

DOCKET SECTION

OFFICIAL TRANSCRIPT OF PROCEEDINGS BEFORE THE POSTAL RATE COMMISSION

In the Matter of:)

EXPERIMENTAL RATE AND)
SERVICE CHANGES TO IMPLEMENT)
NEGOTIATED SERVICE AGREEMENT)
WITH CAPITAL ONE SERVICES,)
INC.)

Docket No. MC2002-2

VOLUME #6

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POSTAL RATE COMMISSION

In the Matter of:)
)
EXPERIMENTAL RATE AND) Docket No. MC2002-2
SERVICE CHANGES TO IMPLEMENT)
NEGOTIATED SERVICE AGREEMENT)
WITH CAPITAL ONE SERVICES,)
INC.)

Room 300
Postal Rate Commission
1333 H Street, N.W.
Washington, D.C.

Volume 6
Wednesday, February 5, 2003

The above-entitled matter came on for hearing pursuant to notice, at 9:32 a.m.

BEFORE:

HON. GEORGE A. OMAS, CHAIRMAN
HON. DANA B. COVINGTON, VICE-CHAIRMAN
HON. RUTH Y. GOLDWAY, COMMISSIONER
HON. TONY HAMMOND, COMMISSIONER

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C O N T E N T S

WITNESSES APPEARING:

JEFF DAVID

CHRISTOPHER D. KENT

<u>WITNESSES:</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>	<u>VOIR DIRE</u>
Jeff David	--	--	--	--	--
Christopher Kent	--	--	--	--	--
by Mr. Baker	1001	--	--	--	--
by Mr. May	--	1112	--	--	--
by Mr. Reiter	--	1199	--	--	--

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E X H I B I T S

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P R O C E E D I N G S

(9:32 a.m.)

CHAIRMAN OMAS: Today we begin hearings to receive evidence filed in response to the direct case presented in support of the proposed negotiated service agreement between the Postal Service and Capital One Services, Inc.

This morning we will receive testimony from witnesses sponsored by the Newspaper Association of America and the National Newspaper Association. Tomorrow we will hear from witnesses sponsored by the Office of Consumer Advocate. This session of hearings will be completed on Friday when we will receive testimony from a witness invited to appear by the presiding officer.

No participant has requested the opportunity to conduct oral cross-examination of the National Newspaper Association Witness David. The Commission's practice in such circumstances is to receive the direct evidence of the witness at the beginning of the day so as to minimize potential inconvenience.

Therefore, I will revise the order of appearance of today's witnesses, and we will receive the testimony of Witness David first.

However, I have one procedural item to

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1 mention. Capital One Services, Inc. has designated an
2 institutional response for the Office of the Consumer
3 Advocate. I think it best that that response is
4 included in tomorrow's transcript before we hear
5 testimony from OCA.

6 Mr. May, will you introduce the designated
7 material as the first order of business tomorrow?

8 MR. MAY: Yes, indeed.

9 CHAIRMAN OMAS: Thank you. Does anyone at
10 this point have a procedural matter to discuss before
11 we begin hearing testimony?

12 (No response.)

13 CHAIRMAN OMAS: Ms. Rush, do you have two
14 corrected copies of the testimony of Witness David?

15 MS. RUSH: Yes, Mr. Chairman.

16 CHAIRMAN OMAS: And you can declare its
17 authenticity?

18 MS. RUSH: I have here two copies of Mr.
19 David's testimony, his signed declaration of
20 authenticity, and I am prepared to move those into
21 evidence at this time.

22 CHAIRMAN OMAS: Is there any objection?

23 (No response.)

24 CHAIRMAN OMAS: Hearing none, I will direct
25 counsel to provide the reporter with two copies of the

1 corrected direct testimony of Jeff David. That
2 testimony is received and will be transcribed into the
3 evidence.

4 (The document referred to was
5 marked for identification as
6 Exhibit No. NNA-T-1 and was
7 received in evidence.)

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NNA-T-1

Before the
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

EXPERIMENTAL CHANGES TO IMPLEMENT
CAPITAL ONE NSA

DIRECT TESTIMONY
OF JEFF M. DAVID
ON BEHALF OF THE
NATIONAL NEWSPAPER ASSOCIATION

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Testimony of Jeff M. David
On Behalf of the
National Newspaper Association

1 My name is Jeff David. I am owner and publisher of the *Livingston Parish* (LA)
2 *News*.

3

4 The *Livingston Parish News* is a 12,000 paid circulation twice weekly newspaper
5 published in Livingston Parish, Louisiana, directly east of Baton Rouge. I also
6 publish a 12,000 circulation shopper, the *Livingston Parish Dispatch*. The
7 *Livingston Parish News* is delivered through Periodicals mail. The *Livingston Parish*
8 *Dispatch* is delivered through Standard mail.

9

10 I am a native of Baton Rouge and a graduate of Louisiana State University and
11 LSU Law School. Between undergraduate school and law school I served in the
12 U.S. Army (1969-71). I practiced law in Baton Rouge for three years, then
13 assumed management of *The News* in July 1977 when my father, then the owner
14 and publisher, died of a sudden heart attack. I am the seventh owner-publisher of
15 *The News*, which celebrated its 104th anniversary in July 2002.

16

17 From 1984-1997 my wife, the former Nancy Estill from Shreveport, and I owned
18 and operated radio stations WBIU 1210 (AM) and 96.1 The River (FM), both of
19 which were marketed throughout the Baton Rouge metropolitan area. The stations
20 were sold in July 1997.

21

22 I am a former president of the Louisiana Press Association (1987-88), and have
23 served as Chairman of LPA's Government Relations Committee since 1997. I have
24 served as a member of the Board of Directors of the National Newspaper
25 Association since 1996, and as Chairman of NNA's Government Relations

1 Committee from 1997 to 2000. During the last three years, I have been NNA
2 Treasurer, Vice-President, and now President.

3

4 I. The Purpose of My Testimony

5

6 The purpose of my testimony today is to address the precedent set by the terms
7 of this particular Negotiated Service Agreement with Capital One Services, Inc.,
8 and describe the impact upon community newspapers that I expect if volume-
9 based rates are introduced into the postal system. I believe some of my concerns
10 can be extended beyond the newspaper business to many locally-owned and
11 operated businesses.

12

13 The proposal of the Postal Service has a work-sharing discount element in it. But
14 it also presents the equivalent of a volume-based discount by rewarding Capital
15 One with incremental discounts after its annual mail volume exceeds 1.225 billion
16 pieces. While the net contribution from Capital One's future mail volumes may
17 increase, it does not equal the contribution that would be made if those volumes
18 paid the full first-class per piece rates that would be due for the same volumes
19 mailed in the absence of this agreement. Therefore, a component of the proposal
20 involves a volume-based rate.

21

22 NNA supports work-sharing arrangements and while we do not object to the
23 aspects of this case that would exchange a discount for Capital One's additional
24 pre-mailing list hygiene, we do believe this arrangement is better handled in a
25 niche classification case where the benefits could extend immediately to other
26 mailers.

- 27

28 My main purpose here, however, is to point out the long-range problems I would
29 expect to see from volume-based discounts. My concern is not limited to the
30 Negotiated Service Agreement presented here. It extends to the many similar

1 agreements that inevitably will face the Postal Service, the Commission and
 2 American businesses if the precedent is established.

3 My concerns are as follows:

4

5 1. If the Capital One NSA is approved, it will open the door for numerous
 6 petitions for volume-based rates, which will create a major competitive advantage
 7 for large, nationally-oriented businesses in our economy.

8

9 2. Volume-based rates in markets involving newspapers will have a negative
 10 impact upon community newspapers, contravening 150 years of public policy.

11

12 3. Volume-based NSA's will inevitably leave money on the table that would
 13 benefit the Postal Service and, thus, all mailers.

14

15 II. Volume-based rates in the postal system will disadvantage small and locally-
 16 based businesses.

17

18 Any resident of a small town—and particularly of a town that became a growing
 19 suburb like Livingston Parish—who has watched the arrival of Wal-Mart knows
 20 what it means when massive economies of scale enter a marketplace. When this
 21 megabusiness enters a community, seismic shifts begin to occur.

22

23 As Wal-Mart comes in, consumers gain a sprawling one-stop shopping store.
 24 What they lose is a business that:

25

26 Keeps its money primarily in a local bank

27 Contributes to local community events

28 Advertises in the local newspaper

29 Handles special orders and provides hands-on customer service

30 And invests in the development of the community.

1 When Walmartization begins, downtowns shrivel. The pleasant strolls through a
2 bustling downtown turn into traffic jams in a suburban parking lot, and the
3 downtown gradually is boarded up.

4

5 Wal-Mart can purchase merchandise on a grand scale. It can order supplies,
6 control inventories, handle bookkeeping and negotiate for capital on a scale that
7 no local business can hope to achieve. Local businesses that hope to survive are
8 up against a daunting foe. Many do survive in spite of the odds, but communities
9 have lost something in the battle, nonetheless. I've read that Wal-Mart opens a
10 new megastore every other day, and that by 2004, it hopes to open one a day.
11 The pace of change in local commerce continues rapidly.

12

13 The analogy is apt. The Postal Service, with a volume of nearly 140 million
14 possible daily deliveries, its private express protections and its government
15 ownership, can carry chosen partners through the mailstream by offering a
16 tremendous economy of scale and scope. Here, its chosen partner is Capital
17 One.

18

19 The consequences of even this limited NSA may be imposed upon businesses in
20 my town, most of which are not yet aware of their peril. It is easy to see how.

21

22 For example, if my local bank wants to promote its credit card service with a
23 letter to the 33,000 households in Livingston Parish, it will pay between 27.5 and
24 30.9 cents at the presort first-class automation rates. As I understand the NSA
25 proposal, if Capital One wishes to promote its own credit card service to these
26 33,000 homes, it may be able to mail a similar size and shape letter for as much
27 as 6 cents less. If both my local bank and Capital One dropped an identical
28 33,000 piece mailing for the same credit card services on the same day and
29 Capital One is enjoying its maximum volume discount, Capital One begins the
30 race for customers \$1,320 to \$1,980 ahead of my bank in just postage savings. It
31 is easy to see why the local bank comes out the loser. And why a company

1 which has no real interest in Livingston Parish community life, culture or
2 business, can push my local bank out of a competitive position.

3

4 Being on this end of the economies of scale battle is a familiar experience for
5 small business owners. A local newspaper like mine experiences the
6 disadvantages of volumes of scale and scope all the time.

7

8 For instance, in my printing operation, I am a reasonably large consumer of ink.
9 In printing two newspapers and the work of various commercial customers, I
10 purchase as much as 25,000 gallons of ink annually. Yet, when my operation is
11 compared to that of a group-owned newspaper in my state—such as the
12 Shreveport Times, owned by the Gannett Company— I am a small ink customer.
13 Ink is priced by volume. Gannett's ink prices are proprietary. But from
14 conversations within the industry, I believe I pay 20 to 40 percent more for ink
15 than such large purchasers. If I compared my costs to those of a major national
16 printer, such as Quad Graphics, the differential would be even greater.

17

18 It's a burden the small business in America has to bear today. It is borne in
19 countless ways in purchases of products and services, from office supplies to
20 insurance to pension benefits. It is a reality of our economic system.

21

22 However, when the seller is a government-owned corporation with a protected
23 monopoly, the smaller purchaser is up against more than simple economies of
24 scale. It is up against an economy created through means other than the private
25 capital that fuels a private business, with all of the attendant risks to shareholders
26 and financiers. A small business, in my view, has a right to object to a misuse of
27 the public trust.

28

29 First, I believe this seller, the Postal Service of today, still relies heavily upon an
30 infrastructure originally created with tax dollars. Second, it is not required to
31 participate in the commercial marketplace on the same terms as any other

1 business. And, finally, because it is the sole source provider, the businesses
2 injured by these volume discounts do not even have the advantage of shopping
3 around to find a less costly provider.

4

5 Let me offer an example of how the sole source problem affects a purchaser.

6

7 I purchase approximately 350 tons of newsprint per year. Compared to a large
8 corporation like Gannett, my purchases are probably less than one percent of its
9 annual purchases. In the newsprint marketplace, discounting is widely practiced.
10 When supplies are limited, my newsprint prices may be as much as 15 to 20
11 percent higher than a nearby competitor with volume purchasing available.

12

13 But the newsprint market is highly competitive. When the market is not tight, I
14 can shop on the spot market and purchase a few tons at a time from the
15 remainder stocks left unclaimed by the big guys. Then, my prices are much more
16 competitive, and possibly even a little lower, because of my flexibility.

17

18 What would it be like if the Postal Service were the only producer of newsprint,
19 as it is a sole deliverer of letters? It would control an essential product for my
20 business, create a favorable rate for my competitors and economically and/or
21 legally restrain me from helping myself out of the bind by shopping elsewhere.

22

23 The Postal Service understandably wishes to follow the patterns of other large
24 businesses by providing volume discounts. But I believe it cannot be permitted to
25 follow the private sector lead in this situation. Extending volume discounts to
26 large mailers would be, in my view, an unfair way to use the monopoly.

27

28 III. Community newspapers specifically will face harms if this precedent is
29 extended further into the direct mail marketplace.

1 My newspaper will be affected by volume discounts that place large national
2 businesses in a preferred competitive position to the local businesses of
3 Livingston Parish. The local businesses are my readers and advertisers. If they
4 are harmed, my newspaper is harmed.

5 Another effect looms in the future, if this precedent is set. It will be the one
6 created by large direct mail firms entering my local advertising marketplace with
7 volume-based rates. If the Commission approves this NSA, it is not hard to
8 imagine that direct mail businesses will be in line for their turn at major discounts.

9

10 The disagreements between the newspaper industry and the Postal Service
11 about the development of the direct mail industry are long standing. They are not
12 always ones that have included NNA, as many of our members are active users
13 of Standard mail. As my biography indicates, I publish a thriving shopper that
14 uses Standard mail. NNA has long urged newspapers to use direct mail and take
15 advantage of the many opportunities it offers.

16

17 But we can do so only if we operate on a reasonably level playing field.

18

19 Just as my business in general is at an economic disadvantage against larger
20 businesses, my newspaper is at a specific disadvantage against large direct mail
21 companies for two reasons.

22

23 One, at least 40 percent of my costs are directly attributable to producing a news
24 and information product for my community. Reporters, photographers and editors
25 are expensive. News-gathering is a complex and costly operation. Competitors
26 interested in distributing only advertising avoid these costs.

27

28 Two, my newspaper is like most NNA members in that our direct mail package is
29 sent only to nonsubscribers. Advertisers reach most homes through the
30 newspaper—a periodicals-rates product. They do not wish to duplicate their ads
31 for our readers by including their ads in a shopper delivered to every household.

1 Our shopper, then, has less than total saturation. We cannot enjoy the saturation
2 discounts as a rule, and our direct mail competitors can. If a competitor enjoyed a
3 work-sharing saturation discount AND a volume-based discount, my small
4 newspaper would truly be operating under a great handicap.

5
6 Community newspaper publishers face daunting circumstances today. The
7 family-owned paper is not as common as in 1977 when I entered the business.
8 Yet many of us have survived. We believe our function in the democracy and in
9 our local communities is vital, and we struggle against the odds to succeed.

10

11 Because of my role as NNA's Government Relations Chairman, I've spent some
12 time with the history of newspaper postal rates. As recently as 1986, I
13 understand, the Commission revisited reasons for a within county mail class. The
14 now 150 year old public policy struck by Congress to encourage local
15 newspapers when it created the local newspaper mailing rate was created
16 specifically to help local papers fend off the impact of larger scale, inexpensive
17 publications from major cities. The notion of encouraging local papers was
18 debated by Congress and examined by several major commissions over the
19 years, as I understand it, and the conclusion was always the same. Local news is
20 important. Local newspapers are still the predominant channel for local news.
21 Even the all pervasive Internet has not displaced newspapers in their traditional
22 function of delivering news, even if the great fragmentation of the advertising that
23 pays for the news has made it more difficult to perform the mission. My paper is
24 still the major source of information for local politics, organizations, schools and
25 government in Livingston Parish.

26

27 I have traveled to other nations in my NNA work. It is striking that the United
28 States enjoys such a widely-diverse local press when most developed nations
29 have mostly national newspapers, with only a few locally-owned papers. I believe
30 postal policy is one major cause for our history of strong local newspapers.

1 The purpose of this policy is not to favor any particular business, but to favor
2 local information and news. Congress has reinforced and readopted the policy so
3 many times in the past 150 years that it is unimaginable to me that it would want
4 to undermine it now by permitting large national direct mail companies to enjoy
5 favorable rates through volume discounts. Such discounts would take a playing
6 field that already operates somewhat to the disadvantage of the local press and
7 tilt it dramatically against us.

8
9 I hope the Commission declines to permit volume-based rates. But if it decides to
10 permit Capital One's specific NSA to go forward, I urge the Commission in the
11 strongest terms to make it clear that the Postal Service may not enter into
12 agreements with national mailers that place local businesses at a direct
13 competitive disadvantage for no reason other than the volumes of their mail.

14
15 IV. Every mailer will be affected if contribution to institutional costs is
16 unnecessarily bargained away.

17
18 As a small mailer, I can attest that the impact of seven rate increases since 1991
19 has made every mailer apprehensive about policies that gamble with the Postal
20 Service's bottom line. As the president of NNA, I can further assure the
21 Commission that the frequent rate increases have been a factor in the severe
22 financial stress that in 2001 forced a major downsizing of the organization.

23
24 NNA has supported many initiatives to reduce the costs of postal operation. We
25 were pleased to learn in 2001 that within county mail fully covered its own costs
26 and even made a contribution to USPS overhead slightly in excess of its legal
27 requirement. We realize that the fixed costs of the postal system are massive,
28 and that when USPS cannot fully cover the costs, financial losses create more
29 frequent increases. Losses may also be created when the Postal Service leaves
30 money on the table in its contractual arrangements, as I believe it does here.

1 One major reservation about this NSA, and future negotiations with private
2 businesses is how the Postal Service will know whether it is leaving money on
3 the table that might have aided the system overall.

4

5 What I mean is that a company may be well aware that it is about to engage in
6 new and expansive commercial activities that would cause its mail volume to
7 grow. Or it may not even be fully aware of possible mail growth, but have merely
8 a sense that it may become a more active mailer. Yet, it may not choose to
9 share everything it senses or knows with the Postal Service. Why would it? The
10 nature of negotiation is to reveal enough and hold back enough to gain an
11 advantage.

12

13 If the Postal Service is the delivery service of choice—and for most of the mail in
14 the mailstream now, it is the only service available—USPS would have carried
15 the new mail volumes anyway. Unless it can tune its crystal ball with perfect
16 accuracy, it cannot predict which promised new volumes it would have had
17 anyway, and which truly are the result of an agreement. Nothing the Postal
18 Service or the Commission can do will force these inchoate plans into being or
19 onto a public record before their time, but the Postal Service can certainly, in its
20 eagerness to induce mail volumes, give away money that it would have gotten
21 anyway.

22

23 I look at it the same way I look at negotiations in my own business.

24

25 Let's imagine a grocery store came to me with a request for a discount and a
26 promise of new advertising lineage in the next year.

27

28 I certainly want the new advertising lineage. Perhaps it would help me post
29 another reporter at the State Capital.

1 But before I offer a discount, I must assess whether this advertiser is likely to
2 take its new volumes to another newspaper or a different advertising medium if I
3 do not provide the discount. If I believe I am likely to get the business anyway, I
4 then need to decide whether the advertiser is likely to spend more than its usual
5 one or two percent of its annual retail sales on advertising because of my
6 discounts.

7

8 If I'm likely to get the business anyway, and the discounts aren't going to change
9 my customer's ad budget, I have to conclude that this advertiser's proffered
10 business is driven by its need to generate new or more customers, and that it will
11 use my newspaper at its current rates if I do not provide the discount. Neither of
12 us knows what the other is thinking, or truly planning. But I do know this: if I give
13 away a lower rate to attract advertising that I would have had anyway, I'm giving
14 away money that I would probably otherwise spend on gathering local news and
15 strengthening my newspaper in its offerings to the readership. There will be an
16 impact to my decision, both to my company and the community, whichever way I
17 go.

18

19 The Postal Service can find itself in the same position. I understand it will offer
20 Capital One discounts in declining block rates after it exceeds 1.2 billion pieces
21 and goes as high as 1.6 billion pieces. But what if Capital One would have mailed
22 1.6 billion pieces anyway, at full rates, even if no NSA were in place? The Postal
23 Service cannot know. Even Capital One cannot perfectly foretell its own future.

24

25 When a business is offering discounts to protect itself from losing business to
26 competitors, the rationale for making discount decisions is different from the
27 rationale it would employ if it is simply trying to get a customer to buy more of a
28 product than it otherwise would. The Postal Service in this case does not need to
29 worry about losing Capital One's business to another Postal Service. Here it is
30 only trying to stimulate more activity. And I cannot see how it will ever know with
31 certainty that it is inducing a business to send more mail than it otherwise would

1 not have sent. Customers may say so, but that is a part of striking the bargain, in
2 my view.

3

4 I offer this perspective as a business owner, who practiced the economics of
5 pricing in commerce. If I owned the Postal Service, I would not take this risk. As a
6 mailer and a citizen, I urge the Commission to recommend strongly against it.

7

8 V. Conclusion

9

10 NNA is customarily in accord with much that the Postal Service does to develop
11 its mail services. We have entered into several niche classification cases and
12 participated in settlements that will allow the Postal Service to give back money
13 in exchange for more work by mailers. Nothing in my testimony changes NNA's
14 view that these agreements—which preferably would come in large enough
15 categories that many mailers could benefit—should continue.

16

17 This case is dramatically different. It will send the Postal Service on a new and
18 unwise course, which future decisions will not be able to reverse. Volume
19 discounting by the Postal Service as it is situated today cannot be equitable in
20 the marketplace. It cannot be productive in local economies. It places the future
21 financial position of the Postal Service at risk in ways that no one will ever be
22 able to precisely analyze. It requires both the Commission and the Postal Service
23 to guess at the future of entities they cannot control, and can only predict at great
24 hazard to all of us who use the mail.

Declaration of Jeff M. David

I declare, under penalty of perjury, that the foregoing Direct Testimony of Jeff M. David (NNA T-1) on behalf of the National Newspaper Association was prepared by me, or under my supervision, and that if called to testify under oath, it would be my testimony.

A handwritten signature in black ink, appearing to read "Jeff M. David", written over a horizontal line.

Jeff M. David

Dated: February 3, 2003

1 MS. RUSH: Mr. Chairman, I had one other
2 quick matter if you don't mind. I'm advised that the
3 thing for us to do with the interrogatories is to
4 provide a separate declaration after the packet has
5 been assembled. We're prepared to do that.

6 We also have filed today as a library
7 reference copies of Mr. David's newspapers, which had
8 been requested by COS in one of its interrogatories.
9 If any party wants a declaration of authenticity of
10 those, we're prepared to provide that as well.

11 CHAIRMAN OMAS: Fine. Without objection, so
12 ordered.

13 MS. RUSH: Thank you.

14 CHAIRMAN OMAS: There is written cross-
15 examination. Ms. Rush, would you please provide two
16 copies of the corrected designated written cross-
17 examination of Witness David to the reporter?

18 The witness has not had a final opportunity
19 to review the answers previously provided in writing.
20 Counsel, will you undertake to get a declaration of
21 authenticity from Witness David concerning responses
22 to designated written cross-examination and provide
23 that declaration within seven days?

24 MS. RUSH: Yes, Mr. Chairman. We'll be
25 happy to do that.

1 CHAIRMAN OMAS: Is there any additional
2 written cross-examination for Witness David?

3 (No response.)

4 CHAIRMAN OMAS: Thank you, Ms. Rush.

5 MS. RUSH: Thank you, Mr. Chairman.

6 CHAIRMAN OMAS: The designated written
7 cross-examination of Witness David is received into
8 evidence subject to the receipt of an appropriate
9 declaration and is to be transcribed into the record.

10 (The document referred to was
11 marked for identification as
12 Exhibit No. NNA-T-1 and was
13 received in evidence.)

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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Experimental Rate and Service Changes
to Implement Negotiated Service
Agreement with Capital One Services, Inc.

Docket No. MC2002-2

DESIGNATION OF WRITTEN CROSS-EXAMINATION
OF NATIONAL NEWSPAPER ASSOCIATION
WITNESS JEFF DAVID
(NNA-T-1)

Party

Interrogatories

American Postal Workers Union,
AFL-CIO

COS/NNA-T1-3

Capital One Services, Inc.

COS/NNA-T1-2, 4, 10

Newspaper Association of America

COS/NNA-T1-5-6, 8

United States Postal Service

COS/NNA-T1-2, 4, 10

Respectfully submitted,



Steven W. Williams
Secretary

INTERROGATORY RESPONSES OF
NATIONAL NEWSPAPER ASSOCIATION
WITNESS JEFF DAVID (T-1)
DESIGNATED AS WRITTEN CROSS-EXAMINATION

Interrogatory

COS/NNA-T1-2
COS/NNA-T1-3
COS/NNA-T1-4
COS/NNA-T1-5
COS/NNA-T1-6
COS/NNA-T1-8
COS/NNA-T1-10

Designating Parties

Capital One, USPS
APWU
Capital One, USPS
NAA
NAA
NAA
Capital One, USPS

COS/NNA-T1-2. Please refer to page 6 of your testimony, which states, "For example, if my local bank wants to promote its credit card service with a letter to the 33,000 households in Livingston Parish, it will pay between 27.5 and 30.9 cents at the presort first-class automation rates."

- (a) Please confirm that this local bank could also mail these letters at Standard Mail rates. If not confirmed, please explain fully.

I assume it could if it wished to purchase that level of service and have its customers identify its mail piece as advertising mail, as could Capital One Services, Inc.

- (b) Please confirm that this local bank could enter these letters at the destination sectional center facility. If not confirmed, please explain fully.

I assume any mailer could do so if its mail were properly prepared and transported.

- (c) Please confirm that it is less costly to enter an entire local mailing at a destination sectional center facility than to enter an entire national mailing at a destination sectional center facility. If not confirmed, please explain fully.

Not confirmed. I assume a variety of factors could affect the cost. For example, the answer might depend upon the location of the printer for the "national mailing." Presumably a "national mailing" could be sent electronically to a variety of points, printed and entered at a destination sectional center facility.

COS/NNA-T1-3 You state on Page 4 of your testimony that, while the net contribution from Capital One's future mail volumes may increase, it won't equal the contribution that would be made if those volumes in excess of 1.225 billion paid the full First-Class per piece rates and were mailed in the absence of the agreement. If those volumes in excess of 1.225 billion were not to be mailed in the absence of the agreement, would additional volume mailed because of the discount incentive increase the net contribution to the Postal Service?

I'm not sure I understand the question, nor which 'discount incentive' you have in mind, but if the question suggests that in the absence of mail there is an absence of contribution, I would agree. But my agreement does not negate my assertion that failing—for no reason other than to reward volume—to capture the full contribution of mail that IS mailed unfairly deprives the Postal Service of revenue. It also deprives other users of the system of the full benefit of the contribution that otherwise would be paid.

NNA-T1-4 On page 8 of your testimony, you state that because the Postal Service is the sole source provider, "the businesses injured by these volume discounts do not even have the advantage of shopping around to find a less costly provider." Is the advertising carried in your shopper, the Livingston Parish Dispatch, material that is covered and protected by the postal monopoly; and is it material that the advertiser can place either with you to be delivered in your Shopper to potential customers, or mailed directly to its potential customers?

I am not an expert on the private express statutes, Some of this material may be subject to the monopoly and some perhaps is not. I assume, whether or not it is covered by the private express statutes, it is mailable material and can be sent to potential customers either through a publication or directly.

COS/NNA-T1-5 Please confirm that you will neither be economically nor competitively injured by the Capital One NSA, assuming it produces a net contribution for the Postal Service. Please explain any negative answer to either parts of the question.

Not confirmed. Please see my response to COS/NNA T1-3.

COS/NNA-T1-6 On page 5 of your testimony, you state that, if the Capital One NSA is approved, "it will open the door for numerous petitions for volume based rates, which will create a major competitive advantage for large, nationally-oriented businesses in our economy." Do you believe that the Postal Rate Commission should decline to recommend highly discounted rate categories that are based on work-sharing efforts that are largely limited to those that are high volume mailers because such discounts create a "major competitive advantage" for those large volume national mailers compared to small local business mailers?

I believe that if work-sharing is the basis for a discount, it should be provided to all mailers capable of performing the work involved. Discounts should not be based upon volume.

COS/NNA-T1-8 Please explain how the Postal Service's monopoly position enables it to offer a lower discounted Standard A rate to advertisers who otherwise might place their advertising in your Shopper, the Livingston Parish Dispatch.

The Postal Service's monopoly position creates an economy of scale and scope that no other channel of printed material can equal, nor in fact, could attempt to equal under the law.

COS/NNA-T1-10

- (a) Please confirm that, your Shopper, the Livingston Parish Dispatch, is not eligible for periodical publication preferred rates, and the postal rates paid by your Shopper do not benefit from application of the educational and cultural rate criteria of the Postal Reorganization Act which is designed to benefit non-advertising media mail.

Confirmed.

- (b) Please confirm that your Shopper is predominantly an advertising vehicle that in no material way differs from other Standard Solicitation Mail sent through the Standard A rate sub-classes. If you cannot confirm, please present all the distinguishing characteristics for your Shopper that would differentiate it from the typical Standard A advertising piece, and submit several specimen copies of the Shopper.

I cannot respond to this question as I do not know what you mean by a "typical Standard A advertising piece." I am placing several copies of the Dispatch, and of my newspaper, the Livingston Parish News, on file as a library reference.

- (c) Please explain why your Shopper, which is predominantly an advertising vehicle, should be protected from the more efficient operations and consequent lower rates that are available to larger advertisers, merely because the owner of the Shopper also happens to be the owner of an eligible preferred-rate periodical publication that has been and remains favored by both the Postal Reorganization Act and by the decisions of this Commission over the years.

I am not seeking protection. I am seeking fairness.

1 CHAIRMAN OMAS: Mr. Baker, would you please
2 call your witness?

3 MR. BAKER: Thank you, Mr. Chairman. The
4 Newspaper Association of America calls Christopher
5 Kent.

6 CHAIRMAN OMAS: Would you stand and raise
7 your right hand?

8 Whereupon,

9 CHRISTOPHER D. KENT
10 having been duly sworn, was called as a
11 witness and was examined and testified as follows:

12 CHAIRMAN OMAS: Mr. Baker?

13 (The document referred to was
14 marked for identification as
15 Exhibit No. NAA-T-1.)

16 DIRECT EXAMINATION

17 BY MR. BAKER:

18 Q Mr. Kent, I am going to be handing you two
19 copies of a document entitled Direct Testimony of
20 Christopher D. Kent on behalf of the Newspaper
21 Association of America designated NAA-T-1 and would
22 ask you to review that and to tell me if I were to
23 examine you directly today would this be your
24 testimony?

25 A This is it.

1 CHAIRMAN OMAS: Would you pull the mike
2 closer, please?

3 THE WITNESS: Sure.

4 CHAIRMAN OMAS: Thank you.

5 MR. BAKER: With that, Mr. Chairman, I move
6 its admission in the record as the direct testimony of
7 Mr. Kent.

8 CHAIRMAN OMAS: Is there any objection?

9 (No response.)

10 CHAIRMAN OMAS: Hearing none, I will direct
11 counsel to provide the reporter with two copies of the
12 corrected direct testimony of Christopher Kent. That
13 testimony is received and will be transcribed into
14 evidence.

15 (The document referred to,
16 previously identified as
17 Exhibit No. NAA-T-1, was
18 received in evidence.)

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Postal Rate Commission
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NAA-T-1

**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

**DIRECT TESTIMONY
OF
CHRISTOPHER D. KENT
ON BEHALF OF THE
NEWSPAPER ASSOCIATION OF AMERICA**

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December 20, 2002

1 I am Christopher D. Kent, Senior Managing Director of FTI Consulting; my office is at
2 1201 Eye Street, NW, Suite 400, Washington, DC 20005. Since 1974, I have been
3 regularly involved in calculating revenues, costs, lost profits and project valuations
4 associated with a wide variety of industries and endeavors.

5 During the period between about 1990 and 1994 I directed numerous projects my
6 firm performed for the United States Postal Service (USPS or Postal Service). These
7 projects ranged from a feasibility analysis of a USPS National Control Center, to
8 operating efficiency studies at distribution centers, to examining the viability of an
9 integrated management system. My detailed qualifications are appended to this
10 testimony. I previously appeared before the Postal Rate Commission in Docket No.
11 R2000-1 as a rebuttal witness on behalf of the Newspaper Association of America.

12 **I. Overview of Testimony**

13 The Postal Service and Capital One Services, Inc. (COS) propose to enter a
14 negotiated service agreement (NSA) that will alter the rates charged and the services
15 provided by the USPS to COS. Among the major terms of the proposed agreement,
16 COS receives volume-based discounts (through a declining block schedule), and the
17 USPS waives the fee for electronic address correction service, in exchange for COS
18 waiving its current right to have nonforwardable undeliverable as addressed ("UAA")
19 mail returned physically to it.¹ The USPS estimates a net positive institutional cost

¹ In addition to being the USPS' largest First-Class mailer, COS experiences an unusually high rate of return mail.

2

1 contribution of \$8.2 million during the first year of the agreement. It calculates this net
2 as:

3 Total New Contribution as a result of NSA (\$8.2 million) = New Volume
4 Contribution (\$1.8 million) + Return Cost Savings (\$13.1 million) -
5 Discount Leakage (\$6.7 million).

6 By any measure, this is a good deal for COS. COS gets rate discounts for volumes
7 it is projected to have mailed anyway² and receives free of charge a service (Change
8 Service Requested, Option 2) soon to be offered by the USPS to other mailers for a
9 fee.³ This new service will allow COS to improve the quality of its mailing lists at no
10 charge. In exchange, COS commits to certain address practices – some of which it
11 already performs⁴ – and waives its right to physical returns. It would be logical to
12 surmise that COS really does not want those physical returns, so long as it can receive
13 address corrections more quickly by other means at no more cost. The USPS forecasts
14 that this combination will result in a net positive contribution to institutional costs.

15 There is ample reason to be concerned that the Postal Service has not calculated
16 the cost savings accurately. This is because: (1) the Postal Service proposes entering
17 a three-year NSA without having fully considered the financial implications of the

² USPS-T-2 at page 6, lines 1-4.

³ USPS witness Wilson testified that CSR, Option 2 will be available to all mailers in January, 2003 (USPS-T-4 at page 4, lines 10-12).

⁴ COS-T-1 at page 5, lines 12-20; page 6, lines 21-22; and page 7, lines 1-4.

3

1 second and third years;⁵ (2) the Postal Service has made no attempt to model the
2 actual costs of COS's mail, but instead relies upon average First Class Mail costs, albeit
3 with certain adjustments; and (3) even taken on its own terms, there are reasons to
4 believe that the USPS calculation of cost savings may be overstated. Because \$8.2
5 million is such a small amount when considering the USPS costs for handling 1.4 billion
6 pieces of mail, or even 768,000,000 pieces of solicitation mail, an error of just a few
7 cents per piece in its estimate would leave the USPS with not only no additional
8 contribution, but with a loss.

9 Essentially, the USPS contends that the cost savings it may experience from
10 reducing the number of physical returns (coupled with a small contribution from
11 additional volume it may mail as a result of the discounts) will override the loss of
12 revenue it will experience from the discounts it is granting COS. The discounts are at
13 mail volume levels that the USPS cost analysis assumes would have been handled in
14 the absence of the proposed agreement. Further, the USPS justification does not even
15 take into account the even larger value of the eACS fees that the USPS proposes to
16 waive for COS.

17 In my experience, no private firm would have negotiated the Postal Service's side of
18 this deal, and certainly would not have agreed to such a deal based solely on a single
19 year of analysis.⁶ Furthermore, in situations where, as here, the value of the deal to the
20 regulated entity is so dependent upon a hoped-for reduction in the costs of serving a

⁵ The USPS and Capitol One NSA has a proposed three-year term.

⁶ The USPS presented no cost estimates for years 2 and 3 of the proposed experiment and despite pressure from the Postal Rate Commission and other parties, has, to date, presented only various sensitivities to the volumes and costs to provide estimates of the effects of the NSA during years 2 and 3.

4

1 single customer, it is important for the regulated entity to understand that customer's
2 specific costs, and not simply base estimates on average costs. Strangely, the USPS
3 made no attempt to model COS's specific costs and there are substantial reasons to
4 believe that the counted-upon cost savings are not properly estimated. I address each
5 of my areas of concern below.

6 **II. The Commission Should Consider All Three Years of the NSA**

7 Despite proposing a three-year agreement, the USPS initially presented a cost
8 analysis for only the first year of the NSA. In response to requests subsequent to its
9 filing, the USPS has prepared several sensitivity analyses, but it has not committed to
10 any one final number for all three years.⁷ Further, several of the sensitivities result in
11 net negative contributions in years two and three.

12 A regulated firm operating under the break-even constraint of the Postal Service
13 should not entertain a multi-year arrangement such as this one without giving fuller
14 consideration to the financial impacts in the second and third years. If the USPS does
15 not realize its projected cost savings (such as if it has overstated the actual cost of
16 handling COS's mail) and actually does lose money, other mailers will pick up the tab.
17 The USPS has no shareholders to absorb the loss. Therefore, it is important to provide
18 a definitive number for the net contribution of the NSA over the full three-year term of
19 the agreement.

⁷ Response of USPS to Oral Request of Commissioner Goldway at Tr. 2/396-7, Response of USPS to APWU-USPS-2.

1 **III. The Volume And Fee Discounts Raise Issues That Should Be Considered**

2 Although the legality of non-cost justified declining block rates and fee waivers under
3 the Postal Reorganization Act is beyond the scope of my testimony, the proposed rate
4 structure does raise some important questions for rate design. First, the discounts
5 proposed in this NSA are not based on the potential cost savings that the USPS might
6 experience as, I understand, are intended by other USPS discounts. In other words,
7 unlike other postal discounts, there is no purported cost justification for the particular
8 volume thresholds for the various discounts.

9 Second, the proposed discounts start at a volume below the level of the predicted
10 volume for COS for FY2003, which assumes no discounted rate. If the discounts are
11 meant to serve as an incentive for COS to mail higher volumes, then the discounts
12 should start at a level above what COS is expected to mail without the discounts. If, on
13 the other hand, the discount is supposed to act as an incentive to motivate COS to
14 better sanitize its mail, then the discount should be based on the costs that will be
15 saved by the USPS. Instead, the proposed discounts seem to serve no purpose other
16 than to reduce USPS revenue. It is troubling to see the USPS offer one mailer a
17 discount that has no basis in either cost savings or volume incentives.

18 It is my understanding that the Postal Service also offers as a justification for the
19 NSA the notion that the declining block discounts will provide COS with an incentive to
20 retain its current First-Class Mail volume levels.⁸ If this is so, the Postal Service has
21 failed to extract any commitment from COS that it will, in fact, maintain its First-Class

⁸ USPS-T-2 at page 4, lines 16-20.

6

1 Mail volumes. Nor has the Postal Service negotiated a meaningful penalty. Although
2 the proposed NSA does contain a penalty provision (the greater of \$1 million or all ACS
3 fees for the year),⁹ it is set at a 750 million piece threshold, which is so significantly
4 below expected volume levels that if the penalty were to come into play COS
5 presumably would be experiencing more serious problems than merely declining First
6 Class Mail volumes.

7 Third, as a matter of rate design, it seems inequitable to give free eACS to a high-
8 cost entity, while mailers that engage in better address hygiene do not get a discount.
9 Essentially, COS receives a gift beyond the volume discounts of between \$15 and \$26
10 million from the USPS in the form of waived eACS fees – depending upon how many
11 eACS notifications it would receive -- apparently for little reason other than that its return
12 rate is so high.¹⁰ Presumably, other mailers will utilize CSR, Option 2, when it becomes
13 available. However, these mailers, unlike COS, will have to pay the \$0.20 fee per
14 notice. It is conceivable that some mailers could look to this proposed NSA and see
15 engaging in high cost behavior as a way to get a better deal with the Postal Service.
16 This would create an incentive exactly the opposite of the purpose of the proposed
17 NSA.

⁹ Witness Crum calculates that COS paid the USPS \$335 million in postage for FCM in FY2001 (USPS-T-3 at Attachment1).

¹⁰ I arrive at the \$15 to 26 million range by adding the eACS fees generated from return mail to those generated from forwards. The return mail fees equal the solicitation mail volume (760 million) multiplied by the return rate (9.6%), UAA success rate (85%), and the eACS fee/piece (\$0.20). The forward fees equal the product of the solicitation mail volume (760 million), forwarding rate (1.96% to 9.6%), CFS forwarding rate (95%), eACS fee/piece (\$0.20). I am using as the range for forwards here Mr. Crum's assumption that Capital One's forwarding rate is the system average of 1.96% (see Mr. Crum's response to POIR 2, Question 7) and 9.6% (set at the COS return rate as a proxy).

1 **IV. The USPS's Estimates of the Alleged Cost Savings Are Likely Overstated And**
2 **Should Not Be Relied Upon To Justify The NSA**

3 **A. The USPS Has Not Modeled COS's Actual Costs**

4 When basing cost savings on altering the cost behavior of such a large customer, it
5 is important to understand that customer's specific costs, and not simply to base the
6 estimated savings on averages. The USPS has a margin of only \$8.2 million in this
7 NSA. Although this may look like a lot of money, when one considers the per piece
8 costs for 1.4 billion pieces in the test year alone, an error in the cost estimates of a
9 penny or two becomes significant. Yet, the USPS projected cost savings are based on
10 average First-Class Mail costs. Those costs include pieces of all shapes and all levels
11 of worksharing. The average costs for First-Class Mail returns and forwards can
12 reasonably be expected to be more costly, per piece, for the USPS to handle than
13 COS's well-formatted First Class bulk mail, and thus using average costs inevitably
14 overstates the cost savings.

15 **B. There Is Substantial Reason To Believe That The USPS Has Overstated**
16 **The Costs To It Of Physically Returning COS's Mail**

17 Rather than determining what it actually costs to return COS's UAA mail, the USPS
18 has used the average costs for all First Class mailers, although with some adjustments.
19 This is likely to overstate the costs of physically returning COS's mail because COS's
20 mail is likely cleaner and easier to process during the return than the average piece. In
21 addition, the Postal Service's estimate of cost savings is based on FY2000 data, which
22 fails to reflect the cost savings likely to stem from the introduction of the Postal

1 Automated Redirection System (PARS) next year and its further deployment in the
2 second and third years of the NSA.

3 The USPS has presented no evidence that the shape mix of COS mail reflects that
4 of the First Class Mail (FCM) average mix. Presorted/bar-coded letters, the type of
5 letter that COS normally mails, comprise only a part of total FCM volume. The First
6 Class mailstream also includes flats and parcels, as well as hand-addressed letters, that
7 cost more to return than COS's mail.¹¹ Witness Crum's adjustment to remove the
8 postage due costs, while correct, does not address the additional costs of other shapes
9 and workshare levels. Thus, the average FCM return cost is unlikely to accurately
10 reflect the cost of returning COS's pieces, because COS's pieces are generally uniform
11 letters.

12 In response to an oral request from the Chairman, the USPS attempted to support
13 the belief that COS returns are as costly as other FCM returns.¹² However, problems
14 encountered in returning other mail, such as further searching for a return address that
15 may be on the back of the mailpiece, would appear not to apply to COS mail. Given
16 COS's typical letter-shaped mail, the average FCM returns cost (which contain the costs
17 for letters, flats, packages, and IPP's) is not appropriate to apply to COS mail.

18 Second, once COS return mail re-enters the mailstream for the trip to Richmond, it is
19 likely to require fewer sortations than the average piece. This is because the high
20 volume of COS mail should enable the USPS to gather COS returns into cases or sacks
21 that will remain together throughout the process. In contrast, the average FCM

¹¹ From LR-J-58; hand-written letters also cost more to process.

1 customer is more likely to have returns go through several sorts before enough pieces
2 are accumulated to gather into a separate container that can remain intact for the rest of
3 the returns process.

4 Third, the mail processing cost of returned mail in the USPS analysis appears to be
5 based on FY2000 IOCS data. The record is by no means clear whether FY00 data
6 accurately reflect even the current means of processing returns. In fact, witness
7 Wilson's testimony seemed to suggest that the process is even more automated than it
8 was a few years ago, although the Postal Service's later written statement appears to
9 back away from that statement. Regardless of the current process, however, these
10 methods will likely change with the implementation of the PARS system for returns and
11 forwards in 2003¹³ which should reduce the cost of returning mail throughout the
12 duration of the proposed NSA.

13 Beginning in July 2003, the USPS will be using the new PARS system to identify and
14 process UAA mail. Witness Wilson has testified that PARS will automate many of the
15 manual processes currently used to handle UAA mail,¹⁴ but the USPS has not included
16 any estimates to account for what should be much lower physical returns costs in its
17 analysis. As I understand, under PARS many of the costs of physical returns will be
18 eliminated for those UAA mailpieces identified by PARS. This is because the mailpiece
19 will be caught and identified as a return to sender piece at a much earlier stage in the
20 returns process

¹² Response of United States Postal Service to Oral Request of Chairman Omas at Tr. 2/342.

¹³ Response to APWU/USPS-T4-1.

¹⁴ Response to APWU/USPS-T4-1.

10

1 For these reasons, the Postal Service's use of average return costs (itself based on
 2 FY00 data) is likely to overstate the costs of physically returning Capital One's mail
 3 during the NSA. This, in turn, means the costs savings relied upon by the USPS are
 4 likely overstated. Although the amount of the overstatement is not known, it would not
 5 take much of an overstatement to eliminate entirely the purported cost savings or even
 6 cause the USPS to lose money. A reduction in the returns cost to reflect COS's lower
 7 costs produces significant changes in the cost savings estimated by the USPS. For
 8 example, a reduction of less than 25% to the returns cost/piece results in a loss to the
 9 USPS under the USPS cost analysis of the proposed NSA. See Table 1.

10 **Table 1: Physical Returns Costs¹⁵**

Difference from USPS Estimate	Physical Returns Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$13,094,000	\$8,205,000
-10%	\$0.480	\$9,574,000	\$4,685,000
-24%	\$0.407	\$4,787,000	-\$102,000
-35%	\$0.350	\$1,267,000	-\$3,622,000

¹⁵ Physical returns cost found in witness Crum's testimony, Attachment 2; the \$0.480, \$0.407, and \$0.350 figures were used instead of the \$0.535 figure as illustrative unit costs; these illustrative unit costs were used to calculate the return cost savings and net contribution in witness Crum's written testimony, Attachment B.

1 **C. The Postal Service Has Not Considered Forwarding Costs**

2 **1. Additional costs due to providing eACS for forwarded mail**

3 As a feature of FCM, COS solicitation mail is currently forwarded when the required
4 conditions are satisfied. Under the proposed NSA, COS solicitation mail will continue to
5 be forwarded, plus eACS will be provided. This occurs because COS has agreed to
6 accept Change Service Requested, Option 2, but it will not have to pay the 20 cent per
7 piece correction fee that all other CSR, Option 2 mailers will pay once that service
8 feature is offered. The additional cost of providing eACS has not been included in the
9 USPS cost analysis, but it should be included to fully account for the costs of the NSA.¹⁶

10 To do this accurately, one would need to know the volume of COS's forwarded mail.
11 However, this quantity is unknown. To estimate that volume and additional eACS costs,
12 three pieces of data need to be considered: the percentage of COS solicitation mail
13 forwarded, the percentage of COS solicitation mail forwarded through CFS
14 (Computerized Forwarding System), and the cost of providing eACS.

15 Taking these in order, in Mr. Crum's attempt to estimate this cost, he assumed that
16 COS's forwarding rate was equal to the FCM average forwarding rate.¹⁷ This is merely
17 an assumption; there is no evidence as to COS's actual forwarding rate. It should be
18 noted, however, that COS's return rate of 9.6% is eight times higher than the FCM
19 average of 1.2%. If COS's return rate so exceeds the average, then it is at least
20 appropriate to question whether its forwarding rate is the system average.

¹⁶ As discussed below, witness Crum admits that the USPS will incur an additional cost of at least \$0.066 per piece.

¹⁷ Witness Crum's response to POIR 2, Question 7.

12

1 As an alternative estimate of forwards, one might assume that the relationship
 2 between COS's forwarding and return rates corresponds to the average for all FCM.
 3 The forwarding average for all FCM (1.96%) is about 159% of the average return rate
 4 (1.23%). Under this assumption, COS's forwarding rate would be 159% of its return
 5 rate, which works out to 15.3%, although use of NCOA presumably should reduce the
 6 forwarding rate somewhat. See Table 2.

7 Second, not only is the amount of COS's forwarded mail unknown, but witness
 8 Crum's use of 85% as an estimate of the percentage of COS mail forwarded through
 9 CFS is questionable. This percentage is important because an eACS notice is only
 10 generated if the mail is forwarded through CFS. His calculation is:

11 Cost of providing eACS notices to forwarded mail = Solicitation mail
 12 volume * Percent of solicitation mail forwarded * **UAA success rate**
 13 (85%)* Cost/piece to provide eACS notice.

14 The UAA success rate of 85% is the number of eACS notices generated, divided by
 15 the UAA mail volume. However, that rate does not necessarily reflect the percentage of
 16 forwarded solicitation pieces that go through CFS. Witness Crum should have used the
 17 following calculation:

18 Cost of providing eACS notices to forwarded mail = Solicitation mail
 19 volume * Percent of solicitation mail forwarded * **Percent of solicitation**
 20 **mail that goes through CFS*** Cost/piece to provide eACS notice.

13

1 The USPS states that all CSR, Option 2, forwarded mail should go through CFS,
2 although some may be forwarded locally by mistake and thus not generate an eACS
3 notification.¹⁸ Currently (without CSR, Option 2), 4-5% of forwarded mail is forwarded
4 locally. Thus, a conservative estimate for the percentage of COS mail forwarded
5 through CFS would be 95%.

6 Third, witness Crum used a cost of \$0.066 for providing eACS for forwarded mail.
7 He acknowledged, however, that the true figure is slightly higher due to the cost of
8 providing media for the eACS transfer to COS.¹⁹ The \$0.066 cost is based solely on
9 letters that can be processed on mechanized terminals.²⁰ Note that in this instance Mr.
10 Crum did use a cost that is likely to reflect COS's mail, the effect of which is to result in
11 a lower cost of producing the eACS.

12 Given the percent of mail forwarded through CFS (either 85% or 95%) and the cost
13 of providing eACS for forwarded mail (\$0.066 per piece, although the true figure is
14 acknowledged to be slightly higher), it is possible to run sensitivities on the percent of
15 mail forwarded to see the effect on the additional contribution claimed by the Postal
16 Service to result from the NSA. I have used both witness Crum's assumption that 85%
17 of forwards go through CFS and the alternative assumption of 95% to calculate the
18 percentage of forwards that will generate the contributions in Table 2.

19

¹⁸ Response to APWU/USPS-T4-16.

¹⁹ Response to NAA/USPS-T3-14.

²⁰ According to LR-J-69 from Docket No. R2001-1, relied upon by Mr. Crum, 83% of FCM forwards are processed on mechanized terminals and 17% on non-mechanized terminals.

1 **Table 2: Forwarding Costs**

% Forwarded Using 85% Assumption for CFS Forwarded Mail	% Forwarded Using 95% Assumption for CFS Forwarded Mail	Additional Cost due to Providing EACS for Forwarded Mail	Total Contribution as a Result of the NSA
2.30%	2.05%	\$1,000,000	\$7,205,000
4.59%	4.11%	\$2,000,000	\$6,205,000
9.18%	8.22%	\$4,000,000	\$4,205,000
17.10%	15.30%	\$7,450,000	\$755,000
20.00%	17.89%	\$8,711,569	-\$506,569

2 This table shows that if as little as under 20 percent of COS's mail is forwarded, all of
 3 the USPS's estimated net contribution would be wiped out, without even considering the
 4 overstated cost savings from returns. Nor does this consider the \$15 to \$26 million in
 5 waived fees. However, it would still be appropriate to consider what costs the USPS
 6 would save from reducing the number of future returns.

7

8 **2. Avoided forwarding costs are overstated**

9 Witness Crum asserts that, because eACS will be used for COS forwarded mail,
 10 many repeat forwards will be avoided, thus saving the USPS the higher cost of
 11 forwarding the mail versus simply delivering it.²¹ He contends eACS will be able to
 12 better match names and addresses than NCOA and COS will be updating its lists with
 13 eACS information more quickly than through its current physical returns process.

²¹ As stated above, the USPS calculates the costs and savings associated with forwarding under CSR, Option 2, but does not rely upon them in their calculation of the net contribution of the proposed NSA.

15

1 There are two factors to consider when calculating the anticipated avoided costs: (1)
2 the number of repeat forwards avoided and (2) the cost difference between a forwarded
3 piece and a normally delivered piece. In order to identify the number of repeat forwards
4 avoided, witness Crum calculated the average number of solicitations to each delivery
5 point per year (5.6) and looked at the effects of several different numbers of notifications
6 that would be necessary before the name and address are corrected on COS's lists.
7 Witness Crum describes the use of any number of notifications other than one in the
8 analysis as conservative. It is clear, however, that (at least at the onset of the NSA)
9 multiple notifications will still be necessary due to the frequency of mailings and the lag
10 time between received the notification and incorporating the information into the mailing
11 lists.

12 Although witness Crum has a valid point regarding a probable improvement in the
13 repeat-forwarded rate, he is overly optimistic in his assumptions regarding avoided
14 costs. First, he failed to remove costs associated with postage due mail in his estimate
15 of the cost difference between a forwarded piece of mail and a normally delivered piece.
16 Second, he failed to account for the overall reduction in the costs of forwards that
17 should come from the introduction of the PARS system.

18 Witness Crum used \$0.307/piece for the cost difference between a forwarded piece
19 and a normally delivered piece. However, he neglected to remove the costs associated
20 with postage due mail, even though he makes this correction for returned mail costs.
21 Adjusting to remove the postage due mail costs reduces that cost figure, slightly, to
22 approximately \$0.306. Even that figure would seem to be high for Capital One's mail,

16

1 because it is an average that reflects the cost for shapes and workshare levels other
2 than the typical COS letter.

3 Most importantly, the Postal Service's \$0.307 cost estimate completely ignores any
4 changes to the forwarding process that will accrue from the introduction of the PARS
5 system early in the three-year period contemplated by the NSA. The PARS system,
6 when implemented, *should, at a minimum, significantly reduce the CFS and carrier*
7 *costs incurred in identifying forwarded pieces.* Thus, witness Crum appears to have
8 overstated the actual cost savings associated with the forwarding of COS mail.

9 **V. Summary**

10 It is easy to understand why COS is eager to sign up for this NSA. It is not as easy
11 to understand why the USPS or other First-Class mailers should be in favor of it. The
12 basis for the NSA, as presented by the USPS, is the positive net contribution that the
13 Postal Service claims will be the result of the proposed NSA. As I have explained, there
14 is ample reason to believe that the USPS has overstated the cost savings significantly.
15 When considering per piece costs for 1.4 billion pieces in the test year alone, a cost
16 error of a penny or two becomes significant.

—

**STATEMENT OF QUALIFICATIONS
OF
CHRISTOPHER D. KENT**

EDUCATION

University of Virginia, Charlottesville, Virginia, 1970
Bachelor of Arts

EMPLOYMENT HISTORY

Western Electric, Inc., King of Prussia, Pennsylvania, 1970-1976
Management Trainee
Production Supervisor
Section Chief Production Planning
Section Chief Costs and Forecasts

Conrail, Philadelphia, Pennsylvania, 1977-1978
Project Manager

United States Railway Association, Washington, DC, 1978-1980
Manager Equipment
Chief, Facilities and Equipment Analysis -- Asset Valuation

Transportation and Distribution Associates, Washington, DC, 1980-1981
Principal Consultant

Kent Associates, Inc. Washington Management Group, Washington, DC, 1981-1984
President, Vice President

Snively, King & Associates, Inc., Washington, DC, 1984-1987
Senior Consultant

Klick, Kent & Allen, Inc., Alexandria, Virginia, 1987-1998
Principal

FTI Consulting, Inc., Washington, DC, 1998-Present
Senior Managing Director

TESTIMONY

January, 1980	In the Matter of the Valuation Proceedings Under Sections 303(c) and 306 of the Regional Rail Reorganization Act. Special Court Misc. No. 76-1
October, 1981	In the Matter of the Valuation Proceedings Under Sections 303(c) and 306 of the Regional Rail Reorganization Act. Special Court Misc. No. 76-1
January, 1986	Oral testimony before the House of Delegates, Commonwealth of Virginia, Courts of Justice Committee
May 15, 1987	I.C.C. Docket No. 38301S - Coal Trading Corporation et al. v. The Baltimore and Ohio Railroad Company et al.
December, 1987	I.C.C. Docket No. 38301S (Sub-No. 1) - Westmoreland Coal Sales Company v. The Denver & Rio Grande Western Railroad Company, et al.
December, 1987	I.C.C. Docket No. 37038 Bituminous Coal -- Hiawatha, Utah to Moapa, Nevada and consolidated proceedings
January 14, 1988	I.C.C. Docket No. 38301S - Coal Trading Corporation et al. v. The Baltimore and Ohio Railroad Company et al.
June 20, 1988	I.C.C. Docket No. 37038 Bituminous Coal -- Hiawatha, Utah to Moapa, Nevada and consolidated proceedings
July, 1989	Oral testimony before the Superior Court of Rhode Island in the matter: National Railroad Passenger Corporation v. DOT, Providence & Worcester Railroad Co. v. RI
July 30, 1990	I.C.C. Docket No. 37038 Bituminous Coal -- Hiawatha, Utah to Moapa, Nevada and consolidated proceedings
October 10, 1990	I.C.C. Docket No. 37063, 38025S - The Dayton Power and Light Company v. Louisville and Nashville Railroad Company
December 14, 1990	I.C.C. Docket No. 37063, 38025S - The Dayton Power and Light Company v. Louisville and Nashville Railroad Company
January 25, 1991	I.C.C. Docket No. 37063, 38025S - The Dayton Power

	and Light Company v. Louisville and Nashville Railroad Company
July 15, 1991	I.C.C. Docket No. 37038 Bituminous Coal -- Hiawatha, Utah to Moapa, Nevada and consolidated proceedings
April 24, 1992	I.C.C. Finance Docket No. 31951 Southern California Regional Rail Authority For an Order Requiring Joint Use of Terminal Facilities of The Atchison, Topeka and Santa Fe Railway Company
May 7, 1993	I.C.C. Finance Docket No. 21215 (Sub-No. 5) Seaboard Air Line Railroad Company -- Merger -- Atlantic Coast Line Railroad Company -- Petition to Remove Traffic Protective Conditions
June 10, 1994	I.C.C. Finance Docket No. 21215 (Sub-No. 5) Seaboard Air Line Railroad Company -- Merger -- Atlantic Coast Line Railroad Company -- Petition to Remove Traffic Protective Conditions
October 11, 1994	I.C.C. Finance Docket No. 32549 Burlington Northern, Inc. And Burlington Northern Railroad Company -- Control and Merger -- Santa Fe Pacific Corporation and the Atchison, Topeka and Santa Fe Railway Company
March 29, 1995	I.C.C. Docket No. 37809, 37809 (Sub-No. 1) McCarty Farms, Inc., et al., and consolidated proceedings
May 30, 1995	I.C.C. Docket No. 41191 West Texas Utilities Company v. Burlington Northern Railroad Company
October 30, 1995	I.C.C. Docket No. 41185 Arizona Public Service Company and PacifiCorp v. The Atchison, Topeka and Santa Fe Railway Company
April 29, 1996	Finance Docket No. 32760. Union Pacific Corporation, Union Pacific Railroad Company and Missouri Pacific Railroad Company -- Control and Merger -- Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and The Denver & Rio Grande Western Railroad Company.
May 23, 1996	S.T.B. Docket No. 41191. West Texas Utilities Company v. Burlington Northern Railroad Company -- Petition of

Burlington Northern Railroad Company to Reopen Proceeding.

October 15, 1996 S.T.B. Docket No. 41242 Central Power & Light Company v. Southern Pacific Transportation Company; Docket No. 41295 Pennsylvania Power & Light Company v. Consolidated Rail Corporation; Docket No. 41626 MidAmerican Energy Company v. Union Pacific Railroad Company and Chicago & North Western Railway Company.

October 25, 1996 S.T.B. Docket No. 41242 Central Power & Light Company v. Southern Pacific Transportation Company; Docket No. 41295 Pennsylvania Power & Light Company v. Consolidated Rail Corporation; Docket No. 41626 MidAmerican Energy Company v. Union Pacific Railroad Company and Chicago & North Western Railway Company.

July 11, 1997 S.T.B. Docket No. 41989 Potomac Electric Power Company v. CSX Transportation, Inc. Reply Statement and Evidence of Defendant CSX Transportation, Inc.

May 26, 1998 S.T.B. Docket No. 42012 Sierra Pacific Power Company and Idaho Power Company v. Union Pacific Railroad Company, Opening Verified Statement.

July 1998 S.T.B. Finance Docket No. 33556. Canadian National Railway Company, Grand Trunk Corporation, and Grand Trunk Western Railroad Incorporated – Control -- Illinois Central Corporation, Illinois Central Railroad Company, and Cedar River Railroad Company.

September 28, 1998 S.T.B. Docket No. 42022 FMC Corporation and FMC Wyoming Corporation v. Union Pacific Railroad Company, Verified Statement Supporting UP's Opposition to FMC's Petition for Partial Revocation of Exemption for Coke.

December 1998 S.T.B. Finance Docket No. 33556. Canadian National Railway Company, Grand Trunk Corporation, and Grand Trunk Western Railroad Incorporated – Control -- Illinois Central Corporation, Illinois Central Railroad Company, and Cedar River Railroad Company.

January 15, 1999 S.T.B. Docket No. 42022 FMC Corporation and FMC

	Wyoming Corporation v. Union Pacific Railroad Company, Opening Verified Statement of Christopher D. Kent and Benton V. Fisher.
March 31, 1999	S.T.B. Docket No. 42022 FMC Corporation and FMC Wyoming Corporation v. Union Pacific Railroad Company, Reply Verified Statement of Christopher D. Kent and Benton V. Fisher.
April 30, 1999	S.T.B. Docket No. 42022 FMC Corporation and FMC Wyoming Corporation v. Union Pacific Railroad Company, Rebuttal Verified Statement of Christopher D. Kent and Benton V. Fisher.
July 15, 1999	S.T.B. Docket No. 42038 Minnesota Power, Inc. v. Duluth, Missabe and Iron Range Railway Company, Opening Verified Statement of Christopher D. Kent and Benton V. Fisher.
August 30, 1999	S.T.B. Docket No. 42038 Minnesota Power, Inc. v. Duluth, Missabe and Iron Range Railway Company, Reply Verified Statement of Christopher D. Kent and Benton V. Fisher.
September 28, 1999	S.T.B. Docket No. 42038 Minnesota Power, Inc. v. Duluth, Missabe and Iron Range Railway Company, Rebuttal Verified Statement of Christopher D. Kent and Benton V. Fisher.
April 4, 2000	Expert Report of Christopher D. Kent, In the Matter of IFL Group, Inc. v. Birmingham Express.
June 15, 2000	S.T.B. Docket No. 42051 Wisconsin Power and Light Company v. Union Pacific Railroad Company, Opening Verified Statement of Christopher D. Kent and Benton V. Fisher.
August 14, 2000	S.T.B. Docket No. 42051 Wisconsin Power and Light Company v. Union Pacific Railroad Company, Reply Verified Statement of Christopher D. Kent and Benton V. Fisher; and Reply Verified Statement of Christopher D. Kent and Michael R. Baranowski.
August 14, 2000	Postal Rate Commission, Docket No. R2000-1, Rebuttal Verified Statement of Christopher D. Kent.

September 28, 2000	S.T.B. Docket No. 42051 Wisconsin Power and Light Company v. Union Pacific Railroad Company, Rebuttal Verified Statement of Christopher D. Kent and Benton V. Fisher.
December 14, 2000	S.T.B. Docket No. 42054 PPL Montana, LLC v. The Burlington Northern Santa Fe Railway Company, Opening Verified Statement of Christopher D. Kent and Benton V. Fisher.
March 13, 2001	S.T.B. Docket No. 42054 PPL Montana, LLC v. The Burlington Northern Santa Fe Railway Company, Reply Verified Statement of Christopher D. Kent and Benton V. Fisher; and Reply Verified Statement of Christopher D. Kent and John C. Klick.
May 7, 2001	S.T.B. Docket No. 42054 PPL Montana, LLC v. The Burlington Northern Santa Fe Railway Company, Rebuttal Verified Statement of Christopher D. Kent and Benton V. Fisher.
January 15, 2002	Docket No. 42057 Texas Municipal Power Agency v. The Burlington Northern Santa Fe Railway Company, Reply Verified Statement of Christopher D. Kent and John C. Klick.
May 22, 2002	Finance Docket No. 32760. Union Pacific Corporation, Union Pacific Railroad Company and Missouri Pacific Railroad Company --Control and Merger-- Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and The Denver and Rio Grande Western Railroad Company.
May 24, 2002	Finance Docket No. 42070. Duke Energy Corporation v. CSX Transportation, Inc., Opening Evidence and Argument of CSX Transportation, Inc.
Sept. 20, 2002	Finance Docket No. 42070. Duke Energy Corporation v. CSX Transportation, Inc., Reply Evidence and Argument of CSX Transportation, Inc.

1 CHAIRMAN OMAS: Mr. Kent, have you had an
2 opportunity to examine the packet of designated
3 written cross examination that was made available to
4 you in the hearing room this morning?

5 THE WITNESS: Yes, sir, I have.

6 CHAIRMAN OMAS: If the questions contained
7 in that packet were posed to you orally today, would
8 your answers be the same as those previously provided
9 in writing?

10 THE WITNESS: Yes, sir, they would.

11 CHAIRMAN OMAS: Are there any corrections or
12 additions you would like to make?

13 THE WITNESS: Not that I'm aware of.

14 MR. BAKER: Mr. Chairman, let me interject
15 at this point that yesterday the Postal Service filed
16 an errata and a declaration of Mr. Wilson, and I
17 believe they filed an amended answer to an APWU
18 interrogatory response. We just got them.

19 There is, in our understanding, a continuing
20 obligation on the part of the Postal Service to update
21 the record, and we respect the good faith of the
22 Postal Service counsel to do so. At the same time,
23 these were filed just a day before Mr. Kent's
24 appearance, and we have not yet had an opportunity to
25 assess whether it makes any difference in his

1 testimony or interrogatory responses.

2 I think we'll just have to take an
3 opportunity to review those things, and if there is a
4 need to update his testimony response we will do so at
5 the appropriate time.

6 CHAIRMAN OMAS: Without objection.

7 Mr. Baker, would you please provide two
8 copies of the corrected designated written cross-
9 examination of Witness Kent to the reporter? That
10 material is received into evidence, and it is to be
11 transcribed into the record.

12 (The document referred to was
13 marked for identification as
14 Exhibit No. NAA-T-1 and was
15 received in evidence.)

16 //

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19 //

20 //

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22 //

23 //

24 //

25 //

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Experimental Rate and Service Changes
to Implement Negotiated Service
Agreement with Capital One Services, Inc.

Docket No. MC2002-2

DESIGNATION OF WRITTEN CROSS-EXAMINATION
OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT
(NAA-T-1)

Party

American Postal Workers Union,
AFL-CIO

Capital One Services, Inc.

United States Postal Service

Interrogatories

COS/NAA-T1-1, 5, 9-10, 15-18, 21-22, 29-30

USPS/NAA-T1-2, 5-6, 12, 14, 19

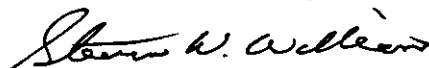
COS/NAA-T1-1-16, 18-20, 22-34, 36-39

USPS/NAA-T1-3-4, 10-11, 15-20

COS/NAA-T1-1-16, 18-20, 22-33

USPS/NAA-T1-1, 3-4, 6-7, 9-20

Respectfully submitted,



Steven W. Williams
Secretary

INTERROGATORY RESPONSES OF
NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT (T-1)
DESIGNATED AS WRITTEN CROSS-EXAMINATION

Interrogatory

COS/NAA-T1-1
COS/NAA-T1-2
COS/NAA-T1-3
COS/NAA-T1-4
COS/NAA-T1-5
COS/NAA-T1-6
COS/NAA-T1-7
COS/NAA-T1-8
COS/NAA-T1-9
COS/NAA-T1-10
COS/NAA-T1-11
COS/NAA-T1-12
COS/NAA-T1-13
COS/NAA-T1-14
COS/NAA-T1-15
COS/NAA-T1-16
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COS/NAA-T1-25
COS/NAA-T1-26
COS/NAA-T1-27
COS/NAA-T1-28
COS/NAA-T1-29
COS/NAA-T1-30
COS/NAA-T1-31
COS/NAA-T1-32
COS/NAA-T1-33

Designating Parties

APWU, Capital One, USPS
Capital One, USPS
Capital One, USPS
Capital One, USPS
APWU, Capital One, USPS
Capital One, USPS
Capital One, USPS
Capital One, USPS
APWU, Capital One, USPS
APWU, Capital One, USPS
Capital One, USPS
Capital One, USPS
Capital One, USPS
Capital One, USPS
APWU, Capital One, USPS
APWU, Capital One, USPS
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APWU, Capital One, USPS
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Capital One, USPS
Capital One, USPS
Capital One, USPS
APWU, Capital One, USPS
APWU, Capital One, USPS
Capital One, USPS
Capital One, USPS
Capital One, USPS

COS/NAA-T1-34	Capital One
COS/NAA-T1-36	Capital One
COS/NAA-T1-37	Capital One
COS/NAA-T1-38	Capital One
COS/NAA-T1-39	Capital One
USPS/NAA-T1-1	USPS
USPS/NAA-T1-2	APWU
USPS/NAA-T1-3	Capital One, USPS
USPS/NAA-T1-4	Capital One, USPS
USPS/NAA-T1-5	APWU
USPS/NAA-T1-6	APWU, USPS
USPS/NAA-T1-7	USPS
USPS/NAA-T1-9	USPS
USPS/NAA-T1-10	Capital One, USPS
USPS/NAA-T1-11	Capital One, USPS
USPS/NAA-T1-12	APWU, USPS
USPS/NAA-T1-13	USPS
USPS/NAA-T1-14	APWU, USPS
USPS/NAA-T1-15	Capital One, USPS
USPS/NAA-T1-16	Capital One, USPS
USPS/NAA-T1-17	Capital One, USPS
USPS/NAA-T1-18	Capital One, USPS
USPS/NAA-T1-19	APWU, Capital One, USPS
USPS/NAA-T1-20	Capital One, USPS

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
CAPITAL ONE SERVICES, INC.**

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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
CAPITAL ONE SERVICES, INC.**

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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
CAPITAL ONE SERVICES, INC.**

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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
CAPITAL ONE SERVICES, INC.**

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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
CAPITAL ONE SERVICES, INC.**

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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
CAPITAL ONE SERVICES, INC.**

(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.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
CAPITAL ONE SERVICES, INC.**

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 (Thousands)</u>	<u>Cost/Piece</u>	<u>Annual Cost (Thousands)</u>	<u>Frequency</u>	<u>Weighted 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
5. Total					\$0.5350

(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.

(8)	Capital One Statement Return Percentage =	4.6%
(7)	Average Present Customer Return Percentage =	1.23%
(6)	Before Rates Customer Mail Volume =	550,000,000
(5)	Before Rates Solicitor Mail Volume =	750,000,000
(4)	Manual Returns Unit Cost =	\$0.558
(3)	Electronic Returns Unit Cost =	\$0.333
(2)	Address Change Service (ACS) Success Rate =	88.9%
(1)	Configuration Factor =	1.830

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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 = $(\$0.2910 \text{ (1)} - \$0.1266 \text{ (2)} - \$0.045 \text{ (3)}) \times 15,458,969 \text{ (4)}$

= **\$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 = $(\$.1359 \text{ (1)} - \$.1266 \text{ (2)}) * 1,408,000,000$

= \$ 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:

$$\begin{aligned} \text{Discount Leakage} = & (1,275,000,000 - 1,225,000,001) * \$.03 + \\ & (1,325,000,000 - 1,275,000,001) * \$.035 + \\ & (1,375,000,000 - 1,325,000,001) * \$.040 + \\ & (1,408,000,000 - 1,375,000,001) * \$.045 \\ = & \boxed{\$ 6,735,000} \end{aligned}$$

Declining Block Discount Table

<u>First-Class Mail Presort Volume Range</u>			<u>Discount</u>
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**

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COS/NAA-T1-15 On page 4, you are critical of the failure to present a three year cost analysis, noting that if the Service fails to realize projected cost savings, in the second and third years, other mailers will have to absorb any losses. Please explain precisely how you would propose that the Postal Service calculate the cost savings and financial impacts of the proposed NSA in years 2 and 3, bearing in mind your further criticism that the postal Service should have modeled the cost of handling Capital One's First-Class Mail, rather than using average First-Class mailing costs. Please specifically describe the methods you propose the Postal Service use to calculate Capital One's costs, Capital One's volumes, and the roll forward programs that you would use for cost and volume projections for all three years of the agreement.

ANSWER:

The point I am making at the referenced page of my testimony is that the Postal Service, as the proponent of the NSA, should have identified the actual costs to it of returning and forwarding Capital One's mail, and what those costs will be in the second and third years of the NSA, rather than relying on averages. It is not the purpose of my testimony to develop the cost model and to calculate those costs in order to accurately analyze the impact of the proposed NSA, a burden that is on the Postal Service.

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COS/NAA-T1-16 Would it be your contention that the Commission should recommend no NSA with any postal customer unless the Postal Service is able to model the costs of that particular customer, if cost savings are an element of the agreement; and unless the future volumes of that customer, of whatever class or sub-class, can be projected in some objectively verifiable form? Please explain your answer.

ANSWER:

I believe that the Postal Service should present an accurate and complete cost and benefit analysis of any proposed NSA. Without knowing the impact of a given NSA, it is impossible to determine if the NSA is beneficial or harmful.

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COS/NAA-T1-17 On page 5, you testify that if the proposed discounts are supposed to act as an incentive to motivate COS to better sanitize its mail, then the discount should be based on the cost that would be saved by the Postal Service. Is it not the case that one of the purposes of the proposed discount is to create an incentive for Capital One to agree to accept free address correction service in lieu of the actual physical return of its UAA First-Class Mail, thereby improving the quality of Capital One's addresses, with resultant cost savings, and saving the Postal Service the costs of physical return of UAA mail? Explain any negative answer.

ANSWER:

As I was not part of the negotiations, it is impossible for me to say what the purpose of the discount is, although I am aware that USPS and COS witnesses have stressed that the discounts and free eACS parts of the agreement cannot be analyzed separately but must be considered as a whole. It seems that a more direct way to address the problem of Capital One's preference for free, but high-cost, physical returns in lieu of less costly, but higher priced, electronic address confirmation service is to correct the faulty pricing signals for physical returns and ACS.

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COS/NAA-T1-18 On pages 5 and 6 of your testimony, you state that the Postal Service has failed to extract any commitment from Capital One that it will, in fact, maintain its First-Class Mail volumes and, consequently, the proposed discounts will not incent Capital One to retain current First-Class Mail. Granted that a penalty for breaching a guarantee of volume would be a strong incentive to maintain the volumes, is it not also the case that providing a discount for current levels of First-Class Mail at the margin would also create an incentive to maintain that volume? Please explain any negative answer.

ANSWER:

Yes. In the proposed NSA, however, the discounts start at anywhere from 1.025 – 1.225 billion pieces, depending on the volume Capital One mails in the first year of the agreement. In absence of the proposed NSA, Capital One expects to mail 1.408 billion pieces in FY2003. See testimony of COS witness Jean, page 5.

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COS/NAA-T1-19 On page 6 you state that the volume penalty provision set at a 750 million piece threshold is set so low that you imply that it is meaningless and would come into play only if something more serious than declining First-Class volumes were afflicting Capital One. Would it not be the case that Capital One, while remaining quite healthy and viable, could still divert all of its First-Class Mail solicitation volume to Standard Class solicitation and make the 750 million piece threshold a very real and very meaningful guarantee and real penalty? Please explain any negative answer.

ANSWER:

I am not privy to Capital One's proprietary and confidential information, such as its algorithm to decide whether or not to mail a FCM solicitation. Therefore, I can neither confirm nor rebut. However, I believe that in this case Mr. Jean has testified that Capital One did not make any representations as to changes in its use of First-Class Mail if the NSA were not reached. See Tr. 2/70 (NAA/COS-T1-11).

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COS/NAA-T1-20 On page 6, you testify that it is conceivable that some mailers will look to this particular NSA and see "engaging in high cost behavior as a way to get a better deal with the Postal Service." Please explain how it makes economic sense to a mailer to deliberately send undeliverable mail so that the mailer might receive free address correction service for that undeliverable address. Please explain how the costs of the preparation of the mail, the postage affixed to the mail, and the lost opportunity cost of being unable to reach your customer, would be economically offset by getting free address correction service rather than paying 20 cents for a correct address?

ANSWER:

Nowhere in my testimony do I say that mailers will deliberately send UAA mail.

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COS/NAA-T1-21 On page 12 of your testimony, you state that "one might assume that the relationship between COS's forwarding and return rates corresponds to the average for all FCM." Isn't it the case that you actually mean that it corresponds to the ratio between forwarding and return rates? Please explain the logical rationale for linking the ratio (percent forwarded to percent returned) to Capital One's First-Class Mail and First-Class solicitations volumes? Please explain what there is about a high return rate for a mailer that would dictate that it would also have an abnormally high forwarding rate?

ANSWER:

Yes, I am comparing the ratio of COS's forwarding to return rate to the FCM forwarding to return rate ratio. The reason I think that Capital One's forwarding rate is high is because their address list quality is poor, as indicated by their return rate of 9.6% (*eight* times the FCM average). This is hardly surprising, given that Capital One has no relationship with the people on their solicitation lists. What is surprising is the contention made by the USPS that Capital One, despite the poor quality of their address lists, is somehow catching the vast majority of the address changes every year. The USPS justifies its assumption that Capital One's forwarding rate is equal to the FCM average on the grounds that COS uses the NCOA (National Change-of-Address) system to update its mailing lists every 60 days. NCOA catches only about 25% of possible change of addresses, which means **75%** will not be caught by NCOA. According to witness Wilson, 17% of households move each year. It is difficult to believe that while COS has incorrect addresses for 9.6% of its solicitation targets, it somehow manages to catch the majority of the 75% of change of addresses that NCOA does not. My rationale for linking the forwarding rate to the return rate is that both are related to poor address quality and if Capital One has a return rate 8

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times higher than the FCM average, then one would expect the forwarding rate for the mail sent using those same address lists to be higher than the FCM forwarding rate.

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COS/NAA-T1-22 On page 16, you state that witness Crum "appears to have overstated the actual cost savings associated with the forwarding of COS Mail." Please confirm that witness Crum did not claim any savings from reduced forwarding costs in calculating his net contribution from the Capital One deal. Is it not the case that there will indeed be some cost savings and that those cost savings would, if included, increase the net contribution from the Capital One deal? Explain any negative answer.

ANSWER:

Confirmed that Mr. Crum did not claim any savings from reduced forwarding costs in calculating his net contribution from the NSA. Further confirmed that there should be some amount of cost savings from reduced forwards. However, I cannot confirm that the net effect would be to increase the net contribution from the NSA, because the net effect cannot be known without knowing the costs and volumes of Capital One's forwarded mail, including the effects of the implementation of PARS.

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COS/NAA-T1-23. Please refer to page 12 of your testimony where you state, "As an alternative 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 the NCOA presumably should reduce the forwarding rate somewhat."

- (a) Please confirm that if the FY 2003 Before Rates forwarding rate for Capital One's First-Class Mail solicitations was 15.3%, then the Postal Service would forward 117.5 million (15.3% times 768 million) Capital One First-Class Mail solicitations in FY 2003 Before Rates. If not confirmed, how many Capital One First-Class Mail solicitations would the Postal Service need to forward?
- (b) Please provide a revised version of Table 2 in your testimony which includes a column showing the "Number of Capital One Pieces Forwarded" that you used to calculate the additional cost due to providing eACS for forwarded mail.

ANSWER:

- a) Confirmed that 15.3% of 768 million is 117.5 million. In my calculations for table 2 in my testimony, however, I used the after-rates FY2003 volume of 776 million solicitation pieces.

b) Table 2: Forwarding Costs

Number of Capital One Pieces Forwarded	% Forwarded Using 85% Assumption for CFS Forwarded Mail	% Forwarded Using 95% Assumption for CFS Forwarded Mail	Additional Cost due to Providing EACS for Forwarded Mail	Total Contribution as a Result of the NSA
15,151,515	2.30%	2.05%	\$1,000,000	\$7,205,000
30,303,030	4.59%	4.11%	\$2,000,000	\$6,205,000
60,606,061	9.18%	8.22%	\$4,000,000	\$4,205,000
112,878,788	17.10%	15.30%	\$7,450,000	\$755,000
131,993,468	20.00%	17.89%	\$8,711,569	-\$506,569

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COS/NAA-T1-24. Please refer to www.usps.com/history/pfact00.htm.

- (a) Please confirm that "[a]bout 17% of the nation's population moves every year, resulting in more than 44 million address changes." If not confirmed, how many addresses change every year? Please provide all relevant citations.
- (b) Please confirm that 44 million address changes every year translates into approximately 3.667 million address changes every month. If not confirmed, how many addresses change every month? Please provide all relevant citations.

ANSWER:

- a) Confirmed that witness Wilson testified to this during his oral cross-examination (see transcript Volume 3 - Hearing Held on December 4, 2002, Testimony of Witnesses Bizzotto (USPS-T-1) and Wilson (USPS-T-4), page 639).
- b) Confirmed that 44 million/12 equals 3.667 million. This is the number of address changes every month on average, although I have not seen evidence showing that this number is consistent every month.

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COS/NAA-T1-25. Please refer to pages 1 and 2 of USPS-T-4 where witness Wilson states, "Whenever a First-Class Mail piece is UAA, the postal carrier must determine if the customer has moved, or if a deficiency in the address prevents the mailpiece from being delivered to the recipient or address shown on the piece. If the customer has moved, the delivery unit is instructed to send the piece to the CFS unit for redirection to the customer's new address...If an address deficiency makes the mail piece undeliverable, the carrier typically notes on the mailpiece the reason for non-delivery and indicates that the mailpiece should be returned to the sender." Please refer further to witness Crum's response to OCA/USPS-T3-24(c) where he states, "Most returns are not related to the fact that a mail recipient moves."

- (a) Please confirm that the primary reason why First-Class Mail has to be forwarded is that postal customers move. If your response is anything other than an unqualified yes, please explain fully.
- (b) Please confirm that forwarded First-Class Mail generally has an accurate old address for the postal customer. If your response is anything other than an unqualified yes, please explain fully.
- (c) Please confirm that the primary reason why a First-Class Mail workshared letter is returned is that the address on the mailpiece is deficient. If not confirmed, please explain fully and provide a description of all analysis that you have performed of the reasons that First-Class mail workshared letters are returned.

ANSWER:

- a) – b) This is my understanding.
- c) Confirmed that Table 4.4 of USPS LR-J-69 shows that mailpieces returned for the following reasons:

Attempted, Not Known,
No such Number/No Such Street, and
Insufficient Address

comprise 42.57% of the total FCM returned to sender by delivery unit.

The table does not have a separate distribution of reasons for non-delivery for workshared letters nor a distribution of reasons for non-delivery for mailpieces returned to sender by CFS units.

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COS/NAA-T1-26. Please refer to witness Crum's response to OCA/USPS-T3-24(c) where he states, "Thus, Capital One can keep their forwarding 'at or below' national averages by running NCOA more frequently." Please refer to witness Crum's response to POIR No. 3, Question 1 where he states, "However, NCOA processing, no matter how frequent, would not resolve the primary cause of return to sender mail—deficient addresses."

- (a) Do you agree that, *ceteris paribus*, the forwarding rate for a mailer will be lower if it runs its lists through the NCOA database more frequently? If you do not agree, please explain fully.
- (b) Do you agree that NCOA processing "would not resolve the primary cause of return to sender mail—deficient addresses"? If you do not agree, please explain fully.

ANSWER:

- a) Agreed, *ceteris paribus*.
- b) Agreed that NCOA processing would not improve deficient addresses.

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COS/NAA-T1-27. Please refer to witness Crum's response to POIR No. 3, Question 1 where he states, "I have also learned another fact about Capital One that supports witness Wilson's estimate that its forwarding rate is no more than average. When Capital One processes its address lists against NCOA, approximately 4 percent of its address are updated. This rate, called a match rate, is close to the average for all mailers that use NCOA. This match rate indicates that Capital One's address lists are about as current as other mailers who use NCOA." Please confirm that having a match rate that is consistent with that of other NCOA mailers suggests that Capital One's forwarding rate is similar to other mailers who use NCOA. If not confirmed, please explain your reasoning fully.

ANSWER:

Not confirmed. COS is continuously mailing solicitations to new persons with whom they have no relationship. Even for those lists used by COS for multiple mailings, there is a lag time between processing against NCOA and the mailings.

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COS/NAA-T1-28. Please refer to page 15 of your testimony, where you state, "It is clear, however, that (at least at the onset of the NSA) multiple notifications will still be necessary due to the frequency of mailings and the lag time between received the notification and incorporating the information into the mailing lists."

- (a) Please describe in detail all analysis that you have performed related to your assertion "that (at least at the onset of the NSA) multiple notifications will still be necessary." Please be as quantitative as possible.
- (b) Please provide your understanding of how frequently Capital One sends a First-Class Mail solicitation to the same postal customer.
- (c) Please provide your understanding of how long the lag time is between Capital One receiving the notification and incorporating it into its mailing lists.
- (d) At the onset of the NSA, how many notifications do you believe will be necessary? Please explain your reasoning fully.

ANSWER:

- a) My statement that multiple notifications will be needed is based on common sense, an understanding that COS mailings occur in real time, and that there are lags between the time the mailing occurs and the time COS lists are updated.
- b) In his response to POIR 2, question 7, witness Crum assumed 5.6 solicitations to each delivery point per year. Some postal customers will certainly receive more and some will receive less, and COS has not provided any information on this matter.
- c) Based on the terms of the proposed NSA, COS is required to update its mailing lists within 2 days of receiving the notification.

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However, multiple future mailings may already be in preparation when notifications from previous mailings are received.

- d) I cannot quantify the number of mailings necessary without more information on COS's mailing practices.

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COS/NAA-T1-29. Please refer to page 15 of your testimony where you state, "witness Crum has a valid point regarding a probable improvement in the repeat-forwarded rate" and where you further state, "Adjusting to remove the postage due mail costs reduces that cost figure, slightly, to approximately \$0.306."

- (a) Please provide your best estimate of the reduction in the repeat-forwarded rate that will result from the agreement and provide all underlying calculations.
- (b) Please confirm that \$0.306 is approximately 4.6 times as large as the \$0.066 cost that witness Crum calculated for eACS forwards. If not fully confirmed, please explain fully.

Assuming that \$0.306 is the cost difference between a mailpiece that is forwarded and a mailpiece that is normally delivered, please confirm that the "breakeven ratio" at which the avoided cost from eliminating forwards is equal to the incurred cost of providing eACS forwarding notifications is 4.6 eACS forwarding notifications per corrected address. If not confirmed, please explain fully and provide your best estimate of this breakeven ratio.

ANSWER:

- a) I do not have the data to quantify the reduction in the repeat-forwarded rate.
- b) Confirmed that $\$0.306/\0.066 equals approximately 4.6.

Not confirmed. This hypothetical does not include enough data to make an accurate and reliable judgment. For example, the actual costs of forwarding COS mail would be needed to estimate the breakeven ratio.

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COS/NAA-T1-30. Please refer to your response to COS/NAA-T1-1 where you state, "Confirmed. However, none of the USPS sensitivities included consideration of the amount of the waived fees." Please refer further to your response to COS/NAA-T1-6. Finally, please refer to USPS-T-3, Appendices A and B where witness Crum calculates the Test Year financial impacts of the NSA. Please also assume that Capital One does not currently pay for or receive electronic "returns" and, in the absence of the NSA, would not pay for or receive electronic "returns" during the period that the NSA would have been in effect.

- (a) Please provide modified versions of USPS-T-3, Appendices A and B that include consideration of the amount of the waived fees.
- (b) Please explain fully why waived fees should be included in the calculation of the Test Year financial impact of the NSA.
- (c) Please explain fully why including waived fees as well as the costs for electronic "returns" in the calculation of the Test Year financial impact of the NSA does not double count the Test Year impact of receiving no-fee electronic "returns."

ANSWER:

- a) Attached are two modified versions of USPS-T-3, Appendix B (Appendix A does not need to be modified). *T3_AttB Modified 1.96.xls* uses a COS solicitation mail forwarding rate of 1.96%, as assumed by the USPS, to calculate the amount of the waived fees and *T3_AttB Modified 15.3.xls* uses a forwarding rate of 15.3%. I would like to reiterate that the 15.3% rate is simply a possible rate, based on COS's high return rate for solicitation mail.
- b) The waived fees should be included because they are potential lost revenue.

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- c) The waived fees are lost revenue and they must be considered separately from the costs, just as witness Crum considered cost savings from electronic returns, revenue leakage, and additional contribution separately.

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COS/NAA-T1-31. Please refer to your response to COS/NAA-T1-2 where you state, "I have not examined the costing of every mail class and special service in Docket No. R2001-1 and thus cannot confirm."

- (a) Please list all mail classes for which you have analyzed Docket No. R2001-1 costing methods.
- (b) Please indicate whether or not FY 2000 IOCS data were used to distribute costs in Docket No. R2001-1 to each of the mail classes listed in your response to subpart (a) of this interrogatory.

ANSWER:

a) First-Class UAA mail and Standard Enhanced Carrier Route mail.

b) The USPS has recently stated that FY2000 IOCS data were used for First-Class UAA mail (see USPS Response to Oral Request of Chairman Omas at Tr. 2/342), although this is not apparent from Library Reference LR-J-69. Although I have not reviewed for purposes of this case the Standard ECR data from R2001-1, I would not be surprised if FY2000 IOCS data were used for Standard ECR in that case.

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COS/NAA-T1-32. Please refer to your response to COS/NAA-T1-5 where you state, "use of NCOA presumably should reduce the forwarding rate somewhat." Please provide your best estimate of the extent to which use of NCOA should reduce the forwarding rate, provide all underlying calculations, and describe your reasoning fully.

ANSWER:

Based on the testimony of witness Wilson, NCOA catches about 25% of possible changes of address (see transcript Volume 3 - Hearing Held on December 4, 2002, Testimony of Witnesses Bizzotto (USPS-T-1) and Wilson (USPS-T-4), page 639). Thus, use of NCOA might reduce COS's forwarding rate by up to 25%.

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COS/NAA-T1-33. Please refer to your response to COS/NAA-T1-7(a) where you state, "I advise [clients] on strategic matters during negotiations." Please assume that one of your clients asked for your advice on a negotiation and told you, "one of our largest customers is using a product on which we currently make \$100 million in profit. Over the last year, this client has started making significant use of one of our lower-profit products and is considering shifting entirely to the use of the lower-profit product. If they shift entirely from using our higher-profit product to the use of our lower-profit product, it will reduce our profitability by \$50 million. (Also, it's important to note that we can't legally stop this customer from moving to the use of this other product or increase our price for the lower-profit product.) During negotiations, the customer told us that it probably would not shift to the use of the lower-profit product if we give his company a discount of \$7 million on the higher-profit product. Based upon this, the customer proposed an agreement where we offer him a \$7 million discount on the higher-profit product. The customer further agreed that if his company does shift a percentage of their high-profit volume to the lower-profit product, we can reduce the discount more than proportionately. Finally, in exchange for receiving this discount, the customer agreed to change its operations in a way that we are certain will reduce our costs by more than \$10 million." Assuming that there is no opportunity to modify the deal, would you advise your client to accept it? If not, please explain your reasoning fully. In particular, explain why it would be good for your client to reject the deal and take the risk of reducing its profitability by \$50 million.

ANSWER:

I would advise my client to accept the deal posited in this hypothetical.

ATTACHMENT B, PAGE 1

Increased Contribution from New Mail Volume

$$\begin{aligned}\text{New Mail Volume Contribution} &= (\$.2910 \text{ (1)} - \$.1266 \text{ (2)} - \$.045 \text{ (3)}) * 15,458,969 \text{ (4)} \\ &= \quad \quad \quad \mathbf{\$1,846,000}\end{aligned}$$

- (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)).

ATTACHMENT B, PAGE 2

Address Change Service (ACS) Return Cost Savings

$$\begin{aligned}\text{Return Cost Savings} &= (\$.1359 \text{ (1)} - \$.1266 \text{ (2)}) * 1,408,000,000 \\ &= \$ \quad 13,094,000\end{aligned}$$

- (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:

$$\begin{aligned} \text{Discount Leakage} = & (1,275,000,000 - 1,225,000,001) * \$.03 + \\ & (1,325,000,000 - 1,275,000,001) * \$.035 + \\ & (1,375,000,000 - 1,325,000,001) * \$.040 + \\ & (1,408,000,000 - 1,375,000,001) * \$.045 \\ = & \boxed{\$ 6,735,000} \end{aligned}$$

Declining Block Discount Table

<u>First-Class Mail Presort Volume Range</u>			<u>Discount</u>
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)

ATTACHMENT B, PAGE 4

Address Change Service (ACS) Return Fee Leakage

Solicitation Fee Leakage = $\$.20$ (1) * 9.6% (2) * 85% (3) + 1.96% (4) * 95% (5) * $768,000,000$ (6)

\$15,394,000

- (1) Per piece fee for eACS (USPS-T-2, page 3)
- (2) COS solicitation mail return rate (COS-T-1, page 6)
- (3) eACS success rate (USPS-T-4, page 7)
- (4) USPS estimated COS solicitation mail forwarding rate (response to APWU/USPS-T-3-4)
- (5) Percent of forwards that are forwarding through CFS, thus generating an eACS notice (NAA-T-1, page 13)
- (6) Test year before rates forecasted COS First-Class solicitation mail volume (COS-T-1, page 5)

ATTACHMENT B, PAGE 5

Summary USPS Financial Impact of NSA

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

= (\$7,189,000)

ATTACHMENT B, PAGE 1

Increased Contribution from New Mail Volume

$$\begin{aligned}\text{New Mail Volume Contribution} &= (\$.2910 \text{ (1)} - \$.1266 \text{ (2)} - \$.045 \text{ (3)}) * 15,458,969 \text{ (4)} \\ &= \quad \quad \quad \mathbf{\$1,846,000}\end{aligned}$$

- (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)).

ATTACHMENT B, PAGE 2

Address Change Service (ACS) Return Cost Savings

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

= \$ 13,094,000

- (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:

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

Declining Block Discount Table

<u>First-Class Mail Presort Volume Range</u>			<u>Discount</u>
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)

ATTACHMENT B, PAGE 4

Address Change Service (ACS) Return Fee Leakage

Solicitation Fee Leakage = $\$.20 (1) * (9.6\% (2) * 85\% (3) + 15.3\% (4) * 95\% (5)) * 768,000,000 (6)$

\$34,860,000

- (1) Per piece fee for eACS (USPS-T-2, page 3)
- (2) COS solicitation mail return rate (COS-T-1, page 6)
- (3) eACS success rate (USPS-T-4, page 7)
- (4) Possible COS solicitation mail forwarding rate (NAA-T-1, page 12)
- (5) Percent of forwards that are forwarding through CFS, thus generating an eACS notice (NAA-T-1, page 13)
- (6) Test year before rates forecasted COS First-Class solicitation mail volume (COS-T-1, page 5)

ATTACHMENT B, PAGE 5

Summary USPS Financial Impact of NSA

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

= (\$26,655,000)

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
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COS/NAA-T1-34. Please refer to your response to COS/NAA-T1-21 and further to lines 5-14 on Tr. 3/639 where witness Wilson states, "I can share with you some historical data about NCOA match rates over the 15 or 16 years of its life cycle. It typically corrects a 4 percent match rate...When that is contrasted with what the Bureau of the Census reports as the typical move rate of American public at 17 percent, I think it indicates that NCOA is capable on average of correcting 4 percent of what would be a 17 percent population, or roughly 25 percent of the potential change of address." Finally, please refer to third page of USPS witness Crum's response to POIR No. 3, Question 1 where he states, "Capital One processes its lists through the National Change of Address database (NCOA) every 30 days for customer mail and 60 days for solicitation mail. This occurs far more frequently than most mailers who process lists every 180 days, the minimum specified by postal regulation."

- (a) Please confirm that the above quoted citation from Tr. 3/639 is the source of your statement that "75% will not be caught by NCOA." If not confirmed, please provide the appropriate citation.
- (b) If Capital One sends a First-Class solicitation to an address that was not "caught by NCOA", will that piece be forwarded, returned, or could it be either? Please explain your response fully.
- (c) Please confirm that the 17 percent move rate cited by witness Wilson is an annual rate. If not confirmed, please explain your response fully.
- (d) Please confirm that if the annual move rate is 17 percent, the move rate over a 180 day period is approximately 8.5 percent. If not confirmed, please explain fully.
- (e) Please confirm that processing lists against NCOA every 180 days is the minimum specified by postal regulation. If not confirmed, please explain fully.

Please confirm that at least one mailer, Capital One, processes its lists against NCOA more frequently than every 180 days. If not confirmed, please explain fully.

ANSWER:

- a) Confirmed.

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- b) Either. In fact, given the parameters of your question, it could go to the intended recipient because correct addresses are not "caught" by NCOA. Nowhere in my testimony do I state that every piece of COS solicitation mail is either returned or forwarded.
- c) This is my assumption.
- d) Not confirmed: $180/365 * 0.17 = 0.0838$ or 8.4%.
- e) I am not an expert in postal regulations and thus cannot confirm.

Confirmed that Witness Crum's response to POIR No. 3, Question 1 is, "Capital One processes its lists through the National Change of Address database (NCOA) every 30 days for customer mail and 60 days for solicitation mail."

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COS/NAA-T1-36. Please refer to your response to COS/NAA-T1-27 where you state, "Not confirmed. COS is continuously mailing solicitations to new persons with whom they have no relationship. Even for those lists used by COS for multiple mailings, there is a lag time between processing against NCOA and the mailings."

(a) Please explain fully why this explanation causes you not to confirm in your response to COS/NAA-T1-27.

(b) Is there also "a lag time between processing against NCOA and the mailings" for other mailers or is Capital One the only mailer for which there is "a lag time between processing against NCOA and the mailings"? Please explain your response fully.

ANSWER:

a) COS/NAA-T1-27 states:

Please confirm that having a match rate that is consistent with that of other NCOA mailers suggests that Capital One's forwarding rate is similar to other mailers who use NCOA.

The explanation I gave in my reply listed additional points I considered to reach my conclusion that COS likely has a higher forwarding rate than other mailers.

b) Yes, it is likely that other mailers experience a lag between NCOA processing and mailings.

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COS/NAA-T1-37. Please refer to your response to COS/NAA-T1-29 where you state, "Not confirmed. This hypothetical does not include enough data to make an accurate and reliable judgment. For example, the actual costs of forwarding COS mail would be needed to estimate the breakeven ratio." Please assume that "the actual costs of forwarding COS mail" is \$0.306 per forwarded piece and that the actual costs of providing eACS forwarding notifications to COS is \$0.066 per notification. Under these assumptions, please confirm that the breakeven ratio is approximately 4.6. If not confirmed, please provide your best estimate of the breakeven ratio. If you need to make additional assumptions to estimate the breakeven ratio, please make the necessary assumptions and list them in your response.

ANSWER:

Confirmed, given the stated assumptions.

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COS/NAA-T1-38. Please refer to your response to COS/NAA-T1-28(a) where you discuss how many "notifications will be needed" to incorporate forwarding information into mailing lists. Please summarize all analyses that you have performed regarding the extent to which eACS forwarding notifications will reduce the number of repeat forwards sent by Capital One.

ANSWER:

As I stated in my response to COS/NAA-T1-28(a),

My statement that multiple notifications will be needed is based on common sense, an understanding that COS mailings occur in real time, and that there are lags between the time the mailing occurs and the time COS lists are updated.

I have not performed, and I cannot perform, any quantitative analyses without more information. For example, I would need to know the actual number of COS repeat forwards and the actual time it takes to prepare a COS mailing (which would aid in estimating the lag time between COS receiving the eACS notice, updating its mailing lists, and the updated mailing lists being incorporated into a mailing).

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COS/NAA-T1-39. Please refer to your response to COS/NAA-T1-30(b) where you state, "The waived fees should be included because they are potential lost revenue." Please assume that Capital One will, under no circumstances, pay for electronic "returns" or for eACS forwarding notifications in the Test Year. Under this assumption, please confirm that "waiving fees" as part of the NSA will not result in a reduction in the Postal Service's actual Test Year revenues. If not confirmed, please explain fully.

ANSWER:

Confirmed, given the assumption that COS will "under no circumstances, pay for electronic returns or for eACS forwarding notifications in the Test Year," which makes the question a tautology. But if the Postal Service nonetheless provides electronic returns or eACS forwarding notifications without a fee, it will receive less revenue than it would if it collected the fee.

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USPS/NAA-T1-1. Please refer to page 3, line 12 of your testimony where you claim that the Postal Service "will experience" a loss of revenue "from the discounts it is granting COS." Please confirm that if Capital One sends fewer than 1.225 billion PERMIT-identified First-Class Mail pieces, it will in fact receive no discounts at all.

ANSWER:

Not confirmed; the proposed NSA lists a second set of discounts if COS's volume falls below 1.225 billion pieces in the first year of the NSA (see proposed NSA, pp 4-5).

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USPS/NAA-T1-2. Please reconcile your claims of "no evidence" of the mail mix of Capital One's mail as compared to the FCM average mix on page 8, lines 3-4 of your testimony, with witness Crum's response to NAA/USPS-T3-16 and Attachment A, Page 1 to testimony of witness Crum, USPS-T-3.

ANSWER:

The two distributions do not correspond. First, Attachment A, page 1 of witness Crum's testimony deals with total COS FCM mail while witness Crum's response to NAA/USPS-T3-16 contains the distribution for only UAA First-Class Mail. Second, the two distributions have different levels of detail regarding the levels of subclasses and shapes described: Attachment A breaks down COS mail by shape and level of presort; witness Crum's response to NAA/USPS-T3-16 groups letters and cards together without differentiating presorted letters.

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USPS/NAA-T1-3. Please refer to page 9, lines 18-20 of your testimony, where you discuss the reduction of the costs of physical returns under PARS because the mailpiece will be caught and identified at a much earlier stage.

- a) Please confirm that in this part of your testimony you are referring to the fact that PARS will be able to intercept certain pieces at the origin processing plant and before it reaches the delivery unit. If you cannot confirm, please explain.
- b) Please confirm that the only mail that PARS will intercept before it reaches the delivery unit is mail bearing an address covered by a change of address order or to a post office box that has closed. If you cannot confirm, please explain.
- c) Please confirm that the only mail that should be physically returned that PARS would intercept before the delivery unit is mail where a forwarding order has expired or a post office box has closed. If you cannot confirm please explain.
- d) Please confirm that PARS will intercept mail has been sorted to the AADC, 3-Digit, or 5-Digit only at the destinating processing facility.
- e) Please refer to Attachment A, p. 1 to the testimony of witness Crum, USPS-T-3. Please confirm that in FY2001, almost 1 billion pieces were sorted to the AADC, 3-Digit, or 5-Digit.
- f) Please assume that Capital One's mail mix reflected in Attachment A, p. 1 remains the same after PARS is implemented. Please confirm that at best, only a very small part of Capital One's mail will be intercepted at the origin facility.

ANSWER:

- a) Not confirmed. I am referring to the fact that PARS will be able to intercept certain pieces prior to where they are intercepted in the current process, not solely at the origin processing plant.
- b) This is my understanding.
- c) This is my understanding.

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- d) This is my understanding.
- e) Confirmed.
- f) Confirmed, given the assumption.

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USPS/NAA-T1-4. Please assume the following:

- Mailings A, B and C have the same volume and mail mix.
- All mailings start with the same address list and that the list contains addresses that match the change of address order on file with the Postal Service.
- Mailings A, B, and C are identical in all respects except that:
 - ✓ The list used for Mailing A was run through NCOA 60 days before the mailing. The list used for Mailing B was run through NCOA 180 days before mailing.
 - ✓ The list for Mailing C was not run through NCOA or FastForward. Instead the mail pieces use an address correction service endorsement.
- Assume that each of the mailings is run through PARS.
 - a) Please confirm that PARS will intercept more pieces of Mailing C than Mailing B. If not please explain.
 - b) Please confirm that PARS will intercept more pieces of Mailing B than Mailing A. If not, please explain.

ANSWER:

- a) Confirmed.
- b) Not confirmed. If all matching change of addresses are in NCOA 180 days before mailing, PARS will intercept the same number of pieces for Mailings A and B.

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USPS/NAA-T1-5. While the Postal Service has stated that Capital One's forwarding rate is unknown, please reconcile your comments that there is "no evidence" as to its forwarding rate with witness Crum's comments in POIR 3 regarding its match rate and witness Wilson's comments in his response to APWU-T2-8 regarding its address management practices. Is it your opinion that unless you know a given piece of information with certainty that there is "no evidence" of its existence? Please explain.

ANSWER:

On page 11, my full statement is that "there is no evidence as to COS's actual forwarding rate" (emphasis added). Both witnesses Crum and Wilson make assumptions about COS's forwarding rate, based on the average forwarding rate for all FCM, but neither the USPS nor COS have offered evidence of, and to my knowledge has performed no study to determine, the actual forwarding rate of COS First-Class Mail.

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USPS/NAA-T1-6. Please refer to your testimony on page 10 at lines 1-10. Please confirm that PARS will likely reduce the cost of providing ACS notices.

ANSWER:

It is possible that PARS will reduce the cost of providing some ACS notices. It is likely it will reduce the total USPS cost of returns and forwards.

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USPS/NAA-T1-7. Please confirm that the Capital One NSA reflects the business judgment of the United States Postal Service.

ANSWER:

I assume that it does.

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THE UNITED STATES POSTAL SERVICE**

USPS/NAA-T1-9. Please confirm that it is possible that the Postal Service overestimated the costs of providing ACS notice for Capital One mail that would otherwise be returned. If you do not confirm, please explain fully.

ANSWER:

Confirmed.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
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THE UNITED STATES POSTAL SERVICE**

USPS/NAA-T1-10. Please refer to your testimony at page 6, line 8, where you state that other mailers have better address hygiene. Please confirm that a key component of address hygiene is that a mailer's list reflects the most current Change of Address information available. If you cannot confirm, please explain fully.

ANSWER:

Confirmed that current Change of Address information is an important component of address hygiene.

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THE UNITED STATES POSTAL SERVICE**

USPS/NAA-T1-11. Please confirm that a mailer who runs NCOA every 60 days will have more current Change of Address information than one who runs NCOA every 180 days.

ANSWER:

Logic would indicate that to be true.

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THE UNITED STATES POSTAL SERVICE**

USPS/NAA-T1-12. Please refer to page 11 of your testimony, footnote 8 and the accompanying text. Please provide a cite to USPS-LR-J-58 where the cost of returns is provided.

ANSWER:

I assume the reference about which you are inquiring should be page 8, footnote 11 of my testimony. USPS-LR-J-58 contains costs of processing and delivering mail. I have extrapolated from the higher processing costs of non-letter mail that it costs more to return these pieces than presorted letters.

**ANSWERS OF NEWSPAPER ASSOCIATION OF AMERICA
WITNESS CHRISTOPHER D. KENT TO INTERROGATORIES OF
THE UNITED STATES POSTAL SERVICE**

USPS/NAA-T1-13. Please confirm that the cost savings of the NSA relate solely to solicitation mail.

ANSWER:

Confirmed.

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THE UNITED STATES POSTAL SERVICE**

USPS/NAA-T1-14. Please refer to your Table 1 on page 10 of your testimony. Please confirm that the figures in Table 1 are based on the assumptions that PARS is implemented on schedule, that it has been fully deployed throughout the country, and that all projected cost savings have been realized. If you do not confirm, please explain fully.

ANSWER:

Not confirmed. The figures in Table 1 are based on the assumption that COS physical returns costs are, for whatever reasons, less than the FCM average physical returns costs.

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USPS/NAA-T1-15. Please refer to your Table 1 on page 10 of your testimony. Please complete the following table to take into account reductions in the electronic "return" cost of 33.2 cents provided in USPS-LR-1/MC2002-2, page 2, in the same increments as the physical return costs. Please note that the physical returns cost at differences of -10% and -35% have been revised to correct errors in your original table.

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332	\$13,094,000	\$8,205,000
-10%	\$0.482	\$0.299		
-24%	\$0.407	\$0.252		
-35%	\$0.348	\$0.216		

ANSWER:

Please note that although I have accepted the changes at 10% and 35%, the physical returns costs in my original table were correct when rounding the percentages to whole numbers.

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332	\$13,094,000	\$8,205,000
-10%	\$0.482	\$0.299	\$11,827,200	\$6,938,200
-24%	\$0.407	\$0.252	\$9,996,800	\$5,107,800
-35%	\$0.348	\$0.216	\$8,588,800	\$3,699,800

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USPS/NAA-T1-16.

- (a) Please confirm that your Table 1 assumes an address change service success rate of 85 percent.
- (b) Please complete the following table, assuming that the address change service success rate is 87 percent.

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332		
-10%	\$0.482	\$0.299		
-24%	\$0.407	\$0.252		
-35%	\$0.348	\$0.216		

- (c) Please complete the following table, assuming that the address change service success rate is 90 percent.

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332		
-10%	\$0.482	\$0.299		
-24%	\$0.407	\$0.252		
-35%	\$0.348	\$0.216		

- (d) Please complete the following table, assuming that the address change service success rate is 93 percent.

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332		
-10%	\$0.482	\$0.299		

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-24%	\$0.407	\$0.252		
-35%	\$0.348	\$0.216		

ANSWER:

a) Confirmed.

b) **87% Address Change Service Success Rate**

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332	\$13,376,000	\$8,487,000
-10%	\$0.482	\$0.299	\$12,108,800	\$7,219,800
-24%	\$0.407	\$0.252	\$10,137,600	\$5,248,600
-35%	\$0.348	\$0.216	\$8,729,600	\$3,840,600

c) **90% Address Change Service Success Rate**

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332	\$13,798,400	\$8,909,400
-10%	\$0.482	\$0.299	\$12,531,200	\$7,642,200
-24%	\$0.407	\$0.252	\$10,560,000	\$5,671,000
-35%	\$0.348	\$0.216	9,011,200	\$4,122,200

d) **93% Address Change Service Success Rate**

Difference from USPS Estimate	Physical Returns Cost	Electronic "Return" Cost	Return Cost Savings for FY2003	Total Contribution as a Result of the NSA
0%	\$0.535	\$0.332	\$14,220,800	\$9,331,800
-10%	\$0.482	\$0.299	\$12,953,600	\$8,064,600
-24%	\$0.407	\$0.252	\$10,841,600	\$5,952,600
-35%	\$0.348	\$0.216	\$9,433,600	\$4,544,600

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USPS/NAA-T1-17

- (a) Please provide the percentage of mail that is returned locally, *i.e.*, the delivery address and return address are processed through the same plant.
- (b) Please confirm that returning mail locally is less expensive than returning mail where the delivery address and the return address are processed through different plants *i.e.*, the origin and destinating plants are not the same.

ANSWER:

- (a) I have not performed this analysis.
- (b) I believe this is likely to be true, *ceteris paribus*..

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USPS/NAA-T1-18. Please refer to your testimony at page 12, line 5, where you state that NCOA may reduce the forwarding rate somewhat.

- (a) Please confirm that a mailer who uses address lists that have been run through NCOA every 180 days is likely to have a lower forwarding rate than a mailer who uses the same lists that have not run through NCOA or Fast Forward.
- (b) Please confirm that a mailer who uses address lists that has been run through NCOA every 60 days is likely to have a lower forwarding rate than a mailer who uses the same lists but runs it through NCOA every 180 days.
- (c) Please confirm that the average First-Class mailer does not use NCOA.
- (d) Please confirm that the relative changes in forwarding rate as discussed in parts (a) and (b) of this question are not correlated to the return rate.

ANSWER:

- a) – b) Confirmed.
- c) I cannot confirm because I do not know the definition of an "average" First-Class mailer.
- d) Confirmed that use of NCOA more or less frequently should not have an effect on a mailer's return rate, *ceteris paribus*.

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USPS/NAA-T1-19. Please refer to your testimony on the forwarding rate, pages 11-12.

- (a) Please confirm that your estimate assumes that Capital One has a higher than average number of addresses with forwarding orders in effect.
- (b) Please confirm that Capital One has repeat forwards, i.e. that it currently mails multiple times to an address with a forwarding order in effect, thus requiring the Postal Service to forward the mail from that address repeatedly. If you do not confirm, please explain.
- (c) At Tr. 2/184, witness Jean testified that Capital One will update within two days of receiving a corrected address. Please confirm that by receiving an ACS notice of the forwarded address, the number of Capital One's repeat forwards will likely decline. If you cannot confirm, please explain.

ANSWER:

- a) Not confirmed. The lag time between an address being updated and when it is incorporated into a mailing should also be considered.
- b) I cannot confirm because COS has not provided this information, but I believe it is likely to be true.
- c) Confirmed.

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USPS/NAA-T1-20. Please describe your personal experience with the following. For each please describe the tasks you saw performed and the location and years in which you saw them performed.

- (a) Observation of a CFS Unit.
- (b) Observation of a carrier processing UAA mail at a delivery unit.
- (c) Observation of a nixie clerk processing UAA mail at a delivery unit.
- (d) Observation of a mail processing plant handling return to sender mail.

ANSWER:

- a) – c) None.
- d) Unknown. I visited the USPS Merrifield, VA and Phoenix, AZ mail processing plants during the early-to-mid-1990s. During those visits I likely saw mail being processed for return to sender, but it was not identified as such.

1 CHAIRMAN OMAS: Is there any additional
2 cross-examination for Witness Kent?

3 (No response.)

4 CHAIRMAN OMAS: This brings us to oral
5 cross-examination. Two parties have requested oral
6 cross-examination, Capital One Services, Inc. and the
7 United States Postal Service.

8 Does anyone other than those participants
9 wish to cross-examine?

10 (No response.)

11 CHAIRMAN OMAS: Mr. May, would you please
12 begin?

13 MR. MAY: Thank you, Mr. Chairman.

14 CROSS-EXAMINATION

15 BY MR. MAY:

16 Q Good morning, Mr. Kent.

17 A Good morning.

18 Q If you will turn to page 10 of your
19 testimony? On page 10 you have a Table 1 called
20 Physical Return Costs. In that table you purport to
21 show the total contribution from the NSA that would
22 result if the cost of physical returns is less than
23 the Postal Service estimated.

24 I want to ask you about what you did to
25 prepare Table 1. Would you agree that you have not

1 developed any estimates of the unit cost of Capital
2 One's physical returns?

3 A Yes.

4 Q So this table is just for illustrative
5 purposes? It isn't based on any actual cost estimates
6 that you've developed, is it?

7 A It's based upon the Postal Service's filing.

8 Q But your estimates are Differences From USPS
9 Estimate, 10 percent, 24 percent. Those differences
10 are simply for purposes of illustration. You have not
11 developed any actual costs of Capital One's returns,
12 so you have not determined any cost numbers that show
13 that percentage difference, have you?

14 A I think the table speaks for itself.

15 Q Mr. Kent, previously when I asked you
16 whether or not you had developed any estimates of the
17 unit cost of Capital One's returns you said no.

18 A That's correct.

19 Q I'm asking you then when you say Differences
20 From USPS Estimate, 10 percent, 24 percent, 35
21 percent, you don't have any actual Capital One return
22 costs that deviate by 10 percent, 24 percent or 35
23 percent, do you?

24 A There's nowhere in the record anything that
25 shows that the Capital One --

1 Q And you don't have --

2 A Pardon me, sir. I wasn't finished with my
3 answer.

4 Q All right. Go right ahead.

5 A I said there isn't anything in the record
6 that indicates any deviation from the system average.

7 Q Can you answer the question?

8 A I already did.

9 Q Well, let me ask it again. Are these
10 percentages merely for illustrative purposes, or do
11 you have any actual numbers to back up these
12 percentages?

13 A Well, I didn't start with the percentages,
14 so I have trouble telling you that they're for
15 illustrative purposes.

16 Q What purpose are they for?

17 A Well, they show at what point you reach
18 certain thresholds of contribution.

19 Q But you have no evidence yourself and
20 there's no evidence in the record that in fact Capital
21 One's costs do deviate by those percentages, do you?

22 A That's correct.

23 Q This could be a long morning, Mr. Kent.

24 A I'm here all day, sir.

25 Q Now, the cost savings from the NSA relate to

1 the unit cost difference between physical returns and
2 electronic returns. Is that not correct?

3 A Would you state that again, please?

4 Q Well, to the extent there are any savings
5 from this NSA they relate to what the unit cost
6 difference is between the cost of physically
7 returning, making a physical return, and making an
8 electronic return. The difference between those costs
9 would be the putative cost savings. Is that correct?

10 A Well, on page 2 of my testimony I lay out
11 what the total contribution calculation is, and they
12 do calculate as part of that contribution a return
13 cost savings.

14 Q Let me ask you again. Are the cost savings
15 the differences between what it cost the Postal
16 Service to physically return a piece of Capital One
17 mail versus the cost to the Postal Service to send an
18 electronic return?

19 A Yes.

20 Q Now back to Table 1. It does demonstrate
21 the effect, as I think you've agreed, of potential
22 overstatements of the cost of the physical returns,
23 depending upon if it were 10, 24, 35 percent, but in
24 that demonstration when you get to your final column
25 what the total contribution would be, that number

1 assumes, does it not, that the Postal Service has
2 correctly estimated the cost of electronic returns,
3 does it not?

4 A All of the figures that go into the
5 calculation of that contribution are based upon the
6 Postal Service's assumptions. Right.

7 Q Well, no, they're not because isn't it the
8 case the Postal Service assumed that Capital One's
9 physical returns cost a certain amount?

10 You are here positing no, that they're
11 wrong; that in fact their costs are 10 percent less
12 than they say, 24 percent less than they say or 35
13 percent less than the Postal Service says, so those
14 aren't based on the Postal Service's assumptions, are
15 they?

16 A I'm demonstrating the sensitivity of the
17 numbers to certain changes in cost change. That's
18 correct. If that's what your question is, yes.

19 Q What I'm asking you is do you not then have
20 to, in order to get the net contribution, which is
21 what your final column is, is it not, the net
22 contribution?

23 A Total contribution.

24 Q Do you not in that exercise have to subtract
25 from the contribution what it will cost the Postal

1 Service to send an electronic return?

2 A Yes.

3 Q Have you not assumed in this table that the
4 Postal Service's estimates of a cost of electronic
5 return are correct?

6 A I have demonstrated in this table what the
7 changes would be starting in the first column, which
8 is the first row, which is the Postal Service's
9 numbers.

10 Q I'll ask you again. Have you not assumed
11 that the Postal Service is correct when it says how
12 much it cost to do an electronic return? Haven't you
13 assumed the Postal Service is correct about that?

14 A Yes. For the purposes of illustrating in
15 this table, that's what that does.

16 Q I want to ask you about the unit cost of
17 physical returns. Let me refer you to the first full
18 paragraph on page 4, and I will hand you this, of the
19 response that the Postal Service made to Chairman
20 Omas' request that he made at the previous hearing.
21 I'll hand you a copy of that response.

22 I'd like to particularly direct your
23 attention to page 4 of that response in a section of
24 the response that deals with returns. This, just to
25 refresh you, was a request the Chairman made to the

1 Postal Service to provide information about forwarding
2 costs of returns.

3 On page 4, the Postal Service says, if you
4 will look at it, and I will quote. It says, "Also
5 when the Postnet bar code..." -- do you see where I'm
6 reading?

7 A The second full sentence in the first full
8 paragraph?

9 Q Yes.

10 A Yes. I'm with you.

11 Q Okay. "Also, when the Postnet bar code for
12 the original delivery address is contained in the
13 address block the Postal Service cannot use the LMLM
14 to cover the Postnet. In that case, the Postal
15 Service may use a grease pencil to manually block out
16 the original Postnet.

17 " This is not particularly effective since
18 part of the delivery address may be blocked. The
19 original Postnet code may still be visible, or there
20 may still be a duplicate Postnet imprinted on the
21 piece that needs to be run on the LMLM."

22 Now, I'm going to show you a typical Capital
23 One solicitation mailing. The only thing that's
24 significant about it is it has a Postnet bar code in
25 the address block, which is the same thing that any

1 bar coded letter has.

2 I'm going to show this. Are you familiar
3 with the Postnet bar code at all?

4 A No.

5 Q You don't know what a bar code is?

6 A I know what a bar code is.

7 Q Let me show you this and see if you can
8 identify that this is a bar code. Do you see a bar
9 code in the address block there under the glycine
10 portion?

11 A Yes. I assume you're referring to this
12 section right here?

13 Q Yes. For the record, the witness was
14 pointing to a bar code that was underneath the alpha-
15 numeric address.

16 You recall that the Postal Service response
17 to Chairman Omas was that when that occurs that the
18 Postal Service may have to block that bar code out by
19 applying a grease pencil to block it out. Do you
20 recall that?

21 A I recall you just reading that.

22 Q Well, that is indeed what the answer to the
23 Chairman was.

24 I'm going to give you a grease pencil -- I
25 had a hard time finding one, by the way -- and ask you

1 to, if you will, block out the bar code on that
2 envelope.

3 A You want me to line this out, correct?

4 Q Yes. I want you to do what the Postal
5 Service told the Chairman the Postal Service might
6 have to do when there's a bar code in the address
7 block of a bar coded letter when they return it. They
8 say they have to block out the --

9 A Okay.

10 Q Have you been able to do that?

11 A I appear to have been able to have blocked
12 out the bar code with your grease pencil.

13 Q Now, would you agree that using a grease
14 pencil to manually block out the original bar code
15 might increase the cost of returning bar coded letters
16 at least as compared to those that don't have a bar
17 code on them?

18 A I don't know. I don't know what the cost is
19 for either one of them.

20 Q Let me ask you the question again. Would
21 the fact that you or the postal worker had to take a
22 grease pencil and take the time to mark out the bar
23 code, would that fact cause that cost to be greater
24 than the particular function for a non bar coded
25 letter where you don't have to do that?

1 A You've already asked me that question, and
2 I've given you the answer that I don't know.

3 Q Well, you don't have to do it to a non bar
4 coded letter, do you?

5 A You don't have to do it?

6 Q You don't have to use a grease pencil to
7 mark out a bar code on a non bar coded letter because
8 it doesn't exist, does it?

9 A If you're asking me if there's not a bar
10 code do you have to mark out the bar code, the answer
11 is obviously not.

12 Q That's right. So at least there is that one
13 cost. There is that one function that you have to
14 perform for a bar coded letter that you don't have to
15 perform for a non bar coded letter, correct?

16 A Without saying, yes.

17 Q And does doing that cost money?

18 A I don't know. I assume it does.

19 Q I didn't ask you how much. I asked you does
20 it cost money. Does it cost time to do it?

21 A It probably costs time. That I will
22 concede.

23 Q And you are or are not familiar with the
24 fact that postal workers are paid by the hour?

25 A I am aware of that fact.

1 Q So the time that they take is what causes
2 postal labor costs, is it not?

3 A The time that they're paid is what causes
4 postal labor costs.

5 Q Presumably they're doing something for what
6 they're being paid.

7 A Is that a question, or was that a statement?

8 Q I suppose it would be proper to require you
9 not to answer that.

10 Now, I take it that when you were asked to
11 compare the cost of bar coded and non bar coded
12 letters and when we asked you about the differences
13 between them you didn't mention the fact that you
14 might have to mark out a bar code because you weren't
15 aware of it. Is that right?

16 A I have no idea what you're speaking about.
17 When I was asked to do what I was unaware of what?

18 Q When you were asked and you answered a
19 response to the Capital One Question No. 11, you were
20 asked whether you believed the cost of returning a
21 presorted bar coded letter is different than the cost
22 of returning an identical letter that wasn't presorted
23 or bar coded. Your response was that presorted bar
24 coded letters are only a part of total first class
25 mail volume.

1 When you made that answer, I take it you did
2 not have in mind that you might have to mark out a bar
3 code; that that might be one difference in the cost of
4 the two letters.

5 A I confess that when I answered that
6 interrogatory I had a great deal of difficulty and
7 counsel had to assist me because I don't understand
8 how you can have an identical letter that isn't bar
9 coded to one that is bar coded. It seems to me by
10 definition they're mutually exclusive, which is why I
11 answered the question the way I did.

12 Are you now telling me that you meant to ask
13 me about a grease pencil?

14 Q No. What I asked you about was what the
15 differences were between a bar coded letter that is
16 identical in all other respects to a non bar coded
17 letter.

18 A But that isn't the question that was asked
19 me in Interrogatory No. 11.

20 Q And you didn't understand that's what the
21 intention of the question was?

22 A As I stated earlier, that's exactly right.

23 Q Well, did you answer the question that you
24 thought was asked?

25 A I did.

1 Q And which question did you think I asked
2 you?

3 A I thought you were inquiring as to the
4 specifics of the costs of bar coded versus non bar
5 coded, and I said I can't tell you the difference
6 between the only cost I have is the average first
7 class mail cost.

8 Q But I asked you about letters, didn't I?

9 A Uh-huh.

10 Q Did you answer about letters?

11 A I don't have the cost for letters. I have
12 the average first class mail cost.

13 Q But that isn't your answer. You gave me an
14 answer talking about packages, parcel packages. You
15 were asked, whether it's identical or not in your
16 mind, but you were asked to compare a letter to a
17 letter, and you gave an answer that included packages,
18 did you not?

19 A Yes, I did. If you'd like me to read the
20 answer to you I'll be glad to.

21 Q No. It's right there. That's why I'm
22 referring to it.

23 Let me ask you this. Now that you perhaps
24 understand the question; that I'm asking you to
25 compare a bar coded letter to a non bar coded letter

1 that was the exception of bar codes is identical in
2 its physical configuration, do you have any view as to
3 the relative cost of returning one letter versus the
4 other letter?

5 A No.

6 Q Thank you.

7 A That's what you asked me 15 minutes ago.

8 Q Now, on pages 7 through 9 of your testimony
9 you discuss reasons you believe might explain why
10 physically returning Capital One's mail might be less
11 expensive than returning first class mail as a whole,
12 do you not?

13 A At pages 7 through 9 I present several
14 reasons why I think that the costs might be
15 overstated.

16 Q Right. You haven't quantified --

17 A Cost savings. I'm sorry, sir.

18 Q Yes. You haven't quantified the impact of
19 any of those reasons, have you?

20 A No, sir. That was not my task.

21 Q And you also haven't compared the reduction
22 of cost for reasons listed on those pages with
23 additional costs that might result from having to do
24 such things as mark out a bar code on a bar coded
25 letter. You haven't included that in any of your

1 comparisons, have you?

2 A No. That wasn't the purpose of my
3 testimony.

4 Q Would you also agree that Capital One's
5 mailings are likely to be national mailings?

6 A I have no idea. I have no idea of what
7 Capital One's business model is.

8 Q Well, let me ask you to accept as an
9 assumption, accept for the purposes of these
10 questions, that Capital One's mailings are
11 predominantly national mailings.

12 MR. BAKER: Could the counsel define what he
13 means by a national mailing?

14 MR. MAY: Versus a local mailing. For
15 purposes of this question, a local mailing would be a
16 mailing that's deposited in say the mailing area here
17 in the Washington area and delivered in the Washington
18 area. A national mailing would be one that's
19 deposited here and delivered outside of the Washington
20 area.

21 BY MR. MAY:

22 Q Does the witness understand the --

23 A I understand your definitions. Yes, sir.

24 Q Now I'm going to ask you to assume that
25 Capital One's mailings are predominantly national, if

1 you will. Would you agree that the cost of returning
2 mail across the country is higher than returning it
3 locally?

4 A I don't know.

5 Q You don't know? I mean, if a piece of mail
6 which is sent from Washington to Alaska and it can't
7 be delivered in Alaska and that piece of mail has to
8 come back from Alaska to Washington, you don't know
9 whether that would be more costly than returning a
10 piece of mail that's deposited in Washington, tried to
11 be delivered in Washington, cannot be delivered here
12 and is returned to Washington? You have no idea
13 whether those costs, one might be more costly than
14 another?

15 A I don't. I assume that there might be an
16 incremental transportation cost to get from Alaska,
17 but whether you pay more in local service or, you
18 know, domestic national service I couldn't tell you.

19 Q What is the level of your knowledge about
20 the constituent parts of the cost for returning a
21 letter?

22 A The constituent parts of the cost?

23 Q Yes.

24 A Help me, sir.

25 Q Well, the different postal functions,

1 handling, those various procedures that the Postal
2 Service has to perform on a piece of mail to return
3 it. What is the level of your understanding of what
4 those various functions are?

5 A It is largely based upon what I've been able
6 to read in this case. I am not a postal mail
7 processing or delivery expert. I am an expert in
8 contracting and negotiated service agreements,
9 however.

10 Q Then what are we to make of your pages 7 to
11 9 where you list a bunch of reasons why you think that
12 Capital One's costs of return may have been overstated
13 by the Postal Service when, as you say, you're not an
14 expert on how mail is returned?

15 A Well, I state right up front three purposes
16 of my testimony, and I state that one of those
17 purposes is that I'm concerned that the use of average
18 cost may not be representative of Cap One.

19 I'm also concerned because there's nowhere
20 in the record by Cap One or by the Postal Service any
21 demonstration that they are representative of the
22 average first class mailer, so I'm simply pointing out
23 that there are a series of things that need to be
24 looked at before you should go ahead and make an
25 approval or the Commission should make an approval of

1 this proposed NSA.

2 Q Does that mean that in fact Capital One's
3 cost of return might be even higher than the Postal
4 Service said?

5 A I suppose that's possible.

6 Q Would you now turn your attention to the
7 Postal Service's Library Reference 1? You attached
8 that to your answer to Capital One's Question 10 to
9 you.

10 A I'm sorry. It was Capital One Services --

11 Q Question 10.

12 A Ten.

13 Q That would be for the purposes of the record
14 and the Commission if they look at your answer to
15 Capital One's Question 10 they will see attached the
16 library reference, USPS Library Reference 1, correct?

17 A Yes, sir.

18 Q Now directing your attention to that
19 attachment to your answer, would you agree that there
20 the Postal Service has listed specific types of costs
21 for physical returns -- carrier preparation, clerk
22 handling, CFS processing and mail stream process?

23 A Yes, sir. Those are the four items they
24 list.

25 Q Do you know what actually any of those

1 things are?

2 A I have a general understanding, I believe.

3 Q I don't want to embarrass you because I'm
4 going to ask you a question about it, and perhaps you
5 don't have sufficient understanding to be able to
6 answer the question. If not, just say so.

7 A I will.

8 Q Would you agree that having to return mail
9 across the country, all the way across the country,
10 might increase the mainstream processing portion of
11 the cost of physical return? That's Item 4 on this
12 table.

13 A The mail stream processing?

14 Q Mail stream processing.

15 A I don't know.

16 Q Now, I guess the carrier preparation would
17 probably be the same whether it's local or national,
18 or you don't know?

19 A I would think so.

20 Q And clerk handling?

21 A I would think so.

22 Q Those two items, carrier preparation and
23 clerk handling, if you roughly calculate that all the
24 way across to the end it says Weighted Cost. If you
25 add that together it's just a little under 19 cents

1 apiece for those two. Is that correct?

2 A That's correct.

3 Q But you don't know whether the mail stream
4 processing might be a significantly different item
5 between local and national? You just don't know
6 between a local and a national mailing?

7 A It would seem to me that in your Alaska
8 example if in fact by the time it left Alaska it was
9 directed back to I think in your hypothetical it was
10 here in the Washington area, you know, except for the
11 transportation costs in theory it wouldn't have to be
12 handled any more until it got back here.

13 I mean, it seems to me that implicit in your
14 question is the assumption that it gets handled
15 multiple times between Alaska and here, and I don't
16 know if that's true or not.

17 Q I say if you don't know, you don't know.
18 Let me ask you at least in the case of electronic
19 returns. Electronic returns presumably, according to
20 page 2 of this exhibit, have exactly the same costs
21 for carrier preparation and clerk mail handling, do
22 they not?

23 A Yes, they do.

24 Q As physical returns?

25 A Yes, they do.

1 Q However, they don't have any mail stream
2 processing costs, do they, according to this?

3 A Is that a question?

4 Q Yes. I'm just asking you. Isn't that
5 correct that they --

6 A Yes. That's true.

7 Q And presumably in the case of a national
8 mailing it wouldn't make any difference whether a
9 mailing was national or local. If it's going to be
10 electronically returned, there wouldn't be any
11 difference.

12 It doesn't make any difference whether you
13 send an electronic signal from anywhere. There are no
14 differences in the cost. Is that correct?

15 A According to this library reference, there's
16 no mail stream processing.

17 Q Now I'd like you to take a look at your
18 answer to Capital One's Question 12. In that question
19 you were asked if you had performed any analysis
20 regarding the percentage of first class mail returns
21 mail stream that is comprised of letters.

22 In other words, did you do an analysis to
23 find out what percentage of all first class returns
24 consisted of letters, bearing in mind that you had
25 said it was not appropriate to compare Capital One

1 mail, letter shaped Capital One mail, to the average
2 first class mail return costs because those average
3 costs contain flats and IPPs in addition to letters.
4 You said no, so you had not performed any analysis.

5 Let me ask you this. If it were the case
6 that only one-half of one percent of the first class
7 mail returns were parcels and IPPs, only one-half of
8 one percent, would you still argue that it is not
9 appropriate to compare Capital One's return cost with
10 the average first class return cost?

11 A I don't know what Capital One's return costs
12 are.

13 Q Well, we know that. Is it your contention
14 that you cannot use average first class mail costs
15 even if first class mail were all letters because you
16 actually need to know Capital One's costs?

17 A I think that is eminently clear that my
18 testimony is that in the case of this NSA you have to
19 know or you at least have to have made an effort to
20 identify what Capital One's return costs are, yes. To
21 answer your question, unequivocally yes.

22 Q And you have testified that it is not
23 appropriate to compare Capital One's costs to the
24 average first class mail stream because, among other
25 reasons, you say that the first class mail stream has

1 parcels in it, and Capital One does not. That you did
2 so state, correct?

3 A You're referring at that point to -- I'm not
4 sure you're accurately categorizing my testimony,
5 counselor.

6 Q Yes. You were asked if you had performed
7 any analysis regarding the percentage of first class
8 mail returns mail stream that is comprised of letters,
9 bearing in mind that you had already said that it was
10 not appropriate to compare Capital One's mail, which
11 was letter shaped, to the average first class mail
12 return cost which contained the cost for flats,
13 packages and IPPs, in addition to letters. This is
14 what you say on page 8 of your testimony.

15 A Point to me exactly where you're reading
16 from. I mean, I'll gladly read you the paragraph I'm
17 looking at. I don't believe you've accurately
18 categorized it.

19 Q Line 15 through 17. It says, "Given Capital
20 One's typical letter shaped mail, the average first
21 class mail returns cost, which contains the cost for
22 letters, flats, packages and IPPs, is not appropriate
23 to apply to COS mail."

24 A And I've given you an example as to why it
25 may not be.

1 Q I know. So I did not mischaracterize your
2 testimony when I said that you had said it was
3 inappropriate to compare them?

4 A I think it's inappropriate for the purposes
5 of this NSA without a demonstration that Cap One's
6 costs are representative of average first class mail
7 costs to use average first class mail costs. Yes.

8 Q But as a reason for that you have cited the
9 inclusion in first class mail of material other than
10 letters?

11 A One of the reasons.

12 Q As one of the reasons.

13 A That's correct.

14 Q What are the other reasons, by the way?

15 A Well, I think that there's been no
16 demonstration at all that Cap One is representative of
17 first class, and I think you've got to make a
18 demonstration that the representative of average first
19 class mail processing, clerk handling and everything
20 and identify their costs specifically if you want to
21 make a demonstration that this NSA should be accepted.
22 That's all I've said.

23 Q And how will you recommend that be done?

24 A It's not my job to have prepared this. I do
25 believe that, you know, it is important when you're

1 dealing with average costs and you want to make a
2 special deal for a particular customer to identify the
3 specific costs of that customer.

4 Q But you don't know how that would be done or
5 could be done?

6 A Well, I do it all the time for my clients so
7 the answer is yes, I know how I would do it. I don't
8 know how the Postal Service and Cap one would have
9 done it.

10 Q Well, certainly Cap One cannot do it, can
11 they?

12 A Certainly Cap One can't identify its own
13 costs, or certainly Cap One can't identify the Postal
14 Service's costs for processing?

15 Q That's what I say.

16 A Okay.

17 Q They can't identify what the Postal
18 Service's costs are.

19 So you would argue that well, the Postal
20 Service can because the Postal Service -- well, what
21 would you do if it was your client, if the Postal
22 Service was your client, and they ask you well, what
23 should we do to demonstrate that our cost of handling
24 Capital One's returns are typical of our average costs
25 of handling first class, all first class returns?

1 What should they do?

2 A I think they should make a demonstration
3 that they're representative of the average first class
4 mail process.

5 Q And what would that demonstration consist
6 of?

7 A I think you have to analyze specifically
8 what you do with Cap One's mail. That's the first
9 step.

10 I mean, basically when one does a costing
11 exercise you have unit costs, and you have service
12 units. Both of those variables need to be taken into
13 consideration when you make an adjustment to costs.
14 It's a standard regulatory costing approach.

15 Q Hasn't the Postal Service stated in this
16 case that in their view Capital One's returns are
17 handled in the same way that other first class mail
18 returns are handled?

19 A I'm not sure they've made that statement,
20 sir. Would you like to point me to where they make
21 that.

22 Q Well, indeed the record will reflect that,
23 but you're not aware whether they have or not, right?

24 A I don't think they've made any demonstration
25 of that.

1 Q I don't mean a demonstration. I'm talking
2 about a statement. I still don't know what you mean
3 by a demonstration.

4 Are you suggesting the Postal Service,
5 whenever it does a deal in the future, is going to
6 have to actually do a separate cost study of every
7 particular handling operation, every postal function
8 performed, for an individual mailer's mail so that
9 they can demonstrate that either that mailer's mail is
10 typical of that mail stream and, therefore, can use
11 the average costs that the Postal Service uses and
12 that this Commission uses to fix rates or they will
13 show that it's different, in which case those
14 different costs would become the basis for a deal. Is
15 that what you're saying?

16 A I apologize. I may have fallen off the bus
17 during that lengthy question.

18 Let me tell you what I am suggesting. In
19 the world of the private sector in which I deal, there
20 are lots and lots and lots of contracts and NSA type
21 deals constructed. I happen to be an expert in what
22 are known as network industries. Network industries
23 are those businesses that have expensive physical
24 infrastructures and run multiple products and services
25 across those infrastructures.

1 Because they are expensive physical
2 infrastructures they most often are what have been
3 considered natural monopolies because it doesn't make
4 sense to have multiple facilities providing multiple
5 services so, you know, in the world of railroads, for
6 example, which I do a lot of work in, they execute
7 contracts and NSAs all the time. They also have
8 standard costing procedures, regulatory costing
9 procedures. Unit costs are developed.

10 Before they enter into any kind of a
11 contract or a negotiated service agreement they
12 perform an evaluation of what the costs and benefits
13 are associated with that. They take into
14 consideration changes in technology that may occur
15 during the course of that. They then run
16 sensitivities after they've run costs for every year.

17 Now, if your question was should the Postal
18 Service do that in the future for every possible deal
19 the answer is I don't know, but it seems to me that
20 for the first one that they're doing, yes, they should
21 do that.

22 This is a precedential setting deal, and
23 they have not done the level of diligence that they
24 should have done and that would have been expected in
25 the private sector.

1 Q Do your clients do a separate cost study for
2 each company they do a deal with, I mean, where they
3 actually go in and keep tabs on every single thing
4 done about that particular customer's product or
5 whatever they're handling, whatever the deal is, or do
6 they use their standard cost?

7 Do they say well, normally it costs us X to
8 perform Function A plus this much to perform Function
9 B. We have to perform Functions A and B in order to
10 do this, so we're going to apply that standard cost to
11 this customer's Functions A and B. Is that what they
12 do?

13 A Well, you posited it as either/or,
14 counselor, and the answer is they do both because
15 there are lots of costs that are comprised and lots of
16 functions that are comprised in performing, for
17 example, a transportation service.

18 It may be that for the cost of ownership of
19 the right-of-way in a railroad situation or for the
20 return on depreciation they'll use a standard cost.
21 On the other hand, if we're examining -- just pick a
22 hypothetical -- a move of coal from the Powder River
23 Basin of Wyoming to a utility in Texas, all of the
24 important cost drivers get evaluated outside of the
25 average unit cost. Even the average unit cost for

1 unit train movements for coal, they get analyzed
2 specifically.

3 Q How do they do that?

4 A They hire me for one thing.

5 Q And what do you do?

6 A I go in, and I do a detailed analysis of
7 where they are likely to vary from the average and
8 then literally quantify how they do vary from the
9 average and incorporate changes in technology that are
10 likely to occur over a five year agreement, for
11 example, or a ten year agreement, for example.

12 Q And you don't believe the Postal Service has
13 that understanding about their customers' mail?

14 A I can only tell you that with regard to this
15 filed NSA they've made no demonstration that they have
16 that understanding of Capital One's costs.

17 Q But haven't they said that they are
18 satisfied that the operations they perform on Capital
19 One do not significantly deviate from the normal
20 operations they perform on returned mail?

21 A I think they have said that, and I think
22 that's why I'm sitting here before the Commission
23 because I have doubts as to whether that's the right
24 statement.

25 Q I'm just trying to find out what burden you

1 would set for the Postal Service. When it's doing
2 deals, you say that perhaps the only time they need to
3 do this is for their first one.

4 A No. I didn't say that. I said they really
5 should have done it for this one, and they didn't.
6 They didn't look at three years worth of costs, and
7 they didn't look at Cap One's costs.

8 Q Should they do it for the next deal?

9 A I'll have to take a look at the next one
10 when it gets filed and tell you.

11 Q What would be the difference?

12 A What would be the difference?

13 Q Yes.

14 A Posit me the next one, and maybe I can tell
15 you what the difference is. Do you want me to now
16 create a hypothetical scenario?

17 Q No. I'll create one for you.

18 A Fine.

19 Q In the next deal the Postal Service is going
20 to avoid the cost of Function X, and Function X has a
21 well established cost in the postal literature. It's
22 used by this Commission all the time in fixing rates.

23 Function X costs so much, and Function X has
24 to be performed on this kind of mail. The Commission
25 has historically charged Function X to the kind of

1 mail that gets Function X. In the next deal, Function
2 X will no longer be performed under the deal.

3 Now, do I take it that you're saying well,
4 the Postal Service will still have to go in and make
5 sure that the cost of performing Function X for the
6 person in the deal is the same as the average cost of
7 performing Function X? Is that what you're saying?

8 A Under your hypothetical, that's what I'm
9 saying.

10 Q So it isn't just Capital One's deal. It's
11 every deal like that in the future. You believe that
12 a special study has to be made of the mail
13 characteristics and the unique cost of that particular
14 customer they're doing the deal with?

15 A I didn't say that.

16 Q Well, when would they --

17 A This deal is predicated on the notion that
18 there are going to be cost savings. That is the
19 entire justification for this deal. If there's going
20 to be a cost savings, you'd best make a demonstration
21 that there's really going to be a cost savings and
22 that the costs you're using are accurate and
23 representative. That's what I'm saying.

24 Q Well, the Postal Service has said that it
25 costs X. You don't dispute that there will be a cost

1 savings here, do you? You're simply disputing the
2 amount of the cost savings as I understand it.

3 A You started our examination this morning on
4 Table 1 in which I posited the possibility that there
5 could actually be a loss. I also have a problem with
6 the fact that, you know, EACS is being waived
7 completely and that there's a revenue loss.

8 Q We can get to that latter, but if you'll
9 stick to the question I asked you, which is, again if
10 you'll listen, is there not in all events going to be
11 a cost savings from avoiding physical returns? Not
12 how much, but isn't there in all events going to be a
13 cost savings?

14 I didn't ask you whether it's going to end
15 up in a net profit for the Postal Service. I'm asking
16 you isn't it the case that there will be a net savings
17 from the avoidance of physical returns?

18 A I think it's a safe assumption, sir, that if
19 you're not performing a function that costs money you
20 probably are saving money.

21 Q So you're simply quarreling with the Postal
22 Service's contention that the amount of savings they
23 will make on avoiding this function is as much as they
24 say they will save?

25 A Again, is that a question or a statement?

1 Q It's a rhetorical question to which you may
2 agree or disagree.

3 A I disagree with it.

4 Q Would you explain why?

5 A I am quarreling with the fact that the
6 Postal Service has proffered a three year agreement
7 and has presented one year of costs. I am quarreling
8 with the fact that the Postal Service is using system
9 average or average first class mail costs and applying
10 it to Cap One, and I'm concerned that even the cost
11 savings that they posit may be overstated.

12 That's my concern. That's what my testimony
13 says.

14 MR. MAY: Mr. Chairman, if you could ask the
15 witness to confine his answers to the question I ask?
16 I did not ask the witness everything in the world that
17 he was quarreling about, which I feared you were going
18 to then leave the hearing room and discuss other
19 matters in your personal life where you had quarreled.

20 BY MR. MAY:

21 Q I asked you on this particular item your
22 quarrel was not with the fact that there would be a
23 cost avoided by avoiding physical returns, but rather
24 on that point your quarrel was that you thought the
25 Postal Service had overstated the amount that they

1 would save from avoiding physical returns. Isn't that
2 the case?

3 MR. BAKER: Mr. Chairman, I'm not sure if
4 that was addressed to the witness or to you.

5 MR. MAY: It's addressed to the witness.

6 THE WITNESS: Well, since you began with,
7 "Would you please direct the witness...", I'll keep
8 that in mind. I mean, yes, I'm concerned that the
9 Postal Service has overstated the magnitude of its
10 savings.

11 BY MR. MAY:

12 Q Are you concerned that they may have
13 understated it?

14 A No, I'm not concerned if they have
15 understated. I'm concerned that they may have
16 overstated.

17 Q And you're not concerned that they've
18 understated it because the Postal Service would make
19 even more profit? Is that right?

20 A Well, there would be a greater net
21 contribution. I'm not sure if that's profit.

22 Q In your response to Capital One's Question
23 14 you were asked about your testimony on page 8 where
24 you said, "Once COS return mail re-enters the mail
25 stream for the trip to Richmond, it is likely to

1 require fewer sortations than the average piece."

2 In replying to Question 14 you began your
3 answer by saying, "While I am not an expert..." If
4 you did not actually study Capital One's returns and
5 if, as you say, you are not an expert on mail
6 processing then why should the Commission give your
7 opinion that Capital One mail is likely to require
8 fewer sortations, why should they give your opinion
9 any credit because it's certainly not an expert
10 opinion, is it?

11 A No, it is not.

12 Q So it's just your opinion?

13 A That's correct.

14 Q Now I'd like to talk a little bit about
15 electronic returns. Again, I believe you have not
16 criticized anywhere in your testimony the Postal
17 Service's estimate of the cost of making an electronic
18 return, have you?

19 A I'm not exactly sure what your question is,
20 but I don't think I have criticized. If you're
21 referring to the 0.66 cents -- is that what you're
22 talking about, sir?

23 Q Yes.

24 A I think I may have mentioned somewhere in my
25 testimony that it might be slightly overstated, but

1 that's not a criticism. I think that's something that
2 Witness Crum acknowledged in fact.

3 Q Now would you turn back again to pages 1 and
4 2 of USPS Library Reference 1? You will recall that
5 that was attached to your answer to the Capital One
6 Interrogatory 10.

7 I believe there we went through previously
8 the total cost for carrier preparation and clerk mail
9 handling on page 1. For physical returns, those two
10 functions cost about 19 cents for physical returns,
11 and then on page 2 it shows the same total, 19 cents,
12 about 19 cents, for those two functions for electronic
13 returns, does it not?

14 A My recollection is that it does. I confess
15 I don't have my glasses.

16 Q Actually, it's 18.72 cents.

17 A Yes. Yes. I'm with you.

18 Q Rounding to 19 cents. Now, these costs are
19 the same because the carrier prep and clerk handling
20 activities presumably are basically the same for
21 physical and electronic returns. Is that your
22 perception of it?

23 A That's my understanding of what they've done
24 here, yes.

25 Q So if Witness Crum misestimated the carrier

1 preparation and clerk handling costs for physical
2 returns -- suppose he got them wrong -- then he almost
3 certainly did the same for electronic returns, did he
4 not?

5 I'm not saying he did misestimate, but if he
6 did. If he did misestimate them then he would have
7 also misestimated those costs for electronic returns,
8 would he not, since the same functions are being
9 performed on physical returns and on electronic
10 returns, or at least according to --

11 A At least according to this library
12 reference. He's using the same numbers.

13 Q That's right.

14 A One has to assume he's estimating the same
15 functions.

16 Q So if he misestimates those two costs for
17 physical returns by let's say 20 percent, then he
18 would have misestimated those same costs by 20 percent
19 for electronic returns, would he not?

20 A I think the answer is obviously yes.

21 Q Now going back to your Table 1 on page 1 of
22 your testimony where you have assumed certain
23 deviations, you've assumed that the Postal Service
24 misestimated return costs by 10 percent, 24 percent
25 and 35 percent.

1 Is there any reason why if in your
2 illustration those costs were misestimated for
3 physical returns by let's say 24 percent it also would
4 follow, wouldn't it, that the cost of electronic
5 returns would have been misestimated by 24 percent?

6 A Would you please ask that question again or
7 have the reporter read it back?

8 Q I'll be happy to ask it again. On page 10
9 you have your table there.

10 A Uh-huh.

11 Q On page 10 you give three illustrations of
12 what would be the results if the Postal Service was
13 wrong about its estimate of return cost, if it had
14 overstated recurrent costs by 10 percent, 24 percent
15 and 35 percent.

16 A Correct.

17 Q I asked you well, if indeed they did
18 overstate the costs for returns, physical returns, by
19 24 percent then following the logic with this table
20 that Mr. Crum has then they would also have overstated
21 the cost of electronic returns by 24 percent, correct?

22 A It is true that if you on one side of the
23 equation multiply by 20 percent you need to multiply
24 the same numbers by 20 percent on the other side of
25 the equation.

1 Q Now would you look at your response to the
2 United States Postal Service Question 15?

3 A Yes, sir.

4 Q Now, in that example, or at least in that
5 question, you were asked to fill in the blanks on a
6 model that the Postal Service gave you in which they
7 said well, what would be the return cost savings using
8 these other assumptions they asked, and you supply
9 that in this table, do you not?

10 A Yes.

11 Q Now, would you confirm that according to
12 this if the unit cost of physical returns and
13 electronic returns are both 24 percent below the
14 Postal Service's estimate that the return cost savings
15 for FY 2003 would still be approximately \$10 million,
16 and the contribution as a result of the NSA would
17 still be approximately \$5 million?

18 A That's what the arithmetic says.

19 Q And if the physical and electronic return
20 costs are 35 percent below the Service's estimate, the
21 Postal Service would still net a \$3.7 million
22 contribution, would they not?

23 A That's what the arithmetic says.

24 Q By what percentage would the Postal Service
25 have had to overstate the unit cost of physical and

1 electronic returns for this NSA to generate no
2 additional contribution? Would they have to be 50
3 percent off?

4 If you don't know, you can supply it for the
5 record.

6 A I'll supply it for the record.

7 Q Thank you. I'd like to examine you a little
8 bit about forwarding now, to change subjects. If
9 you'll go to page 14 of your testimony?

10 A I'm sorry, sir. Did you say 14?

11 Q Fourteen

12 A Okay.

13 Q There is a Table 2 there which is labeled
14 Forwarding Costs. In this table you purport to show
15 the total contribution that would result from the NSA
16 based upon different forwarding rates for Capital One,
17 and then you have the various percentage forwarding
18 rates listed and what the financial consequences would
19 be depending upon which of those proved to be correct.

20 Would you agree that the calculations in
21 that table assume that the Postal Service incurs a
22 cost of 6.6 cents per piece to provide electronic
23 forward notifications to Capital One?

24 A My recollection is yes, that's right.

25 Q Thank you. And you got that from, and it's

1 in the transcript, just for the record, Transcript
2 Volume 2 at page 284. That's where that 6.6 cent
3 number comes from. You got it from the Postal
4 Service, if you will recall?

5 A I got it from the record somewhere. Right.

6 Q Yes. There is a record citation for it.
7 Now, would you agree that to assess the entire impact
8 of providing electronic notification to Capital One
9 that one should also include the cost savings that
10 will result from a reduction in the number of repeat
11 forwards if you knew what those savings were?

12 A Ask me that question again, please.

13 Q Would you agree that if you assess the
14 entire impact of providing electronic notifications to
15 Capital One, you should also include the cost savings
16 that would result from a reduction in the number of
17 repeat forwards, a reduction that flowed from the
18 electronic notifications?

19 A I would agree that that's part of the
20 consideration you need to make.

21 Q Yes.

22 A I wouldn't say that's the total.

23 Q No.

24 A I think your question did say --

25 Q That you should include it. So to include

1 the cost savings from a reduction in the number of
2 repeat forwards, your Table 2 here should include a
3 further column, should it not, which would be
4 captioned Cost Savings From Reducing the Number of
5 Repeat Forwards, assuming we knew what that was?

6 A Again, you failed to posit a question.

7 Q I'm asking do you not agree that your table
8 should include a fourth column, a fifth column,
9 captioned Savings From Repeat Forwards, Savings From
10 Reducing the Number of Repeat Forwards, since I
11 believe you just agreed --

12 A It could be put on that table as part of an
13 overall consideration. Correct.

14 Q And I believe you did elsewhere state in
15 your testimony that, "Witness Crum has a valid point
16 regarding a probable improvement in the repeat forward
17 rate."

18 A Yes. I think he does.

19 Q But nowhere does he in any of his
20 calculations claim a savings from that, does he?

21 A I'm not sure how to answer that question.
22 The issue of forwards is not part, as I understand it,
23 of the proposed justification for the NSA.

24 Subsequent to the filing of this the issue
25 of forwards was raised, and I think he does -- I mean,

1 when you say part of the testimony, I'm not sure what
2 you're talking about.

3 Q Well, Witness Crum failed to, and he had a
4 long calculation of the puts and takes, savings,
5 costs, where he adds it all up and gets a net
6 contribution to institute costs or what you might call
7 a net profit from the deal.

8 In that he does not include as part of the
9 net contribution savings from the avoidance of repeat
10 forwards. That's not in his calculation, is it?

11 MR. BAKER: Is counsel referring to Witness
12 Crum's direct testimony?

13 MR. MAY: Yes.

14 THE WITNESS: That is correct, as I said
15 earlier.

16 BY MR. MAY:

17 Q And he also failed, on the other hand, to
18 include the cost of providing electronic notification,
19 did he not?

20 A Yes, he did. He also failed to include the
21 foregone revenue.

22 Q I mean, we'll get to that later. If you
23 could just stick to what I'm asking you about, which
24 is forwards. I'm asking you about forwards.

25 A And I was answering about forwards.

1 Q No. And then we had to hear about the
2 failure to include the fees from waiver. Does that
3 have anything to do with forwards? It doesn't, does
4 it?

5 A I would argue that it does, but go ahead.

6 Q Well, we're just talking about forwards now.

7 A And I was, too.

8 Q So you have failed in this table to take
9 account of the net savings from repeat forwards.
10 Isn't that correct?

11 A No.

12 Q Well, it's not anywhere here, is it?

13 A I don't consider that a failure, given the
14 fact that there's absolutely no information on it.

15 Q Well, but if there were it should be
16 included, shouldn't it?

17 A In your hypothetical it should be included.
18 There's no question about that.

19 Q Well, both in the real world if the
20 information existed about how much was saved then it
21 should be included. It's not just a hypothetical.
22 The only thing hypothetical is --

23 A If in the real world you had it, it should
24 be included.

25 Q Right. Now let me refer you to Witness

1 Crum's response to POIR-2, No. 7. I'll hand that out.
2 Now, I believe you've seen this before. In fact, you
3 cite it on page 11 of your testimony in Footnote 17,
4 so I believe you're familiar with this document.

5 In fact, that may be where you got some of
6 your data from like the 5.6 annual solicitations per
7 delivery point. Is that correct?

8 A It may well be.

9 Q Now, the POIR references Crum's response to
10 Capital One's Question 11, does it not?

11 MR. BAKER: Can counsel direct us to the
12 place?

13 MR. MAY: The POIR itself.

14 MR. BAKER: Do you mean the question?

15 MR. MAY: Yes.

16 MR. BAKER: Okay. What's the pending
17 question?

18 BY MR. MAY:

19 Q If you'll see, the presiding officer
20 references the Postal Service response to your
21 Interrogatory 11, the NAA's Interrogatory 11. That's
22 a reference that the POIR uses.

23 MR. BAKER: The POIR Question 7, the
24 question stated by the presiding officer referred to
25 an NAA interrogatory, but not necessarily Mr. Kent's.

1 MR. MAY: Yes.

2 BY MR. MAY:

3 Q Also, the POIR references and quotes from
4 Witness Crum's response where he says, "Witness Crum
5 goes on to assert that the costs of notification
6 'would likely be more than offset' by the cost savings
7 accruing to the Postal Service from the reduction of
8 forwarded Capital One mail." The POIR question itself
9 references Crum's answer.

10 Now, in his response here Mr. Crum then
11 performs a series of calculations showing why he
12 believes this to be the case. Is that not correct?
13 On the following pages is a rather lengthy answer, but
14 I thought you might be familiar with it since it's
15 cited in your footnote in your testimony.

16 A We're back to me? You're not asking Mr.
17 Baker questions anymore?

18 Q Back to you.

19 A Okay. Yes, that's true.

20 Q If Witness Crum is correct about those
21 calculations, then the cost savings figures that would
22 go into a column in your table, which column would be
23 labeled Cost Savings From Reducing the Number of
24 Repeat Forwards, those would be larger than the
25 additional cost of providing the EACS notification if

1 Witness Crum is correct, correct? Is that right?

2 A That's correct.

3 Q That would also mean that in your table that
4 the total contribution as a result of the NSA column
5 would also be higher than estimated by the Postal
6 Service if Witness Crum is correct, wouldn't it?

7 A That's correct. Basic arithmetic.

8 Q Yes. Now let me refer you to your answer to
9 Capital One's Question 38. Therefore, you there
10 confirm that you have done no analysis to disprove Mr.
11 Crum's analysis that he details in his POIR-2 response
12 to Question 7. You say I have done no analysis, and I
13 cannot, you say, do one without more information. Is
14 that correct?

15 A Uh-huh, and I tell you why.

16 Q But you do fault Mr. Crum for not removing
17 postage due costs, I believe, on page 15 of your
18 testimony, and you propose an adjustment to Witness
19 Crum's forwarding cost. You adjust it from 30.7 cents
20 to 30.6 cents.

21 A That's correct.

22 Q So you think Crum overstated the costs
23 avoided from reducing forwards by a staggering one-
24 tenth of one cent? Is that correct?

25 A That's correct. I wouldn't categorize it as

1 staggering. I was simply pointing out that the number
2 was wrong.

3 Q By one-tenth of one cent. You thought that
4 was worth making that correction, but you didn't feel
5 troubled at all by the fact that Mr. Crum failed to
6 include even a stab at including the costs that would
7 be saved from repeat forwards, which his testimony
8 says definitely will happen.

9 He goes on for pages explaining his
10 calculations of why that will happen in his answer to
11 the POIR. That didn't trouble you at all?

12 A A gross mischaracterization of my testimony.
13 Interesting speech, but gross mischaracterization.

14 Q Please explain how I've mischaracterized
15 your testimony. You are troubled by the fact? Is
16 that what you mean? You are troubled by the fact that
17 Mr. Crum did not include savings?

18 A I'm troubled by the fact that Mr. Crum
19 didn't address any of the forwarding aspects or the
20 lost revenue to the Postal Service.

21 Q Included in that --

22 A That is not something about which there is
23 anything in the record that I can find. I will point
24 out, however, that the 30.7/30.6 cent issue is a math
25 error, and I simply pointed it out. Any attempt to

1 equate those two as being of equal import is a gross
2 mischaracterization. That's all I'm saying.

3 Q I mean, surely you don't think that a one-
4 tenth of one cent error in any way compares to the
5 failure of Mr. Crum or the Postal Service to include
6 the savings from repeat forwards. You're not equating
7 those, are you?

8 A And in fact I just distinguished between the
9 two and said that they weren't of equal import.

10 Q And indeed the cost of savings from repeat
11 forwards would be considerably more important, would
12 it not?

13 A Potentially. It depends upon what Cap One's
14 repeat forward rate is.

15 Q Now I'd like to take you through an example
16 of how receiving electronic correction notices might
17 affect the repeat forward rate. I will try to keep it
18 as simple as I can so that the lawyers in attendance
19 will be able to follow it.

20 MR. BAKER: That better be very simple.

21 MR. MAY: Yes.

22 BY MR. MAY:

23 Q Let us assume that we have a mailing list
24 that before NCOA processing, and you know what NCOA is
25 I take it?

1 A It's referenced in my testimony.

2 Q Yes. That before NCOA processing has 400
3 accurate addresses in it, but they're old addresses.
4 The people don't live there anymore, but they were
5 accurate.

6 A Hence they're no longer accurate.

7 Q Yes.

8 A Correct?

9 Q Well, the Postal Service, you'll find out,
10 they call them accurate addresses, and in fact a piece
11 of mail can be delivered to that address. It's just
12 that the person doesn't live there anymore. In any
13 event, there are 400 of these addresses that the folks
14 have moved, and the Postal Service knows where they've
15 moved.

16 Now, although you may later want to change
17 your testimony as Mr. Baker advises you after you see
18 the response that the Postal Service introduces today
19 about the percentage of corrections caught by NCOA,
20 but at least you were operating on the assumption that
21 Mr. Wilson's testimony was correct that the NCOA
22 caught 25 percent of the addresses when it went
23 through NCOA. That was the previous testimony given.

24 When these 400 names are sent through NCOA,
25 if the 25 percent had been correct then the NCOA would

1 catch 100 of those, would it not?

2 A On average.

3 Q All right. So now we have --

4 A It may have caught all 400 on that list.

5 Q Yes. Well, the list is more than 400, but
6 there are 400 names on the list that have addresses
7 where the folks have moved. When this list is run
8 through the NCOA, assuming NCOA only catches 25
9 percent of the corrections, then they will correct 100
10 of those 400, and they will forward 100 of those, send
11 an address correction for about 100 of those.

12 Three hundred pieces would have to be
13 forwarded because the 100 -- the person with the list
14 corrects the 100, but that still leaves 300 bad
15 addresses in the mailing. On those 300, they'll get
16 forwarded.

17 Now let's say a mailer first class mails to
18 this list five times a year. Okay. Again, to keep it
19 simple we'll assume that there are no additional
20 moves; that this person who moved didn't move a second
21 time just to try to keep it simple.

22 A This is long past being simple.

23 Q Well, he puts his 400 list, puts his list
24 through NCOA.

25 A I'm with you. I'm with you. I'm just

1 pointing out that --

2 Q NCOA catches 25 percent, so 100 of those
3 addresses got corrected. The other 300 had to be
4 forwarded. The mailer may have five times a year.
5 Okay. Now, the next four times he mails --

6 A The next four times he mails after the five
7 times he's mailed?

8 Q Yes.

9 CHAIRMAN OMAS: Mr. May, excuse me.

10 MR. MAY: Do you want to take a break?

11 CHAIRMAN OMAS: Could we take a break?

12 MR. MAY: Sure.

13 CHAIRMAN OMAS: Maybe you could figure out
14 the question, and then we can get back.

15 MR. MAY: Well, I'm trying to keep it
16 simple.

17 CHAIRMAN OMAS: Yes. We understand that.

18 MR. MAY: I had a feeling I was losing
19 people here.

20 CHAIRMAN OMAS: It's been quite simple this
21 morning. Thank you.

22 We'll take a break for about 10 minutes.

23 We'll come back at 11:10.

24 (Whereupon, a short recess was taken.)

25 CHAIRMAN OMAS: Would you like to proceed?

1 MR. MAY: Yes. Just to refresh everyone's
2 recollection, we were talking about hypothetical
3 mailing list that started out with 400 old addresses
4 on it, and this is a mailer who mails five times a
5 year to his mailing list. And so he submits his
6 mailing list to NCOA, and those 400 old addresses are
7 on that mailing list, and NCOA corrects 100 of the 400
8 because on average that's what they correct, or, at
9 least, so Mr. Wilson told us previously. He has now
10 adjusted that, but going with the 25 percent for the
11 time being, that means that since only 100 addresses
12 were corrected, those remaining 300 old addresses will
13 have to be forwarded. So in that first mailing 300
14 pieces of mail got forwarded.

15 Also, 300 notices came back to the mailer.
16 The mailer got notices that these 300 addresses were
17 old addresses, and they gave him the new address. So
18 now the next time this mailer makes a mailing, his
19 second mailing, he now has information on these 300
20 addresses, but he actually only has 285 corrections
21 because, as we know, only 95 percent, according to
22 your testimony, only 95 percent of those forwarded
23 get an address correction sent.

24 BY MR. MAY:

25 Q Do you recall your testimony on that?

1 A That's not my testimony, but --

2 Q Well, you quoted other testimony that 95
3 percent get a notification for forwards. So that
4 would mean of those 300 forwards the mailer got
5 notifications of about 285 addresses, and there are 15
6 addresses he didn't get any notification about, so he
7 can't correct those 15 addresses. But after he has
8 got all of these back, this mailer now has a mailing
9 list that if he has put all of these changes into his
10 mailing list, all of the change notices he got, he now
11 only has 15 bad addresses in his mailing list. Is
12 that correct?

13 A Assuming, that's correct, that we're dealing
14 with the exact same mailing list we started with.
15 Right?

16 Q Yes. And so he mails a second time, and the
17 second time he mails there are only 15 bad addresses
18 this time, assuming that these moves didn't move
19 again. And so the third time he mails he still only
20 has 15 bad addresses, and the fourth and the fifth.
21 So the total number of bad addresses he mails, the
22 total number of forwards that have to be made are the
23 original 300 plus another 60, 15 each of the next four
24 times, so there has only been 360 pieces forwarded
25 because of the address corrections. The EACS

1 correction system has caused that efficiency.

2 So for 285 electronic notifications in this
3 hypothetical the mailer has managed to avoid 1,140
4 repeat forwards, which is if he kept mailing the same
5 number of 300 bad addresses each time, that's what
6 would have happened. So he has avoided mailing that
7 many. And I believe the Postal Service says it costs
8 6.6 cents per notification and that, on the other
9 hand, they save 30.6 cents, which is your number. You
10 corrected their 30.7 to 30.6. So they save 30.6
11 cents.

12 So for an expenditure of 6.6 cents on a
13 notification, in this example they would have saved
14 30.6 cents times the number of repeat forwards
15 avoided. So that, would you not agree, is quite an
16 efficiency from the address correction system in this
17 example?

18 A In your hypothetical, the arithmetic would
19 say it is.

20 Q And so there is an enormous amount of
21 savings to the Postal Service in this hypothetical
22 from the avoidance of repeat forwards. Is that not
23 correct?

24 A In that hypothetical.

25 Q Now, could you explain why Capital One's

1 mailings would not fit this hypothetical where, at
2 least the Postal Service says they mail each address
3 5.6 times a year? In the hypothetical, I used the
4 mailer mails to his list five times a year. The
5 Postal Service says Cap One does it 5.6 times a year.
6 Explain what is different about Capital One's savings
7 from avoiding repeat forwards that they will be able
8 to make from getting electronic address notifications
9 under the NSA they are not getting now. Why would
10 Capital One not show the same kinds of very large cost
11 savings from avoidance of repeat forwards as does the
12 mailer in our hypothetical example?

13 A Well, you know, I think the basic answer is
14 I don't know because I don't know what Capital One's
15 business model is, and your hypothetical strikes me as
16 being borderline absurd. Let me give you a couple of
17 reasons why I would guess or I believe that that
18 doesn't apply. There is a fair body of research and
19 data in the world of survey research that says what
20 you really ought to be doing is you ought to be
21 targeting your audience, and in this case I'm assuming
22 that's potential credit card people. There is a lot
23 of very strong statistical support that says that in
24 order to do that, you make mailings on a very well-
25 timed basis.

1 In your hypothetical, there is the
2 assumption that the whole process of the notification
3 gets back to the mailer, the mailer updates his list,
4 and then he mails again. If, in fact, you're doing a
5 targeted mailing, it's likely that you are going to do
6 that mailing in the time frame before you get all of
7 the data back. So that would be one reason I would
8 believe it doesn't apply.

9 Another reason is that I seem to recall a
10 Capital One witness, and I apologize, sir, I don't
11 remember if it was Mr. Jean or not, talking about the
12 fact that there is a Capital One mailing list,
13 whatever that might be, but then there are also vendor
14 lists that they acquire or rent and that updates don't
15 occur to those. So to the extent that you're using
16 third-party mailing lists that haven't been updated,
17 that Cap One doesn't notify those third-party mailers,
18 that wouldn't apply either.

19 However, the basic concept of repeat
20 forwards ought to have the beneficial effect,
21 certainly not to the magnitude that you would like to
22 have in your hypothetical, but, as I've admitted in
23 the testimony, I think Mr. Crum is right. There is a
24 probability that that's going to improve and,
25 therefore, should reduce some Postal Service costs.

1 Q Just for the record, you may or may not have
2 stated what the Capital One testimony was. You're not
3 sure. Is that correct?

4 A I'm pretty sure that's what the testimony
5 was. I just wasn't sure who it was.

6 Q Well, assuming that, indeed, Capital One in
7 the future under this deal, assuming that Capital One,
8 when it gets a forward notice, their mail is
9 forwarded, and they get an address-correction notice
10 electronically, assume that Capital One will then use
11 that correct address, assume that they will use that
12 correct address in every mailing going to that
13 individual for the remainder of the year. Assume
14 that.

15 A Okay. And I'm to make that assumption
16 relative to both their lists and all third-party lists
17 they acquire.

18 Q Assume that any mailing they make --

19 A Okay.

20 Q -- that they will make the correction if
21 they have gotten the correction in time before they
22 make the mailing. Now, you did point out the
23 possibility that the mailer would have made their
24 second mailing because of timing issues before they
25 got all of the corrections, did you not?

1 A Yes, sir. I think there is a fair body of
2 research that says that's --

3 Q So assume that they don't get all of the
4 notifications before they make the second mailing, but
5 assume that they do get all of the notifications
6 before they make the third mailing. Would that be an
7 unreasonable assumption?

8 A I think all of the assumptions thus far are
9 unreasonable.

10 Q But you just told us that you seem to have
11 expertise upon mailing strategies. You went on at
12 some length about there is a whole wealth of
13 literature about targeting mailings, what have you,
14 and I'm asking you, is it a reasonable assumption that
15 under this NSA agreement, which requires Capital One
16 to correct and/or update their list within two days of
17 receipt of the notification, and then also in the case
18 of a corrected address, to use that in future
19 mailings, is that now what the agreement requires?

20 A That's my understanding, sir.

21 Q All right. Well, then assume that they are
22 going to obey the rules of the agreement. Why is it
23 an absurd assumption to believe that they will have
24 the notifications of these incorrect addresses in time
25 to correct their third mailing, if not their second?

1 A I didn't say that that was an absurd
2 assumption. I said what you were proffering was an
3 absurd assumption.

4 Q But that isn't an absurd assumption. Right?

5 A I don't know. Maybe it will be the fourth,
6 Maybe it will be the fifth. I don't know that there
7 is any reason to believe that the second isn't going
8 to happen and the third is, or that the third isn't
9 going to happen and the fourth is. There is no data
10 that's been presented by anybody that would indicate
11 what the pattern is of mailing by Capital One.

12 Q Well, the only data that we have, to the
13 extent that it's data, is the Postal Service's
14 testimony in this case that Capital One promotes an
15 address 5.6 times a year. Isn't that correct? Or you
16 don't regard that as data in the record.

17 A I thought that what the assumption was was
18 that there is an average of 5.6 moves per year.

19 Q No.

20 A I'm sorry. I think your statement is
21 accurate. I do consider that data. What I don't
22 consider to be valid is whether that's applicable to
23 Cap One or not.

24 Q Their testimony was it was Cap One that
25 mailed each address 5.6 times a year, so --

1 A I understand, but your assumption -- I'm
2 sorry. Go ahead. Your assumption is that there would
3 be even mailings throughout the year, and I'm saying I
4 don't accept that assumption. At least based upon the
5 receipt of mail I get from Capital One, it appears to
6 be highly targeted and concentrated in periods of
7 time.

8 Q But you also agreed that it would not be an
9 absurd assumption to assume that, whatever their
10 pattern, they would at least get these notifications
11 by the time of their third mailing when they make 5.6.

12 A I don't know. I don't know whether that's a
13 reasonable assumption relative to the fourth or the
14 fifth or even the second. I just don't know. That
15 assumes a series of facts that --

16 Q But you do agree that if, indeed, Capital
17 One gets all of those notifications either by the time
18 of the second or third mailing, that there will be
19 significant savings from the avoidance of repeat
20 mailings for Capital One, if that happens.

21 A If that were to happen, I do agree with
22 that, sir.

23 Q If you would look at your changing -- really
24 one final question on this. If you would look at your
25 response to Postal Service Question 18(d) --

1 A Did you say 18(d) as in "David"?

2 Q "D" as in "David."

3 A Thank you.

4 Q In 18(d) you were asked to confirm that the
5 relative changes in forwarding rate from NCOA
6 processing every 160 days or every 60 days would have
7 no correlation to the return rates, and you say
8 confirmed that use of NCOA more or less frequently
9 should not have an effect on a mailer's return rate,
10 caderas paribus. In other words, fewer forwards from
11 NCOA, more frequent NCOA, will not mean that there
12 will be fewer returns.

13 A I think that the question is answered right
14 there.

15 Q Will more forwards mean that there will be
16 more returns?

17 A Well, the answer is I don't know. If you
18 look statistically at the average, the average first-
19 class mail, one would say yeah.

20 Q You just simply said that all things being
21 equal that there is no correlation between --

22 A -- the rate, not the absolute numbers.

23 Q -- the rate and the number of returns.

24 A The rate. We know that there is a
25 relationship of roughly 159 percent. If you have

1 10,000 items at issue, that results in a certain
2 absolute number. If you move to 20,000, the absolute
3 number gets larger, but the rate doesn't change.

4 Q Yes, but presumably -- the question was,
5 presumably you would have less frequent forwards
6 depending upon whether you do NCOA 180 or every 60
7 days, which is what you were asked about in parts A
8 and B, and then it just says, asks you to confirm that
9 the relative changes in forwarding rate between 180-
10 and 60-day NCOA, whatever those relative changes in
11 forwarding rate are, would have no correlation to
12 returns. Is that correct?

13 A To the return rate. That's correct.

14 Q Now, on page 12 of your testimony, you noted
15 that Capital One's forwarding rate is likely to be
16 higher than the average forwarding rate for first-
17 class mail, and you say because its return rate is
18 higher. Correct?

19 A Yes. I speculate that there might be a
20 correlation.

21 Q But I thought you just told us that there is
22 no correlation in forwarding rates and return rates.

23 A Rates.

24 Q I said forwarding rates and return rates.

25 A Correct.

1 Q Well, basically, what you've got here in
2 this answer is that you've really made an assumption,
3 haven't you, that the more forwards, the more returns,
4 or the more returns, the more forwards? You have made
5 that assumption, have you not?

6 A I say explicitly as an alternative estimate
7 of forwards, one might assume that's the relationship
8 because there certainly isn't any data to tell us
9 about it.

10 Q Okay. Now, have you ever processed a
11 mailing list against the NCOA data base, you,
12 yourself?

13 A No.

14 Q So you're not an expert about NCOA
15 processing, are you?

16 A I am not an expert about NCOA processing.

17 Q Okay. If you'll look at your answer again
18 to Capital One's Questions 25(a) and (b), --

19 A If I will look again at what?

20 Q Your answers to Capital One's Questions
21 25(a) and (b), and there you agree that mail that is
22 forwarded, you say, does have an accurate address on
23 it but that it just happens to be an old one. Is that
24 right?

25 A I say that's my understanding.

1 Q And so, forgetting percentages, but I take
2 it, you agree that if a new address is known, the NCOA
3 processing will provide the current address for an
4 accurate but old address, at least to whatever
5 percentage it turns out that the Postal Service now
6 says is going to happen. Originally, it was 25
7 percent of the case that they give you a new, correct
8 address. They have now today filed an answer putting
9 in question the 25 percent.

10 A I have not seen that, but okay.

11 Q But in any event, the NCOA catches, then it
12 simply updates and gives you a new, correct address.
13 Now, again, if you'll look at your answer to 26(b),
14 you there say that the NCOA will not correct a
15 deficient address. Correct?

16 A It's my understanding from the record in
17 this case that if there is not an exact match, that's
18 correct. NCOA only does an exact correct.

19 Q And back in your response to Question 25(c),
20 you agreed that a major reason for mail that is
21 returned to sender is that it has a deficient address.
22 Isn't that correct?

23 A I think that's a reasonable characterization
24 of what I said.

25 Q And so forwarding is about getting corrected

1 addresses for old addresses, not for deficient
2 addresses. Returns are a function of deficient
3 addresses. Isn't that correct?

4 A As a general proposition, that's probably
5 correct. There are obviously certain circumstances in
6 which, and the Postal Service, I should say, takes
7 account of these, in which you may have a good
8 address, but the person is no longer alive. I don't
9 know if I would call that a deficient address.

10 Q Well, the deceased might. Moving along, I
11 would like to get to what you would call another
12 aspect of forwarding, I believe, waiver of fees.
13 Somehow or other you were going to explain earlier why
14 waiver of fees really was a forwarding issue. Perhaps
15 you will have that opportunity in the course of
16 answering the next line of questions.

17 In responding to Capital One's Question
18 30(c) -- can you get that in front of you? -- in that
19 question you were asked to explain why you had
20 included waived electronic return fees in your
21 calculation to test your financial impact of the NSA,
22 the financial impact, and you state that "waived fees
23 are lost revenues, and they must be considered
24 separately from the costs, just as Witness Crum
25 considered cost savings from electronic returns,

1 revenue leakage, and additional contributions
2 separately. Now, is it not the case that there, in
3 fact, are currently costs incurred for physical
4 returns of Capital One's mail?

5 A I assume there are, yeah. It's certainly
6 part of the justification of the Postal Service's, but
7 whether they've used the right numbers or not, I don't
8 know.

9 Q But there is a cost, no question.

10 A There is a cost to return mail.

11 Q Is it not also the case that, according to
12 you, at least, there may be a reduction in revenue
13 from first-class mail that would have been paying the
14 full rate but for the discount that they are giving?
15 In other words, they may get a discount on mail that
16 would otherwise materialize anyway, so that's a
17 revenue consequence, a real one. Is that correct?

18 A Let me make sure I understand your question.
19 Are you asking me do you lose revenue when you
20 discount rates?

21 Q Yes. That's something that's real. That
22 would be an actual loss of revenue, would it not?

23 A I think the NSA includes a loss of revenue.

24 Q From what they are receiving, yes, the
25 Postal Service is currently receiving full postage

1 from Capital One, and you would argue that under the
2 NSA for some of that mail they will no longer be
3 getting full postage, so that's a real revenue effect,
4 is it not?

5 A I don't know that I would argue that. I
6 would say that's part and parcel to what the
7 submission is.

8 Q Now, is there any revenue currently being
9 received by the Postal Service from Capital One for
10 electronic address corrections?

11 A I don't know. I believe the answer to that
12 is no, but I don't know.

13 Q If the record shows that they are not
14 currently paying any revenues to the Postal Service
15 for electronic address corrections, please explain how
16 the continued lack of revenue from those fees would be
17 a financial consequence of the deal? I'm not getting
18 the money now.

19 A Okay. It's my understanding, sir, that the
20 record states that soon EACS customers will be charged
21 20 cents. This is a proffered three-year deal.
22 Therefore, when other customers start getting charged
23 the 20 cents, if, in fact, Capital One receives that
24 service for free, that is lost revenue.

25 Q It's only lost revenue of Cap One were to

1 elect to pay for that service. Correct?

2 A And?

3 Q Well, Capital One, the record will disclose,
4 or I ask you to assume that the record so discloses,
5 will not pay for address- correction fees, electronic
6 address-correction fees now, and I'm asking you to
7 assume the record shows this, as hardly anyone does,
8 and the record will also disclose that. Assume that
9 the record so does disclose that not only is Capital
10 One not doing that at all, and assume that Capital One
11 will continue to refuse to do that in the future, NSA
12 or no, then how can there be a loss of revenue from
13 Capital One if the Postal Service is currently not
14 receiving those fees and in the future would not be
15 receiving such fees from Capital One?

16 MR. BAKER: Could the question be clarified
17 to include whether or not Capital One would be
18 receiving electronic notifications in the future under
19 the assumption stated?

20 BY MR. MAY:

21 Q The assumption is that Capital One, if it
22 has to pay for electronic address correction, just as
23 now, they will not pay for it; and, therefore, they
24 won't get it.

25 A And does the question also assume that other

1 customers are going to start being charged for it at
2 20 cents each?

3 Q Other customers are already being charged
4 for it if they get the service, and no one is using
5 it. I'm asking you to assume that's what the record
6 shows, that hardly anybody is paying those fees right
7 now, and despite the Postal Service's high hopes for
8 the future, at least my client has no intention of
9 paying for them in the future, NSA or no NSA, because
10 right now, and in the absence of an NSA in the future,
11 Capital One will get the information that this address
12 is no good for free. Why should they pay? Explain
13 that.

14 A It makes no sense to me that they would pay
15 for a service that's given to them for free, if that's
16 an option. My belief is that they should pay for it
17 if they receive the service.

18 Q Well, the service they are currently
19 receiving, as is every first-class mailer, a free
20 physical return of their undeliverable mail, and there
21 is no plan to change that for the future.

22 A I said right up front in my testimony, I
23 thought Capital One got a good deal on this. I just
24 am not sure about the Postal Service.

25 Q But you still haven't explained how the

1 Postal Service can be shown to have lost revenue from
2 fees that they are not collecting now and, according
3 to my client, never intend to pay under any
4 circumstances.

5 A I think any analysis in which a service is
6 provided for free has an opportunity cost associated
7 with it. In this case, that opportunity cost is
8 foregone revenue, and it should be included in. It
9 may be part of the deal.

10 Q Well, it may be part of the value to Capital
11 One of the deal, but you still haven't explained how
12 it's a revenue consequence of the deal because there
13 is no money being lost by the Postal Service because
14 of this deal with Capital One.

15 MR. BAKER: Mr. Chairman, I object because I
16 believe the witness did answer the question. He said
17 there was an opportunity cost of the loss of the
18 foregone revenue when a new service is being provided.

19 BY MR. MAY:

20 Q But what is the opportunity cost here?

21 A Twenty cents per EACS.

22 Q How is it an opportunity when, indeed, the
23 uncontroverted testimony is that Capital One will not
24 pay this fee? There is no opportunity to the Postal
25 Service, according to this record, for them to ever

1 collect such a fee from Capital One. So what
2 opportunity is being foregone?

3 A The fact that a customer doesn't pay doesn't
4 mean that it doesn't cost the Postal Service
5 something.

6 Q How does it cost the Postal Service
7 anything? Does it cost it anything now that Capital
8 One is foregoing paying 20 cents to get address-
9 correction service? Is it costing the Postal Service
10 anything today?

11 A Absolutely.

12 Q What's it costing them?

13 A Well, according to the record, 20 cents an
14 EACS.

15 Q Today?

16 A Absolutely, in foregone revenue.

17 Q Then, indeed, since no one in first-class
18 mail appears to be using it, the Postal Service must
19 be losing billions, according to you, billions --

20 A I think the Postal Service is losing --

21 Q -- of dollars in opportunity costs because
22 first-class mailers have chosen not to pay the 20-cent
23 address-correction fee.

24 A How they decide to account for it is not the
25 subject of my testimony. I'm simply telling you that

1 in the analysis of this proposed NSA, it ought to be
2 considered.

3 Q Are you saying that the Postal Service
4 accounting reports and the reports to this Commission
5 should in the future reflect on its books the fact
6 that 50 million Americans who use first-class mail
7 have elected not to use and pay them 20 cents for an
8 address-correction fee and multiplied by the many,
9 many billions of pieces of first-class mail for which
10 a 20-cent, first-class correction fee could be
11 collected, the sum of losses in the billions in
12 opportunity costs, are you saying the Postal Service
13 should take account of that and report that to
14 anybody, the public, the Commission?

15 MR. BAKER: Mr. Chairman, I'm not sure that
16 accurately reflected what the witness said, but I
17 think I heard the question include should they be
18 reporting as lost revenue when people are not
19 accepting EACS, so is the question including that?

20 MR. MAY: That's right. No. The witness, I
21 believe -- correct me if I'm wrong -- you testified
22 that there is currently a cost to the Postal Service
23 from the fact that Capital One chooses not to use the
24 address-correction service and pay a 20-cents fee for
25 corrections. You say that's a cost to the Postal

1 Service. My question is, well, if it's a cost to the
2 Postal Service because Capital One doesn't use it, is
3 it also a cost to the service for the fact that hardly
4 anyone in first-class mail uses it; and, therefore, at
5 a 20-cent-per-piece rate, it would be in the billions?
6 Is that what you're saying?

7 A Well, if that's what I said, I spoke
8 incorrectly. To the extent that a customer, such as
9 Cap One, is receiving the service, it is costing the
10 Postal Service money, yes.

11 Q Well, they are not receiving the service
12 now, are they?

13 A And if they do receive the service, they
14 should be charged 20 cents, just like every other
15 customer should be charged 20 cents.

16 Q Well, I assume you would also argue that if
17 they use the service now, they should be charged 20
18 cents.

19 A Yes, I would.

20 Q But they choose not to use it now, and they
21 intend not to use it in the future if they have to pay
22 for it, so I fail to see what lost revenue the Postal
23 Service is experiencing.

24 A If the Postal Service provides EACS, which I
25 understand is part of the proposed NSA, and it costs

1 20 cents per EACS, that ought to be considered as part
2 of the evaluation of the total financial impact of
3 this proposed NSA. It's very straightforward.

4 Q Well, indeed, it costs them 6.6 cents, and
5 everyone concedes that that 6.6 cents per piece should
6 be charged to the deal. You're, on the other hand,
7 claiming that the Postal Service should also charge to
8 the deal a loss of revenues from fees that presumably
9 would otherwise be received, but if they would not
10 otherwise be received, how can there be a loss of
11 revenue?

12 A I think I've answered that question at least
13 four times. You know, I can't help it if you don't
14 understand it.

15 Q You choose not to further elaborate on why a
16 fee the Postal Service will never receive is
17 nevertheless a revenue loss.

18 A I believe, and I'll try this one more time,
19 sir, that if the Postal Service is going to give Cap
20 One that service, whether or not Cap One wants that
21 service or would pay for it in the future, if, in
22 fact, Cap One receives that service, it is a cost that
23 should be factored into the consideration of this NSA.

24 Q Is it a cost or a revenue loss?

25 A I've dealt with it as a revenue loss.

1 Q We know there is a cost. Right?

2 A The entire basis of this NSA appears to be a
3 cost justification.

4 Q Well, the cost is 6.6 cents, the cost, but
5 you say, in addition to that, you want to charge the
6 difference between the 6.6 cents and the 20 cents fee,
7 you also want to charge that as -- I think you call it
8 a financial consequence.

9 A I think you need to consider that as a
10 financial consequence. That's correct.

11 Q Now, if you would refer to your response to
12 Capital One's Question 19, in that question we
13 referenced your testimony on page six, which asserted
14 that the volume penalty under the Cap One NSA, that
15 they would have to pay a million-dollar penalty for
16 failing to achieve 750 million pieces of first-class
17 mail as a threshold. You say in your testimony that
18 that was set so low as to be a meaningless penalty,
19 and so we asked you in this question whether it could
20 not be the case at Capital One, while remaining quite
21 healthy and viable, could still divert all of its
22 first-class mail to standard-class solicitations and
23 make the 750-million-piece threshold a very real and
24 very meaningful guarantee and \$1 million penalty, and
25 your response was that you were not privy to Capital

1 One's proprietary information and, therefore, couldn't
2 confirm or rebut that.

3 And so what I would like is to answer the
4 question, which is simply this: Why do you need any
5 proprietary information about Capital One to answer a
6 hypothetical question? And that question, again, is
7 this: You stated that a 750-million-piece threshold
8 would only come into play if something much more
9 serious than declining first-class volumes were
10 afflicting Capital One. And, again, we asked you
11 whether or not it could be that Capital One could be
12 quite healthy financially and viable and still divert
13 all of its first-class mail to standard mail. Now,
14 can you answer that question, or if you can't, tell me
15 what proprietary information you need in order to
16 answer that question?

17 A That question, again, is?

18 Q Couldn't Capital One still be totally
19 financially viable and healthy and still divert all of
20 its first-class mailings to standard mail?

21 A Yes.

22 Q Now, if you'll look at your answer to
23 Question 20 --

24 A Capital One?

25 Q Excuse me. Capital One. In that question,

1 we ask you about your testimony on page six, where you
2 said that it was conceivable that some mailers look to
3 the Capital One NSA and see "engaging in high-cost
4 behavior as a way to get a better deal with the Postal
5 Service." We asked you to explain how it would make
6 economic sense to a mailer to deliberately send you AA
7 mail so that a mailer might receive free address
8 corrections. Your response was that nowhere in your
9 testimony do you say that mailers would deliberately
10 send you AA mail. If that's so, then please explain
11 what you meant by "engaging in high-cost behavior as a
12 way to get a better deal with the Postal Service."
13 What did you mean by that?

14 A Cap One has an extraordinarily high return
15 rate relative to the first-class mail average. It
16 seems to be extracting a wonderful deal from the
17 Postal Service here. That is the wrong price signal
18 for the Postal Service to be sending to the mailing
19 community in general.

20 Q What do you mean exactly by "engaging in
21 high-cost behavior as a way to get a better deal"?
22 What high-cost behavior is it you say that they would
23 be engaging in?

24 A They, Cap One, or they, other mailers?

25 Q Other mailers.

1 A Oh, I'm not speculating about other mailers.
2 I'm telling you that Cap One is engaging in high-cost
3 behavior and being rewarded.

4 Q No. You, indeed, speculated about other
5 mailers. I'll quote your testimony directly. You
6 said it was conceivable that some mailers --

7 A -- will look to this particular NSA --

8 Q So you are speculating about other mailers,
9 are you not?

10 A It is conceivable that other mailers could
11 see that Cap One has been rewarded for high-cost
12 behavior and think that that is the reason that Cap
13 One is being rewarded.

14 Q Well, they would see that engaging in high-
15 cost behavior is a way to get rewarded. What is the
16 high-cost behavior either they would engage in, you're
17 afraid of, or what is the high-cost behavior that
18 Capital One is engaging in?

19 A A 9.6 percent return rate.

20 Q And they have a choice about engaging in
21 that?

22 A I don't know, but I will tell you yes.

23 Q What's their choice?

24 A To change their mailing practices.

25 Q To switch from first class to standard?

1 A That might be one.

2 Q Is that a profitable choice for the Postal
3 Service to have them make?

4 A I don't know. It depends on how much they
5 shift.

6 Q Suppose they shifted at all. Wouldn't they
7 have to shift all of it to avoid that high return?

8 A Yes, yes.

9 Q So your answer is for them to take all of
10 this first-class mail and switch it to standard mail
11 as the way to fix their high return rate.

12 A No. I'm saying that is a way to fix their
13 high return rate. You're the one who said by shifting
14 it from first class. I would suggest that they might
15 have different mailing practices. I don't know what
16 their algorithm is. I don't know what their business
17 practice is. It's not been revealed in this.

18 Q You're not suggesting that they are
19 deliberately mailing to addresses they know are
20 undeliverable, are you?

21 A I don't think they care, if you want my
22 personal opinion.

23 Q Well, we don't want your personal opinion.
24 You're supposedly an expert witness. Does that belief
25 form the basis of your testimony?

1 A I don't believe that they are deliberately
2 engaging in high-cost behavior in order to get this
3 NSA.

4 Q Now, you speculated that some mailers would
5 see this as a way for them to engage in high-cost
6 behavior and get a good deal. So, again, I ask you,
7 what high-cost behavior do you think it's going to
8 lead other mailers to engage in?

9 A Asked and answered.

10 Q No. You haven't asked what high-cost
11 behavior other mailers might engage in in order to get
12 a deal.

13 A Well, at least one example is a high return
14 rate.

15 Q So that would be deliberate. Mailers would
16 deliberately send undeliverable mail so they could get
17 a deal.

18 A I don't think I said deliberately.

19 Q Well, then what does it mean that mailers
20 would see engaging in high-cost behavior? That sounds
21 like something that's intentional, or did you just
22 misspeak?

23 A No, no. I think that there is a reasonable
24 perception that could be gathered from this that Cap
25 One is being rewarded for having a high return rate.

1 Q But you talked about other mailers being led
2 into that same behavior. That's what your testimony
3 was. Now, maybe you didn't intend to say that.

4 A It's conceivable that some could do that.

5 Q That some people would say, "Gee, I'm going
6 to mail some undeliverable mail so I can get a deal"?

7 A I didn't say that.

8 Q But you say it's a knowing, intentional
9 behavior of the other mailers.

10 A I didn't say that either. That's a gross
11 mischaracterization.

12 Q Well, what does it mean that somebody will
13 be led to engage in something? That means a choice,
14 doesn't it? They choose to engage in this behavior so
15 they can get a deal.

16 A Or not to do certain things.

17 Q To get a deal. What is the "not"?

18 A Well, good address hygiene.

19 Q I'm going to ask you about that, the very
20 next question. On page six of your testimony, you
21 imply that Capital One has poor address hygiene, and
22 you state there: "Mailers that engage in better
23 address hygiene do not get a discount." Do you see
24 that?

25 A I'm not with you yet, sir.

1 Q Page six of your testimony.

2 A I'm on page six. I just haven't gotten to
3 where you are.

4 Q You say that mailers that engage in better
5 address hygiene do not get a discount.

6 A Yes, the opening sentence in that paragraph.

7 Q Okay. Now, in your response to Capital
8 One's Question 8, you conceded that you had performed
9 no analyses of any other mailers to compare their
10 hygiene practices with Capital One, your defense of
11 your statement being simply that Capital One appears
12 to have a very high return rate compared to others,
13 but you made no analyses of any other mailer's hygiene
14 practices. Isn't that what your answer was?

15 A No, but COS appears to have a very high
16 return rate compared to --

17 Q And that's your defense of saying that other
18 mailers engage in better address hygiene than Capital
19 One.

20 A Well, I don't see any other mailers being
21 offered this NSA.

22 Q Do you know of a single mailer that you can
23 testify to on the basis of your personal knowledge
24 that has better address hygiene than Capital One?

25 A Mailers being bulk mailers?

1 Q Yes. Mailers who would use address-
2 correction service and who would use NCOA and who are
3 required to use NCOA.

4 A No.

5 Q So you've accused them of not having better
6 hygiene practices, and, in fact, you can't even name
7 one single bulk mailer, first-class mailer, that you
8 know has better hygiene practice, can you?

9 A No.

10 Q Isn't it the case that theoretically a
11 mailer could have a 100-percent delivery rate without
12 engaging in any of the established address hygiene
13 practices?

14 A I don't know.

15 Q Theoretically, it's possible, isn't it?

16 A I don't know.

17 Q You don't know that it's theoretically
18 possible.

19 A I guess anything is possible, if that's what
20 you're asking.

21 Q Not anything is possible, but isn't it
22 possible that I could have a list of a thousand names,
23 and every address is correct on it, and I don't send
24 it to NCOA, and I don't do anything else, but isn't it
25 possible that every address is correct?

1 A I have a list of a thousand addresses, and
2 they are all right.

3 Q So it is theoretically possible that without
4 engaging in any address hygiene practice you could do
5 that.

6 A Yeah, but I'm not comparable to Cap One, I
7 don't think.

8 Q Isn't it also the case that, as a matter of
9 fact, a mailer that engages in the highest level of
10 established address hygiene practices could have,
11 conversely, a very high return rate?

12 A Well, I think the answer to that is
13 theoretically, yeah.

14 MR. MAY: Thank you. That's all, Mr.
15 Chairman.

16 CHAIRMAN OMAS: Thank you. Ms. McKenzie,
17 due to the hour, I think maybe we ought to break for
18 lunch at this point.

19 MR. REITER: On behalf of the Postal
20 Service, this is Scott Reiter, Mr. Chairman.

21 CHAIRMAN OMAS: Oh, I'm sorry.

22 MR. REITER: I would always agree with you
23 that we should break.

24 CHAIRMAN OMAS: We need to relax after that
25 Mr. Mays' amazing cross-examine. All right. Why

1 don't we come back about ten-after-one?

2 (Whereupon, at 12:02 p.m., a luncheon recess
3 was taken.)

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1 Q And do you know what that rate is for the
2 average first-class mailer?

3 A I believe it's 159 percent of returns, which
4 would, if you applied that 159 to the 9.6, would give
5 you something on the order of, like, 15.3 percent.

6 Q Now, in general, a forwarding rate would be
7 the rate at which first-class mail is forwarded from
8 one address to another. Is that correct?

9 A Yes.

10 Q And the Postal Service forwards first-class
11 mail when it has a change of address order on file.
12 That's also correct?

13 A That's my understanding.

14 Q And could you conclude that a mailer that
15 has a higher-than-average forwarding rate mails to
16 more addresses with a change-of-address order on file
17 than does the average first-class mailer?

18 A Do you mean in terms of the absolute number?

19 Q Looking at average forwarding rates. Let me
20 ask you again. Would you conclude that a mailer that
21 has a higher-than-average forwarding rate mails to
22 more addresses with a change-of-address order on file
23 than the average first-class mailer?

24 MR. BAKER: Could the counsel define
25 "forwarding rate" in terms of addresses, or is it in

1 terms of pieces?

2 MR. REITER: Either way.

3 THE WITNESS: I think that that's possible,
4 although I'm not sure that that's -- if one assumes
5 that there was a linear relationship, the answer would
6 be yeah.

7 BY MR. REITER:

8 Q And if we're talking about looking at
9 addresses as opposed to pieces, that would be your
10 answer then?

11 A I thought that the answer was addresses.

12 Q I believe you stated earlier, and I would
13 appreciate it if you would clarify this, that Capital
14 One has its own address lists and then also lists that
15 it purchases from vendors. Is that correct?

16 A Yes. My recollection was, and that was the
17 circumstance in which I couldn't remember who the
18 Capital One witness was, the statement was made that
19 when changes of addresses came to Cap One, they
20 updated their own list but didn't update third-party
21 lists.

22 Q So you did state, did you not, that Capital
23 One does not process the lists from vendors through
24 NCOA?

25 A That was my understanding, but I don't know.

1 Q Would you look at your answer to Postal
2 Service Interrogatory 18(c), please?

3 A I'm sorry. The number again?

4 Q 18(c).

5 A I'm having a little trouble hearing you,
6 sir.

7 Q Sorry. 18(c).

8 A I have that.

9 Q And there we asked you to confirm that the
10 average first-class mailer does not use NCOA, and you
11 said you couldn't confirm because you did not know the
12 definition of an average first-class mailer. Is that
13 correct?

14 A That's correct.

15 Q Now, let's change that slightly and focus on
16 a single-piece mailer, somebody who pays 37 cents a
17 piece for all of their mail and doesn't do any
18 presortation of bar coding.

19 A Like me?

20 Q Yes. Sure. Like you. But let's assume
21 that your list has a 9.6 percent return rate. What
22 would you then conclude is the forwarding rate for
23 that mail?

24 A Well, I would speculate that if it's at the
25 same relationship as the average first-class mailer,

1 it's 15.3 percent.

2 Q Now, if the same mailer decides to presort
3 and bar code and uses NCOA every 180 days to qualify
4 for the automation rates, assume that the return rate
5 is still 9.6 percent, what would the forwarding rate
6 then be?

7 A I don't know.

8 Q And would that forwarding rate change if the
9 NCOA processing was done more often than every 180
10 days?

11 A Presumably.

12 Q And in which direction would it change?

13 A Presumably, it would go downward. I found
14 that, I confess, sir, that interrogatory somewhat
15 confusing, so I hope I answered it right. Since the
16 entire NSA seems to be predicated on the notion that
17 Cap One is an average, first-class mailer, you asked
18 me to confirm that the average, first-class mailer
19 doesn't use NCOA, which Cap One does.

20 Q I think you've responded to my question.
21 Earlier, with Mr. May, you made some comments
22 regarding targeted mailing strategies and the credit
23 card industry. I just wanted to clarify. You did say
24 that you are not an expert in those fields. Is that
25 correct?

1 A That's correct.

2 Q But you did say that you're an expert on
3 railway transportation, I believe.

4 A I'm not sure I said that. I think I did say
5 I was an expert on contracting and the general concept
6 of NSAs. I also happen to be an expert, by the way,
7 in railway transportation.

8 Q Now, your expertise on contracting and NSAs;
9 is that within the railway industry, by and large?

10 A By and large, but it also includes some
11 electric utility work as well as work in the
12 communications industry.

13 Q Have you testified in those areas?

14 A In the electric power?

15 Q Or telecommunications, yes.

16 A Well, I have testified in the
17 telecommunications industry.

18 Q Is that listed in your C.V. that you
19 provided us?

20 A I don't know. I could check.

21 Q That's all right. You don't have to do that
22 now.

23 A Okay.

24 Q The record will speak for itself in that
25 regard. I would like to focus on the railway

1 industry. I take it, that's where the bulk of your
2 work is.

3 A That's correct.

4 Q Where you do have a contractor in NSA for
5 railway transportation, what's the typical number of
6 origin points that would be covered by that contract?

7 A It really varies, sir, and it has a tendency
8 to vary on a commodity-specific basis, and I use the
9 broadest definition of "commodity" there. If it's,
10 for example, something like coal, it may encompass as
11 many as 50 or 60 origins. In the East, it's not
12 unusual for electric utilities to buy coal from, let's
13 say, multiple-origin mines within central Appalachia,
14 which would encompass sort of western West Virginia,
15 the bulk of Kentucky, and some of Tennessee.

16 Q And that would all be covered in one
17 contract possibly.

18 A Usually.

19 Q What would the typical number of destination
20 points be of those contracts?

21 A In the East, I would say probably three or
22 four, and in the western United States, where coal is
23 acquired out of the river basin, it's usually on a
24 unique-destination basis, and then there is often what
25 I would refer to on sort of a shorthand basis is

1 called an umbrella contract, where you may have a
2 utility holding company that's got five or six
3 utilities, and each of those utilities has five or six
4 plants.

5 Q Now, do those contracts cover just the
6 railway transportation costs? There is no cost for
7 getting the coal or the commodity to the final
8 destination beyond the railroad, is there?

9 A That also varies. It is not unusual for
10 utilities that are located along waterways to acquire
11 coal that is a combination movement of rail from
12 origin to a barge terminal, for example, along the
13 Mississippi or Ohio River and then include a barge
14 transportation move to the destination. And also, in
15 the East, it's not unusual for -- well, it doesn't
16 happen a whole lot, but there are certain mine-loading
17 facilities. The East is different from the West in
18 that quite often you don't have a tipple located
19 directly at the mine, and you have to truck from the
20 mine origin to the tipple or to a series of tipples if
21 they want to have competition between two railroads
22 like Norfolk Southern and CSX do.

23 Q And is that additional transportation,
24 whether water or truck, included in the contract, or
25 is it separate?

1 A It can be either way.

2 Q What's typical?

3 A I'm not sure there is a typical. I'll give
4 you another example. Railroads very often, and may,
5 in fact, even with the Postal Service, have contracts
6 involving the intermodal transportation, in other
7 words, moving container loads of a commodity on a flat
8 car or on a double-stack on a well car, and there are
9 lots and lots of different service plans that range
10 from the railroad providing the origin from the
11 customer dock to the destination customer dock or from
12 the origin customer dock to the railhead but then
13 turning it over at the destination railhead to a
14 private. There are all sorts of combinations.

15 Q But it's mainly transportation costs that
16 would be involved in these contracts. Is that right?

17 A Yes, sir.

18 Q What other commodities are typically
19 involved in the contracts that you work on other than
20 coal?

21 A Grain. Coal and grain are both considered
22 bulk commodities. I do assist my clients with
23 intermodal movements and with what are considered to
24 be high-value-merchandise movements, and those could
25 involve things such as automotive parts and

1 accessories.

2 Q Now, the products such as coal or grain,
3 when you look at the costs for those, I take it by
4 your earlier remark that you don't have to measure or
5 count each lump of coal or grain of corn or whatever.

6 A That's correct.

7 Q Although they may vary in size.

8 A Well, --

9 Q I guess that's a question. Do they vary in
10 size?

11 A Yeah. Normally, they are, in the case of
12 coal, ground to a certain level, and the variable that
13 you would be reaching for there, I think, would be
14 called the weight. So it becomes a weight measurement
15 as opposed to a size measurement. Now, I will tell
16 you that the weight becomes important depending upon
17 the type of freight car that's used, and in the case
18 of coal you can have a 100-ton steel car or a 130-
19 pound aluminum car.

20 Q Except at that bulk level there is no piece
21 measurement of those commodities.

22 A No. The piece measurement becomes in the
23 number of cars and the number of locomotives that are
24 used.

25 Q Right, at that bulk level.

1 A That's correct.

2 Q Now, these contracts or NSAs in the railway
3 industry; are they subject to any kind of regulatory
4 review before they go into effect?

5 A No, they are not. Since 1980, when Congress
6 deregulated the rail industry, a willing buyer and a
7 willing seller can enter a contract. You are
8 required, however, to file the general parameters of
9 that contract with what is known as the Surface
10 Transportation Board, which is the successor agency to
11 the Interstate Commerce Commission.

12 Q But there is no regulatory review before
13 they go into effect so that the parties are free to --

14 A That's correct.

15 Q Would you take a look again at your Table 1
16 in your testimony at page 10 and also your response
17 to Cap One Interrogatory 10, specifically, the
18 attachment to that?

19 A Just so I'm right, I'm looking at Table 1 on
20 page 10 of the testimony and the interrogatory
21 response to Cap 110?

22 Q That's correct.

23 A Yes, sir. I have it.

24 Q Specifically, the first page of the
25 attachment. Now, looking at your Table 1, I take it

1 that the differences, as you increase them from zero
2 to 35, are attributable, if I heard you correctly
3 earlier, entirely to mail-stream processing. Is that
4 right? And I get to that conclusion by recollecting
5 that you told Mr. May that the carrier-preparation and
6 the clerk-handling costs did not change. Am I correct
7 in that, that they were the same on page 1 and page 2
8 of those attachments?

9 A I guess you could infer that from what I
10 said.

11 Q Okay.

12 A What Table 1 actually did was to look, as
13 you know, at row 1 being the figures that are
14 essentially presented in the NSA, and it looked at the
15 sensitivities of the net contribution at a series of
16 different levels. So rather than deriving from left
17 to right, it actually went from right to left and
18 said, you know, okay, at the \$8 million level, what
19 kind of a percentage reduction would you see? And
20 obviously the answer is zero; that's a given. If it
21 were around \$5 million, you would come out with
22 roughly 10 percent. If you have a break-even, how
23 close do you come at a whole number? Minus 24
24 percent, and it was derived that way.

25 Q Okay.

1 A So there wasn't any explicit assumption
2 relative to which components of the physical return
3 were to be changed.

4 Q So you didn't make those initially, but I do
5 want to follow up on your discussion earlier. I
6 believe I'm correct in remembering that before and
7 after, you agreed there was no change in the carrier
8 or the clerk costs. Is that right?

9 A That's my recollection, you know, and I
10 could look real quickly, but --

11 Q Please do.

12 A On page 1 of Library Reference 1, Mr. May
13 read four items -- carrier preparation, clerk
14 handling, CFS processing, and mail-stream processing -
15 - and I agreed with him that under the electronic only
16 the carrier prep and the clerk handling, and he said,
17 Aren't they the same? I said the numbers were.

18 Q Okay. So can you conclude from that that
19 the cost differences are primarily based on changes in
20 mail-stream processing costs?

21 A On the order of big numbers, absolutely,
22 because the mail-stream processing is 30 cents of the
23 remaining 35 or whatever.

24 Q Okay. Back to your Table 1, as we go from
25 zero to minus 35 percent, we're going from .535 to

1 .350, and that difference is about 18 cents. Would
2 you agree?

3 A Yes.

4 Q Now, if you look at page 1 of the library
5 reference, at the mail-stream processing costs per
6 piece, the number there is 29.95.

7 A Uh-huh.

8 Q So is it your contention that at the level
9 of a 35 percent difference, all that's left in mail-
10 stream processing costs is about 12 cents, or about 30
11 minus about 18?

12 A Well, it would be my contention that the CFS
13 processing and the mail-stream processing --

14 Q Yes, but the CFS is small, so I put that
15 aside, but I would agree with you.

16 A Yeah.

17 Q So you would be left with about 12 cents,
18 then.

19 A If you made the assumption that it all came
20 out of mail-stream processing, that's correct.

21 Q So do you disagree with that assumption? I
22 thought we agreed earlier that that was a logical
23 assumption or a logical conclusion.

24 A It is a logical conclusion. I don't know if
25 it's accurate or not in the real-world measurement.

1 Q It's accurate based on these figures,
2 though.

3 A Absolutely.

4 Q So you would agree that in order to reach
5 the level on your chart of a minus-35-percent
6 difference, there would have to be a reduction in
7 mail-stream processing costs of about two-thirds. Is
8 that right? Again, I'm going from about 30 to about
9 12.

10 A About two-thirds, yeah.

11 Q That's all I have on those.

12 You had a discussion with Mr. May earlier
13 about other mailers seeing high-cost behavior. Do you
14 recall that discussion?

15 A Yes. I think you're referring to the last
16 set of discussions that Mr. May and I had this
17 morning.

18 Q Yes. I don't recall whether you answered
19 this question or not. I think you didn't, so let me
20 know if I'm wrong. Were you able to state
21 specifically what kind of high-cost behavior you
22 thought these other mailers might engage in in order
23 to encourage the Postal Service to give them some kind
24 of better deal?

25 A Could you ask me that question again,

1 please?

2 Q Sure. What specific high-cost behaviors do
3 you believe might be engaged in by other mailers who
4 see this particular NSA in order to encourage the
5 Postal Service to give them a better deal on their
6 postage or whatever than they have today?

7 A Okay. Well, I confess that I think I maybe
8 got Mr. May and myself wrapped around the axle during
9 that discussion, so let me try and clarify.

10 Q Okay.

11 A My statement there was, as I said, I know at
12 least at one point during our lengthy discussion
13 sending the wrong price signals, in my opinion, to
14 other mailers, and Mr. May kept trying to impute that
15 that was deliberate high-cost behavior by other
16 mailers, and that's not what I intend by that
17 statement. I, obviously, have never been involved in
18 working for the Postal Service and negotiating with
19 customers, but I can tell you, in the other industries
20 that I work in, it's not unusual when you have a
21 longstanding relationship between a supplier and a
22 consumer, and the consumer is doing something that is
23 resulting in difficulty for the supplier -- in the
24 case of Cap One, I know that that's a high return
25 rate. Maybe in the case of another customer he is

1 mailing in the wrong place, or he is mailing in a
2 place that's less efficient from the Postal Service
3 perspective, or he is doing something to his mail,
4 putting rubber bands around it, that's causing it to
5 crinkle up, and it can't go through a machine, and I
6 would assume that the Postal Service, like most
7 businesses, would go to the customer and say, Hey, is
8 there something you can do to fix this problem to make
9 it easier for me? And, hopefully, the customer says,
10 Yeah, I can do this, or I can do this, or I can do
11 this.

12 I wasn't party to the NSA negotiations
13 between Cap One and the Postal Service. I don't know
14 what happened, but one could certainly envision the
15 Postal Service coming to Cap One and saying, "You guys
16 have a 9.6 percent return rate. What can we do to fix
17 this?" And I could envision Cap One saying, "Give me
18 a rate reduction." And that's the wrong signal, and
19 that's what I meant by, you know, encouraging or
20 perhaps other mailers envisioning -- you know, I can
21 see the Postal Service now going to the next problem
22 customer or customer with a problem and saying, "Hey,
23 do this," and then saying, "Why should I do that for
24 you? Give me a rate reduction."

25 Q Let me take one of your examples. A mailer

1 preparing its mail -- I think you used the example of
2 rubber bands crinkling up. We'll just go with that.
3 I realize that you're not an expert on postal
4 operations, and I'm not really either.

5 A I picked that example because for a long
6 time I was the president of my local swim club in
7 Northern Virginia, and we had to do these mailings.
8 We put these little stickers on.

9 Q Newsletters.

10 A We put rubber bands on the things, and I can
11 imagine what a mess that was for you guys.

12 Q Well, let's follow that. Was that a mess
13 just for us or --

14 A I just imagine it was.

15 Q Yes. I'll accept that, and I guess where I
16 want to go with it is maybe that affected the
17 condition of your mail when it was delivered. Maybe
18 it affected our ability to keep your mail intact and
19 eventually deliver it. So the point there is that if
20 the Postal Service comes back to you and says, "Hey,
21 Mailer, don't put the rubber bands that way because
22 half of your stuff is not getting there," are you
23 going to need any additional inducement other than the
24 fact that you paid 37 cents per piece to get them
25 there to want to get them there next time?

1 A I certainly wouldn't, but I can't speak for
2 anybody else, and I certainly --

3 Q I'm sorry. Go ahead.

4 A But I do perceive that, you know, Cap One
5 appears to be getting a discount here that has no
6 relationship in any way, shape, or form to the
7 proffered cost reductions that are in the NSA.

8 Q I still want to come back to your statement
9 about some mailers may see this, and you said, at
10 least for yourself, your prime motivation in that
11 instance would be to get your mail delivered for what
12 you paid.

13 A That's correct.

14 Q Can you think of an example where the cost
15 to the Postal Service of mailer behavior that is not
16 ideal would be something that the mailer would
17 continue to do? In other words, it would have no
18 adverse effect on the mailer as well as the Postal
19 Service.

20 A I'm not really sure I understand the
21 question.

22 Q Okay. Let me try it this way. In the
23 example that you came up and that I pursued, the
24 Postal Service comes back to you and says, "Your mail
25 is getting messed up. You might want to consider

1 fixing it." That's to your benefit, and you'll do it
2 even if we don't do anything for you.

3 A Yes.

4 Q Are you saying that you can imagine
5 situations where the mailer's behavior would have no
6 effect on the quality of service the mailer is
7 attempting to buy such that it wouldn't want to comply
8 with the Postal Service's request?

9 A No, sir. I don't think that's what I'm
10 saying. I'm just saying that in this circumstance it
11 seems to me to be sending the wrong price signal.

12 Q But your statement wasn't some mailers might
13 see this and engage in high-cost behavior, and I'm
14 just trying to figure out what that high-cost behavior
15 might be.

16 A Well, maybe I should say "continue engaging
17 in high-cost behavior."

18 Q And, again, following up on what we just
19 discussed, what kind of high-cost behavior would a
20 mailer want to continue to engage in that wouldn't
21 come back to hurt itself, either through not getting
22 its mail delivered or higher rates in the future or
23 some other benefit that it would get without the need
24 for a contract with the Postal Service and NSA?

25 A I'm with you on the question.

1 Q Do you have any examples of that?

2 A I don't have any examples.

3 MR. REITER: Thank you. That's all I have,
4 Mr. Chairman.

5 CHAIRMAN OMAS: Thank you, Mr. Reiter. Is
6 there any follow-up questions?

7 (No response.)

8 CHAIRMAN OMAS: Are there any questions from
9 the bench?

10 MR. HAMMOND: I have a couple.

11 CHAIRMAN OMAS: Commissioner Hammond.

12 MR. HAMMOND: Mr. Kent, during your cross-
13 examine by counsel for Capital One earlier today, you
14 were asked about your views on the kind of analysis
15 that should be performed to support a contemplated
16 negotiated service agreement, and, of course, these
17 kinds of agreements are new territory for this
18 Commission. We haven't had one before. So I would
19 just like to know, based upon your experience with
20 NSAs in other regulatory settings, if you could answer
21 some general questions about what you regard as
22 generally accepted practice in designing an NSA, just
23 generalized.

24 Can you tell me, do NSAs commonly contain
25 volume or revenue guarantees by the potential

1 customers?

2 THE WITNESS: As a general proposition in
3 the rail industry, the answer is yes. In the
4 communication industry, there is often a financial
5 guarantee that's not related to volume, and that is
6 because in the transportation industry, sir, there is
7 almost always some sort of a contract by the utility
8 and its suppliers of coal which contain volume
9 commitments.

10 MR. HAMMOND: Okay. Well, I guess maybe the
11 way I should say it is what is the purpose of such
12 guarantees?

13 THE WITNESS: From the perspective of the
14 rail industry or the provider, the carrier, it often
15 is required to make a capital investment or to realign
16 its priorities in such a way that it guarantees a
17 level of service, and it needs to know -- the concept
18 of a network industry is that you have a capacity
19 issue, and how do I manage that capacity to the best
20 of my ability?

21 MR. HAMMOND: Now, assuming that a potential
22 agreement doesn't contain those guarantees, then in
23 what way could a carrier reasonably assure itself that
24 a proposed agreement would be financially viable?

25 THE WITNESS: There are usually very steep

1 financial penalties for not fulfilling the contracts.

2 MR. HAMMOND: That's the only questions I
3 had, Mr. Chairman.

4 CHAIRMAN OMAS: Thank you, Mr. Hammond. Mr.
5 Baker, would you like some time with your witness?

6 MR. BAKER: Five minutes.

7 CHAIRMAN OMAS: Five minutes, it is. We'll
8 come back at ten-minutes-of-two.

9 (Whereupon, at 1:42 p.m., a brief recess was
10 taken.)

11 MR. BAKER: We have no re-direct, Mr.
12 Chairman.

13 CHAIRMAN OMAS: Thank you. Mr. Kent,
14 without re-direct, that completes your testimony here
15 today. We appreciate your appearance and your
16 contribution to our record. Thank you, and you are
17 now excused.

18 THE WITNESS: Thank you, sir.

19 (The witness was excused.)

20 CHAIRMAN OMAS: That completes our business
21 for today, and this hearing is adjourned until 9:30
22 a.m. in the morning, when we will hear testimony from
23 Mr. Callow and Mr. Smith of OCA. Thank you and have a
24 good afternoon.

25 //

1 (Whereupon, at 1:50 p.m., the hearing was
2 adjourned, to be reconvened at 9:30 a.m. on Thursday,
3 February 6, 2003.)

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REPORTER'S CERTIFICATE

DOCKET NO.: MC2002-2

CASE TITLE: Experimental Rate and Service Changes to
Implement Negotiated Service Agreement with
Capital One Services, Inc.

HEARING DATE: February 5, 2003

LOCATION: Washington, D.C.

I hereby certify that the proceedings and evidence are
contained fully and accurately on the tapes and notes
reported by me at the hearing in the above case before the
Postal Rate Commission.

Date: February 5, 2003


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