

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 UNITED STATES POSTAL SERVICE WITNESS BIZZOTTO  
TO INTERROGATORIES OF THE NEWSPAPER ASSOCIATION OF AMERICA  
(NAA/USPS-T1-4-8(h), 8(j)-15)

The United States Postal Service hereby provides the responses of witness Bizzotto to the following interrogatories of the Newspaper Association of America: NAA/USPS-T1-4 – 8(h), 8(j) –15, filed on November 15, 2002. Interrogatory NAA/USPS-T1-8(i) was redirected to witness Plunkett.

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

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.  
Chief Counsel, Ratemaking

Scott L. Reiter

475 L'Enfant Plaza West, S.W.  
Washington, D.C. 20260-1137  
(202) 268-2999 Fax -5402  
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**NAA/USPS-T1-4.** Were you the Postal Service officer with principal supervisory authority over the negotiations with Capital One?

**RESPONSE:**

No. The Postal Service officer with principal supervisory authority over the negotiations with Capital One was Stephen M. Kearney, Vice-President, Pricing and Classification.

As Chief Marketing Officer and Senior Vice-President, I am responsible for the overall strategic direction of the Postal Service's marketing initiatives including negotiated service agreements; however, I do not directly supervise contract negotiations.

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**NAA/USPS-T1-5.** Please describe the review process by which the Postal Service internally considered the Capital One NSA and contrast that to the process for an omnibus rate case. In particular, please summarize the major ways in which that review was similar to, and different from, the review accorded the preparation of an omnibus rate case filing.

**RESPONSE:**

The process used to review the Capital One NSA is the same process used to review an omnibus rate case or any other rate or classification request filed with the Postal Rate Commission. Any proposed rate or classification request including the Capital One NSA is:

1. Discussed with senior management for review of the proposal and the projected impact on the Postal Service's finances.
2. Presented to the Executive Committee for review prior to submission to the Board of Governors.
3. Presented to the Board of Governors with a financial summary, the policy rationale, and a Management recommendation for a Postal Rate Commission filing.
4. Approved for filing by a vote of the Governors of the Postal Service.
5. Filed with the Postal Rate Commission for review as required by the Postal Reorganization Act.

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**NAA/USPS-T1-6.** Did the Postal Service prepare, for internal purposes, an analysis of the return on investment of the Capital One NSA? If so, please describe how the Postal Service and/or the Governors used that analysis.

**RESPONSE:**

No. The Postal Service does not generally prepare an analysis of the return on investment for rate or classification proposals, including the Capital One NSA. The Postal Service's objective in developing new rates or classifications is not to maximize the return on investment; rather, it is to meet the policy goals set out in the Postal Reorganization Act. Therefore, as with any rate or classification proposal, the Postal Service carefully evaluated the Capital One NSA for consistency with the statutory criteria (USPS-T-2 at 8-10), and developed a financial analysis evaluating the estimated net contribution from the proposal and ensuring that no cross-subsidies exist (USPS-T-3.) As described in the response to NAA/USPS-T1-5, the results of these analyses are presented to senior management and the Board of Governors.

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**NAA/USPS-T1-7.** As the Chief Marketing Officer of the Postal Service, do you believe that, as a general policy applicable to all NSAs, an NSA for a specific customer should be based on postal costs applicable to the mail of that specific customer, or on average costs for all mail of the relevant type?

- a. Should the Capital One NSA be based on postal costs applicable to the mail of that specific customer, or average costs for all mail of the relevant type?
- b. Do the “unique circumstances” of the Capital One NSA warrant any departure from what you would advocate as a general policy? Please explain your answer.

**RESPONSE:**

I believe that any rate or classification proposal, including negotiated service agreements such as the Capital One agreement, should be developed using the best data available including the Postal Service’s understanding of the characteristics and requirements of specific mailers.

- a. To the extent that data are available on the specific cost characteristics of serving an individual customer, that data should be used in evaluating a negotiated service agreement. At the same time it is not practical to expect that the Postal Service’s data systems can be used to measure the costs for selected customers in the same way they are designed to measure costs for entire classifications in the aggregate.

In the case of the Capital One NSA, the Postal Service has used data about Capital One’s mailing and returns profile as a fundamental input in developing the financial analysis of the agreement. However, it is appropriate to take and to appropriately adjust aggregate cost data to reflect customer-specific information.

Analysis of any NSA must take a reasoned approach, balancing the need for customer-specific information with the difficulty and expense in developing customer-specific cost studies. Finally, this hybrid approach to developing NSAs

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must be measured against our understanding of the customer and its mailing operations and requirements. Informed judgment has always played a role in postal ratemaking, especially in evaluating the policy implications of a proposal, and we cannot ignore this in a quest for a formulaic approach to the evaluation of NSAs.

- b. No. The approach used to develop the Capital One NSA was consistent with the general policy that I describe in the response to NAA/USPS-T1-7(a). This policy considers the specific attributes of a customer and along with the practical restrictions of collecting sampling data or developing entirely customer specific models.

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**NAA/USPS-T1-8.** In your response to ABA/USPS-T1-1, you quote witness Plunkett as saying:

In the course of developing the [Capital One] NSA, the Postal Service has not identified any other customers with Capital One's combination of attributes that makes this agreement uniquely valuable. The Postal Service recognizes that if there were other mailers that use First-Class Mail as an advertising medium, and that if they exhibited similar mail usage and growth potential, it could be beneficial to enter into a similar agreement with those mailers. (Emphasis added.)

- a. Please itemize and explain each specific attribute in Capital One's "combination of attributes" that make the Capital One NSA uniquely valuable.
- b. If the fact that Capital One has the largest volume in the First-Class Mail Subclass is one of the attributes in this "combination of attributes," by definition no other mailer in the country would have the same "combination of attributes"?
- c. Please explain the steps the Postal Service has taken to determine whether other mailers have the combination of attributes similar to that of Capital One, except, perhaps, for its uniquely large First-Class Mail volume.
- d. Is it your opinion that very few mailers, other than Capital One, use First-Class Mail for solicitation purposes?
- e. Is one of the unique attributes of Capital One that it is willing to have its mail pieces destroyed if they cannot be delivered, provided that the ACS service is provided free of charge?
- f. Is one of the unique attributes of Capital One that the proportion of its solicitation pieces that are UAA and cannot be forwarded is approximately eight times the national average for First-Class Mail?
- g. Is one of the unique attributes of Capital One that it does not participate in the Postal Service's ACS service, which is designed to be a computerized, electronic way to improve the quality of addresses on a list?
- h. Do you believe that Capital One's decision not to participate in the Postal Service's ACS service is irrelevant to the decision to enter into this NSA?
- i. Please explain the analysis the Postal Service performed to determine whether Capital One had "growth potential."
- j. Consider a mailer who was not viewed by the Postal Service as having "growth potential" but who would send additional volume if given declining

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block discounts, and that both the Postal Service and the mailer would consider that growth to be a positive development. Please explain the extent to which you would argue that this mailer is a poor candidate for an NSA involving declining block discounts.

RESPONSE:

- a. It is important to recognize that respective attributes in isolation do not necessarily make the agreement valuable, but, as indicated in the testimony of witness Plunkett (USPS-T-2), it is the combination of attributes that is crucial. The Agreement itself identifies many conditions, or attributes, that were sufficiently critical to warrant inclusion. See Attachment G to the Request at Sections I and II and witness Plunkett's responses to VP-T2-1 and 2. In addition to those, I would also point to the willingness of Capital One to work with the Postal Service to develop a mutually beneficial agreement. This includes cooperation in identifying opportunities for rates and classifications that increase contribution for the Postal Service, in sharing company-specific mailing data, and in actively appearing before the Postal Rate Commission.
- b. Capital One's large volume of First-Class Mail was a pertinent attribute. While, by definition, only one mailer can be the "largest" mailer of First-Class Mail, First-Class Mail volume alone was not the only consideration for entering into the NSA and the Postal Service does not consider being the largest " mailer in a specific class or subclass to be a prerequisite for an NSA.
- c. The Postal Service is having ongoing discussions with potential NSA partners. The fact that we have not, as of now, entered into agreements with



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other customers does not imply that we have eliminated them from consideration. Witness Plunkett (USPS-T-2) explains why the Postal Service believes that no other customers have the same combination of attributes as Capital One. However, this does not imply that the Postal Service would not consider entering into mutually beneficial NSAs with other customers based on those customers' attributes.

- d. No. However, it is my understanding that Capital One does use First-Class Mail for solicitations quite extensively.
- e. No.
- f-h. No. All of Capital One's mail characteristics combined to provide the Postal Service and Capital One a unique opportunity to reduce Postal Service costs and provide incentives for Capital One to continue to use the mail. The Postal Service's goal was to develop an agreement that reduced operational costs, thereby providing a benefit to postal ratepayers as a whole. Obviously, any one characteristic is likely similar to that of some as-of-yet unidentified mailer who, for example, may have a return rate equal to that of Capital One. However, I do not believe that mere speculation that some mailer, somewhere, could have similar attributes is sufficient reason not to proceed with the proposed negotiated service agreement. In addition, it is not clear that the return rate for Capital One's solicitation mail volume differs from that of other mailers using First-Class Mail for solicitations.
- i. Redirected to witness Plunkett.

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- j. If a mailer does not have “growth potential,” I am not sure how it could appreciably increase its mail volume. In evaluating a potential NSA, I believe Postal Service should look not only at the customer’s mail volume, but also at the characteristics of that mail volume, potential opportunities for reducing Postal Service costs, opportunities for providing enhanced services or combinations of services not currently contemplated by today’s classification schedule, as well as the customer’s capabilities and willingness to work with the Postal Service to develop a mutually-beneficial agreement.

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**NAA/USPS-T1-9**

- a. Please confirm that First-Class Mail, without an endorsement to the contrary, is given “free” forwarding (in the sense that there is no additional charge beyond the postage rate to the mailer or the recipient) for 12 months and if an undeliverable-as-addressed piece cannot be forwarded, or is beyond the 12-month period, it is returned to the sender at no additional charge.
- b. Do you agree that the arrangement described in (a) involves intentional rate averaging among mailers in the sense that the cost to the Postal Service of providing this service to some mailers is much higher than the cost of providing it to others?
- c. Do you agree that mailers that cause the Postal Service to incur higher-than-average costs (due to having higher-than-average proportions of pieces either forwarded and/or returned) are, at least with respect to forwarding, being cross subsidized (perhaps implicitly) by other mailers? If you do not agree, then state the definition of cross-subsidy on which you base your answer and explain how the phenomenon in question coincides with that definition.
- d. Would charging each mailer of First-Class bulk mail a rate that recognizes the degree to which its mail uses forwarding and return services be fairer than the current pricing of First-Class mail? Please explain.
- e. If each mailer of bulk First-Class Mail were charged according to its use of forwarding and return services, possibly through a code placed on the mail piece, would an NSA of the kind and character of the instant proposal still be worth considering? Please explain.

**RESPONSE:**

- a. Confirmed. See DMM 57 F010.5.1.
- b. Yes, rate averaging across different mailer and mail characteristics, including use of forwarding, exists within First-Class Mail as well as all other classes of mail. While the standard First-Class Mail product offerings provide a specified level of service with known characteristics, this should not preclude the Postal Service from taking opportunities to reduce costs through customer-specific product and pricing initiatives. In

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this instance, the Postal Service has worked with Capital One to develop an agreement that will reduce the Postal Service's costs for handling Capital One's UAA mail.

- c. No, Postal Service rates and fees are designed to avoid cross-subsidy and to meet the requirements of the Postal Reorganization Act. See, for example, Docket No. R2001-1, PRC Op. and Rec. Dec. at 37-40; and Docket No. R2000-1, PRC Op. and Rec. Dec. at 193-199.

As a policy decision, the Postal Service has decided to provide forwarding and return services as an integral part of First-Class Mail. On an ongoing basis, we re-evaluate the characteristics of all our product offerings including consideration of whether deaveraging rates based on varying cost characteristics is appropriate. Opinions about whether deaveraging First-Class Mail rates based on differential use of forwarding and return services would be "fair" would likely depend on whether a customer's postage rates would be more likely to increase or decrease with deaveraging. However, in developing the Capital One NSA, the Postal Service has identified an opportunity to increase the contribution from an individual customer (with that customer's agreement) through the proposed NSA structure.

- d. Not necessarily. The Postal Service has not evaluated the effect of this type of rate and fee design on each of the thousands of affected customers.. The Capital One NSA was developed as a mutually beneficial agreement as compared to the current rate structure; not as compared to

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every possible alternate hypothetical rate structure. In this instance, the proposal permits the Postal Service to achieve some savings without having to change the forwarding and return features of all presorted First-Class Mail.

- e. As described in the response to (d), the Postal Service evaluated the Capital One NSA agreement in comparison to the current rate and fee structure and determined that, in comparison to the current rate and fee structure, the proposed NSA provided an opportunity to reduce Postal Service costs and thus was beneficial.

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**NAA/USPS-T1-10.** Does Capital One currently receive a substantial implicit subsidy from its dramatically above-average usage of the forwarding and return services of the Postal Service? Please explain any negative answer.

**RESPONSE:**

No. With the high implicit cost coverage for presorted First-Class Mail, it is extremely unlikely that the rates paid by Capital One or any other customer mailing presorted First-Class Mail do not cover the cost of providing mail services. See Docket No. R2001-1, PRC Op. and Rec. Dec., Appendix G at 1, presorted First-Class Mail cost coverage of 192.0 percent (PRC methodology).

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**NAA/USPS-T1-11.** Do you believe that, in this NSA, Capital One could be said to agree to forego an implicit subsidy from its above-average usage of forwarding and return services if the Postal Service will use the savings to provide it with free ACS service and with declining block discounts that start well below projected volume levels?

- a. Please explain any disagreement you have with this question, including, but not limited to, any statement of fact you contend is incorrect.
- b. Please explain why the Postal Service's arrangement with Capital One is fair to mailers who are paying the same postal rates but are not receiving dramatically above-average returns and therefore do not receive the same implicit subsidy.

**RESPONSE:**

- a. As explained in my responses to NAA/USPS-T1-9 and NAA/USPS-T1-10, I do not believe that Capital One is receiving an "implicit subsidy." In addition, your characterization of the NSA agreement's terms and conditions is incomplete and I would not necessarily agree that the proposed thresholds are "well below" projected volume levels.
- b. All postage rates and fees involve averaging across some cost-causing characteristics. However, the Capital One NSA identifies and works with a customer to reduce Postal Service costs in a way that benefits that customer, other customers, and the Postal Service. The Capital One agreement results in a reduction of the costs associated with the current level of cost averaging within First-Class Mail. This is possible because we were able to work with Capital One to develop a comprehensive proposal that provided benefits to not only the Postal Service and Capital One, but also to other customers by reducing the overall level of costs.

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**NAA/USPS-T1-12.** As the Postal Service's Chief Marketing Officer, is it your belief that the use of declining block discounts depends upon the size of the mailer? Please explain your answer.

**RESPONSE:**

I assume that your question refers to the declining block rates (not discounts) incorporated in the Capital One agreement.

I do not think that the use of declining block rates necessarily depends upon the size of the mailer. Declining block rates are one tool that can be used in an NSA to the mutual benefit of a customer and the Postal Service. Any potential agreement incorporating declining block rates (or any other rate design) must be evaluated as a whole.



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**NAA/USPS-T1-13.** If 10 percent of the addresses in a particular mailing list are UAA and cannot be forwarded, would you consider mail using that mailing list to be of poor quality or “dirty”? Please explain any negative answer.

**RESPONSE:**

No. Address quality is a relative concept and only one characteristic of many (barcode quality, presortation, automation-compatibility) that affect the Postal Service’s costs of handling a given mail piece. It is my understanding that Capital One currently complies with the Postal Service’s mail preparation requirements for presorted First-Class Mail. The proposed agreement requires Capital One to comply with additional conditions not required of other mailers to reduce the Postal Service’s costs of processing Capital One’s mail. While I am not an expert in mailing lists, I do not believe it is always appropriate to believe that mailing lists used for solicitations can be expected to have the same return or forwarding rates as those mailings such as billings where there may be an ongoing relationship with the customer.

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**NAA/USPS-T1-14.** If a large First-Class mailer could demonstrate that 12 to 15 percent of its mail is UAA and cannot be forwarded, would such fact help qualify that mailer for an NSA similar to the Capital One NSA? Please explain any negative answer.

**RESPONSE:**

The Capital One NSA cannot be oversimplified as an agreement whose sole requirement is a reduction in UAA mail. It must be viewed as a comprehensive whole of which Capital One's pre-implementation UAA percentage is only one component. In evaluating other potential NSAs, the Postal Service will determine whether the terms and conditions of those potential NSAs would result in a net benefit to the Postal Service. While it is possible that a customer's existing UAA percentage may be a factor in that evaluation, neither a high nor a low UAA percentage would necessarily qualify or disqualify a mailer from consideration for an NSA.

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**NAA/USPS-T1-15.** If a large First-Class mailer could demonstrate that 3 to 4 percent of its mail is UAA and cannot be forwarded, would such fact reduce that mailer's likelihood of qualifying for an NSA similar to the Capital One NSA? Please explain any affirmative answer.

**RESPONSE:**

See response to NAA/USPS-T1-14.

## **CERTIFICATE OF SERVICE**

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

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Scott L. Reiter

475 L'Enfant Plaza West, S.W.  
Washington, D.C. 20260-1137  
November 25, 2002