

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

RESPONSES OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORIES OF THE NEWSPAPER ASSOCIATION OF AMERICA
(NAA/USPS-T2-11-21)

The United States Postal Service hereby provides the responses of witness Plunkett to the following interrogatories of the Newspaper Association of America: NAA/USPS-T2-11-21, 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:

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
November 25, 2002

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-11: Please refer to your response to NAA/USPS-T2-5. To your knowledge, does any other mailer annually mail more than 750 million pieces of solicitation mail via First-Class Mail?

NAA/USPS-T2-11 Response:

No.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-12: Please refer to your response to OCA/USPS-T2-2, in which you distinguish between NSAs, which you appear to limit to domestic mail, and “customer-specific pricing arrangements” used by the UPS with certain international customers. Please state the differences, if any, between the “three distinct goals” for NSAs for domestic mail and the purposes of “customer-specific pricing arrangements” for international mailers.

NAA/USPS-T2-12 Response:

See my responses to OCA/USPS-T2-2 and OCA/USPS-T2-16

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-13: Please refer to your response to APWU/USPS-T2-1, and in particular to the passage where you state that the Postal Service “was concerned about higher volumes during FY2002.” Please elaborate on the nature of that concern, and why the Postal Service would be “concerned” about higher volumes.

NAA/USPS-T2-13 Response:

As is described in the testimony of witness Elliot (COS-T-2 , at 2-3), Capital One’s FY 2002 volume was driven by some anomalous events, and during the period of time that the Agreement was being negotiated, volumes remained well above historical levels.

Given the structure of declining block discounts, the Postal Service was concerned that if the growth described in witness Elliot’s testimony were to be sustained indefinitely, the block discount tiers would have been set lower than necessary to sustain and promote higher volume levels.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-14: Please refer to Section II.G of the NSA, which provides that Capital One “agrees that it cannot use the CSR endorsement as a means to comply with the published Postal Service Move Update requirements for automation compatible mail. Capital One will continue to comply with Move Update through either NCOA match or FastForward.” What is the purpose of this provision?

NAA/USPS-T2-14 Response:

This provision is intended to ensure that Capital One continues its existing addressing practices, else the volume of forwarded and/or returned mail would tend to increase, all else being equal.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-15: The NSA agreement attached to the Request in this proceeding does not appear to prohibit Capital One from satisfying the various volume thresholds by shifting solicitation mail from Standard to First-Class Mail. Please describe what measures, if any, the Postal Service has in place, or intends to implement, that would enable it to know whether Capital One is, during the NSA, shifting Standard to First-Class Mail rather than originating "new" First-Class Mail?

NAA/USPS-T2-15 Response:

The Postal Service will not be instituting any specific measures to capture this information. During the course of the Agreement, the Postal Service will of course monitor Capital One's volume, but as witness Jean (COS-T1, p.3) points out, the Agreement is not expected to result in switching of mail from Standard to First-Class Mail.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-16: Please refer to your testimony at page 7, lines 19-22, where you state: "Because First-Class Mail service includes forwarding and return, the cost of handling forwarded and returned solicitations is included in First-Class Mail-related forwarding and return costs and included in the cost basis used in the development of First-Class Mail rates."

As an economist familiar with postal ratesetting, please answer the following:

- a. What are the principal justifications for making "free" forwarding a basic characteristic of First-Class Mail?
- b. Do you believe that First-Class Mail rates are characterized by a large, small, or moderate amount of rate averaging?
- c. Do you agree that the rate averaging in First-Class Mail is intentional (*i.e.*, the rate averaging is understood and was purposeful)? Please explain any disagreement.
- d. When rate averaging occurs, do you agree that Postal Service costs can vary substantially among mailers or among mailings while the rates are the same? Please explain any disagreement.
- e. Consider a situation where, because of a particular characteristic of a mailing, a mailer in fact imposes unusually high costs on the Postal Service while paying the same rates as other mailers. Do you agree that, in common parlance, the mailer is receiving a subsidy, or perhaps an implicit subsidy or a "free ride" from the other mailers with respect to the particular characteristic involved?
- f. When a mailer receives the kind of implicit subsidy explained in part e, do you believe the mailer should be able to negotiate with the Postal Service in the following way: "I will stop doing that which is costing you extra money, so that my rate relates more equitably to the costs I cause just like most other rate payers, if you will use the money you save to give me other services free of charge or to give me discounts from the rates I pay"? Please explain your response.
- g. If a mailer is allowed to negotiate with the Postal Service in the manner suggested by part f, would this provide mailers with an incentive to say, in effect, "If you do not give us a special discount, we will begin doing something that will cost you extra money but not change our rates"? Please explain any negative answer.
- h. From a rate-design perspective, please explain whether it would be your preference to charge each First-Class bulk mailer according to the services used by that mailer. For example, with respect to forwarding, each bulk mailer could place a simple barcode on the piece and be charged according to the forwarding or return service actually provided.

NAA/USPS-T2-16 Response:

- a. I am not personally aware of any attempt to isolate the specific features of First-Class Mail for the purposes of the justification implied here. First-Class Mail rates are set in accordance with the pricing criteria in the Act, but the

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

- application of specific criteria is at the rate level, not at the level of product features.
- b-c Whatever is implied by the designations “large”, “small”, and “moderate,” it would be difficult to apply any of these terms to all First-Class Mail rates. There are a number of different subclasses within First-Class Mail, each characterized by differing amounts of averaging. I would confirm that the single piece First-Class Mail rate, being required by law to be uniform and universally available suggests that a high degree of averaging is a goal for that specific rate.
- d. I would agree that variation is inevitable. It is unclear what is meant by the term substantially.
- e. In such a case, the mailer clearly benefits from averaging with respect to the particular characteristic involved.
- f. I believe that customers should be given the opportunity to negotiate specific business terms with the Postal Service to the extent such terms can be demonstrated to be in compliance with the Act.
- g. My understanding is that one of the conditions under which NSAs are considered to be legal is their availability to all similarly situated customers. Thus, to the extent other customers can meet the qualifying criteria embodied in an agreement they are entitled to the same terms. To the extent customers wish to negotiate with the Postal Service regarding terms of service, they should be free to do so as I replied in response to part f.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

- h. I have not studied the hypothetical suggestion in this question enough to provide an informed response as to its merits. Nor do I have the information necessary to do so. As far as I know the Postal Service has no plans to institute a per-piece charge for forwarding as this question seems to suggest.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-17: Please confirm your understanding that the Postal Service's average total cost to return a piece of Capital One First-Class Mail is approximately 53.5 cents (USPS-LR-1/MC2002-2, page 1)? If you cannot confirm, please provide your understanding of the correct number.

NAA/USPS-T2-17 Response:

Confirmed.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-18: Please confirm your understanding that the average mailstream processing cost to return a piece of Capital One First-Class Mail from the CFS back to the mailer is 29.95 cents (USPS-LR-1/MC2002-2, page 1). If you cannot confirm, please provide your understanding of the correct number.

NAA/USPS-T2-18 Response:

Confirmed.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-19: Please confirm your understanding that the Postal Service's average cost of providing electronic Address Change Service ("ACS") to Capital One for a piece of non-forwardable First-Class Mail is approximately 14.5 cents (USPS-LR-1/MC2002-2, page 2). Please also confirm that this 14.5 cent cost also supports the current 20 cent charge for eACS. If you do not confirm either of these, please provide your understanding of the correct number.

NAA/USPS-T2-19 Response:

Confirmed.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-20: Under the forwarding option that Capital One will place on its envelopes, and under terms of the NSA between the Postal Service and Capital One, would you agree that for Capital One electronic ACS becomes a substitute for physical return of the First-Class Mail that is Undeliverable As Addressed (“UAA”) and cannot be forwarded? Unless your answer is an unqualified affirmative, please explain how, from an economic perspective, you would regard the relationship in the NSA between electronic ACS and physical return of First-Class Mail that cannot be forwarded.

NAA/USPS-T2-20 Response:

I would agree to the extent Capital One has agreed to these terms they appear to view electronic ACS as a substitute for physical return of mail pieces.

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

NAA/USPS-T2-21: Please refer to your testimony at page 3, lines 14-15), where you state: “[T]he Postal Service currently charges 20 cents for each electronic address correction” and at page 7, lines 19-20, where you state “First-Class Mail service includes forwarding and return.” Please compare the average unit costs for Capital One mail that you confirmed or provided in preceding questions NAA/USPS-T2-18 and NAA/USPS-T2-19 and for each of the following statements, please (i) state whether you agree or disagree, and (ii) explain fully any disagreement.

- a. The Postal Service currently charges 20 cents for a service (*i.e.*, electronic ACS) that would cost 14.5 cents to provide to Capital One, while providing the mailer free of additional charge – *i.e.* , presenting mailers with an implicit price of 0 cents (*i.e.*, ZERO cents) -- for a substitute service (mailstream processing for the physical return of the mail piece) that costs 29.95 cents to provide to Capital One.
- b. The relationship of fees and costs described in (a) applies to Capital One’s First-Class Mail in the absence of the NSA.
- c. Even if the Postal Service charged 0 cents (*i.e.*, ZERO cents) for electronic ACS, it would on average save money on every piece of First-Class Mail that used electronic ACS in lieu of physical return of pieces that cannot be forwarded.
- d. Charging 20 cents for a service with an average cost of 14.5 cents, while charging an implicit price of 0 cents for a substitute service with an average cost of 29.95 cents, is good economics.
- e. Charging 20 cents for a service with an average cost of 14.5 cents, while charging an implicit price of 0 cents for a substitute service with an average cost of 29.95 cents, is a good illustration of cost-based pricing.
- f. The relationship of prices and costs described in (a) above provides First-Class Mailers with appropriate economic incentives to engage in behavior that, on average, will result in lowest combined costs for mailers and the Postal Service.

a. I agree.

b. I agree.

c. I agree that the cost of providing a physical return exceeds the fee for electronic ACS, but disagree that waiving the fee would result in a net savings on every piece as suggested here. See also my response to VP/USPS-T2-7.

d. The tradeoff is neither as simple nor as obvious as is suggested by the interrogatory. For a mailer like Capital One, with a large volume of mail and a large stream of returned pieces, it may be advantageous to develop an efficient means of dealing with returned pieces, such that it is a relatively

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS PLUNKETT
TO INTERROGATORY OF THE NEWSPAPER ASSOCIATION OF AMERICA

- simple trade off. Other customers – particularly smaller customers – may view the service considerations very differently. For example, if returns are in smaller quantities or are received sporadically, the customer may prefer the convenience of receiving the information electronically and consider electronic ACS a superior alternative even at the \$0.20 cent fee. Also, subscription to electronic ACS is, as I understand it, a low cost way for many smaller customers to meet MOVE update requirements and thereby qualify for automation rates. In this case the fees associated with returns may be dwarfed by postage savings resulting from access to automation discounts.
- e. The 20-cent fee provides an adequate cost coverage given the 14.5 cents average cost, and is therefore consistent with the Act.
 - f. See my response to parts d and e.

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.

Scott L. Reiter

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