

Before The
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

Rate and Service Changes to Implement)
Functionally Equivalent Negotiated Service) Docket No. MC2004-4
Agreement with Discover Financial)
Services, Inc.)

OFFICE OF THE CONSUMER ADVOCATE
INTERROGATORIES TO UNITED STATES POSTAL SERVICE
WITNESS ALI AYUB (OCA/USPS-T1-35-40)
August 5, 2004

Pursuant to Rules 25 through 28 of the Rules of Practice of the Postal Rate Commission, the Office of the Consumer Advocate hereby submits interrogatories and requests for production of documents. Instructions included with OCA interrogatories OCA/DSF-T1-1-5, dated June 25, 2004, are hereby incorporated by reference.

Respectfully submitted,

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OCA/USPS-T1-35. Please refer to your response to OCA/USPS-T1-12, which states that the

Postal Service's understanding of the 'stop-loss' provision is that the 'stop-loss' is equal to 95% of the ACS cost savings over the term of the agreement. The ACS cost savings are presented in Appendix A, page 11, line (2), of my testimony is \$8,006,949.

Also, please refer to Table 8-2 from PRC Op. MC2002-2, reproduced as an attachment to this interrogatory.

- a. Please confirm that Table 8-2 presents the Commission's methodology for calculating the "ACS Related Savings" used in estimating the stop-loss for the Capital One NSA. If you do not confirm, please explain.
- b. Please confirm that the Commission did not use in its development of Table 8-2 the Return Cost Savings figure (\$13,094,000) calculated by witness Crum (USPS-T-3) in Attachment B, page 2 of his testimony in Docket No. MC2002-2. If you do not confirm, please explain.
- c. Please confirm that, in preparing your response to OCA/USPS-T1-12 as it relates to the Discover NSA, you did not use the Commission's methodology as presented in Table 8-2 to calculate "the 'stop-loss' [that] is equal to 95% of the ACS cost savings over the term of the agreement." If you do not confirm, please explain and calculate the stop-loss that is equal to 95% of the ACS cost savings over the term of the agreement using the same methodology and format as presented by the Commission in Table 8-2. Provide citations to all sources.

OCA/USPS-T1-36. Please refer to your response to OCA/USPS-T1-28(a), where you failed to confirm that “the calculated stop-loss estimate for Discover is consistent with the Commission’s calculation of the stop-loss estimate with respect to Capital One.” Also, please refer to Table 8-2 from PRC Op. MC2002-2, reproduced as an attachment to this interrogatory.

- a. For Year 1 of the Discover NSA, please calculate the “ACS Related Savings” for the stop-loss using the same methodology and format as presented by the Commission in Table 8-2. For each line in Table 8-2, please provide the corresponding figures for Discover, and show all calculations used to derive each line. Provide citations to all sources.
- b. For Year 2 of the Discover NSA, please calculate the “ACS Related Savings” for the stop-loss using the same methodology and format as presented by the Commission in Table 8-2. For each line in Table 8-2, please provide the corresponding figures for Discover, and show all calculations used to derive each line. Provide citations to all sources.
- c. For Year 3 of the Discover NSA, please calculate the “ACS Related Savings” for the stop-loss using the same methodology and format as presented by the Commission in Table 8-2. For each line in Table 8-2, please provide the corresponding figures for Discover, and show all calculations used to derive each line. Provide citations to all sources.
- d. Based upon the “ACS Related Savings” developed in parts (a) – (c) of this interrogatory, please provide the total “ACS Related Savings” during the three years of the Discover NSA, and the amount equal to “95% of the ACS cost

savings over the term of the agreement.” Please show all calculations and provide citations to all sources.

OCA/USPS-T1-37. Please refer to your response to OCA/USPS-T1-27, which states “The higher the proportion of marketing mail the higher the cost savings would be which would in turn increase the cap.” Also, please refer to the attachment to this interrogatory.

- a. Please refer to Table 1, Year 1 – ACS Related Savings in the attachment. Please confirm that Discover’s Year 1 ACS unit cost saving is \$0.01644240 $[(\$0.55 - 0.34) * 0.093 * 0.85 * 1.00]$, where $(\$0.55 - 0.34)$ represents the difference between manual return unit costs and electronic return unit costs, 0.093 represents Discover’s physical return rate, 0.85 represents the ACS success rate, and 1.00 represents Discover’s solicitation mail as a percent of extra BR volume. If you do not confirm, please explain and show all calculations.
- b. Please refer to Table 2, Year 1 – Discount Leakage in the attachment. Please confirm that Discover’s BR Equilibrium First-Class Volume is 518,233,050. If you do not confirm, please explain and show all calculations.
- c. Please refer to Table 1, Year 2 – ACS Related Savings in the attachment. Please confirm that Discover’s Year 2 ACS unit cost saving is \$0.01710010 $[(\$0.57 - 0.36) * 0.093 * 0.85 * 1.00]$, where $(\$0.57 - 0.36)$ represents the difference between manual return unit costs and electronic return unit costs, 0.093 represents Discover’s physical return rate, 0.85 represents the ACS

- success rate, and 1.00 represents Discover's solicitation mail as a percent of extra BR volume. If you do not confirm, please explain and show all calculations.
- d. Please refer to Table 2, Year 2 – Discount Leakage in the attachment. Please confirm that Discover's BR Equilibrium First-Class Volume is 526,559,959. If you do not confirm, please explain and show all calculations.
- e. Please refer to Table 1, Year 3 – ACS Related Savings in the attachment. Please confirm that Discover's Year 3 ACS unit cost saving is \$0.01778410 $[(\$0.60 - 0.37) * 0.093 * 0.85 * 1.00]$, where $(\$0.60 - 0.37)$ represents the difference between manual return unit costs and electronic return unit costs, 0.093 represents Discover's physical return rate, 0.85 represents the ACS success rate, and 1.00 represents Discover's solicitation mail as a percent of extra BR volume. If you do not confirm, please explain and show all calculations.
- f. Please refer to Table 2, Year 3 – Discount Leakage in the attachment. Please confirm that Discover's BR Equilibrium First-Class Volume is 535,772,530. If you do not confirm, please explain and show all calculations.

OCA/USPS-T1-38. The following interrogatory concerns Discover Financial Services' "free rider" volumes.

- a. Please confirm that in PRC Op. MC2002-2, para. 8016, the Commission described "free riders" as "mail that would have been sent even absent the NSA" If you do not confirm, then explain why not.

- b. Using the definition cited in part a., please confirm that the Discover NSA contains 46 million “free riders,” determined as follows;
- i. The NSA (§III.D.) provides for a threshold for the first year of 405 million, at which point discounts of 2.5 cents will be paid; these discounts continue to be paid up to 435 million pieces.
 - ii. The Before Rates volume forecast is 451 million (Attachment A, page 6 (USPS-T- 1)). Discounts of 3 cents are paid up to the 451 million-piece level (and beyond).
 - iii. The Before Rates volume forecast of 451 million falls within the Commission’s description of “volume that would have been sent even absent the NSA.”
 - iv. If you do not confirm, then state the number of “free riders” in the Discover NSA. Show all calculations and provide all source documents.
- c. Please confirm that the Commission concluded that, absent a stop-loss provision, “there is a serious risk that discounts given to ‘free riders’ will exceed savings to the Postal Service and that other mailers will be worse off because of the NSA.”

OCA/USPS-T1-39. For Discover Financial Services (DFS), please provide an analysis equivalent to that submitted by witness Crum at Tr. 2/318-22 (Docket No. MC2002-2), in response to POIR 2, question 7.

- a. In your analysis, address specifically the fact that DFS' estimated First-Class Mail (FCM) solicitation volumes are approximately 23% of Capital One's FCM solicitation volumes.
- b. Also, address specifically the fact that in contrast to Capital One, which had an obligation to update its address lists within two days of receipt of electronic ACS notices (Tr. 2/321), DFS is given a longer period of time – 30 days – to update its address lists.
- c. Isn't it generally correct that dividing Capital One's annual volumes of FCM solicitations – 768 million – by the number of delivery points in the United States (witness Crum used a figure of 137,682,00, from the Postal Service's 2001 Annual Report; Tr. 2/320) yielded an implied average number of pieces per delivery point of 5.6? If you do not agree, please explain.
- d. Isn't it generally correct that dividing DFS' estimated annual volumes of FCM solicitations – 174 million – yields an implied average number of pieces per delivery point of 1.27? If you do not agree, please explain.
- e. Doesn't a comparison of the figures set forth in parts c. and d., *i.e.*, 5.6 versus 1.27, suggest that the Postal Service is much less likely to benefit from avoided forwards in the case of DFS than it does in the case of Capital One? If you do not agree, please explain.
- f. Please confirm that an obligation to update address lists within 30 days (DFS) compared to 2 days (Capital One) is likely to result in higher costs for the Postal Service for forwarding and returning DFS' UAA mail as compared to Capital One. If you do not confirm, please explain.

OCA/USPS-T1-40. Please compare the NSA requirement (§II.C.) for Capital One, *i.e.*, “In exchange for a waiver/suspension of ACS fees, Capital One agrees to update its databases within 2 business days and use the information in all future marketing campaigns,” with the much weaker, non-specific obligation imposed on DFS (NSA §II.B.2.), “For every mailing whose address source is an outside list, DFS agrees to forward the ACS notices to its third party list processor, or arrange to have the Postal Service forward the ACS notices directly to its list processor. DFS will work with its third party list processor to use this data for all future marketing campaigns.”

- a. Please confirm that witness Giffney testifies (at page 6 of DFS-T-1) that:

On a monthly basis, DFS procures over 40 mailing lists that make up the entire acquisition campaign mailing. We mail from these lists and not from an internal prospect database.

If you do not confirm, please explain why not.
- b. Please confirm that, given DFS’ practice of using purchased mailing lists, as contrasted with Capital One’s practice of using an internal prospect database, there is less certainty that provision of eACS notices will result in reduced DFS UAA pieces compared to Capital One.
- c. Describe in detail the specific procedures that DFS will employ to reduce future UAA mailings to addresses identified as subject to forwarding or return notices.
- d. Please state which provisions of the Data Collection Plan will require reports on the procedures employed by DFS to utilize the eACS information provided under the NSA to reduce the number of future mailings of UAA pieces to addresses identified by the Postal Service as subject to forwarding or return notices.

Table 8.2

ACS Related Savings

(1)	FC Physical Return Unit Cost	\$	0.5347
(2)	"Electronic Return" Unit Cost	\$	0.3321
(3) = (1)-(2)	Difference		\$0.2026
(4)	Solicitation Percentage of Revised Capital One TYBR First-Class Volume		55.3%
(5)	Capital One TYBR First-Class Volume (thousand)		1,559,248
(6) = (4)*(5)	Capital One TYBR First-Class Solicitation Volume (thousand)		862,612
(7)	Capital One First-Class Solicitation Return Rate		9.6%
(8) = (6)*(7)	Capital One TYBR First-Class Solicitation Return Volume (thousand)		82,811
(9)	ACS Success Rate		85%
(10) = (8)*(9)	Volume of Capital One Physical Returns converting to ACS (thousand)		70,389
(11) = (3)*(10)	Total Test Year Savings (thousand)		\$14,259

Sources: (1) & (2) - USPS-LR-1
(4) - COS-LR-4, Exhibit 3
(7) & (9) - USPS-T-3, Attachment A, page 2

**DISCOVER NSA
 Stop Loss Estimate Model**

**TABLE 1
Year 1 - ACS Related Savings**

[1]	Manual Letter Returns Unit Cost	\$0.55
[2]	Electronic Letter Returns Unit Cost	\$0.34
[3]	Discover Return Rate - Solicitation Mail	9.3%
[4]	Address Change Service (ACS) Success Rate	85%
[5]	Discover BR Customer Mail Volume	295,000,000
[6]	Discover BR Solicitation Mail Volume	156,000,000
[7]	Solicitation Mail % of Extra BR Volume	100.00%
[8]	Discover ACS Unit Cost Savings	\$0.01644240
[9]	Discover BR Equilibrium First-Class Volume	518,233,050
[10]	Discover BR Solicitation Letter Volume	223,233,050
[11]	Total ACS Test Year Savings	\$3,670,487

**TABLE 2
Year 1 - Discount Leakage**

<u>Volume Block</u>		<u>Incremental Volume</u>	<u>Discount</u>	<u>Discount Leakage</u>	
[a]	[1]	[b]	[2] = [1b] - [1a]	[3]	
				[4] = [2] * [3]	
405,000,000	to	435,000,000	30,000,000	\$0.025	\$750,000
435,000,001	to	465,000,000	29,999,999	\$0.030	\$900,000
465,000,001	to	490,000,000	24,999,999	\$0.035	\$875,000
490,000,001	to	515,000,000	24,999,999	\$0.040	\$1,000,000
515,000,001	to	518,233,050	3,233,049	\$0.045	\$145,487
Total					\$3,670,487
Difference - ACS Savings and Discount Leakage					(\$0)

**DISCOVER NSA
 Stop Loss Estimate Model**

**TABLE 1
Year 2 - ACS Related Savings**

[1]	Manual Letter Returns Unit Cost	\$0.57
[2]	Electronic Letter Returns Unit Cost	\$0.36
[3]	Discover Return Rate - Solicitation Mail	9.3%
[4]	Address Change Service (ACS) Success Rate	85%
[5]	Discover BR Customer Mail Volume	290,000,000
[6]	Discover BR Solicitation Mail Volume	156,000,000
[7]	Solicitation Mail % of Extra BR Volume	100.00%
[8]	Discover ACS Unit Cost Savings	\$0.01710010
[9]	Discover BR Equilibrium First-Class Volume	526,559,959
[10]	Discover BR Solicitation Letter Volume	236,559,959
[11]	Total ACS Second Year Savings	\$4,045,198

**TABLE 2
Year 2 - Discount Leakage**

<u>Volume Block</u>		<u>Incremental Volume</u>	<u>Discount</u>	<u>Discount Leakage</u>
[a]	[1]	[2] = [1b] - [1a]	[3]	[4] = [2] * [3]
	[b]			
405,000,000	to 435,000,000	30,000,000	\$0.025	\$750,000
435,000,001	to 465,000,000	29,999,999	\$0.030	\$900,000
465,000,001	to 490,000,000	24,999,999	\$0.035	\$875,000
490,000,001	to 515,000,000	24,999,999	\$0.040	\$1,000,000
515,000,001	to 526,559,959	11,559,958	\$0.045	\$520,198

Total **\$4,045,198**

Difference - ACS Savings and Discount Leakage **(\$0)**

**DISCOVER NSA
 Stop Loss Estimate Model**

**TABLE 1
Year 3 - ACS Related Savings**

[1]	Manual Letter Returns Unit Cost	\$0.60
[2]	Electronic Letter Returns Unit Cost	\$0.37
[3]	Discover Return Rate - Solicitation Mail	9.3%
[4]	Address Change Service (ACS) Success Rate	85%
[5]	Discover BR Customer Mail Volume	285,000,000
[6]	Discover BR Solicitation Mail Volume	156,000,000
[7]	Solicitation Mail % of Extra BR Volume	100.00%
[8]	Discover ACS Unit Cost Savings	\$0.01778410
[9]	Discover BR Equilibrium First-Class Volume	535,772,530
[10]	Discover BR Solicitation Letter Volume	250,772,530
[11]	Total ACS Third Year Savings	\$4,459,764

**TABLE 2
Year 3 - Discount Leakage**

<u>Volume Block</u>		<u>Incremental Volume</u>	<u>Discount</u>	<u>Discount Leakage</u>	
	[1]	[2] = [1b] - [1a]	[3]	[4] = [2] * [3]	
	[a]	[b]			
405,000,000	to	435,000,000	30,000,000	\$0.025	\$750,000
435,000,001	to	465,000,000	29,999,999	\$0.030	\$900,000
465,000,001	to	490,000,000	24,999,999	\$0.035	\$875,000
490,000,001	to	515,000,000	24,999,999	\$0.040	\$1,000,000
515,000,001	to	535,772,530	20,772,529	\$0.045	\$934,764
Total					\$4,459,764
Difference - ACS Savings and Discount Leakage					\$0

TABLE 1 (Years 1-3)

Notes & Sources

- [1] USPS-T-1 (Ayub), Appendix A, page 1
- [2] USPS-T-1 (Ayub), Appendix A, page 1
- [3] USPS-T-1 (Ayub), Appendix A, page 1
- [4] USPS-T-1 (Ayub), Appendix A, page 1
- [5] USPS-T-1 (Ayub), Appendix A, page 2
- [6] USPS-T-1 (Ayub), Appendix A, page 2
- [7] Assumes all extra BR volume is solicitation mail.
- [8] = ([1] - [2]) * [3] * [4] * [7]
- [9] = Table 2 [1b]
- [10] = [9] - [5]
- [11] = [8] * [10]

TABLE 2 (Years 1-3)

Notes and Sources: Request, Attachment B

- [1] Request, Attachment B
- [3]

DISCOVER NSA

TABLE 3
Calculation of Total Stop Loss Estimate

	<u>Volume</u> [1]	<u>Discount</u> <u>Leakage</u> [2]	<u>Return</u> <u>Cost</u> <u>Savings</u> [3]
Year 1	518,233,050	\$3,670,487	\$3,670,487
Year 2	526,559,959	\$4,045,198	\$4,045,198
Year 3	535,772,530	\$4,459,764	\$4,459,764
			\$12,175,449
Passthrough Percent			95%
TOTAL STOP LOSS ESTIMATE			\$11,566,676

Notes and Sources

[1] & [2] TABLE 2, for the year indicated

[3] TABLE 1, for the year indicated