

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 VALPAK DIRECT MARKETING SYSTEMS, INC. AND
VALPAK DEALERS ASSOCIATION, INC.
(VP/USPS-T1-1-5)

The United States Postal Service hereby provides the responses of witness Bizzotto to the following interrogatories of Valpak Direct Marketing Systems, Inc. and Valpak Dealers Association, Inc.: VP/USPS-T1-1 -5, filed on November 15, 2002.

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

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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November 25, 2002

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TO INTERROGATORY OF VALPAK DIRECT MARKETING SYSTEMS, INC. AND
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VP/USPS-T1-1. Your testimony (at p. 4, l. 24 through p. 5, l. 2) states: “We should not be afraid to move forward, particularly when remaining in the current ‘comfortable’ spot will not necessarily resolve the Postal Service’s inherent difficulties.”

Please state whether you believe the merits of the instant proposal and the justification for Negotiated Service Agreements (“NSAs”) in general depend on the extent to which the Postal Service is facing economic difficulties, and explain in detail the basis for your answer.

RESPONSE:

Negotiated service agreements are a tool that can allow the Postal Service to address our customers’ needs through targeted rate and classification initiatives. I hope that NSAs will provide opportunities to increase the value of the mail and thereby encourage our customers to continue to send messages, correspondence, and other transactions through the mail. This goal is not dependent on the financial state of the Postal Service at any particular time, but is an outgrowth of fulfilling our mission of providing postal services to bind the nation together. NSAs have been discussed for many years, through financial ups and downs.

Nevertheless, I am mindful of our responsibility to maintain a viable Postal Service and the additional challenges resulting from economic and financial uncertainty. Although the proposed legislation regarding the Postal Service’s ongoing CSRS retirement funding obligation, if enacted, would mitigate some financial pressures, the Postal Service still must operate in a continually changing environment. Our customers are interested in innovative solutions to their mailing requirements. These requirements are driven by their business needs, not by the financial condition of the Postal Service. I intend to continue working with interested customers develop mutually beneficial NSAs and other rate and classification proposals to meet their business needs and to help

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maintain a Postal Service that will remain viable and able to meet the needs of our
customers and the nation at large for many years to come.

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VP/USPS-T1-2. Your testimony (at p. 5, ll. 15-17) states: "Capital One's mail volume is expected to grow over the term of the contract, thus offsetting some of the decline in volume expected in other segments of the mail stream."

Please state whether you believe the merits of the instant proposal and the justification for NSAs in general depend on the extent to which the Postal Service may be facing declining volume in other segments of the mail stream, and explain in detail the basis for your answer.

RESPONSE:

As described in my response to VP/USPS-T1-1, NSAs are one tool for meeting customers' needs. Successfully doing so will help increase the value of the mail for customers who might otherwise look for nonmail alternatives. Declines in mail volume alone are not the sole reason for pursuing NSAs, but, if we do not continue to address our customers' needs, customers will continue to look for alternatives to the mail, including ones they may not be currently contemplating.

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VP/USPS-T1-3. As the policy witness for the Capital One NSA, please explain the extent to which the attractiveness of the NSA to the Postal Service and the justification for the proposal depend on the absolute magnitude of Capital One's First-Class Mail volume.

RESPONSE:

The Postal Service's decision to enter into the Capital One NSA was based on a consideration of possible rate and product changes that would not only increase contribution from Capital One's mail, but would also provide a product offering that Capital One would find attractive. Clearly, the absolute magnitude of Capital One's volume presented some opportunities that may not necessarily exist with smaller customers. However, by no means does this imply that size alone makes a customer a potential candidate for a negotiated service agreement. As we work to develop future NSAs, the Postal Service will look to tailor any subsequent agreements to the individual customer's needs, the potential for reducing Postal Service costs, and consistency with the overall policy goals set forth in the Postal Reorganization Act

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VP/USPS-T1-4. In your testimony (at p. 3, l. 20), you state that your view NSAs as '[a] natural next step in the evolution of postal pricing '

- a. In terms of the direction you provide in the areas of pricing and marketing, do you see any fundamental difference between an NSA with one customer and a niche classification that might be used by only a few (e. g., two, three, or four) mailers? If so, please explain what that difference is.
- b. Do you see any difference in the pricing principles that you would apply to an NSA with one customer and a niche classification that might be used by only a few (e. g., two, three, or four) mailers? If so, please explain what that difference is.

RESPONSE:

- a. Yes. A negotiated service agreement addresses needs specific to one customer and works to tailor a solution that is mutually beneficial for both the customer and the Postal Service. Because of the unique, tailored nature of an NSA, that agreement is made between the Postal Service and one individual customer only. A "niche" classification is a classification that we expect to be used by only a small number of customers; however, it is generally available to any customer that chooses to use the classification. The Postal Service views an NSA as the outcome of a cooperative partnership between the Postal Service and one mailer to identify combinations of product and customer attributes that offer the potential for unique solutions to the customer's mailing requirements. However, working to develop these cooperative agreements will not prevent the Postal Service from proposing broader classifications if an identified opportunity can reasonably be extended to other customers.
- b. No. The criteria that are used to develop and evaluate postal rates and classifications are set forth in the Postal Reorganization Act. These criteria apply

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regardless of whether the proposal is for an NSA with an individual customer or for a
broader classification.

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VP/USPS-T1-5. Within the framework of the direction you provide for rate setting for the Postal Service, consider the following policy statement:

By providing discounts for volume beyond projected levels, or for volume that would not otherwise be sent, declining block discounts can promote volume growth, benefit the mailer (who voluntarily uses the discounts), and benefit the Postal Service (in the sense that the overall contribution to fixed costs is higher after the discounts than before).

- a. Please explain the extent to which you agree with this statement.
- b. Do you agree that declining block discounts can make economic and policy sense without tying them to any funding that might be associated with a change in forwarding arrangements? Please explain any negative answer.
- c. Do you have any reason for not supporting declining block discounts as an effective mechanism for promoting growth? Please explain any affirmative answer.
- d. In your opinion, do any of the benefits of declining block discounts depend on the expected growth rate (negative, zero, or positive) of the volume of the mailer involved? Please explain your answer.

RESPONSE:

- a. I don't think you meant to say declining block discounts, since that implies rates become higher as volume increases. I agree that declining block rates, by stimulating new volume, can benefit the mailer, the Postal Service, and all mailers by increasing contribution.
- b. Yes, declining block rates are a viable rate design tool in and of themselves and the decision to use this tool will depend on the specific nature of the rate design challenge. In developing the Capital One NSA, the Postal Service determined that declining block rates in conjunction with the other terms and conditions of the agreement provided a mutually beneficial solution addressing Capital One's mailing needs.
- c. See responses to VP/USPS-T1-5(a) and (b).

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- d. The benefits of any rate proposal, including the declining block rate proposals incorporated in the Capital One agreement, will depend on many factors. In this proposal, the opportunities presented by Capital One's extensive use of First-Class Mail for solicitation, the high volume of First-Class Mail it presents every year, the opportunities available because of the relative level of UAA mail combine to present an opportunity to develop an agreement that provides benefits to both the Postal Service and Capital One. The evaluation of the Capital One agreement should not proceed by singling out a limited number of factors (e.g., rate structure and forwarding arrangements or rate structure and expected growth rates) of the many components of the agreement and trying to piecewise determine if each potential combination of factors would make good economic and policy sense. The Postal Service did not do this in its evaluation of the agreement and would not expect that this process would lead to a reasonable evaluation of the agreement as a whole. The various elements of the Capital One NSA could conceivably be combined in many different ways to reach product and rate solutions that might make good economic and policy sense in some as-of-yet unexamined circumstance. For instance, there may be a case where declining block rates would make sense for a customer with relatively little growth in mail volume. However, those possibilities must be examined in the context of a specific product or rate initiatives and not as hypothetical examples.

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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