adjustment Unit Cost (\$/unit)	Current Returns Adjustment Unit Cost (\$/unit)	After Rates Returns Adjustment Unit Cost (\$/unit)	After Rates Returns Adjustment Unit Cost (\$/unit)					
Nonautomation Presort Letters															
Automation Presort Letters															
Automation Mixed ADC	\$0.115	\$0.163	\$0.063	\$0.018	\$0.244	3,702,478,000	7.84%	\$0.244	57,664,188	5.01%					
Automation Mixed ADC		\$0.055	\$0.045	\$0.018	\$0.118	2,634,682,000	5.58%	\$0.118	55,754,928	5.10%					
Automation 3-Digit		\$0.042	\$0.042	\$0.018	\$0.104	22,424,269,000	47.80%	\$0.104	536,430,082	46.78%					
Automation 5-Digit		\$0.032	\$0.041	\$0.018	\$0.091	14,038,959,000	29.73%	\$0.091	389,430,336	32.10%					
Automation Carrier Route		\$0.021	\$0.064	\$0.018	\$0.103	1,020,856,000	2.16%	\$0.103	63,511,973	5.52%					
Automation Presort Flats															
Automation Mixed ADC		\$0.448	\$0.095	\$0.018	\$0.562	52,631,000	0.11%	\$0.562	31,247	0.00%					
Automation ADC		\$0.348	\$0.095	\$0.018	\$0.461	28,190,000	0.06%	\$0.461	16,737	0.00%					
Automation 3-Digit		\$0.235	\$0.095	\$0.018	\$0.348	18,789,000	0.40%	\$0.348	3,683	0.03%					
Automation 5-Digit						234,233,000	0.34%		5,376	0.00%					
WEIGHTED AVERAGE / TOTAL	\$0.115	\$0.062	\$0.045	\$0.018	\$0.115	47,214,206,000	100.00%	\$0.108	1,161,030,386	100.00%	\$0.024	\$0.130	\$0.0153	\$0.1229	

Total Unit Cost Estimates, including Contingency = **\$0.139** Current (24) **\$0.1266** After Rates (25)

(1) Capital One witness Jean
 (2) Capital One witness Jean
 (3) USPS-LR-68 FROM UAA % from Table 4.2 allocated by Return to Sender % from Table 4.3.3
 (4) COS-T-2, Exhibit 6
 (5) COS-T-2, Exhibit 6
 (6) "MANUAL RETURNS UNIT COST" Spreadsheet
 (7) "ELECTRONIC RETURNS UNIT COST" Spreadsheet
 (8) USPS witness Wilson
 (9) Docket No. R2001-1, PRC LR-3, Volume 4, "TY08", page 3
 (10) Letter Docket No. R2001-1, PRC LR-4, "ELECTRONIC RETURNS UNIT COST" spreadsheet, page 1
 (11) Letter Docket No. R2001-1, PRC LR-4, "ELECTRONIC RETURNS UNIT COST" spreadsheet, page 1
 (12) Docket No. R2001-1, PRC LR-7, Page 2
 (13) (10) - Weighted Average(11) - Weighted Average(12)
 (14) (11) + (12) + (13)

MC2005-2, Appendix A, page 5

Rate Category	HSBC MAIL MIX													(18)		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)		(14)	(15)
	TYBR 2003 Unit Cost (Dollars)	TYBR 2003 Mail Proc Unit Cost (Dollars)	TYBR 2003 Delivery Unit Cost (Dollars)	TYBR 2003 Other Unit Cost (Dollars)	TYBR 2003 Total Unit Cost (Dollars)	FY 2005 Total Unit Cost (Dollars)	BY 2000 Mail Volume (Pieces)	FY 2003 Mail Volume (Pieces)	FY 2003 Mail Volume (Percent)	TY 2005 Total Unit Cost (Dollars)	FY 2004 Mail Volume (Pieces)	FY 2004 Mail Volume (Percent)	Current Returns Adjustment Unit Cost (Dollars)	Current w/Ret's Adj Total Unit Cost (Dollars)	After Rates Returns Adjustment Unit Cost (Dollars)	After Rates w/Ret's Adj Total Unit Cost (Dollars)
FIRST-CLASS MAIL LETTERS																
Nonautomation Presort Letters	0.163		0.063	0.021	0.247	0.267	3,748,977,000	2,673,332,488	5.9%	0.267	9,805,861	2.2%				
Automation Presort Letters																
Automation Mixed AADC	0.055		0.045	0.021	0.121	0.130	2,504,846,824	2,820,686,002	6.1%	0.130	31,387,770	7.1%				
Automation AADC	0.046		0.044	0.021	0.110	0.119	2,680,656,176	2,636,650,800	5.7%	0.119	41,788,164	9.5%				
Automation 3-Digit	0.042		0.043	0.021	0.108	0.115	21,832,339,000	22,571,247,888	48.6%	0.115	294,042,110	60.1%				
Automation 5-Digit	0.032		0.041	0.021	0.093	0.101	12,729,447,000	14,870,254,100	34.1%	0.101	79,252,286	17.5%				
Automation Carrier Route	0.021		0.044	0.021	0.105	0.114	1,075,353,000	602,292,629	1.7%	0.114	14,357,085	3.3%				
WEIGHTED AVERAGE TOTAL	0.050		0.045	0.021	0.111	0.120	44,562,599,000	46,415,243,896	100.0%	0.117	439,697,836	100.0%	(0.0055)	0.112	(0.0055)	0.112
Total Unit Cost Estimates, Including Contingency =															(17)	(18)
																0.113

(1) Docket No. R2001-1, PRC LR-2, Volume 4, TYBRP, page 3
 (2) Docket No. R2001-1, PRC LR-4, FGLTPRCFALXLSF, page 1
 (3) Docket No. R2001-1, PRC LR-7, Page 2
 (4) (1) - Weighted Average(2) - Weighted Average(3)
 (5) (2) + (3) + (4)
 (6) (1) - Weighted Average(2) - Weighted Average(3) * (1 + inflation cost adjustment factor)
 (7) Docket No. R2001-1, PRC LR-7, Page 2
 (8) Revenue, Pieces, and Weight (RPW) Report.
 (9) (8) / (Sum (8))
 (10) Line Item (6), Weighted Average weighted by percentages in (12).
 (11) CBS 2004 HSBC Volume Data
 (12) (10) * (13)
 (13) (Manual Letter Return Unit Cost * After Rates Statement Mail) + (Statement Mail Return Forecast - USPS FCM Avg. Return Rate) / After Rates Statement Mail
 (14) (10) * (13)
 (15) (Manual Letter Return Unit Cost * After Rates Statement Mail) + (Statement Mail Return Forecast - USPS FCM Avg. Return Rate) / After Rates Statement Mail
 (16) (10) * (15)
 (17) Contingency Factor (Assumptions)
 (18) (16) * Contingency Factor (Assumptions)

6. USPS-T-1 states at page 13:

The Postal Service evaluated the proposed cap using Commission's logic of the Docket MC2004-4 to establish its position while in negotiations with HSBC. The Postal Service used a 100 percent pass through of the ACS cost savings of \$8.1 million plus the competitive adjustment given in Docket MC2004-04 of 10.09 percent. This equals \$8.9 million (\$8.1 million + \$.8 million).

(a) Please refer to the following table. Following the Commission's methodology for calculating the value of the stop-loss cap used in Docket No. MC2004-4 (at 100 percent pass through) and then increasing this value by 10.09 percent, please verify that the calculated cap would equal \$8.727 million. See PRC Op. MC2004-4 at 38, Table 6.

(b) Please verify that the Postal Service then adds an additional [(\$9 million / \$8.9 million) - 1] or 1.12 percent to its calculated value, which when similarly added to the calculated value above would result in a final stop-loss cap value of \$8.825 million.

Table 1. Calculation of Stop-Loss Cap

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total NSA</u>
A. Effects of ACS (Savings Estimate)				
First-Class Mail Marketing Letters:				
Avg. Savings from Returns	0.0088	0.0092	0.0096	
Avg. Savings (Cost) from Forwards	0.0000	0.0000	0.0000	
Total Avg. Savings from ACS	0.0088	0.0092	0.0096	
Before Rates Volume	195,735,891	297,522,231	361,504,700	
Net Contribution Gain from ACS (Savings)	1,731,501	2,737,190	3,458,859	7,927,549
B. Effects of Lost Contribution (Revenue Leakage)				
Before Rates First-Class Volume	678,757,162	815,929,752	917,974,638	
Volume Threshold for Discounts	615,000,000	725,000,000	810,000,000	
Before Rates Volume Eligible for Discounts	63,757,162	90,929,752	107,974,638	
Average Discount on "Exposed" Volume	0.0272	0.0301	0.0320	
Total Discounts on Before Rates Volume (Leakage)	(1,731,501)	(2,737,190)	(3,458,859)	(7,927,549)
Net Increase in Contribution (before rates volume)	-	-	-	-
Savings from ACS at Break-Even Volume	7,927,549 ^{1/}			
Pass-through Percentage	100%			
Stop-Loss Cap Amount	7,927,549			
Ratio of DFS "Competitive Cap" to PRC Cap	1.1009			
Cap with "Competitive Adjustment"	8,727,439			
Percentage increase to round up to \$9 million	1.12%			
Cap with "Competitive Adjustment" and rounding effect	8,825,187			

1/ This figure reflects the methodology employed by the Commission in Docket Nos. MC2004-3 and MC2004-4.

7. In Docket Nos. MC2004-3 and MC2004-4, the Postal Service's estimates of cost savings from the avoidance of physical returns were modified by the application of a contingency factor to the estimated total savings in each year of the agreement. In contrast, witness Dauer applies the contingency factor to the costs of physical and electronic returns (i.e., at the beginning of the calculation, instead of the end). Please explain the rationale for this change in methodology. Include a discussion of the impact on the estimated before and after rates unit

costs of HSBC's solicitations and operational First-Class Mail. Specifically, address the implications of using the contingency adjusted costs of physical and electronic returns in the calculation of cost estimates that are themselves adjusted by the contingency factor.

8. Please refer to HSBC-T-1 at 6-9.

(a) Has HSBC used Address Correction Service for First-Class Mail solicitations? If so, please provide the following information:

- i. Identify any time period over which the service was used;
- ii. Identify the date the service was last used; and
- iii. If the service is no longer used, describe the reasons for discontinuing use of the service.

(b) Witness Harvey bases his return rate estimates on historical business records. Please provide this information (or a detailed summary of this information) including the time period upon which the estimate is based.

(c) Please identify any changes in the nature of HSBC's recent First-Class Mail solicitations that may have affected return rates as compared to the mail upon which witness Harvey based his estimates. Also please discuss the effect, if any, that HSBC's planned business expansion might have on the return and forwarding rates of HSBC's First-Class Mail (both solicitations and operational mail) during the term of the agreement. Please explain any adjustments incorporated into witness Harvey's estimates to account for such changes.

9. Please refer to USPS-T-1 at 13-17 and Docket No. MC2002-2, Tr. 2/334. Witness Dauer accepts the forecasts of before-rates volume, after-rates volume and estimated return rates provided by HSBC witness Harvey (HSBC-T-1) and

characterizes the after-rates volume estimates as conservative. Please provide any independent analysis done by the Postal Service to evaluate the reasonableness of the mailer-provided forecasts of: (a) before-rates volumes, (b) after-rates volumes, and (c) estimated return rates.

10. Please Refer to Docket No. MC2002-2, Opinion para. 3050-51, and Tr. 9/1868 and 1876. In that case, the Postal Service indicated that it was reviewing possible pricing approaches to physical return of mail and electronic equivalents to consider alternative ways to address the apparent pricing anomaly with respect to the return of undeliverable-as-addressed First-Class Mail. Please update the Commission on the status of this review and how it affected the Postal Service's decision to enter into the proposed agreement with HSBC.

George Omas
Presiding Officer