

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

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA  
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF  
CAPITAL ONE SERVICES, INC. (COS/NAA-T1-1-14)  
January 9, 2003**

The Newspaper Association of America hereby provides submits the answers of  
Christopher D. Kent to interrogatories of Capital One Services, Inc., filed December 26,  
2002.

Respectfully submitted,

NEWSPAPER ASSOCIATION OF AMERICA

By:

\_\_\_\_\_  
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**CERTIFICATE OF SERVICE**

I hereby certify that I have this date served the instant document on all  
participants requesting such service in this proceeding in accordance with section 12 of  
the Rules of Practice and the Presiding Officer's Rulings.

January 9, 2003

\_\_\_\_\_  
William B. Baker

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA  
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CAPITAL ONE SERVICES, INC.**

**COS/NAA-T1-1.** Please refer to page 4 of your testimony where you state, "In response to requests subsequent to its filing, the USPS has prepared several sensitivity analyses, but it has not committed to any one final number for all three years. Further, several of these analyses result in negative contributions in years two and three."

- (a) Have you prepared any forecasts of Capital One's First-Class Mail volumes in FY 2004 or FY 2005? If so, please provide all of your forecasts and all underlying calculations.
  
- (b) Please confirm that none of the sensitivities presented in the Postal Service's response to the referenced Oral Request of Commission Goldway result in a net negative contribution over the entire three-year term of the agreement. If not confirmed, please explain fully.

**RESPONSE:**

- (a) No.
  
- (b) Confirmed. However, none of the USPS sensitivities included consideration of the amount of the waived fees.

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**COS/NAA-T1-2.** Please refer to page 9 of your testimony where you state, “the mail processing cost of returned mail in the USPS analysis appears to be based on FY 2000 IOCS data.” Please confirm that FY 2000 IOCS data was used in Docket No. R2001-1 to distribute costs to all mail classes and special services. If not confirmed, please explain fully.

**ANSWER:**

I have not examined the costing of every mail class and special service in Docket No. R2001-1 and thus cannot confirm.

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CAPITAL ONE SERVICES, INC.**

**COS/NAA-T1-3.** Please refer to Table 1 on page 10 of your testimony where you calculate the total contribution as a result of the NSA based upon “illustrative” unit costs regarding physical return costs.

- (a) Have you developed any estimates of the Postal Service’s cost to physically return First-Class Mail pieces? If so, please provide all estimates and all underlying calculations.
- (b) Have you developed any estimates of the Postal Service’s cost to physically return First-Class Mail letters? If so, please provide all estimates and all underlying calculations.
- (c) Have you developed any estimates of the Postal Service’s cost to physically return First-Class Mail barcoded letters? If so, please provide all estimates and all underlying calculations.
- (d) Have you developed any estimates of the Postal Service’s cost to physically return First-Class Mail letters to Capital One? If so, please provide all estimates and all underlying calculations.

**ANSWER:**

(a) – (d) No.

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CAPITAL ONE SERVICES, INC.**

**COS/NAA-T1-4.** Please refer to the section of your testimony titled “Avoided forwarding costs are overstated”, which begins on page 14.

- (a) Have you developed any estimates of the Postal Service’s cost to forward First-Class Mail pieces? If so, please provide all estimates and all underlying calculations.
- (b) Have you developed any estimates of the Postal Service’s cost to forward First-Class Mail letters? If so, please provide all estimates and all underlying calculations.
- (c) Have you developed any estimates of the Postal Service’s cost to forward First-Class Mail barcoded letters? If so, please provide all estimates and all underlying calculations.
- (d) Have you developed any estimates of the Postal Service’s cost to forward First-Class Mail letters to Capital One? If so, please provide all estimates and all underlying calculations.
- (e) Please confirm that your adjustment to witness Crum’s model to remove the costs associated with postage due mail reduces the unit cost of forwarding by approximately 0.3 percent. If not confirmed, by what percentage does your adjustment to witness Crum’s mode decrease the unit cost of forwarding?

**ANSWER:**

(a) – (d) No.

(e) Confirmed.

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**COS/NAA-T1-5.** Please refer to Table 2 on Page 14 of your testimony. Have you developed any estimates of the percentage of Capital One's First-Class Mail letters that are forwarded? If so, please provide all estimates and all underlying calculations.

**ANSWER:**

Yes. As stated on page 12 of my testimony, for an alternative (to the USPS estimate of 1.96%) estimate of forwards, one might assume that the relationship between COS's forwarding and return rates corresponds to the average for all FCM. The forwarding average for all FCM (1.96%) is about 159% of the average return rate (1.23%). Under this assumption, COS's forwarding rate would be 159% of its return rate, which works out to 15.3%, although use of NCOA presumably should reduce the forwarding rate somewhat.

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**COS/NAA-T1-6.** Please refer to page 6 of your testimony where you discuss eACS fees and USPS-T-3 at 5. Please confirm that witness Crum calculated the return cost savings based upon the assumption that Capital One would receive eACS notification. If not confirmed, please explain fully.

**ANSWER:**

Confirmed.

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CAPITAL ONE SERVICES, INC.**

**COS/NAA-T1-7.** Please refer to page 3 of your testimony where you state, “In my experience, no private firm would have negotiated the Postal Service’s side of this deal.”

- (a) Please provide a list of all agreements that you personally have negotiated for private firms.
- (b) Please provide, as library references, copies of all agreements listed in your response to subpart (a) of this interrogatory.

**ANSWER:**

(a) I do not negotiate agreements for my clients; I advise them on strategic matters during negotiations.

(b) I have not retained copies of the agreements or contracts, which would be confidential in any case.



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**COS/NAA-T1-8.** Please refer to page 6 of your testimony where you state, “as a matter of rate design, it seems inequitable to give free eACS to a high-cost entity, while mailers that engage in better address hygiene do not get a discount.”

- (a) Have you performed any analyses that compare Capital One’s address hygiene practices to that of any other mailers? If so, please provide a copy of each analysis.
  
- (b) Have you performed any analyses that compare Capital One’s address hygiene practices to those required by Postal Service rules and regulations? If so, please provide a copy of each analysis.

**ANSWER:**

- (a) – (b) No, but COS appears to have a very high return rate compared to the FCM average return rate.

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**COS/NAA-T1-9.** Please refer to page 7 of your testimony where you state, "The USPS has a margin of only \$8.2 million in this NSA. Although this may look like a lot of money, when one considers the per piece costs for 1.4 billion pieces in the test year alone, an error in the cost estimates of a penny or two becomes significant." Please refer to further to footnote 10 on page 6 of your testimony.

- (a) Please confirm that the cost estimates to which you referred on page 7 are estimates of the cost of returns and forwarded pieces. If not confirmed, to what cost estimates does this reference apply?
- (b) Please confirm that, based upon the calculations described in the footnote on page 10 of your testimony, FY 2003 eACS return mail volume for Capital One will be 62 million pieces. If not confirmed, please explain fully and provide your best estimate of FY 2003 Capital One's eACS returns.
- (c) Please confirm that, based upon the calculations described in the footnote on page 10 of your testimony, FY 2003 eACS forwarded mail volume for Capital One will be between 14 and 70 million pieces. If not confirmed, please explain fully and provide your best estimate of FY 2003 Capital One's eACS forwards.

**ANSWER:**

(a) Not confirmed. This reference applies to the overall per piece cost of handling Capital One First-Class mail, such as that calculated by witness Crum in his Attachment A.

(b) Confirmed that the calculations in footnote 10 result in FY 2003 eACS return mail volume for Capital One of 62 million pieces. However, the figure I used for before-rates Capital One First-Class solicitation mail volume was 760 million and the figure I should have used is 768 million, which results in FY 2003 eACS return mail volume of 62.7 million pieces. Using after-rate volumes (776 million pieces), the FY 2003 eACS return mail volume is 63 million pieces.

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(c) Confirmed that the calculations in footnote 10 result in FY 2003 eACS forwarded mail volume for Capital One of 14-70 million pieces. However, as explained in my response to part (b), I should have used 768 million pieces for the solicitation volume. Also, I used 1.96-9.6% as a conservative range for the forwarding rate for Capital One. As I described in my response to question 5, it is possible that Capital One's solicitation forwarding rate may be closer to 15.3%. Using that percentage and 768 million pieces, an estimate of the FY 2003 eACS forwarded mail volume for Capital One is about 112 million pieces. Using the after-rates volume, the FY2003 eACS forwarded mail volume would then be about 113 million pieces.

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**COS/NAA-T1-10.** Please refer to Table 1 on page 10 of your testimony.

- (a) Please provide in an electronic spreadsheet all calculations underlying the cost savings and contribution figures shown in Table 1.
- (b) In calculating the "Return Cost Savings for FY2003" and the "Total Contribution as a Result of the NSA" that are presented in this table, did you assume that the unit cost of eACS was 33 cents, as estimated by witness Crum? If not, what unit cost did you use?
- (c) Is it your testimony that witness Crum overstated the unit cost of physically returning mail to Capital One, but accurately estimated the cost of eACS returns? If so, please explain why the reasons you believe witness Crum overstated the unit cost of physically returning mail to Capital One do not apply to witness Crum's estimation of eACS costs.

**ANSWER:**

(a) See attachment 1, which contains 5 sheets: "Physical Returns," from USPS LR-1; "COF UNIT COSTS," from witness Crum's attachment A; "New Mail Contribution," "Return Cost Savings," "Discount Leakage," and "Summary," from witness Crum's attachment B. These sheets have been modified so that any change to the physical returns cost in cell J3 of the "Physical Returns" sheet will flow through and the impact on total contribution will be displayed in the "Summary" sheet

(b) Yes.

(c) No; this table addressed only the impact on overall contribution if the costs to physically return Capital One mail are lower than witness Crum's estimate.

However, I do believe that the mail processing portion of the Capital One

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physical returns cost is overstated in witness Crum's estimate (see USPS Library Reference 1) and this cost is not included in the electronic returns cost.

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**COS/NAA-T1-11.** Please refer to page 8 of your testimony where you note, "Presorted/bar-coded letters, the type of letter that COS normally mails, comprise only a part of total FCM volume." Do you believe that the cost of returning a presorted/bar-coded letter is different than the cost of returning an identical letter that wasn't presorted or barcoded? If so, please explain, in detail, why you believe this to be the case.

**ANSWER:**

Presorted/bar-coded letters are only a part of total FCM volume. I believe that the cost of returning presorted/bar-coded letters is less than the cost of returning the average FCM piece, which includes the cost of returning parcel packages.

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**COS/NAA-T1-12.** Please refer to page 8 of your testimony where you state, "Given COS's typical letter-shaped mail, the average FCM returns costs (which contain the costs for letters, flats, packages, and IPP's) is not appropriate to apply to COS mail." Have you performed any analysis regarding the percentage of the First-Class Mail returns mailstream that is comprised of letters? If so, what did you find?

**ANSWER:**

No.

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**COS/NAA-T1-13.** Please refer to page 8 of your testimony where you state, "However, problems encountered in returning other mail, such as further searching for a return address that may be on the back of the mailpiece, would appear not to apply to COS mail." What percentage of First-Class Mail returns has return addresses on the back of the mailpiece? Please explain in detail how you calculated this figure.

**ANSWER:**

I did not calculate such a figure.



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**COS/NAA-T1-14.** Please refer to page 8 of your testimony where you state, "Second, once COS return mail re-enters the mailstream for the trip to Richmond, it is likely to require fewer sortations than the average piece."

- (a) Please confirm that First-Class Mail letters in 3-digit and 5-digit trays generally are not sorted as individual pieces until they reach destination facilities. If not confirmed, please explain fully.
  
- (b) Taking into account your response to subpart (a), is it possible that Capital One's undeliverable-as-addressed mail is not determined to be UAA until it is deeper into the postal system than the average piece of undeliverable-as-addressed First-Class Mail. If your response is anything other than an unqualified yes, please explain fully.

**ANSWER:**

(a) & (b) While I am not an expert on mail processing, it is certainly possible that, on average, Capital One's UAA mail is not determined to be UAA until it is deeper into the postal system than other UAA pieces.

## USPS-LR-1/MC2002-2, page 1

### Physical Return Costs Cost for UAA Mail Being Returned to Sender Capital One Physical Mailpieces Returned

	A	B	C	D	E
	<u>Annual Volume</u> <u>(Thousands)</u>	<u>Cost/Piece</u>	<u>Annual Cost</u> <u>(Thousands)</u>	<u>Frequency</u>	<u>Weighted</u> <u>Cost/Piece</u>
1. Carrier Preparation	1,370,471 (1)	\$0.0545 (2)	\$74,676	1.00	\$0.0545
2. Clerk Handling	670,618 (3)	\$0.2711 (4)	\$181,802	0.49 (5)	\$0.1327
3. CFS Processing	475,667 (6)	\$0.1386 (7)	\$65,923	0.35 (8)	\$0.0481
4. Mailstream Processing	1,370,471 (1)	\$0.2995 (9)	\$410,410	1.00	\$0.2995
<b>5. Total</b>					<b>\$0.5350</b>

- (1) Refer to Table 5.2.1.2, Row 3.a, Column D (USPS LR-J-69).
- (2) Refer to Table 5.2.1.2, Row 3.a, Column G (USPS-LR-J-69).
- (3) Refer to Table 5.2.1.3.1 (USPS-JR-J-69). This is the sum of Row 1, Column A and a portion of Row 3, Column A. Refer to Volume Section, Volume Profile, Table 4.3, "Disposition at CFS Unit", of the portion of mail that is returned to sender.
- (4) This is the ratio of Table 5.2.1.3, Column H, and Table 5.2.1.3.1, Column A, Row 4 (USPS-LR-J-69).
- (5) This is the portion of return to sender mail that is returned by the Nixie clerk at the delivery unit, along with the portion of ACS Nixie that is returned at the CFS unit. This is the ratio of Rows 2 and 1, Column A.
- (6) Refer to Volume Section, Volume Profile, Table 4.3, "Disposition at CFS Unit", Total Returned.
- (7) Refer to Table 5.2.2, Column G, (Non-ACS) Total.
- (8) This is the portion of return to sender mail returned from the CFS unit, along with the portion of ACS Nixie that is returned from the CFS unit. This is the ratio of Rows 3 and 1, Column A, Table 5.2.2.
- (9) Refer to Table 5.2.4.1, Row 2, Column F.

**ATTACHMENT A, PAGE 2**

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

Capital One Solicitation Return Percentage =	9.6% (1)
Capital One Statement Return Percentage =	1.2% (2)
Average Presort Letters Return Percentage =	1.23% (3)
Before Rates Customer Mail Volume =	640,000,000 (4)
Before Rates Solicitation Mail Volume =	768,000,000 (5)
Manual Returns Unit Cost =	\$0.535 (6)
Electronic Returns Unit Cost =	\$0.332 (7)
Address Change Service (ACS) Success Rate =	85.0% (8)
Contingency Factor =	1.030 (9)

Rate Category	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)	(21)	(22)	(23)
	DOCKET NO. R2001-1 PRC FIGURES - NATIONWIDE MAIL MIX							DOCKET NO. R2001-1 PRC FIGURES - CAPITAL ONE MAIL MIX						
	TY 2003 Total Unit Cost (Dollars)	TY 2003 Mail Proc Unit Cost (Dollars)	TY 2003 Delivery Unit Cost (Dollars)	TY 2003 Other Unit Cost (Dollars)	TY 2003 Total Unit Cost (Dollars)	FY 2001 Mail Volume (Pieces)	FY 2001 Mail Volume (Percent)	TY 2003 Total Unit Cost (Dollars)	FY 2001 Mail Volume (Pieces)	FY 2001 Mail Volume (Percent)	Current Returns Adjustment Unit Cost (Dollars)	Current w/Rets Adj Total Unit Cost (Dollars)	After Rates Returns Adjustment Unit Cost (Dollars)	After Rates w/Rets Adj Total Unit Cost (Dollars)
<b>FIRST-CLASS MAIL LETTERS</b>														
Nonautomation Presort Letters		\$0.163	\$0.063	\$0.018	\$0.244	3,702,479,000	7.84%	\$0.244	57,664,168	5.01%				
Automation Presort Letters														
Automation Mixed AADC		\$0.055	\$0.045	\$0.018	\$0.118	2,634,662,000	5.58%	\$0.118	58,754,928	5.10%				
Automation AADC		\$0.046	\$0.044	\$0.018	\$0.107	2,820,125,000	5.97%	\$0.107	62,890,886	5.46%				
Automation 3-Digit		\$0.042	\$0.043	\$0.018	\$0.104	22,474,263,000	47.60%	\$0.104	538,406,052	46.78%				
Automation 5-Digit		\$0.032	\$0.041	\$0.018	\$0.091	14,038,959,000	29.73%	\$0.091	369,430,336	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		\$0.348	\$0.095	\$0.018	\$0.461	187,788,000	0.40%	\$0.461	318,683	0.03%				
Automation 5-Digit		\$0.235	\$0.095	\$0.018	\$0.348	254,253,000	0.54%	\$0.348	5,376	0.00%				
<b>WEIGHTED AVERAGE / TOTAL</b>	<b>\$0.115</b>	<b>\$0.052</b>	<b>\$0.045</b>	<b>\$0.018</b>	<b>\$0.115</b>	<b>47,214,206,000</b>	<b>100.00%</b>	<b>\$0.108</b>	<b>1,151,030,386</b>	<b>100.00%</b>	<b>\$0.0244</b>	<b>\$0.1320</b>	<b>\$0.0153</b>	<b>\$0.1229</b>
<b>Total Unit Cost Estimates, Including Contingency =</b>											<b>\$0.1359</b>	<b>\$0.1266</b>		
											Current (24)	After Rates (25)		

(1) Capital One witness Jean  
 (2) Capital One witness Jean  
 (3) USPS-LR-J-69 (FCM 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  
 (10) Docket No. R2001-1, PRC LR-2, Volume 4, "TYBR", page 3  
 (11) Letters: Docket No. R2001-1, PRC LR-4, "FCLETPRCFA.XLS", page 1  
 Flats: Docket No. R2001-1, PRC LR-4, "FCFLATSPRCFA.XLS", page 1  
 (12) Docket No. R2001-1, PRC LR-7, Page 2  
 (13) (10) - Weighted Average(11) - Weighted Average(12)  
 (14) (11) + (12) + (13)

(15) FY 2001 Billing Determinants  
 (16) (15) / [Sum (15)]  
 (17) Line Item (14), Total - Allocated by (19)  
 (18) Attachment A, Page 1  
 (19) (18) / [Sum (18)]  
 (20) (6) \* [ (4) \* [ (2) - (3) ] + (5) \* [ (1) - (3) ] ] / [ (4) + (5) ]  
 (21) Sum (17) + (20)  
 (22) [ [ (8) \* (7) + [ 1 - (8) ] \* (6) ] \* [ (5) \* [ (1) - (3) ] ] + (6) \* (4) \* [ (2) - (3) ] ] / [ (4) + (5) ] - (3) \* (6) - (7) \* (8) \* (5) / ((4) + (5))  
 (23) Sum (17) + (22)  
 (24) (21) \* (9)  
 (25) (23) \* (9)

Response to COS/NAA-T1-10, Page 3 of 6

Source: "New Mail Contribution" from witness Crum's attachment B

## **ATTACHMENT B, PAGE 1**

### Increased Contribution from New Mail Volume

New Mail Volume Contribution =  $(\$0.2910 \text{ (1)} - \$0.1266 \text{ (2)} - \$0.045 \text{ (3)}) * 15,458,969 \text{ (4)}$

= **\$1,846,000**

- (1) Test year estimated Capital One FCM presort revenue per piece (Attachment A, page 1)
- (2) Test year after rates estimated Capital One FCM presort cost per piece (Attachment A, page 2)
- (3) Applicable discount from declining block table tier 1.375 B - 1.450 B (Attachment B, page 5)
- (4) New Mail Volume (Bottom range estimate of test year after rates Capital One FCM volume minus test year before rates FCM volume from testimony of witness Elliot (COS-T-2)).

Response to COS/NAA-T1-10, Page 4 of 6

Source: "Return Cost Savings" from witness Crum's attachment B

## **ATTACHMENT B, PAGE 2**

### Address Change Service (ACS) Return Cost Savings

Return Cost Savings =  $(\$0.1359 \text{ (1)} - \$0.1266 \text{ (2)}) * 1,408,000,000$

**= \$ 13,094,400**

(1) Test year before rates estimated Capital One FCM presort cost per piece (Attachment A, page 2)

(2) Test year after rates estimated Capital One FCM presort cost per piece (Attachment A, page 2)

(3) Test year before rates forecasted Capital One FCM presort volume (COS-T-1, page 5)

**ATTACHMENT B, PAGE 3**

Discount Leakage

Discount leakage equals the estimated revenue foregone from discounts provided on mail volume that would have been sent even in the absence of the Negotiated Service Agreement (NSA). Since Capital One's test year before rates volume forecast equals 1.408 billion pieces, the discount leakage can be calculated as below:

$$\begin{aligned}
 \text{Discount Leakage} = & (1,275,000,000 - 1,225,000,001) * \$0.03 + \\
 & (1,325,000,000 - 1,275,000,001) * \$0.035 + \\
 & (1,375,000,000 - 1,325,000,001) * \$0.040 + \\
 & (1,408,000,000 - 1,375,000,001) * \$0.045 \\
 = & \boxed{\$ \quad 6,735,000}
 \end{aligned}$$

Declining Block Discount Table

First-Class Mail Presort Volume Range		Discount
0	to 1,225,000,000	\$ -
1,225,000,001	to 1,275,000,000	\$ 0.030
1,275,000,001	to 1,325,000,000	\$ 0.035
1,325,000,001	to 1,375,000,000	\$ 0.040
1,375,000,001	to 1,450,000,000	\$ 0.045
1,450,000,001	to 1,525,000,000	\$ 0.050
1,525,000,001	to 1,600,000,000	\$ 0.055
1,600,000,001	to above	\$ 0.060

1,408,000,000 Test year before rates Capital One FCM volume (COS-T-1)

Response to COS/NAA-T1-10, Page 6 of 6

Source: "Summary" from witness Crum's attachment B

## **ATTACHMENT B, PAGE 4**

### Summary USPS Financial Impact of NSA

Total New Contribution as a result of NSA = New Volume Contribution + Return Cost Savings - Discount Leakage

= **\$8,205,400**