BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C.   20268-0001

EXPERIMENTAL RATE AND SERVICE
CHANGES TO IMPLEMENT NEGOTIATED
SERVICE AGREEMENT WITH
CAPITAL ONE SERVICES, INC.
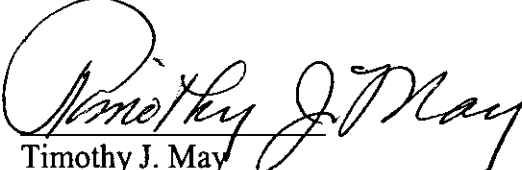
DOCKET No. MC2002-2

RESPONSE OF CAPITAL ONE SERVICES, INC.

WITNESS STUART ELLIOTT TO INTERROGATORIES OF

OFFICE OF CONSUMER ADVOCATE

FILED ON OCTOBER 4, 2002

(OCA/COS-T2-1-4)

Capital One Services, Inc hereby provides the response of witness Stuart Elliott to the following interrogatories of Office of Consumer Advocate: OCA/COS-T2-1-4, filed on October 4, 2002.

Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted

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Dated: October 15, 2002

OCA/COS-T2-1.   Please turn to Exhibit 6 of your testimony.

(a) At line 7, does any of the increase in the "First-Class Mail Solicitation Volume

Increase" consist of mail that would be sent via Standard Mail absent the

proposed NSA? If your answer is "Yes," please provide the increase in volume

that is Standard Mail.

(b) At line 8, does any of the "First-Class Customer Mail Volume Increase" consist of

mail pieces that would have been sent absent the proposed NSA? If your

answer is "Yes," please provide the increase in volume that would have been

sent in the absence of the proposed NSA.

(c) At line 8, does any of the "First-Class Customer Mail Volume Increase" consist of

pieces migrating from other billing mediums as a result of the NSA? If your

answer is "Yes," please provide the increase in volume that is migrating from

other billing mediums as a result of the NSA.

(d) At line 10, you project "After-Rates First-Class Mail Solicitation Volume" at

776,432,165 pieces. Under what circumstances would the annual increase to

this volume, 8,432,165 (at line 7), be larger in future years? Please explain why

there would be an increase, and please quantify the projected increase.

(e) At line 10, you project "After-Rates First-Class Mail Solicitation Volume" at

776,432,165 pieces. Under what circumstances would the annual increase to

this volume, 8,432,165 (at line 7), be smaller in future years? Please explain why

there would be a decrease, and please quantify the projected decrease.

(f) At line 11, you project "After Rates First-Class Customer Mail Volume" at

647,026,804 pieces. Under what circumstances would the annual increase to

this volume, 7,026,804 (at line 8), be larger in future years? Please explain why there would be an increase, and please quantify the projected increase.

(g) At line 11, you project "After Rates First-Class Customer Mail Volume" at 647,026,804 pieces. Under what circumstances would the annual increase to this volume, 7,026,804 (at line 8), be smaller in future years? Please explain why there would be a decrease, and please quantify the projected decrease.

ANSWER

OCA/COS-T2-1 Response.

(a)   No.

(b)   No.

(c)   No.

(d)   Aside from any hypothetical future change to the underlying price elasticity, the projected annual increase would be larger in "future years" if the projected First-Class Mail Solicitation Volume in future years were larger than is projected for FY 2003.

(e)   Aside from any hypothetical future change to the underlying price elasticity, the projected annual increase would be smaller in "future years" if the projected First-Class Mail Solicitation Volume in future years were smaller than is projected for FY 2003.

(f)   Aside from any hypothetical future change to the underlying price elasticity, the projected annual increase would be larger in "future years" if the projected First-Class Customer Mail Volume in future years were larger than is projected for FY 2003.

(g)   Aside from any hypothetical future change to the underlying price elasticity, the
        projected annual increase would be smaller in "future years" if the projected First-
        Class Customer Mail Volume in future years were smaller than is projected for
        FY 2003.

OCA/COS-T2-2.   **Please refer to Exhibit 6.**

(a)   At line 5, please confirm that the "Marginal Price Discount from NSA" of –15.5

percent is estimated on the basis of achieving a certain level of mail volume,

specifically 1.375 to 1.45 billion pieces. If you do not confirm, please explain and

provide a detailed explanation of your conclusion(s).

(b)   Please confirm that the "Marginal Price Discount from NSA" of –15.5 percent at

line 5 and the "Price Elasticity-Workshared First-Class Letters" of –0.071 at line 4

are then used in an elasticity analysis to estimate the increase in solicitation mail

volume. If you do not confirm, please explain and provide a detailed explanation

of your conclusion(s).

(c)   Please confirm that the increase in mail plus the original, assumed volume of

mail yield after-rates volume of 776, 432,165, which coupled with the increase in

after-rates First-Class customer mail volume, results in total volume of

1,423,458,969 pieces. If you do not confirm, please explain and provide a

detailed explanation of your conclusion(s).

ANSWER

OCA/COS-T2-2 Response.

(a)   Confirmed.

(b)   Confirmed.

(c)   Confirmed.

OCA/COS-T2-3.   Please refer to Exhibit 6, footnote 5.

Please confirm that you have estimated the amount of the discount based on an assumed volume projection, and this assumed volume projection is then used with an elasticity estimate to arrive at the final volume projection. If you do not confirm, please explain. If you do confirm, please explain why your reasoning is not circular.

ANSWER

OCA/COS-T2-3 Response.

Confirmed. The analysis in Exhibit 6 involves simultaneity, not circularity. Essentially it is the solution of a problem of two equations with two unknowns. The two unknowns are the marginal price discount and the after-rates volume. One equation is provided by the price elasticity, which specifies that the quotient of the marginal percentage volume change and the marginal percentage price change must be -0.071. (The marginal percentage volume change implies, in turn, the after-rates volume.) The second equation is provided by the terms of the NSA, which relate the marginal price discount to the after-rates volume. Because the second equation is a step function, it is possible to solve the two equations by using an "assumed volume projection" to derive the marginal price discount and then to confirm that the final volume projection is consistent with the assumed volume projection.

OCA/COS-T2-4.   Please turn to your testimony at page 5, lines 11-16.

(a)   Please confirm that you apply the Postal Service's Standard Mail elasticity to

estimate the upper bound of the increase in the after-rates volume of First-Class

solicitation mail. If you do not confirm, please explain.

(b)   Please provide an economic rationale that supports the use of the Standard Mail

elasticity rather than an elasticity for First-Class Mail to estimate the upper bound

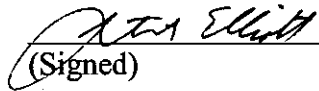of the increase in the after-rates volume of First-Class solicitation mail.

ANSWER

OCA/COS-T2-4 Response.

(a)   Confirmed in part. My testimony applies the Postal Service's Standard Regular

Mail elasticity in its second method for estimating the increase in the after-rates

volume of First-Class solicitation mail. However, my testimony does not

calculate an "upper bound" for the increase in the after-rates volume of First-

Class solicitation mail.

(b)   On economic grounds, it is reasonable to think that different types of mail within a

subclass may have different price elasticities, depending on the economic

calculations that underlie the decisions about how much volume to mail. Since

advertisements make up 90.8 percent of Standard Mail mailpieces received by

households (USPS-LR-J-104/R2001-1, Table A3-1), the Postal Service's

estimate of the price elasticity of Standard Regular Mail is likely to be a good

proxy for the price elasticity of solicitation mail in general. The second method

uses this Postal Service estimate as a proxy for the price elasticity of Capital

One's First-Class Mail solicitations. Note, however, that my testimony does not

calculate an "upper bound" for the increase in the after-rates volume of First-Class Mail solicitations.
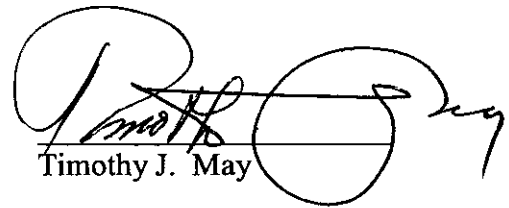
DECLARATION

I, Stuart Elliott, declare under penalty of perjury that the foregoing answers are true and correct to the best of my knowledge, information and belief.

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(Signed)

October __/4__ , 2002

CERTIFICATE OF SERVICE

I hereby certify that I have this date served six (6) copies of the foregoing document upon the United States Postal Service by hand in accordance with Section 12 of the Rules of Practice.

Timothy J. May

Dated: October 15, 2002